



## Procurement and development agreements update

### Key points

The long awaited guidance from the OGC on the application of public procurement rules to development agreements was published on 16 October against the background of a number of significant decisions by the European Commission and the European Court of Justice.

The decisions confirm the principles that:

- Developers can no longer simply rely upon the argument that development agreements can be treated as land agreements and therefore outside the scope of the procurement regime.
- The definition of a public works contract is satisfied if a public authority procures by any means a work corresponding to specified requirements. How far a public authority can go in setting out its wishes without indirectly procuring works is unclear.
- It is not always necessary for the public authority to benefit in order for the procurement rules to apply.
- Procurement laws cannot simply be avoided by parties entering into separate agreements for works and for lease.

The recent OGC Procurement Policy Note contains some useful pointers as to factors to be taken into account in assessing whether or not a development agreement is likely to comprise a public works contract. However it is not, nor does it purport to be, definitive and each set of circumstances needs to be considered individually.

The message for developers and public authorities - seek procurement advice early on in discussions or negotiations for future development projects exceeding £3.49 million in value, or risk direct contracts for works entered into without a prior tender being challenged and set aside.

### Introduction

In the last year, the Commission has issued three reasoned opinions, amounting to a formal statement of infringement, concerning the application of public procurement law to regeneration/development agreements. Last week the European Court of Justice also confirmed an opinion by the Commission that a lease of four exhibition halls amounted to a public works contract for the purposes of procurement law.

These cases highlight the uncertainty for public authorities and developers regarding the type of agreement that will constitute a public works contract and consequently may need to be put out to tender. They also evidence the Commission's wide application of the procurement rules to works contracts adopted by the European Courts of Justice in the *Roanne*<sup>1</sup> case and intention to enforce the rules.

### The reasoned opinions

In March 2009, the Commission rejected arguments that the procurement rules did not apply to the purchase of land in *Quedlinberg* by a German public authority upon which a tax office building was to be constructed by the owner. It decided that the value and nature of the construction were such that the subject matter of the contract could not be said to concern the purchase of land only. It rejected the developer's argument that it was the only party who could construct the tax office building, finding that mere ownership of the land by the developer was insufficient justification.

The subsequent infringement cases involve property concessions in *Osbaldwick* in York for a residential development and *Eindhoven* in the Netherlands for a community centre. Under procurement law, concession

<sup>1</sup> 18 January 2007. A landmark case involving the development of a multiplex cinema and commercial centre, part of which would be put to public use and part of which would be sold to third parties, referred to the European Courts of Justice following a complaint by an aggrieved party that the development contract was not put out to tender.

contracts are not subject to the full advertising and tendering requirements but are required to be subject to a fair and transparent tendering procedure. The Commission has taken the view that the public authorities' have in some way procured works corresponding to their specified requirements and consequently have entered into public works contracts<sup>2</sup>. This was the finding notwithstanding the developers were granted the right to develop the schemes at their own risk and without payment from the public authority. The extent of the public authority's involvement in Eindhoven was limited to specifying the size and number of apartments to be built and number of car parking spaces to be provided.

These reasoned opinions confirm the principles in Roanne that:

- Developers can no longer simply rely upon the argument that development agreements can be treated as land agreements and therefore outside the scope of the procurement regime.
- It is not always necessary for the public authority to benefit in order for the procurement rules to apply. For example, there is no obvious direct benefit to the public authority arising out of the construction of the residential development in Osbaldwick.
- The specified requirements for works may not have to be detailed for the purposes of satisfying the definition of a public works contract. However how far a public authority can go in setting out its wishes without indirectly procuring works is unclear.

### **Commission v Germany dated 29 October 2009**

This case arose out of a reasoned opinion by the Commission that the construction of new exhibition halls and their subsequent letting to the City of Cologne without a tender process infringed EU procurement law.

This case demonstrates that the procurement laws cannot be avoided by parties entering into separate agreements for works and for lease. The City of Cologne entered into a lease of land with a private developer, upon which the exhibition halls were to be constructed by way of a separate agreement. The funding for the works was principally derived from the lease.

The European Court of Justice held that:

- the lease would not have been entered into without the construction of the exhibition halls on the land;

- the specifications for the buildings in the lease went far beyond those that a tenant would normally require;
- the main purpose of the lease was for the construction of the exhibition halls. The lease was simply used as a financing mechanism for the works.

In these circumstances, the lease amounted to a public works contract for the purposes of procurement law.

### **The OGC Guidance**

On 16 October 2009, the OGC published its preliminary guidance on the application of the public procurement rules to development agreements.<sup>3</sup> The guidance is useful in describing some of the procurement issues which can arise in relation to development cases, in accordance with its stated aim. It also contains some pointers as to factors to be taken into account in assessing whether or not a development agreement is likely to comprise a public works contract. Nonetheless, it is not definitive nor does it address some issues such as whether a s106 agreement can constitute a public works contract.

### **The risks**

The application of the public procurement rules to development agreements is likely to continue to be uncertain. Having issued these reasoned opinions, the Commission may decide to continue legal action against a Member State for breach of the rules, as happened in the case of *Commission v Germany*, or agree steps for the cessation of the infringement. If it decides to proceed with legal action, it is hoped that the Commission and the European Court of Justice will take the opportunity to further clarify their views.

Importantly the risk for non-compliance with the procurement rules increases significantly in respect of agreements entered into after 21 December 2009, when the Remedies Directive will be implemented in the UK. Under the Remedies Directive, illegal direct agreements may be set aside even after they have been entered into.

### **What should you do?**

In the meantime, the message for public authorities and developers is clear - consider the issues early and carefully (where appropriate with legal advice) to implement strategies and structures to minimise the procurement risk.

<sup>2</sup> Regulation (2)(1) of the Public Contracts Regulations 2006 defines a public works contract as a contract, in writing, for consideration - (a) for the carrying out of a work or works for a contracting authority; or (b) under which a contracting authority engages a person to procure by any means the carrying out for the contracting authority of a work corresponding to specified requirements.

<sup>3</sup> [http://www.ogc.gov.uk/documents/PPN\\_11\\_09\\_Development\\_Agreements.pdf](http://www.ogc.gov.uk/documents/PPN_11_09_Development_Agreements.pdf)

## **Contacts**

**John Houlden**, Partner, on +44 (0)117 902 2796 or email: [john.houlden@burges-salmon.com](mailto:john.houlden@burges-salmon.com) or

**Stephanie Rickard**, Senior Associate on +44 (0)117 902 6682 or email: [stephanie.rickard@burges-salmon.com](mailto:stephanie.rickard@burges-salmon.com)