Tendered is the Contract:
Nuances of EU Land Development

BY JAMES THOMSON AND MATTHEW HALL

"Like the dull uncle at Christmas ... there is simply no way to avoid public procurement" [the new economics foundation (UK); *Public Spending for Public Benefit* (2005)]. It was thought for a long time that land development agreements in the European Union (EU) easily avoided this fate — this is no longer the case.

Consider this scenario: your EU subsidiary has been in discussions with a local authority about working on a town centre redevelopment. The managing director thinks that some of his competitors may be interested and, having obtained all internal approvals for the contract, wants to sign up quickly so that the company can start work. He assures you that "these arrangements happen all the time without tendering" and that this issue is nothing to worry about in terms of procurement law. Is he correct, or do you need to check this out?

START
EU LAND DEVELOPMENT

Unfortunately, you almost certainly will need to investigate further. The EU public procurement rules to which he refers are wide-ranging and catch many land development agreements, meaning that tendering may be required, and one of those competitors may have a claim if this is not done.

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The law: What are the EU public procurement rules?

In the European Union, land development agreements take a variety of forms. Typically, such agreements are between a government body, such as a local authority, and a developer concerning either a greenfield (never developed) site, or regeneration of a brownfield (previously developed) site, within the area for which the authority is responsible. Often, but not always, the same authority will have statutory planning responsibilities for the area.

The basic rules relevant to this situation are contained in EU Directive 2004/18 (the Public Sector Procurement Directive, or the Directive). The Directive requires "contracting authorities" (public bodies, including central government entities and local authorities) to award their contracts for goods, works or services, where these are above an estimated value threshold, pursuant to a public tendering process in accordance with the rules set out in the Directive and EU case law. Works contracts subject to these rules are called "public works contracts."

> It is important to realize that ***bona fide* land sales and purchases** by a public body are **outside the regime** imposed by the Directive.

It is always possible for a public sector purchaser to comply with the rules, even on a "failsafe" basis (where it uses the required public tendering process just in case the rules apply, to ensure that it is complying with the law). However, purchasers are often reluctant to do this because the rules are complex and difficult to interpret; cause delay and cost; and most importantly, generally stop the purchaser from negotiating directly with one chosen provider (since the point of the tendering process is to ensure a competition open to all qualified contractors).

When considering whether the Directive applies, the issue with a land development agreement that seems deceptively simple, but unfortunately often is not, is essentially whether a "public works contract" will be (or has been) entered into. A "public works contract" is a contract in writing for pecuniary interest (consideration) for the carrying out of works, or under which works corresponding to specified requirements are carried out.

Therefore, there are two key issues to consider in analysing a land development agreement to determine whether it will fall subject to the public procurement rules:

- Is there pecuniary interest?
- If so, does the contract have as its object the carrying out of works, or are works corresponding to specified requirements carried out under it?

A land sale is just a land sale and not subject to the rules

It is important to realize that *bona fide* land sales and purchases by a public body are outside the regime imposed by the Directive. The sale of land/buildings by a public body for market value (plus any truly ancillary elements agreed as part of the sale) is the disposal of an asset and is not a procurement of anything. There is no consideration paid by the public body for goods, works or services, and there will be no provision of works, services or supply of goods to the public body. The simple purchase of land or buildings by a public body for market value (plus any truly ancillary elements) is also generally not caught because of a specific exclusion in the Directive. However, anything going beyond a simple sale or purchase can give rise to issues. You need to be confident that all you have is such a sale or purchase before ignoring the possible application of the Directive.

An example of a case where a land purchase was part of a wider transaction, and as a result was considered to fall subject to the regime, is provided by the European Commission's investigation [using its general enforcement powers under the Treaty on the Functioning of the European Union (TFEU)] of a project in Germany (the *Quedlinburg* case). This concerned an untendered 2008 contract in which the German "Land" of Saxony-Anhalt purchased from a third party a piece of land, on which an adminis-

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trative building was to be constructed by that third party. The Commission took the preliminary view that the main purpose of the contract was to acquire a building for the German tax administration, which accordingly should have been tendered, and that the works could not be considered to be purely secondary (ancillary) to the purchase of the land. The Commission also held, on a preliminary basis, that the ownership of the land where public works are carried out does not automatically confer to the land-owner an exclusive position justifying the direct award of the works contract. The result of the case is not yet clear since the Commission is still investigating and cannot take a final decision; it would have to challenge the transaction in the European Court of Justice (ECJ), which would ultimately hand down its judgment on the issue.

A contrasting example of a land sale that was accepted as just a land sale is provided by the ECJ judgment on March 25, 2010, in the *Helmut Müller* case. This case concerned a land sale by one public authority, with another authority exercising urban planning powers over it. No link between the two arrangements/actions was found, save that the latter authority approved the sale, and there was no procurement. This case is considered in more detail below.

The *Auroux* case

The seminal authority in this area of law, and the one that has really caused all the current difficulty, is the 2007 ECJ judgment in *Auroux* (European Court of Justice judgment in Case C-220/05 *Jean Auroux and Others v Commune de Roanne, intervening party: Société d'équipement du département de la Loire (SEDL)* of Jan. 18, 2007). It is worth understanding this case in reasonable detail given its importance.

In 2002, the French municipality of Roanne decided, as an urban development measure, to construct a leisure center in the area around the railway station, including a multiplex cinema, commercial premises, a public car park, access roads and public spaces. The construction of other commercial premises and a hotel were envisaged subsequently. Roanne engaged a third party to acquire land, get funding, carry out studies, organize an engineering competition, undertake construction works, coordinate the project and keep the municipality informed. Roanne was not itself going to be the owner of the various facilities, apart from elements such as the public spaces and the car park. The contract with the third party had not been tendered.

In broad terms, the ECJ held that the contract was a public works contract, which should have been tendered. There were various specific findings that shed light on the analysis of the two key issues referred to above. In particular, the following points are relevant to the issue of the existence and level of pecuniary interest (consideration) involved in the contract:

- The total value of the opportunity to potential tenderers is what is relevant, not just the consideration directly received from the authority;

Ignore the Rules at Your Peril

If the public procurement rules apply but are ignored [because the public body (the purchaser) takes the risk or concludes incorrectly that the rules do not apply when they do], the purchaser faces a potential challenge from private sector contractors who feel that, given a proper tendering procedure, they would have had a chance of winning the contract.

The principal routes available to aggrieved potential contractors seeking enforcement of the rules are:

- Make a complaint to the European Commission, which might ultimately bring a case before the European Court of Justice; and
- Bring proceedings before a national court.

Of these two options, a complaint to the European Commission is cheaper and more straightforward for an aggrieved potential provider. However, it will be slow and leads to a loss of control over the process. For this reason, national court action is often attractive. In a national court, aggrieved potential contractors are able to obtain a range of remedies (including an injunction stopping a contract from proceeding, suspension of an award procedure and damages against the purchasing body). Recent changes to the law introduced by the Commission have improved the position of challenging parties, which is leading to increased litigation.

As an alternative, it may be possible to complain to the relevant government procurement policy body [for example, the Office of Government Commerce (OGC) in the United Kingdom]. In practice, at least if a central government body is the purchasing entity, this can result in significant pressure being brought to bear on the entity in question. Use can also be made of the network of central government procurement policy officials in Europe, called the Public Procurement Network (PPN). Members have agreed on common rules for how informally to pursue suspicions of irregularities before contracts are signed.

In addition, companies can use the SOLVIT system, which is monitored by the European Commission. SOLVIT tries to find informal solutions to internal market (including public procurement) issues of all types in the European Union. SOLVIT is, however, generally quite slow.

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Apart from a simple statement of intent, the sales contract **did not contain a legally binding obligation** for the developer to **realize the envisaged building;** it only stipulated a right to purchase the land for the City of Flensburg, **in the event the building was not constructed.**

- If the only consideration is the right to exploit works (such as by selling private flats), then the contract may be a "public works concession contract." This is a type of public works contract under which the consideration consists of or includes the right to exploit the work. This type of contract is subject to special treatment under the Directive, but still subject to an obligation to advertise; and
- A public body's contribution of cash or land, for no consideration or at an undervalue, will give rise to consideration. There may also be a benefit simply from providing the land, even if purchased by the developer for value. The developer is still gaining something.

On the second issue (whether there is a public works contract at all), the key learning from the case is that it is first necessary to consider the main purpose or object of the agreement. If this is another objective, which is outside the Directive (such as a land sale; see above), then the Directive will not apply. However, as soon as the public body specifies even in an outline what it wants to be constructed, then there is a risk that a public works contract will arise — in *Auroux* the authority had just specified in broad terms what it wanted to be done on the site. Generally, it is helpful to analyse this from a supplier's perspective; if the public body wants something done, that is likely to be a "requirement"— giving rise to a public works contract. This requires a case-by-case examination, as considered below.

Auroux follow-ups

There has been recent case law of varying use following the seminal *Auroux* judgment, and in addition to the Commission's *Quedlinburg* investigation (considering the treatment of a land purchase) referred to above.

The European Commission decided in another investigation that there was no legal obligation to carry out any works and therefore the rules did not apply (*City of Flensburg*; press release of June 5, 2008). This concerned a land sale for urban development purposes by the public utility company of the City of Flensburg, Germany. The public utility company, a 100 percent affiliate of the City of Flensburg, had sold a piece of land to a private property developer for the construction of a building that would correspond to certain urban development needs. Apart from a simple statement of intent, the sales contract did not contain a legally binding obligation for the developer to realize the envisaged building; it only stipulated a right to purchase the land for the City of Flensburg, in the event the building was not constructed. In the view of the Commission, such a land sale could neither be considered as a public works contract nor as a public works concession, because the contract in question did not contain a legally binding obligation to execute works specified by the contracting authorities. The mere right for the public authority to (re-) purchase the land in case of non-construction was not, in the Commission's view, a sufficient sanction that could give rise to a legal obligation to execute the works. The Commission therefore closed its investigation and did not challenge it before the ECJ.

Another case considered the issue of the main object of a contract, applying *Auroux*. This concerned a contract for the construction of four trade fair halls and additional premises concluded between the City of Cologne, Germany and a private investment company (*City of Cologne* case). Under the contractual arrangement, the investment company was to construct the trade fair premises in accordance with detailed specifications. The city would rent the buildings for a fixed period of 30 years, paying a total rent of more than EUR600 million. Under a sub-lease agreement, the city would, in turn, let the premises to the trade fair company Koelnmesse GmbH. The German government argued that the agreement between the city and the investment company was a simple rental contract that was not subject to the rules of public procurement law. However, in the view of the Commission, the contract was a public works contract because the city, which is a public

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The UK Office of Government Commerce: Characteristics of a Development Agreement that is Less Likely to Fall Subject to the Public Procurement Rules

1. The proposed development or a significant part of it is to be undertaken at the initiative and autonomous intention of the developer (which is particularly likely if the developer already owns or has control of the land to be developed).
2. The agreement is ancillary or incidental to a transfer, or lease of land or property, from the authority to the developer, and is intended to protect the interests of a contracting authority that is the lessor or otherwise retains an interest in the land or property.
3. The agreement is based on proposals put forward by the developer (these proposals may be sought and the winner "chosen" by the authority).
4. There is no pecuniary interest passing from the contracting authority to the developer directly or indirectly, for example, through the assumption of obligations such as contributions towards project finance, or guarantees against possible losses by the developer.
5. The agreement does not contain specific contractually enforceable obligations on the developer to realise works (even if the work is recognised as being the general intent of the parties to the agreement).
6. The development does not consist of or contain works for the direct economic benefit of the contracting authority.
7. The involvement of the contracting authority consists only in the exercise of statutory land-use planning powers.
8. The "totality and overall nature" of the agreements put in place must be considered.

authority, obtained works executed in accordance with its requirements. The city was therefore obliged to award the contract in a EU-wide contract award procedure. The Commission challenged the arrangement before the ECJ, which agreed in its judgment of Oct. 29, 2009, holding that the contract had as its main object the construction of the exhibition halls in accordance with the requirements of the City of Cologne.

An important case is the *Helmut Müller* judgment of the ECJ, March 25, 2010, which was referred to above. It was held that there will not be a "public works contract" potentially subject to the rules unless the works are carried out for the "authority's immediate economic benefit" and this is not the case if all the authority is doing is exercising "regulatory urban-planning powers" (including "examining building plans submitted to it" and "taking a decision applying its powers in that sphere"). Further, there will not be a public works contract potentially subject to the rules unless the contractor assumes a legally enforceable obligation to carry out the works (see also *Flensburg*, referred to above). There will also not be a public works contract unless the purchaser has "taken measures to define the type of work," or at least "had a decisive influence over its design." Finally, if there is no consideration other than the grant of a right to exploit the work in question (there must be consideration to be caught by the rules), and if the contractor already owns the land, the arrangements cannot be subject to the rules because it already has all rights to exploit.

As noted above, the case concerned a land sale by one public authority, and another authority exercising urban planning powers over it, with there being no link between the two arrangements/actions, save that the latter authority approved the sale. Clearly a (more usual) unitary situation in which the same authority sells the land and deals with planning is different. Nevertheless, the above points, concerning immediate economic benefit/urban-planning powers, the need for a legally enforceable obligation and the definition of the type of work involved, are generally important.

The Commission appeared to apply *Auroux* in its investigation of another situation in which a local authority owned land and transferred it for a particular use. The transaction in question was the award of a contract by the City of York Council, United Kingdom, relating to the residential development of a piece of land known as "Osbaldwick" (the *Osbaldwick* case). The award was made directly to a UK housing trust and it was a concession contract, with the trust being paid in part by the right to exploit the development after it had been built. The contract award was reopened following the Commission's investigation, and the council decided to award it in four phases, each following a separate tendering process. The Commission therefore closed its investigation on May 5, 2010.

The most recent ECJ judgment in this area looked at the main object of a contract and found that it was not a public works contract in the case in question. This was an ECJ judgment of May 6, 2010, concerning the partial privatization of a public casino business (*Club Hotel Loutraki* case).

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- *European Briefings: European Procurement and Secrecy (June 2009).* In view of higher expense, slower process and tighter policies, consider taking a closer look at European public procurement laws before signing a contract. *www.acc.com/docket/pro&sec_jun09*

Articles

- *Loan Purchase Transactions: An Innovative Approach to Acquiring Real Estate Assets in a Downturn Market (June 2008).* Read this article for a guide to loan purchase transactions. It includes guidance on understanding the characteristics of the loan, direct purchase of mortgage loan, purchase of foreclosure bid and consensual deed in lieu of foreclosure. *www.acc.com/loanpurtrans_jun08*
- *Environmental Due Diligence In Real Estate Transactions (April 2007).* This article covers the necessary evaluations of environmental issues a practitioner must consider in real estate transactions. *www.acc.com/envidue dil_retrans_apr07*
- *All Appropriate Inquiries in Commercial Real Estate Due Diligence: What Inquiring Minds Need to Know (Feb. 2007).* This article discusses the purpose of the "All Appropriate Inquiries" (AAI) rule, the history of AAI, defenses to CERCLA and Florida law liability, and key provisions of the AAI rule. *www.acc.com/comre_duedil_feb07*

Quick Reference

- *Real Estate Financing (March 2006).* Review this key risk management provisions checklist for notes and mortgages. It includes provisions for defaults and remedies, commercial general liability insurance (CGL), property insurance, escrow accounts, maintenance, environmental indemnification, and carve-outs and non-recourse provisions. *www.acc.com/quickref/re_fin_mar06*

Program Material

- *Tips and Traps in Negotiating Contracts in Eastern Europe (June 2007).* Learn the right tips for dealing with contract negotiation in Eastern Europe. *www.acc.com/eurocontraps_jun07*

Webcast Transcript

- *Managing International Real Estate Portfolios (Nov. 2007).* Examines a case study of a fortune 500 US multi-national that operates across multiple jurisdictions, and addressed the most common issues that arise in managing real estate across the globe. *www.acc.com/transcript/iraports_nov07*

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A single contract was granted, which dealt with the sale of shares, the right to nominate board members, the obligation to assume management of the casino business, and the obligation to refurbish and improve the sites concerned and surrounding land. The contract had to be entered into with a single partner capable of purchasing the shares and operating the casino. The purchase was found to be the main object, and the works and services were ancillary to this. It was relevant that the income the purchaser would get as a shareholder would be significantly more than the remuneration it would obtain as manager. The most recent European Commission investigation concerned a contract for land development in Eindhoven that was awarded without a competitive tender (see *Eindhoven*). On June 3, 2010, the European Commission challenged this before the ECJ. The transaction appears to be a classic example of a structure caught by the EU public procurement rules following *Auroux*. It involved a sale of land (presumably for value) with no additional payment. However, the contract obliged the developer to realise, at its risk and for its account, a specific number of buildings and apartments of a specific size, and a specific number of parking places and facilities, such as a shopping mall and a health center. In the Commission's view, this was the main object of the contract, as the authority had a decisive influence on the work that was to be constructed, took the initiative and had influence far beyond the mere exercise of urban planning powers. There was also a "right of exploitation," and therefore consideration, since the developer acquired "a tailor-made building license that gives [it] the right to construct and to exploit the work." Finally, the Commission took the view that the authority obtained a clear and direct economic benefit within the meaning of the *Helmut Müller* case. The contract was intended to regenerate the area, ensure the availability of specific services and offer economic advantages. Further, the authority received a subsidy from the Dutch state for each house to be built. The ECJ has yet to rule on this case.

UK guidance

There are definitely some themes developing, but the analysis of all cases will continue to be very fact-specific.

Perhaps reflecting this, the European Commission has not produced guidance in this area. However, the UK Office of Government Commerce (OGC), a government body responsible for procurement policy in the United Kingdom, has attempted to do so, given particular concerns and confusion in the United Kingdom as to the implications of *Auroux*. The guidance is, however, extremely cautious, stating for example that "understanding and interpretation of the law in this area still remains subject to change, and this ... guidance is not definitive." The OGC says it "may ... revise this guidance, or issue additional guidance, in due course."

Particular structures and "exemptions"

From the case law referred to above and other sources including the OGC guidance, it is possible to construct an analysis of particular structures and exemptions, which may be useful in relation to land development agreements.

Ancillary to a contract of another kind: As described above, it is necessary in any case to identify the main object of the contract. Any elements genuinely incidental or ancillary to that main purpose are considered part of the main purpose. This could apply where, for example, a land sale/lease or acquisition, or a business sale is genuinely the main object of the contract. This is a question of fact and degree in each case, but one could ask in relation to a land sale, for example: "Is the public body's main purpose for entering into the arrangements to effect an advantageous land transaction, in the context of an essentially private development scheme; and not to benefit from the works to an overriding extent, save by way of enhanced consideration for the public body's land ownership?" If the answer to this question is "yes" then arguably the public procurement rules do not apply. However, the inclusion of conditions relating to other land, or that impose obligations clearly not consequential to the sale, are likely to give rise to concerns.

The OGC guidance comments regard that, "a conservative and purposive approach would be prudent," and one of the relevant factors is the scope and value of the works, compared with the value of the sale.

Planning obligations — if that is all there is: Similar arguments can apply to planning requirements. Thus, a distinction can be drawn between works in planning terms that are an essential incident of the development, and works in planning terms that are something extra.

No obligation to construct, not enough specification and/or developer-led arrangements: *Flensburg* and *Helmut Müller* illustrate that there needs to be a contractual/binding obligation to construct; an intention is not enough. Regarding the level of specification, the OGC guidance indicates that to fall within the Directive, "requirements have to be sufficiently specific and detailed ... such that they can be legally enforceable" and that "the setting of broad parameters for a development is qualitatively different from the type of specification [that would bring a contract within] the requirements of the public procurement rules." Developer-led arrangements, under which the developer takes the lead, are also easier to justify (see *Eindhoven*).

Exclusive rights and technical reasons: The Directive contains exemptions allowing for direct negotiations with only one provider, where for reasons connected with the protection of exclusive rights or for technical reasons, the contract may only be awarded to a particular operator. It is undecided whether these can be used in the case of a land development to justify direct negotiations with a third party, for example, because it owns necessary land or access to it and there are no alternatives.

Policy not specification — a possible way out: If there is an existing policy applicable to the area in question, there may be an argument that a requirement to implement it is not a specification of works required (but implementation of a policy). The OGC guidance states that a development "in accordance with applicable national or local land-use planning policies" is unlikely to be caught.

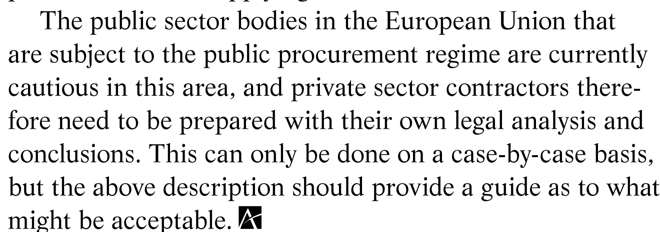
> From the case law referred to above and other sources including OGC guidance, **it is possible to construct an analysis** of particular structures and exemptions, **which may be useful in relation to land development agreements.**

No direct economic benefit: If the purchasing public body does not receive a direct economic benefit, the transaction will not fall subject to the regime. This is a difficult concept, but the OGC guidance offers an example of a situation outside the regime: a requirement that a certain proportion of housing in a development is to be "affordable" (for low-paid/essential workers), in accordance with central government rules, provided the purchasing body has no rights over the use of the housing (such as the right to nominate tenants).

However, like all EU law, **arrangements have to be analyzed thoroughly** and in the round, so that artificial arrangements **intended to circumvent the application of the rules** are unlikely to be acceptable.

Individual analysis is best bet for now

This is a difficult area. There is no formal single definition of a development agreement, and each case is different. However, like all EU law, arrangements have to be analyzed thoroughly and in the round, so that artificial arrangements intended to circumvent the application of the rules are unlikely to be acceptable. In broad terms, in cases where a public body is bringing something to the table, other than its ability through its statutory powers to facilitate a development (and/or imposes its own requirements in a development agreement as a condition of permitting the development), even if it is for the public and not for its own benefit, there will be a real prospect of the public procurement rules applying.



The public sector bodies in the European Union that are subject to the public procurement regime are currently cautious in this area, and private sector contractors therefore need to be prepared with their own legal analysis and conclusions. This can only be done on a case-by-case basis, but the above description should provide a guide as to what might be acceptable.

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Notes

1. European Court of Justice judgment in Case C-220/05 *Jean Auroux and Others v Commune de Roanne, intervening party: Société d'équipement du département de la Loire (SEDL)*, Jan. 18, 2007.
2. European Commission press release IP/08/867 "Public procurement: Commission closes infringement case against Germany concerning an urban development project in Flensburg," June 5, 2008.
3. European Commission press release IP/09/437 "Public procurement: infringement proceedings against Germany concerning award of public works contract for construction of tax office building in Quedlinburg," March 19, 2009.
4. European Court of Justice judgment in Case C-536/07 *Commission of the European Communities v Federal Republic of Germany,* Oct. 29, 2009 (*City of Cologne* case). See also European Commission press release IP/10/683 "Public procurement: Commission requests Germany to comply with Court judgment on the construction of trade fair halls in Cologne and to ensure fair access to waste disposal contracts in Hamm," June 3, 2010.
5. European Court of Justice judgment in *Case C-451/08 Helmut Müller GmbH v Bundesanstalt für Immobilienaufgaben*, March 25, 2010.
6. European Commission press release IP/10/507 "Public procurement: Commission closes infringement procedure against United Kingdom over land contract in York," May 5, 2010.
7. European Court of Justice judgment in joined Cases C-149/08 and C-145/08 *Club Hotel Loutraki AE, Athinaïki Techniki AE, Evangelos Marinakis v Ethniko Simvoulio Radiotileorasis, Ipourgos Epikratias, intervening parties: Athens Resort Casino AE Simmetokhon, Ellaktor AE, formerly Elliniki Tekhnodomiki TEV AE, Regency Entertainment Psikhagogiki kai Touristiki AE, formerly Hyatt Regency Xenodokhiaki kai Touristiki (Ellas) AE, Leonidas Bompolas* (C-145/08) and *Aktor Anonimi Tekhniki Etairia (Aktor ATE) v Ethniko Simvoulio Radiotileorasis, intervening party: Mikhaniki AE* (C149/08), May 6, 2010.
8. European Commission press release IP/10/679 "Public procurement: Commission refers Netherlands to court over land development project in the Municipality of Eindhoven," June 3, 2010.
9. UK Office of Government Commerce Information Note 12/10 "Public Procurement Rules, Development Agreements and s106 'Planning Agreements', Updated and Additional Guidance," June 30, 2010.

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