CER

The Voice of European Railways

# POSITION PAPER

## CER views on the revision of the 'utilities' Directive

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## INTRODUCTION

The European Commission launched a recast of the public procurement directives in December 2011 further to a stakeholder consultation organised earlier that year[1]. The recast concerns two texts, the directive on public procurement, also called the 'classic' directive and the one on procurement by entities operating in the water, energy, transport and postal services, called the 'utilities' directive.

The Community of European Railway and Infrastructure Companies (CER) welcomes the revision of the existing legal framework inasmuch as it aims at simplifying and clarifying the texts with a view to ultimately reduce unnecessary administrative and legal costs. CER wishes however to draw the attention of the European Parliament and the Council to a certain number of provisions which would have serious negative consequences on the rail sector if not appropriately amended.

In that context and as a general overall comment, CER wishes to express its surprise with regard to the mismatch between the proposed new texts and the overall objective of simplification pursued by the European Commission.

**No overregulation of utilities procurement law**

The European Commission's proposal for a revision of the utilities directive (hereinafter referred to as the "proposal") is intended to provide simplification and enhanced flexibility of the existing public procurement rules as well as substantial relief for contracting entities and bidding companies. CER however, fears that this objective is unlikely to be achieved. The proposed text provides surprisingly for **more regulation** and **over-detailed procedures**. The increasing 'legalistic approach' and red tape in procurement rules will inevitably increase the costs incurred in carrying out procurement procedures in accordance with the law. Such costs will largely offset or even exceed the competitive effects and cost savings resulting from the application of European procurement law.

Moreover, CER understands that the European Commission's proposed directives aims to further harmonise utilities procurement law with the "classic procurement directive" (e.g. with regard to framework agreements). In CER's views, however, the special characteristics of utilities procurement are not taken into account sufficiently in this proposal. In this regard, it should be kept in mind that:

Utilities operators generally carry out supply activities in line with entrepreneurial principles; in carrying out supply activities, utilities operators compete in many areas with private enterprises which are not subject to procurement law:

- The high percentage of the utilities procurement volume (more than 75%) exceeds the thresholds and is awarded according to the rules of Directive 2004/17/EC;
- As a result, companies in the utilities sector are bound by strict procurement rules which entail substantive additional costs. This does not contribute to putting them on a competitive level playing field with their competitors on the market.

With this position paper CER wishes to highlight the **major issues of concern** of the rail sector with regard to the proposed utilities directive.

This position paper was elaborated with the expertise of the *UIC Legal Group* – sub group on public procurement.

[1]See CER/UIC position paper within the context of the stakeholder consultation. It can be consulted on www.cer.be

## 1. EXEMPTION FOR ACTIVITIES DIRECTLY EXPOSED TO COMPETITION (ART 27, 28 & ANNEX III)

One of the basic principles underlying the existing public procurement rules, which is taken over in the proposed revised directives is that they apply to markets that

- are not fully open to competition and
- are still managed, somehow, under public supervision and orientations.

When a market is opened to competition, the principle is that normal commercial rules apply and it is then not necessary to regulate the conditions under which a company purchases works, services and goods on the market. CER fully agrees with this principle, which is further applied in the specific transport sector in Article 8. This article states clearly that the Directive applies only to those transport activities where conditions are fixed by the competent authority. The **rail freight** sector for example is opened to competition since 15 March 2007 (Directive 91/440 as amended by Directive 2001/12) and **not subject to any conditions** whatsoever imposed by any public authority. It is entirely managed under commercial conditions and access to this market is not restricted.

On the other hand, the **rail passenger** market is in a different situation as it has to date only been **partially opened to competition**. Directive 91/440 as amended by directive 2007/58 opens international passenger transport, including cabotage, to competition. Domestic passenger services are not yet opened to competition throughout the EU, even if they may be opened in some Member States on an own initiative basis. Directive 91/440 will be further amended in the short future to fully open the domestic market to competition.

Against this background, CER was disappointed to read that Annex III of the Commission's proposal was referring to Directive 91/440/EC (main rail liberalization Directive) only as far as it relates to freight activities. However, Directive 91/440/EC covers also passenger traffic which has been partially opened to competition to date. This situation should be fully reflected in the text of the proposed revising directive: Annex III should therefore make reference to Directive 91/440/EC. This would allow interested parties to obtain an individual exemption for the specific market, **where appropriate**. An **additional clarification** in **recital 24 of the proposal** would be needed.

Both these changes relating to the freight and passenger rail market will result in providing an accurate picture of the rail market in the EU, with all the legal and economic consequences attached to such situation. This is important for the rail sector as it is a sector currently under important mutations. From a political perspective, it is important that the EU institutions acknowledge these changes.

## 2. ABOLITION OF THE DISTINCTION BETWEEN "A" AND "B" SERVICES

The Directives currently in force divide services into so called "*Part A*" (or "*priority*") services and "*Part B*" (or "*residual*") services. Only Part A services are fully caught by the Regulations. Part B services are caught by a simplified regime, with only a few of the detailed rules of the Directives applying. The scope of application Part B services has been clarified by the European Commission in an interpretative Communication[2].

[2]Interpretative Communication on the Community law applicable to contract awards not or not fully subject to the provisions of the Public Procurement Directives, OJEC C 179 of 2006.

CER regrets to see that this useful distinction has disappeared from the current proposal. As a consequence, the "simplified" procedure has been simply eliminated. Removing this distinction means restrictions are significantly strengthened, as all service contracts will be subject to the new directive as a whole. Admittedly, another category of services is created in Article 12, that of social service contracts, for which a threshold of 1 million Euros is set. However, these contracts only represent a marginal proportion of the contracts awarded by Railway Operators and do not compensate for the removal of non-priority contracts. **This approach is particularly surprising for CER as the overall aim of the Commission is actually to simplify procurement rules!**

We disagree with this new approach. In our opinion, such abolition should be reversed. To the contrary, the position of other institutions[3] as well as that of stakeholders, were to keep the lighter procedure[4]. Moreover, the COM (2011) 895 final (Proposal of a New "*Utilities*" Directive, Recital 16) argues that «*The results of the Evaluation demonstrated that the exclusion of certain services from the full application of this directive should be reviewed. As a result, the full application of the Directive is extended to a number of services (such as hotel and legal services, which both showed a particularly high percentage of cross-border trade)*». We don't understand what the highlighted paragraph exactly refers to. (What does mean[5] *"cross-border hotel services"*? In addition, it must be taken into account that some of these services, like legal services, have an "*intuitu-personae" basis*[6] therefore legal services shall continue in the list of "B" services. (If the abolition were approved, then Art. 19 lit. b should include legal services -at time B-services-: there is almost no cross-border business in legal matters. International law firms that operate in different European countries with local lawyers should not count for cross border activities).

Taking all of this into account, we consider that the differentiation between A & B services in the Utilities Directive should be kept, and said *Interpretative Communication on the Community law applicable to contract awards not or not fully subject to the provisions of the Public Procurement Directives, (2006/C 179/02*[7]*)* ) should continue to apply.

[3]In the Opinion of the EESC on the Commission Green Paper It is stated that in the Directive, services are divided in two categories, A and B. A services must comply whilst B services have, generally, a lighter regime. The Green Paper asked whether, in view of the increasingly cross-border nature of many types of service, the division is any longer appropriate. The EESC was in favour of maintaining the difference between the two categories subject to legal certainty and the possible transfer of cross- border B services to the A list. It recommends a periodical review of the list of B services by the Commission to examine whether some could, with advantage, be moved to A services. See Opinion of the EESC on the "*Green Paper on the modernisation of EU public procurement policy — Towards a more efficient European Procurement Market*", OJEC of 29 October, 2011, C-318.

[4]Moreover, it should be stressed that the "*Utilities*" Directive has to be applied by entities but with a different scope than the "*Classical Directive*": not by Governments, Ministries, etc., but by undertakings (either state-owned or private ones) that operate in Utilities sector. Therefore the regulation is more flexible, as undertakings need more flexibility (then, for example, a Ministry) to reach agreements as soon as possible, in order to provide its services to the public. Therefore, Utilities Directive is different from the Classical Directive, and therefore a more flexible regime is needed, including the distinction between A and B services.

[5]It must be taken into account that the need of hotel services is always linked to a concrete place: the place where someone needs to stay during the night). In addition, it is our experience –as Railway Operators- that there is very little cross-border competition when purchasing A services, and even less when purchasing B services.

[6]It means that the contract is awarded not on the lowest price basis or on the "*most economically advantageous tender*" (MEAT), but mainly *on a personal basis*, because there is the element of personal trust -common in agreements and when appointing people- and this means that they nominated him because they trust him, because it is known that he is worth it and a good choice: professional prestige, that's it.

[7] Official Journal of the European Union on 1-August-2006, C-179.

## 3. NOTION OF 'ENTIRETY OF WORKS' (ART. 1 PARA 2 SUB-PARA 2)

The utilities directive provides in its proposed new Article 1 (Subject matter and scope), paragraph 2 *in fine* that it will apply to "*An entirety of works, supplies and/or services, even if purchased through different contracts, constitutes a single procurement within the meaning of this Directive, if the contracts are part of one single project*".

This notion of '***entirety of works***' or '***one single project***' are too general and vague and would result in being obliged to bundling up many contracts with a view to systematically reach the EU thresholds. While CER can understand the objective of avoiding artificially splitting up contract to avoid reaching the thresholds, it must be stressed that the opposite is also counterproductive from a commercial point of view. For example, building a high speed railroad track ("*single project*") can last several years and can require a multiplicity of different contracts spread throughout the entire period. The multiplication of contracts will correspond to the economic, industrial and legal construction underlying the project. Imposing to bundle them up all together could lead to mismanagement on the longer term.

## 4. THE CONCEPT OF A BODY GOVERNED BY PUBLIC LAW (ART. 2)

The concept of a body governed by public law has been defined in Article 2 of the Proposal in a more extensive manner when compared to the existing text. This addition is likely to modify the concept of a 'body governed by public law', by expanding its scope in such a way that State-owned railway operators could be classified as a 'body governed by public law'.

CER wishes to stress that it is essential that all definitions contained in the text are unambiguous. The new proposed definition would result in railway operators being imposed ever more restrictive regulations. It is our understanding that this is not the ultimate objective pursued. CER therefore proposes to revert to the current definition included in Directive 2004/17 which is clear enough and more efficient.

## 5. PRESUMPTION OF DOMINANT INFLUENCE & SPECIAL OR EXCLUSIVE RIGHTS (ART. 4(2))

The definition of a public company as foreseen in Article 4 could raise a number of issues of concern and in particular that of equal treatment between public and private companies which have been granted special or exclusive rights.

As regards the issue of equal treatment between public and private companies having been granted special or exclusive rights, we believe that the proposed text of article 4, paragraph 2 would be contrary to several principles laid in the TFEU such as the principles of non- discrimination, impartiality and neutrality vis-à-vis the system of property ownership.

As a matter of fact (according to article 4, paragraph 2 read in conjunction with article 4 paragraph 3) the proposal establishes that only private companies, which have been granted special or exclusive rights through a transparent open procedure, would not be subject to the application of the proposed new utilities directive when carrying out the related services. On the contrary, public undertakings entrusted with the same rights, even if entrusted with such rights through a transparent open procedure, do fall within the scope of that piece of legislation!

This is a clear discrimination between entities operating under similar conditions but with a different ownership. This would be contrary to the principle of equal treatment established by article 345 of TFEU as well as to recital 7 of the proposal.

Therefore, in order to assure that both private and public companies would be treated equally, the directive should establish that where exclusive or special rights have been awarded through a transparent public procedure, companies –irrespective of their private or public ownership - should be treated in the same way and comply with exact same legal provisions.

## 6. EXEMPTION FOR 'AFFILIATED UNDERTAKINGS' (ART. 22)

Article 22 deals with contracts awarded to an affiliated undertaking. In its paragraph 3, it provides for an exemption from the directive for affiliated undertakings. This exemption is of great importance for the rail sector in particular as it touches directly upon labour conditions within a group. CER wishes to stress on the one hand, the need to further safeguard the exemption and on the other, the importance of not making it more stringent.

In order to avoid procurement procedures on multiple market levels (which make no sense from an economic point of view), every utilities operator should be entitled to directly award contracts to its affiliated undertakings for the time being without additional prerequisites such as revenue thresholds.

Furthermore, to the extent that the exemption for affiliated undertakings is subject to the prerequisite that the contractor must demonstrate that at least 80% of the average turnover derives from the provision of services to undertakings with which it is affiliated, it should be stipulated that turnover in this case refers to turnover from the same or similar supplies, services and works as that addressed in the contract to be awarded . So, this provision would be aligned with the last sentence of Article 22 of the proposal according to which turnover from other affiliated undertakings are, in turn, only to be included in the calculation if they result from "*same or similar services, supplies or works*".

## 7. FRAMEWORK AGREEMENTS (ART. 45)

Framework agreements are firmly established as a cost-efficient procurement instrument, particularly in the utilities sectors[8]. According to Article 14 (4) of the existing procurement directive (directive 2004/17/EC), framework agreements may not be misused to hinder, limit or distort competition. As far as can be seen, such misuse has never been the subject of proceedings in the Court of Justice of the European Communities since the first Utilities Directive entered into force in 1993. This indicates that utilities operators use framework agreements as part of sound and fair procurement. This is why CER believes that there is no need to now institute a detailed regulatory framework for awarding framework agreements or for single call-offs under the terms of a framework agreement (Article 45 of the proposal).

Moreover, in the new proposed text, framework agreements may not exceed four years, save in exceptional cases duly justified, in particular, by the subject of the framework agreement. Limiting the duration to four years poses a problem as it withdraws the flexibility that had been left to contracting

[8]European Commission – Evaluation Report: Impact and Effectiveness of EU Public Procurement Legislation Part 1, Section 6.4.

entities in this regard. The applicable provisions in this field are aligned with those applicable to contracting authorities subject to Directive 2004/18/EC. This alignment with stricter applicable provisions thus leads to an even higher degree of rigidity which does not appear to be justified.

Indeed utilities procurement consists largely of plants, machinery and equipment to set up and maintain utilities networks (e.g. power plants, rail infrastructure, communication platforms, energy distribution facilities, vehicle fleets). These are characterised by a high degree of complexity, substantial development and planning expenses, high procurement volume, long periods of implementation (especially in cases of trans-network roll-outs) and long depreciation periods. Planning and investment certainty would no longer be ensured for such procurement projects if framework agreements were regularly terminated after four years and had to be re-tendered. Suppliers are also usually only willing to take on the economic risks inherent in the research and development of innovative products if there is the prospect of sufficient amortisation through individual orders over a longer period of time[9].

The exception provided is rather unclear, which may create a situation of **legal uncertainty**. **The terms of the current directive should therefore be preserved**, as it did not provide for a maximum duration – it stipulated that the use of framework agreements could not result in the prevention, restriction or distortion of competition.

The article is much more specific than the former Article 14. New restraints are created to be borne by the contracting entities. The conditions under which contracts based on a framework agreement can be concluded with or without reopening of competition are described in too much detail, which means **the flexibility that currently exists in this regard is lost**. Moreover these terms are confused, which creates a situation of **legal uncertainty**.

## 8. NOTION OF 'SUBSTANTIAL MODIFICATION' OF PROVISIONS OF A CONTRACT (ART. 82)

In the proposed text, a substantial modification of the provisions of a contract during its period of validity is considered to be a new awarding of a contract and requires a new procurement procedure (Article 82). This issue is governed by case law today as it requires the assessment of too many precise aspects. A case by case approach is therefore the most appropriate one. Against this background, CER does not agree with the approach proposed by the Commission which consists in addressing this issue in a very restrictive manner in the text: **a 'one size fits all' approach is not adapted to the rail sector**.

It is also worth noting that the terms used to define a substantial modification are not sufficiently precise. This is particularly the case in paragraph 2 which employs a tautological formulation: "*a modification is considered to be substantial when it substantially changes the contract from that concluded at the outset*".

According to Article 82 (4) of the proposal, modifications to the contract are permissible where the value of a modification can be expressed in monetary terms if "*its value does not exceed the thresholds set out in Article 12 and it is below 5% of the price of the initial contract*" provided that the modification does not alter the overall nature of the contract. Development is furthermore limited to 5% in financial terms,

[9]For the same reasons, Directive 2009/81/EC for the award of contracts in the fields of defence and security includes a standard term longer than 4 years for framework agreements in its Article 29 (2).

which is far too low. In addition, setting a percentage is reductive and reduces the flexibility of an overall and case-by-case assessment of the extent of modifications made to a contract. In light of the fact that supplementary services amounting to 5% to 10% of the price of the initial contract are common for works contracts in utilities procurement, the 5% threshold appears to be unreasonable.

## 9. CREATION OF AN UNNECESSARY ADDITIONAL SUPERVISORY LAYER (ART. 93)

The new Title IV (Governance) of the proposal Directive essentially requires Member States to establish national supervisory authorities for public procurement and to equip such authorities with comprehensive monitoring powers. Considering the fact that the procurement review authorities, established according to Directive 92/13/EC are active in the member states, additional supervisory authorities intended to ensure compliance with the targets stipulated by European procurement directives is totally unnecessary. To the contrary, it will amount to the creation of additional unnecessary administrative costs at a time when the EU and Member States are devoting tremendous efforts at reducing such administrative costs. Whether or not to establish a national supervisory authority should thus be left to the Member States to decide. More far-reaching European initiatives for monitoring compliance with procurement law in the Member States must, in any case, be strictly measured against the principles of subsidiarity and proportionality. In this context, it must again be pointed out that only 1.6% of public contracts are awarded to operators from other Member States10.

The establishment of additional procurement law supervisory authorities is not compatible with the goal of reducing bureaucracy. Rivalry between authorities and competing procedures will lead to further barriers to investment in public infrastructure in European Union. This will especially be the case if, as planned; the authorities are to also operate independent of the economic operators who have a specific interest in the contract being awarded.

Such a structure is above all likely to result in an increase in legal disputes and litigation (insofar as it can be accessed by citizens, without this referral being restricted, even if only by the concept of a legal interest in bringing proceedings) with possibly very questionable foundations, which would have significant negative consequences on the economic efficacy of contracting entities and the effective implementation of contracts awarded to economic operators.

[10]European Commission, GREEN PAPER on the modernisation of EU public procurement policy Towards a more efficient European Procurement Market, COM 2011(15), p. 5, footnote 9.

## Disclaimer

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