Directive 2009/81/EC on the award of contracts in the fields of defence and security

Guidance Note
Subcontracting

Directorate General Internal Market and Services

1) Subcontracting in defence and security procurement

1. One of the defence-specific innovations of Directive 2009/81/EC is the rules on subcontracting. Directive 2004/18/EC provides only very limited obligations with regard to subcontracting[1] and basically leaves it up to the successful tenderer to organise its supply chain. By contrast, Directive 2009/81/EC contains a detailed set of provisions laid down in Articles 21 and Title III (Articles 50-54) allowing contracting authorities in particular to require that successful tenderers subcontract a certain share of the main contract and/or put proposed subcontracts out to competition. At the same time, it sets basic rules for the fair and transparent awarding of such subcontracts.

2. This approach is built on the assumption that, in a genuine European Defence Equipment Market, competition should not be limited to the level of prime contractors. Sub-suppliers will benefit from the opening-up of national defence markets if they have a fair chance of gaining access to the supply chains of big system integrators located in other Member States. This is important economically, since it increases the prime contractor's choice of potential sub-suppliers — but also politically, since the defence industrial base of many Member States consists mainly of small and medium-sized enterprises (SMEs).

3. Hence, the Directive's provisions on subcontracting aim to inject competition into the supply chain of prime contractors. Many Member States have traditionally requested (sub)-contracting to their local defence companies as compensation for buying military equipment from suppliers abroad. Offset arrangements have thus been used to give local industries access to other defence markets via the supply chain of foreign prime contractors. This practice, however, goes against the principle of non-discrimination and the basic freedoms of the Internal Market. Consequently, the Directive does not allow this practice, but fosters market access for SMEs throughout the entire European Union via competition in the supply chain.

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[1] Article 25 and the specific obligations for subcontracting by concessionaires (Articles 60 and 62 to 65).

2) Principles

4. The subcontracting provisions of the Directive are built on the principle of non-discrimination. This means that:

- Where a contracting authority/entity requires that a successful tenderer subcontract a certain minimum share of the main contract, the subcontracts concerned must be awarded in accordance with the specific rules set out in Title III. The contracting authority may not require the successful tenderer to award subcontracts to specific subcontractors or to subcontractors of a specific nationality.
- Where a contracting authority/entity requires a successful tenderer to award specific subcontracts via competitive bidding, this competition must also be organised on a European-wide level and in a fair and transparent way.
- For all subcontracts that are not covered by one of the above-mentioned requirements, the successful tenderer remains free to select its subcontractors and '*shall in particular not be required to discriminate against potential subcontractors on grounds of nationality'* (Article 21 (1)).

5. The subcontracting provisions may be applied in all contract award procedures under Directive 2009/81/EC, including the negotiated procedure without publication of a contract notice (Article 28).

6. The provisions of Articles 21 and Title III are an exhaustive description of the possible ways in which the contracting authority/entity can oblige a successful tenderer to subcontract a certain share of the contract to third parties and/or to intervene in the way successful tenderers select their subcontractors. This results from the restrictive wording of the relevant provisions (such as, for example, Article 21 (4)) and also from the principle expressed in Article 21 (1) that *'the successful tenderer shall be free to select its subcontractors for all subcontracts that are not covered by the requirement referred to in paragraphs 3 and 4' of that Article*.

7. Furthermore, it should be noted that the subcontracting provisions refer only to subcontracts awarded to 'third parties'. According to Article 50 (2), *'groups of undertakings which have been formed to obtain the contract, or undertakings related to them, shall not be considered third parties'*. This means that contracts concluded between undertakings belonging to groups of candidates or tenderers within the meaning of Article 5 (2) are not subject to the requirements on subcontracting, in particular to the possible obligation to award subcontracts in competitive tendering. At the same time, such contracts awarded between undertakings of such groups are not eligible for fulfilling a minimal percentage of subcontracting.

8. According to Article 20, '*contracting authorities/entities may lay down special conditions relating to the performance of a contract, provided that these are compatible with Community law and are indicated in the contract documentation (contract notices,*

contract documents, descriptive documents or supporting documents). These conditions may, in particular, concern subcontracting …, in accordance with Article 21.'

Requirements on subcontracting will thus typically take the form of contract performance conditions: contracting authorities/entities will impose contractual stipulations spelling out the successful tenderer's obligations.

9. Article 21 (7) states that the subcontracting requirements *'shall be without prejudice to the question of the principal economic operator's liability'*. This does not mean, however, that the successful tenderer must always bear the sole responsibility for the execution of the contract if the subcontracting obligations are invoked. Subject to the applicable contract law, it may be appropriate to introduce in the contract a risk-sharing system between the successful tenderer and the contracting authority/entity. In a negotiated procedure or competitive dialogue, the exact content of such an arrangement could be determined through negotiations between the parties (see below, point 29).

3) Options for Member States and contracting authorities/entities

10. Article 21 provides several options for subcontracting. Whether contracting authorities can (or must) use these options depends on how Member States transpose the Directive.

No matter which option they use, contracting authorities may never require successful tenderers to discriminate against potential subcontractors on grounds of nationality (Article 21 (1)).

Option A): The successful tenderer determines how much, which parts and to whom to subcontract — the contracting authority limits itself to verifying reliability and security of the supply chain

11. The first option for the contracting authority, described in Article 21 (1) and (2), is to leave it up to the successful tenderer to determine a) which share of the main contract, b) which part(s) of the main contract and c) to whom he wants to sub-contract. The contracting authority would basically accept the tenderer's sub-contracting proposal, subject to a possible verification of its selection criteria, in accordance with Article 21 (5).

The Directive's provisions relating to this option must be transposed, but Member States can either leave it up to their contracting authorities to use them or require them to do so.

Option B): The successful tenderer determines how much and which parts to subcontract — the contracting authority decides which subcontracts to award in competition

12. The second option for the contracting authority, described in Article 21 (2) and (3), is to leave it up to the successful tenderer to determine a) which share of the main contract and b) which parts of the main contract it wants to sub-contract, but to require that it award some or all of these subcontracts in accordance with Title III. This requirement may concern all parts of the main contract the successful tenderer intends to subcontract, no matter whether the latter has already identified possible subcontractors for these parts or not.

13. In this case, the contracting authority must indicate in the contract notice that it may use this option (depending on the tender). The tenderers first state, in their tenders, their intentions for subcontracting (how much, which parts, and the proposed sub-contractors). The contracting authority then tells the tenderers which of the intended subcontracts it requires to be awarded in accordance with Title III. The successful tenderer is obliged to award the subcontracts concerned in accordance with the transparent and non-discriminatory procedures of Title III.

The Directive's provisions relating to this option must be transposed, but Member States can either leave it up to their contracting authorities to use them or require them to do so.

Option C): The contracting authority decides how much to subcontract in competition — the successful tenderer decides which parts to subcontract in competition

14. The third option for the contracting authority, described in Article 21 (4), is to require subcontracting for a certain share of the main contract. The Directive refers to this share as the 'minimal percentage' which is to be expressed *'in the form of a range of values, comprising a minimum and maximum percentage. The maximum percentage may not exceed 30 % of the value of the contract.*'

15. In this case, the contracting authority must specify the minimal percentage of the value of the main contract it wants to be subcontracted (for example 15-20 % or 25-30 %) and ask the selected tenderers to indicate in their tenders which parts of their offer they intend to subcontract to fulfil this requirement. Hence, the contracting authority determines the minimal percentage of the main contract to be subcontracted while the successful tenderer decides which parts are to be subcontracted.

All subcontracts concerned by this provision must be awarded in a transparent and non-discriminatory procedure under the rules laid down in Title III.

16. The national law transposing the Directive fixes only the upper limit of 30 %. On that basis, contracting authorities/entities will then define for each individual case the minimum and maximum percentage, depending on the specificities of the contract

concerned. The Directive points out that an excessive distortion of the supply chain should be avoided: Article 21 (4) states that the range of percentages defined '*shall be proportionate to the object and value of the contract and the nature of the industry sector involved, including the level of competition in that market and the relevant technical capabilities of the industrial base*. Recital 40 insists that '*the proper functioning of the successful tenderer's supply chain should not be jeopardised. Therefore, the percentage that can be subcontracted to third parties at the request of the contracting authority/entity should appropriately reflect the object and value of the contract*.'

17. It should also be pointed out that, under Article 21 (4), the successful tenderer is free to decide which subcontracts it wants to award in accordance with the rules set out in Title III to meet the percentage required. The contracting authority/entity can only impose the relevant percentage values; it may not require that the successful tenderer subcontract specific parts of the contract.

The Directive's provisions relating to this option do not have to be transposed. If a Member State decides to do so, then again it can either leave it up to the contracting authorities to use these provisions or it can require them to do so.

Option D): the contracting authority sets a minimum percentage to be subcontracted in competition and, in addition, imposes competition for subcontracts which the successful tenderer intends to award on top of the minimum percentage

18. The fourth option for the contracting authority would be to combine the provisions of Article 21 (3) and (4). It would thus require the successful tenderer to subcontract a minimal percentage of the main contract and then, based on the tenderer's proposal, it would require that some or all of the proposed subcontracts above the required percentage be awarded in a transparent and non-discriminatory procedure.

19. In this case, the contracting authority would specify in the contract notice the minimal percentage of the main contract it wants to be subcontracted, and it would ask the selected tenderers to specify in their tenders (1) which parts of their offer they intend to subcontract to fulfil the minimal percentage requirement, and (2) which parts of their offer they intend to subcontract beyond the required percentage. Based on the tender, the contracting authority/entity would then require that some or all of the proposed subcontracts beyond the required percentage be awarded in a transparent and non-discriminatory procedure. However, the tenderer remains free to decide which parts he wants to subcontract (to meet the minimal percentage or beyond). In any case, all subcontracts which are imposed by contracting authorities must be awarded by the successful tenderer in accordance with Title III.

Not all of the Directive's provisions related to this option have to be transposed. If a Member State decides to transpose them all, it can then again either leave it up to the contracting authorities to use them or it can require them to do so.

4) Subcontracting requirements in the contract award procedure

4.1) Contract notice

20. According to Article 21 (6), contracting authorities/entities have to indicate all their subcontracting requirements in the contract notice. This applies to each of the options described under point 3 and in all procedures involving the publication of a contract notice (restricted procedure, negotiated procedure with publication of a contract notice or competitive dialogue).[2] In view of the general principle of transparency and in the interest of practicability, it is important that the contracting authority/entity informs economic operators as comprehensively as possible on its subcontracting requirements.

21. This applies in particular to contracting authorities/entities which intend to make use of options B or D (Article 21 (3)). They should already give in the contract notice as much information as possible about the objective and non-discriminatory criteria they intend to apply for selecting those proposed subcontracts they want to be awarded under the rules set out in Title III. They could, for instance, announce that they intend to apply this requirement to all proposed subcontracts, or to certain parts of the contract (for example, specific subsystems), if the tenderer proposes to subcontract these parts. Such information might be of crucial importance for prospective candidates and tenderers.

22. Contracting authorities/entities that make use of Article 21 (4) (options C and D), have to indicate in the contract notice the minimal percentage of the contract's global value which they require to be subcontracted through a competitive procedure.

23. In all cases (options A to D), contracting authorities/entities must indicate in the contract notice

- the selection criteria regarding the personal situation of subcontractors that may lead the contracting authority/entity to reject potential subcontractors, and the required information proving that these subcontractors do not fall within the cases justifying rejection, and
- the information and documentation required for assessing the minimum economic and technical capacities of subcontractors.

According to Article 21 (5), rejection of a subcontractor may only be based on criteria applied for the selection of tenderers for the main contract.

[2] If the main contract is awarded under Article 28 by a negotiated procedure without publication of a contract notice, the contracting authority/entity may publish the subcontracting requirements in a possible (voluntary) *ex prior* information notice published under Article 30 (1) in TED or on the buyer profile of the contracting authority entity. In any case, the information has to be published in the contract award notice in accordance with Article 30 (3) and Annex IV of the Directive.

4.2) Preparation of the tender

24. If the contracting authority/entity makes use of Article 21 (2) or (3), the tenderer has to indicate in its tender

- any share of the contract it intends to subcontract to third parties,
- the subject-matter of the subcontracts it intends to award, and
- the identity of the proposed subcontractors, if these are already known.

25. In the case of Article 21 (4), the tenderer must specify in the tender

- which part or parts of its offer it intends to subcontract to fulfil the minimal percentage requirement, and
- if the tenderer intends to subcontract beyond the minimal percentage:
  - the subject-matter of the subcontracts beyond the minimal percentage and
  - the identity of the proposed subcontractors, if these are already known.

26. In all cases, the tender must contain the information and documentation needed to assess the required capacities of proposed subcontractors.

The Directive contains specific provisions concerning requirements on security of information. Under Article 22 (c) and (d), contracting authorities/entities may require that the tender contain *'sufficient information on subcontractors already identified to enable the contracting authority/entity to determine that each of them possesses the capabilities required to appropriately safeguard the confidentiality of the classified information to which they have access or which they are required to produce when carrying out their subcontracting activities'* as well as a commitment from the tenderer to provide the same information in due course with respect to any new subcontractor. In practice, this information will normally consist of statements of the proposed subcontractors that they hold the relevant security clearances (statements to be verified by the contracting authorities/entities at the competent National Security Authorities).

Finally, the tenderers belonging to a group of undertakings formed to obtain the contract have to include in the tender an exhaustive list of the members of the group and their related undertakings (Article 50 (2)).

4.3) Examination of the tender

27. In examining the tenders, the contracting authority/entity will first verify whether they comply with the requirements set out in the contract documentation, in particular whether they contain all required information and documentation. This includes the particulars regarding subcontracting. In this respect, the contracting authority will check whether the tenderer has provided the information required under Article 21 (2) and, in case of options C and D, whether the tender contains all relevant details on how the tenderer will meet the minimal percentage. If these basic conditions are fulfilled, the further steps depend on which option the contracting authority/entity has chosen.

28. In option A, the contracting authoring/entity leaves it basically to the tenderer to choose its subcontractors. A possible intervention is limited to the rejection of individual subcontractors under Article 21 (5). The contracting authority/entity can therefore immediately go ahead and check the suitability of proposed subcontractors. Article 21 (5) points out that this verification may only be based on criteria used for the qualitative selection of the tenderers for the main contract. If the contracting authority/entity rejects a proposed subcontractor, it must send the tenderer a written justification, setting out why it considers that the subcontractor does not meet the criteria (see below, point 4.4.6).

29. In options B and D, the contracting authority/entity reserves to itself the right to oblige the successful tenderer to award proposed subcontracts through the procedures described in Title III. This obligation may apply to all subcontracts or only to specific subcontracts chosen by the contracting authority/entity. If the contracting authority/entity has not announced from the outset that it will require the application of Title III for all subcontracts proposed by the tenderers, it must, during the contract award procedure, tell the tenderers which subcontracts will in fact be subject to these rules.

30. Although the Directive contains no formal limitation in this respect, the contracting authority/entity should nevertheless be aware that its decision must comply with the principle of equal treatment of tenderers (Article 4). This means that the relevant subcontracts could be designated on a case-by-case basis, but not in an arbitrary manner. The contracting authority/entity should therefore determine an objective, non-discriminatory approach and provide as much information as possible on the criteria for its decision. In particular, the decision of the contracting authority/entity cannot be based on the nationality of the tenderer's initial choice of subcontractors.

31. Furthermore, in view of its practical and economical implications for the tenderer, the subcontracts to be awarded in competition should be designated as early as possible in the contract award procedure. Consequently, in a restricted procedure, the contracting authority/entity should communicate its decision immediately after examining the tenders. The designation of subcontracts to be awarded under the rules set out in Title III will then be binding upon the tenderer. In a negotiated procedure or competitive dialogue the situation is slightly different. According to recital 40, '*the contracting authority/entity and the tenderers may discuss subcontracting requirements or recommendations with a view to ensuring that the contracting authority/entity is fully informed on the impact of different subcontracting options on, in particular, cost, quality or risk*'. In these procedures, the exact content of subcontracting obligations is therefore determined at a later stage, following negotiations between the parties.

32. In option C, it is for the tenderer to specify which subcontracts it wants to award following the rules laid down in Title III to meet the minimal percentage imposed by the contracting authority/entity. All the contracting authority can do, therefore, is require the application of Title III to any subcontracts that the tenderer wants to award beyond the minimal percentage.

4.4) Rules to be applied by the successful tenderer after the award of the main contract

4.4.1) Principles

33. Once the contract has been concluded, the successful tenderer has an obligation to apply the rules set out Title III for the award of subcontracts covered by the subcontracting requirements imposed by the contracting authority/entity. Although the wording of the Directive suggests that the subcontracting is done by the successful tenderer after the award of the main contract, it would also be possible for a tenderer to select its subcontractors earlier, i.e. already during the preparation of the tender, using the procedures provided Title III. Such subcontracts would then be concluded under the condition that the tenderer is awarded the main contract. Alternatively, the successful tenderer might also fulfil the subcontracting requirement by awarding subcontracts on the basis of a framework agreement concluded in accordance with Title III (see below, point 4.4.3).

The rules set out in Title III are limited to an obligation to publish a EU-wide subcontract notice and to respect certain basic principles for awarding the subcontracts. They allow great flexibility in the conduct of the procedure.

Recital 40 points out that subcontractors initially proposed by the successful tenderer are free to participate in the competitive procedures organised under Title III.

4.4.2) Subcontract notice

34. For the award of subcontracts with a value above the threshold for applying the Directive (Article 8), successful tenderers have to publish in TED[3] a subcontract notice which must contain basic information on the subcontract to be awarded. The exact content of the notice is listed in Annex V of the Directive. The notice has to be drawn up using a standard form.

As is pointed out in Article 53, the subcontract notice must in particular contain *'the criteria for qualitative selection prescribed by the contracting authority/entity entity, as well as any other criteria [the successful tenderer] will apply for the qualitative selection of subcontractors.'*

35. According to Article 52 (4), a subcontract notice is not required when a subcontract meets the conditions justifying the use of the negotiated procedure without publication of a contract notice (Article 28). In such a case, even a contracting authority/entity would be entitled to award a contract without advertising; the same must apply to a successful tenderer.

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[3] Tenders Electronic Daily, the online version of the 'Supplement to the Official Journal of the European Union', http://ted.europa.eu.

36. For subcontracts below the threshold for applying the Directive, there is no obligation to publish a subcontract notice. Article 52 (7) provides, however, that, for such contracts, successful tenders have to apply the principles of the Treaty regarding transparency and competition. According to ECJ case-law, this may imply an obligation to ensure an adequate degree of publication if the subcontract in question might be of interest for economic operators from other Member States.[4]

4.4.3) Framework agreements

37. Article 52 (6) gives Member States the option of allowing the successful tenderer to fulfil subcontracting requirements by awarding subcontracts on the basis of a framework agreement concluded in accordance with the rules set out in Title III. Such subcontracts are deemed to have been awarded in a competitive procedure under Title III; they are therefore eligible for fulfilling any subcontracting requirements imposed by the contracting authority/entity.

The duration of the framework agreement is basically limited to seven years. The last subparagraph of Article 52 (6) also warns that *'framework agreements may not be used improperly or in such a way as to prevent, restrict or distort competition'*.

Framework agreements allow undertakings in the defence and security sector to constitute a supply chain of subcontractors selected in a transparent and non-discriminatory manner. At the same time, they give sub-suppliers — in particular SMEs — an opportunity to build up cross-border business relationships and to become part of the supply chain of big system integrators from other Member States. They can therefore be an important instrument for opening up established supply chains.

4.4.4) Exception clause

38. According to Article 53, *'the successful tenderer shall not be required to subcontract if it proves to the satisfaction of the contracting authority/entity that none of the subcontractors participating in the competition or their proposed bids meet the criteria indicated in the subcontract notice and thereby would prevent the successful tenderer from fulfilling the requirements set out in the main contract'*.

This concerns, in particular, cases where none of the participating undertakings would meet the selection criteria prescribed by the contracting authority/entity, or where none of the submitted bids would comply with mandatory requirements in the main contract, such as security of supply requirements. If the successful tenderer has provided the contracting authority/entity with the appropriate evidence, he is relieved of the obligation to subcontract and can decide freely whether to supply the required elements by his own means or to conclude a subcontract without observing the rules set out in Title III.

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[4] See judgment of 15 May 2008 in Cases C-147/06 and C-148/06 SECAP, paragraphs 18 to 35; Commission Interpretative Communication on the Community law applicable to contract awards not or not fully subject to the provisions of the Public Procurement Directives, OJ 2006, C 179, p. 2; judgment of 20. May 2010 in Case T-258/06 Germany v Commission, paragraphs 68-100.

4.4.5) Principles for the award of subcontracts

39. '*Where successful tenderers are contracting authorities/entities, they shall comply with the provisions on main contracts laid down in Titles I and II of the Directive when they award subcontracts*' (Article 54). All other successful tenderers must apply only a limited set of rules to the award of subcontracts. Article 51 provides only that *'the successful tenderer shall act transparently and treat all potential subcontractors in an equal and non-discriminatory way'*.

However, Article 53 (1) refers to criteria which the successful tenderer will use for the qualitative selection of subcontractors. Such criteria might be prescribed by the contracting authority/entity or chosen by the successful tenderer. In both cases, they must be *'objective, non-discriminatory and consistent with the criteria applied by the contracting authority/entity* [in accordance with Articles 39 to 42] *for the selection of the tenderers for the main contract. The capabilities required must be directly related to the subject of the subcontract, and the levels of ability required must be commensurate with it'*.

The existence of a specific rule for qualitative selection implies that the procedure used by the successful tenderer must provide for a separate assessment of the suitability and the capability of potential subcontractors. In that assessment, the successful tenderer must at least apply the selection criteria prescribed by the contracting authority/entity.

Apart from these requirements, it is left to the successful tenderer to define the award criteria and to organise the procedure for awarding the subcontracts. There is, in particular, no obligation to apply the formal procedures provided by the Directive for contracting authorities/entities.

4.4.6) Rejection of subcontractors

40. Finally, once the successful tenderer has selected the subcontractors using the procedures laid down in Title III, the contracting authority/entity will verify the suitability of the selected subcontractors under Article 21 (5). This verification may only be based on criteria used for the qualitative selection of the tenderers for the main contract. In practice, the selection criteria used to reject subcontractors will be a subset of the selection criteria used in the award of the main contract since not all of the original selection criteria may be relevant for a particular proposed subcontractor or its activity.

If the contracting authority/entity rejects a proposed subcontractor, it should communicate its decision to the successful tenderer as soon as possible. It must produce a written justification, setting out why it considers that the subcontractor does not meet the criteria, subject to the application of Article 35 (3).

4.4.7) Remedies

41. Article 55 (1) states that the review procedures provided in Articles 55 to 64 apply only to *'contracts referred to in Article 2'*, i.e. the main works, service or supply contracts concluded between the contracting authority/entity and the successful tenderer. Consequently, a firm that takes part, or would be interested in taking part, in a competition for a subcontract organised by the successful tenderer under Title III cannot launch a review procedure against the successful tenderer.

If the successful tenderer fails to comply with his obligations in respect of subcontracting, he will be in breach of contract towards the contracting authority/entity. Subject to the applicable contract law, the contracting authority/entity might therefore use remedies such as damages or cancellation of the contract against the successful bidder. Under certain conditions, such instruments might also be available to firms which took part, or were interested in taking part, in the relevant competition.

42. By contrast, a tenderer may launch a review procedure under Articles 55 to 64 against the contracting authority/entity for an alleged infringement of the subcontracting rules when awarding the main contract. This might happen, for instance, in cases where a tenderer considers that the subcontracting requirements set by the contracting authority/entity go beyond what is admissible under Article 21 or where a successful tenderer wants to challenge the rejection of a subcontractor by the contracting authority/entity.

This guidance note reflects the views of the services of DG MARKT and is legally not binding. Only the Court of Justice is competent to give a legally binding interpretation of EU law.