

Update on local authority owned companies Part 2 Teckal exemption

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The exemption in *Teckal SRL v Comune de Viano* (Case C-107/98) (**Teckal**) and codified in regulation 12 of the Public Contracts Regulations 2015 (the **PCR**) continues under the Procurement Act 2023 (the **Act**). The exemption in the Act is generally consistent with the current position under the PCR. The key change is whether or not a local authority trading company would otherwise be a contracting authority and any sub-contract under a contract awarded under the vertical arrangements (Teckal) exemption will need to comply with the Act.

Contract awards to Teckal companies

The PCR codified the Teckal exemption. The current position under regulations 12(1) and (4) of the PCR is that contracts awarded to a company (or other legal person) owned by a contracting authority (or jointly owned by one or more contracting authorities) is exempt from the PCR where:

1. the contracting authority (or contracting authorities) exercises over the company a control similar to that which it exercises over its own departments (the **Control Test**);
2. more than 80% of the activities of the company are carried out in the performance of tasks entrusted to it by the controlling contracting authority (or contracting authorities) or by other legal persons controlled by that contracting authority (the **Activities Test**); and
3. there is no direct private capital participation in the company.

The Teckal exemption in the has carried over to the Act. Contracting authorities can continue to directly award contracts to companies they wholly own because a contract is an exempted contract if it is between a contracting authority and a person controlled by one or more contracting authorities (schedule 2, paragraph 2 of the Act).

In order to make a direct award of a contract to its company, the contracting authority must, either alone or together with other contracting authorities, be a parent undertaking within the meaning of the Companies Act 2006 with no shares owned by any person that is not a public authority. The contracting authority company must:

1. pass the Activities Test ;
2. have no person other than the authority (or authorities) exerting a decisive influence on the activities of the company (a restated **Control Test**).

The Government Commercial Function Procurement Act 2023 Guidance: Contracting Authority Definition clarifies that there is no intention to capture new entities or exclude entities covered previously; the aim is a smooth transition from the previous regime.

Contract awards by Teckal companies

Under the PCR, Teckal companies that do not have an industrial or commercial character will fall within the definition of a contracting authority, i.e. bodies governed by public law which:

1. are established for the specific purpose of meeting needs in the general interest and not having an industrial or commercial character;
2. have legal personality; and

3. have any of the following characteristics:

- 3.1. financed by the State, regional or local authorities or by other bodies governed by public law;
- 3.2. subject to management supervision by those authorities or bodies; or
- 3.3. have a board, more than half of which is appointed by those authorities or bodies.

Accordingly, above-threshold procurement by Teckal companies (other than awards to their controlling authorities or another Teckal company owned by that authority) will generally need to comply with the PCR.

Under the Act, companies who were contracting authorities under the PCR will continue to be contracting authorities. A company owned by a contracting authority will itself be a contracting authority if it falls within the definition of a public authority (being a person wholly or mainly funded out of public funds or subject to public authority oversight which does not operate on a commercial basis). Section 2(4) sets out a non-exhaustive list of factors to take into account in determining whether a company (or other entity) operates on a commercial basis:

1. whether its losses would be borne or its continued operation be secured by a public authority (whether directly or indirectly);
2. whether it contracts on terms more favourable than might reasonably have been available to it without the association with the public authority; and
3. whether it operates in a market that is subject to fair and effective competition.

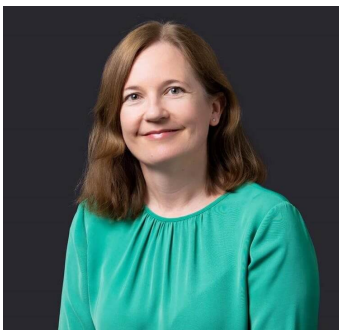
The Government Commercial Function Procurement Act 2023 Guidance: Contracting Authority Definition provides useful further guidance and suggests consideration of the intended purpose of the entity. Companies that provide a service in the public interest (such as social housing) are less likely to be operating on a commercial basis while local authority trading companies established for a commercial purpose are more likely to be operating commercially.

Under the Act, a company (or other entity) that operates on a commercial basis will not usually be a public authority (and therefore not a contracting authority). However, one key change is that where a company is awarded an exempted contract by a public authority under the vertical arrangements Teckal exemption, it will be treated as a public authority in relation to any relevant subcontract (section 2(10)). This will prevent contracting authorities from avoiding the application of the Act by awarding contracts through their commercial entity companies.

When acting as contracting authorities, companies should be mindful that procurement has been expanded to cover the entire lifecycle of a procurement being award, entry into and management of contracts.

[Read part 1](#) →

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