

# WHEN IS PUBLIC PROCUREMENT SUBJECT TO COMPETITION LAW?



By Simon Taylor

## Contracting and procurement

The recent Keating article authored by Sean Wilken KC, *Government by Contract*, raises the interesting issue of whether contractual schemes such as the Self Remediation Terms imposed on developers by the Department for Levelling Up, Housing and Communities are subject to competition law scrutiny under the Competition Act 1998 (CA 98).

This article relates to an area of Government contracting which already attracts a considerable degree of scrutiny in the courts – public procurement. Contracting authorities and utilities subject to the Public Contracts Regulations 2015 (PCR 2015) and the Utilities Contracts Regulations 2016 (UCR 2016) are regularly sued for a failure to follow rules designed to ensure that procurement procedures comply with the principles of transparency, equal treatment and proportionality.

Typically, these cases relate to the way in which the process was conducted in challenges brought by unsuccessful tenderers. But occasionally, they also relate to the design of the tender rules and that may include often non-negotiable contractual terms.

For example, in *Abbvie Ltd v The NHS Commissioning Board* [2019] EWHC 61 (TCC) a challenge was brought both to the award criteria and to a contractual mechanism (Unmetered Access Model) by which a fixed fee would be payable to successful tenderers even though they may have to supply surplus treatments. The jurisdictional argument that the fixed fee was contractual and therefore not subject to the PCR 2015 was rejected at [151] on the basis that the relevant provisions in regulation 18 (the equal treatment principle) apply to the design of the procurement – of which the proposed conditions of contract are plainly a part.<sup>1</sup>

<sup>1</sup> The definition of "procurement document" in regulation 3(1) expressly includes "proposed conditions of contract".

Given that terms are imposed on tenderers and Government/utilities often have a very high share of the buying market for the goods or services being procured, the question arises whether and to what extent competition law constrains or should constrain those contractual terms. Terms could include liquidated damages clauses, long term exclusivity and market sharing arrangements – all of which are potentially caught by competition law prohibitions.

This article considers briefly first, the outline differences between the regimes, second, why competition law has traditionally not been applied to public procurement and third, whether that is changing or could change in the post Brexit environment.

## Differences between procurement and competition law

These regimes tackle different problems. Procurement law is a means of addressing the risk of corruption by public officials, the tendency of public bodies to prefer local or national suppliers and agreements reached in international treaties to secure reciprocal access for suppliers to public markets. The rules were based on the Treaty on the Functioning of the European Union (TFEU). Now, post Brexit, the UK is bound in its own right to the WTO General Procurement Agreement (GPA), has procurement commitments to the EU via the EU-UK Trade and Cooperation Agreement (TCA) and is also in the process of adopting new procurement legislation.

By contrast, competition law, though also mirrored in EU law and subject to ongoing international commitments under the TCA and WTO rules, is a means of ensuring that markets operate efficiently, fairly and for the benefit of consumers.

The scope for challenging contractual terms under competition law is broader than under procurement law and the remedies are more extensive.

Possible bases for challenging conditions of contract under the current procurement rules include the equal treatment principle and the regulation 18 requirement that the design of the procurement shall not be made with the intention of artificially narrowing competition. Technical specifications may also be challenged if imposed without allowing tenderers to use equivalent standards.<sup>2</sup> In general, the requirement for an advertised tender should ensure that there is some competition for the market, even if the contractual terms are dictated by the public buyer.

Competition law goes further as it prohibits (with certain exemptions and safe harbours) agreements which have the object or effect of preventing, restricting or distorting competition<sup>3</sup> (eg. by fixing prices in or sharing markets) and conduct by a dominant undertaking which amounts to an abuse<sup>4</sup> (eg. by imposing unfair prices or otherwise limiting production, markets or technical development to the prejudice of consumers without objective justification). Competition law applies to buyer as well as supplier markets and joint purchasing may cause competition concerns through 'oligopsony power' (ie. where the buyers jointly make up a significant share of demand).

Remedies in procurement cases can extend to setting aside decisions or ordering the authority to amend a document (before the contract is entered into), damages and a declaration of contractual (prospective) ineffectiveness in narrow circumstances (such as an unlawful direct award without publicity).

But competition law remedies are more coercive with the prospect of a contract being declared null and void, damages and even a fine of up to 10% of turnover in serious cases. The limitation period for procurement challenges is also shorter (30 days) than for competition cases (6 years).

A hybrid area is subsidy control, formerly known as state aid. Under EU law, this was a means of ensuring that member states did not distort competition by unfairly

subsidising national providers, though there were myriad exceptions which allowed for a controlled industrial policy and aid to underdeveloped regions. Post Brexit, there continue to be reciprocal requirements under the TCA<sup>5</sup> and the Subsidy Control Act 2022 has been adopted in the UK giving the right to challenge non-compliant public subsidies to the Competition Appeal Tribunal (CAT).

EU state aid law has been invoked as a further weapon in procurement challenges on the basis that the failure to conduct a transparent and fair procurement procedure can amount to the grant of unlawful state aid.<sup>6</sup> There may continue to be a role under the Subsidy Control Act 2022 in considering the competition implications of public procurement.

These regulatory tools are not necessarily mutually exclusive. However, challenges to public procurements or procured contractual terms based on the CA 98 have been few and far between in the UK.<sup>7</sup>

There is a policy question as to whether a clearer and more extensive application of competition law principles to public procurement and Government contracting would be beneficial from an economic, political and social perspective in the UK. This article does not attempt to tackle that policy issue but takes stock as to where the law now stands and how it could evolve.<sup>8</sup>

## Undertakings in competition law

The competition law prohibitions in section 2 and 18 of the CA 98 apply only to 'undertakings'.

Neither the EU Treaties nor the CA 98 define an undertaking. The definition has evolved through rulings of the Court of Justice of the EU. The Competition and Markets Authority (CMA) and UK courts have been required by section 60 of the CA 98 to ensure so far as possible that questions arising under the competition prohibitions in the UK are dealt with in a manner which is consistent with the treatment of corresponding questions arising under EU law.

<sup>2</sup> Regulation 42, PCR 2015.

<sup>3</sup> Section 2, CA 98.

<sup>4</sup> Section 18, CA 98.

<sup>5</sup> Articles 362 – 375.

<sup>6</sup> See most recently *R (Good Law Project Limited) v The Secretary of State for Health and Social Care* [2022] EWHC 2468 (TCC) at [407] – [497].

<sup>7</sup> See *Arriva the Shires Ltd v London Luton Airport* [2014] EWHC 64 (Ch). While this case related to a tender for a bus route concession, the case was brought under the CA 98. The Defendant was held to be an undertaking within the meaning of the CA 98.

<sup>8</sup> The reader is referred to a comprehensive and scholarly analysis of the legal and economic issues in "*Public Procurement and the EU Competition Rules, Second Edition*" by Albert Sanchez Graells, published by Bloomsbury, 2014.



An undertaking has been defined in the case-law as any natural person engaged in economic activity, regardless of its legal form or the way in which it is financed.<sup>9</sup> For public bodies, the “basic test is whether the entity in question is engaged in an activity which consists in offering goods or services on a given market and which could, at least in principle, be carried out by a private operator in order to make profit.”<sup>10</sup> They are not undertakings when they perform essential functions of the state, such as social or regulatory functions.

The concept of an undertaking is functional so a public body could be acting as an undertaking for some activities but not others. In *FENIN*<sup>11</sup> which concerned the purchase of goods and services by the body which ran the Spanish health service (a free service), it was held that the nature of the purchasing activity (ie. whether it was economic) must be determined according to whether or not the subsequent use of the purchased goods amounts to an economic activity. In that case, the subsequent use was not economic and the authority did not therefore act as an undertaking.

Applying these EU tests, procurement by utilities caught by the UCR 2016 is arguably also caught by the CA 98. In *Achilles Information Ltd v Network Rail Infrastructure Ltd* [2019] WL 038992580 and [2020] EWCA Civ 323, the CAT and Court of Appeal applied *FENIN* in finding that Network Rail’s rules (requiring suppliers accessing the network infrastructure to use a certain provider of assurance services) were subject to the CA 98 on the basis that they were an essential part of and dissociable from its operation of the rail infrastructure. It appears to have been accepted that Network Rail’s monopoly over the rail infrastructure was an economic activity and the argument that the activity in question was of a regulatory nature was rejected.

The procurement activity of certain public bodies caught by the PCR 2015 could also be subject to the CA 98 on the basis of *FENIN*. These might include universities, registered social providers and NHS Foundation Trusts, all of which engage in market-based activities.

In fact, post Brexit, the UK courts now have greater freedom to move away from the EU case-law constraints and expand the list of publicly funded bodies subject to competition law. In particular, section 60A of the CA 98 now provides that the CMA or courts (or other persons applying the CA

98) are not required to ensure consistency with EU law if the person:

*“thinks that it is appropriate to act otherwise in the light of one or more of the following –*

*(a) differences between the provisions of this Part under consideration and the corresponding provisions of EU law as those provisions of EU law had effect immediately before IP completion day;*

*(b) differences between markets in the United Kingdom and markets in the European Union;*

*(c) developments in forms of economic activity since the time when the principle or decision referred to in subsection (2)(b) was laid down or made;*

*(d) generally accepted principles of competition analysis or the generally accepted application of such principles;*

*(e) a principle laid down, or decision made, by the European Court on or after IP completion day;*

*(f) the particular circumstances under consideration.”*

The door is therefore open for the courts to adopt a UK formulation of the threshold test for the application of competition law to bodies engaging in public procurement.

## Changing procurement landscape

There is an equivalent opportunity following Brexit for the UK procurement regime to introduce new definitions of bodies subject to procurement regulation.

Currently, the definitions in clause 2 of the Procurement Bill allow room for interpretation and suggest an ongoing need for the overlapping application of the two regimes:

*“public authority” means a person that is— (a) wholly or mainly funded out of public funds, or (b) subject to public authority oversight, and does not operate on a commercial basis”*

<sup>9</sup> *Höfner and Elser* (C-41/90); [1991] E.C.R. I-1979 paragraph 21. See also *Bettercare Group Limited v The Director General of Fair Trading* [2002] CAT 7, in which it was held that an entity providing State funded residential care and nursing home services was acting as an undertaking and December 2011 Guidance of the Office of Fair Trading: Public bodies and competition law.

<sup>10</sup> *Ambulanz Glöckner v Landkreis Südwestpfalz* EU:C:2001:284, [2001] E.C.R. I-8089. Applied by the CAT in *Strident Publishing Limited v Creative Scotland* [2020] CAT 11. See also *UKRS Training Limited v NSAR Limited* [2017] CAT 14 at [57] to [67].

<sup>11</sup> C-205/03P *FENIN v Commission* EU: [2006] E.C.R. I-6295.

*“The following are examples of factors to be taken into account in determining whether a person operates on a commercial basis—*

*(a) whether the person operates on the basis that its losses would be borne, or its continued operation secured, by a public authority (whether directly or indirectly);*

*(b) whether the person contracts on terms more favourable than those that might reasonably have been available to it had it not been associated with a public authority;*

*(c) whether the person operates on a market that is subject to fair and effective competition.”*

Conversely, a ‘public undertaking’, which is subject to the procurement rules only to the extent that it carries out a specified utility activity (in areas such as water or rail networks), is defined as “a person that (a) is subject to public authority oversight, and (b) operates on a commercial basis”.

The draft definition of a public authority has similarities to that used under the PCR 2015 and interpreted by the UK (and EU) caselaw.<sup>12</sup> However, it is not the same as it moves away from a test based on the purpose for which the body is established towards a test based on its activity. It is unclear whether it is intended to apply to buyer as well as provider markets. It is also unclear whether it means that a person could be considered a public authority for some (purely social) purchases, but not others (commercial purchases).

The definition appears to envisage the unfortunate but possibly familiar scenario in which a state supported body operates on the market with an unfair advantage and thus distorts effective competition. That body would be subject to procurement regulation as a public authority. Clearly, the need for competition regulation of its activities is also all the greater given its advantages and it may be assumed that it would also be considered an undertaking, possibly a dominant one. If the state-controlled body operates on a competitive market without any unfair advantage it would be treated as a public undertaking; though it is difficult to see how such a body would ever be subject to the procurement rules given that competitive utility markets are excluded from regulation.<sup>13</sup>

Finally, it is noted that the Procurement Bill provides less scope for the sort of challenge brought in *Abbvie*. In particular, there is no direct equivalent in the Procurement Bill of the regulation 18 prohibition on intentionally designing the procurement to artificially narrow competition.

## A legislative solution

The Subsidy Control Act 2022 defines a “public authority” in Section 6 as “a person who exercises functions of a public nature”. It might have been simpler if the same definition of a public authority had been used in the Procurement Bill or an improved version which limited it to bodies which exercise exclusively functions of a public nature and do not offer goods or services on a market. CA 98 could then be amended to ensure that all bodies not within this definition are treated as undertakings. That might more clearly take certain categories of body outside the remit of procurement law (e.g. universities, registered social providers, NHS Foundation Trusts, possibly certain arms’ length Government bodies)<sup>14</sup> but these bodies would be subject to the full rigour of the CA 98. This might achieve a degree of mutual exclusivity, though utilities would continue to be subject to both regimes.

## The case law options

As explained above, the current and draft legislation do, not separate out the application of procurement and competition law.

Assuming no further relevant changes to the definitions in the Procurement Bill or other legislation, there appear to be two roads that the UK case law in this area could take, now that the courts are relatively unconstrained by EU rules in this area.

The first, ‘the hybrid road’, is that there will continue to be a limited overlap between procurement and competition law, in that competition law will only apply to public procurement needed for market based activity under a *FENIN* type analysis or similar. Utilities and state supported public bodies, such as Foundation Trusts, central purchasing bodies, some ‘arms’ length’ Government bodies, registered social providers and universities may continue to be subject to scrutiny under both regimes.

The second, ‘the radical road’, would be if the courts were to conclude that any major public procurement and contracting is in essence a commercial activity with a potential risk to fair and effective competition and that both procurement and competition law should apply, providing complementary relief. On this approach, Government departments designing and conducting procurements would also need to consider the competition law rules and this could restrict their ability to use procurement to make or shape markets or promote market entry. There will be limited tools under the Procurement Bill to vet this kind of market manipulation, particularly given that regulation 18 of the PCR 2015 is being dropped.

## Conclusion

The interface between competition and procurement law remains unresolved. The current definitions under the CA 98 and the Procurement Bill sit alongside each other uneasily and the rules may need to be determined by litigation rather than legislation. This leaves public bodies and utilities in an uncertain position. In the meantime, it may be prudent for public bodies, as well as utilities, to ensure that all tender documents and proposed contractual terms are vetted for competition law considerations before being issued to tenderers.

<sup>12</sup> In particular bodies “established for the specific purpose of meeting needs in the general interest, not having an industrial or commercial character”, as interpreted in cases such as *Korhonen Oy* (Case C-18/01) and, in the UK, *Alstom Transport v Eurostar International Limited* [2012] EWHC 28 (Ch).

<sup>13</sup> See regulation 34 of the UCR 2016, clause 2(1) and Schedule 4, Part 2 of the Procurement Bill.

<sup>14</sup> This would require modifications to the UK GPA coverage Annexes.