



Public Procurement

In-house Procurement and Public/Public Co-operation

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Introduction

When a contracting authority needs specific supplies, services or works, it has two choices: (1) it can buy them on the market (“externalisation”); or (2) it can produce them internally, within its own organisation.

The Public Sector Directive (the Directive)¹ clearly states that a contracting authority is free to choose the way in which it prefers to proceed, and it is not obliged to follow the externalisation route. The application of public procurement rules does not affect the freedom of contracting authorities to perform the public service tasks conferred on them by using their own resources². Any decision as to whether or not to externalise should be based on a careful examination of the specific economic and social aspects of the situation concerned. Functions that are traditionally considered to be the state’s prerogatives, such as some aspects of administration or justice, are unlikely to be externalised. Both options are possible for other functions, such as public building maintenance, collection of waste, or even public transport. The ultimate aim is to determine which solution best achieves the set objectives in the public interest and best ensures the efficient expenditure of public funds.

Usually, a contracting authority is established for the purpose of performing non-economic activities, and in practice, the supplies, services or works required are commonly obtained by using private sector resources. To this end, in almost all cases the contracting authority conducts a competition, in accordance with the requirements of the Directive, and concludes a contract for pecuniary interest with other legal entities. For reasons of efficiency, two or more contracting authorities may agree to perform specific procurement procedures jointly, and in that event the final result for each of them will be the conclusion of a contract.

A contracting authority may also obtain supplies, services or works from another legal entity that is a contracting authority (a “public entity”). The general principle regarding the obligation to observe the public procurement rules is applicable, irrespective of the fact that the contractual partner is a public entity. The provisions of the Directive³ make no distinction between a private entity and a public entity that offer, on the market, to supply goods, provide services or execute works. A contracting authority may therefore organise a procurement procedure, in accordance with the provisions of the Directive, when it intends to award a contract to a distinct legal entity⁴, without regard to the nature of the entity. Public entities may perform economic activities in the same way as entities in the private sector, but their public status does not give them the freedom to be awarded a procurement contract without participating in a competition. If public entities participate as tenderers in procurement procedures conducted by contracting authorities, they are to be treated equally in relation to any private entities that are participating, without benefiting from any special advantages linked to their status.

The concept of the in-house exception covers those situations where a contracting authority performs certain activities internally, without using external resources. The contracting authority itself provides the supplies, services or works that it requires. In this case, the contracting authority is not required to organise a competition under the public procurement rules in order to award a contract. A broad interpretation of this in-house concept permits the activities to be performed by a separate legal entity that is part of the contracting authority’s structure.

The public/public co-operation concept and exception covers those situations where contracting authorities co-operate in the performance of certain activities, without organising a competition

¹ Directive 2014/24/EU on public procurement and repealing Directive 2004/18/EC, 26 February 2014.

² Recitals 5 and 31 and Article 1, paragraph 4 of the Directive clearly state this rule.

³ Article 2, paragraph 1 (10) of the Directive.

⁴ CJEU Case C-480/06, Commission v Germany, paragraph 33: “... the fact that the service provider is a **public entity** [emphasis added] distinct from the beneficiary of the services does not preclude the application of Directive.”

under the public procurement rules prior to entering into the co-operation arrangements between themselves.

This public procurement brief explains to what extent and in which conditions a contracting authority is free to apply these exceptions without breaching the public procurement rules.

Development of the in-house and public/public exceptions: The in-house exception and the public/public exception have been developed over many years in the case law of the Court of Justice of the European Union (CJEU). They were regulated for the first time by the EU legislator in 2014. This brief provides information on the relevant CJEU case law and shows how that legislation has been applied and developed in the Directive. For more information on the new package of EU procurement legislation in 2014, see SIGMA Public Procurement Brief 1, *Public Procurement in the EU: Legislative Framework, Basic Principles and Institutions*⁵.

In-house procurement

In-house procurement is a way of using public sector resources, and the contracting authority is exempted from application of the procurement rules when it resorts to this solution. Two “in-house” situations are described below:

- “pure” in-house
- “institutionalised” in-house procurement

“Pure” in-house

The “pure” in-house context concerns the performance by a contracting authority of certain activities using its own administrative, human and technical resources exclusively, without any support from outside.

Example: An internal department of the contracting authority performs street cleaning services.

In this case, there is no need to award a contract, since there are no externalised activities and no distinct and separate legal entity is involved. The public procurement rules are not applicable in this case, as they are only applicable if a contract is concluded between at least two distinct persons (or legal entities), namely a contracting authority and an entity that is legally separate from the contracting authority.

“Institutionalised” in-house procurement – case law of the CJEU

The situation becomes more complicated when the contracting authority does not perform a certain activity through an internal department, but through an entity that is legally separate from the contracting authority, even though that contracting authority is its founder and owner.

In practice, a contracting authority may establish a company or other type of separate legal entity providing supplies, services or works. The Directive does not include any legal constraints in this respect, and usually the decision to establish such an entity is governed by reasons of efficiency or social considerations. The legal entity established by the contracting authority has its own legal personality.

⁵ SIGMA (2016), Public Procurement Brief 1, *Public Procurement in the EU: Legislative Framework, Basic Principles and Institutions*, OECD Publishing, Paris.

Example: The Ministry of Agriculture establishes a company (Company A) to provide essential services in the field of rural development and environmental protection. The activities and objectives of Company A are as follows:

- to carry out various types of actions, works and services in the areas of agriculture, forestry, rural development, conservation and protection of nature and the environment, aquaculture and fisheries;
- to prepare studies, plans and projects and to provide all types of advice, technical assistance and training in the areas of agriculture, forestry, rural development, environmental protection, aquaculture and fisheries, and nature conservation as well as in respect of the use and management of natural resources.

In this situation, when a contracting authority intends to award a contract for certain supplies, services or works, it needs to consider whether:

- it is necessary to organise a competition and to conduct a tendering procedure where any interested economic operators are invited to participate;
- it is permitted to award the contract directly to a legal entity that it owns.

The general principle and starting assumption is that where a contracting authority plans to conclude a contract for pecuniary interest with an entity that is legally distinct from it, the provisions of the Directive will cover that contract.

Despite this general principle, the award of the contract can be excluded from the scope of the Directive. According to the case law of the CJEU, a legal entity established by a contracting authority may be regarded in specific circumstances as being equivalent to an internal department of that contracting authority. Where the legal entity is equivalent to an internal department, then an arrangement that is made between that legal entity and the contracting authority for the provision of supplies, services or works may fall outside the scope of application of the Directive, provided that specific conditions are strictly observed.

Note: In the remainder of this brief, the term *company* is used for convenience purposes to describe a separate legal entity set up by a contracting authority with the aim of applying the in-house exception.

No restriction is made in the Directive, however, concerning the type of separate legal entity that may be set up by a contracting authority with the aim of applying the in-house exception. Other types of separate legal entities may qualify as in-house entities, provided that they meet the conditions described below.

Limitations of the in-house exception: It is important to understand that when a contracting authority decides to establish its own company to carry out specific activities, this decision does not automatically signify that the in-house exception will apply. The company needs to be set up and to operate in a manner that complies with the conditions set out in the Directive.

The contracting authority needs to understand the application of the in-house exception and the relevant conditions that must be met in order to ensure that the in-house exception will apply to its company. Otherwise, the arrangements made in setting up the company may not be correctly structured or operated so as to qualify the company as “in-house”. In that event, it is possible that the company will not be able to carry out all of its tasks. In the worst-case scenario, the company could be completely useless from the public interest perspective, and it is possible that contracts awarded to the company by the contracting authority (and vice versa) would be considered as illegal, direct awards in breach of the Directive.

In-house conditions (or “Teckal conditions”): The conditions for the in-house exception were defined for the first time in 1998 in the CJEU’s *Teckal* judgement⁶, which is a landmark case as far as the in-house concept is concerned. Over the years, the CJEU has based subsequent rulings on the conditions that were first set out in the *Teckal* case, and it has since considerably expanded and refined the concept of the in-house exception.

The Teckal conditions must be strictly interpreted. Each situation must be investigated on an individual basis, and the burden of proving the circumstances justifying the derogation from the general principle lies with the contracting authority that is seeking to rely on the in-house exception.

Two main conditions must both be satisfied for the in-house exception to apply, or the award of the contract cannot be exempted from the Directive, and the contracting authority will be obliged to organise a competition in accordance with the Directive’s provisions. If both of the conditions are satisfied, the award of the contract will be classified as “in-house” procurement and will not be subject to the Directive.

Condition 1: Control (organisational dependence)

The contracting authority must exercise over the distinct entity a control that is similar to the control that it exercises over its own departments.

The first condition seems to be clear, but it has proved to be difficult to apply in practice, and some clarifications are therefore needed. In order to assess whether the control condition is satisfied, it is necessary to take into account all the legislative provisions in the documents governing the relationship between the parties and of the practical circumstances. The following comments are based on decisions of the CJEU.

Strong organisational relations must be established between the contracting authority and the separate entity, similar to the relations between divisions or departments within any public authority.

The control condition will not automatically be met if the contracting authority sets up a company that is fully owned by that authority. Full ownership indicates a certain control, but it is not sufficient to assert that the control condition has been met. The fact that the contracting authority has 100% public ownership of the company is not a decisive argument⁷.

Of particular importance are the circumstances indicating whether the company is subject to an effective control, enabling the contracting authority to have a decisive influence over both the strategic objectives and the significant decisions of that entity.

The control condition is likely to be fulfilled where the board of the company has a very limited autonomy and where the decisions that can be adopted without prior approval of the contracting authority are strictly related to matters of daily work. The CJEU has decided, for example, that the in-house exception applies where a separate legal entity has no say in the matter when it receives an order from the contracting authority owner, and it does not have the possibility of refusing a task or fixing the tariffs for its activities⁸.

⁶ CJEU Case C-107/98, *Teckal Srl v Comune di Viano and Azienda Gas-Acqua Consorziale (AGAC) di Reggio Emilia*, paragraph 50.

⁷ CJEU Case C-340/04, *Carbotermo SpA and Consorzio Alisei v Comune di Busto Arsizio and AGESP SpA*, paragraph 37: "The fact that the contracting authority holds, alone or together with other public authorities, all of the share capital in a successful tenderer tends to indicate, without being decisive, that that contracting authority exercises over that company a control similar to that which it exercises over its own departments, as contemplated in paragraph 50 of *Teckal*."

⁸ CJEU Case C-295/05, *Asociación Nacional de Empresas Forestales (Asemfo) v Transformación Agraria SA (Tragsa) and Administración del Estado*, paragraphs 60-61: "It appears [...] that *Tragsa* is required to carry out the orders given it by the public authorities [...]. It also seems [...] that [...] *Tragsa* is not free to fix the tariff for its actions and

Example: The demand for each relevant action is formally communicated by the contracting authority to the management of the entity by means of an **instruction** containing, in addition to the appropriate information, the period within which the instruction is to be carried out as well as its value. There is no possibility of negotiation; the tariffs are established exclusively by the contracting authority, in such a way as to reflect the total actual costs. Even in the case where a formal contract has been signed, this document basically reflects only the will of the contracting authority.

Therefore, in line with the contracting authority's power of self-organisation, public procurement rules do not apply if a contracting authority concludes a contract with a third party that is only formally, but not substantially, independent from it.

A company does not fulfil the control condition if it has a board with considerable managerial powers, which may be exercised independently of the owner (the contracting authority). In such cases, the contracting authority is not allowed to award the contract directly to the company and will be obliged to apply the public procurement rules.

Joint control of the company: What happens when two or more contracting authorities together hold all of the share capital in a company? Can the control condition be met in a situation where the control over a company is exercised jointly by several contracting authorities?

The CJEU has clarified that, although control exercised over an in-house entity must be effective, it is not essential for this control to be exercised individually; the control can be exercised jointly by a number of contracting authorities⁹. This control has to be similar to the control that the authorities exercise over their own departments, but it does not need to be identical in every respect.

As a general rule, in order to meet the control condition, each contracting authority must retain a sufficient degree of control so that it has the possibility of restricting the freedom of action of the company concerned.

Example: Three municipalities establish an inter-municipal co-operative, which is a distinct legal person, with specific objectives in the municipal interest. This co-operative comprises a general assembly, a governing council and a board of auditors. Each municipality has representatives in the general assembly and holds the chairmanship of the various inter-municipal management and control bodies. The control that those contracting authorities exercise over the entity is exercised jointly, as each has the power to influence the decision-making process.

A "purely formal affiliation" to the company is not sufficient in the absence of a real capability of exerting control. The starting assumption is that a very small level of participation by one contracting authority in the capital of the company is an indication that it does not have enough power to influence the decisions of that company. This assertion can be overturned, however, in situations where, despite the low level of participation in the capital of the company, that contracting authority is nevertheless able to contribute to effective control, either alone or in conjunction with the other contracting authorities.

Example: The level of participation in the capital of the company becomes irrelevant if a contracting authority holds a *veto* power.

The same situation can be seen where a contracting authority maintains control on the way in which **its own objectives** are to be fulfilled by the company.

Private participation in the company's capital

that its relationships with them are not contractual." and "It seems therefore that *Tragsa* cannot be regarded as a third party in relation to the Autonomous Communities which hold a part of its capital."

⁹ CJEU Case C-324/07, *Coditel Brabant SA v Commune d'Uccle and Région de Bruxelles-Capitale*, paragraph 46.

The next question concerns the situation where, in addition to the public entities holding shares of the capital in the company, a private entity also holds a share of the capital.

As a general rule¹⁰, where a private undertaking participates in the capital of a company in which the contracting authority also participates, the control condition is not fulfilled. The private capital participation excludes the possibility of the contracting authority's exercise of control over that company that is "similar to that which it exercises over its own departments". Any private capital investment indicates the presence of a private interest, which pursues objectives of a different kind to the interests of the public sector. If the company were a semi-public one, a private undertaking having a capital presence in that company would have an advantage over its competitors¹¹. This would be the case even if the private participation was only minor in nature and the contracting authority was able to take independently all decisions regarding that company.

Potential private participation in the company's capital: In this context, it is important to mention that *potential* private investment does not automatically exclude the classification of the contract as an in-house arrangement. As a general rule, the determination of the existence of private participation in the capital of the company to which the public contract is awarded is to be undertaken at the time of the award. The private participation in the company's capital is possible in an undefined future. On the other hand, a real problem would arise if, during the execution of that contract, the capital of the company were opened to private shareholders¹².

Example: A contracting authority awards a contract to a company that it wholly owns, and all of the control conditions are fulfilled at the time of the award. Subsequently, but still during the period for which that contract is valid, private shareholders are permitted to hold capital in that company. This action would constitute an alteration of a fundamental condition of the contract, thereby obliging the contracting authority to put the contract out for competitive tender.

Condition 2: Activity (economic dependence)

The separate entity carries out the essential part of its activities for the contracting authority

This condition aims to limit the participation of the company on the commercial market and to ensure that public procurement law remains applicable if that company is in competition with other undertakings on the market.

The company's activities must be devoted principally to those of the contracting authority, and any other activities should have only marginal significance. The lack of market orientation could be seen as a prerequisite for meeting this condition. A lack of market orientation could be ascertained where the range of the company's activities was limited to the performance of tasks for the contracting authority that owned it and where the geographical scope of the company's activities was restricted to the territory of that contracting authority.

If the company is, or becomes, "market-oriented" or if the objects of its activity are too broad, it will not fulfil the activity condition. Market orientation is also an indication that its degree of independence is too high and, in these circumstances, the company will fail to meet the control condition as well.

¹⁰ A precise exception is provided in Article 12 of the Directive.

¹¹ CJEU Case C-26/03, *Stadt Halle and RPL Recyclingpark Lochau GmbH v Arbeitsgemeinschaft Thermische Restabfall- und Energieverwertungsanlage TREA Leuna*, paragraphs 49-51.

¹² CJEU Case C-573/07, *Sea Srl v Comune di Ponte Nossa*, paragraphs 50-51 and 53.

Example: A contracting authority sets up Company B, and the company's activity is initially limited to the management of a local public car park.

Company B starts to undertake significant amounts of work in new areas of activity, including the transport of persons and supplies, information technology and telecommunications. The new areas of activity are carried out in the context of the market pressures that characterise those markets.

In order to be economically efficient, Company B needs to act in a more commercial manner, by making quick decisions, establishing appropriate tariffs in accordance with the competitive market environment, and permanently adapting its services to customer requirements.

This market orientation is incompatible with the relevant control exercised by the contracting authority, and therefore the powers of the company's management need to be extended. In practice, the contracting authority will lose its influence on the management of Company B and will not be able to maintain effective control.

In order to assess whether the activity condition is satisfied, all of the activities that the company carries out must be taken into account. This requirement is valid regardless of whether those activities are paid for by the contracting authority itself or by the user of the services. If the essential part of the activities is not devoted principally to the contracting authority, the territory in which the activities are carried out is irrelevant¹³.

The CJEU has never indicated precisely what the "essential part" of the activities means. Usually, in the cases analysed, the share of activities performed for the contracting authority (or contracting authorities) was more than 90%, but the CJEU avoided establishing a clear rule. The 2014 Directive resolves this legal uncertainty by introducing a minimum share, which is set at 80%. This minimum share is further explained below.

Where several contracting authorities jointly control a company, the condition relating to "the essential part" of its activities may be met if the company carries out those activities for all of the contracting authorities together.

Provisions of the Directive on the in-house exception

The main objective of the public procurement rules provided by the Directive is to ensure that the award of the relevant public procurement contracts is open to competition among all of the economic operators in the internal market.

At the same time, the Directive does not restrict the freedom of a contracting authority to perform the public interest tasks that have been conferred on it by using its own administrative, technical and other resources, without being obliged to organise a tendering procedure. In this respect, the in-house exception that has been addressed in the CJEU case law has been codified to a large extent in Article 12 of the Directive.

Article 12 clarifies the situation where contractual relations between public entities fall outside of the Directive's scope. It covers both institutionalised in-house procurement and public/public (non-institutionalised) horizontal co-operation.

It is important to emphasise that the codification is general, and does not cover in detail all the facts taken into account and analysed by the CJEU over the years. Therefore, the jurisprudence shall continue to be a relevant source for interpretation of the in-house exemption.

A short analysis of the provisions stipulated in Article 12 of the Directive is presented below:

¹³ CJEU Case C-340/04, *Carbotermo*, paragraphs 66-67.

Institutionalised in-house procurement

Article 12, paragraphs 1 to 3, of the Directive covers institutionalised in-house procurement. Its provisions determine how the control and activity conditions must be satisfied for institutionalised in-house arrangements. It also allows the institutionalised in-house exception to be applied in cases that are considered to be “reverse vertical” or “horizontal institutionalised co-operation”. These terms are further explained below.

According to Article 12 (1) of the Directive:

“A public contract awarded by a contracting authority to another legal person governed by private or public law shall fall outside the scope of the Directive where all of the following conditions are fulfilled:

- a) the contracting authority exercises over the legal person concerned a control which is similar to that which it exercises over its own departments;
- b) more than 80% of the activities of the controlled legal person are carried out in the performance of tasks entrusted to it by the controlling contracting authority or by other legal persons controlled by that contracting authority; and
- c) there is no direct private capital participation in the controlled legal person with the exemption of non-controlling and non-blocking forms of private capital participation required by national legislative provisions, in conformity with the Treaties, which do not exert a decisive influence on the controlled legal person.”

In the text of Article 12 (1) not only the main two conditions (control and activity) laid down by the Teckal judgement can be identified, but also the subsidiary requirement related to ownership.

Control: Subparagraph a) refers to the control condition, reiterating the requirement established by the CJEU that the control exercised by the contracting authority over the company it owns must be “similar to that which it exercises over its own departments”.

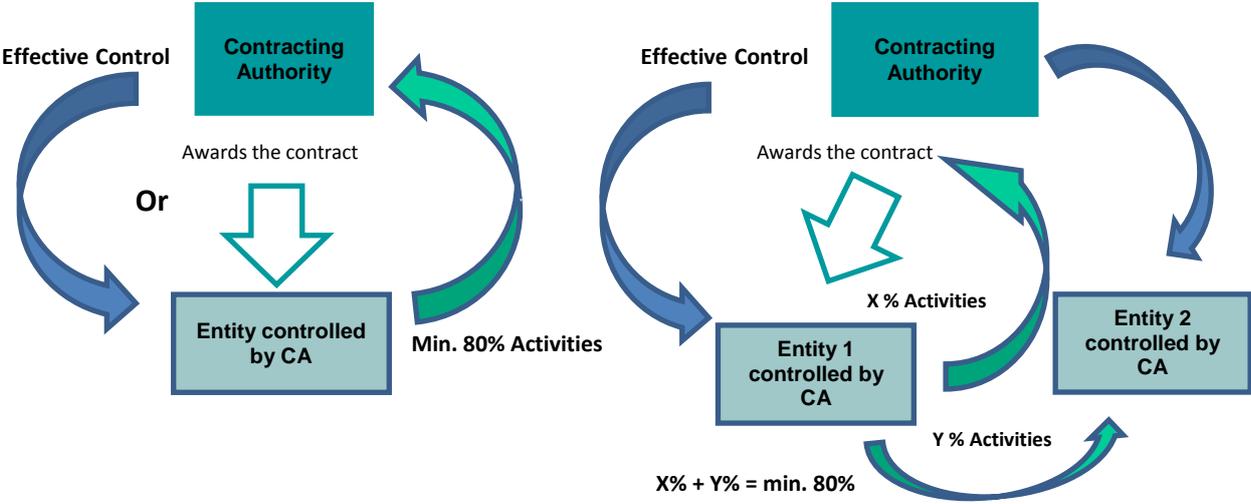
This control requirement is further explained in the second subparagraph of Article 12 (1). This provision confirms that a contracting authority is deemed to exercise the required level of control where it exercises “a decisive influence over both strategic objectives and significant decisions” of the company.

Chain of control: The second subparagraph of Article 12(1) adds a further possibility. It confirms that a chain of control is possible: “Such control may also be exercised by another legal person, which is itself controlled in the same way by the contracting authority.”

Activity: A clear explanation is now provided in subparagraph b) for the previously undefined expression “essential part of activities”. This fundamental portion is equated with more than 80% of the company’s activities.

In the same subparagraph b), it is clear that the 80% activity requirement can be met by performing activities not only for the contracting authority that is the owner of the separate entity, but also for other legal persons controlled by that contracting authority.

These two situations can be represented as follows:



Ownership: With regard to the third subsidiary condition, in subparagraph c), a provision has been added that is not derived from CJEU case law. While, apparently, according to the CJEU any form of private capital participation is not permitted, the provisions of subparagraph c) allow for “non-controlling and non-blocking forms of private capital participation”, provided that this participation is required by national legislative provisions, in conformity with the Treaties, and only if such participation does not accord the power to exert a decisive influence on the controlled legal person.

“Reverse vertical” institutionalised co-operation: According to Article 12 (2) of the Directive, the in-house exception can be applied in the case of “reverse vertical” co-operation.

The contractual arrangements examined so far in this brief assume that a contracting authority awards a contract to a company that it owns. The “reverse vertical” exception covers the situation where the company owned by a contracting authority and satisfying the *Teckal* conditions described above, awards a contract to its contracting authority owner. Where specific conditions are met, the company may grant such an award without having to apply the Directive.

According to Article 12 (2) of the Directive:

“Paragraph 1 also applies where a controlled legal person which is a contracting authority awards a contract to its controlling contracting authority, or to another legal person controlled by the same contracting authority, provided that there is no direct private capital participation in the legal person being awarded the public contract with the exemption of non-controlling and non-blocking forms of private capital participation required by national legislative provisions, in conformity with the Treaties, which do not exert a decisive influence on the controlled legal person.”

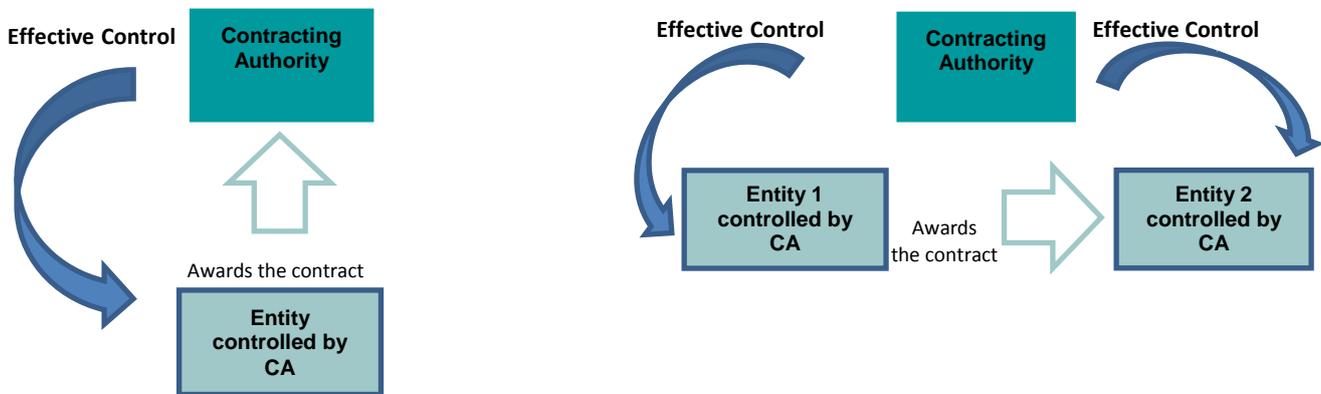
The condition that there should be no direct, private capital participation in the legal person being awarded the contract is a prerequisite for the in-house exception, and this condition is applied in the “reverse-vertical” situation.

In the case where the controlled entity awards a contract to the “parent”, the in-house logic – the lack of two entities with independent wills – is still pertinent.

“

Reverse-vertical” institutionalised co-operation

Horizontal” institutionalised co-operation



Article 12 (2) clearly states that the in-house exception can also be applied in the case of “horizontal” institutionalised co-operation, which is where a contracting authority owns more than one company, both of which satisfy the Teckal tests (“sister” companies).

The condition that there be no direct private capital participation in the legal person being awarded the contract is a prerequisite for the in-house exception, and it is again applied in this situation of “horizontal” institutionalised co-operation.

In the case of contracts between “sisters”, neither entity controls the other, but the same “parent” controls both “sisters”. It is considered that they are both fully subordinated to the contracting authority, and the decision to award the contract to one of the “sisters” is the result of an order given by the controlling contracting authority.

Moreover, the task to deliver certain supplies, services or works to the purchasing “sister” is also the result of an order given by the controlling contracting authority.

Consequently, none of the entities has an independent will, and therefore the in-house logic is applicable.

Test 1 – the activity condition, in the context of “reverse-vertical” and “horizontal” institutionalised co-operation: As the text of Article 12 (2) is silent regarding the activity condition, it could be inferred that this condition is not applicable in the cases of “reverse-vertical” and “horizontal” institutionalised co-operation. However, paragraph (2) should be read together with paragraph (1), although there is still room for interpretation as it is unclear which entity is obliged to meet the activity condition.

In the case of “horizontal” institutionalised co-operation, the logical answer would be that at least the provider “sister” must fulfil the condition.

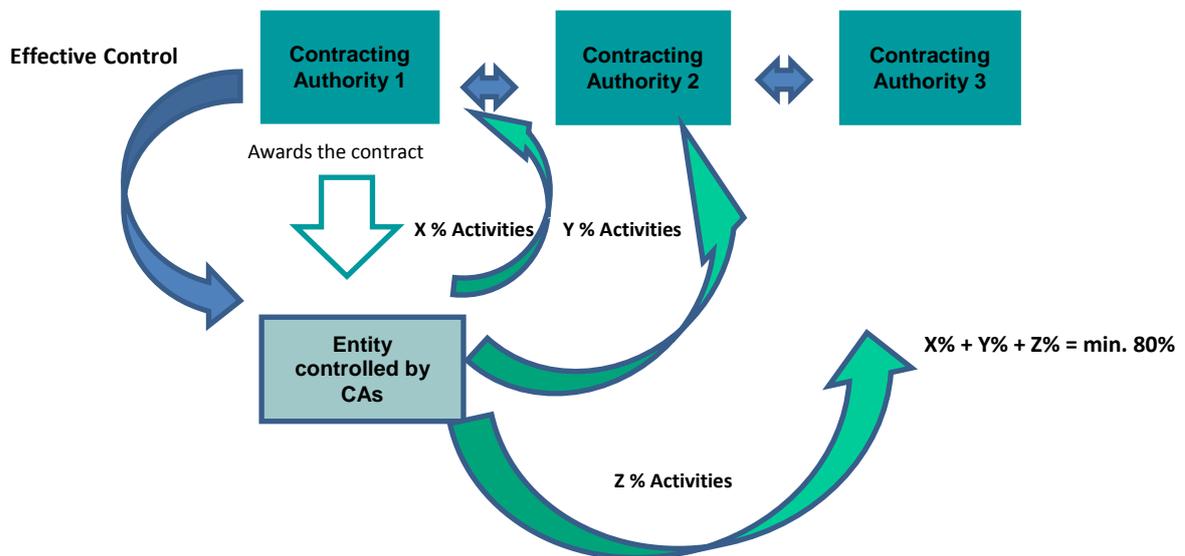
The question remains unanswered in the case of “reverse-vertical” institutionalised co-operation, where the Directive does not clarify whether the contracting authority or the entity should fulfil the activity condition.

Joint control: Article 12 (3) specifies that a contracting authority may award a public contract directly to an entity over which it exercises the control jointly with other contracting authorities, even if it cannot control the economic operator individually.

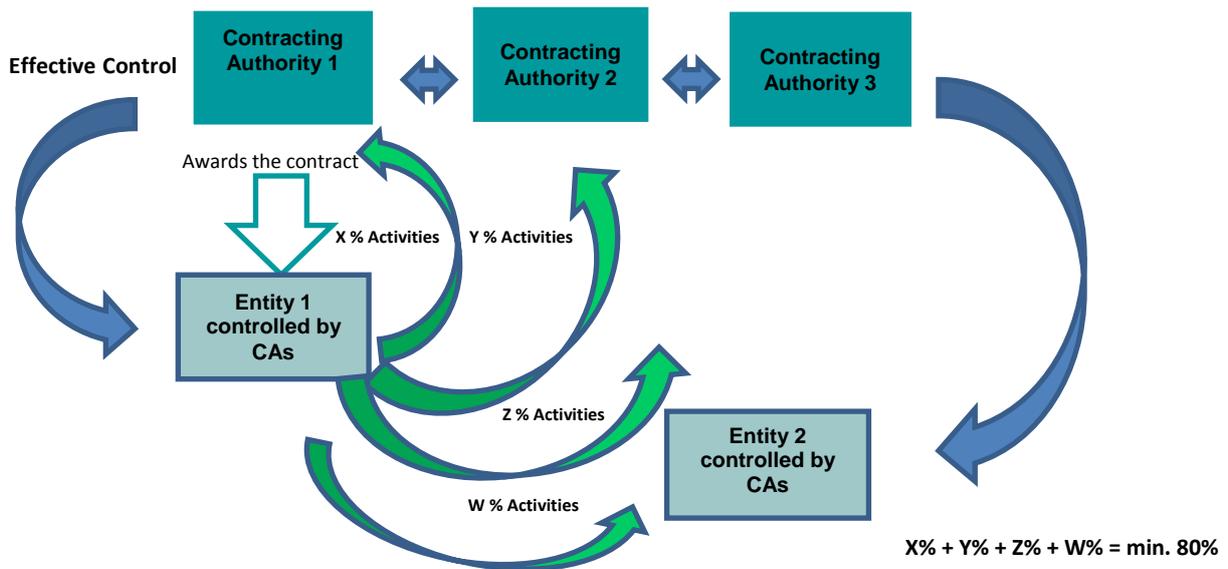
According to Article 12 (3) of the Directive:

“A contracting authority, which does not exercise over a legal person governed by private or public law control within the meaning of paragraph 1, may nevertheless award a public contract to that legal person without applying this Directive where all of the following conditions are fulfilled:

- a) the contracting authority exercises jointly with other contracting authorities a control over that legal person which is similar to that which they exercise over their own departments;
- b) more than 80 % of the activities of that legal person are carried out in the performance of tasks entrusted to it by the controlling contracting authorities or by other legal persons controlled by the same contracting authorities; and
- c) there is no direct private capital participation in the controlled legal person with the exception of non-controlling and non-blocking forms of private capital participation required by national legislative provisions, in conformity with the Treaties, which do not exert a decisive influence on the controlled legal person.”



Or



The second subparagraph of Article 12 (3) establishes three conditions to be fulfilled in the exercise of joint control:

“For the purposes of point (a) of the first subparagraph, contracting authorities exercise joint control over a legal person where all of the following conditions are fulfilled:

- i) the decision-making bodies of the controlled legal person are composed of representatives of all participating contracting authorities. Individual representatives may represent several or all of the participating contracting authorities;
- ii) those contracting authorities are able to jointly exert decisive influence over the strategic objectives and significant decisions of the controlled legal person; and
- iii) the controlled legal person does not pursue any interests which are contrary to those of the controlling contracting authorities.”

The first two points reiterate to some extent specific aspects resulting from CJEU case law. In addition, the third point states that the controlled legal person is not allowed to pursue any interests that are contrary to those of the controlling contracting authorities.

Article 12 does not contain any provisions regarding “reverse-vertical” and “horizontal” institutionalised co-operation, where more than one contracting authority exercises control over a legal person (a joint control situation). This omission denotes that the in-house exception is not applicable in such situations and that a jointly controlled company is not allowed to award a contract to one of its “parents” or “sisters”.

“Public/public” co-operation and “non-institutionalised” horizontal co-operation

Article 12 (4) regulates those cases that are usually referred to as “public/public” co-operation or “non-institutionalised” horizontal co-operation. In these cases two or more contracting authorities may establish horizontal co-operation, without creating a jointly controlled in-house entity.

In its Hamburg judgement¹⁴, the CJEU accepted this public/public exception, explaining that EU law did not require contracting authorities to use any particular legal form in order to jointly carry out their public service tasks.

The public/public exception involves the conclusion of contracts that are not covered by public procurement rules if certain conditions are met. These conditions are codified in Article 12 (4) as follows:

“A contract concluded exclusively between two or more contracting authorities shall fall outside the scope of this Directive where all of the following conditions are fulfilled:

- the contract establishes or implements a cooperation between the participating contracting authorities with the aim of ensuring that public services they have to perform are provided with a view to achieving objectives they have in common;
- the implementation of that cooperation is governed solely by considerations relating to the public interest; and
- the participating contracting authorities perform on the open market less than 20% of the activities concerned by the cooperation.”

Article 12 (5) establishes the basic rules for calculating the percentage of activities referred to in the set of conditions related to the verification of the existence of an effective control.

The average total turnover or “an appropriate alternative activity-based measure, such as costs incurred by the relevant legal person or contracting authority with respect to services, supplies and works... shall be taken into consideration”. The relevant period for calculating the turnover covers the last three years preceding the award of the contract. Where these indicators are not available for the preceding three years, or are no longer relevant due to the date on which the relevant legal person or contracting authority was created or to a re-organisation of activities, “it shall be sufficient to show that the measurement of activity is credible, particularly by means of business projections”.

Other exceptions

Two other situations are provided for in the Directive, which it is appropriate to mention in the context of in-house and public/public co-operation exceptions. These are not in-house or co-operation arrangements, but they may be considered as possible alternatives when discussing the availability of these exceptions. They are service contracts awarded on the basis of an exclusive right and central purchasing bodies.

The contracting authority is permitted to award a contract to a distinct and separate public entity without being obliged to organise a competition in both of these contexts.

Service contracts awarded on the basis of an exclusive right: Article 11 of the Directive stipulates the following:

“This Directive shall not apply to public service contracts awarded by a contracting authority to another contracting authority or to an association of contracting authorities on the basis of an exclusive right which they enjoy pursuant to a law, regulation or published administrative provision which is compatible with the TFEU.”

¹⁴ CJEU Case C-480/06, Commission v Germany.

In this case, the right to perform a specific (economic) activity is granted by law, which also establishes which entity will be the holder of that exclusive right. That entity is always a contracting authority, and as a result of the exclusivity acquired, it represents the sole source for that particular service.

In this case, competition from private-service providers is not possible and, as a result, the contracting authority concerned is exempted from the obligation to conduct tendering procedures.

Only in a limited number of cases can exclusive rights be granted to entities, in accordance with the Treaties, since exclusive rights constitute a restriction to the four freedoms of the internal market. This approach may be used where the performance of a particular service of general economic interest would not be provided, or not to an adequate degree, by the market, and therefore public intervention is imperative. For this reason, the service concerned can **only** be ensured by means of the grant of exclusive rights to a contracting authority, provided that the development of trade is not affected to such an extent as would be contrary to the interests of the Community.

Example: It might be justified to grant an exclusive right to a specialised public body for the provision of occupational training and language training for immigrants, although potential solutions can be found on the market. However, due to the current sensitivity of immigration issues, public intervention could be seen as crucial.

Central purchasing bodies: Article 37 of the Directive provides for a particular situation where a central purchasing body performs specific service on the basis of a special right.

A central purchasing body is a contracting authority that provides centralised purchasing activities (and, possibly, ancillary purchasing activities). According to the Directive, Member States may provide that contracting authorities may acquire supplies and/or services from a central purchasing body. Member States may also provide that contracting authorities may acquire works, supplies and services by using contracts awarded by a central purchasing body, dynamic purchasing systems operated by a central purchasing body, or framework agreements concluded by a central purchasing body.

Example: Hansel, Finland is a central purchasing body that concludes framework agreements covering, among other supplies and services, ICT hardware, software and services; administrative services (financial administration, organisational and human resource development, travel and conference management); materials and technical services (material and facility services, vehicle and transport services, office and energy supply services).

The special right for central purchasing bodies to provide centralised and ancillary purchasing activities is conferred in the Directive. Contracting authorities are allowed to award a public service contract for the provision of centralised purchasing activities to a central purchasing body, without having to apply the procedures provided for in the Directive.

However, central purchasing bodies do not have exclusive rights, because contracting authorities are generally not obliged to use the services that these bodies perform. In some countries, central government authorities are obliged to do so, but only for a limited list of items.

The rationale for this exception is the goal of obtaining economies of scale, including lower prices and transaction costs, and the concern for improving and professionalising procurement management. As the aggregation of demand by public purchasers is seen as a good tool for achieving such objectives, it was natural to set up an appropriate legal framework for supporting and encouraging this trend.

It should be noted that only the acquisition of (centralised/ancillary) purchasing activities falls outside the common procurement rules. Central purchasing bodies must fully comply with the provisions of the Directive when they award contracts or conclude framework agreements.

For further information, see SIGMA Public Procurement Brief 20, *Central Purchasing Bodies*.

Utilities

The same in-house and public/public exceptions apply under the Directive and the Utilities Directive¹⁵. The CJEU has applied the same interpretation to both the public sector and the utilities sector. For this reason, the two Directives have parallel provisions: the text of Article 28 of the Utilities Directive is identical to that of Article 12 of the Directive.

In addition to the in-house and public/public exceptions, which are applicable only to contracting authorities, the Utilities Directive provides, in Articles 29 and 30, special exclusions that are applicable to all contracting entities.

Article 29 Affiliated undertakings and Article 30 Joint ventures

Where the term “undertakings” comprises a number of mutually-owned or mutually-dependant companies, a specific exclusion, under certain conditions, is provided for purchases made between these companies. These purchases are similar to “in-house” contracts, although the conditions are not exactly the same.

The contracts excluded are those that have been awarded to affiliates, whose essential purpose is to act as central service-providers to the group to which they belong, rather than selling their services commercially on the open market.

Two categories of contracts are excluded. The first category includes contracts awarded:

- by a contracting entity to an affiliated undertaking;
- by a joint venture, formed exclusively by a number of contracting entities for the purpose of carrying out relevant activities, to an undertaking that is affiliated to one of the contracting entities.

Affiliated undertakings (Article 29, Utilities Directive): An affiliated undertaking is one in which the annual accounts are consolidated with those of the contracting entity, in accordance with the requirements of the Accounting Directive 2013/34/EU (Accounting Directive)¹⁶.

In the case of contracting entities not subject to the Accounting Directive, an affiliated undertaking is any undertaking over which the contracting entity may exercise, directly or indirectly, a dominant influence, in the same way as a public authority may exercise a dominant influence over a public undertaking. This position will be the same where it is the undertaking that exercises a dominant influence over the contracting authority or where both the undertaking and the contracting entity are subject to the dominant influence of a third undertaking.

This exclusion is nevertheless subject to a specific condition: the undertaking must exist essentially to provide supplies, services or works to the group and not to sell them on the open market. The exclusion only applies if at least 80% of the average turnover of the affiliated undertaking over the preceding three years has derived from the provision of supplies, services or works to undertakings with which it is affiliated.

Where more than one undertaking affiliated to the contracting entity provides the same or similar supplies, services or works, the above percentages are calculated by taking into account the total

¹⁵ Directive 2014/25/EU on procurement by entities in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC, 26 February 2014.

¹⁶ Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, 26 June 2013.

turnover derived respectively from the provision of services, supplies or works by those affiliated undertakings.

Joint ventures (Article 30, Utilities Directive): The second category of contracts subject to the special exclusion includes contracts awarded:

- by a joint venture, formed exclusively by a number of contracting entities for the purpose of carrying out relevant activities, to one of those contracting entities;
- by a contracting entity to a joint venture of which it forms a part.

This exclusion is subject to the conditions requiring the joint venture to be set up to carry out the activity concerned over a period of at least three years and the instrument setting up the joint venture to stipulate that each of the contracting entities forming the joint venture is to be part thereof for at least the same period.

Further information

Publications

SIGMA (2015), *Public Procurement Training Manual* – Module D3, OECD Publishing, Paris,
<http://www.sigmaweb.org/publications/public-procurement-training-manual.htm>

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SIGMA (2016), *Public Procurement in the EU: Legislative Framework, Basic Principles and Institutions*, Brief 1, OECD Publishing, Paris

SIGMA (2016), *Central Purchasing Bodies*, Brief 20, OECD Publishing, Paris