

Current case law from the European Court of Justice with implications for the notarial practice*

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1. How Community law operates

As is well known, Community law is **part of the respective national legal systems of the Member States**. This means that Community law does not amount to foreign law that the Notary does not have to know¹. Yet even today Community law still has a shadowy existence in everyday notarial practice. The reason for this is due partly to the fact that the majority of Community law still affects fields of law such as the common agricultural market, customs union, competition law, employment and social security law and intellectual property, areas which have little significance in notarial practice. Slowly but apparently inexorably, however, the regulatory scope of Community law is extending to the core areas of notarial work such as property law, succession and family law, company law and general private law².

The minor significance of Community law in notarial work is, however, also due to the **mode of operation** of Community law. Community law does indeed apply immediately in all Member States and takes precedence over conflicting national law. But a distinction has to be drawn between the precedence of Community law and the question of direct applicability, so whether the specific provision of Community law has to be applied directly by the authorities and courts without any further act of implementation and whether the provision creates immediate rights and duties for individuals. If a provision of Community law is formulated in such a way that it allows Member States discretionary powers with regard to its application, there still has to be a national legislative act in order for the Community law to become important in respect of notarial practice.

In the area of **primary Community law**, meaning in particular under the EU Treaty, the ECJ has granted direct

applicability to only a few legal provisions. Of particular note in the area of private law are: Article 12 EC (General Prohibition on Discrimination³), Articles 43 and 48 EC (Freedom of Establishment⁴), Articles 49 and 50 EC (Freedom to Provide Services⁵), Article 56 EC (Free Movement of Capital⁶) and Article 88 para. 3 EC (Prohibition on Unlawful State Aid⁷).

The provisions of **EU Regulations** which, with their general, abstract effect are comparable to (national) laws in the substantive sense are, it is true, applicable without any further act of implementation in the same way as primary law in all Member States. Rights and duties of individuals are, however, only created if the specific provision of the regulation contains clear and unconditional obligations on the part of the Member States.

Yet more complicated is the mode of operation of **Directives**. Directives must first be implemented by the Member States in national law. The interpretation of this national law must be carried out in light of the directive, with preference having to be given to the interpretation which assists in application of the directive (interpretation consistent with the directive). The provisions of a directive will only become of direct practical significance if the directive has not been implemented within the specified period by the Member States and the specific provision is sufficient and certain enough in order to be applied directly. But even in the latter case the unimplemented directive only has vertical effect, i.e. it is only applicable as between state power and citizen⁸. In case law the ECJ has consistently refused to permit horizontal application between citizens⁹.

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1 Thus regarding German law: WINKLER, *Beurkundungsgesetz* (BeurkG) (Notarial Recording Act), 16th edition, 2008, section 17 BeurkG marginal No. 271.

2 A current project of the Commission is the drafting of a common frame of reference for civil law. This project has however seen a significant loss of momentum in recent months – see e.g. LEIBLE, *Europäisches Privatrecht am Scheideweg*, NJW 2008, 2508, KAMPAUSEN, *Europäisches Vertragsrecht – quo vadis?*, notar 2008, 56 und 87. For the development of the project see *inter alia*, from a notarial viewpoint: J. SMITS, *Some Critical Remarks on the Use of the Principles of European Contract Law*, Notarius International 2001, 142; G. WEHRENS, *Convergence of the Civil and Commercial Law of EU Member States*, Notarius International 2001, 212; SCHMUCKER, DNotZ 2005, 897; JEEP/VOSSIUS, notar 2005, 101; LANGHEIN, notar 2005, 119; LEHNE/SCHULTE-NÖLKE/STAUDENMAYER, notar 2005, 157).

3 ECJ, Judgment of 13.2.1985 C-293/83 (*Gravier*), [1985] ECR 593.

4 ECJ, Judgment of 21.6.1974, C-2/74 (*Reyners*), [1974] ECR 631.

5 ECJ, Judgment of 3.12.1974, C-3/74 (*van Binsbergen*), [1974] ECR 1299.

6 ECJ, Judgment of 31.1.1984, joined cases C-282/82 and C-26/83 (*Luisi and Carbone*), [1984] ECR 377.

7 ECJ, Judgment of 11.12.1973, C-120/73 (*Lorenz*), [1973] ECR 1471.

8 The directive cannot of itself, however, create obligations for individuals, so that thus, for example, criminal penalties under a directive cannot be derived directly (see in this regard, *inter alia*, ECJ judgment of 3.5.2005, joined cases C-387/02, C-391/02 and C-403/02 (*Berlusconi*), [2005] ECR I-3565. All decisions of the ECJ since mid 1997 are accessible on its home page on the internet: <http://curia.europa.eu/>).

9 See in particular ECJ, judgment of 14.7.1994, C-91/92 (*Facini Dori*), [1994] ECR I-3325, marginal No. 25.

Thus directives are of no direct significance with regard to private law relationships. The fact that the Notary, as an organ of public authority, is exercising a sovereign function does not alter anything in this regard. What the drafting of contracts involves is precisely the recording of agreements between private parties. If the Notary were obliged to apply the directive directly, the Community legislator could have achieved this by acting via an obligation of recording, at the expense, however, of at least one of the contracting parties, although it only has the power to do so in cases where it is entitled to adopt regulations¹⁰.

Against this background it is clear that reading the Official Journal of the European Union or other official case reports of the European Court of Justice does not, at least at present, represent a sensible cost/benefit ratio for Notaries. Nevertheless some recent decisions of the European Court of Justice and their national follow-up decisions do deserve attention as they have direct reference to notarial practice.

2. Property law

The greatest practical effects hitherto of ECJ case law can be found in property law.

2.1. Property sales by state authorities and state aid law

Here we shall look firstly at the prohibition on implementing unnotified and unauthorised **state aid**. In notarial practice, sales of property by local authorities, municipalities, the federal government or federal states (*Länder*) are frequently to enterprises to whom various forms of incentives have been granted. This may involve the sale of a former military area for civilian re-use as an amusement park, the privatisation of formerly state-owned agricultural or forestry areas by the Federal Agency for Special Re-unification Tasks (*Bundesanstalt für vereinigungsbedingte Sonderaufgaben*) or the disposal of commercial land in the industrial or trading estates that sprang up all over the place in the 90s. In the competition to encourage businesses to locate in their area, municipalities and local authorities often vie with each other in offering incentives to enterprises, be it to generate local business tax and income tax revenues in the long term or to create jobs, or quite simply to generate at least a part of the development costs for the often oversized industrial estates.

In the case of such sales, however, the provisions of Community law are frequently overlooked.

2.1.1. Prohibition of subsidies

Article 87 et seq. EC in principle prohibits the granting of any aid 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**. According to the case law of the ECJ, the question as to whether the element of trade interference is present must be answered in the affirmative if, as a result of the fiscal advantage afforded to

an undertaking, it appears possible that this will have future effects on intra-community trade¹¹. Such an assumption is already created if the financial power of the undertaking is strengthened. The ECJ thus interprets this element very broadly. Moreover, with increasing cross-border trade relations and greater mobility of consumers, in practice the cross-border aspect may represent the norm. Only in the case of purely local economic activities can there be an absence of aid within the meaning of Article 87 et seq. EC¹².

2.1.2. Legal consequences

In accordance with Article 88 para. 3 sentence 1 EC the European Commission must be informed of any plans to grant or alter aid in sufficient time to enable it to express its views. In accordance with Article 88 para. 3 sentence 3 EC the Member State concerned must not put its proposed measures into effect until the Commission has issued a final decision on the matter. Back in 1973 the Court of Justice recognised the direct effect of the **notification obligation** pursuant to Article 88 para. 3 sentence 1 EC and of the **prohibition on implementation** pursuant to Article 88 para. 3 sentence 3 and ruled that a breach of the notification obligation and of the prohibition on implementation obliged the Member State to reclaim and the aid recipient to repay the aid respectively¹³. In 1991 the Court of Justice decided in the case of **FNCE** that “for the benefit of individuals who can invoke such an infringement, national courts [must] draw the appropriate conclusions [from an infringement of the notification obligation], in accordance with their national law, as regards the validity of measures giving effect to the aid, the recovery of financial support granted in disregard of that provision and possible interim measures¹⁴.” In the opinion of the ECJ the fact that unnotified aid is subsequently categorised by the Commission as materially lawful also does not result in the elimination of the aforementioned consequences¹⁵.

As a result of this ECJ case law, in recent years the opinion has also come to prevail in German legal litera-

10 Cf. ECJ, judgment of 14.7.1994, C-91/92 (*Facini Dori*), op cit., marginal No. 24.

11 ECJ, judgment of 17.9.1980, C-730/79 (*Philip Morris*), [1980] ECR 2671, marginal No. 11.

12 The Commission ascertained such a purely local business activity in, for example, its *Freizeitbad Dorsten* decision (published under http://europa.eu.int/comm/secretariat_general/sgb/state_aids/industrie/n258-00.pdf). This case involved the privatisation of 2 indoor swimming pools and an outdoor pool that were operated by the town of Dorsten, a town of 80,000 inhabitants in North Rhine Westphalia at an annual loss of DM 2.4 million. The town granted the new operator a building lease with a duration of 35 years in return for reasonable ground rent and undertook to pay an annual operating cost subsidy of DM 2 million. The Commission said that there was no infringement of Article 87 et seq. EC in particular because the case concerned an establishment that was by no means unique in North Rhine Westphalia and Germany with a catchment area of around 50 km and the distance to the Netherlands was greater than 50 km.

13 ECJ, judgment of 11.12.1973, C-120/73 (*Lorenz GmbH*), [1973] ECR 1471, marginal No. 8.

14 ECJ, judgment of 21.11.1991, C-354/90 (*FNCE*), [1991] ECR I-5505, marginal No. 12.

15 footnote 15 see page 64.

ture that failure to give prior notification leads to **invalidity of the contract containing the aid**¹⁶. The German Federal Constitutional Court (BGH) also concurred in this view in 2003 and ruled that Article 88 para. 3 sentence 3 EC represents a prohibition statute within the meaning of section 134 of the German Civil Code (BGB) and accordingly a corresponding purchase contract is wholly null and void¹⁷. The BGH's decision does not, however, permit any inference to be drawn as to whether the invalidity also includes the conveyance of the property. In the specialist literature on the subject both views are advocated¹⁸. If one sees aid involved in the grant of the piece of land as such, in my opinion it is only logical to proceed on the assumption that the conveyance is also invalid.

In any event the ECJ case law means that where aid within the meaning of Article 88 EC is present and no notification procedure has been carried out¹⁹, the Notary must refuse to record and execute the deed. It is, however, very difficult for the Notary to identify the existence of aid requiring notification.

2.1.3. Exceptions

In 1997 the Commission summarised in the form of a **Communication** the cases in which it never assumes the presence of state aid in relation to the sale of buildings and land by public authorities²⁰.

In terms of the Communication, a sale following a sufficiently well-publicised, **open and unconditional bidding procedure** (comparable to an auction) in principle does not constitute state aid. The publicising of the sale must take place repeatedly over an extended period of time (two months or more) in the national press, estate gazettes or other appropriate publications. An offer is 'unconditional' when any buyer, irrespective of whether or not he runs a business or of the nature of his business, is generally free to acquire the land and buildings and to use it for his own purposes. Restrictions imposed for the prevention of public nuisance, for reasons of environmental protection or to avoid purely speculative bids as well as urban and regional planning restrictions imposed on the owner pursuant to domestic law on the use of the land and buildings do not affect the unconditional nature of an offer. Conditions which exceed the foregoing limits are only regarded as unconditional if all potential buyers would be in a position to meet the obligation, irrespective of whether or not they run a business or of the nature of their business.

If no bidding procedure is used, it is assumed that no aid is present if, prior to notarisation, an independent evaluation is carried out by an **independent expert or experts** in asset valuation and the market value was established in this way on the basis of generally accepted market indicators and valuation standards. If the market price established in this way is agreed as the purchase price or is even exceeded, in any event there is no notification obligation. If, after reasonable efforts, it becomes clear that it will not be possible to sell the land and buildings at the market value established by the independent evaluation, the Commission deems a **downward diver-**

gence of up to 5% as still being in line with market conditions. If the property is also not sellable at this price, according to the Commission a new valuation can be carried out by the valuer. Special obligations that relate to the land and buildings and not to the purchaser or his economic activities may be attached to the sale in the public interest provided that every potential buyer is required, and in principle is able, to fulfil them, irrespective of whether or not he runs a business or of the nature of his business. The economic disadvantage of such obligations should, in the view of the Commission, be evaluated separately and may be set off against the purchase price. If the public authorities acquired the land and buildings within a relatively short period, in particular within the last three years, the cost incurred by the public authorities in acquiring land and buildings is an indicator for the market value and the market value may not be set below this without an expert opinion.

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- 15 The aforementioned FNCE decision also states in this regard: "The Commission's final decision does not have the effect of regularising ex post facto the implementing measures which were invalid because they had been taken in breach of the prohibition laid down by the last sentence of Article 93 (3) (3) of the EEC Treaty [now Article 88 para. 3 sentence 3 EC], since otherwise the direct effect of that prohibition would be impaired and the interests of individuals, which, as stated above, are to be protected by national courts, would be disregarded. Any other interpretation would have the effect of according a favourable outcome to the non-observance by the Member State concerned of the last sentence of Article 93(3)(3) and would deprive that provision of its effectiveness" (ECJ, judgment of 21.11.1991, C-354/90 (FNCE), op cit., marginal No. 16).
 - 16 STEINDORFF, EuZW 1997, 7 et seq; *idem* ZHR 152 (1988), 7, 8 et seq; SCHROEDER, ZHR 161 (1997), 805, 811 et seq.; PECHSTEIN, EuZW 1998, 495; REMMERT, EuR 2000, 476 et seq., MARTIN-EHLERS, WM 2003, 1601.
 - 17 BGH, judgment of 4.4.2003 – V ZR 314/02, MittBayNot 2004, 250 = WM 2003, 1491 = ZfIR 2004, 73 with comments e.g. by MARTIN-EHLERS, WM 2003, 1601, 1603 et seq.; PECHSTEIN, EuZW 2003, 447; KIETHE, RIW 2003, 782, 785, affirming e.g. KNAPP, MittBayNot 2004, 252, 253; The initial case involved the statutory recognition of invalid purchase contracts under section 141 BGB by means of section 3a Equalisation Payments Act (*AusglLeistG*). The notarial purchase contracts by which formerly state-owned agricultural and forestry areas were sold to leaseholders at below value were, in the opinion of the BGH, void because of the unnotified aid contained therein.
 - 18 GRZIWOTZ, ZfIR 2004, 53 and 54, does not preclude nullity of the conveyance following an infringement of Art. 88 para. 3 EC; alternative viewpoint: SCHMIDT-RANTSCH, NJW 2005, 106, 109, HÖFINGHOFF, RNotZ 2005, 387, 399 et seq.
 - 19 The details of the investigation procedure by the Commission are regulated in Council Regulation No. 659/1999 of 22.3.1999 which lays down detailed rules for the application of Article 93 of the EC Treaty, OJ EC L 83, 1 – hereinafter the "Regulation". After receipt of the complete notification the Commission must undertake a preliminary investigation within a period of two months (Arts. 2 and 4 of the Regulation). If the Commission finds in the course of this preliminary investigation that the notified measure gives rise to doubts as to its compatibility with the common market, the Commission initiates the so-called formal investigation procedure in accordance with Art. 93 para. 2 EC (Art. 4 para. 4 of the Regulation). If the Commission has not taken a decision within two months the aid shall be deemed to have been authorised by the Commission (Art. 4 para. 6 of the Regulation). The formal investigation procedure can result in the decision that the notified measure does not constitute aid (Art. 7 para. 2), that the notified aid is compatible with the common market (Art. 7 para. 3) or that the notified aid is not compatible with the common market (Art. 7 para. 5).
 - 20 Commission Communication on State aid elements in sales of land and buildings by local authorities of 10.07.1997, OJ EC C 209, 3.

In addition the Commission also refers in its Communication to the so-called **de minimis rule** which has, in the meantime, become binding law in the form of a Regulation²¹. In terms of this Regulation aid not exceeding a total of **EUR 200,000 over a period of three fiscal years** (up to 31.12.2006: EUR 100,000 within a period of three years) is not liable to affect trade between Member States and/or does not distort competition. Such aid does not therefore fall within Article 87 (1) EC and accordingly also does not require notification. The threshold of EUR 200,000 refers to the total amount of aid granted to an enterprise, regardless of the form of aid or the objective pursued²². The three year period furthermore has a mobile character, i.e. in relation to each new grant of de minimis aid the total amount of the de minimis aid granted during the preceding three fiscal years is applicable²³. In terms of the Regulation the de minimis aid should be considered to be granted at the moment the legal right to receive the aid is conferred on the enterprise. Aid payable in several instalments is discounted to its value at the moment of its being granted²⁴.

In terms of No. 3 of the Communication all sales by public authorities which do not take place on the basis of a bidding procedure as described in greater detail above or whose compatibility with the common market is not supported by an expert opinion, or which are not covered by the de minimis rule must be notified to the Commission.

2.1.4. Consequences for notarial recording

Only at first glance does the de minimis rule make life easier for Notaries. By the addition of all aid, regardless in what form, during the last three fiscal years, even with a purchase price of under EUR 200,000 for the land and buildings there may be a grant on the part of the public authorities which leads to the limit being exceeded.

As in most cases the public authorities do not carry out a bidding procedure within the meaning of the Communication prior to the recording of land contracts and also, in accordance with current municipal practice, it is only in the rarest cases that an expert opinion is obtained, the question arises as to whether the Notary, in the case of the non-observance of the terms of the Commission Communication, must refuse to record the contract.

The Commission's Communication of 10.7.1997 does not represent a legislative act within the meaning of Article 249 of the Treaty that is directly binding in all Member States. Rather the Communication summarises present administrative practice and gives the Member States general guidance in respect of the notification obligation²⁵. For this reason the Communication itself cannot create **any direct obligations for the Notary**, even if the Notary is an organ of sovereign power. For these same reasons the Notary is also not obliged to obtain an expert opinion establishing market value. When the public authorities and the enterprise are not obliged to call in an expert, this applies all the more so in the case of the Notary.

On the other hand, the Notary cannot completely ignore the administrative practice of the Commission summarised in the Communication. If the requirements of the Communication are observed, the Notary can, as a rule,

assume that there is no aid requiring notification and accordingly no invalid contract. Conversely, an infringement of the Communication at least gives the Notary an indication that there may be a requirement to give notification. However, it is up to the recording Notary in the individual case as to whether, by virtue of such an infringement, he becomes convinced that the sale is taking place at below market value. **If the parties involved declare** in the deed itself, for example, that the sale is not taking place at below value, the Notary can rely on these actual statements by the parties. The situation is, of course, different if, instead of the agreed purchase price, for his valuation the Notary himself assumes a higher consideration, in his opinion, for the land²⁶.

Thus, if an infringement of the Communication still does not in itself compel the Notary to refuse recording, the question ultimately arises as to whether such non-compliance with the terms of the Communication at least leads to doubts on the part of the Notary regarding the validity of the legal transaction and whether in accordance with section 17 subsection 2 of the Notarial Recording Act (*Beurkundungsgesetz: BeurkG*) the Notary should note these doubts in the deed. The inclusion of such a **statement of doubt** does, however, lead to severe restrictions on the practical applicability of the deed²⁷. Therefore, here again it must also be up to the recording Notary in each individual case as to whether a departure from the terms of the Communication does lead to doubts about validity²⁸. As a rule this will not be the case if the parties declare that there is no aid involved which requires notification within the meaning of Article 87 et seq. of the EC Treaty²⁹.

21 Commission Regulation No. 69/2001 of 12.1.2001 on the application of Articles 87 and 88 of the EC Treaty to *de minimis* aid, OJ EU L 30/10, with effect from 1.1.2007 replaced by Regulation (EC) No. 1998/2006 of 15.12.2006, OJ EU L 379/5 of 28.12.2006.

Along with this so-called block exemption regulation there are two further provisions providing exemption from the notification requirement, namely Commission Regulation No. 70/2001 of 12.1.2001 on the application of Articles 87 and 88 of the EU Treaty to State aid to small and medium-sized enterprises (OJ EC L 10/33) and Council Regulation No. 68/2001 of 12.1.2001 on the application of Articles 87 and 88 of the EC Treaty to training aid (OJ EC L 10/20). Exemption in accordance with Regulation No. 70/2001 does, however, require in terms of Art. 7 thereof that either an application for aid has been submitted to national authorities by the beneficiary company or a right to aid exists on the basis of national provisions.

22 Art. 2 para. 2 Regulation No. 69/2001.

23 Art. 2 para. 2, Art. 3 paras. 1 and 5. of the recital to Regulation 69/2001.

24 Art. 2 para. 3 Regulation No. 69/2001.

25 See section I of the Communication.

26 Cf. section 20 subsection 1 sentence 2 Court Costs Act (KostO).

27 Cf. WINKLER (Footnote 1), section 17 BeurkG marginal No. 273.

28 This does not preclude the Notary from, for example, including a note in the deed in the event of non-compliance with the Communication to the effect that the Commission Communication of 10.7.1997 on State aid elements in sales of land and buildings by local authorities was pointed out to the parties and they declare in this regard that no aid is present which requires notification within the meaning of Article 88 et seq. EC.

29 In the event of non-compliance with the Communication the Notary may, for example, include a note in the deed to the effect that the Commission Communication of 10.7.1997 on State aid elements in sales of land and buildings by local authorities was pointed out to the parties.

2.2. Observance of public procurement law in relation to sales of property with construction obligations and land improvement contracts

Various ECJ decisions on EU public procurement law highlight possible consequences for land development contracts and sales of property with construction obligations by public authorities³⁰.

2.2.1. EU public procurement legislation and Remedies Directive

The Community legislator has regulated the award of public contracts in the Member States by a raft of directives on behalf of the Member States, regional administrative bodies and other public law organisations³¹. For public contracts that exceed certain thresholds, compliance with a particular procedure is prescribed, which, *inter alia*, involves publication of the invitation to tender, the time limits for submission of offers, disqualification of tenderers and the award criteria.

- In accordance with the latest **Public Procurement Directive**, which was actually to be implemented by 1.2.2006³², in the case of public supply and public service contracts the thresholds are EUR 162,000 and EUR 249,000 respectively, and in the case of public works contracts, the threshold is EUR 6,242,000.
- In order to ensure the implementation of these public procurement regulations, the so-called **Remedies Directive**³³ stipulates that in the event of breaches of Community law in the area of public procurement or of domestic regulations that are issued in implementation of this law, Member States must provide possibilities for an effective and prompt review in order that, *inter alia*, unlawful decisions can be set aside.

2.2.2. Alcatel: review process must be possible

In 1999 the ECJ decided in the **Alcatel**³⁴ case that, in accordance with Article 2 para. 1 a) and (b) of the Remedies Directive, the Member States are required to make the contracting authority's decision prior to the conclusion of the contract as to the bidder in a tender procedure with which it will conclude the contract open in all cases to a **review procedure**. It is thus, in particular, contrary to Community law if award and conclusion of the contract take place at the same time and as a result of the validity of the contract the unsuccessful bidder is then only able to claim damages.

2.2.3. SECAP and Coditel Brabant: tendering procedure and review proceedings also outside of the public procurement directives

In what has come to be the settled practice of the court, the ECJ is of the view that in relation to the award of contracts, the value of which is **below the threshold values** stipulated in the relevant directives³⁵, and in relation to the award of **public works and service concessions**³⁶ that are likewise not covered by the public procurement directives, the fundamental rules of the EU Treaty must nevertheless be observed.

In the case of public works and service concessions the agreed remuneration consists in the right of the concessionaire to economically exploit its own performance; the payment is therefore made by third parties. The concessionaire accordingly also assumes the operating risk associated with the works or services.

The **principle of equal treatment** and the prohibition on discrimination on grounds of nationality result in an obligation of transparency in particular in relation to contracts and concessions with cross-border significance.

- According to EU case law a works contract could, for example, be of **cross-border significance** because of its estimated value in conjunction with its technical complexity or the fact that the works are to be located in a place which is likely to attract the interest of foreign operators from other Member States³⁷.
- For the benefit of any potential tenderer, there must then be a **degree of advertising** sufficient to enable the service concession to be opened up to competition and the impartiality of procurement procedures to be **reviewed**. It is for the concession-granting public authority to evaluate, subject to review by the competent courts, whether the detailed arrangements of the call for competition are appropriate. However, a complete lack of any call for competition does not comply with the requirements of Articles 43 EC and 49 EC any more than with the principles of equal treatment, non-discrimination and transparency³⁸.

2.2.4. Implementation in Germany

The provisions of the Public Procurement Directives and of the Remedies Directive have been implemented in **Germany** in sections 97 et seq. of the Law Against Restraints on Com-

30 Observance of public procurement law in connection with company transformations is not dealt with here. See in this regard SUPPLIET, *Ausgliederung nach § 68 UmwG* (Spin-off under section 168 UmwG) – German Transformation Act), 2005, p. 81.

31 The Directive, still originating partly from 1971, was replaced by Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors (Official Journal EC L 134, 1) and Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts (OJ EC L 134, 114).

32 Germany has as yet not implemented this Directive in national law. Under the previous directive the limits were, in the case of public service contracts, EUR 200,000 and in the case of public works contracts, EUR 5 million.

33 Council Directive 89/665/EEC of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts, OJ L 395, 33.

34 ECJ, judgment of 28.10.1999, C-81/98 (*Alcatel*), [1999] ECR I-7671, marginal No. 43.

35 See, for example ECJ, judgment of 15.5.2008, cases C-147/06 and C-148/06 (*SECAP*), not yet published in the official court reports, with further references.

36 ECJ, judgment of 13.9.2007, case C-260/04 (*Commission/Italy*), European Court Reports 2007, I-7083, paragraph 22 et seq.; ECJ, judgment of 13.11.2008, case C-324/07 (*Coditel Brabant*), not yet published in the official court reports.

37 ECJ, judgment of 15.5.2008, cases C-147/06 and C-148/06 (*SECAP*), op cit., paragraph 24.

38 ECJ, judgment of 13.10.2005, case C-458/03 (*Parking Brixen*), European Court Reports 2005, I-8612, paragraph 50.

petition (Gesetz gegen Wettbewerbsbeschränkungen: GWB). Section 13 of the Public Procurement Regulations (Vergabeverordnung: VgV) issued on the basis of the authority contained in section 97 subsection 6 GWB stipulates, *inter alia*, that public contracting entities must inform bidders whose tenders will not be considered of the name of the tenderer to whom the contract is to be awarded and of the reasons for the intended non-consideration of their tenders by no later than 14 days prior to conclusion of the contract. In terms of section 13 sentence 4 old version or sentence 6 new version, a contract concluded prior to expiry of the 14 day period or without the information being issued is null and void.

According to a judgment by the BGH from 2005, however, the general nullity of the contract which is brought about as a result of the award, even if no insufficiently informed unsuccessful bidder demands legal redress against the contract award decision, goes beyond what the purpose of the rule demands in light of the Alcatel case³⁹. According to the BGH, a restrictive interpretation based on the purpose of the law is therefore necessary in relation to section 13 page 6 VgV. Nullity of the conclusion of contract created by the award as a rule only occurs, according to the BGH, if an unsuccessful bidder whose rights to information have been infringed claims that his rights to information have been infringed and applies for a review procedure. The initial case at the basis of the BGH judgment involved the public contracting authority's application for damages on account of non-performance of the contract. The tenderer tried to defend itself on the basis of the lack of notification to the unsuccessful bidder and the nullity resulting from this. In a situation such as this, at least, it appears justified to disallow the originally preferred tenderer from invoking the nullity of the contract.

In my opinion, however, the general conclusion of the BGH, that a contract is only to be null and void if it is challenged by the unsuccessful bidder, deprives the Community law of some of its effect. The validity of the contract makes implementation of the work contracted for legally binding. Implementation of the contract and lapse of interest in performance thus become all the more likely. At the same time a new, properly conducted invitation to tender becomes less likely. If, after performance of the work contracted for, an unsuccessful bidder subsequently challenges the contract award, the only way remaining open to him is that of compensation. This applies all the more so if no invitation to tender takes place at all and the competitor only learns of the contract award by chance. According to the ECJ this compensation is not, however, sufficient to penalise the lack of a public procurement procedure. In the view of the BGH it would therefore have been at least advisable to obtain a preliminary ruling from the ECJ on this point.

Even if one were to follow the BGH and give section 13 sentence 6 VgV a restricted interpretation, this means for the recording Notary that in the case of a deed which contains a public sector contract award above the thresholds mentioned, the nullity of the contract must be contemplated.

2.2.5. *La Scala Milan*: public procurement procedure necessary for development contract

In 2001, the ECJ decided in a reference for a preliminary ruling, which concerned the renovation of **La Scala in Milan**⁴⁰ and the building of an annex during the renovation, that the conclusion of a development contract in accordance with Italian law also falls within the Public Procurement Directive. According to the ECJ, in the case of such development contracts either the local authority

must carry out the public procurement procedures itself or must require the public infrastructure provider, under the agreements concluded with it, to carry out the work contracted for in accordance with the procedures laid down in the Public Procurement Directive.

Under **Italian law** the local authority is permitted to grant permission for the construction of a complex of buildings on the basis of a development plan only after conclusion of a contract which must, *inter alia*, include the transfer free of charge of the areas of land required for the secondary infrastructure works⁴¹. Under Article 4(2) of Law No 847/64⁴², secondary infrastructure works comprise pre-school facilities; primary and secondary schools; buildings and campuses to accommodate higher and further education facilities; local markets; municipal branch offices; churches and other religious buildings; local sports facilities; community centres; cultural and health and fitness facilities, and local parks and gardens.

2.2.6. *Auroux and others v Municipality of Roanne*: tendering procedures necessary without acquisition of property by the public authority

Continuing its previous practice, the ECJ ruled in 2007 on a submission by the *Tribunal administratif de Lyon* that in the case of a public development agreement concluded under French law, public procurement law must be observed even where the contracting authority is not nor will become the owner of all or part of the work⁴³.

Facts of the case: the agreement between the municipality of Roanne and a public-private company as contractor provided for the construction of a leisure centre including a multiplex cinema, commercial premises and other structures such as car parks and access roads. The contractor was to acquire the relevant plots of land and have the works carried out. The constructed plots of land were to be sold by the contractor to third parties. The car parks and the areas of land not yet sold at the time the closing balance sheet was drawn up were to be transferred into the ownership of the municipality. The municipality was to contribute several million euros towards the financing of the project, paying among other things, around €8 million for the works not yet sold and €2.95 million for the transfer of the car park.

The French Government in particular argued that there was no public works contract as the works were intended

39 BGH, Judgment of 22.2.2005 – KZR 36/03, BauR 2005, 1026 = DB 2005, 1380 = NVwZ 2005, 845; all judgments of the BGH from 2000 onwards can also be accessed on the internet under: www.bundesgerichtshof.de.

40 ECJ, Judgment of 12.7.2001, C-399/98 (*Ordine degli Architetti and others*), [2001] ECR I-5409.

41 Section 28 subsection 5 of Law No. 1150 of 17th August 1942 on Town Planning (*Legge urbanistica*, GURI No. 244 of 17th August 1942) as amended by Framework Law No. 765 of 6th August 1967.

42 Law No. 847 of 29th September 1964 on the power of local authorities and local authority associations to raise loans for the acquisition of plots of land pursuant to Law No. 167 of 18th April 1962 (*Legge n° 847, autorizzazione ai Comuni e loro consorzi a contrarre mutui per l'acquisizione delle aree ai sensi della legge 18 aprile 1962, n° 167*), amended by Article 44 of Law No. 865 of 22nd January 1971 and Article 17 of Law No. 67 of 11th March 1988.

43 ECJ, judgment of 18.1.2007, case C-220/05 (*Jean Auroux and others versus the municipality of Roanne*), European Court Reports 2007, I-385.

for sale to third parties and accordingly they did not correspond to the municipality's requirements. The acquisition of the car park essentially involved the sale of works yet to be constructed.

The ECJ rejected this argument and ruled that the applicability of the public procurement law does not depend on the question of whether the contracting authority will become **owner of the works**.

- The court held that the leisure centre was a work within the meaning of Article 1 (c) of the Public Works Directive⁴⁴ that fulfils an economic function, namely commercial and service activities.
- The municipality acted as the contracting authority and the public-private company as contractor.
- According to the ECJ the public development agreement was concluded for pecuniary interest as the municipality at least paid a sum for the transfer of the car park. The service elements included in the agreement such as the acquisition of land, obtaining finance, organising an architecture and/or engineering competition and marketing the buildings are, according to the ECJ, part of the main purpose of the agreement, the completion of the work.

In relation to another question from the *Tribunal administratif de Lyon* the ECJ ruled in the same case that it is irrelevant for the applicability of the tendering procedures for the award of public works contracts that the **contractor itself is obliged** as a contracting authority to **observe the procedures for the award of public works contracts**. No such exemption from the applicability of the directive is provided for in the Directive. Otherwise there would be the risk that with successive individual contracts the subcontracts would in each case lie below the threshold and the application of the Directive could thus be avoided.

By contrast the **European Commission** held in other proceedings that a simple agreement giving the public authority a repurchase right without any legally binding obligation to execute works did not give rise to the applicability of the law on public procurement. The Commission therefore closed infringement proceedings against Germany⁴⁵.

2.2.7. Higher Regional Court of Appeal Düsseldorf: tendering procedures necessary in relation to the sale of property with a construction obligation

The Awards Senate of the OLG (*Oberlandesgericht* - Higher Regional Court of Appeal) Düsseldorf used the ECJ ruling in the *Roanne* case as the basis for a series of decisions requiring observance of the public procurement law in the case of sales of property by public authorities, at least where a **construction obligation on the part of the acquirer** is agreed at the same time⁴⁶.

The **German legislature** corrected what it viewed as the excessively wide ruling of the OLG Düsseldorf by an amendment of the national public procurement law⁴⁷.

Probably as a reaction to the foregoing amendment of the GWB (Law against Unfair Competition), by ruling

dated 2.10.2008⁴⁸ the OLG Düsseldorf submitted the following questions to the **ECJ**:

1. Is it a requirement, in order for there to be a public works contract under Art. 1(2)(b) of European Parliament and Council Directive 2004/18/EC of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, that the works be physically carried out for the public contracting authority and bring it an **immediate economic benefit**?
2. In so far as, according to the definition of a public works contract in Article 1(2)(b) of Directive 2004/18/EC, the element of procurement is indispensable: Is procurement to be regarded as having taken place, in accordance with the second variant of the provision, if the intended works for the public contracting authority fulfil a **particular public purpose** (for example the development of part of a town) and the public contracting authority has the legal right under the contract to ensure that the public purpose is achieved and that the necessary works will be available?
3. Does the concept of a public works contract in accordance with the first and second variants of Article 1(2)(b) of Directive 2004/18/EC require that the contractor be directly or indirectly obliged to provide the works. If so, must there be a legally enforceable obligation?
4. Does the concept of a public works contract in accordance with the third variant of Article 1(2)(b) of Directive 2004/18/EC require that the contractor be obliged to carry out works, or that works form the subject-matter of the contract?
5. Do contracts by which, through the requirements specified by the public contracting authority, it is intended to ensure that the works to be carried out for a particular

44 In the specific case Council Directive 93/37/EEC of 14.6.1993 concerning the coordination of procedures for the award of public works contracts (OJ L 199, p. 54) in the version amended by the European Parliament and Council Directive 97/52/EC of 13.10.1997 (OJ L 328, p. 1).

45 Decision of 5.6.2008, IP/08/867 (*Stadtwerke Flensburg*).

46 OLG Düsseldorf, decision of 13.6.2007 – VII-Verg 2/07 (*Fliegerhorst-Alhorn*), NZBau [Neue Zeitschrift für Baurecht und Vergaberecht = *New Journal for Construction Law and Procurement Law*] 2007, 530 = VergabeR [Vergaberecht = *Procurement Law*] 2007, 406 = VergabeR 2007, 634 = ZfIR [Zeitschrift für Immobilienrecht = *Journal of Property Law*] 2007, 859 with annotations. Grziwotz; decision of 12.2.2007 – VII VerG 30/07 (*Wuppertal-Vohwinkel*), NZBau 2008, 138 = VergabeR 2008, 99 = ZfBR [Zeitschrift für deutsches und internationales Bau- und Vergaberecht = *Journal for German and International Construction and Procurement Law*] 2008, 207; ruling of 6.2.2008 – VII VerG 37/07 (*Oer-Erkenschwick*), IBR [Immobilien- und Baurecht, Recht für die Immobilienverwaltung = *Real Estate and Construction Law*] 2008, 169 = KommJur [Kommunaljurist = *Municipal Lawyer*] 2008, 188 = NZBau 2008, 271 = VergabeR 2008, 229 = ZfIR 2008, 254).

47 Amendment of sections 99 (3) and (6) GWB (Gesetz gegen Wettbewerbsbeschränkungen = Law against Unfair Competition) by the Law to modernise the law of public procurement (Gesetz zur Modernisierung des Vergaberechts). Cf. Government Draft Bill, BR-Drucks. [Bundesrat offprint] 349/08 of 2.5.2008 = BT-Drucks. [Bundestag offprint] 16/10117 of 13.8.2008; Resolution Recommendation and Report of the Economy and Technology Committee, BT-Drucks. 16/11428 of 17.12.2008; Parliamentary Resolution, BR-Drucks. 35/09 of 23.1.2009. At the time of the copy deadline the Bundesrat had already approved but not yet promulgated the law.

48 OLG Düsseldorf, decision of 2.10.2008, Verg 25/08, NZBau 2008, p. 727. The proceedings are being brought in the ECJ as case C-451/08 (*Helmut Müller*).

public purpose be available, and by which (by contractual stipulation) the contracting body is given the legal power to ensure (in its own indirect interest) the availability of the works for the public purpose, fall within the third variant of Article 1(2)(b) of Directive 2004/18/EC?

6. Is the concept of 'requirements specified by the contracting authority' in Article 1(2)(b) of Directive 2004/18/EC fulfilled, if the works are to be carried out in accordance with plans examined and approved by the public contracting authority?
7. Must there be held to be no public works concession under Article 1(3) of Directive 2004/18/EC, if the **concessionaire** is or will become the **owner of the land** on which the works are to be carried out, or the concession is granted for an indeterminate period?
8. Does Directive 2004/18/EC – with the legal consequence of an obligation on the public contracting authority to invite tenders – apply if a sale of land by a third party and the award of a public works contract take place at different times and on the conclusion of the land sale the public works contract has not yet been awarded, but at the last-mentioned time there was, on the part of the public authority, the intention to award such a contract?
9. Are separate but related transactions concerning a sale of land and a public works contract to be regarded from the point of view of the law on the awarding of contracts as a unity, if at the time the land sale contract was entered into the award of a public works contract was intended and the participants deliberately created a close connection between the contracts from a substantive – and possibly also temporal – point of view (see Case C 29/04 *Commission v Austria* [2005] I 9722)?

The ECJ will thus have the opportunity to further develop its case law.

2.2.8. *pressetext Nachrichtenagentur*: new call for competition only in the case of material contractual amendment

It is only mentioned in passing here that in its decision in *pressetext*⁴⁹ the ECJ commented on the conditions under which amendments to an existing contract between a contracting authority and a service provider are to be regarded as a new award of contract within the meaning of Directive 92/50⁵⁰. The court stated that a new award of contract is necessary when the terms of the public contract are **materially different in character** from the original contract and thereby demonstrate the intention of the parties to renegotiate the essential terms of the contract.

- According to the ECJ an amendment may be regarded as material when it introduces conditions which, had they been part of the initial award procedure, would have allowed for the admission of tenderers other than those initially admitted or the acceptance an offer other than the originally accepted offer.
- An amendment may also be regarded as material when it extends the scope of the contract considerably to encompass services not initially covered or when it changes the economic balance of the contract in favour of the contractor in a manner not provided for in the initial contract.

In the specific case the ECJ regarded the transfer of the contract to a wholly-owned subsidiary of the original contractor as an internal reorganisation and not as a material

contractual amendment. In the view of the ECJ a subsequent waiver of the right to terminate the contract in favour of the contractor for the period of three years also did not represent a material contractual amendment in the case of a contract originally concluded for an unlimited period.

2.2.9. Consequences for notarial recording

The ECJ decisions discussed above and the decisions of the OLG Dusseldorf have considerable consequences for notarial practice. If the line taken by the OLG Dusseldorf should achieve acceptance and be confirmed by the ECJ, which it is likely to happen in my view, the risk of nullity exists not only in relation to land improvement contracts but also in relation to sales of property with a construction obligation.

The **threshold of EUR 6,242,000**, or at an earlier stage EUR 5 million, in relation to public works contracts does, of course, reduce the problem to major municipal or state projects. Nonetheless, in view of the trend towards public/private partnership and the increasing privatisation of formerly municipal or state facilities, the practical importance of this must not be underestimated.

- In land improvement contracts, in contrast to the situation in relation to the level of aid, the order volume is not difficult for the recording Notary to ascertain; the total expenditure by the public infrastructure provider corresponds to the amount for assessment of the underlying transaction value⁵¹. In my opinion, in the case of corresponding public works contracts, the Notary might therefore be obliged to point out the public procurement regulations. Otherwise, because of the terms of section 13 sentence 6 VgV, there is a risk that the deed will be invalid or, according to the BGH, at least subject to subsequent challenge⁵².
- In the case of **sales of property** by public authorities with a construction obligation, identifying that the threshold has been reached is, however, only possible from the information of the parties involved.
- It is also only with difficulty that the notary can judge whether a contract has **cross-border significance**. As a safeguard it is recommended, for example, that a passage be included in the contract which states that after being advised on the law on public procurement the contracting authority declares that the provisions of the law on public procurement have been observed or that the relevant thresholds under national and Community law have not been reached and that the contract does not have cross-border significance.

49 ECJ, judgment of 19.6.2008, case C-454/06 (*pressetext Nachrichtenagentur GmbH/Republic of Austria and others*), not yet published in the official court reports, with annotations NIESTADT/HÖLZL, *Um Kleinigkeiten kümmert sich der Prätor nicht!* (The magistrate has no regard for trifles), NJW [Neue Juristische Wochenschrift = *New Weekly Law Journal*] 2008, p. 3321 et seq.

50 Council Directive 92/50/EEC of 18.06.1992 relating to the coordination of procedures for the award of public service contracts, OJ L 209, p. 1.

51 KORINTENBERG, *Kostenordnung* (KostO) (Costs in Non-Contentious Matters Act), 16th edition. 2005, section 39, marginal No. 37.

52 As here also GRZIWOTZ, in: *Beck'sches Notar-Handbuch*, 4th edition 2006, A XI, marginal No. 29 at the end.

2.3. Permissibility of authorisation requirements in the case of cross-border property acquisition

The legal systems of the Member States provide various planning permission, notification and disclosure requirements in respect of the acquisition of real property. In relation to the acquisition of properties by EU foreigners or by companies which are subject to the law of another Member State, these regulations are coming under the spotlight of Community law. Particular suspicion on the part of the EU Commission is aroused by regulations which affect particular EU foreigners.

2.3.1. Relevant fundamental freedoms

The ECJ stated its position on the unequal treatment of EU citizens in connection with the acquisition of property as early as 1988⁵³. Since then the Court of Justice has further fleshed out the admissibility criteria of such restrictions⁵⁴.

- According to the case law of the ECJ, restrictions on the acquisition of property must satisfy the measures of **freedom of movement of workers, freedom to provide services and freedom of establishment** and also free movement of capital⁵⁵. According to the ECJ, the right to acquire, use and dispose of immovable property in another Member State represents a necessary addition to this fundamental freedom⁵⁶. This can be seen particularly from Article 44 (2) (e) EU (previously Article 54 (3) (e) EEC Treaty), which confers upon the Council and the Commission the task of abolishing restrictions on the acquisition of immovable property in order to produce freedom of establishment, and from the General Programmes for the Abolition of Restrictions on Freedom of Establishment and Freedom to Provide Services⁵⁷. On account of these express provisions even Article 295 EU (previously Article 222 EEC Treaty), in accordance with which the EU Treaty leaves the system of property ownership in the various member states unaffected, is not an obstacle⁵⁸. Secondary residences can also fall within the scope of protection of the fundamental freedoms⁵⁹.
- In addition, the acquisition of immovable property falls within the scope of application of **free movement of capital** in accordance with Article 56 et seq. EU Treaty (previously Article 73b et seq. EEC Treaty)⁶⁰. As a consequence of Annexe I to Directive 88/366⁶¹, which continues in this respect to be valid⁶², the movement of capital also includes all legal transactions by which non-residents undertake investment in immovable property. The scope of application of free movement of capital thereby also comes into play when other fundamental freedoms are not applicable. Every acquisition of immovable property by an EU citizen in another Member State thus at least falls within the scope of application of free movement of capital⁶³.

2.3.2. Prohibition of discrimination

The fundamental freedoms prohibit as materialisation of the general prohibition of discrimination under Article

12 EU (previously Article 6 EEC Treaty) both **overt discrimination**, which is linked to nationality, and also **covert discrimination**, which is linked in form to other criteria which, however, can typically only be fulfilled or not fulfilled as the case may be by the Member State's own nationals, such as, for example, place of residence or seat of a company⁶⁴.

According to ECJ case law, discriminatory restrictions are only permissible on grounds of **public policy, public security or public health**.

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- 53 ECJ, judgment of 14.1.1988, C-63/86 (*Commission v Italy*), [1989] ECR 29 et seq.
 - 54 See most recently judgment of the Court of Justice of 1.12.2005, C-213/04 (*Burtscher*), [2005] ECR I-10309.
 - 55 ECJ, judgment of 1.6.1999, C-302/97 (*Konle*), [1999] ECR I-3099, marginal No. 22.
 - 56 ECJ, judgment of 30.5.1989, C-305/87 (*Commission v Greece*), [1989] ECR 1461, marginal Nos. 19, 22, 24.
 - 57 General Programme for the Abolition of Restrictions on Freedom of Establishment of 18.12.1961, OJ 1962, 36 and General Programme for the Abolition of Restrictions on Freedom of Establishment of 18.12.1961, OJ 1962, 32.
 - 58 ECJ, judgment of 6.11.1984, C-182/83 (*Fearon*), [1984] ECR 3677, marginal No. 6 et seq; judgment of 1.6.1999, C-302/97, (*Konle*), op cit., marginal No. 38.
 - 59 ECJ, judgment of 14.1.1988, C-63/86 (*Commission v Italy*), [1989] ECR 29, marginal No. 19, judgment of 16.6.1992, C-351/90 (*Commission v Luxembourg*), [1992] ECR I-3945, marginal No. 12.
 - 60 ECJ, Judgment of 1.6.1999, C-302/97 (*Konle*), op cit, marginal No. 22.
 - 61 ECJ, Judgment of 16.3.1999, C-222/97 (*Trummer*), [1999] ECR I-1661, marginal No. 21.
 - 62 Nomenclature for Capital Movements, Annexe I to Council Directive 88/361 of 24.6.1988 in implementation of Article 67 of the Treaty (OJ L 178, 5).
 - 63 Alongside these provisions of primary law, the acquisition of immovable property is also covered by several provisions of secondary law. Art. 9 (1) of Council Directive No. 1612/68 (Regulation (EEC) No 1612/68 of 15 October 1968 on freedom of movement for workers within the Community (OJ L 257, 2) provides that workers who are nationals of a Member State and who are employed in the territory of another Member State shall enjoy all the rights and benefits accorded to national workers in matters of housing, including ownership of the housing they require. In accordance with Article 1 (1) of Directive 90/364 (Council Directive of 28.6.1990 on the right of residence (90/364), OJ L 180 of 13.7.1990, 26 et seq.) Member States shall grant the right of residence to nationals of Member States who do not enjoy this right under other provisions of Community law and to members of their families provided that they themselves and the members of their families are covered by sickness insurance and have sufficient means of subsistence. The same right is conferred by Article 1 of Directive 90/365 (Council Directive of 28.06.1990 on the right of residence for employees and self-employed persons who have ceased their occupational activity (90/365), OJ L 180 of 13.7.1990, 28 et seq.) on former employees and self-employed persons with old age pensions of a sufficient amount to ensure their subsistence and to members of their families. Finally, reference must also be made to Directive 93/96 (Arts. 1 and 2 of Council Directive of 29.10.1993 on the right of residence of students (93/96), OJ EC L 317, 59 et seq.) which extends the right of residence to students and their family members.
 - 64 See, for example, judgments by the Court of Justice of 12.2.1974, C-152/73 (*Sotgiu*), [1974] ECR 153, marginal No. 11 et seq. (on free movement of workers; of 28.4.1977, C- 71/76 (*Thierry*), [1977, 765,] ECR marginal No. 13 (on freedom of establishment); of 18.3.1980, C-62/79 (*Coditel*), [1980] ECR 88, marginal No. 15 and of 22.1.1998, C-266/96 (*Corsica Ferries*), [1998] ECR I-3949, 4000, marginal No. 56 (on freedom to provide services).

2.3.3. Proportionality in the case of non-discriminatory restrictions

Non-discriminatory restrictions on the acquisition of immovable property can, on the other hand, be justified if they meet objectives which are in the **general interest**, such as town and country planning, protection of regional economic infrastructure⁶⁵, prevention of land speculation⁶⁶ or the preservation of viable agricultural operations⁶⁷.

In addition, both overt and covert restrictions must be capable, in accordance with the **proportionality principle**, of ensuring realisation of the objectives they pursue; they must not go beyond what is necessary for attaining this objective⁶⁸ and they must be in reasonable proportion to the objectives sought.

2.3.4. Particular authorisation and notification requirements

The ECJ has in particular ruled in relation to prior **authorisation requirements** in the case of immovable property purchases by EU foreigners that such authorisation requirements are not permitted to cause the exercise of fundamental freedom to be subject to the discretion of the administrative authorities and thus be such as to render, for example, the exercise of the free movement of capital illusory⁶⁹. Such an authorisation requirement is thus not permissible if the objectives pursued by it could also be achieved by means of an appropriate notification system. Thus in 1999 the ECJ regarded the system still existing at that time in Tyrol of prior authorisation in relation to the purchase of built-on plots of land as disproportionate, as a system of prior written declaration by the purchaser with the possibility of subsequent intervention by the authorities in the event of non-compliance represented a less restrictive means of achieving the objectives of land planning and strengthening the regional economy (**Konle** case⁷⁰). By its judgment of 5.3.2002 concerning the Salzburg regulations in the case of **Reisch**⁷¹ and also its judgment of 15.05.2003 concerning the Vorarlberg Land Transfer Act in the case of **Salzmann**⁷², the ECJ continued this line of case law and made it clear that a system requiring prior authorisation is also disproportionate in the case of unbuilt plots of building land.

Further, the ECJ already previously ruled that the requirement of authorisation in Italy in relation to the purchase of plots of land in particular coastal regions and tourist areas by non-Italians, which the Italian legislator justified on the grounds of national defence, is not compatible with free movement of capital⁷³. According to the ECJ, the position would be different only if it could be demonstrated to the national court that non-discriminatory treatment of the nationals of all the Member States would expose the military interests of the Member State concerned to real, specific and serious risks which could not be countered by less restrictive procedures.

Also in respect of the less restrictive **notification procedure** the ECJ recently advocated the view that the sanction of the retroactive invalidity of the purchase contract in the event of late submission of the requisite noti-

fication by an EU foreigner was not in reasonable proportion to the objective pursued of preventing illegal use of plots of land for holiday purposes⁷⁴. Such regulations are accordingly also invalid.

Alongside second homes, restrictions upon the acquisition of agricultural property have also been the focus of recent ECJ rulings:

In the case of **Ospelt and Schlössle Weissenberg**⁷⁵ the ECJ stated its position on the authorisation requirement for agricultural and forestry plots of land pursuant to the Vorarlberg Land Transfer Act. These proceedings are not only of significance for Notaries but also illustrate how far Community law has made inroads into the property ownership systems of the Member States.

Facts of the case: In the *Ospelt* proceedings, the Land Transfer Commission of the Land of Vorarlberg (*Grundverkehrs-Landeskommission des Landes Vorarlberg*) refused to allow the transfer of agricultural and forestry operations with an area of around 43 hectares, also including a castle, to a foundation domiciled in Liechtenstein. The owner herself, who was also a Liechtenstein national, resided in the castle. Most of the agricultural and forestry plots were leased to third parties. The beneficiary of the foundation was the owner of the property. The purpose of the transfer to the foundation was to prevent any division caused through inheritance of the family property. The foundation declared to the authorisation authority that its intention was that the plots of land should continue to be leased to the same farmers as before. The Vorarlberg Land Transfer Act (VGVG) did not stipulate any special authorisation requirement in relation to agricultural and forestry plots for acquisition by non-Austrians, but did lay down a general authorisation requirement. Authorisation in accordance with section 5 VGVG could only be granted if the acquirer himself cultivated the plot as part of an agricultural establishment and also had his permanent place of residence there. Since the property was not cultivated by the owner itself as the land was leased and since the foundation, as a corporation, also had no place of residence within the meaning of the Vorarlberg Regulations on the holding, authorisation was refused.

On the basis of Article 40 of the EEA Agreement, the principle of free movement of capital contained in Community

65 ECJ, judgment of 1.6.1999, C-302/97 (*Konle*), op cit., marginal No. 40.

66 ECJ, judgment of 6.11.1984, C-182/83 (*Fearon*), op cit., marginal No. 3 et seq.

67 ECJ, judgment of 23.9.2003, C-452/01 (*Ospelt*), [2003] ECR I-9743, marginal No. 39.

68 ECJ, judgment of 30.11.1995, C-55/94 (*Gebhard*), [1995] ECR I-4165, marginal No. 37.

69 ECJ, judgments of 23.2.1995, C-358/93 and C-416/93 (*Bordessa*), [1995] ECR I-361, marginal No. 25; of 14.12.1995, C-163/94, C-165/99 and C-250/94 (*Sanz de Lera*), [1995] ECR I-4821, marginal No. 25; of 1.6.1999, C-302/97 (*Konle*) op cit., marginal No. 44.

70 ECJ, judgment of 1.6.1999, Rs. C-302/97 (*Konle*), op cit., marginal No. 46 et seq. The exemption for secondary residences negotiated for Austria at the time of its accession to the EU only covered the legal situation on 1.1.1995. Most of the Austrian regulations were, however, further tightened after 1995.

71 ECJ, judgment of 5.3.2002, C-515/99, C-519/99 to C-524/99 and C-526/99 to C-540/99 (*Reisch*), [2002] ECR I-2157.

72 ECJ, judgment of 15.5.2003, C-300/01 (*Salzmann*), [2003] ECR I-4899.

73 ECJ, judgment of 13.7.2000, C-423/98 (*Albore*), [2000] ECR I-5965.

74 ECJ, judgment of 1.12.2005, C-213/04 (*Burtscher*), op cit., marginal No. 53 et seq.

75 ECJ, judgment of 23.9.2003, C-452/01 (*Ospelt*), op cit.

law also applies in legal relations between nationals of Member States of the EEA, which also includes the Principality of Liechtenstein, and the EU States.

In reviewing the compatibility of the Vorarlberg regulations with free movement of capital, the ECJ firstly held that the requirement as to residence was not in this case, a priori, discriminatory in nature⁷⁶ as the unequal treatment took place not on the basis of nationality but with the specific objective of preserving agricultural communities and viable farming establishments⁷⁷.

On the matter of the proportionality of the authorisation requirement the ECJ explained that, unlike in the case of holiday residences, subsequent supervision by the authorities could not ensure the same guarantee as a prior authorisation requirement that excludes the discontinuation of the cultivation of agricultural plots and thereby ensures their long-term use for farming needs⁷⁸. Subsequent annulment by the courts would lead to delays in cultivation and legal certainty, which is one of the most importance concerns of any system of land transfer, would be undermined.

According to the ECJ, the condition of authorisation that the landowner cultivates the land himself and takes residence there is, however, not permissible if the land that is being transferred is, at the moment of sale, farmed by a tenant farmer rather than the landowner and the new owner who likewise would not farm the property and would not be resident on the land has undertaken to continue to have the land farmed by the same tenant⁷⁹. The objective of preserving a viable agricultural community can, according to the ECJ, be achieved through less restrictive measures. The transfer of agricultural land to a legal person could, for instance, be made subject to the obligation that it be let on a long lease. According to the ECJ, mechanisms could also be put in place giving a right of first refusal to tenants which would make it possible, where the latter did not acquire the property, for title to be acquired by non-farming owners who would undertake to keep the land in agricultural use.

In the Vorarlberg case the ECJ salvaged the statutory regulation insofar as it considered it possible to find an **interpretation which was in conformity with the directive** and obliged the national authorities in the initial situation to grant authorisation.

In the **Festersen**⁸⁰ case the ECJ applied the aforementioned practice to the **Danish Agriculture Act** in terms of which the acquisition of agricultural property is dependent on the establishment of the acquirer's fixed residence on the property.

The **legal policy objective** of this provision is, according to the Danish Government's submission to the ECJ, to preserve the farming of agricultural land by means of owner-occupancy, to preserve a permanent agricultural community and to avoid pressure on the property market.

After finding that there was no direct discrimination according to nationality, the ECJ did, however, hold that in these objectives in the public interest there was a **breach of the principle of proportionality**. The residence requirement was not an appropriate means of ensuring traditional farming by the owner as, under the Danish Agriculture Act, the obli-

gation to farm the land does not apply to areas of less than 30 hectares. Also, the objective of preserving the agricultural community cannot be attained by means of the residency obligation as it might be necessary for the viability of the farming operations for a farmer already living on another farm to acquire additional areas. Finally, pressure on property prices could, the court admitted, be prevented by the residence requirement; however, in the view of the court, other less drastic measures are available, such as state regulation of property prices, incentives to lease residences acquired on agricultural property, higher taxes on resale of land occurring shortly after acquisition or the requirement of a substantial minimum duration for leases of agricultural land⁸¹.

2.4. Implications of cancellation in the case of doorstep transactions on the notarial purchase contract

The requirements for and consequences of a cancellation under the Doorstep Selling Directive⁸² has occupied the ECJ repeatedly in recent years. From a notarial point of view the effects of a cancellation of credit agreements on the notarial purchase contract are of particular interest.

2.4.1. Heininger: right of cancellation

The **Doorstep Sales Directive** obliges the Member States in Article 5 to grant the consumer, *inter alia*, a right of cancellation in respect of contracts which are concluded during a visit by a trader to the consumer's home or to the home of another consumer. In accordance with Article 3 (2) a) the directive does not, however, apply to contracts for the construction, sale and rental of immovable property or to contracts concerning other rights relating to immovable property.

The **German Law on the cancellation of doorstep transactions** (*Haustürwiderrufgesetz: HWiG*), on the other hand, initially did not give the consumer a right of cancellation in the case of secured credit agreements but only permitted cancellation in accordance with the German Consumer Credit Act (*Verbraucherkreditgesetz: VerbrKrG*).

In its judgment of 13.12.2001 in the case of **Heininger**⁸³, however, the ECJ interpreted the doorstep sales directive to the effect that the directive on mortgage credit agreements, i.e. on credit agreements which were concluded for financing a property purchase, is applicable. Even if such a contract is linked to a right relating to immovable property because the credit granted must be secured by means of a charge on immovable property, in the opinion of the ECJ that feature is not sufficient for the

76 ECJ, judgment of 23.9.2003, C-452/01 (*Ospelt*), op cit., marginal No. 37.

77 Cf. also ECJ, judgment of 6.11.1984, C-182/83 (*Fearon*), [1984] ECR 3677, in which the ECJ held that an Irish regulation on the expropriation of agricultural property from owners who did not have their place of residence on the property was permissible.

78 ECJ, judgment of 23.9.2003, C-452/01 (*Ospelt*), op cit., marginal No. 43 et seq.

79 ECJ, judgment of 23.9.2003, C-452/01 (*Ospelt*), op cit., marginal No. 51.

80 ECJ, judgment of 25.1.2007, case C-370/05 (*Festersen*), European Court Reports 2007, I-1129.

81 ECJ, judgment of 25.1.2007, case C-370/05 (*Festersen*), op cit., marginal No. 29 et seq.

82 Council Directive 85/557/EEC of 20 December 1985 to protect the consumer in respect of contracts negotiated away from business premises, OJ L 372, 31.

83 ECJ, judgment of 13.12.2001, C-481/99 (*Heininger*), [2001] ECR I 9945, marginal No. 32 et seq.

agreement to be regarded as concerning a right relating to immovable property for the purposes of Article 3 (2) a) of the directive. Accordingly the consumer has a right of cancellation in respect of the credit agreement in accordance with Article 5 of the directive where the consumer has not been given information regarding the right of cancellation. The effects of such a cancellation of the credit agreement on the purchase contract in respect of the property and on the creation of the charge on immovable property are, however, according to the ECJ governed by the relevant national law.

The **BGH** subsequently granted the consumer a right of cancellation but took the view that by virtue of section 3 (2) No. 2 of the VerbrKrG, section 9 of the VerbrKrG is not applicable to secured credit agreements⁸⁴ and that the secured credit agreement and financed property transaction do not amount to linked agreements to be regarded as a single economic unit within the meaning of section 9 of the VerbrKrG. According to the settled case law of the BGH, even lay persons who are legally uninformed and inexperienced in business know that the lender and the seller of the property are generally different people. The legislator took this into account by specifying in section 3 (2) No. 2 of the VerbrKrG that the provisions regarding linked transactions for secured lending within the meaning of section 3 (2) No. 2 of the VerbrKrG (*Note: it would seem likely that section 9 is intended here*) do not apply. Cancellation of the secured credit agreement therefore does not, in principle, affect the validity of the purchase contract for the immovable property.

In a judgment on 12.11.2002 the 11th Senate of the BGH further ruled that after cancellation of the loan agreement the consumer had a claim to reimbursement of the interest paid and loan repayments as well as a claim for the payment of interest at the normal market rates on the instalments paid to the lender⁸⁵. In turn, however, the lender had a claim pursuant to section 3 of the HWiG (old version) to reimbursement of the net amount of credit paid with interest thereon at normal market rates⁸⁶. The lender did not, however, have a claim for administrative costs and/or discount. The BGH expressly acknowledged at the same time that with the obligation of immediate repayment and to pay interest at normal market rates on the amount of the loan, a right of revocation of the declaration of intent to enter into a loan agreement is of little or no interest economically for many consumers. The fact that the consumer who is caught unawares in a doorstep situation is accordingly in a considerably worse position than he would have been before the HWiG came into effect is based on a conscious decision by the legislator⁸⁷, a decision in respect of which it can be argued that no reasonable ground can be seen as to why a borrower who has been induced in a doorstep situation to make a declaration of intent to enter into a contract, in the case of rescission on the basis of the law of unjust enrichment, is put in a better position than a person who has been induced to do so by wilful deception.

2.4.2. *Schulte and Crailsheimer Volksbank: consequences of cancellation*

Some of the lower instance courts did not follow the BGH and applied again to the ECJ. By its decision of 25.10.2005 in the case of **Schulte**⁸⁸ the ECJ reiterated that the **consequences of the cancellation are governed by national law**.

- The ECJ took from this that the directive does not force Member States to regard the loan agreement and

purchase contract as linked legal transactions, even if both contracts form a single economic unit. **Cancellation of the loan agreement thus does not necessarily have to lead to the invalidity of the purchase contract.**

- The ECJ further set forth in this judgment that in the event of the cancellation of the loan agreement, in line with German case law it is consistent with the directive to require the consumer to **repay the amount borrowed** immediately plus interest at normal market rates, if the consumer was properly advised of his rights.
- In contrast to the previous case law of the 11th Senate of the BGH, the ECJ does, however, make it clear that a credit institution which does **not properly comply with its obligation to give information on the right of cancellation must bear the risks** associated with the relevant financial investment. In the initial proceedings, in the view of the ECJ, these risks lay alongside the risk that the apartment was over-valued at the time of its purchase, particularly because the estimated rental receipts out of which, in conjunction with tax advantages, interest payments and capital repayment were supposed to be made, could not actually be achieved and the expectations relating to the trend of property prices turned out to be mistaken. These risks only have to be borne by the credit institution, however, if the consumer could have avoided exposure to such risks if he had been duly informed of his right of cancellation. The ECJ thus stipulates that along with the lack of information on the right of cancellation there must also be causality between the breach of duty by the credit institution and the materialisation of the risks.

In its parallel decision in the case of **Crailsheimer Volksbank**⁸⁹ expressly in relation to the existence of a doorstep-selling situation that the determination of the risks inherent in the investment must be undertaken **objectively**. It thus does not depend on whether the credit institution was or should have been aware of the features of the investment. An attribution of the knowledge of an agent who induced the consumers to give their declarations in a doorstep-selling situation in accordance with the criteria developed for attribution of knowledge in accordance with section 123 (2) of the Civil Code is not necessary.

84 BGH, judgment of 9.4.2002 – XI ZR 91/99, BGHZ 150, 248 = DNotZ 2002, 859 = NJW 2002, 1881.

85 BGH, judgment of 12.11.2002 – XI ZR 47/01, BGHZ 152, 331 = DNotZ 2003, 338 = NJW 2003, 422, 423 = WM 2002, 2501 = ZIP 2003, 64.

86 Likewise BGH judgment of 26.11.2002 – XI ZR 10/00, DNotI-Report 2003, 20 = DNotZ 2003, 203 = NJW 2003, 885, 886.

87 Section 3 subsection 3 HWiG old version expressly specified that for the right to use or apply goods and for the other services supplied up to the date of cancellation, the value of such right or services must be paid; loss of value as a result of normal use of goods or other services shall be disregarded.

88 ECJ, judgment of 25.10.2005, C-350/03 (*Schulte*), [2005] ECR I-9215, marginal No. 79.

89 ECJ, judgment of 25.11.2005, C-229/04 (*Crailsheimer Volksbank*) [2005] ECR I-9273, marginal No. 42 et seq.

The 2nd Senate of the BGH has, in agreement with the 11th Senate, in the meantime followed this “objectification” in respect of the question of attribution of knowledge of the doorstep situation as such⁹⁰.

As a result of the Schulte decision, by judgment of 26.2.2008⁹¹ the Bundesgerichtshof (Federal Constitutional Court: **BGH**) derived a **genuine legal obligation on the part of the business operator to provide proper information on cancellation** from section 2 (1) of the Law on the cancellation of doorstep transactions and analogous transactions [*Gesetz über den Widerruf von Haustürgeschäften und ähnlichen Geschäften*: HWiG, old version] and ruled that where cancellation information is not given, **the investor may have a claim for compensation based on fault upon conclusion of contract**.

According to the BGH, for such a claim to exist it is, however, necessary that, at the time the credit agreement was concluded, the borrower was not yet bound under the purchase contract, that the failure to provide the cancellation information was based on the fault of the financing bank, in particular on an error in law based on its own fault, and that the breach of the obligation to provide information is established as the cause of loss. According to the BGH a claim for compensation also comes into consideration if the doorstep situation was involved not at the time the contract was concluded but only during the contract initiation stage. The BGH expressly rejected no-fault liability on the part of the financing bank⁹².

2.4.3. *Hamilton*: exclusion of right of cancellation after performance permissible

By judgment of 10.4.2008 the ECJ ruled in the case of **Hamilton**⁹³ that it is **compatible** with the Doorstep Selling Directive that section 2 (1) sentence 4 HWiG, old version, precludes the **right of cancellation where the obligations under a contract were performed in full more than one month previously**.

In its judgment in the *Heininger* case the ECJ again held that no temporal limitation can be imposed on the right of cancellation in the event that the consumer has not been properly informed⁹⁴. The ECJ has now made it clear that the *Heininger*, *Schulte* and *Craillsheimer Volksbank* cases always concerned situations in which the credit agreements had not yet been fully implemented. The wording of the Doorstep Selling Directive and its purpose to release consumers from their obligations do however, according to the ECJ, result in consumer protection finding its limits where the consumer no longer has any obligations because they have been fulfilled.

2.4.4. BGH submission: cancellation and the faulty company

Reference is made merely in passing to the pending proceedings **E. Friz GmbH/von der Heyden**⁹⁵. By ruling dated 5.5.2008⁹⁶ the BGH submitted questions to the ECJ asking whether the entry of a consumer into a partnership, commercial partnership, association or cooperative, and in particular to a closed-end real estate fund, falls under the scope of application of the Doorstep Selling Directive and whether it is compatible with the Directive that in the event of cancellation the consumer only has a claim to his severance balance (doctrine of the **faulty company**) or whether the consumer can claim back the capital contribution originally

paid from the company. According to the previous case law of the ECJ in the event that the severance balance is negative the consumer can even find himself obliged to settle this negative balance⁹⁷.

3. Unfair contractual terms

Along with the doorstep-selling directive, the directive on unfair contractual terms in consumer contracts, known as the **unfair contract terms directive**⁹⁸, is also of significance for notarial practice, especially in respect of the drafting of developers' construction and sale contracts. The regulatory impact of the directive and the competence of the ECJ to give rulings on interpretation are, however, sometimes greatly overestimated.

In the case of **Océano Grupo**⁹⁹ the ECJ did, it is true, give its view **directly in relation to a specific contractual clause** and held that the term drafted in advance by a tradesman which conferred jurisdiction for all legal disputes arising out of the contract to the court in the jurisdiction of which the tradesman had his place of business satisfied all the criteria necessary for it to be judged unfair within the meaning of the unfair contract terms directive.

Two years later in the case of **Commission v Sweden**¹⁰⁰, however, the ECJ emphasised that Article 3 of the **unfair contract terms directive merely defines in a general manner the factors** that render unfair a contractual term that has not been individually negotiated. The list of contractual terms contained in the annexe to the unfair contract terms directive contains, in the view of the ECJ, merely an indicative and not an exhaustive list of the claus-

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- 90 BGH, judgment of 12.12.2005, II ZR 327/04, NJW 2006, 497. The BGH now holds the view following the ECJ decision that section 1 HWiG must be interpreted in conformity with the directive to the effect that the credit institution does not have to have knowledge of the objective existence of a doorstep situation.
- 91 BGH, decision of 26.2.2008 – XI ZR [Civil Senate] 74/06, MDR [Monatsschrift für Deutsches Recht = *Monthly German Law Reports*] 2008, p. 635 = NJW [Neue Juristische Wochenzeitschrift = *New Weekly Law Reports*] 2008, p. 1585 = ZIP [Zeitschrift für Wirtschaftsrecht = *Economic Law Journal*] 2008, p. 686.
- 92 From a notarial point of view the BGH's compensation solution has the consequence that the purchase contract is not invalid or revocable as such, but in the worse case a conveyance of the property to the financing bank must occur.
- 93 ECJ, judgment of 10.4.2008, case C-412/06 (*Hamilton*), not yet published in the official court reports.
- 94 ECJ, judgment of 13.12.2001, case C-481/99 (*Heininger*), op cit., paragraphs 16 and 18. Following the ECJ judgment the German legislature amended Article 355 (3) BGB [*German Civil Code*] and deleted the exclusion of the right of cancellation upon fulfilment.
- 95 Case C-215/08 (*E. Friz GmbH/von der Heyden*).
- 96 BGH, decision of 5.5.2008 – II ZR 292/06, DStR [*German Tax Law Journal*] 2008, 1100 = EuZW [*European Journal of Business Law*] 2008, p. 377 = NZG [*New Journal of Company Law*] 2008, 460 = ZIP 2008, p. 1018.
- 97 See in relation to this, for example *Oechsler, Die Geschichte der Lehre von der fehlerhaften Gesellschaft und ihre Stellung im europäischen Gesellschaftsrecht [The Story of the Doctrine of the Faulty Company and its place in European Company Law]*, NJW 2008, p. 2471 et seq.
- 98 Council Directive 93/13/EEC of 05.04.1993 on unfair terms in consumer contracts, OJ L 95, 29.
- 99 ECJ, judgment of 27.6.2000, joined cases C-240 to C-244/98 (*Océano Grupo*), [2000] 4941.
- 100 ECJ, judgment of 7.5.2002, C-478/99 (*Commission v Sweden*), [2002] ECR I-4147.

es that may be declared to be unfair. A term appearing on the list should not, according to the ECJ, automatically be considered unfair and conversely a term that does not appear on the list may nevertheless be declared to be unfair.

In its judgment in the case of **Freiburger Kommunalbauten**¹⁰¹ issued on 1.4.2004, the ECJ in conclusion stated that the unfairness of a contractual term is to be assessed in accordance with Article 4 of the unfair contract terms directive by taking into account the nature of the goods or services for which the contract was concluded and all the circumstances attending the conclusion of the contract. In this connection the consequences of the term under the law applicable to the contract must also be taken into account, which requires consideration to be given to the national law. It follows from this that in the context of its jurisdiction under Article 234 EU to interpret Community law, the Court may interpret general criteria used by the Community legislature in order to define the concept of the unfair term. However, it should not rule on the application of these general criteria to a particular term, which must be considered in the light of the particular circumstances of the case in question. The latter is a matter for the **national court**. The ECJ therefore left unanswered the question referred by the BGH as to whether the purchaser's payment obligation in relation to a developer's construction and sale contract under the conditions of the Regulations governing contracts with brokers and property developers (Makler- und Bauträgerverordnung: MaBV) is prohibited.

The ECJ thus does not see itself as being appointed to review millions of contractual terms in the Member States for unfairness but shifts this task, which is too demanding for it in terms of personnel and technical skills, on to the level of the Member States.

- It certainly does not appear to be completely ruled out that **in particularly blatant cases** and in legal matters where the degree of regulation is greater, such as in relation to jurisdiction, in the law relating to proceedings for the taking of evidence and in civil procedure law, the ECJ will indeed again state its position on the unfairness of a specific term.
- The main burden of interpretation of the directive will, however, lie with the **national courts**. The risk of legal fragmentation appears to me in this connection to be small.
- As long as there are 25 different private law systems in the European Union, almost every clause will operate differently in each legal system. Thus **only case-by-case consideration is possible**.

4. Company law

4.1. Municipal enterprises and compliance with public procurement law

As already mentioned, over the whole of the European Union municipalities are more and more frequently going over to having public functions performed by private law associations. Sometimes tax considerations play a role and sometimes it is done to involve private capital in the performance of functions.

For the Notary, the latest case law of the ECJ on public procurement law has here too resulted in important guidelines for choice of legal form and shareholders, and also for the structure of the shareholders' agreement.

4.1.1. Contract award to a consortium of local authorities (*Teckal and Coditel Brabant*)

In the **Teckal**¹⁰² and **Coditel Brabant**¹⁰³ cases the ECJ ruled that the public procurement law must also be observed (or in the case of service concessions, the general Community legal order) when a municipality awards contracts to a special undertaking in the form of a **public consortium of several municipalities or a cooperative**¹⁰⁴ whose **members consist solely of municipalities**. The position can only be otherwise where the local authority exercises over this consortium control which is similar to that exercised over its own departments and, at the same time, this entity carries out the essential part of its activities with the controlling local authority or authorities.

4.1.2. Mixed undertakings (*Stadt Halle and Commission v Austria*)

In the case of **Stadt Halle**¹⁰⁵ the ECJ continued to develop this case law in relation to **mixed undertakings**, in which both public and private partners are involved.

Facts of the case: In the initial proceedings the city of Halle decided, without first initiating a tendering process, to undertake negotiations regarding the conclusion of a contract for the disposal of the city's residual waste with RPL Lochau GmbH. 75.1 % of the capital of RPL Lochau GmbH was held by Stadtwerke Halle GmbH, the shareholder of which, *Verwaltungsgesellschaft für Versorgungs- und Verkehrsbetriebe der Stadt Halle mbH*, was wholly owned by the city of Halle. The remaining 24.9 % of the capital of RPL Lochau GmbH was owned by a private limited liability company. A competitor challenged the award of contract.

After the ECJ had declared that Article 1 (1) of directive 89/665 also provides the possibility of review for decisions taken outside a formal award procedure and ahead of a formal tendering process¹⁰⁶, it turned to the question of whether the Community legislation on the award of public contracts also applies to mixed public/private partnerships. The ECJ began by stating that EU legislation regulating the award of public contracts aims to open up public procurement to the widest possible competition¹⁰⁷.

101 ECJ, judgment of 1.4.2004, C-237/02 (*Hofstetter*), [2004] ECR I-3403.

102 ECJ, judgment of 18.11.1999, case C-107/98 (*Teckal*), European Court Reports 1999, I-8121.

103 ECJ, judgment of 13.11.2008, case C-324/07 (*Coditel Brabant*), op cit.

104 The initial case involved a cooperative society formed on the basis of the Belgian Law on inter-municipal cooperatives, a special form of public collaboration.

105 ECJ, judgment of 11.1.2005, C-26/03 (*Stadt Halle*), [2005] ECR I-1.

106 ECJ, judgment of 11.1.2005, C-26/03 (*Stadt Halle*), op cit., marginal No. 22 et seq.

107 ECJ, judgment of 11.1.2005, C-26/03 (*Stadt Halle*), op cit., marginal No. 47.

- The public procurement law thus, in principle, only does not apply if the public agency fulfils its public interest functions using its own administrative, technical and other resources, through its **own departments** which are not legally distinct from it.
- According to ECJ case law it cannot, however, be excluded that there could be other circumstances in which a tendering process could be dispensed with even if the contracting party is a body which is legally distinct from the public agency. The public agency must exercise **similar control** over the body in question **as it exercises over its own departments**. In addition the body must carry out the essential part of its activities with the controlling public authority or authorities which hold(s) its shares.

In the view of the ECJ, **participation**, even if it is only a minority interest, **by a private undertaking** in the capital of a company in which the public agency in question also holds a participatory interest in any case precludes the public agency from exercising the same control over this company as it exercises over its own departments because the relationship between a public agency which is a contracting authority and its departments is determined by considerations and requirements associated with the pursuit of objectives which are in the public interest.

The investment of private capital in an undertaking is, by contrast, based on considerations connected with private interests and pursues different objectives. Moreover, the award of a public contract to a mixed undertaking without a call for tenders would interfere with the objective of free and undistorted competition and the principle specified in directive 92/50¹⁰⁸ of equal treatment for all interested parties, particularly because such a process would provide a private undertaking with a capital participation in the undertaking in question with an advantage over its competitors.

The ECJ therefore concluded that in the initial case there was an obligation to carry out a tendering process.

Also in the case of **Commission v Austria**¹⁰⁹ the ECJ again confirmed the applicability of the EU public procurement law in the case where a private undertaking holds shares in the contracting company. Moreover, the court amplified its finding by stating that the applicability of the public procurement law could not be circumvented by the contract already being awarded and the **private undertaking only taking a shareholding in the company thereafter**¹¹⁰. To this extent the applicability of the public procurement law must be determined by taking an overall view of the steps taken and also of the aim of these steps.

Thus, if a municipality should decide to set up a company in which private co-shareholders have an interest in order to execute public functions, the provisions of the public procurement legislation must be observed.

The Commission used the foregoing case law, in particular the decision in the *Stadt Halle* case, as the basis for summarising its opinion on the observance of Community law when Institutionalised Public-Private Partnerships (IPPP) are set up and upon the subsequent award of contracts to such institutions in a **Communication**¹¹¹.

- This states that depending on the nature of the task (public contract or concession) to be assigned to the IPPP, either the public procurement directives or the general principles of the EU Treaty are applicable to the **selection of the private partner**. For the setting up of an IPPP, Community law does not require a double tendering process i.e. one for selecting the private partner to the IPPP and another one for awarding public contracts or concessions to the public-private entity. Instead, according to the Commission, it is sufficient to have a selection process when the IPPP is set up.
- In each case all potential bidders must have equal access in the selection process to suitable information by **public notification of eligibility and award criteria**. According to the Commission's Communication this obligation of equal treatment and transparency means that this notification must include the **statutes and articles of association**, any shareholder agreements and must specify all other elements governing the contractual relationship between the contracting entity and the private partner on the one hand, and the contracting entity and the future public-private entity on the other hand.
- The call for competition should further include information on the anticipated duration of the public contract or concession. The type of business must accordingly be precisely defined in the statutes. Finally, in the Commission's view the articles of association should be so formulated that it is possible to change the private partner in the future.

4.1.3. Wholly owned subsidiary of the local authority (*Parking Brixen and Carbotermo*)

The ECJ did not, however, free the award of contracts to wholly owned subsidiaries of municipalities from the requirement of a tendering process across the board. The case of **Parking Brixen**¹¹² concerned the operation of a car park which the town of Brixen had transferred to its **wholly owned subsidiary**, Stadtwerke Brixen AG, without a call for tenders, for an annual payment of EUR 151,700.

Stadtwerke Brixen AG came into existence through the conversion of the special undertaking Stadtwerke Brixen. Under Article 4 of its statutes, Stadtwerke Brixen AG may carry on, *inter alia*, the following activities at local, national and international level:

108 Council Directive 92/50/EEC of 18.06.1992 relating to the coordination of procedures for the award of public service contracts, OJ L 209, p. 1.

109 ECJ, judgment of 10.11.2005, C-29/04 (*Commission v Austria*), [2005] ECR I-9705, marginal No. 45 et seq.

110 ECJ, judgment of 10.11.2005, C-29/04 (*Commission v Austria*), op cit., marginal No. 39 et seq.; likewise ECJ, judgment of 06.04.2006, C-410/04 (*ANAV*), [2006] ECR I-3303, marginal No. 30.

111 Commission Interpretative Communication of 5.2.2008 on the application of Community law on Public Procurement and Concessions to Institutionalised Public-Private Partnerships (IPPP), C (2007) p. 6661 – OJ EU No. C 091 of 12.04.2008 pp. 4 – 9.

112 ECJ, judgment of 13.10.2005, C-458/03 (*Parking Brixen*), [2005] ECR I-8612, marginal No. 62 et seq.

“g) the management of car parks and garages and related activities.”

Article 18 of Stadtwerke Brixen AG's statutes provided that the following powers are conferred on its Administrative Board:

- “1. The Administrative Board shall have the broadest possible powers relating to the company's routine administration with the authority to carry out all acts which it deems appropriate or necessary to attain the objective of the company.
2. Unless authorised by the shareholders' meeting, the Administrative Board is prohibited from providing guarantees with a value of over EUR 5 (five) million and from signing promissory notes and accepting drafts which exceed this amount.
3. The purchase and sale of holdings in other companies, the purchase, sale and leasing of businesses or branches of businesses, and the purchase and sale of vehicles up to a value of EUR 5 (five) million per transaction shall be regarded as acts of routine administration.
4. Those decisions which relate to the fixing and/or amendment of remuneration for special tasks in accordance with Article 2389(2) of the Italian Civil Code shall fall within the exclusive competence of the Administrative Board.”

Under Article 5(2) of Stadtwerke Brixen AG's statutes, “the municipality of Brixen's holding in the nominal capital shall, in no circumstances, be below the absolute majority of nominal shares”. In addition, the municipality of Brixen has the right to appoint a majority of the members of the company's Administrative Board. Since the supervisory board of the company is to be composed of three full members and two alternates, the municipality appoints at least two full members and one alternate of that board.

The decisive criterion for the non-application of the public procurement law is the question of whether the municipality exercises **similar control** over the contracting company **as over its own departments**¹¹³. On this point the ECJ stated that in the specific case the special undertaking, Stadtwerke Brixen, was a municipal body whose specific function was the uniform and integrated provision of local public services. The municipal council laid down the general guidelines, allocated the start-up capital, ensured that any social costs were covered, monitored the operating results and exercised strategic supervision, the undertaking being guaranteed the necessary autonomy. By contrast, Stadtwerke Brixen AG became market-oriented, which rendered the municipality's control tenuous. Militating in this direction are:

- the conversion of Stadtwerke Brixen – a special undertaking of the municipality of Brixen – into a company limited by shares (Stadtwerke Brixen AG) and the nature of this type of company;
- the broadening of its objects, the company having started to work in significant new fields, particularly those of the carriage of persons and goods, as well as information technology and telecommunications;
- the obligatory opening up of the company, in the short term, to outside capital;
- the expansion of the geographical area of the company's activities to the whole of Italy and abroad;

- the considerable powers conferred on its Administrative Board, which were, in practice, exercised without any management control by the municipality.

It emerges from the deliberations of the referring court that the control exercised by the municipality over Stadtwerke Brixen AG was essentially limited to those measures that company law assigns to the majority of shareholders, which considerably attenuates the relationship of dependence which existed between the municipality and the special undertaking Stadtwerke Brixen, in the light, above all, of the broad powers possessed by Stadtwerke Brixen AG's Administrative Board.

The ECJ therefore comes to the conclusion that the award of contract to Stadtwerke Brixen AG should not have taken place without a tendering process.

In the **Carbotermo** judgment of 11.5.2006¹¹⁴ the ECJ expounded on its reasoning in Parking Brixen to the effect that in assessing whether the contracting authority exercises similar control as it exercises over its own departments, it is necessary to take account of all legislative provisions and relevant circumstances. This examination must, according to the ECJ, lead to the conclusion that the company to whom the contract is being awarded is subject to control which enables the contracting authority to influence the decisions of the company. This must involve the possibility of exerting decisive influence over both strategic objectives and significant decisions of this company.

4.1.4. Consequences for notarial contract drafting

For notarial contract drafting the foregoing case law means that, insofar as a German company is involved, the legal form of the GmbH (private limited liability company) is to be preferred to that of the AG (public limited company) because in the case of the former, the influence of the municipality as shareholder is greater.

Furthermore, care should be taken to provide the municipality with the **strongest possible control mechanisms** over the company.

- For example, the statutes may contain a list of important legal transactions which require the prior **approval of the municipal council**.
- The **strategic monitoring** of the company by the municipality could, for example, be established by an obligation on the management under the company's statutes to draw up a budget and/or business plan.
- The object of the company should, as far as possible, be restricted to **specific functions**.
- Expansion of the activities of the company beyond the **municipality area** should be excluded.
- Finally, as far as possible only holders of official posts within the municipality should be appointed as directors in order to increase the influence of the municipality on the management.

¹¹³ Likewise ECJ, judgment of 6.4.2006, C-410/04 (ANAV), op cit., marginal No. 24 et seq.

¹¹⁴ ECJ, judgment of 11.5.2006, C-340/04 (*Carbotermo*), [2006] ECR I-4137, marginal No. 36 et seq.

4.2. Restrictions on freedom of establishment of companies with their registered offices in other Member States

To conclude this article, the case law of the ECJ regarding restrictions on the freedom of establishment of companies with their registered offices in other Member States must be considered¹¹⁵.

4.2.1. *Centros*: company can be formed in a different EU country to the one in which it conducts its business

In 1999 the ECJ decided in the case of **Centros**¹¹⁶ that a Member State may not refuse to effect registration of a branch of a company which has its registered office in another Member State and has been lawfully founded in conformity with the legislation of that Member State, even if the company carries on its entire business in the State in which the branch office is situated and establishment of the branch office only serves to circumvent the higher requirements on the paying up of the minimum share capital under the rules governing the formation of companies in the State where the branch office is situated.

4.2.2. *Überseering*: transfer of company's actual centre of administration to another EU Member State permissible

In 2002 the ECJ ruled in the case of *Überseering*¹¹⁷ that it infringes freedom of establishment if a company which has been formed in accordance with the law of the Member State within whose jurisdiction it has its seat prescribed by its statutes, and who has transferred its actual centre of administration to another Member State, is denied legal capacity and, consequently, the capacity to be a party to legal proceedings in the other Member State. In this judgment the ECJ further expressed the opinion that in the context of the exercise of freedom of establishment, the host State must respect the legal capacity and, consequently, the capacity of the company to be a party to legal proceedings which this company possesses under the law of the State of its incorporation.

4.2.3. *Inspire Art*: State where a company has its centre of administration cannot require compliance with its domestic company law even in the case of exclusive business activity in that State

In its decision in the case of **Inspire Art**¹¹⁸ the ECJ expounded on its reasoning in relation to the establishment of branches by EU companies. In terms of this ruling, it is contrary to Articles 43 EC and 48 EC for a regulation which makes the setting up of a secondary establishment in a Member State by a company formed in accordance with the law of another Member State dependent on certain conditions prescribed by domestic law in respect of company formation relating to minimum capital and directors' liability. The reasons for which the company was formed in the other Member State, and the fact that it carries on its activities exclusively or almost exclusively in the Member State of establishment, do not deprive it of the right to invoke the freedom of establishment guaranteed by the EU Treaty unless the existence of an abuse is proved in the specific case. According to the ECJ it is un-

lawful, without prejudice to the information obligations imposed on branches under social or tax law, or in the field of statistics, to impose disclosure obligations on companies which are not provided by the directive on the disclosure requirements in respect of branches (Eleventh Directive¹¹⁹). The Eleventh Directive is, to this extent, exhaustive¹²⁰.

4.2.4. *innoventif Limited*: registration of the branch and the attendant costs

In its decision of 1.6.2006 in the case of **innoventif Limited**, the ECJ ruled that it is compatible both with Articles 43 EC and 48 EC and with the Eleventh Directive for legislation of a Member State to make registration of a branch in the register of companies subject to the payment of an advance to cover the anticipated cost of the publication of the full objects of the company as set out in its instrument of constitution¹²¹. In the specific case the Amtsgericht (local court) of Charlottenburg stipulated an **advance payment amounting to EUR 3000 for the publication of the full objects (filling several sides) of the limited company** although the activity of the registered branch was limited to only some of these objects¹²².

The ECJ stated by way of explanation that Article 2 para. 2 b) of the Eleventh Directive expressly permits Member States to make the registration of the branch subject to disclosure of the full instruments of constitution of the company and the memorandum and articles of association, if they are contained in a separate instrument¹²³. Sections 13b subsection 3 and 13g subsection 3 of the HGB in conjunction with section 19 subsection 1 of the Law on Private Limited Liability Companies (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung*: GmbHG), which applies equally to domestic and foreign companies, only however require disclosure of the undertaking's business objects and not, as the directive permits, disclosure of the full instrument of constitution of the company¹²⁴. It further results from Arti-

115 The articles in professional journals on the consequences and interpretation of the above mentioned ECJ judgments are abundant and never-ending. The problems arising from these decisions can only be gone into briefly here. Annotations of judgments can be accessed on the website of the European Court of Justice (www.curia.eu), under the heading Annotation of Judgments. In the EU judgment in the case of *Inspire Art* of 30.9.2003 alone, in the period up to 31.12.2005 the ECJ lists 77 annotations without any claim that the list is exhaustive.

116 ECJ, judgment of 9.3.1999, C-212/97 (*Centros*), [1999] ECR I-1459.

117 ECJ, judgment of 5.11.2002, C-208/00 (*Überseering*), [2002] ECR I-9919.

118 ECJ, judgment of 30.9.2003, C-167/01 (*Inspire Art*), [2003] ECR I-10155.

119 Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State, OJ L 395, 36.

120 ECJ, judgment of 30.9.2003, C-167/01 (*Inspire Art*), op cit., marginal No. 69 et seq.

121 ECJ, judgment of 1.6.2006, C-453/04 (*innoventif Limited*), [2006] ECR I-4929.

122 The previous practice of the courts was not uniform here. Thus, for example, the OLG Frankfurt, decision of 29.12.2005, 20 W 315/05 (DB 2006, 269) and the OLG Hamm, decision of 28.6.2005, 15 W 159/05 (GmbHR. 2005, 1130), in each case citing a requisite interpretation in conformity with the directive, regarded publication only of the objects of the branch as sufficient.

123 ECJ, judgment of 1.6.2006, C-453/04 (*innoventif Limited*), op cit., marginal No. 34.

124 ECJ, judgment of 1.6.2006, C-453/04 (*innoventif Limited*), op cit., marginal No. 35.

cle 3 of the First Company Law Directive¹²⁵ in conjunction with Article 1 para. 1 of the Eleventh Directive that disclosure has to be announced in the form of publication in an official gazette to be specified by the Member States. Finally, according to the ECJ, the imposition of an advance payment, the level of which only corresponds to the actual administrative cost of such a publication, does not represent a restriction on freedom of establishment as it neither inhibits nor interferes with the exercise of this freedom, nor does it make it less attractive¹²⁶.

4.2.5. *Sevic*: cross-border merger

The contest between systems triggered by the Centros, Überseering and Inspire Art judgments was yet further accentuated by the judgment of the ECJ of 13.12.2005 in the case of *Sevic*¹²⁷ on cross-border mergers.

With reference to section 1 of the Company Transformation Act (*Umwandlungsgesetz*), which at that time only permitted mergers in respect of domestic companies, the ECJ ruled that Articles 43 EC and 48 EC prohibit a Member State from generally refusing registration in the national commercial register of the merger by dissolution, without liquidation, of one company with another company where one of the two companies is established in another Member State whereas such registration is possible where the two companies participating in the merger are both established in the territory of the first Member State.

According to the ECJ, the right of establishment covers all measures which permit or even merely facilitate access to another Member State and/or the pursuit of an economic activity in that Member State by allowing the persons concerned to participate in the economic life of the country effectively and under the same conditions as national operators. Cross-border merger operations, like other company transformation operations, respond in the view of the ECJ to the need for cooperation and consolidation between companies established in different Member States. They constitute particular methods of exercise of the freedom of establishment, important for the proper functioning of the internal market, and are therefore amongst those economic activities in respect of which Member States are required to comply with the freedom of establishment laid down by Article 43 EC¹²⁸. Harmonisation of the rules for cross-border mergers, as is, in the meantime, taking place for mergers by limited liability companies by means of the cross-border mergers directive¹²⁹, cannot, according to the ECJ, be made a precondition for the implementation of the freedom of establishment¹³⁰. Finally, in principle, imperative reasons in the public interest such as protection of the interests of creditors, minority shareholders and employees may justify restrictions on the freedom of establishment; in the opinion of the ECJ, however, a general exclusion on mergers is in any event disproportionate¹³¹.

The German Company Transformation Act has, in the meantime, been correspondingly amended by inserting sections 122a et seq¹³².

4.2.6. *Cartesio*: registration of the transfer of a company's seat in the register of the Member State of incorporation

In the case of *Cartesio*¹³³, the ECJ confirmed in its judgment of 16.12.2008, with express reference to the

Daily Mail decision¹³⁴, that as Community law currently stands, Articles 43 EC and 48 EC do not preclude the national law of a Member State from preventing a company incorporated under its national law from transferring its seat to another Member state whilst retaining its status as a company governed by the law of the Member State of incorporation and therefore the **national company law does not have to permit the transfer of the seat of a company with maintenance of the company's legal form**.

In accordance with Article 48 EC, in the absence of a uniform Community law definition of the companies which may enjoy the right of establishment and in the absence of a uniform connecting factor determining the law applicable to a company, the question as to whether Article 43 EC applies to a company which seeks to rely on the fundamental freedom enshrined in that article is, like the question as to whether a natural person is a national of a Member State and hence entitled to enjoy that freedom, a **preliminary question** which, as Community law currently stands, can **only be answered in accordance with the applicable national law**. The question as to whether the company is faced with a restriction on the freedom of establishment, within the meaning of Article 43 EC, can arise only if it has been established, in the light of the conditions laid down in Article 48 EC, that the company actually has a right to that freedom. The Member State can determine both the connecting factor required of a company in order to be regarded as a company incorporated under its domestic law and, as such, capable of enjoying the right of establishment, and also the connecting factor required if the company is to maintain that status.

The situation where the transfer of the seat of a company incorporated under the law of one Member State is transferred to another Member State without any change in the law applicable to it must, however, according to the ECJ, be distinguished from the case where a company moves from one Member State to another **with an attendant change as regards the national law applicable and in the process is converted into a form of company**

125 First Council Directive 68/151/EEC of 9.3.1968 on co-ordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community, OJ L 65, 8.

126 ECJ, judgment of 10.6.2006, C-453/04 (*innoventif Limited*), op cit., marginal No. 38.

127 ECJ, judgment of 13.12.2005, C-411/03 (*Sevic*), [2005] ECR I-10805.

128 ECJ, judgment of 13.12.2005, C-411/03 (*Sevic*), op cit., marginal No. 18 et seq.

129 Directive 2005/56/EC of the European Parliament and of the Council of 26.10.2005 on cross-border mergers of limited liability companies, OJ EC L 320, 1.

130 ECJ, judgment of 13.12.2005, C-411/03 (*Sevic*), op cit., marginal No. 26.

131 ECJ, judgment of 13.12.2005, C-411/03 (*Sevic*), op cit., marginal No. 30.

132 Art. 1, n° 17 of the *Zweites Gesetz zur Änderung des Umwandlungsgesetzes* (Second Act on the Amendment of the Company Transformation Act), Federal Gazette 2007 I, 542.

133 ECJ, judgment of 16.12.2008, case C-210/06 (*Cartesio*), not yet published in the official court reports.

134 ECJ, judgment of 27.9.1988, case 81/87 (*Daily Mail*), European Court Reports 1988 I, p. 5483.

which is governed by the law of the second Member State. In the latter case the powers of the Member States referred to above, far from implying that national legislation on the incorporation and winding-up of companies enjoys any form of immunity from the rules of the EC Treaty on the freedom of establishment, cannot, in particular, justify the Member State of incorporation, by requiring the winding-up or liquidation of the company, in preventing that company from converting itself into a company governed by the national law of the other Member State, to the extent that it is permitted under that law to do so.

The case which gave rise to the judgment in **SEVIC Systems, distinguishing it from the Cartesio case**, concerned the recognition, in the Member State of incorporation of a company, of an establishment operation carried out by that company in another Member State by means of a cross border merger, which is a situation fundamentally different from the circumstances at issue in the case which gave rise to the *Daily Mail* but similar to the situations considered in other judgments of the Court¹³⁵. In such situations, the issue which must first be decided is not the preliminary question as to whether the company concerned may be regarded as a company which possesses the nationality of the Member State under whose legislation it was incorporated but, rather, the question as to whether or not that company – which, it is undisputed, is a company governed by the national law of a Member State – is faced with a restriction in the exercise of its right of establishment in another Member State.

4.2.7. Taxation of cross-border mergers

In accordance with the **taxation of mergers directive**¹³⁶, which was actually to be implemented by no later than 1.1.1992, the Member States must facilitate tax-neutral cross-border mergers insofar as the hidden reserves of a domestic transferring company continue to be subject to deferred domestic taxation where, for example, these hidden reserves can still be allocated to a domestic business establishment after the merger.

The ECJ has not as yet commented definitively on the fiscal issues connected with the transfer of the central management of a company to another Member State or on cross-border mergers.

- In the **Daily Mail** decision in 1988, the ECJ held that it was still permissible for a Member State to make the transfer of a company's central management and control abroad subject to prior approval in order to ensure that hidden reserves could thus be taxed¹³⁷.
- In March 2004 in the case of **Hughes de Lasteyrie du Saillant**¹³⁸ the ECJ however held that a French provision which provided for the taxation of unrealised capital gains on securities if an individual transferred his tax residence abroad was not permitted. In its 2004 decision the ECJ found that the provision in question led to a restriction on the freedom of establishment because it had a dissuasive effect on taxpayers wishing to establish themselves in another Member State¹³⁹. In the view of the ECJ, the prevention of tax avoidance, the loss of tax revenues or ensuring the coherence of the national tax system do not represent imperative reasons in the public interest which could

justify the restriction. The parallels with the “exit taxation” of companies if they move their central management and control abroad are obvious.

- In the case of **Marks & Spencer**¹⁴⁰ the ECJ regarded a distinction between resident and non-resident cases as unlawful.

Germany only implemented the taxation of mergers directive in national law by means of the “Law on the Tax Features for the Introduction of the European Company and Amendment of Other Tax Rules” (*Gesetz über steuerliche Begleitmaßnahmen zur Einführung der Europäischen Gesellschaft und zur Änderung weiterer steuerrechtlicher Vorschriften: SEStG*) of 7.12.2006¹⁴¹. In order to avoid prohibited unequal treatment of cross-border reorganisation operations the **whole statutory system was reversed**:

Whereas under the old law, in the case of a transformation or merger the hidden reserves were in principle preserved – the transformation thus did not lead to a fiscal disclosure of the difference between market value and the tax basis of the assets – in accordance with the new law, in all cases of transformation the hidden reserves are, in principle, uncovered. On request, however, book value can be maintained if the hidden reserves are involved operationally and remain taxable in Germany (sections 3, 11 and 12 of the Reorganisation Tax Act (UmwStG)). The transfer of the seat of a company within the EU leads to the disclosure of its hidden reserves (section 4 of the Income Tax Act (EStG) and section 12 of the Corporation Tax Act (KStG)). As a result the amended legislation does not result in any change for domestic cases, while in the case of the transfer of a company seat or merger abroad the payment of tax on the hidden reserves is safeguarded. Thus it is not that the German legislator has created an exception for transformations involving foreign companies; rather the legislator made this the basic rule and conversely introduced an exception for domestic situations.

The transfer of any fiscal loss carried forward which previously applied in domestic cases was also abolished. Behind this was the fear that otherwise foreign losses would have to be recognised in cases of inward mergers in accordance with the ECJ's decision in the case of **Marks & Spencer**.

For notarial practice it should accordingly be noted that large-scale cross-border mergers should only be contemplated when the fiscal issues have been resolved.

135 Cf. Judgment of 9.3.1999, case C 212/97 (*Centros*), European Court Reports 1999, I 1459; judgment of 30.9.2003, case C-167/01 (*Inspire Art*), European Court Reports 2003, I-10155.

136 Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, OJ EC L 225, 1.

137 ECJ, judgment of 27.9.1988, 81/87 (*Daily Mail*), [1988] ECR I, 5483.

138 ECJ, judgment of 11.3.2004, C-9/02 (*Hughes de Lasteyrie du Saillant*), [2004] ECR I-2409.

139 ECJ, judgment of 11.3.2004, C-9/02 (*Hughes de Lasteyrie du Saillant*), op cit., marginal No. 45.

140 ECJ, judgment of 13.12.2005, C-446/03 (*Marks & Spencer*), [2005] ECR I-10837.

141 *Gesetz über steuerliche Begleitmaßnahmen zur Einführung der Europäischen Gesellschaft und zur Änderung weiterer steuerrechtlicher Vorschriften* (SEStEG) (Law on the Tax Features for the Introduction of the European Company and Amendment of Other Tax Rules) of 7.12.2006, BGBl. (Federal Gazette) 2006 I, page 2782, in force since 13.12.2006.