

Client Alert

13 February 2014

European Procurement and Government Contracts Digest:

Closing the Gap on Concession Contracts

European Union sets up harmonised framework for awarding of “concession contracts”

By Felix Helmstädter

In the European Union (EU), around 60% of Public-Private Partnerships (PPP) are entered into on a concession basis. This represents an EU-wide market worth more than €100 billion (\$135 billion) each year. For the first time, the EU has now issued legislation to harmonise and regulate procurement in the market for public concession contracts.

CONCESSION CONTRACTS IN PRACTICE

A concession is a grant of rights – perhaps of land or property or, often, a right to operate in a particular sector – by a government, local authority, corporation, individual or other legal entity. The concession may include the right to build and/or use some form of public infrastructure or the right to exploit certain natural resources.

Under a concession contract, the concessionaire (typically a private company) builds and/or operates some form of infrastructure project (e.g., a toll road, bridge or port) or provides services of public interest (e.g., energy, public and ambulance transport services, or broadband cable network services in private households).

CURRENT REGULATORY FRAMEWORK: MINIMUM STANDARDS DEVELOPED BY THE EUROPEAN COURT OF JUSTICE

Unlike public contracts and works concessions (which are already governed by Directives 2004/17/EC and 2004/18/EC), the awarding of service concessions is currently not regulated by specific EU legislation. In order to avoid the requirement to follow formal contract award procedures as required under those Directives, there has been a considerable incentive for public authorities to treat a contract as a concession rather than as a public contract and, in extreme cases, to award such contracts directly (and sometimes even clandestinely) to a certain company favored by the public entity. Lack of precise criteria to distinguish between the two concepts of contracts fostered this practice.

Accordingly, national courts have frequently referred cases to the European Court of Justice (ECJ) in litigation concerning the awarding of concession contracts. Starting with its judgment in the *Teleaustria* case in 2000 (C-324/98), the ECJ has developed minimum standards of transparency and equal treatment to be guaranteed by contracting authorities when awarding concession contracts. Only recently, the ECJ held in two further cases related to the provision of cable network services (C-221/12 – *Belgacom*) and an infrastructure project (C-388/12 – *Comune di Ancona*) that the direct awarding of concession contracts without prior advertising or use of competitive tendering would be in violation of the general principles of the Treaty on the Functioning of the European Union (TFEU).

Client Alert

NEW DIRECTIVE DESIGNED TO BRING EU-WIDE HARMONISATION AND FURTHER PROMOTION OF COMPETITION

As a result of the EU Commission's initiative to harmonise the legal framework and to promote competition for service concessions, on 15 January 2014, the EU adopted, as part of its major reform package on public procurement laws a separate "Directive of the European Parliament and of the Council on the award of concession contracts" ("Concession Contracts Directive" or CCD). The CCD contains a comprehensive set of rules to be followed in concession contract award procedures and essentially codifies the prior ECJ rulings.

The new CCD regime is part of a package of three new directives, two of which replace the existing rules outside the concession sector. The directives are:

- a replacement of Directive 2004/18 on the procedures for the award of public supply, public service and public works contracts – the **Public Procurement Directive**;
- a replacement of Directive 2004/17 dealing with procurement by entities operating in the water, energy, transport and postal services sectors – the **Utilities Directive**; and
- a directive on the award of concession contracts – the **Concession Contracts Directive**.

We have published a separate [article](#) in the *European Procurement and Government Contracts Digest* about the main changes made by the Public Procurement Directive and the Utilities Directive. What follows is a summary of the key reforms made in the Concession Contracts Directive.

TIMELINE FOR IMPLEMENTATION

Following the publication of the CCD in the EU's *Official Journal* (expected in March 2014), the EU member states will have a period of 24 months to transpose the CCD into their national laws. Despite the time allotted for implementation, several member states seem likely to amend their national laws well in advance of this deadline.

MAJOR ELEMENTS OF THE CCD

- **Definition:** The CCD applies to both so-called service concession contracts and works concessions (the latter are currently governed by Directive 2004/18/EC). "Concessions" are defined by the CCD as contracts under which the contracting authority grants a right to exploit certain works or services to an economic operator, while the contracting authority obtains the benefits of the works or services. Moreover, the CCD codifies a key characteristic of concession contracts which is that the operational risk in exploiting works or services is transferred to the concessionaire. According to the CCD, the concessionaire is said to bear this risk if "*under normal operating conditions, it is not guaranteed to recoup the investments made or the costs incurred in operating the works or the services which are the subject matter of the concession*".
- **Thresholds:** The CCD applies to contracts worth €5,186,000 (approx. \$7 million) or more, based on an estimate of the concessionaire's total turnover during the term of the contract. It is a feature of this type of contract that contract durations are often quite long in view of the requirement for up-front investment; although one aim of the CCD is, in future, to avoid unnecessarily long durations.
- **Procedure:** The CCD obliges public authorities to guarantee transparency (e.g., by way of publication of requirements) and non-discrimination (e.g., through binding application of pre-defined awarding criteria), but

Client Alert

does not prescribe any specific formal procedure. The flexibility to design an individual awarding procedure is one major difference compared to the award of other types of public contracts.

- **Selection of bidders and awarding criteria:** The CCD obliges the contracting authorities carefully to assess the bidders' compliance with the conditions for participation in the tender proceedings which may relate to specific qualitative requirements justified by the subject of the concession contract. Moreover, the contract award decision has to be based on the assessment of the bids with regard to objective and pre-defined criteria that collectively offer an overall economic advantage for the contracting authority.
- **Simplified regime for specific services:** With regard to specific services listed in Annex IV of the CCD, such as health, social and related services as well as postal services, a light-touch regime applies. Under this regime, the contracting authority is only required to publish (1) a prior information notice about the authority's intention to award a concession, and (2) a concession award notice after the contract has been concluded. Contracting authorities therefore have wider discretion to conclude concession contracts related to those types of services.
- **Legal protection:** In addition, concession contracts will now fall into the scope of the EU Remedies Directives, ensuring that bidders have access to a system of effective legal protection, in particular against violation of the basic principles of transparency and equal treatment.

OTHER ELEMENTS AND EXCLUSIONS OF SPECIFIC CONCESSION CONTRACTS

As is the case for the amended Public Procurement Directive and the Utilities Directive, the CCD contains, amongst others, detailed rules related to sub-contracting and to modifications of contracts.

The scope of the CCD is limited due to a broad set of exclusions which particularly concern sectors that are subject to specific regimes (e.g., public transport and defence). In addition, the CCD is not applicable in case of so-called in-house contracts (i.e., in simple terms, contracts for services or works provided by an entity which is controlled by the contracting authority) as well as in certain scenarios of cooperation among several contracting authorities.

PRACTICAL CONSEQUENCES

In the light of the new regime on concessions, contracting authorities and private companies should align their activities with the new provisions at an early stage. Several countries are set to amend their national laws promptly and others (e.g., Austria, France and Spain) already had adopted specific rules on concessions before and independently of the present EU reform.

Public authorities in countries currently lacking any specific rules on service concessions (e.g., Germany, the UK) will have to amend their practice of awarding concessions in order to ensure compliance with the new rules.

For potential bidders, the new regime allows easier comprehensive monitoring of upcoming major concession contracts for companies interested in business opportunities across the EU. In addition, companies may rely on more precise procedural guarantees and can seek legal protection in case of non-compliance with the open tendering rules under the new regime.

Client Alert

Taken as a whole, the new regulatory framework ought to prevent public authorities from awarding concession contracts directly to preferred bidders without carrying out a transparent contract award procedure – a practice which impeded competition within the EU-wide internal market. However, there remains a substantive difference between formal proceedings under the EU Directives on public contracts and the rather vague requirements defined by the new CCD. Therefore, the distinction between a public contract and a concession contract remains important in each individual case and it is likely that the question of whether the major part of operational risk has been transferred to the economic operator (in which case, the concessions regime applies) or remains with the contracting authority (in which case, the public contracts regime applies) will still keep the courts busy.

Contact:

Felix Helmstädter

49 (0)30 72622-1353

fhelmstaedter@mofo.com

Alistair Maughan

44 (20) 79204066

amaughan@mofo.com

About Morrison & Foerster:

We are Morrison & Foerster—a global firm of exceptional credentials. Our clients include some of the largest financial institutions, investment banks, Fortune 100, technology and life science companies. We've been included on *The American Lawyer's* A-List for 10 straight years, and *Fortune* named us one of the "100 Best Companies to Work For." Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. This is MoFo. Visit us at www.mofo.com.

Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations. Prior results do not guarantee a similar outcome.