

NEW ACT ON PUBLIC CONTRACTS IN THE FIELDS OF DEFENCE AND SECURITY

D&I Focus
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- New Act is expected to enter into force in the beginning of 2012
- New Act implements Directive 2009/81/EC which aims to increase competition in the EU-wide defence and security market
- State security related matters will be taken into consideration in defence and security procurements

> ACT ON PUBLIC CONTRACTS IN THE FIELDS OF DEFENCE AND SECURITY IS UNDER WAY

The object is to bring defence and security procurements under statutory regulations

On 14 October 2011 the Finnish government gave a Government Bill (the "Bill") on a new Act on Public Contracts in the Fields of Defence and Security (the "Act"). The proposed Act should presumably enter into force in the beginning of 2012. The Act would implement the Directive on the coordination of procedures for the award of certain works contracts, supply contracts and service contracts by contracting authorities or entities in the fields of defence and security 2009/81/EC (the "Directive"). The object of the Directive is not to alter the scope of application of other legislation on public procurement but to bring defence and security procurements under statutory regulations. Therefore the implementation of the Directive would not affect how the tendering proceedings of other procurements than defence and security procurements are regulated. The Directive differs from the earlier Directives on public contracts only slightly. Consequently, the proposed Act is very similar, for instance, to the general Act on Public Contracts.

The approximated yearly value of defence and security procurements in Finland is approximately EUR 800 – 900 million. However, Finnish legislation has not previously set any provisions on tendering of defence and security procurements. The current Act on Public Contracts specifically excludes from its scope procurements which are mainly for military use.

The Directive could have been implemented through either amending the Act on Public Contracts or through passing a separate act. A separate act was chosen due to several technical differences between the Directive and previous directives on public procurement. It will be clarified in the existing procurement legislation that defence and security procurements are regulated in the new Act.

> SCOPE OF APPLICATION

The new Act only applies to defence and security procurements. All procurement entities would apply the proposed Act instead of other legislation on public procurement if the object of the procurement relates to defence or security matters. According to the Bill such matters would be supply of defence equipment and procurements that require security measures.

The new Act would be applicable to the procurement of defence and security equipment and procurements requiring statutory security measures

Defence equipment is defined as equipment that is designed or suited for military use or parts or components for that kind of equipment. The basis for the definition of defence equipment is the list of arms, munitions, and war material adopted by the Council on 15 April 1958 (Decision 255/58). In order to take into account technological development the list must, however, be interpreted broadly and also other sources, such as Common Military List of the EU (2011/C 86/01), should be considered. In addition, procurements that concern building contracts, goods or services that are especially used for military purposes or are related to the above mentioned defence equipment also fall under the definition, even if they were originally designed for civilian use.

Security procurements relate to the award of goods, services or building contracts which require special statutory security measures. Therefore these procurements have two criteria: (i) the equipment in question must have a security purpose and (ii) involve, require or contain classified information. The requirement for certain information to be classified has to be provided by legislation, regulation or administrative provision. The procurement entity may not decide on its own initiative that certain information is considered classified. According to the Bill, for example, technical systems to prevent crime and terrorism as well as border guard equipment and electronic infrastructure would fall under the scope of the proposed Act.

Procurements that require publication of information which endangers essential security interests of the State would be excluded

Individual Member States are granted a possibility to derogate from the Directive in exceptional situations where the Directive does not sufficiently protect the essential security interests of the State. A Member State could rely on the exception when a particular procurement sets demanding requirements in terms of security of supply or is exceptionally confidential or important to national sovereignty. The exclusion is based on Article 346 of the Treaty on the Functioning of the European Union ("TFEU") that gives the Member States a possibility to depart from EU regulations if a Member State considers it necessary for the protection of its essential security interests. However, this right must be interpreted strictly because it is a derogation from the TFEU. According to the case law of the European Court of Justice it should be limited to clearly exceptional cases based on a case-specific evaluation.

> EU AND NATIONAL VALUE THRESHOLDS

There are intended to be separate thresholds for EU and national procurements. The EU thresholds would be set by the European Commission and revised every two years. Procurements which exceed the EU thresholds must be put out to tender on an EU-wide level. At the entry into force of the Act, the thresholds would be the following:

(i) EU thresholds

EUR 400,000 for goods and services; and

EUR 5,000,000 for building contracts.

(ii) National thresholds

EUR 100,000 for goods and services; and

EUR 500,000 for building contracts.

> THE EU PROCEDURES

Procurements which exceed the EU thresholds must follow the detailed procedures based on the Directive. In contrast with the general Act on Public Contracts under which open procedure is most commonly used, the new Act has no open procedures. This is due to the complex nature of defence and security procurements and the specific data protection as well as maintenance and supply security requirements in the national legislation. These specific aims require that the suitability of the candidates is evaluated before invitations to tender are sent out. Negotiations between the procurement entity and the tenderers would also often be necessary.

Consequently, according to the Bill, the following procedures would be available when EU thresholds are exceeded:

- (i) Restricted procedure;
- (ii) Negotiated procedure;
- (iii) Competitive dialogue;
- (iv) Framework arrangements; and
- (v) Direct award of contracts.

Under the proposed Act, open procedures are not available – restricted and negotiated procedures would be primarily used instead

Restricted procedure and negotiated procedure would be primarily used in all defence and security procurements.

Restricted procedure is a two-phase procedure where the procurement entity is allowed to restrict the number of tenderers. The procurement entity publishes a procurement announcement based on which candidates submit their entry applications. The procurement entity will then select the candidates, who will receive the actual invitation to tender based on the criteria set out in the announcement.

Negotiated procedure is a more flexible procedure which enables negotiations between the procurement entity and candidates during the tendering process. After the selection of the tenderers, the procedure continues with negotiations between the tenderers and the procurement entity.

There are few differences in the procedures compared to the general Act on Public Contracts

In contrast to the general Act on Public Contracts the procurement entity could freely choose between these two procedures. In both procedures the procurement entity has to choose at least three candidates to take part in the competitive bidding.

The competitive dialogue procedure, directly awarded contracts, and framework agreements could be used under special conditions laid down in the proposed Act. These procedures correspond to a large extent to the ones in the general Act on Public Contracts. There are, however, certain specific additional justifications for the direct award of contracts. According to the proposed Act, directly awarded contracts could be used, for example, in case of urgent procurements related to establishing a new military or civilian crisis management operation or for the procurement of air or sea traffic services for the purpose of moving armed or security forces abroad.

> NATIONAL PROCEDURES

A less stringent national procedure would apply to procurements falling short of the EU threshold values

A separate national procedure would be applicable to procurements whose value falls short of the EU thresholds but exceeds the national thresholds. The national procedure is notably less stringent than the EU procedure. General provisions on equal and non-discriminative treatment and transparency of the procedure are the basis for the national procedure.

The national procedure would also apply to defence procurements that exceed the national threshold value but remain outside the application of the EU procedures due to State security reasons based on Article 346 TFEU.

The national procedure would require a public notification of an intended procurement unless specific criteria laid down in the Act are met.

The procurement entity would be allowed to negotiate all the aspects of the procurement with the tenderers if the invitation to tender or the procurement description includes a mention on possible negotiations. The procurement entity could arrange negotiations before publishing the invitation to tender in order to clarify legal, financial and technical details of the procurement. The procurement entity could also negotiate with the tenderers on the terms and conditions of the procurement contract. The negotiations may not compromise the fairness of the tendering procedure.

> ROLE OF SUBCONTRACTING

Under the general Act on Public Contracts the procurement entity is allowed to require that the tenderer specifies which part of the contract would be fulfilled by a subcontractor and who would be the nominated subcontractor.

Procurement entities could require that subcontractors are used

Under the proposed Act the procurement entity would be allowed to require that the tenderer fulfills the contract by offering a part of the contract (up to 30% of the value of the entire contract) to subcontractors directly or via competitive bidding. The aim is to open competition on the subcontractor level. The procurement entity could reject a subcontractor chosen by the tenderer but only based on the same selection criteria that are applied to the tenderer itself.

> LEGAL REMEDIES

Use of legal remedies must not endanger the security of the State

The legal remedies in the proposed Act would be to a large extent similar to the proceedings under the general Act on Public Contracts. The proposed Act takes into consideration the special nature of the defence and security procurements. The objective is to ensure that the use of legal remedies does not endanger the security of the State. According to the Bill, matters such as protection of the State's sovereignty, protection of classified security information and requirements regarding emergency supply are relevant in relation to State security interests.

The legal remedies would consist of two procedures: (i) procurement correction by the contracting entity and (ii) appeal to the Market Court and possibly further to the Supreme Administrative Court.

Two parallel procedures – procurement correction and appeal to the Market Court

Procurement correction is intended to be a fast and efficient procedure to correct clear errors in the procurement procedure before the procurement contract is signed. It could be used for all defence and security procurements including procurements which are outside the scope of the tendering proceedings of the proposed Act, *i.e.*, procurements fulfilling the

criteria of TFEU 346 and procurements whose value is less than the national threshold.

The procurement correction procedure could be initiated by the procurement entity or a party to the procedure (*i.e.*, candidate tenderers or tenderers whose legal position the procurement decision otherwise affects). According to the Bill, subcontractors would not be allowed to appeal against the decision of the procurement entity to reject the subcontractor chosen by the tenderer.

Procurement correction procedure could be used for all procurements

The procurement entity could set aside a faulty decision and make a new award decision on its own initiative and without the consent of the parties to the procurement procedure.

A prerequisite for using the correction procedure would be that there has been a legal error. The Bill provides examples of erroneous application of law:

- The procurement entity notices a mistake in comparing the tenders;
- A new decision is necessary to correct unfair treatment of the tenderers or candidate tenderers due to faulty procedure, *e.g.*, the procurement entity has not delivered the same information to all the tenderers;
- Breaches of other legislation which is related to the procurement procedure, *e.g.*, provisions on the disqualification of the decision makers of the procurement entity.

Procurement entity could correct a legal error in the procurement even if the matter was already taken to Market Court

The tenderer or candidate tenderer would need to initiate the procurement correction procedure within 14 days from being informed of the decision. The procurement entity could initiate the procedure within 60 days from the making of the decision. This would allow the procurement entity to correct the matter itself even if the matter is already brought to the Market Court. The Bill does not set a time limit for concluding the procurement correction procedure. However, the matter should be solved without unnecessary delay.

The procurement decision cannot be corrected if the invitation to tender has been in breach of the proposed Act. In such case the procurement entity can interrupt the procurement. The reason for interruption must be real and the interruption must not cause discriminative or unfair treatment of the tenderers or candidates.

The parties to the procedure could also refer procurement decisions to the Market Court. The subject of the appeal would be the decision made by the procurement entity or other similar measure which affects the legal position of a party to the matter. According to the Bill, preparatory actions cannot be brought into the Market Court.

The petition would have to be submitted in writing and no later than 14 days after the candidate or tenderer has received written information about the decision and the petition instructions. If the decision was not given to a participant properly, *e.g.*, the petition instructions are deficient, the participant's appeal period begins to run but the appeal can be submitted up to six months after the procurement decision was made. If the decision was not given to a participant at all, then the participant's appeal period does not begin to run. The Market Court is allowed to prohibit, suspend or permit the enforcement of the procurement decision or otherwise interrupt the procurement procedure for the duration of the court proceedings.

According to the Bill, the Court would have discretionary power to choose between different remedies but the primary remedies would be:

- (i) Wholly or in part cancelling a decision by a procurement entity;
- (ii) Forbidding the procurement entity to apply a section in a document relating to the contract or otherwise to pursue an incorrect procedure;
- (iii) Requiring the procurement entity to rectify an incorrect procedure.

If the harm caused to the procurement entity, rights of third parties, State security or public interest outweighs the benefits to the petitioner or if the petition has been initiated after the conclusion of the contract, the Market Court could only award compensation. The procurement entity would then have to pay compensation to a party who would have had a genuine chance of winning the contract if the procedure had been correct.

***Certain remedies
would only apply to
procurements that
exceed the EU thresholds***

Additional remedies, which would only be applicable to procurements above the EU threshold, include declaring the contract null and void, imposition of fines on the procurement entity, and shortening the duration of the contract. The Market Court would also be allowed to impose a threat of fine to ensure that the sanction will be obeyed.

The Market Court could impose a sanction only if the error has affected the result of the procedure. Appeals against the rulings issued by the Market Court could be lodged in the Supreme Administrative Court.

> RESTRICTED USE OF LEGAL REMEDIES FOR CERTAIN PROCUREMENTS

*In certain situations
appeal to the Market
Court is only possible with
permission to appeal*

Decisions within framework arrangements and procurements which fall outside the scope of the Directive due to Article 346 of TFEU could be taken to the Market Court only if the Court grants a permission to appeal. When deciding if permission to appeal is granted, the severity of the procurement entity's possibly erroneous procedure and its general significance would be balanced against both the tenderer's need for judicial relief and the security interests of the State.

The restrictions in the right to appeal aim to ensure that the procurement is not delayed in a way which would endanger Finland's ability to fully take care of its national defence and security.

In framework arrangements the right to appeal to the Market Court is restricted because the tenderers have already had a possibility to appeal when the procurement entity chose tenderers that are admitted into the framework arrangement. Therefore an unrestricted appeal to the Market Court could mean that the same matter is under appeal procedure twice.

In the procurements which, due to Article 346 of TFEU, fall outside the scope of the Directive, the Market Court could only order the procurement entity to pay compensation to the petitioner.

The Directive on defence and security procurements does not set any requirements for the legal remedies relating to procurements outside the scope of the Directive. Therefore the legal remedies in the proposed Act exceed the level required in the Directive.

The objective of restricting the possibility to appeal is to prevent appeals which are made on clearly insufficient grounds or to cause harm. If the Market Court does not grant the permission to appeal, complaint to the Supreme Administrative Court about the Market Court's refusal is also subject to appeal.



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