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Public Procurement

Procurement by Utilities

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Utilities Procurement in context

The term “utilities” is commonly used to describe the organisations that deliver services – such as the provision of water, electricity, gas or transport – to a community as a whole, typically through fixed networks. In many Member States, activities in the utilities sector are entrusted to government organisations that are public entities. In some Member States, however, bodies operating in the utilities sector are wholly private undertakings that would not fall within the definition of a contracting authority for the purposes of the Public Sector Directive¹ (the Directive). In other Member States, there may be a mixed economy, meaning both private and public entities operate in the same utilities markets.

This mixed picture presented a problem when the authorities of the European Union (EU) were considering the regulation of procurement activity in the utilities market. In Member States where contracting authorities operated in the utilities sector, there was no reason, in principle, why they should not also be covered by the public procurement system set up by the Directives. However, this system did not “capture” private companies, and there was some reluctance to cover these companies in the first place. The EU authorities could not simply impose the rules on the “public” utilities because this would create an uneven playing field, which would distort competition, and Member States were not ready to take such half-measures.

Another reason for regulating entities operating in these sectors was the closed nature of the market in some Member States, where the existence or the granting of special or exclusive rights by the state would create a monopoly situation that would limit competition. Competition is also limited by the fact that fixed networks are expensive to build but relatively inexpensive to maintain and operate. These networks may also require rights of way, which typically are expensive or administratively complex to obtain. This situation creates a long-term, monopolistic advantage for the operator who first puts such a network into place. In this situation the public interest (the interest of all users of the service, in particular in relation to value for money) has to be protected by imposing special rules on how utilities operators (public or private) organise their purchases, in addition to other regulations that may govern their investments and operations.

By 1990, the EU regulator had come up with a means of applying the procurement rules to the utilities sector. It did so in a separate Utilities Directive (Directive 90/531/EEC), in which it was made clear that it was not only the “public” entities that were bound to follow EU rules with regard to their procurement of goods, works and services, but also the private undertakings operating on the basis of special or exclusive rights. This approach has been continued and confirmed in the 2014 Utilities Directive².

The paramount consideration in both public and private sectors is the extent to which contracting entities are subject to state influence and whether this influence is exercised through direct control or indirect influence (e.g. the state's power to control the granting and operation of special or exclusive rights to private undertakings). It is worth noting in this context that the telecommunications sector used to be regulated, but full liberalisation of the market in the late 1990s and 2000s led to a decision to remove this sector from regulation under the 2004 Utilities Directive³. In addition, under the same 2004 Utilities Directive, exploring for oil or gas was a relevant activity. However, it is excluded from the 2014 Utilities Directive because that sector has consistently been found to be subject to such competitive pressure and therefore the procurement discipline brought about by the EU procurement rules is no longer needed.

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

² 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.

³ Directive 2004/17/EC on co-ordinating the procurement procedures of entities operating in the water, energy, transport and postal service sectors, 31 March 2004.

The rules on utilities are adopted in a separate directive because the provisions are more flexible than in the Directive. It has been recognised that the entities in the utilities sectors are operating in a more commercial market, which means that although the main principles of the public procurement rules need to be respected, it is also necessary to provide some flexibility in order to take account of the reality of the environment in which they operate.

The Utilities Directive therefore places generally less stringent requirements on procuring entities than the Directive. Examples include: higher financial thresholds, a wider range of options in terms of when and how to advertise contract opportunities, less control over the conduct of the selection and evaluation phases, and the use of more flexible purchasing tools than are provided for in the Directive. These requirements reflect the more commercial nature of the business and operation of utilities in many Member States. General principles derived from the Treaty⁴ apply, including equal treatment and transparency. It has to be noted that, although the Utilities Directive has more flexible rules than the Directive, fewer differences remain between the two sets of rules as compared to the 2004 Directives.

When does the Utilities Directive apply?

It is important to note that the Utilities Directive applies to contracts in relation to specific activities in four utility sectors only: water, energy, transport, and postal services.

The Utilities Directive only applies (1) when a procuring entity falls within the definition of a utility as set out in the Utilities Directive, and (2) then only to the extent that the utility carries out a relevant activity defined in the Utilities Directive and in relation to contracts of a defined type. When these requirements are met, the Utilities Directive applies to specified types of contract where the value of the contract exceeds the relevant EU financial threshold.

Which entities are subject to the application of the Utilities Directive?

Whether or not an entity falls within the definition of a utility to which the Utilities Directive applies is not linked to whether an entity is private or public in nature. It is linked to two factors: whether the entity operates in a specified field of activity (a “relevant activity”) and on which basis the entity carries out that activity.

There are three types of defined entity:

- **Contracting “authorities”:** The definition of a contracting authority is the same as in the Directive. There are two main types of contracting authority: “public authorities” and “bodies governed by public law”. The case law on this issue has resulted in a flexible definition. For further information, see SIGMA Public Procurement Brief 3, *Contracting Authorities*.
- **Public undertakings:** A public undertaking is defined in the Utilities Directive as “any undertaking over which the contracting authorities may exercise directly or indirectly a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it”.
- **Entities operating on the basis of special or exclusive rights:** The Utilities Directive also applies to entities that fall within a three-part definition. These are entities that:
 - are not contracting authorities or public undertakings;
 - have as one of their activities any of the relevant activities outlined below;

⁴ Treaty on the Functioning of the European Union - consolidated version of the Treaty on the Functioning of the European Union OJ C 326, 26.10.2012. Referred to in the Procurement Brief as “TFEU” or “Treaty”.

- operate on the basis of “special or exclusive rights” granted by a competent authority of a Member State.

For this purpose, “special or exclusive rights” means rights granted by a competent authority of a Member State by way of any legislative, regulatory or administrative provision the effect of which is to limit the exercise of relevant activities to one or more entities, and which substantially affects the ability of other entities to carry out such activity. However, rights that have been granted by means of a procedure in which adequate publicity has been ensured and where the granting of those rights was based on objective criteria do not constitute special or exclusive rights. Such procedures include:

- procurement procedures with a prior call for competition, in conformity with Directive 2014/24/EU, Directive 2009/81/EC, Directive 2014/23/EU or Directive 2014/25/EU;
- procedures pursuant to other legal acts of the Union ensuring adequate prior transparency for granting authorisations on the basis of objective criteria. Those procedures are listed, together with related activities, in Annex II of the Utilities Directive. Examples include granting authorisation to operate natural gas installations and authorisation or an invitation to tender for the construction of new electricity production installations.

What are the “relevant activities”?

Contracting entities falling within the above definitions are covered by the Utilities Directive, but only to the extent that they carry out a “relevant activity” and only in relation to contracts awarded for the purpose of carrying out that activity.

In summary, the relevant activities are:

- **Water:** Activities concerned with the “supply of drinking water” cover “the provision or operation of fixed networks intended to provide a service to the public in connection with the production, transport and distribution of drinking water” or the supply of drinking water to such networks. A “fixed network” can be distinguished from other supply methods, such as the sale of bottled water, which are not covered by the Utilities Directive.

Contracts connected with hydraulic engineering, irrigation and land drainage and the disposal or treatment of sewage may also be covered where they are awarded by an entity engaged in the supply of drinking water.

- **Energy – gas, heat and electricity:** Relevant activities are the provision or operation of a fixed network intended to provide a service to the public in connection with the production, transport or distribution of electricity, gas or heat. Also covered is the supply (generation/production, wholesale and retail sale) of electricity, gas and heat to such networks. Other activities include the exploitation of a geographical area for the purposes of exploring for, and extracting, coal or other solid fuels and of extracting oil and gas.
- **Transport services:** Relevant activities are some, but not all, transport services. Included is the exploitation of a geographical area for the provision of airports and maritime or inland ports or other terminal facilities to carriers by air, sea or inland waterway. Also covered is the operation of specific types of transport networks providing services to the public – railway, automated systems, tramway, trolley bus, bus and cable networks.
- **Postal services:** Relevant activities are the clearance, sorting, routing and delivery of postal items as well as other defined services, such as mailroom management services and direct mail bearing no address.

The Utilities Directive provides a mechanism for distinguishing between various situations where a contract is a “mixed” contract: for example, where the contract encompasses several relevant activities or activities covered by both the Utilities Directive and the Directive.

It is worth noting that when an entity that is a utility carries out activities that are not “relevant activities”, contracts awarded by the utility in that context are not subject to the Utilities Directive. For example, when an entity operating an airport wishes to award a contract for the construction and operation of a hotel that is not located on the airport site, the contract will not be subject to the Utilities Directive. The reason for this is that the “relevant activity”, namely the provision of the airport, is limited geographically. Similarly, the provision of a transport network that is not intended to serve the public – such as the operation of a freight railway line wholly within a large commercial factory site – will not be subject to the Utilities Directive, as it is a purely commercial service that is not provided for the benefit of the public. Extreme care does need to be taken in establishing whether in particular circumstances a specific contract is or is not covered by the Utilities Directive.

What types of contracts are covered?

The Utilities Directive covers three main types of contracts, for:

- works
- supplies
- services: all services are fully regulated unless they are “light regime services” or fall within one of the exclusions.

See SIGMA Public Procurement Brief 4, *Contracts Covered by the Public Procurement Directives*, for more information on the definition of works, supplies and services contracts and light regime services.

What are the EU financial thresholds for contracts subject to the Utilities Directive?

The relevant EU financial thresholds are higher under the Utilities Directive than the thresholds applying to contracts covered by the Directive. The financial thresholds are fixed for a period of two years. The thresholds for the period 1 January 2016 to 31 December 2017 are EUR 5 225 000 for works contracts, EUR 418 000 for supplies and services contracts and EUR 1 000 000 for social and other specific services. For up-to-date threshold values, consult the Europa website⁵.

Detailed provisions cover the way in which the value of contracts is calculated for specific types of contracts and specific situations. The main aims of the provisions relating to the calculation of the value of the contracts are to ensure that there is a genuine and transparent pre-estimate of the value of the contract to be awarded and that the contracting entity does not attempt to avoid the application of the Utilities Directive, for example by splitting a requirement or a contract into smaller sub-threshold packages or contracts.

See also SIGMA Public Procurement Brief 5, *Understanding the EU Financial Thresholds* .

Procurement procedures

The Utilities Directive provides for five main procurement procedures:

- open procedure
- restricted procedure
- negotiated procedure with a prior call for competition

⁵ http://ec.europa.eu/growth/single-market/public-procurement/rules-implementation/index_en.htm#t1

- competitive dialogue
- innovation partnership.

Contracting entities are free to use either the open, restricted or negotiated procedure with prior call for competition. These options were the same under the 2004 Utilities Directive. Member States must also ensure that contracting entities have the freedom to use the competitive dialogue or innovation partnership procedures. No conditions apply to the use of these competitive procedures where negotiation is permitted. Contracting entities therefore have the freedom to choose any of the five procedures.

Contracting entities also have flexibility in terms of how they advertise – the process is referred to in the Utilities Directive as a “call for competition”.

When conducting an open procedure, contracting entities have no choice and must use a Contract Notice.

When conducting a restricted procedure or a negotiated procedure with a prior call for competition, contracting entities can choose to use one of the following:

- a contract-specific notice
- an annual “periodic indicative notice”
- a notice on the existence of a qualification system.

When conducting a competitive dialogue procedure or an innovation partnership, contracting entities have two choices:

- a contract-specific notice
- a notice on the existence of a qualification system.

Statutory time limits apply, and a standard format Contract Notice must be used and published in the *Official Journal of the European Union (OJEU)*.

Conduct of the procurement process: The provisions in the Utilities Directive covering the conduct of the procurement process are generally less detailed and less prescriptive than the rules applying to the public sector. For example, there is no exhaustive list of criteria for qualitative selection, apart from contracting entities that are also contracting authorities. There are also provisions allowing for the time limit for receipt of tenders to be set by mutual agreement. Contracting entities are nevertheless obliged to observe general principles to ensure equal treatment and transparency and to not distort competition.

Purchasing tools

Contracting entities have a number of purchasing tools that they can use:

Qualification systems: A qualification system is unique to the Utilities Directive. It is a system, advertised in the *OJEU*, under which economic operators interested in contracting with the contracting entities apply to be registered as potential providers for specific works, supplies or services. Using predefined and published qualification criteria, the contracting entity registers some or all of these economic operators in the system. The registered economic operators form a pool for specified works, supplies or services, from which the contracting entity may draw those that are to be invited to bid or negotiate on contracts.

Framework agreements: A framework agreement is an arrangement advertised in the *OJEU* under which one or more economic operators are appointed as framework members following the submission and evaluation of selection stage information and tenders. The framework agreement

establishes the terms governing the award of contracts, in particular relating to price and, where relevant, quantity. Once the framework agreement is established, there is no further obligation to advertise in the *OJEU* when individual contracts are awarded under the terms of the framework agreement.

The process under the Utilities Directive is much more lightly regulated than under the Directive. No detailed provisions cover how framework agreements are to be set up or operate. The term of a framework agreement for utilities may generally not exceed eight years and may be shorter. The Utilities Directive provides that the duration may exceed eight years only “in exceptional cases duly justified, in particular by the subject of the framework agreement.” For further information on framework agreements in the public sector, see SIGMA Public Procurement Brief 19, *Framework Agreements*.

Dynamic purchasing systems: A dynamic purchasing system is a completely electronic process for making commonly used purchases. The maximum duration of the system is not defined. The restricted procedure is used to appoint economic operators, which are free to apply to join the system at any time by submitting requests to participate. When a contracting entity wishes to award a contract by using the dynamic purchasing system, it invites all admitted participants or participants having been admitted to the specific category of works, products or services to submit a tender for each specific procurement. See also SIGMA Public Procurement Brief 11, *Procurement Tools*, and SIGMA Public Procurement Brief 17, *e-Procurement*.

Electronic auctions: An electronic auction is an electronic process that allows for the submission of new prices (revised downwards) and/or the submission of new elements of tenders after an initial full evaluation of tenders has been undertaken. Electronic auctions occur at the final stage of a tender process that has been conducted up to that point in accordance with one of the standard procurement procedures provided for in the Utilities Directive. See also SIGMA Public Procurement Brief 11, *Procurement Tools*, and SIGMA Public Procurement Brief 17, *e-Procurement*.

Design contests: Special provisions govern the conduct of design contests. The rules of conduct are similar to those that apply to the public sector.

Exemptions specific to the utilities sector

The Utilities Directive provides for sector-specific exemptions in a number of utility sectors based on practical considerations relating to supply or to the degree of competition in these markets. Such exemptions apply in respect of the purchase of fuel and energy for the production of energy and of the purchase of water for the provision of water services.

The Utilities Directive contains a number of exemptions applying across the utilities sector:

- **Activities outside the EU:** The Utilities Directive does not apply to contracts that contracting entities award for purposes other than the pursuit of their relevant activities or “for the pursuit of such activities in a third country, in conditions not involving the physical use of a network or geographical area within the European Union”.
- **Affiliated undertakings:** Where “undertakings” consist of a number of mutually owned or mutually dependant companies, the Utilities Directive provides a specific exemption for purchases made between them under certain conditions. They are treated like “in-house” contracts, referred to as “intra-group transactions”.
- **Joint ventures:** The Utilities Directive does not apply to 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, or by a contracting entity to such a joint venture of which it forms a part.

- **Purchases for re-sale or lease:** The Utilities Directive excludes from its scope of application contracts awarded for purposes of re-sale or lease to third parties. This exclusion is intended to cover, for example, contracts for goods where the contracting entity intends to sell or hire the equipment purchased in a competitive market. These contracts will only be excluded if the contracting entity enjoys no special or exclusive right to sell or hire the subject of such contracts. Other entities are free to sell or hire it under the same conditions as the contracting entity.
- **Contracts between contracting authorities:** Contracts awarded by a contracting authority to a legal person governed by private or public law fall outside the scope of the Utilities Directive where specific conditions on control, percentage of activities, and private capital participation are fulfilled (identical to the “in-house” exemption under the Directive. See SIGMA Public Procurement Brief 39, *In-house procurement*).

What is the Article 34 exemption?

Under Article 34, the European Commission may in certain cases grant an exemption from the provisions of the Utilities Directive to contracting entities. This exemption applies where, in the Member State in which it is performed, the relevant activity is directly exposed to competition and on a market to which access is not restricted.

The test of whether markets are competitive necessarily takes account of both the legal and factual situations in the Member State concerned. It is considered on a case-by-case basis. Common exemptions granted in relation to activities in individual Member States include the production and supply of electricity, oil and gas exploration, and the provision of express and courier services.

The exemption is granted by means of a Decision by the European Commission, which is prompted by the application of a Member State or a contracting entity. The procedure for establishing whether Article 34 is applicable is supplemented by an implementing act adopted by the European Commission, which covers, among other issues, publication requirements, extensions, and details of requests.

A list of the exemptions granted can be found on the Europa website⁶.

Remedies

Remedies are legal actions available to economic operators participating in contract award procedures. These remedies allow them to request the enforcement of the public procurement rules and provide them with rights under those rules in cases where a contracting entity, intentionally or unintentionally, fails to comply with the law.

Directive 92/13/EEC⁷, amended by Directive 2007/66/EC⁸ (Remedies Directive), regulates remedies relating to utilities contract award procedures.

The aim of the Remedies Directive is to allow irregularities occurring in contract award procedures and in the contract award decision to be challenged and corrected as soon as they occur. Application of the Remedies Directive should result in an increased lawfulness and transparency of such

⁶ http://ec.europa.eu/growth/single-market/public-procurement/rules-implementation/exempt-markets/index_en.htm

⁷ Directive 92/13/EEC co-ordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors, 25 February 1992.

⁸ Directive 2007/66/EC amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts, 11 December 2007.

procedures, build confidence among businesses, and facilitate the opening of local public contract markets to foreign competition.

Although basic principles and requirements apply across all Member States, they have different legal and judicial regimes, and as a result the detailed implementation of the Remedies Directive varies to reflect the particular circumstances. However, all national remedies must be:

- clear and straightforward, i.e. understandable and easy to use for economic operators;
- available to all economic operators wishing to participate in a specific contract award procedure without discrimination, especially not on grounds of nationality;
- effective in preventing or correcting instances of unlawfulness on the part of other economic operators and/or contracting authorities.

The Remedies Directive requires that Member States, in specific circumstances, provide for a standstill period at the contract award stage, when economic operators participating in the procurement process are notified of a contract award decision. This requirement aims to ensure the right to challenge an award procedure before the implementation of the procurement contract. Other provisions include an obligation to notify direct awards and the availability in certain cases of a sanction for the ineffectiveness of a concluded contract.

Further information

Publications

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

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SIGMA (2016), *Understanding the EU Financial Thresholds*, Brief 5, OECD Publishing, Paris

SIGMA (2016), *Procurement Tools*, Brief 11, OECD Publishing, Paris

SIGMA (2016), *e-Procurement*, Brief 17, OECD Publishing, Paris

SIGMA (2016), *Framework Agreements*, Brief 19, OECD Publishing, Paris

SIGMA (2016), *In-house Procurement*, Brief 39, OECD Publishing, Paris

Other Sources

The Commission's website on procurement covers both the public sector and utilities.

http://ec.europa.eu/internal_market/publicprocurement/index_en.htm