

European and German Public Procurement Law Update

February 2005

The Scope of In-House Procurement Narrowed by ECJ Several New EC-Treaty Infringement Cases Against Germany

The freedom to award contracts to joint public-private companies or public authorities without the need for compliance with formal award procedures has been the subject of intense debate. In two recent judgments, the European Court of Justice (ECJ) further narrowed such a freedom to a bare minimum. The Court also extended judicial review to contract awards that are made without any formal award procedure.

The European Commission has been monitoring Germany's public procurement practice in this area for quite some time. In January 2005, it decided to pursue several more cases against Germany, alleging infringement of EU law and trying to enforce a broader scope of application of public procurement law.

These developments on the European level will have a significant impact on the ongoing reform of the German procurement law.

I. ECJ: NARROWER SCOPE FOR IN-HOUSE PROCUREMENT

In two recent judgments of January 11, 2005 (Case C-26/03, "City of Halle") and January 13, 2005 (Case C-84/03, "Commission v. Spain") the European Court of Justice (ECJ) narrowed the scope of the so-called "in-house transactions" with (semi-) public entities and thereby broadened the applicability of public procurement law in the Community.

The key elements of these decisions are:

- A contracting authority cannot award a contract outside a formal award procedure if the shares in the contractor are held

partly by a private undertaking, irrespective of whether the private shareholding is a minority or majority participation.

- As a matter of principle, cooperation agreements between state authorities on the one hand and any other public body on the other hand, or between such bodies themselves, fall within the scope of public procurement law. An exception applies only if the state authority exercises over the entity concerned a control which is similar to that which it exercises over its own departments and, at the same time, that entity carries out the essential part of its activities with the controlling state authority or authorities.
- Judicial review of contract awards is also available against a decision by a contracting authority not to initiate a formal award procedure. Such proceedings may be initiated by any person having an interest in obtaining the contract who has been or risks being harmed by an alleged infringement of procurement law rules.

Consequences:

As a consequence of these judgments, contracting authorities will in future only be able to award contracts to companies without public award procedures if the contracting authority holds 100% of the shares in the contractor. However, a call for tender is mandatory if the contract is to be awarded to a company in which a private investor has a shareholding.¹

Concurrently, the ECJ has strengthened the rights of (potential) bidders. As a result, not only must contracting authorities pay greater attention in order to comply with

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“No In-House-Transaction if a contract is awarded to a joint public-private-entity”

public procurement laws, it is also important for contractors to ensure that such rules are adhered to, since any violations may result in the invalidity of the contract entered into with the contracting authority.

Moreover, public authorities and private investors should pay regard to the Court's judgments when contemplating the privatization of state-owned entities or the development of public-private-partnership projects. As regards public-public cooperation agreements, the consequences of the ECJ's judgment remain to be seen. The decision could open up currently protected markets to private investors, particularly in the waste, water and sewage industries.

In Detail:

Scope of In-House Transactions. In the “City of Halle” decision (Case C-26/03), the ECJ was faced with a number of questions referred to it by the OLG Naumburg (Court of Appeals). Without formally announcing a call for tenders, the City of Halle had awarded a contract to a company in which 75% of the capital was held indirectly by the City itself and the remainder by a private company. The ECJ affirmed its previous opinion that public authorities may perform their tasks by using their own administrative, technical and other resources without being obliged to call on outside entities. In such a case, they are not required to apply public procurement law. If, however, the contractor is an entity legally distinct from the contracting authority, a call for tender is mandatory unless the “contracting authority exercises over the separate entity concerned a control which is similar to that which it exercises over its own departments and that entity carries out the essential part of its activities with the controlling public authority or authorities” (Case C-107/98, “Teckal”). In the “City of Halle” case, the ECJ has now held that “the participation, even as a minority, of a private undertaking in the capital of a company in which the contracting authority in question is also a participant excludes in

any event the possibility of that contracting authority exercising over that company a control similar to that which it exercises over its own departments.” (Case C-26/03, para 49).

Public-Public Cooperation Agreements. In the case C-84/03 (“Commission v. Spain”) the ECJ had to assess as to whether Spain had adequately transposed the Supplies and Public Works Coordination Directives into national law. The disputed rules in the Spanish public procurement statute excluded from its scope ‘cooperation agreements between the State authorities, on the one hand, ... any other public body, on the other hand, or between these bodies.’ In Germany, the treatment of such contracts was highly disputed. Whereas one Court of Appeals held that municipal co-operations in the field of public transport were not subject to public procurement law,² the Courts of Appeals of Düsseldorf and Frankfurt/Main came to the opposite conclusion with regard to municipal waste collection and disposal co-operations.³ The ECJ has now backed the latter decisions by applying the Teckal-principles to public-public cooperation agreements. Therefore, public procurement law is applicable to such cooperation agreements unless (i) the local authority exercises over the entity concerned a control which is similar to that which it exercises over its own departments and, (ii) at the same time, that entity carries out the essential part of its activities with the controlling local authority or authorities. (Case C-84/03, para 38).

Judicial Review. Finally, in the “City of Halle” case, the ECJ clarified the position as to the amenability to judicial review of contract awards made without any prior formal award procedure. Until now, the majority of German courts has held that such awards – made after a decision by a contracting authority not to initiate a public award procedure – are generally not subject to judicial review. In contrast, the ECJ has now taken the view that a contracting authority's decision not

1. For sector contracting entities, Art. 23 of Directive 2004/17/EC sets forth special rules for contracts awarded to an affiliated undertaking. Under these rules, public procurement law shall – in general – not apply to such contracts provided that at least 80 % of the average turnover of the affiliated undertaking with respect to services, supplies or works for the preceding three years derives from the provision of such services, supplies or works to undertakings with which it is affiliated.

2. OLG Koblenz, decision of 12/20/2004, NZBau 2002, 346.

3. OLG Düsseldorf, decision of 5/5/2004, NZBau 2004, 398; OLG Frankfurt/Main, decision of 9/7/2004, NZBau 2004, 692.

to initiate a public award procedure may be regarded as the counterpart of its decision to terminate such a procedure. Therefore, where a contracting authority decides not to initiate an award procedure on the ground that the contract in question does not, in its opinion, fall within the scope of the relevant Community rules, such a decision constitutes the very first decision amenable to judicial review. Judicial review is accessible regardless of whether that act is adopted outside a formal award procedure or as part of such a procedure. (Case C-26/03, para 33 and 34).

II. EUROPEAN COMMISSION: SEVERAL INFRINGEMENT CASES AGAINST GERMANY

On January 14, 2005 the European Commission decided to pursue seven alleged infringement cases against Germany concerning the award of service contracts and concessions without competition.⁴ In one of these cases, the Commission has referred the matter to the ECJ, whereas in the other cases the Commission has issued reasoned opinions.

- **Public-Public Cooperation Agreements.** The Commission has taken the view that EU procurement rules have been violated as a result of a) the award of a service concession for the provision of sewage disposal services by the City of Hinte (Lower-Saxony) to a public sewage disposal association, and b) the award of a long-term service contract for waste disposal services by several counties in Lower-Saxony to the public city cleaning authority of Hamburg, both without formal award procedures. In these cases, the Commission's views appear to be in line with the principles laid down in the ECJ's judgment concerning public-public cooperation agreements.
- **In-House Transaction.** Furthermore, the Commission is taking action against the award of a waste disposal services contract to a company in which the contracting authority – the waste disposal corporation of the Rhine-Neckar-County (Baden-Wuerttemberg) – holds 51% of the shares. According to the

view taken by the Commission, the award does not constitute an in-house transaction and is, therefore, subject to public procurement law. The recent ECJ decisions would also support the Commission's standpoint in this case.

- **Award Procedure for Contracts below Threshold Values.** With regard to two other cases concerning contract awards made by German museums and the City of Oestrich-Winkel (Hesse) without prior notification, the Commission holds the view that, even in respect of contracts below the EU-threshold values, the principles of EU law require an adequate and transparent award procedure. This would preclude a direct award if a developed European market for the respective service exists, or indeed any direct award made without any form of advertising or publicity.

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**“Public-Public
cooperation agreements
generally fall within the
scope of public
procurement law”**

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4. IP/05/44, dated 1/14/2005.

5. Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, Official Journal L 134 of 4/30/2004, p. 1.

6. 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; Official Journal L 134 of 4/30/2004, p. 114.