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(Information)

INFORMATION FROM EUROPEAN UNION INSTITUTIONS, BODIES, OFFICES AND AGENCIES

EUROPEAN COMMISSION

COMMISSION NOTICE

Guidance on the award of government-to-government contracts in the fields of defence and security (Article 13(f) of Directive 2009/81/EC of the European Parliament and of the Council)

(2016/C 450/01)

1. Introduction

Government-to-government sales ('G2G') is a method that allows governments to procure defence equipment, services, and works from other governments. The purchasing government does not deal directly with any defence contractor; instead, the sale is made by the other government, either by offering from its own stocks or after having itself procured the equipment for that purpose. G2G often includes but is not limited to product support, maintenance, training, and infrastructure construction.

G2G transactions represent a non-negligible part of the defence market in the EU. Between 2005 and 2012, the value of defence purchases made by a Member State from another government was approximately EUR 22,8 billion (9 %) of the total EU spending on defence equipment.

Governments may decide to purchase military equipment or services from another government for a variety of reasons. In many cases, G2G offers 'selling Member States' the opportunity to dispose of surplus equipment, and 'buying Member States' to purchase defence capabilities at affordable prices. It can, therefore, be a useful tool to cope with the challenges of budget constraints and the restructuring of armed forces. In certain circumstances, G2G can also be the most appropriate — or even the only — procurement option to satisfy specific military capability requirements that are needed to ensure interoperability or the 'operational advantage' of Member States' Armed Forces. G2G can also be a rapid means of meeting urgent operational requirements.

G2G can also be used as a tool for cooperation among Member States. This may be the case, for example, where one Member State purchases, in compliance with the Directive, equipment or services on behalf of all cooperating Member States and subsequently transfers parts of these equipment and services to the other governments. Sections 3 to 7 of this Communication do not cover, in these situations, the contracts awarded for such transfers.

G2G transactions can take various forms and concern diverse types of equipment and services. The role of, and benefit for, industry vary considerably, and, depending on the size and the subject matter of the contract, G2G can have an important impact on the market. A failure to investigate all procurement options and justify the chosen procurement strategy prior to the contract award between governments may imply discrimination against one or more economic operators within the EU, be in some cases the result of circumvention of applicable rules, and have a negative impact on the well-functioning of the internal market.

In the Communication 'Towards a more competitive and efficient defence and security sector' [1] of July 2013, the Commission stated that specific exclusions contained in Directive 2009/81/EC of the European Parliament and of the Council [2] 'might be interpreted in a way undermining the correct use of the Directive. This could jeopardise the level

[1] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, COM(2013) 542 final, http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52013DC0542&rid=1

[2] OJ L 216, 20.8.2009, p. 76.

playing field in the internal market. The Commission will therefore ensure that these exclusions are interpreted strictly and that they are not abused to circumvent the Directive'. In order to do so, the Commission announced its intention to provide, in consultation with Member States, guidance on these exclusions, starting with contracts awarded from a government to another government ([1]).

The purpose of this Notice is to provide guidance by setting out good procurement practices for applying this exclusion, especially in view of reducing the risks of contravening EU law. This Notice does not lay down additional obligations or pre-conditions for the use of this exclusion to those of existing EU law. It is not legally binding. Only the Court of Justice of the European Union ('the Court') is competent to give a legally binding interpretation of EU law.

2. **The legal framework**

Under Article 2 of Directive 2009/81/EC ('the Directive'), contracts in the fields of defence and security have to be awarded in conformity with the provisions of this Directive.

Article 13(f) of the Directive provides for the exclusion of contracts awarded by a government to another government relating to (i) the supply of military equipment or sensitive equipment; (ii) works and services directly linked to such equipment; or (iii) works and services specifically for military purposes, or sensitive works and sensitive services.

Recital 1, which states that 'national security remains the sole responsibility of each Member State, in the fields of both defence and security', is relevant in relation to this exclusion as national security can be the reason why Member States choose to envisage G2G procurement.

Recital 30 of the Directive states that 'given the specificity of the defence and security sector, purchases of equipment as well as works and services by one government from another should be excluded from the scope of this Directive'. A distinctive feature of this sector is the extent that defence and security procurement is influenced by national security, which may, for example, be driven by the need for interoperability with allies.

According to Article 1(9) of the Directive, 'government means the State, regional or local government of a Member State or third country'. This implies that contracts concluded by, or on behalf of, other contracting authorities/entities, such as bodies governed by public law or public undertakings, cannot be excluded on the basis of Article 13(f).

Only contracts concluded exclusively between two governments can constitute 'contracts awarded by a government to another government' in the sense of Article 13(f) of the Directive. G2G supply contracts entail, in principle, transfer of title from the selling government to the purchasing government ([2]). By contrast, the fact that a government provides guarantees of good execution, or similar forms of support, to an economic operator competing for a contract does not make the exclusion applicable to that contract. Moreover, the exclusion only covers the contract between the two governments; it does not cover related contracts concluded between the selling government and an economic operator.

Article 11 of the Directive concerns the use of exclusions and states that 'none of the rules, procedures, programmes, arrangements or contracts referred to in this section may be used for the purpose of circumventing the provisions of this Directive'. Furthermore, it is well-established case-law of the Court of Justice of the European Union ('the Court') that provisions, which authorise exceptions to EU public procurement rules, must be interpreted strictly ([3]). At the same time, the Court has held that an exception 'must be construed in a manner consistent with the objectives that it pursues'. Therefore, the principle of strict interpretation does not mean that the terms in which an exception is framed 'must be construed in such a way as to deprive that exception of its intended effect' ([4]).

([1]) Report from the Commission to the to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, COM(2014) 387, http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014DC0387&rid=1

([2]) This is without prejudice to Article 1(4) of the Directive, which defines 'supply contracts' as 'contracts other than works contracts having as their object the purchase, lease, rental or hire-purchase, with or without the option to buy, of products'.

([3]) See, inter alia, Case C-337/06 Bayerischer Rundfunk, paragraph 64.

([4]) See Case C-19/13 Fastweb, paragraph 40.

According to the case-law of the Court, in interpreting a provision of European Union law, it is necessary to consider not only its wording but also the context, in which it occurs and the objectives pursued by the rules of which it is part ([1]). This means, in particular, that in interpreting and applying Article 13(f), the objectives of the Directive must be taken into account. These objectives are, inter alia, laid down in recitals 2 and 3, which state that 'the gradual establishment of a European defence equipment market is essential for strengthening the European Defence Technological and Industrial Base [EDTIB] (…)' and that 'Member States agree on the need to foster, develop and sustain a [EDTIB] that is capability driven, competent and competitive. In order to achieve this objective, Member States may use different tools, in conformity with [Union] law, aiming at a truly European defence equipment market and a level playing field at both European and global levels'.

Contracts falling outside the scope of application of the Directive may still be found subject to the rules and principles of the Treaty on the Functioning of the European Union (TFEU). There is, however, no case-law of the Court on the extent to which the rules and principles of the TFEU may apply to contracts excluded on the basis of Article 13(f) of the Directive.

3. **Market analysis**

It follows from the above that contracting authorities can, in duly justified cases, decide to award a contract to another government applying the exclusion under Article 13(f) of the Directive.

Decisions to award a contract to another government, therefore, should be preceded by an appropriate analysis, which clearly establishes that awarding a particular contract to another government is the only or the best option to fulfil the procurement requirements identified by the buying government.

This analysis should, in particular, identify whether competition is absent or impracticable (see Section 4) or whether, on the contrary, competition for the contract appears to be possible (see Section 5). When assessing whether competition is absent or impracticable or, on the contrary, appears to be possible, contracting authorities may choose to limit their analysis to the internal market.

This analysis implies an appropriate market examination adapted to the market conditions and to the specific requirements, which can also be done before finalising the definition of the requirement. For example, a contracting authority could publish a Request for Information notice on its website to initiate a technical dialogue, as referred to in recital 49 of the Directive, in order to give potential economic operators the opportunity to comment on the proposed requirement that could result in identifying alternative solutions.

Contracting authorities should document their analysis to be able, whenever required, to demonstrate, on the basis of supporting documentation, that their decisions are justified.

This is in line with effective procurement methods, especially in a situation of general budgetary constraints, and meets rules and standards of sound financial management. In addition, it considerably limits risks related to legal challenges both under EU and national law. Under EU law, it minimises the risks that the contracting authority's decision to award a contract to another government, applying the exclusion under Article 13(f), is successfully challenged, in particular, on the grounds of circumvention of the Directive (Article 11) and/or breach of the rules and principles of the Treaty.

4. **When competition is absent or impracticable**

Certain contracts, by their very nature, can only be awarded to other governments. This may be the case, for example, when one Member State provides military training to another Member State. Such contracts are generally awarded within the framework of military cooperation between States. Since there can be no commercial alternative, they have no impact on the functioning of the internal market.

In addition, there can be cases, where the analysis referred to in Section 3 clearly shows that commercial competition is absent or impracticable.

Some of the circumstances where competition is absent or impracticable in a commercial environment may be relevant for G2G procurement (e.g. single operator due to technical reasons or exclusive rights; urgency; additional supplies; repetition of works and services).

([1]) See, inter alia, Case 292/82 Merck, paragraph 12; Case C-34/05 Schouten, paragraph 25; Case C-433/08 Yaesu Europe, paragraph 24; and Case C-112/11 Ebookers.com, paragraph 12.

In these kind of situations, contracting authorities may have no viable alternative to awarding a contract directly to another government. This includes, for example, the following situations: i) the requirements identified by the contracting authority can, for technical reasons or reasons connected with the protection of exclusive rights, only be satisfied by one particular government; ii) the contracting authority faces urgent operational requirements such as an urgency resulting from a crisis or extreme urgency brought about by unforeseeable events; iii) additional supplies from the original selling government are needed as partial replacement or extension of existing supplies and a change of source of supply is not practicable due to reasons related to interoperability. Other circumstances can be envisaged where it is clear from the outset that a call for competition would not trigger more competition or better procurement outcomes than G2G procurement.

In cases, where contracting authorities consider competition to be absent or impracticable, they should document their analysis (see Section 3) to be able, whenever required, to demonstrate on the basis of supporting documentation that their decisions are justified.

Contracting authorities relying on Article 13(f) of the Directive because competition is absent or impracticable are advised to make their decision known by publishing either a free text in the OJ of the EU (see Section 5) or a voluntary ex ante transparency (VEAT) notice. Through such publication for procurement outside the Directive, the contracting authority announces its decision to award a contract to another government, based on Article 13(f), in situations where competition is absent or impracticable. The published text or VEAT will include a description of the intended G2G transaction, which will alert economic operators and provide an opportunity for them to present alternative solutions to the contracting authority that may have been overlooked.

'Annex D3 — Defence and Security' to the VEAT notice requires the contracting authority to provide a justification for the award of the contract without prior publication of a contract notice. Contracting authorities publishing a VEAT notice under the circumstances described in this paragraph would choose the option in paragraph 2 'the contract falls outside the scope of application of the Directive' and provide a short rationale for their decision.

For the sake of transparency, contracting authorities are also advised to publish — *ex post* — an announcement of the award of the G2G contract on, for example, their website or through a statement to the news media. Some of the information may be withheld from publication where its release would impede law enforcement or otherwise be contrary to the public interest, in particular defence and/or security interests, or would harm legitimate commercial interests.

5. **When competition appears to be possible: pre-procurement advertising and finalisation of procurement strategy**

There can be cases where contracting authorities considering procurement from another government — based on the analysis referred to in Section 3 — are uncertain, whether competition for the satisfaction of their specific procurement requirements is absent or impracticable.

In these situations, in the interest of effective procurement, to comply with standards of sound financial management, and to avoid legal risks, contracting authorities should examine the market further by making their requirements known via pre-procurement advertising. The objective of this further market examination is to establish whether, at least, one EU economic operator could genuinely compete to satisfy the requirements of the contracting authority (i.e. is able to deliver a similar or better solution than the G2G one). This will enable contracting authorities to finalise their procurement strategy (G2G or commercial procurement) with full knowledge of the market.

In this context, possible means of pre-procurement advertising include:

— the *Official Journal of the European Union* (OJ),

— national official journals or procurement portals,

— advertisements on the contracting authorities' own website or procurement portal,

— as complementary means of advertising, professional journals.

In cases, in which it is clear from the market analysis that all potential suppliers are known, sending requests for information to such potential suppliers can constitute an alternative to publication.

In case it is not clear from the market analysis that all potential suppliers are known, contracting authorities are advised to publish, as pre-procurement information notice, a free text in the OJ of the EU. In this specific situation, contracting authorities have the possibility to request publication of a free text in the OJ of the EU (ojs@publications.europa.eu), if standard forms are not suitable. Contracting authorities also have the option of using the VEAT notice (see Section 4).

The information included in this pre-procurement information notice, or in a request for information, can be limited to a general description of the requirements and an indication of the available budget. Contracting authorities should explicitly mention that they are finalising their procurement strategy, which might lead to the award of a contract to another government or to the launch of a formal procurement procedure under the Directive. Contracting authorities should also mention that they are giving potential economic operators the opportunity to provide evidence that they are economically and technically capable of meeting the requirements.

Contracting authorities could also choose to invite potential economic operators to comment on the proposed requirements, and to offer solutions that might facilitate competition or generate better value for money. Should contracting authorities decide to do so, they must ensure that equal treatment is respected and competition is not distorted.

At the same time, contracting authorities can contact other governments to explore whether their requirements can be satisfied via G2G.

Contracting authorities will use the information gathered from the advertisement and from discussions with other governments to finalise their procurement strategy in full knowledge of the market.

6. **Negotiations with governments**

If, based on an impartial assessment of the information gathered from pre-procurement advertising, contracting authorities reach the conclusion that awarding a particular contract to another government is the only, or the best, option to fulfil their requirements; they will proceed with the negotiations with such government(s) and ultimately award the G2G contract under the exclusion of Article 13(f) of the Directive.

In order to ensure that the contracting authorities' requirements are satisfied in the best possible way in accordance with effective procurement methods, and to avoid legal risks, contracting authorities should conduct impartial negotiations with governments. This is particularly important, when several government offers exist, and when the impact on the internal market is significant.

The final selection should be based on objective criteria such as quality, price, technical merit, functional characteristics, running costs, lifecycle costs, after sales service and technical assistance, delivery date, security of supply, interoperability, and operational characteristics.

In any case, contracting authorities should document their assessment to be able, whenever required, to demonstrate on the basis of supporting documentation that their decisions are justified.

7. **Procurement under the Directive**

If, on the contrary, an impartial assessment of the information gathered from pre-procurement advertising shows that one or more EU economic operators is able to deliver a better value for money solution than the one offered by G2G and there is no objective justification to procure from the selling government, contracting authorities will start a procurement procedure under the Directive. The relevant provisions of the Directive will then have to be complied with.