



# Grants and contracts

Guidance for third sector organisations and public authorities

Written by Geldards LLP

**Geldards**  
law firm

Funded by



**Wales Council for Voluntary Action**

Head office: WCVA, Baltic House,  
Mount Stuart Square, Cardiff CF10 5FH

Helpdesk: 0800 2888 329

Fax: 029 2043 1701

Minicom: 0808 180 4080

Email: [help@wcva.org.uk](mailto:help@wcva.org.uk)

Website: [www.wcva.org.uk](http://www.wcva.org.uk)

Registered charity 218093

Company Limited by Guarantee 425299

**Swansea Council for Voluntary Services**

SCVS, Voluntary Action Centre, 7 Walter Road,  
Swansea SA1 5NF

Telephone: 01792 544 000

Fax: 01792 544 037

Email: [scvs@scvs.org.uk](mailto:scvs@scvs.org.uk)

Website: [www.scvs.org.uk](http://www.scvs.org.uk)

Registered charity 1063242

Company Limited by Guarantee 3346236

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# Purpose

This document is intended to be a general guide to the commissioning by public bodies in Wales of social care services from the third sector. It is not meant to be a comprehensive guide, to replace legal or professional advice or to constitute legal advice applicable to any particular situation. This is particularly important in the context of both the Public Procurement rules and the State Aid rules where a careful analysis should be undertaken each time with reference to the relevant legislation.

# Audience

This document is aimed at social care commissioners and local authority procurement teams in Wales, third sector providers and infrastructure organisations and Welsh Government ministers and officials.

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# Commissioning of services by public bodies and the procurement of services from the third sector

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The public sector funds the third sector through a mixture of grants and contracts although there has been a noticeable shift from grants to contracts in funding of the third sector, in part due to a recognition from Government of the role of the third sector in delivering public services.

‘In these tight economic times it is particularly important that maximum value in public spending is achieved.’<sup>1</sup>

The financial pressures faced by the public sector combined with increasing demand for public services present both significant opportunities and challenges for the third sector. The UK government’s take on public service delivery in the current economic climate is that more public services, including social services will be outsourced.’<sup>2</sup> By comparison, the Welsh Government’s perspective appears to be more balanced:

‘Realistically social care markets will continue to combine a balance of services which may be delivered internally by the local authority or secured externally through grants or via a

procurement exercise. Local authorities should consider the potential benefits and risks of the options available and have a clear decision-making process for deciding when to use the different approaches.’<sup>3</sup>

This section of the guidance looks at the external delivery of social care services by third sector organisations, the funding of such delivery through grants or contracts and aims to clear up the confusion between grants and contracts that still appears to exist within both the public sector and the third sector.

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<sup>1</sup> Procurement Policy Note-The Public Services (Social Value) Act 2012- advice for commissioners and procurers Information Note 10/12 20 December 2012 page 2 paragraph 8. Whilst the Act in question has only limited application to Wales, the need to maximise the value obtained from public spending is as relevant to Wales as it is to the rest of the UK and indeed elsewhere in Europe.

<sup>2</sup> ‘the landscape for public service delivery in this country is changing fast. In the future ever more of our public services will be delivered not by the public sector itself but from outside, whether by employee-led mutual, joint ventures, social or charitable enterprises or conventional commercial providers. It’s a new era – and anyone in the public sector

thinking that this won’t affect their organisation very much can think again...Every part of the public sector is facing up to the challenge of reduced budgets – but at the same time demand for services is relentless and public expectations for services are rising. There is a huge pressure to do more for less’. *Speech at the Commissioning Academy launch on 31 January 2013 by Cabinet Minister Francis Maude*

<sup>3</sup> Welsh Government *Fulfilled Lives, Supportive Communities, Commissioning Framework Guidance and Good Practice; August 2012 p 15*

# 1. Terminology

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## 1.1 Commissioning

Increasingly in the field of delivery of social care services the emphasis is on commissioning and, in particular, good commissioning:

‘The public sector, including Welsh Government itself, has a collective responsibility to ensure that we use public money wisely, for the benefit of the people of Wales and a duty to ensure the right skills and resources are in place’.<sup>4</sup>

‘This country needs more than ever effective commissioners able to deliver better outcomes for citizens and better value for money on ever tighter resources. Commissioners that will embrace new and innovative forms of delivery and build public services that better reflect the needs of their user.’<sup>5</sup>

The Oxford Dictionary definition of the verb ‘to commission’ is simply to authorise the production of something but when used in the context of the delivery of social care services, commissioning tends to be used to describe the whole cycle from investigation of the services required, to design/specification of the services to be procured, the procurement of those services including the management/monitoring of the provision of those services.

‘Social care commissioning’ is a set of activities by which local authorities and partners ensure that services are planned and organised to best meet the social care outcomes required by their citizens. It involves understanding the population need, best practice and local resources and using these to plan, implement and review changes to services. It requires a whole system perspective and applies to services provided by local

authorities, as well as public, private and third sector services.<sup>6</sup>

## 1.2 Procurement

The Oxford Dictionary definition of the verb ‘to procure’ is simply to obtain.

‘Social care procurement’ is a set of activities by which local authorities secure best value services to meet the social care outcomes required by their citizens. It is one part of the commissioning process, and involves specifying requirements, securing services from the best providers and monitoring service effectiveness.<sup>7</sup>

So, within the context of social care services, procurement is one part of the commissioning cycle and the delivery of services could be achieved in one of two ways:

- (a) internally by the public body (whether alone or in collaboration with other public bodies); or
- (b) externally by private or third sector organisations through procurement or grant funding

‘Procurement is governed by legislation, policy and principles at EU and UK level and by internal regulations within statutory commissioning bodies themselves.’<sup>8</sup>

This section of the guidance looks at the external delivery of social care services by third sector organisations. All public sector procurement must adhere to the EU rules on public procurement and State aid, government policy, public and administrative law and be based on value for money.

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<sup>4</sup> Maximising the Impact of Welsh Procurement Policy – Wales Procurement Policy Statement, Annex 1, page 2, Jane Hutt AM, 6 December 2012

<sup>5</sup> *speech at the Commissioning Academy launch on 31 Jan 2013 Cabinet Office minister Francis Maude*

<sup>6</sup> Welsh Government *Fulfilled Lives, Supportive Communities Commissioning Framework Guidance and Good Practice pp 27*

<sup>7</sup> Welsh Government *Fulfilled Lives, Supportive Communities Commissioning Framework Guidance and Good Practice pp 27*

<sup>8</sup> Procurement Law and Principles (Public Services): [www.ncvo-vol.org.uk/commissioning/procurement/legal\\_framework](http://www.ncvo-vol.org.uk/commissioning/procurement/legal_framework)

## 2. Grants and contracts

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The third sector has a long and rich history of delivering public services.

‘The third sector has long played an important role in providing public services, identifying needs, campaigning for change and developing dynamic, innovative solutions’.<sup>9</sup>

‘Over recent years third sector organisations have become increasingly involved in the delivery of a wide range of public services. third sector organisations work in many areas, from health and social care, advocacy and campaigning, education and learning, housing, employment and welfare, to community support and safety.’<sup>10</sup>

‘The Welsh Assembly Government (WAG) recognises the critical role the third sector plays in sustaining a just, inclusive and responsible society, including their role as service providers to the public sector.’<sup>11</sup>

### 2.1 The options for funding

The options available to public bodies to fund the delivery by third sector organisations of social care services are:

- (a) grants;
- (b) contracts; or
- (c) a mixture of grants and contracts.

### 2.2 Grants and contracts: what is the difference?

#### (a) Grants

‘Grants are very important in Wales: specific grant funding is used more heavily in Wales than in any other part of the UK.

The Welsh Government and other statutory funders use grants as a powerful lever for achieving their policy objectives. They enable local government and the voluntary sector to provide specific services to Welsh people. Grants both initiate and sustain significant economic and social activity and also represent significant investments of time and taxpayers’ money.’<sup>12</sup>

So, grants are important but what are they?

According to the Welsh Government:

‘Grants are forms of financial assistance, which encourage organisations to undertake social care activities that would not normally be undertaken by the statutory sector or arranged through the case/care management process.’<sup>13</sup>; and

Grants are ‘funding that can be provided by the [Welsh Government] and other public bodies as a means of offering financial support to third sector organisations to enable them to undertake activities the [Welsh Government] and other public bodies wish to support. Grants may be aimed at assisting with the core costs of running and developing an organisation or more specifically to help it carry out a particular project or services. The grant giver is not contracting for a service that forms part of its own business.’<sup>14</sup>

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<sup>9</sup> ‘The Third Dimension’ A Strategic Plan for the Voluntary Sector January 2008, page 34, paragraph 4.47

<sup>10</sup> Improving financial relationships with the third sector: Guidance to funders and purchasers May 2006, page 13, section 2.1

<sup>11</sup> Procurement and the Third Sector: Guidance for the Public Sector in Wales, page 4, section 2

<sup>12</sup> <http://wales.gov.uk/funding/fundgrantareas/?lang=en>

<sup>13</sup> Welsh Government Fulfilled Lives, Supportive Communities, Commissioning Framework Guidance and Good Practice: August 2012

<sup>14</sup> Code of Practice for Funding the Third Sector January 2009, page 6.

## 2. Grants and contracts (continued)

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According to the National Audit Office (NAO), 'Grant is an extremely useful way for a public body to fund a TSO for activity that is in line with one or more of the public body's objectives. For example, a council that is concerned about the poor wellbeing of one of the communities in its area may give a grant to a TSO that is dedicated to raising the wellbeing of that community.'<sup>15</sup>

According to HM Treasury, 'A grant is a financial transfer used to fund an activity because that activity is in broad alignment with the funder's objectives.'<sup>16</sup>

According to the European Commission, grants are direct financial contributions awarded as donations to third parties engaged in certain activities or projects that the EU wishes to support and are based on the reimbursement of eligible costs.<sup>17</sup>

From a legal perspective, in its most simple and basic form, a grant is a financial payment given by the funding body to the recipient to support the recipient either generally or in connection with specific activities that the recipient undertakes. The recipient is under no legal obligation to do or to deliver anything. This does not, however, mean that the recipient is free to do what it likes with any grant monies received: the recipient of a grant may only use the grant monies received for the specific purposes for which they have been made available. The funding body receives nothing in return and is under no legal obligation to provide the grant monies.

### (b) Contracts

The Welsh Government draws a distinction between grants and procurements rather than between grants and contracts: 'Procurement is the acquisition of goods and services from third party suppliers under legally binding contractual terms, where all the conditions necessary to form a legally binding contract have been met. Such contracts benefit the contracting authority and are necessary for the running of its business or its statutory duty.'<sup>18</sup>

Such a distinction also appears in HM Treasury's guidance: 'Procurement is the acquisition of goods and services in line with the Government's policy of value for money, normally achieved through competition.'<sup>19</sup>

As discussed at paragraphs 1.2 and 2.1 above, procurement is the activity of securing the delivery of social care services which, in the case of delivery by third sector organisations, could be funded by grant or contract.

From a legal perspective, a contract is a legally binding arrangement under which the services provider receives a payment from the funding body in return for the supply by the services provider of the services.

In the context of social care services contracts, this basically means two sided arrangements under which a public body makes payments to an organisation in return for the provision by that organisation of specified social care services. Both parties get something out of the arrangement: the public body gets the services that it wants provided, and the organisation gets paid for the provision of the services.

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<sup>15</sup> [www.nao.org.uk/sectors/third\\_sector/successful\\_commissioning/successful\\_commissioning/sourcing\\_providers/when\\_can\\_i\\_use\\_grant.aspx](http://www.nao.org.uk/sectors/third_sector/successful_commissioning/successful_commissioning/sourcing_providers/when_can_i_use_grant.aspx)

<sup>16</sup> Improving financial relationships with the third sector: Guidance to funders and purchaser May 2006, page 15, paragraph 2.11

<sup>17</sup> <http://ec.europa.eu/europeaid/work/funding>

<sup>18</sup> Code of Practice for Funding and the Third Sector January 2009, page 6

<sup>19</sup> Improving financial relationships with the third sector: Guidance to funders and purchasers May 2006, page 15, paragraph 2.11

## 2. Grants and contracts (continued)

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### 2.3 Grants and contracts: why the confusion?

According to the European Commission, 'The difference between a public contract and a grant is clear:

- in the case of a contract, the contracting authority receives the product or service that it needs in return for payment.
- in the case of a grant, it makes a contribution either to a project carried out by an external organisation or directly to that organisation because its activities contribute to EU policy aims.'<sup>20</sup>

Notwithstanding the European Commission's view and various guidance documents that have been issued on the subject of grants and contracts, there remains confusion amongst both the public sector and the third sector.

So why is there such confusion?

Perhaps the principal reason for the confusion is because, in practice, very few grants are true grants in the strict legal sense. Most grants are subject to terms and conditions detailing how the grant monies can be used and providing for grant monies to be repaid in certain circumstances. These terms and conditions are intended to be legally binding.

It is not, therefore, always clear at first sight whether the chosen funding mechanism is, in fact, a grant or a contract. From a legal perspective it is the substance rather than the form of, or the name applied to, a document that is important in deciding what type of

arrangement is involved. In order, therefore, to determine whether a particular arrangement is a grant or a contract, an analysis needs to be carried out to see whether the requirements for a legally binding contract are met. For a legally binding contract to arise under the laws of England and Wales, there are 5 requirements that must be met:

1. one party must make an offer
2. which is unequivocally accepted by the other party
3. which is clear with regard to the terms of what is to be provided or done
4. consideration (money or money's worth) passes between the parties and
5. the parties intend to be legally bound by the terms agreed.

### 2.4 Why is it important to understand the difference between grants and contracts?

It is important to understand whether funding is by grant or by contract as there are important differences between the two:

- (a) the legal rules and principles that apply to true grants are different to those that apply to contracts:
  - (i) true grants are subject to trust law: the recipient of a grant holds the sum of money on trust, to be used for the specified purpose for which the payment was made. Under a grant, the recipient is not obliged

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<sup>20</sup> <http://ec.europa.eu/europeaid/work/funding>

## 2. Grants and contracts (continued)

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to deliver any goods or services although the funding body may claw back a grant which has not been spent or has been misapplied as all of the grant monies must be used for the purpose specified. In the case of a true grant, the funding body receives nothing in return and, unless the grant agreement is a deed, is under no obligation to pay the grant;

- (ii) contracts are subject to contract law: under a contract the public body is legally obliged to pay the monies due under the contract and the third sector organisation is legally obliged to provide the services, the subject of the contract. If either party fails to perform their part of the bargain, the other party will have a claim for breach of contract and will be entitled to recover damages for loss suffered, such damages may exceed the amount of any monies received by the third sector organisation from the public body.

(b) the tax treatment of grants and contracts is very different;

- (c) different legislative frameworks may apply: the Public Procurement Rules apply to public services contracts but not to true grants: 'Member States and/or public authorities remain free to provide [social services] themselves or to organise social services in a way that does not entail the conclusion of public contracts, for example, through the mere financing of such services...'<sup>21</sup>; the State aid rules may apply to grants but have only limited application to public services contracts: where public services contracts have been competitively tendered (whether in accordance with the Public Procurement Rules or otherwise) and the public body is paying a competitive market price for the services in question, there will be no element of subsidy and, therefore, no State aid.

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<sup>21</sup> Proposal for a Directive of the European Parliament and of the Council on public procurement 16725/1/12 REV1 30 November 2012, recital 11

## 2. Grants and contracts (continued)

### Recognising the difference between grants and contracts: things to look for

In deciding whether an arrangement is a true grant consideration needs to be given to the following factors:

Grants:	Contracts:
<ul style="list-style-type: none"><li>• The arrangement will comprise a financial payment to support the recipient either generally or in respect of certain specific activities undertaken by the recipient.</li></ul>	<ul style="list-style-type: none"><li>• The arrangement will create a legally binding contract (see further paragraph 2.3 above).</li></ul>
<ul style="list-style-type: none"><li>• The recipient will be under no legal obligation to deliver any services.</li></ul>	<ul style="list-style-type: none"><li>• The recipient will be legally obliged to deliver the specified services.</li></ul>
<ul style="list-style-type: none"><li>• The funding body will be under no legal obligation to provide the grant monies to the recipient.</li></ul>	<ul style="list-style-type: none"><li>• The funding body will be legally obliged to pay the recipient for the provision of the services.</li></ul>
<ul style="list-style-type: none"><li>• The recipient will only be permitted to use the grant monies for the specific purposes for which they are made available. The funding body will typically have a right to clawback the monies if not used or if misused.</li></ul>	

Note: just because an arrangement is called a 'grant' or a 'grant agreement', it doesn't mean the arrangement is a true grant in the strict legal sense. Many arrangements which are called 'grants' or 'grant agreements' will in fact satisfy the requirements of a contract.

# 3. The Public procurement rules

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## 3.1 What are the Public procurement rules?

The Public Procurement Rules are made up of EC Directives, the UK Regulations that implement these Directives and case law of both the UK and the European Court. For the public sector, the relevant Directive is Directive 2004/18/EC (the ‘**Directive**’) and the relevant Regulations are the Public Contracts Regulations 2006 (the ‘**Regulations**’).

Public bodies in Wales, like public bodies in the rest of the EU, are subject to the Public Procurement Rules. In addition, public bodies are subject to the principles of the Treaty on the Functioning of the European Union (the ‘**Treaty**’), and, in particular the free movement of goods, freedom of establishment and the freedom to provide services as well as the general principles deriving therefrom, namely, the principles of transparency, non-discrimination, equality of treatment, proportionality and mutual recognition (the ‘**general Treaty principles**’).

## 3.2 When do the Public procurement rules apply?

In very simple terms, the Public Procurement Rules will apply whenever a public body seeks to award a public contract, the value of which exceeds the relevant threshold value for that type of contract<sup>22</sup> and which is not expressly excluded from the operation of the Public Procurement Rules.

In this context it is important to understand that the Public Procurement Rules ‘are not intended to cover all forms of disbursement of public money,

but only those aimed at the acquisition of works, supplies or services for consideration by means of a public contract. The notion of acquisition should be understood broadly in the sense of obtaining the benefits of the works, supplies or services in question, not necessarily requiring a transfer of ownership to the contracting authorities. Furthermore, the mere financing, in particular through grants, of an activity, which is frequently linked to the obligation to reimburse the amounts received where they are not used for the purposes intended, does not usually fall under the public procurement rules.’<sup>23</sup>

Public contracts are public works, public supply or public services contracts. Public services contracts are defined in the Regulations as contracts ‘in writing, for consideration (whatever the nature of the consideration) under which a contracting authority engages a person to provide services’<sup>24</sup> but does not include a public works or public supply contract.

As can be seen from this definition, the first requirement is that the contract be in writing. This does not mean that the contract must be in the form of a signed contract or agreement; it will be sufficient if the contract is evidenced in some way in writing, for example, an exchange of emails or letters. Public bodies are extremely unlikely to enter into oral contracts which are not evidenced in writing in some way, not least because of audit requirements. The second requirement is that of consideration. Consideration may be but does not have to be money. The third requirement is the provision of services.

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<sup>22</sup> The current threshold value for services is £113,057 where the public body is a part of central government and £173,934 for all other public bodies

<sup>23</sup> proposal for a Directive of the European Parliament and of the Council on public procurement: 16725/1/12 REV1 30 November 2012, recital 3

<sup>24</sup> Regulation 2(1) of the Regulations

## 3. The Public procurement rules (continued)

When dealing with contracts for public services, it is important to note that the Public Procurement Rules currently draw a distinction between those services called Part A services to which the Regulations and Directive apply in their entirety and those called Part B services to which only certain limited provisions of the Regulations and Directive apply<sup>25</sup>. This means that there is no obligation under the Directive and the Regulations to tender competitively contracts for Part B services through the Official Journal of the European Union (OJEU) although where such services have a cross border interest, compliance with the general Treaty principles will require some form of advertising and competitive tendering to be undertaken.

This current distinction between Part A and Part B Services is extremely important in the context of third sector delivery of social care services. Social care services are Part B services and, accordingly, contracts for such services will fall outside the full application of the Public Procurement Rules. In addition, the majority of such contracts are likely to be well below the threshold value for services and likely to have no cross-border interest. The practical effect of this is that the majority of social care delivery service contracts awarded to third sector organisations will not be subject to the Public Procurement Rules. This position may, of course, change if some of the concerns voiced within the third sector come into effect:

‘We all know the public sector is under pressure to be more efficient. Inevitably they are looking to their procurement to make efficiency savings by:

- Making the actual process of procurement more efficient, for example, by writing fewer and larger contracts ...<sup>26</sup>

Of course, it is important to remember in this context that the obligation on public bodies to secure best value and their own internal financial regulations and standing orders may require some form of competitive tendering for such contracts, although such tendering processes (where required) will typically be much simpler and more straightforward than any competitive tendering processes under the Public Procurement Rules.

### 3.3 What does the application of the Public procurement rules mean in practice?

If the Public Procurement Rules apply the public contract must be competitively tendered through the OJEU using either the open or restricted procedures or, in certain limited circumstances, the negotiated or competitive dialogue procedures. In summary, where the Public Procurement Rules apply, they create a framework of rules, procedures and timescales that must be adhered to by public bodies when letting public contracts. The Public Procurement Rules therefore lay down the procedural rules that public bodies must follow with regard to how to buy works, goods and services but not what to buy: it is up to the public bodies to decide what to buy and to define the characteristics of the services that best fit their needs and to put in place the conditions which are the most appropriate for their desired policy objects (as long as they are transparent and non-discriminatory).

<sup>25</sup> Under the Directive only those provisions relating to technical specifications (Article 23) and notices (Article 35(4)) apply to Part B services. Under the Regulations, Regulation 4(3) requires, in addition, public bodies (a) to treat economic operators equally and in a non-discriminatory way and (b) to act in a transparent way. In practice, these requirements are very similar to those requirements imposed on public bodies under administrative law principles, notwithstanding that the principles themselves and tests are different.

<sup>26</sup> [www.ncvo-vol.org.uk/commissioning/procurement/legal\\_framework](http://www.ncvo-vol.org.uk/commissioning/procurement/legal_framework): ‘Efficiency’

## 3. The Public procurement rules (continued)

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### 3.4 What are the consequences of breaching the Public procurement rules?

The obligations contained in the Public Procurement Rules are statutory duties owed by public bodies to providers. If the duties are breached, aggrieved providers can bring a claim in the High Court against the public body. Aggrieved providers can also make complaints to the European Commission which can investigate the complaint and, if necessary, take action against the relevant Member State. However, the European Commission has limited resources and is therefore likely to concentrate on the most high profile cases.

#### (a) Consequences for public bodies

If proceedings are brought in respect of a tender process before a contract has been concluded, the contract award process is automatically suspended as an interim measure. That suspension remains in force until a court brings it to an end or the proceedings themselves are brought to an end. If the challenger is ultimately successful, the potential remedies against the public body include the setting aside of unlawful decisions (e.g. to exclude the challenger from the tender process), the setting aside of a decision to award a contract and/or the award of damages to the challenger.

In the most serious circumstances, a court is even able to set aside a contract that has already been concluded. For example, where the concluded contract ought to have been competitively tendered under the Public

Procurement Rules but wasn't. In addition or as an alternative to the setting aside of a concluded contract, financial penalties can be imposed against the public body. The penalties are decided on a case by case basis but have to be effective, proportionate and dissuasive. An alternative to set aside is the shortening of a contract where the court considers appropriate.

In addition to the formal consequences described above, there are a number of other potential consequences of breaching the Public Procurement Rules for public bodies such as bad publicity and wasted time and costs.

#### (b) Consequences for third sector organisations

The most serious potential consequence for a third sector organisation awarded a contract following a breach of the Public Procurement Rules is the set aside of that contract. Another consequence is the wasted time and costs spent in participating in a tender process that has to be abandoned or restarted following a breach. Certain losses and wasted costs may be recoverable from the public body, but this will depend upon the circumstances of the tender process, the contract and breaches.

## 3. The Public procurement rules (continued)

### 3.5 Changes to the Public procurement rules

In December 2011 the European Commission published proposals to modernise the Public Procurement Rules. 'Public procurement plays a key role in the Europe 2020 strategy as one of the market-based instruments to be used to achieve a smart, sustainable and inclusive growth while ensuring the most efficient use of public funds. For that purpose, the current public procurement rules ... have to be revised and modernised in order to increase the efficiency of public spending, facilitating in particular the participation of small and medium-sized enterprises in public procurement and to enable procurers to make better use of public procurement in support of common societal goals.'<sup>27</sup>

Whilst the final text of the new directive to replace the Directive has not yet been fully agreed, the proposed new directive no longer distinguishes between Part A and Part B services. Instead a new separate regime for social services is to be introduced which will have a higher threshold value (EUR 750,000 as compared with EUR 130,000 (central government services threshold) and 200,000 (non central government services threshold)) and will have limited applicable procedural obligations that will only include the obligations to respect the general Treaty principles of transparency and equal treatment.

'Certain categories of service continue by their very nature to have a limited cross-border dimension, namely such services that are known as services to the person, such as certain social, health and educational services. These services are provided

within a particular context that varies widely amongst Member States, due to different cultural traditions....Given the importance of the cultural context and the sensitivity of these services, Member States should be given wide discretion to organise the choice of the service providers in the way they consider most appropriate. The rules of this directive take account of that imperative, imposing only observance of basic principles of transparency and equal treatment and making sure that contracting authorities are able to apply specific quality criteria for the choice of service providers....'<sup>28</sup>

[Social care services will be social services for the purposes of the new directive.] It is also likely that most, if not all, of the social services contracts that are likely to be awarded to third sector organisations will be significantly below the proposed threshold of EUR 750,000. Such below threshold contracts will fall outside the new public procurement rules and are unlikely to have any cross border interest which would bring into play the general Treaty principles: 'Services to the person with values below this threshold will typically not be of interest to providers from other Member States, unless there are concrete indications to the contrary, such as Union financing for transborder projects.'<sup>29</sup>

Even in the case of above threshold social services contracts under the new directive as currently proposed, public bodies when looking to award contracts for social services although required to publish either a contract notice or prior information notice (PIN) will then be free to decide on the type of procurement process to be

<sup>27</sup> Proposal for a Directive of the European Parliament and of the Council on public procurement: 16725/1/12 REV1 30 November 2012, recital 2

<sup>28</sup> Proposal for a Directive of the European Parliament and of the Council on public procurement: 16725/1/12 REV1 30 November 2012, recital 11

<sup>29</sup> Proposal for a Directive of the European Parliament and of the Council on public procurement: 16725/1/12, REV1 30 November 2012, recital 11

## 3. The Public procurement rules (continued)

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used, including negotiations, provided that they act fairly and transparently.

So, in practice for most social care services contracts awarded to third sector organisations, the position under the new proposals will be the same as the current position. However, as is the position now, the obligation to obtain best value and the need to comply with internal financial regulations and standing orders will mean that for all but the smallest contracts some form of competitive tendering will be required although not through OJEU.

The new proposed directive like the current Directive will not prevent public bodies from deciding to fund the provision of social care services through grants.<sup>30</sup>

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<sup>30</sup> See footnote 23 above

## 4. State aid rules

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### 4.1 Overview

The rules on State aid take a benign view of payments for social care services. Although the rules on State aid should be consulted on each occasion, it is highly likely that payments for social care services either will not constitute State aid at all or will be exempt from notification. Further information on the key exemptions is included in paragraph 4.2 below.

Even if none of the key exemptions mentioned in paragraph 4.2 below apply, there are a number of other reasons why contracts relating to social care services may either not involve State aid at all, or may be exempt from the notification requirement. Should it be necessary to consider these further matters, paragraph 4.3 below explains what 'State aid' is; paragraph 4.4 below sets out the other main grounds on which it could be possible to argue that State aid either isn't present or need not be notified in the context of social care services; paragraph 4.5 below summarises the ways in which third sector organisations could be affected by the rules on State aid and paragraph 4.6 below, for the sake of completeness, summarises the consequences of unlawful State aid.

This document is not intended to constitute legal advice applicable to any particular situation, and if a transaction may involve State aid, a careful analysis should be undertaken each time, with reference to the relevant legislation and communications from the European Commission. Ultimately, if there is State aid and none of the exemptions apply, the aid must be notified to the European Commission in advance. There then

follows a standstill period while the Commission reaches a decision whether or not to permit the aid, and the aid cannot be given until the Commission has reached its decision as to whether or not to allow it.

### 4.2 The key exemptions

Social care services provided pursuant to a public sector contract will generally count as 'services of general economic interest' (or 'SGEI'). SGEI are economic activities that would not be produced by market forces alone or at least not in the form of an affordable service available indiscriminately to all. SGEI are therefore carried out in the public interest under conditions specified by the State and those conditions may be set out in legislation or in a contract.

There are exemptions<sup>31</sup> for aid for SGEI in the following areas, meaning that any resulting State aid is seen as compatible with the internal market and therefore exempt from the requirement to be notified:

- (a) payment not exceeding EUR 15 million (approximately £12.9 million as at March 2013) per annum per recipient (other than for services in the area of transport and transport infrastructure);
- (b) payment for SGEI services by hospitals providing medical care;
- (c) payment for SGEI meeting social needs as regards health and long term care, or the care and social inclusion of vulnerable groups.

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<sup>31</sup> Under the terms of Commission Decision of 20 December 2011 on the application of Article 106(2) of the Treaty on the Functioning of the European Union to State aid in the form of public service compensation granted to certain undertakings entrusted with the operation of services of general economic interest (2012/21/EU)

## 4. State aid rules (continued)

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There are certain conditions to be satisfied in order for these exclusions to apply, as follows:

- (a) the contract for the services must not exceed 10 years, unless significant investment is needed from the service provider which needs to be amortised over a longer period (in accordance with generally accepted accounting principles).
- (b) there are particular requirements as to the content of the contract, in terms of defining the services, the payment mechanism and the arrangements for avoiding or recovering any overpayment.
- (c) the payment must be no more than necessary to cover the cost of providing the services, including a reasonable profit, and must not be used towards the provision of any services apart from the SGEI.
- (d) the recipient must be obliged to repay any overcompensation received, and there must be checks at least every three years to ensure that there is no overcompensation.

It is therefore advisable to ensure that any contract or grant relating to social care services meets these conditions, in order to benefit from the exemption.

### 4.3 What is State aid?

Under Article 107(1) of the Treaty, State aid is any 'aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods...in so far as it affects trade between Member States.'

State aid is unlawful unless it:

- falls within one of the very limited exclusions in Article 107;
- falls within the scope of a group or 'block' exemption (such as the exemptions for SGEI discussed in section 4.2); or
- has been notified to, and authorised by, the European Commission in advance.

The rules on State aid are an additional layer of regulation. Even if a particular aid is permitted under State aid rules, this does not excuse the public sector body granting the aid from having to comply with any other applicable rules, such as those on public procurement.

State aid can take any form whatsoever. Most obviously, it covers grants and other subsidies but it also covers other dealings where the recipient gets a better deal than it could have achieved in the open market – for example, the purchase of services by a public body on terms which are more preferential than those offered by customers in the private sector.

In order for there to be State aid, all of the criteria set out in Article 107(1) of the Treaty must be met, namely:

#### **(a) the aid is provided through State resources**

This includes national, regional and local authority resources and European government funds. It also includes monies distributed by a non-public body if the origin of those monies is the State – e.g. the distribution of grant monies by a third sector organisation.

## 4. State aid rules (continued)

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### **(b) the aid is selective in nature because it favours certain undertakings or the production of certain goods**

Aid is selective if it is available only to particular undertaking(s), or only to undertakings within a particular market sector.

In this context, an 'undertaking' means an entity carrying out economic activities in a market environment. If the recipient is providing goods or services which could be offered commercially on a given market, then it will count as an undertaking, even if it provides those goods or services on a not-for-profit basis. Therefore even voluntary and non-profit making public, private or third sector bodies such as charities count as an 'undertaking' for the purpose of the rules on State aid if they are carrying out economic activities of a sort for which a market exists in the UK.

### **(c) the aid favours the recipient**

This requirement is met if the aid confers an economic advantage on the recipient which it would not have enjoyed under normal market conditions. This requirement has given rise to the 'private investor test' (also known as the 'market economy investor principle' or 'MEIP'). The test involves a comparison of the State's behaviour with the behaviour which would be expected from a private investor in the same circumstances. It is therefore an assessment of whether the terms attached to the aid are more generous than could have been obtained by the recipient on arms length commercial terms in the market. Perhaps the

aid in question would not have been available in the market place on any terms, or only on more onerous terms.

Generally, if the MEIP test is satisfied, then there will be no State aid. However, in the context of payments for public services which count as Services of General Economic Interest, rather than apply the MEIP test it is necessary to consult the special rules relating to SGEI (see paragraph 4.2 above).

### **(d) the funding distorts or threatens to distort competition and affects trade between Member States**

There is a very low threshold for determining whether the aid distorts or threatens to distort competition. Essentially, if an undertaking has received the benefit of aid, by definition other undertakings operating in the same market will have been disadvantaged in comparison.

More relevant in relation to social care services, is the issue of whether the funding affects trade between Member States. This involves asking whether the aid affects a market in which there is trade between Member States. It is irrelevant whether or not the recipient of the aid trades in other Member States itself. Again, there is a very low threshold when deciding whether this requirement has been satisfied. It is only where the aid is distinctly local in character and in a sector with little intra-Community trade, that it may be possible to argue that there is no effect on trade between Member States. There is more information about this in paragraph 4.4(a) below.

## 4. State aid rules (continued)

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### 4.4 Other grounds on which procurement of social care services may not involve State aid at all or may be exempt from notification under the State aid rules

#### (a) the services are purely local in nature

If the services are purely local in nature, then there is no scope for affecting trade between Member States, and therefore no State aid. One example of where the European Commission has concluded that services were of a purely local character was in relation to local hospital services aimed exclusively at the local population. However, if competitors in the market for services of the type in question tend, as a matter of fact, to trade cross-border, this would tend to suggest that the services are not purely local in nature.

#### (b) the services are not an 'economic activity'

If there isn't a competitive market for the services concerned, then the provision of those services will not be an economic activity and there will not be State aid. BIS gives as an example of a non-economic activity a service which is monopolised by a state body or a charity and run on a non-commercial basis as a function of the State. However, since the social care sector is highly fragmented, and very competitive, it is very difficult to think of an example of social care services which are not subject to competition, and therefore not economic activities.

Even if the services in question are non-economic activities, if the recipient also engages in economic activities, care is needed to ensure that any public funding received for the non-economic activities cannot be used to benefit the economic activities.

### 4.5 How do the State aid rules apply to third sector organisations?

State aid issues could affect third sector organisations in one of three ways:

- (a) public funding in the form of grants provided to a third sector organisation may constitute a State aid if that funding is provided or used to support commercial activities; and/or
- (b) public funding in the form of higher than commercial/market payments under contracts for the provision of services; and/or
- (c) a third sector organisation may itself be a body that grants State aid when, for example, distributing public funding or when using public funding in order to provide services in the market at less than commercial/market rates. In this regard, there is an exemption (in article 107(2) of the Treaty) for aid given to individuals which has a social character, but there are criteria to satisfy and an obligation to notify the aid in advance so that the Commission can confirm that the aid does in fact fall within the exemption.

## 4. State aid rules (continued)

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### 4.6 Consequences of unlawful State aid

The Commission is under an obligation to order recovery of any unlawful aid that is found to be incompatible with the common market. The recipient must be required to repay the unlawful State aid with interest. The power to order recovery becomes time barred 10 years after the aid is granted.

Both the public body giving the aid and the recipient may also face damages claims from disgruntled competitors who claim to have been disadvantaged by the payment of the aid or by any failure to notify the aid and observe the standstill period.

Any risk that aid may have to be repaid is obviously of great concern to the aid recipient. It is also of concern to the public body which provides the aid because of the political and reputational damage that can be suffered if it is found that the aid was unlawful.

It is common for public bodies to include provisions in the aid documentation enabling them to claw-back the aid if it is found to constitute unlawful State aid. Having a contractual provision to rely on in order to enforce recovery is much easier than having to directly apply the State aid rules.

In cases where the aid documents are entered into in advance but the aid needs to be notified, the parties should consider including a condition precedent in the documentation to ensure that the grant of the aid is conditional on the Commission first authorising it.

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# 5. Public and administrative law considerations

## 5.1 Introduction

In paragraphs 5.2 to 5.5 below we look at the responsibilities for social care within the devolved constitution, the law relating to local authority powers and duties including the duty of continuous improvement ('best value'), relevant procedural requirements in relation to contracts, the statutory powers and duties of local authorities in relation to social care and the judicial control of local authorities with particular reference to social care.

## 5.2 Devolution context

Since 2011 the legislative powers of the National Assembly for Wales have included powers to legislate generally by Act of the National Assembly in relation to the structure, powers and duties and finance of local authorities in Wales, under the Government of Wales Act 2006.

During the Third National Assembly between 2007 and 2011 the National Assembly had powers to pass primary legislation conferred on it by a combination of provisions in Westminster primary legislation and legislative competence orders. Some Wales only local government legislation (known as 'Measures') was passed under these provisions.

The National Assembly now has legislative powers in relation social welfare including social services, subject to certain exceptions which relate to the overlap with social security and certain children's services.<sup>32</sup>

Although many of the basic statutes relating to local government and social care are Acts of the Westminster Parliament that pre-date the current legislative powers of the National Assembly for Wales, for example the Local Government Act 1972, these can now be repealed or amended by Acts of the National Assembly for Wales.

Following enactment of the Government of Wales Act 2006 it is an established constitutional convention that Westminster will not legislate on a subject where legislative competence is devolved to the National Assembly for Wales without the consent of the National Assembly for Wales.<sup>33</sup> An example of this in the procurement context is the Public Services (Social Value) Act 2012, which requires certain public authorities to consider how, in the context of procuring services, economic, social and environmental well-being may be enhanced. However, the National Assembly for Wales was not asked to consent to this duty extending to devolved institutions. Accordingly, the Act expressly states that it does not extend to devolved institutions in Wales.<sup>34</sup>

<sup>32</sup> See the Government of Wales Act 2006, Schedule 7, part 1, para. 15:

15 Social welfare

Social welfare including social services. Protection and well-being of children (including adoption and fostering) [ and of young adults] 1 Care of [children,] 2 young adults, vulnerable persons and older persons, including care standards. Badges for display on motor vehicles used by disabled persons.

Exceptions –

Child support.

Child trust funds, apart from subscriptions to such funds by—

(a) a county council or county borough council in Wales, or (b) the Welsh Ministers.

Tax credits.

Child benefit and guardian's allowance.

Social security.

[Independent Living Funds.

Motability.

Intercountry adoption, apart from adoption agencies and their functions, and functions of 'the Central Authority' under the Hague Convention on Protection of Children and Co-operation in respect of Intercountry Adoption.

The Children's Commissioner (established under the Children Act 2004 (c. 31)).

Family law and proceedings, apart from—(a) welfare advice to courts, representation and provision of information, advice and other support to children ordinarily resident in Wales and their families, and (b) Welsh family proceedings officers.

<sup>33</sup> Which is given by means of a Legislative Consent Motion

<sup>34</sup> Defined as the Welsh ministers, the First Minister for Wales, the Counsel General, the national Assembly Commission and 'a relevant authority whose functions are wholly or mainly Welsh devolved functions', which will encompass Welsh local authorities.

## 5. Public and administrative law considerations (continued)

### 5.3 Local authority powers and duties

Local authorities are bodies created by statute. This means that they do not have any independent source of authority to act other than that which has been conferred upon them by the legislature. Powers must be exercised and duties fulfilled in accordance with relevant legislation.

In addition, the Courts have developed a body of administrative law to ensure that public bodies exercise their functions in a procedurally fair and proportionate manner.

Public bodies and the Courts are also bound to protect the fundamental rights and freedoms which now form part of UK law through the Human Rights Act 1998. These include the rights to family life, non-discrimination and the right not to be deprived of one's property except in the public interest under due process including rights of compensation.

Local Authorities in Wales have general powers under the Local Government Act 2000<sup>35</sup> to do anything which is calculated to further the economic, social and environmental well-being of their areas. These powers, while broad, are not unrestricted. For example, a local authority has to be satisfied that a proposal is for the benefit of its area and it cannot use these powers for something which would be for the benefit of local government generally unless there is also a demonstrable benefit to its own area. Similarly, the Courts have held that financial interests of the local authority do not constitute economic, social or environmental well-being within the meaning of the 2000 Act.<sup>36</sup>

It is worth noting in this context that the 2000 Act powers have been repealed in England by the Localism Act 2010 and replaced with a 'general power of competence' to do anything that a natural person can legally do subject to any specific statutory prohibitions or conditions.

In addition, where local authorities in Wales have a function conferred upon them the Local Government Act 1972 provides that those authorities can do anything that is 'calculated to facilitate or is conducive or incidental to, the discharge of any of their functions'. This power, although apparently wide, has been narrowly construed by the Courts.<sup>37</sup>

Local authorities have also been subject over the years to various improvement initiatives from central government. In 1980 legislation introduced compulsory competitive tendering ('CCT') for certain local government activities. Initially aimed at functions such as direct labour organisations its scope was progressively extended. The UK Government elected in 1997 was committed to introducing a new duty on local authorities to achieve 'best value' and CCT was abolished in 2000. Best value was intended to focus not only on effectiveness and economy of local government services but also effectiveness and quality of services.

The approaches in Wales and England to best value have progressively diverged. In 2005 the Welsh Government dropped the term when it adopted the 'Wales Programme for Improvement' in 2005. This was subsequently underpinned by legislation in the form of the Local Government (Wales) Measure 2009.

<sup>35</sup> See ss. 2 and 3

<sup>36</sup> See *R (Risk Management Partners Ltd) v Brent London Borough Council* [2009] EWCA Civ 490 – the case was subject to further appeal to the Supreme Court, but not in relation to the interpretation of the 'well-being' powers.

<sup>37</sup> See s.111

## 5. Public and administrative law considerations (continued)

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In broad outline the 2009 Measure places a duty on the unitary local authorities in Wales to set annual objectives for improving the exercise of their functions. Each improvement objective must be framed to improve the exercise of functions in terms of at least one of the following seven elements:

- (a) strategic effectiveness: which will be improved by an authority exercising its functions in a way which is reasonably likely to lead to the achievement of, or to assist in achieving, any of its strategic objectives;
- (b) service quality: which will be improved if there is an improvement in the quality of services;
- (c) service availability: which will be improved if there is an improvement in the availability of services;
- (d) fairness: which will be improved if disadvantages in accessing or taking full advantage of services experienced by some members of the community are reduced, or social well-being is improved as a result of the way services are provided or functions exercised;
- (e) sustainability: which will be improved if the carrying out of functions or the provision of services contributes to sustainable development in an authority's area;
- (f) efficiency: which will be improved through an improvement in the efficiency with which resources are used; and
- (g) innovation: which will be achieved if the way services are provided or functions

are exercised is changed in a way that is reasonably likely to lead to any of the above outcomes.

The strategic objectives of a local authority are set out in its community strategy, which is now being incorporated into a Single Integrated Plan by each Local Service Board in Wales.

Other features of the improvement system are:

- (a) a duty to consult residents, non-domestic rate payers, representatives of service users and any other stakeholders who appear to the authority to have an interest.
- (b) the duty to have regard to guidance from the Welsh Ministers.
- (c) the power of the Welsh Ministers to specify performance indicators.
- (d) a duty on local authorities to collaborate with other local authorities where a local authority concludes that this will assist it to meet its improvement objectives.
- (e) requirements to publish performance information each year and to publish an improvement plan for subsequent years.
- (f) arrangements for auditing and inspection by the Wales Audit Office, Estyn, health and social care inspectorates and an authority's own statutory auditors.

It should be noted that the powers of collaboration cover not only collaboration with other local authorities but also any person or the employees of that person, authorised to exercise the functions of a local authority by the Welsh Ministers under the Deregulation and Contracting Out Act 1994, although no such

## 5. Public and administrative law considerations (continued)

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orders have been made to date by the Welsh Ministers.

The pressure that the improvement system places local authorities under is an important driver for local authorities to consider the outsourcing of services in areas such as social care.

In addition to the general statutory powers and duties outlined above, local authorities in Wales have specific functions and duties in relation to the provision of social care.

The main provision relating to the provision of accommodation and welfare services by local authorities is the National Assistance Act 1948 as amended by Part III of the National Health Service and Community Care Act 1990.

The Welsh unitary authorities in their capacity as social services authorities have powers and duties in relation to the provision of residential accommodation for people over the age of 18 (who are ordinarily resident in their area or in urgent need) who, because of age, illness or disability or other circumstances are in need of care and attention not otherwise available to them otherwise than by the provision of residential accommodation under this particular power. The local authority may itself provide accommodation or may make other arrangements with voluntary organisations, the private sector or another local authority.

Local authorities may also provide domiciliary services and may employ voluntary organisations and private sector providers as their agents in the provision of welfare services, under powers contained in the National Assistance Act 1948. In addition, the Chronically Sick and Disabled

Persons Act 1970 imposes duties on authorities to make arrangements for the provision of services to disabled persons.

Local authorities are under a duty to prepare and consult on a plan for the provision of community care services in their area under the National Health Service and Community Care Act 1990. Local authorities are also under a duty to assess the needs of persons who appear to them to be in need of community care services. There is a considerable body of case law on the carrying out of needs assessments and on the extent to which the resources available to local authorities can determine the level of support provided.

### 5.4 Procedural requirements in relation to contracts

Where local authorities procure services or contract out functions the larger value contracts will come within the scope of public procurement legislation. For more information on the public procurement rules see paragraphs 3.1 to 3.5 above. However, where the value of contracts falls below the threshold values under the public procurement rules and subject to compliance with the 'general Treaty principles' described at paragraph 3.1 above, it is a matter for the local authority to specify its own procurement procedures.

Each local authority is required by legislation to maintain and publish a constitution and to make it available on the authority's website. There are prescribed models for local authority constitutions issued by the Welsh Ministers. Constitutions will also include the standing order

## 5. Public and administrative law considerations (continued)

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relating to contracts that local authorities are required to adopt under section 135 of the Local Government Act 1972.

Contract standing orders may differ from authority to authority but they will generally prescribe greater levels of formality as contract values increase. They will also deal with procedural matters such as the delivery and opening of tenders.

In preparing to participate in procurement that is not being conducted under public procurement legislation it is always prudent to check the local authority's contract standing orders.

### 5.5 Judicial control

In common with any other body exercising public functions local authorities are subject to the general principles of administrative law in the exercise of their functions.

It is important to recognise that administrative law is concerned with the way in which decisions are taken and not with the merits of a decision under challenge. Provided a decision was taken in a procedurally lawful manner, the Courts will not interfere with the conclusions of the decision-maker.

A lawful decision will be one which:

- (a) is within the limits of the powers being exercised or fulfils a legal duty placed on the decision-maker.
- (b) is not irrational, in the sense that it is not a decision which a decision-maker taking into account all the material consideration could not reasonably have taken. The bar for finding

a decision is irrational is deliberately set high, or otherwise the quashing of a decision on these grounds could become a form of judicial review of the merits of a decision.

- (c) is procedurally fair. Fairness covers a range of considerations, for example:
  - (i) hearing both sides of an argument,
  - (ii) not applying policy in blanket fashion that means the decision-taker does not take account of new or exceptional circumstances,
  - (iii) not relying upon or taking into account irrelevant considerations, and
  - (iv) ensuring that consultations are conducted in a manner that enables proposals to be understood and rationally commented upon.

Administrative decisions are subject to judicial oversight through judicial review proceedings. Judicial review is only available in cases with a public law basis and the procedure has a number of unique characteristics:

- (a) the challenge must refer to a specific action or decision, such as an individual needs assessment, or a decision to adopt a plan or policy.
- (b) there is a time limit for bringing the claim, which is currently as soon as practicable after the decision or action and in any event within three months.
- (c) the claim is initially reviewed by a judge who must decide whether to allow the claim to proceed. The test is whether the application discloses an arguable case.

## 5. Public and administrative law considerations (continued)

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(d) judicial review cases are dealt with on the basis of paper submissions and oral argument and seldom involve the taking of evidence.

law and should be brought by means of an action for judicial review.

(e) the Court may make one of a number of orders that are specific to administrative cases:

(i) a quashing order which overturns the decision complained of. It should be noted that the consequences of such an order is that the decision-maker is put in a position where it must take the decision again. It is possible in such cases that when the decision is made again even though the procedural defect in the original decision is cured, the decision on the merits is still the same.

(ii) an order prohibiting a public authority from acting outside its powers.

(iii) a mandatory order to compel a public authority to fulfil duties placed upon it. Nowadays such duties usually emanate from legislation.

(iv) a declaration which states the legal position, leaving it to the parties to act subsequently in accordance with its terms.

In appropriate cases public bodies may also be liable in damages for a breach of statutory duty or subject to an injunction to prohibit an unlawful act. These may be sought by ordinary action, thereby avoiding the 'filtering' stage of the judicial review process, although ordinary actions against public bodies are at risk of being rejected on the grounds that they concern matters of public

## 6. Factors to be taken into account when deciding whether to use grants or contracts

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In deciding whether to fund social care services through grants or contracts, public bodies will need to consider a range of different factors: legislative (including powers ('vires'), best value, State aid rules, Public Procurement Rules); policy (internal, local, regional and national); internal requirements (financial regulations and standing orders); and their objectives.

According to the NAO<sup>38</sup>, grants can be used as a funding mechanism if the following three pre-conditions are met:

1. legal power: the public body must have the legal power to make a grant for the purpose in question;
2. State aid: the public body must be satisfied that the grant that it wishes to award will not be an illegal State aid; and
3. 'right' kind of money: the public body must be satisfied that the money that it intends to use for the grant is the 'right' kind of money for the activity envisaged.

According to the NAO<sup>39</sup>, a public body can use procurement (in the context of this guidance, contracts) when:

1. outsourcing a function of the public body; and
2. it has the money in a suitable block relative to the service that it intends to buy.

The NAO considers that there may be situations where a public body satisfies both the rules regarding the use of grants and those regarding use of procurements/contracts. In such cases,

public bodies 'need to decide which one is more suitable for [their] programme, service or intended outcome'.<sup>40</sup>

According to HM Treasury:

'It is important to distinguish between procurement and grants and consequently to apply the appropriate procedures. The decision on which funding stream to use should be based on a combination of factors including:

- what level of control is appropriate;
- the state of the market; and
- the specificity of the outcomes which the funder intends and the indicators available for qualitative and quantitative measurement of these intended outcomes.

In general, however, the main determinant of the nature of the financial relationship is the nature of the intended outcomes. When the intended outcomes are relatively specific, and there are indicators available to evaluate the quality and quantity of those outcomes, a procurement process open to competition and leading to a conventional trading relationship under contract is likely to be the most appropriate option ... Grants ... on the other hand ... are more likely to be suited to supporting third sector organisations engaged in activities aligned with the Government's wider objectives and which the Government values ...'<sup>41</sup>

This appears to address the fundamental distinction between grants and contracts: grants are used to support an organisation

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<sup>38</sup> Tool kit – when can I use a grant?

<sup>39</sup> Tool kit – when can I use procurement?

<sup>40</sup> [www.nao.org.uk/sectors/third\\_sector/successful\\_commissioning/successful\\_commissioning/sourcing\\_providers/grant\\_or\\_procurement.aspx](http://www.nao.org.uk/sectors/third_sector/successful_commissioning/successful_commissioning/sourcing_providers/grant_or_procurement.aspx)

<sup>41</sup> Improving financial relationships with the third sector: Guidance to funders and purchasers May 2006, page 18, paragraphs 2.19 – 2.22

## 6. Factors to be taken into account when deciding whether to use grants or contracts (continued)

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that is operating in general or broad alignment with the policies and objectives of the public body; contracts are about legally requiring an organisation to deliver services required by the public body in return for a payment. If the public body needs the recipient of the funding to be under a legally binding obligation to deliver the services in question then contract rather than grant will be the more appropriate funding mechanism.

## 7. Charities and public services – a reminder

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- 7.1 It is important that all third sector organisations seeking to deliver public services, ensure that the services they are bidding to deliver will be within the objects or purposes of their governing document – whether this be a trust deed, the articles of association of a company, the rules of an industrial and provident society or the constitution of an incorporated charitable organisation.
- 7.2 Third sector organisations that are charities must function within their charitable objects for the benefit of the public. This is not to be taken as synonymous with the provision of public services.
- 7.3 It is important therefore that before deciding to bid for a contract to deliver public services, a charity should consider carefully whether, if it is successful, the services will fall within its mission for the benefit of the public.
- 7.4 The Charity Commission’s guidance on ‘Charities and Public Service Delivery’ (CC37)<sup>42</sup> and on ‘The Independence of Charities from the State’ (RR7)<sup>43</sup> should be consulted in the first instance and, if necessary in cases of doubt or uncertainty, appropriate legal advice should be sought.

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<sup>42</sup> <http://www.charity-commission.gov.uk/Publications/cc37.aspx#h1>

<sup>43</sup> <http://www.charity-commission.gov.uk/Publications/rr7.aspx>