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The Teckal exemption from procurement – new guidance from the ECJ on the essential activity test

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In the 1999 judgment of *Teckal* (C-107/98) the ECJ established an exemption from public procurement for the award of contracts by a public authority to a separate entity provided certain requirements were met. Those requirements were that:

1. The contracting authority must exercise sufficient control over the separate entity (with the test applied being that the control should be similar to that which the contracting authority exercises over its own departments); and
2. The separate legal entity must carry out the essential part of its activities for its owner authority/ies ("the essential activity test").

This exemption, widely known as the "Teckal exemption", was formally codified into the 2014 EU Procurement Directive (Article 12), and therefore our Public Contracts Regulations 2015 (Regulation 12), which also clarified that the requirement that the separate entity carried out the essential part of its activities for the owner authority meant that at least 80% of its activity must be for that authority. Regulation 12 also confirmed the principle established in case law that there can be more than one contracting authority owner.

On 8 December 2016, the ECJ handed down its judgment in the case of *Undis Servizi Srl v Comune di Sulmona and others* (C-553/15). It should be noted that this case was decided before the implementation of the 2014 Directive such that the Court considered the situation in light of the provisions of the 2004 Directive and relevant case law.

The facts of the case were that on 30 September 2014 the Municipality of Sulmona awarded a contract for the management of its waste to Cogesa, a company wholly owned by several municipalities in the Abruzzo region of Italy, including Sulmona (which itself owned 200 of the company's 1,200 shares). It appears that the documents initially formalising the ownership of Cogesa did not provide that the local authorities exercised jointly a control similar to that exercised over their own departments (as per the first limb of the Teckal test) but an agreement to that effect was entered into on 30 October 2014 (before the contract with Cogesa was concluded).

A key issue was that the regional government of Abruzzo had issued legislation requiring certain municipalities in the region to use Cogesa to treat and recover their waste. These municipalities were **not** shareholders of Cogesa.

A claim was issued in the Italian court by Undis, a provider of waste services in the region, which argued that requirements for the Teckal exemption to apply had not been met and that the Sulmona contract should have been subject to procurement. In order to determine the issue, the court referred two questions relating to the essential activity test to the ECJ:

1. Whether in order to determine whether the contractor carries out the essential part of its activity for the contracting authority, including local authorities which are its controlling shareholders, an activity imposed on that contractor by a non-shareholder public authority for the benefit of local authorities which are also not shareholders of that contractor and do not exercise any control over it must be taken into account. By this question, therefore, the ECJ was required to consider whether the activity carried out by Cogesa for non-shareholder authorities *as a result of the statutory requirement for it to do so* should be taken into account.

2. Whether, for the purpose of determining whether the contractor performs the essential part of its activity for the shareholder local authorities which jointly exercise over it control similar to that which they exercise over their own departments, the activity of that contractor performed for those local authorities before such joint control took effect must also be taken into account.

The ECJ confirmed in relation to question 1 that when calculating the essential activity, services provided to public authorities that were not shareholders of the Teckal company must be treated as activity carried out for third parties. As such, in order for the Teckal exemption to apply, that activity must be no more than "marginal" in comparison with the activity carried out for the controlling authorities. The fact that the activity for the non-owning municipalities was *imposed* on Cogesa by the regional government made no difference to this conclusion where the regional government itself was not a shareholder or controller of the company.

Since the implementation of the 2014 Directive, the test for whether activity for a third party is "marginal" is whether that activity amounts to less than 20% of the company's overall activity.

With regard to question 2, the ECJ confirmed that in calculating the Teckal company's essential activity account must be taken of all the circumstances of the case, which may include activity carried out by Cogesa for the relevant municipalities before they took joint control of the company. The Court therefore concluded that activities which were already carried out for controlling authorities before the conclusion of the formal cooperation agreement and which continue after conclusion of that agreement must form part of the calculation of the company's essential activity (rather than counting as activity carried out for a third party). The Court also commented, although did not formally conclude, that in general, activity carried out before control was taken, but not on a continuing basis, may be relevant in the overall qualitative and quantitative assessment required in order to establish essential activity.

The case clearly focussed around some very specific facts and was decided on the basis of the law prior to the implementation of the 2014 Directive. However, it provides clear confirmation of a well-established principle: that the essential activity of the Teckal company (i.e. at least 80%) must be for owner controlling authorities and that activity for other non-owner controlling authorities counts towards the permitted 20% of activity for third parties. It also confirms that ongoing contract arrangements are relevant to the assessment of essential activity and indicates a willingness on the part of the ECJ to look at previous arrangements as an indication of future intentions.