

Navigating Subsidy Control: Unveiling the Risks for Teckal Companies under the UK Subsidy Control Act 2022

On 4 January 2023, the new domestic subsidy control regime came into force. Established by the Subsidy Control Act 2022 (“**SCA**”), the regime has introduced a new era of regulation impacting various aspects of public funding and subsidy control for the UK. The Government has described the new regime as a radical departure from the EU State Aid rules.

After more than 12 months of operation, the regime has lived up to the Government’s expectations. New risks and new opportunities for public authorities and for recipients of public funding have become clear. One particular area that now requires careful consideration is how local government and their use of ‘Teckal’ companies are affected. A Teckal company is a specific type of entity used by public authorities to deliver local services that may alleviate procurement issues but, at the same time, may give rise to subsidy control concerns under the new SCA regime.

Understanding Teckal Companies

Teckal companies derive their name from the landmark case of *Teckal SRL v Comune de Viano* (Case C-107/98). That case found that public procurement rules will not apply to the letting of a contract to an entity which is subject to the direct control of a local authority – i.e. where the local authority’s control over the entity is similar to the control that it exercises over its own departments.

The use of the Teckal exemption is complex and subject to challenge, given that it takes contract awards outside the controls imposed by the public procurement regime. As such, local government must be careful to ensure that these companies are within the Teckal parameters.

For instance, the local authority must control all the shares in the company and exercise effective day-to-day control over its affairs in other words, the same as the relationship between the council and one of its internal directorates. As for the company, it must be “*inwardly and not outwardly focused*”. This means that at least 80% of the activity of the Teckal company – that is, over 80% of its turnover – must be for its public sector owners.

As a result, a Teckal company is a company which benefits from contracts for works, services or supply from its controlling contracting authority without having to go through a competitive tender process. In essence, the nature of its power and function derives from a public authority, for or on behalf of that public authority. There is also a heightened level of transparency and accountability to the public sector owners.

The SCA: New Regime, New Challenges

Following the end of the transition period for the UK’s departure from the EU on 31 December 2020, the Procurement Act 2023 lays down a wholly domestic procurement regime distinct from EU law. The Act nonetheless continues the precedent set by Teckal and it exempts contracts “*between a contracting authority and a person that is controlled by... the contracting authority*”.

The SCA, replacing the EU State Aid rules, introduces a new UK subsidy control regime which enables UK public authorities, including devolved administrations and local authorities, to give subsidies that are tailored to their local needs and that drive economic growth, while minimising distortion to UK competition and protecting our international obligations. There are, however, important processes that public authorities must undertake to assess the compatibility of subsidies with these rules. Understanding the detail and implications of the SCA is crucial - getting it wrong could lead to legal challenges, and potential disruptions to public funding allocations.

Importantly, the changes made by the SCA have direct consequences for Teckal companies, caused by the intersection of the criteria Teckal companies must meet to benefit from the public procurement exemption, and the application of the SCA regime. In particular, the exceptional treatment of Teckal companies from a procurement perspective is justified by the closeness of the links they have with their public authority partners that use the Teckal companies as a means to discharge certain statutory duties. However, that could also mean that for SCA purposes, the Teckal company is a

public authority – and its grants of financial assistance must therefore be subject to the same scrutiny and treatment as subsidies granted directly by the public authority itself.

As such, whilst using a Teckal company may alleviate public procurement challenges, under the SCA there will be an increased need for scrutiny of their commercial arrangements and whether they have been entered into on an arm's length basis. The Teckal companies will need to be able to demonstrate that they are complying with the SCA and that any potential arrangement is lawful for subsidy control purposes. Particular risks might arise if Teckal companies are asked to provide a parent guarantee to a subsidy or to provide other forms of support on better terms than those available at arms-length on the open market.

Public bodies need to be aware of the implications of the SCA for their Teckal company arrangements. This may necessitate a proactive assessment of their commercial relationships and funding arrangements to identify any corrective measures required to ensure compliance.

Through our tried and tested methodologies and subject matter expertise, KPMG's Regulatory Law team, working alongside public law specialists in our market-leading KPMG Law Disputes team, can support public authorities and Teckal companies in navigating these requirements.