

Commercial Property - Germany

Compulsory tender process for public sector property transactions

Contributed by **SIBETH Partnerschaft**

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On March 25 2010 the European Court of Justice (ECJ) delivered an eagerly awaited decision on the obligation to carry out a tender process for public sector property transactions.⁽¹⁾ Initial reaction in Germany was enthusiastic, the suggestion being that local communities, project developers and investors could relax since the ECJ had ruled that municipal property transactions were fundamentally not subject to EU public procurement law. However, an examination of the finely differentiated grounds given for the ruling shows that such conclusions were too hasty and did no justice to the deliberations of the court.

Dusseldorf Higher Regional Court ruling

The background of the judgment was a request to the ECJ for a legal ruling from the Dusseldorf Higher Regional Court. The Federal Agency for Public Property had carried out a tender process for the development of the Wittekind barracks complex in Wildeshausen. After four candidates submitted proposals, the town decided to implement one of the proposals and the agency sold the land to that developer. The purchase contract included no obligation for the purchaser to realise the project, but the municipal authority indicated that it would be willing to issue a project-based development plan if appropriate. The defeated claimant – one of the other three candidates – appealed to the review bodies, alleging that the purchase was null and void because no proper contract award procedure had been carried out.

Since 2007 the Dusseldorf Higher Regional Court has regularly taken the view that urban development contracts and property transactions with an obligation to build must be classified as public construction contracts as defined under public procurement law. As such, they are subject to a compulsory tender process. This case law policy was regarded as detrimental by the public sector and severely criticised by urban planners and investors. In the 2009 revision of the Public Procurement Act, the legislative body clarified that the concept of a public sector building contract presupposes that the public sector client has its own procurement need. Under Section 99(3) of the Restrictive Practices Act, there must be "construction services which provide a direct economic benefit to the client"; with this wording, the legislative body aimed to ensure that sales of land do not constitute a building contract with a compulsory tender process even if they are subject to urban development conditions.

In keeping with its previous case law policy, the Dusseldorf Higher Regional Court regarded the sale of the barracks as a building contract which falls under public procurement law. The court saw the central reason for a compulsory EU-wide tender process in the indirect interest of the municipality of Wildeshausen in achieving positive urban development effects through the specific building work. It argued that by deciding in favour of a specific usage concept on the basis of urban development considerations, it was in fact ordering a specific construction project. The plea by the federal agency and the municipal authority that the sale of the barracks complex did not meet any procurement need of the town as defined in the newly introduced provision of Section 99(3) of the Restrictive Practices Act was rejected by the Dusseldorf Higher Regional Court, which argued that EU procurement legislation envisages no such procurement need and the national legislative body is not entitled to pass national legislation limiting the concept of a public sector building contract. However, in view of the vehement reactions to its case law rulings and the change in German procurement law, the court considered it necessary to submit various questions to the ECJ on the interpretation of the concept of a "public sector building contract" and the compulsory

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tender process for property-related contracts in the public sector.

ECJ ruling

In its ruling of March 25 2010, the ECJ stated its view on these questions and decided that the circumstances of the case, involving the Federal Agency for Public Property, the investor and the town of Wildeshausen, did not effectively constitute a public sector building contract as defined under public procurement law. The ECJ especially based this conclusion on two principles.

First, the concept of a public sector building contract means that the contractor directly or indirectly undertakes to carry out building work, and this involves a construction or implementation obligation which can be legally enforced under national law. Secondly, the concept of a public sector building contract also assumes that the building work which is the subject of the order is materially or physically procured for the client, or that the client directly benefits from it economically. This direct economic interest is not applicable if the property transaction is merely in the urban development interest of the local community. Therefore, the exercise of urban development powers by the local authority does not automatically lead to a public sector building contract.

Thus, the ECJ decision supports the German legislation and confirms that the clarification under Section 99(2) of the Restrictive Practices Act (ie, that a compulsory tender process for a building contract only applies if the client has a procurement need) complies with EU law. In addition, the ECJ pointed out that the purchaser of the barracks entered into no obligation for building work since the purchase contract with the Federal Agency for Public Property envisaged no construction or implementation obligation. The court agreed that a project-based development plan (which the town has indicated that it would be willing to grant to the purchaser) would automatically lead to an implementation obligation for the purchaser. However, in fact, the town had indicated only its willingness to issue such a plan, so that at the time of the land purchase the purchaser entered into no binding obligation to build. Moreover, the court considered that there was no direct economic advantage for the town, since the urban development interests which the town welcomes in connection with the purchaser's usage concept establish no direct economic advantage which would constitute 'a procurement need' as defined under public procurement law. Here too the court considered that these circumstances could not be classified as a building contract (with a compulsory tender process).

This ECJ ruling overturns the strict case law policy of the Dusseldorf Higher Regional Court by rejecting a far-reaching application of the public procurement rules in public sector property transactions. The main conclusion that can be drawn from the ruling is that local communities now have a certain degree of leeway regarding the sale of land. This gives legal certainty to local communities, project developers and investors insofar as EU public procurement law does not apply to local community property transactions in the following circumstances if: (i) the purchaser is not under obligation to implement a specific project under the property transaction itself or a project-based development plan (Section 12 of the Building Code); or (ii) the local community is merely pursuing urban development interests through the transaction.

Comment

It would be a dangerous misreading of this ruling to conclude that the ECJ has declared all or most municipal property transactions to be free from the public procurement rules. For political or purely factual reasons, it is often inconceivable for the local community not to insist on a construction or implementation obligation for the purchaser. For example, if the property transaction is linked with a project-based development plan, the implementation contract also creates a (legally actionable) obligation to carry out the building work. In addition, the ECJ explicitly pointed to circumstances which could constitute a direct economic advantage for the local community and therefore lead to a building contract which is subject to the public procurement rules. In this connection, the court underlined that such an economic interest must be assumed on principle if the local community is to become the owner of the building (eg, by establishing hereditary building rights). The ECJ also suggested that an economic interest could also apply if the local community were to use the building in question. Financial participation in the project also indicates an economic interest, and if contractual requirements for the project which could not be enforced by exercising urban development powers are combined with financial contributions by the municipal authority, this can still lead to the application of public procurement law.

When applying this ruling, it must not be overlooked that the local community, the town of Wildeshausen, was not a party to the land purchase contract. The ECJ ruled on the sale of land belonging to the national government. In this situation, whereby the national government and the investor are the parties to the contract, the local community is involved only as the party granting planning permission for a specific project. However, the interests in the property transaction may be different from the outset if the local community itself is a party to the contract – especially in the sale of its

own municipal land. It may seem logical to suggest that the local community could first sell the property and then issue a project-based development plan, but this is likely to prove dangerous. This process could be interpreted as a way for the local community deliberately to avoid the application of public procurement law, since the ECJ has ruled against such practices on several occasions. In this connection, the ECJ ruling indicates that breaking down a process which is normally subject to public procurement law into two transactions which occur at different times does not avoid the need to observe public procurement law.

All future investor tender procedures must include an exact review of whether the property transaction is subject to compulsory tender under the new ECJ requirements. Those who claim that local community transactions in general are now free from compulsory tender may well have applied the ECJ ruling in an undifferentiated manner. This could prove to be a costly misjudgement.

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Endnotes

(1) Decision C-451/08.

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