

14.05.2020

## COMPLIANCE & INVESTIGATIONS

### ON BREACHES OF BUDGETARY TRUST LIABLE TO CRIMINAL PROSECUTION IN PROCUREMENT VIOLATIONS

In its ruling of 8 January 2020, case 5 StR 366/19, Germany's Federal Court of Justice commented on whether breaches of procurement rules are liable to criminal prosecution. In terms of criminal law, according to this ruling, representatives of contracting authorities do not always act in breach of their duties if they fail to select the most economical, i.e. lowest offer. But the Federal Court of Justice's decision does draw attention to the precautions that heads of public authorities need to take in procuring services so that the procurement is lawful.

#### The facts

A prosecution was brought against a German mayor (the defendant in what follows). Under the city council's rules of procedure, he was authorised to award contracts of up to EUR 25,000 net on his own. Any expenditure in excess of this needed to be resolved upon by the city council or a committee.

Over several years, there had been indications that employees of the city council's works depot had been engaged in private activities during working hours. In particular, they had felled wood in state-owned forests and sold it for their own account. In 2015, indications mounted that misconduct liable to criminal prosecution and relevant under employment and labour law had occurred. The mayor instructed a private investigator to clarify the facts of the matter, but did so without having reviewed whether the investigator's prices were market-rate. The contract was subject to termination at any time without notice, which in and of itself was a sensible precaution.

Straight away in the first month, the private investigator made observations that suggested the employees concerned were committing theft and breaches of employment and labour law. These observations were backed up by video sequences. The mayor was notified of this on 3 December 2015. On this date, the mayor approved payment of a **EUR 100,000** instalment plus VAT, which was made to the private investigator.

The surveillance continued until 18 December 2015. The private investigator then issued a final invoice to the city for EUR 276,762.43 net (EUR 328,157.29 gross). The defendant signed off on this bill in January 2016, having verified it in terms of the calculation and facts, and instructed payment to be made.

After this procedure became known, a criminal charge was brought against the mayor.

The data protection officer with competence for the matter also issued a fine notice as punishment for the limits of permissible employee surveillance having been exceeded.

#### The decision in the first instance

The regional court had jurisdiction over the matter in the first instance. Among the facts it established was that at the time the contract was concluded the mayor had been aware that he would exceed the EUR 25,000 limit on sums at his direct disposal. Furthermore, the court ruled, when the contract was concluded he had knowingly accepted that the private investigator's prices were above market-rate, such that the city would be burdened with unnecessarily high costs.

The regional court then gave the mayor a suspended custodial sentence of one year and three months for breach

of budgetary trust.

### **Decision by the Federal Court of Justice**

The Federal Court of Justice largely upheld the mayor's appeal on points of law.

As mayor entitled to represent the city, the Federal Court of Justice stated, the defendant had a duty of responsibility for assets vis-à-vis the city (this duty being mostly regulated in municipal statutes). Moreover, the supreme-level court continued, the mayor must observe the budgetary principles of best value for money and economy when awarding contracts.

But the regional court's findings did not provide grounds to assume a breach of fiduciary duty through the instruction of the private investigator at excessive prices, under section 266 of the German Criminal Code. The regional court had found that the defendant had already intended to exceed the EUR 25,000 limit on sums at his direct disposal when the contract was awarded, thus breaching his fiduciary duty. This was not backed up by sound evidence, however.

Moreover, the Federal Court of Justice continued, it does not follow from the fiduciary duty and principle of economy that costs must be reduced "at any price". Even in public administration, decision-makers do not always act in breach of duty if they fail to select the most economical, i.e. lowest offer. In such discretionary decisions, in fact, breach of trust liable to criminal prosecution is only possible where there has been an evident and serious violation of duty.

In this case, the Federal Court of Justice was unable to discern such evident and serious violation of duty, because the mayor was able to accord precedence to a variety of factors over the price criterion. These factors include the contractor's integrity, its presence on the market, its size, how long it had existed, recommendations, evaluations and personal impression.

The Federal Court of Justice saw no evidence that the mayor had deliberately exceeded the EUR 25,000 limit on contract awards at his discretion when the contract was awarded on 1 October 2015. The contract with the private investigator was **subject to termination at any time**, the Court stated, which meant that its "goal" – conviction of the employees in question – could also have been met below this threshold.

However, additional costs would have been avoided had the mayor duly terminated the contract with immediate effect after the initial findings by the private investigator, i.e. no later than 3 December 2015. Insofar, a serious violation of his fiduciary duty by the mayor was possible, when he failed to terminate the contract. But the regional court had not established sufficiently whether the bodies with competence for these contract values (city council or competent committee) would nevertheless have continued the contract until at least 18 December 2015 under the terms and conditions agreed upon, with a probability bordering on certainty.

### **Conclusion**

The decision makes it clear again that only really serious violations of public procurement in Germany fall within the area liable to criminal prosecution. It is not the case that every mistake, however minor, constitutes a breach of trust.

In addition, the Federal Court of Justice has given several important pointers with regard to how public procurement is organized and checked:

- › In awarding a contract, a mayor (accused) is bound by the principles of best value for money and economy; it is recognized that breaching the budgetary requirements of best value for money and economy may constitute a breach of duty, and of trust, and may therefore be liable to criminal prosecution.
- › A violation of fiduciary duty with intent may also be committed by omitting to take action. This can happen where an instalment is demanded (as the private investigator here did) and the principal adheres to the contract even though it knows that the limit on the sum it can permissibly award on its own has been exceeded. The fact that bodies with competence for higher contract values will then automatically approve continuance of such a contract can in no way be simply assumed.
- › Harm (in this case, to the municipality) that leads to a breach of trust liable to criminal prosecution may also arise where the municipality is supposed to pay for a service that the principal should not in fact have let be performed. This might be the case where there is already a fine notice from the data protection officer because employees have been subject to surveillance that is not permitted under data protection law. The surveillance undertaken is then of no value to the municipality.

EXPERTISE

Compliance & Investigations

Public Law

Public Procurement

LAWYERS

**Dr. Eike Bicker**

**Dr. Andreas Neun**

**Dr. Thomas Fritsche**