

Public procurement and State aid control — the issue of economic advantage

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1. Introduction

In recent years, the Commission received several State aid notifications in which Member States asked the Commission to confirm in advance that the complex public procurement transactions they were planning would not lead to the granting of State aid. This indicates some uncertainty regarding the application of State aid rules in the case of public procurement: Are public procurements affected by the State aid rules at all? If so, what would be considered State aid in this context? How could this be avoided before concluding the contract award procedure?

Based on the Commission's experience in the field of telecommunications and in particular of a recent State aid decision concerning the procurement of broadband services, this article aims at clarifying the above issues.

2. Procurement and State aid in general

Public purchases of goods, services and infrastructure in all EU Member States are subject to public procurement rules. These aim at creating a level playing field for private operators to compete for public contracts, and to increase the efficiency of public expenditure. The public procurement rules of the Member States are coordinated by two EU Directives adopted on the basis of the Treaty provisions on freedom of establishment and free movement of services:

- Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public service contracts and public supply contracts; and
- Directive 2004/17/EC on the coordination of the procurement procedures of entities operating in the water, energy, transport and postal services sectors ⁽²⁾.

⁽¹⁾ Directorate-General for Competition, unit C-4. The views expressed are purely those of the authors and may not under any circumstances be regarded as stating an official position of the European Commission. Responsibility for the information and views expressed lies entirely with the authors.

⁽²⁾ In addition to these two directives concerning the procedures for the award of public contracts, there are two directives concerning the remedies available in the field of public procurement (Directive 89/655/EEC and Directive 92/13/EEC), which have been amended by Directive 2007/66/EC.

These Directives do not cover all public procurement throughout the EU. For instance, contracts with a value below certain thresholds and service concessions ⁽³⁾ are outside their scope. However, these contracts are also subject to the general principles of the EC Treaty concerning transparency and non-discrimination ⁽⁴⁾.

As there are detailed secondary rules at Community level concerning the award of public contracts, it could be argued that there is no reason for the same contracts to be subject to State aid control as well. However, automatically exempting public purchases from State aid control would not be in line with Article 87 (1) of the EC Treaty, which refers without distinction to “any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market”. Therefore, procurement transactions may fall within the scope of State aid control and may be prohibited if they qualify as State aid.

Such a transaction would be considered to have benefited from State aid if it displays all of the following characteristics:

- it is financed directly or indirectly through State resources;
- it confers an economic advantage to undertakings ⁽⁵⁾ exercising an economic activity;
- the advantage is selective and distorts or threatens to distort competition; and
- it has an effect on intra-Community trade.

⁽³⁾ In line with the procurement directives, a service concession “is a contract of the same type as a public service contract except for the fact that the consideration for the services consists either solely in the right to exploit the service or in this right together with payment.”

⁽⁴⁾ See for instance the judgement of the European Court of Justice in the case C-324/98 *Telaustria and Telefonadress* [2000] ECR I-10745 and the Commission Interpretative Communication on the Community rules applicable to contract awards not or not fully subject to the provisions of the Public Procurement Directives, OJ C 179, 1.8. 2006, p. 2.

⁽⁵⁾ The concept of an undertaking encompasses every entity engaged in an economic activity, regardless of the legal status of the entity and the way in which it is financed. See for instance: judgement of the Court of 23 April 1991 in case C-41/90, *Klaus Höfner and Fritz Elser vs Macrotron GmbH*.

Since according to the jurisprudence of the European courts, the majority of public procurements could be considered as being financed through State resources ⁽⁶⁾, the key issue is to consider whether, and under which conditions, public procurement favours certain undertakings by giving them an economic advantage. In case there is an economic advantage above the de minimis threshold ⁽⁷⁾ under the State aid rules, the remaining conditions concerning selectivity, distortion of competition ⁽⁸⁾ and effect on trade are likely to be met.

The issue of economic advantage

In line with the case law of the European Courts, the concept of economic advantage under the State aid rules includes any advantage “*which the recipient undertaking would not have received under normal market conditions*”. With regard to the economic operator selected as a result of a tender procedure, this implies that if a public purchase corresponds to a normal commercial transaction and the authorities are paying a market price for the works, goods or services procured, no State aid is involved. However, the question is: what is necessary in practice to meet the market economy buyer test in the case of public procurement?

In the field of State aid, the use of competitive, transparent and non-discriminatory public tenders has traditionally been considered sufficient to presume that no State aid is provided to the economic operator selected as a result of the procedure. In the London Underground Public-Private Partnership case ⁽⁹⁾, the Commission concluded that “*when these types of infrastructure arrangements are concluded after the observance of an open, transparent and non-discriminatory procedure, it is, in principle, presumed that the level of any market sector support can be regarded as representing the market price for the execution of the project.*”

⁽⁶⁾ There may be some exceptions in the case of contracts granted by contracting entities (in particular private undertakings operating on the basis of special or exclusive rights) in the field of utilities, depending on whether these entities may be considered as being under State control. However, these considerations go beyond the limits of the present article.

⁽⁷⁾ Up to € 200,000 may be granted to an undertaking over any period of three years without prior Commission approval, see Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty to de minimis aid, OJ L 379, 28.12.2006.

⁽⁸⁾ Except in the case of the provision of general infrastructure with public funds, where no selectivity element would be present as regards the users of the infrastructure.

⁽⁹⁾ Case N 264/2002 *London Underground Public Private Partnership*, para 79

This conclusion should lead to the assumption that, in principle, no State aid is involved”. Albeit in a different context, the Altmark judgement of the European Court of Justice concerning services of general economic interest also expressed the view that public procurement procedures allow for the selection of the tenderer capable of providing the given services “*at the least cost to the community*” ⁽¹⁰⁾.

However, in practice, the assessment of procurement transactions under the State aid rules before they have taken place has not always been entirely straightforward. Sometimes, doubts have been expressed concerning the ability of certain procurement procedures to guarantee a market price. In addition, it has also been argued that the Commission would not be in a position to declare in advance that State aid would not be provided through a particular tender procedure. Moreover, especially in the case of the provision of network infrastructures or network services, it has been suggested that the presence of aid at the level of the end users or third parties should also be considered. More recently, a notification concerning the procurement of broadband services for the public sector in Wales gave the Commission an opportunity to clarify these issues.

3. The Welsh Public Sector Network Scheme ⁽¹¹⁾

The notification submitted by the UK authorities concerned the procurement of high bandwidth network services by the Welsh Assembly Government for public sector organisations in Wales.

Initially, public organisations in Wales had their own networks, which were procured separately by the different public service organisations. According to the UK authorities, this resulted in higher costs, lack of sufficient connectivity and duplication of resources. Moreover, in their view, the fragmentation and lack of interconnectivity, interoperability and common network standards between the Welsh public service bodies reduced the efficiency of public services and hampered their improvement.

In order to address the above shortcomings, the Welsh Assembly Government decided to award a service contract for the provision of consolidated network services. The public service contract included:

⁽¹⁰⁾ Case C-280/00 *Altmark Trans and Regierungspräsidium Magdeburg* [2003] ECR I-7747, para 93

⁽¹¹⁾ Case N 46/2007 “*Welsh Public Sector Network Scheme*”, United Kingdom, of 30.5.2007, see http://ec.europa.eu/community_law/state_aids/comp-2007/n046-07.pdf

- (i) a collective electronic communications network service consisting of a range of core infrastructure services;
- (ii) an initial connection of selected public sector organisations (around 1000 connections shared between the Health Service, local government and the Higher Education / Further Education Sectors).

Given that the existing networks of private operators already reached 98 % of all public buildings in Wales, there appeared to be no need for significant new infrastructure.

The procurement aimed to ensure common standards of service, increased interoperability and extended service reach throughout Wales. This allowed these organisations to work more effectively together and to improve the delivery of public sector services to the citizens. By aggregating the needs of the individual bodies and conducting a centralised procurement, the procurement also aimed to avoid duplications and to make economies of scale.

In view of the particular complexity of the public contract⁽¹²⁾, the Welsh Assembly Government followed the competitive dialogue procedure in compliance with the Directive 2004/18/EC, awarding the contract to the most economically advantageous tender. For the application of this award criterion, several sub-criteria were used concerning commercial, technical and quality aspects, risk distribution and contractual compliance. The UK authorities also envisaged specific mechanisms to ensure that the price paid would remain cost effective (gain sharing, benchmarking by means of independent reviews of tariffs and service performance, etc.).

The contract award procedure was not yet concluded at the time of the State aid assessment. In line with the general considerations outlined above, the pivotal point of the Commission's assessment under the State aid rules was whether the procurement of the Welsh Public Sector Network Scheme provides an economic advantage to any undertaking within the meaning of Article 87 (1) of the EC Treaty.

⁽¹²⁾ The Welsh authorities considered the public contract particularly complex, since there were a large number of various users with different service requirements and needs (for instance in case of security, bandwidth or managed services) and these differences had to be dealt with in the implementation of a single managed network. Moreover, the best technical means for achieving the new network were not known.

Advantage to the service provider

In relation to the service provider, the decision of the Commission confirmed the possibility to assess in advance that a procurement transaction does not involve State aid to the operator selected as a result of the procedure. The Commission concluded that the award of the contract would not provide any economic advantage to the service provider which would go beyond market conditions. To arrive at this conclusion, the Commission first ascertained that the award of the contract was a pure procurement transaction, aiming to satisfy a public need⁽¹³⁾. This was clearly the case since the objective was to purchase network services for UK public service organisations.

Furthermore, the Commission verified whether a competitive procurement procedure was being carried out in compliance with the EU public procurement rules. In this context, it has also examined whether in line with the requirements of the public procurement directives, the award criteria correspond to the objective of achieving best value for money. This condition was also met. The award in question was made in line with the EU procurement directives, using a competitive procurement procedure with prior publication at EU level in which any economic operator could request to participate under equal conditions. In compliance with the requirements of Directive 2004/18/EC, the contract was to be awarded to the most economically advantageous tender, using criteria which corresponded to the objective of achieving best value for money.

The Commission also concluded that the contract did not give rise to extra advantages to the service provider beyond the scope of the contract. Beyond the initial order fixed in the public service contract, there was no obligation for the public service organisations to use the connectivity services provided by the service provider. In addition, the provision of the network services did not result in additional spare capacities which could have been exploited commercially. Finally, the Commission valued positively the fact that there were appropriate mechanisms to ensure cost-effectiveness over the whole duration of the contract⁽¹⁴⁾.

⁽¹³⁾ In general, public procurement serves to satisfy a public sector need, by definition. However, it cannot be excluded that, in certain exceptional circumstances, the State may enter into transactions without a clear public need and may thereby grant aid to a certain enterprise, see for example Case T-14/96 *Bretagne Angleterre Irlande (BAI) v. Commission* [1999] ECR II-139.

⁽¹⁴⁾ For instance benchmarking by means of independent reviews of tariffs and service performance, etc.

Additional levels of assessment

In addition to the issues concerning the service provider, the decision of the Commission concerning the Welsh Public Sector Network Scheme also verified the presence of State aid concerning the users of the network and third parties.

The users of the network were all part of the public administration and exercised public functions⁽¹⁵⁾. Therefore, these entities were not found to exercise an economic activity and hence did not qualify as undertakings under the State aid rules. However, note that, had the State been purchasing network services for economic undertakings, State aid could have been present at their level.

Similarly, in the Welsh case, the network was not considered to provide an advantage to third party operators given that the need for significant new infrastructure was unlikely and wholesale access was not envisaged beyond potentially existing regulatory requirements⁽¹⁶⁾. Had there been a possibility for wholesale access for commercial use by third parties on preferential terms, depending on the conditions, State aid could have been found to be present.

On the basis of the above, the Commission concluded that the procurement of the Welsh Public Sector Network Scheme does not constitute State aid within the meaning of Article 87 (1) of the EC Treaty.

4. Conclusion

Public procurement in the EU is subject to the principles of the Treaty, and to the detailed provisions of the EU public procurement Directives coordinating the national procurement rules. However, this does not automatically exempt public procurements from the scope of the State aid rules.

To see whether a public procurement involves State aid to the winning economic operator, the most important issue is to consider whether the procurement may entail any advantage which the operator would not receive under normal market conditions. As confirmed by the Welsh Public Sector Network Scheme, in the case of pure procurement transactions, the use of a competitive procurement procedure which is in line with the EU public procurement rules and thus suitable to achieve best value for money, i.e. fair market price for the goods, services or infrastructure purchased, creates a presumption that no State aid will be involved to the economic operator concerned.

In certain cases, such as the provision of broadband networks, State aid might be provided to the end users of the network — in case there are economic undertakings among them — or to third parties which get access to the network provided out of public funds.

⁽¹⁵⁾ Such as the National Health Service Wales, local authorities, fire services, police, national parks authorities, the Welsh Assembly Government and the National Assembly for Wales, higher and further education and assembly sponsored public bodies, such as the Welsh language board.

⁽¹⁶⁾ There may be a regulatory obligation to provide wholesale access if the selected provider was deemed to have significant market power.