

## Public Procurement Legislation – When Public Entities go Shopping



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**Public procurement legislation applies to the purchase of goods and services by public entities and compliance with it is time-consuming and costly. It is therefore important to consider whether public procurement legislation applies to a specific transaction.**

The value of Swiss public procurement transactions is estimated at more than CHF 30 billion a year – an amount that indicates the significance of public procurement and therefore the importance of the rules and regulations governing it.

### The legal framework

Public procurement in Switzerland is regulated on three levels:

- International treaties, such as the World Trade Organisation Agreement on Government Procurement (GPA) and the bilateral Agreement between the European Community and the Swiss Confederation on certain Aspects of Government Procurement provide the basic framework for federal, cantonal and municipal public procurements.
- On a national level, public procurement by the Confederation (and other enterprises) is governed by the Federal Act on Public Procurement (FAPP) as well as the Ordinance on Public Procurement (OPP).
- At the cantonal and municipal level, the Intercantonal Agreement on Public Procurement, as well as the Federal Act on the Internal Market provide framework legislation for the 26 individual cantonal laws.

Public procurement law applies if the transaction meets the definition of a “public procurement” and the procuring entity and its services are within the scope of the public procurement law.

### Which entities are subject to the Federal public procurement legislation?

On a national level, the FAPP rules are applicable to the following entities:

- the Federal Administration,
- the Federal Alcohol Board,

- the Federal Institutes of Technology and their research centres,
- the Swiss Post with regard to its non-competitive postal and transport services; and
- federal enterprises in the sectors of water, energy, transport and telecommunications (so-called “sector entities”, as defined in Art. 2a OPP).

The sector entities may apply to the Federal Department of the Environment, Transport, Energy and Communications (DETEC) for an exemption from the application of the procurement rules if there is competition between them with regard to the specific sectors involved. Currently, the following sectors are exempted: railway freight transportation on standard gauge tracks and telecommunication services involving fixed-line network communication, mobile communication, internet access and data communication. Further, the sector entities are only subject to procurement rules with regard to their core functions. With competition slowly developing in the sectors, the need for procurement rules will fade.

### What is the definition of a “public procurement”?

The applicable laws and regulations do not define the term “public procurement” (*öffentliche Beschaffung*), but the courts have developed more or less precise criteria for identifying a public procurement. According to the Swiss Federal Court, the acquisition of goods or services qualifies as public procurement if the public entity otherwise subject to the FAPP rules acts as an “acquirer” of goods or services which are necessary for the fulfilment of a public task from a provider in exchange for a purchase price. It is important that the public entity acts as a “consumer”, as is the case when the public entity calls for bids for the construction of a public building or for the towing of illegally parked cars. In contrast, if the public entity acts as the provider of a service, but not as

a "consumer", then the provision of that service does not qualify as public procurement. For example, if the public entity makes public grounds available for a market stand or rents public space for billboard advertising, the provision of these services does not qualify as a public procurement because the public entity provides, rather than obtains, the service.

### **Are public procurement rules applicable to in-house awards?**

As a rule, the public procurement regime is not applicable to goods purchased or services sourced from a public entity's in-house entities. In fact, a public entity is free to buy a service from an external entity or to use its own resources to provide a service unless specific legislation provides otherwise (the so called "make-or-buy decision"). As long as the service is rendered in-house, private providers are not negatively affected: In fact, none of them receives the award. Only if an award is given to a private provider without complying with the public procurement rules is the private provider given preferential treatment compared to other potential private providers. The failure to publicly request bids deprives the remaining potential providers of the opportunity to make competing offers and violates fundamental principals of equal treatment and competition. These issues require a closer examination of the legal nature of an in-house award.

Swiss public procurement legislation does not specify when a contract is to be considered an "in-house" contract. Generally, there are two types of in-house procurement: a public entity may award the contract either directly to a department within the public entity itself (*direct internal awards*) or to a body which is legally distinct from the public entity, but which may still be considered in-house due to its close relationship with the public entity (*indirect internal awards*). It is generally accepted that direct internal awards are not subject to public procurement regulations, but the treatment of indirect internal awards is controversial. There are no decisions of Swiss courts on indirect internal awards. In the EU, the European Court of Justice (ECJ) has held that a call for tenders is not necessary if two conditions are met: first, the public entity must exercise control over the contracting entity, similar to the control which it exercises over its own departments; and second, the contracting entity must carry out the essential part of its activities with the local authority that controls it. It is likely that Swiss courts will take the ECJ's criteria into consideration if they are called to decide whether a contract is an indirect internal award. For the sector entities, specific group privileges are granted by the applica-

ble EU Directive which take precedence over the rules for in-house awards developed by the ECJ.

It also is unclear whether one or more private holdings in a contracting entity that is controlled by a public entity, such as a minority shareholding held by a private entity, always trigger the public procurement rules. The ECJ has a formal approach: It held that even a minority ownership interest by a private undertaking in the capital of a contracting entity controlled by a public entity means that the public entity no longer exercises a sufficient degree of control over the contracting entity and therefore public procurement rules would apply to the relevant award. With regard to Switzerland, it can be argued that a minor private ownership interest in the contracting entity does not mean *per se* that the award is not an in-house procurement.

### **Revision of the FAPP**

Currently, the FAPP is being revised. The preliminary draft of the FAPP dated 30 May 2008 aims at modernising, clarifying, and harmonising public procurement rules and regulations and making them more flexible. Among other amendments, the draft adopts the definition of public procurement developed by the courts and excludes, to some extent, the applicability of the FAPP to in-house awards. The consultation period for the draft of the revised FAPP ended on 15 November 2008, but it remains to be seen whether the draft bill will be submitted to parliament. Although a partial harmonisation of public procurement rules is long overdue, it is doubtful that the cantons will follow suit.

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