

Public-Public and Public-Private Cooperation: Do the EU rules add up?

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In the European Council's [proposed compromise text](#) for new procurement directives, public-public cooperation is marked as an area for further negotiations. The relevant provisions are found in Recital 14 and Article 11 of the draft, which attempt to codify the decisions of the European Court of Justice in the *Teckal* line of cases on the in-house exemption and the *Hamburg* case ([C-480/06](#)) on horizontal cooperation. This article analyses the extent to which different forms of public-public and public-private cooperation are currently subject to the procurement rules and offers a critique of the proposed changes. The critique addresses both the legal cogency of the provisions and how they might work in practice.

***Teckal* and the In-house exemption**

It is now well-established in EU law that the award of a contract by a public authority to an in-house entity will not be covered by the procurement rules, where certain conditions are met:

- i) The public authority exercises a level of control over the entity similar to that which it exercises over its own departments;
- ii) The entity carries out the essential part of its activities for the controlling authority;
- iii) There is no private participation in the controlled entity.¹

The conditions are cumulative. Subsequent cases have established that more than one public authority may exercise the control over the entity, and that it may carry out the essential part of its activities for those authorities collectively (See cases [C-340/04 Carbotermo](#), [C-295/05 Asemfo](#) and [C-324/07 Coditel Brabant](#).) The precise percentage of activities which such an entity must carry out for the controlling authorities has not been decided in case law. In *Stadt Halle*, the Court left open the possibility that 80% of such activities might be sufficient to meet the test, but did not resolve the issue conclusively.

The rationale for all three aspects of the test is to limit the 'in-house' exemption to prevent it applying in cases where this would lead to a distortion of competition. If an entity is independent in its decisions, operates on the market or includes private participation, the Court considers that the procurement rules should apply where public contracts are awarded to it. It is worth noting that this does not interfere with the ability of public authorities to provide goods, services or works out of their own resources. It also does not mean that award of a contract to an entity not meeting the conditions is impossible, only that the procurement rules would apply, unless another exemption is available.

Horizontal cooperation: *Hamburg* case

The *Hamburg* case concerned an arrangement between the City of Hamburg Sanitation Department and four local authorities in the Lower Saxony region. Each of the four authorities had agreed to provide a certain volume of waste throughput to the incineration facility built by Hamburg. Payments were made to Hamburg to cover the cost of incineration, and it assumed responsibility for providing replacement capacity in certain circumstances and representing the authorities' interests

¹ This was established by the Court in Case [C-26/03 Stadt Halle](#).

against the private operator of the facility. A citizen concerned about the charges for waste management in the region made a complaint to the Commission, who brought the case upon learning that the arrangement between the authorities had not been subject to tender. The Advocate General in the case applied the *Teckal* logic and found that the arrangement did not qualify for the in-house exemption, as the control condition was not met.

The Court however considered that as the arrangement constituted a form of genuine cooperation between the authorities, and was not intended to circumvent the procurement rules, it could stand. In reaching this conclusion, the Court stated that:

“Community law does not require public authorities to use any particular legal form in order to carry out jointly their public service tasks... such cooperation between public authorities does not undermine the principal objective of the Community rules on public procurement ... where implementation of that cooperation is governed solely by considerations and requirements relating to the pursuit of objectives in the public interest and the principle of equal treatment of the persons concerned ... is respected, so that no private undertaking is placed in a position of advantage vis-à-vis competitors.” (Case C-480/06, Para 47)

The *Hamburg* judgment was welcomed by many who felt that the *Teckal* exemption had become too narrow to accommodate forms of public-public cooperation which are in use in many Member States. Nevertheless, it was not clear to what extent the Court’s judgment in *Hamburg* might be limited by the facts of that case. In particular, the Court emphasised that the arrangement aimed to fulfil specific obligations regarding waste treatment set out in European directives, that the facility would not have been built without the guarantee of throughput from the four authorities, and that a separate service contract was awarded by Hamburg for the operation of the facility.

Practical applications

Public authorities wishing to set up or avail of the services of an in-house entity (*‘Teckal company’*) or organise shared services have had cause to scrutinise the above case law. In the UK, a Supreme Court decision in 2011 upheld the right of various London Borough Councils to avail of the services of a jointly-owned mutual insurance company (LAML), despite the necessary degree of independence of that company from the individual authorities.² This overturned the finding of the Court of Appeal that the requirement of an arms’ length relationship between insured and insurer precluded the type of control needed to avail of the *Teckal* exemption. Despite this finding, the authority bringing the appeal (Harrow) was not able to avail of the insurer’s services due to a lack of powers. The coming into force of the [Localism Act 2011](#) removes restrictions on the powers of local authorities, and so opens up new possibilities to exploit such arrangements.

Shared services have a particular role to play as public authorities face cutbacks, and there is a desire to realise efficiencies by availing of the capacity of other authorities where these exist. Collaborative or joint procurement – whether through a *Teckal* company or otherwise – is also considered to hold the potential for significant savings, as underlined by a [recent report](#) of the Northern Ireland Audit Office. At the same time, private operators who feel they are denied the opportunity to compete for contracts, or indeed citizens concerned about the value-for-money of such arrangements, may seek to challenge or complain to the Commission. It is important then to look at the detail of what is proposed, to see if it strikes a fair balance between these competing interests.

² *Brent London Borough Council and others v Risk Management Partners Ltd* [2011] UKSC 7, paras 28 and 32-33.

Proposed changes

Recital 14 of the proposal sets out the intention to offer clarity on public-public cooperation and incorporate the Court's jurisprudence into the directives. It reiterates the view adopted by the Court and in a previous Commission working paper ([SEC \(2011\) 1169](#)) that there is no general exemption for public-public cooperation from the procurement rules, only the specific exemptions established in case law. Article 11 then goes on to set out the specific exemptions, covering in-house (*Teckal*) entities controlled by one or more contracting authorities, and the *Hamburg*-type of horizontal cooperation. In doing so, Article 11 proposes more prescriptive rules than exist at present in the case law. Unlike other aspects of the proposals, there is no scope for Member States to choose whether to implement these rules into domestic law. A few potentially problematic aspects are identified here.

Article 11(1) and 11(3) set out rules for determining whether the *Teckal* exemption applies based on control, essential activities and private participation. 90% of the in-house entity's activities must be carried out for the controlling authority or authorities, or other bodies controlled by them. To determine whether this threshold is met, the average total turnover of the entity over the previous three years is to be taken into account. In addition to the arbitrariness of the threshold, no indication is given of how the rule would be applied in the case of a newly established *Teckal* company, without previous turnover. A further problem arises where joint control is exercised by two or more authorities. Article 11(3) requires that the entity "does not pursue any interests which are distinct from that of the public authorities affiliated to it" – this could rule out the award of a contract to a mutual insurance company such as LAML, which must act independently of its owners in making certain decisions.

Article 11(4) sets out five cumulative conditions for exempting horizontal cooperation:

- a) it is part of an agreement establishing genuine cooperation between the contracting authorities aimed at carrying out jointly their public service tasks and involving mutual rights and obligations;
- b) it is governed only by considerations related to the public interest;
- c) the contracting authorities carry out 90% of their relevant activities within the agreement;
- d) financial transfers correspond to the reimbursement of actual costs; and
- e) there is no private participation in any of the contracting authorities involved.

Conditions a, b and d appear to derive directly from *Hamburg*. The requirement that the authorities carry out 90% of their relevant activities within the arrangement may be aimed at preventing distortion of competition, but it is not clear why this should apply to authorities availing of services, as well as those providing them. Similarly condition e) seems overly broad – it extends beyond the arrangement in question to cover all aspects of the authorities' operations. Determining whether financial transfers correspond to actual costs, as required by condition d), leaves room for challenge and may require expensive professional opinions, updated frequently. Overall, Article 11(4) is likely to deter public authorities from entering into *Hamburg*-type arrangements. This is unfortunate, at a time when such arrangements may offer good value and efficiencies as noted above.

Other forms of cooperation: Central purchasing bodies and occasional joint procurement

Articles 35 and 37 set out the possibilities for using central purchasing bodies and conducting occasional joint procurement with other public authorities. Article 38 aims to encourage the use of

central purchasing bodies established in other Member States, by removing national restrictions. For occasional joint procurement, the proposal is mainly concerned with how liability is allocated between participants. While the procurement rules would apply to contracts awarded jointly, Article 37 does not refer to any rules for the award of agreements governing joint procurement. This appears to run contrary to Article 11, although in many cases the value of the procurement services themselves would be below-threshold. Article 35 (5) contains an explicit exemption for the award of contracts for the provision of central purchasing and ancillary services to a central purchasing body. As such bodies are defined only by the fact that they carry out central purchasing and ancillary activities, this would appear to be an easier approach to the *Hamburg*-type situation, where one contracting authority can simply be designated as a central purchasing body. Notably, there is no requirement that central purchasing bodies provide services only to the public sector.

Subsidisation and Public-Private Partnerships

The absolute ban on private involvement under Article 11 may lead authorities to consider other options where the participation of a private partner is essential or desirable. Curiously, the scope to award contracts via a joint venture or PPP may now be broader than the scope to award contracts directly to a *Teckal* company or another public authority. Article 12 in the proposal deals with subsidisation of civil engineering and public construction contracts, and associated services. As in the current Public Sector Directive, if the level of public subsidy is 50% or less, the procurement rules will not apply to the award of contract by the private partner. The Commission has also produced guidance to the effect that where an institutional PPP is set up, it is sufficient to have a competition at the outset to choose the private partner, and not for each subsequent contract awarded to the venture, provided the contracts fall within the advertised scope ([C\(2007\) 6661](#)). The combined effect may be that it will be easier for public authorities to subsidise an engineering or works contract awarded by the private sector, or to set up a joint venture, then it would be for them to award contracts to each other.

Conclusion

The proposal aims to elaborate the rules on public-public cooperation, drawing on case law. In doing so, it effectively narrows the scope of the exemptions, by setting a 90% threshold for the essential activities test, restricting the possibility of a *Teckal* company having any outside interests, and setting stringent conditions for *Hamburg*-type horizontal arrangements. Conversely, the rules on occasional joint procurement and use of central purchasing bodies appear quite liberal – but may lead to uncertainty about whether these arrangements are also subject to Article 11. Likewise the rules on subsidisation and PPPs offer the opportunity to avoid full application of the procurement rules for many contracts which have an element of private participation. There is a need to consider three factors in finalising the text. First, are the rules internally consistent and clear? Second, how will the Article 11 rules affect forms of public-public cooperation currently in broad use, such as mutual insurance companies? Finally, the combined effect of these provisions should strike an appropriate balance between ensuring competition and transparency in the award of public contracts, and allowing flexibility.

This article arose from a seminar conducted by Achilles Procurement Services on Public-Public Co-operation on 5th October 2012 in Malahide, Co. Dublin. Further information is available [here](#).