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(Information)

COURT OF AUDITORS

SPECIAL REPORT No 5/2000

on the Court of Justice's expenditure on buildings (annexe buildings Erasmus, Thomas More and Annexe C), together with the Court of Justice's replies

(pursuant to Article 248(4), second subparagraph, of the EC Treaty)

(2000/C 109/01)

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Introduction

1. On 15 November 1994, the Court of Justice of the European Communities concluded a rental agreement with the Luxembourg administration with a view to buying ⁽¹⁾ three buildings annexed to the main building, the 'Palais', situated on the Kirchberg plateau, which this institution has occupied since 1972.

2. Between 1986 and 1994, the Luxembourg administration arranged for the construction ⁽²⁾ of these three buildings (see photo below), covering a total surface area of 65 949 m², in accordance with the Court of Justice's specific requirements ⁽³⁾. These constructions have gradually been added on to each other in response to the Court of Justice's constantly developing needs and, since completion of the work in 1994, one single building complex has thus been able to accommodate all the Court of Justice's staff, which had previously been dispersed over a number of sites. The expenditure relating to this construction programme (Annexe A or 'Erasmus', Annexe B or 'Thomas More' and Annexe C) amounted in total to LUF 9 200 million (i.e. about ECU 200 million, excluding VAT) (see Table 1). This expenditure was the subject of a Court of Auditors' audit which focused on the construction of these three annexe buildings, the conclusion of the Agreement of 15 November 1994 and its implementation up until 1998.



Table 1

Construction cost

		(million LUF)	
Cost factors (inclusive of VAT)		Amounts	Variation
Authorising Laws			
(a) Total costs initially planned			
First law (Annexe A)		1 320	
Second law (Annexe B)		1 750	
Third law (Annexe C)		870	
Initial total ceiling		3 940	
(b) Increase in ceiling for additional work			
Fourth law		740	
(c) Ceiling finally authorised		4 680	
Situation as at 31.12.1998			
(d) Construction cost found		5 848	
(e) Overrun of initial ceiling	((d)-(a))	1 908	+ 49 %
(f) Overrun of final ceiling	((d)-(c))	1 168	+ 25 %
(g) Total financial expenses		3 320	
(h) Total construction cost		9 168	
(i) Updating ⁽¹⁾		2 038	
(j) Updated total cost ⁽¹⁾		11 207	
(k) Updated total of the amounts paid by the Court of Justice ⁽¹⁾		7 138	
(l) Updated VAT total ⁽¹⁾		1 177	
(m) Amount still outstanding	((j)-(k)-(l))	2 892	

⁽¹⁾ The figures are updated on the basis of the weighted average of the rates charged on the loans granted for financing the construction.

Source: Law of 25.7.1985 (Annexe A)

Law of 1.6.1989 (Annexe B)

Law of 18.12.1990 (Annexe C)

Law of 28.12.1992 (increase in ceiling)

Rental agreement 15.11.1994

KPMG calculation of the selling price: Updated at 31.12.1998.

Launch of the construction programme

3. By 1979, the Court of Justice's workload and staff had expanded to such an extent that it was obliged to rent office accommodation outside its main building. From the early 1980s onwards, it entrusted the Luxembourg administration with the task of carrying out on its behalf a construction programme that was defined piecemeal in the course of the years that followed. At the time, no contracts were concluded with the Luxembourg administration governing the financial arrangements for this programme or how it was to be monitored and audited.

4. The Court of Justice launched and proceeded with this construction operation, which involved long-term financial obligations for the Communities, without first submitting it to its Financial Controller for examination. It also failed to inform the Budgetary Authority about the scale of the planned operations with a view to obtaining its prior authorisation.

5. The legal ⁽⁴⁾ and financial ⁽⁵⁾ arrangements agreed between the Court of Justice, the Luxembourg administration and the property developer, a wholly-owned subsidiary of the constructor, made it virtually impossible for the Communities to exercise technical and financial control over an operation for which, in the end, they would bear the final cost ⁽⁶⁾.

6. The whole programme was organised by the Luxembourg administration without abiding by the spirit of the Community procedures for public contracts ⁽⁷⁾. The invitation to tender was particularly limited. The constructor of Annexe A was chosen by means of a restricted invitation-to-tender procedure whereby the tenderers had only 20 days, in August 1985, to submit their bids. In 1989 when it came to building Annexe B and again in 1992 for Annexe C, the contract was awarded to the same constructor, without the contract being genuinely put out to tender.

Execution and occupation of the buildings

7. The conditions under which the buildings were constructed (adaptation to meet the Court of Justice's needs) and the cost of this work were directly affected by poor coordination and by the fact that the Court of Justice had little power to exercise any control during the course of the work (especially as regards the extra costs arising from putting right defects caused by bad workmanship and from design and execution errors).

8. The expenditure ceilings (totalling LUF 3 940 million, inclusive of VAT, or about ECU 100 million) initially laid down by the laws ⁽²⁾ authorising the Luxembourg administration to have the annexes built were not complied with. The overall financial budget had to be increased, as of 1992, by LUF 740 million (about ECU 18 million) to cover the additional work requested by the institution, and also to cover the work on public roads and the remedying of bad workmanship, the cost of which looks likely to end up being borne by the Court of Justice.

9. The Court of Justice put itself into a situation from which it was unable to extricate itself: as of September 1988, without first agreeing any lease, it went ahead with gradually occupying buildings for which it did not know the exact cost and where the financial conditions concerning its tenancy had been neither defined nor approved beforehand by the parties concerned

10. Between 1989 and 1994, the Court of Justice, which was occupying the buildings without a lease, paid over LUF 1 500 million (about ECU 35 million) by way of advances on rent payments to be adjusted. These amounts corresponded to the total budgetary appropriations available under the budget item 'Rent'. The Court of Justice's Financial Controller granted his approval to the commitment proposals and the corresponding payment orders even though these practices were irregular under the Community's Financial Regulation, which allows rent to be paid only on the basis of adequate supporting documents, in this case, a lease agreement.

11. At the time, the Court of Justice was in the situation of renting and not yet of buying the buildings. Even though the Luxembourg administration clearly expressed its intention of setting the rent at a level sufficient to offset the construction costs ⁽⁶⁾, the amounts thus paid for the annexes were not fixed on the basis of a prior assessment, involving consultation of the parties concerned, of the true costs of each of the buildings, but in accordance with the amount asked for by the Luxembourg administration, whose requests the Court of Justice passed on to the Budgetary Authority. This being so, the amounts paid by the institution are not the result of verified economic parameters but mainly of the appropriations it was thought likely the Budgetary Authority would grant.

Agreement with a view to purchasing the buildings

Legal and financial aspects

12. An Agreement was signed on 15 November 1994 between the Luxembourg administration and the Court of Justice whereby the Luxembourg administration rents out Annexes A, B and C to the Court of Justice, with a view to their purchase by the European Communities. The Agreement expires on the date on which the European Communities take over ownership of the buildings, at the latest in 2015. It can be revoked prior to that, in the event of the seat of the Court of Justice being moved outside Luxembourg by a decision taken on the basis of Article 289 of the EC Treaty. There are some grave inconsistencies in this Agreement. The Luxembourg administration undertakes to sell buildings which, at the time, it does not yet own. The Agreement also contains clauses ⁽⁸⁾ which derogate from ordinary law and are likely to do grave damage to the Communities' financial interests, and it is vague on the crucial matter of the arrangements for determining and checking the selling price.

13. The financial arrangements made for building the annexes impose upon the Court of Justice the obligations of a borrower, without granting it the corresponding advantages in return (for example, ownership of the buildings thus financed). Formally, the intermediaries, the Luxembourg administration and the property developer, are legally responsible. However, they do not bear the cost of the commitments they have entered into. Quite apart from the fact that the Communities' Financial Regulation does not make any provision for having recourse to borrowing in order to make purchases of property, under such an arrangement the Communities are in the position of being unable to exercise any control over the financial costs they are obliged to bear, whatever their amount.

14. Within the framework of the implementation of the Agreement of 15 November 1994, the Communities are currently finding that they are being obliged to bear numerous items of expenditure related to the construction costs of the buildings (expenditure for work outside the buildings, construction of a link road). The Communities had to negotiate in order finally to obtain the exemption from VAT stipulated in the Protocol on the Privileges and Immunities of the Communities. Before they finally become the owner of these buildings, the Communities will also have to pay for the land at a price which was not fixed in the Agreement. The fact that the Communities have to bear the burden of these costs goes beyond what was initially agreed (?) when the two partners were still in a renting situation. In addition, there is no justification whatsoever for meeting the cost of the road.

Construction costs and financial costs

15. The task of determining and checking the construction costs was put in the hands of an expert. These costs were supposed to be determined and checked on the basis of data received by the Luxembourg administration, but in this particular case, these data do not on the whole give adequate information on the nature of the work carried out. The Court of Justice did not ask for documents to be provided which could have supplied documentary proof of additional work amounting to LUF 629 million (approximately ECU 15 million) although the expert brought them to its attention.

16. The construction costs for the annexes were not kept under control. On the basis of the calculations made by the expert, they exceeded the initial estimate by 49 % and were 25 % in excess of the new ceiling fixed in 1992 to allow additional work to be carried out on the three annexes (see *Table 1*).

17. The documentation compiled to date by the expert to justify the financial expenses and financial revenue booked to the operation remains inadequate and his checks incomplete. The documentation still does not give adequate assurance that these costs and products have been calculated correctly. The financial costs, which represent 36 % of the cost of the operation, appear high. They include considerable charges connected with the advance financing of the operation by the property developer.

18. The audit reveals shortcomings in the checks on the invoices submitted by the property developer (supporting documents for certain additional work, allowances made for less costly work/materials than originally estimated). In view of the amounts involved (just over ECU 2,5 million) and the risk that the Communities will continue to have to bear them, the Court of Justice should institute additional inquiries.

Rent for the Palais

19. Contrary to a commitment, made in 1984 within the framework of the negotiations concerning the building of the annexes, to reduce the rent for the main building, the Palais, by an amount equivalent to the repayment of loans on this building, in 1994 payment in full of the sums due under the initial rental agreement continued to be demanded, even though the Palais had by then been paid off. The Court of Justice then decided to suspend payment of this rent as from 1995. Subsequently, in 1996, the Court of Justice agreed to resume paying this rent as from 1997. The Court of Justice's motive at the time went beyond the mere obligation to fulfil its contractual commitments and had more to do with its assessment of what was acceptable in budgetary terms in respect of the total amount of rents demanded than with an evaluation of their justification. Such an attitude, which results in the Communities having to bear financial costs according to the amount of appropriations entered in their budget, is not in itself indicative of sound financial management.

Conclusion

20. The Court of Justice undertook a major property-development programme in order gradually to extend the premises it occupies on the Kirchberg plateau under circumstances which call for the following comments:

- (a) implementation of the programme was entrusted to the Luxembourg administration without adequate information having been passed on beforehand to the Budgetary Authority and without the financial, administrative and technical conditions for its implementation having been laid down in a contract between the parties concerned;
- (b) the implementation of this programme was in turn subcontracted to a property developer within the framework of legal and financial arrangements which have proved costly;
- (c) the arrangements accepted by the Court of Justice, the user of the buildings, made it virtually impossible to monitor the implementation and to control the costs;
- (d) as from September 1988 the Court of Justice occupied the buildings placed at its disposal without a rental agreement and made 'payments on account' for these buildings which were in contravention of the Community's Financial Regulation;

- (e) subsequently, in November 1994, it concluded a lease-option agreement in respect of which we must express the following reservations:
- (i) in particular, in order to become the unconditional owner of the buildings, the Court of Justice will have to pay the market price for the building sites, which were initially supposed to be made available to it free of charge;
 - (ii) the task of determining the selling price of the buildings was entrusted to an independent expert but the restrictions imposed on his checks mean that no assurance can be given that the selling price truly reflects the real costs of the operation;
 - (iii) certain costs which the Communities were not supposed to have to pay have to date been entered in the accounts as being charged to the Communities;
- (f) lastly, invoicing irregularities involving significant amounts have been discovered, which should necessitate additional inquiries by the Court of Justice to ensure that the Communities do not end up having to pay for them.

Recommendations

21. The circumstances surrounding the construction and acquisition of the Court of Justice's annexes are a graphic illustration of the problems encountered by the European institutions in trying to carry out their building projects in accordance with the principles of legality and regularity and sound financial management. Recurrence of such situations could be avoided by means of appropriate measures (the need for which has already been pointed out on several occasions by the Court of Auditors⁽¹⁰⁾), which would put the Communities' buildings policy on a transparent, efficient footing. Consideration should, in particular, be given to the following recommendations:

- (a) the Community institutions must always obtain the *prior approval of the Budgetary Authority* before embarking on a large-scale building project, whatever form this takes and whatever the purpose (rent, lease-option, acquisition, etc.);
- (b) the purely annual budgetary approach to expenditure on buildings does not satisfy the *criteria of sound management*. It induces the institutions to launch their building projects without taking a sufficiently long-term perspective and, subsequently, to confront the Budgetary Authority with a *fait accompli*. In order to plan their property policy with the greatest

transparency and efficiency possible, the creation of a multi-annual investment budget, to which differentiated appropriations should be allocated, appears indispensable;

- (c) the Communities must have *complete administrative, technical and financial control* over their building projects and must equip themselves with the necessary legal, technical and financial means. In this connection, interinstitutional Community departments should be set up on the initiative of the Commission, for example, in order to assist each Institution in defining and managing the administrative, technical and financial aspects involved in the overall control of the construction project. Consideration should also be given to amending the Community regulations in order to allow the Communities, where necessary, to finance their building programmes by borrowing directly under better conditions of transparency and cost than those which can be observed today in respect of the intermediaries and the financial arrangements to which they have recourse;
- (d) in the event of the Communities nevertheless wishing, by way of an exception, to delegate their powers of overall control of a project to third parties, a watering-down of responsibilities and the risk of cost overruns must be avoided. For this purpose, the *terms and conditions of the delegation* should be agreed in advance with the representatives of the parties concerned, on a contractual basis, and the latter should comply with the same obligations, in particular in respect of complying with competition rules, as those to which the Communities are subject. The way in which the respective responsibilities are to be shared out during the various phases of implementation of the programme must be clearly laid down. In particular, it should be compulsory for such contracts to contain a clause fixing a price ceiling, and to define meticulously the conditions under which it may be amended. This should not be allowed to take place without the agreement of the client institution and the prior approval of the Budgetary Authority.

22. Lastly, in the specific case of the annexes to the Court of Justice's main building, the Court of Justice should approach the Luxembourg administration to renegotiate those aspects of the 1994 Agreement which are causing problems (in particular, the question of who bears the cost of the work done outside the buildings and the question of the provision of the building sites).

This report was adopted by the Court of Auditors in Luxembourg at its meeting of 23 and 24 February 2000.

For the Court of Auditors

Jan O. KARLSSON

President

NOTES

- (¹) According to the terms of Article 1 of the Agreement of 15 November 1994.
- (²) According to the terms of the Luxembourg Authorisation Laws of 25 July 1985, 1 June 1989, 18 December 1990 and 28 December 1992.
- (³) According to the terms of the preamble to the Agreement of 15 November 1994.
- (⁴) For the purpose of constructing the extensions, the Luxembourg administration granted the property developer the surface rights and the right to the subsoil in respect of the land on which each building was to be constructed, in order for the property developer to arrange for the construction of the buildings of which he would become the owner. Upon expiry of the concession contracts, which were concluded for a period of 20 years starting from the provisional acceptance of the buildings, the contracts stipulated that ownership of the buildings would revert to the Luxembourg administration. Furthermore, the Luxembourg administration concluded with the property developer a leasing-purchase agreement for each building whereby, as of the provisional acceptance of the buildings, they would be rented to the Luxembourg administration for a period of 20 years. The agreements made provision for the possibility of the Luxembourg administration subletting or transferring its rights. The price of the leasing-purchase was fixed in accordance with the amount of the loans granted to the property developer. Under this arrangement, the Court of Justice has the status of sublessee.
- (⁵) The constructions were financed by means of bank loans granted to the property developer, the terms of which were negotiated by the Luxembourg administration. However, some items of expenditure, such as the architects' fees, were paid directly by the Luxembourg administration. The loans were used by the property developer to settle the invoices submitted by the general company in charge of the work, once they had received the prior approval of the public works administration, and for the annual loan repayments during the construction stage. In reality, as soon as each construction was accepted, the Luxembourg administration directly paid off the amounts still due to the bank in respect of the loans granted to the property developer. In order to regularise this transfer of obligations, in 1994 the property developer officially passed over to the bank the claims he held on the Luxembourg administration under the leasing-purchase agreements.
- (⁶) Initially, the amounts of rent to be paid by the sublessee (the Court of Justice) were supposed to be fixed taking into account both the period of repayment of the loans that would have to be taken out and the rates of interest to which these loans would be subject.
- (⁷) In particular, Council Directive 71/305/EEC concerning the coordination of procedures for the award of public works contracts (OJ L 185, 16.8.1971), which was transposed into Luxembourg law by means of the Law of 4 April 1974 (*Mémorial grand-ducal* A Issue No 36 of 13 May 1974).
- (⁸) Basically, a clause whereby, if the Court of Justice does not announce its intention of purchasing the land on which the annexes are built at the market price, these annexes will become the property of the Luxembourg administration upon expiry of the surface rights granted in the Agreement (49 or 98 years, depending on the case).
- (⁹) In June 1983, the Chairman of the Coordinating Committee for the setting-up of European institutions and bodies had told the Court of Justice that the Luxembourg government would be prepared to bear the cost of the price of the land and the development of the surrounding area and to grant a special VAT exemption.
- (¹⁰) See previous work by the Court of Auditors on this subject:
— Special Report on accommodation policies of the institutions of the European Communities (OJ C 221, 3.9.1979);
— Annual Report concerning the financial year 1987, paragraphs 10.41 to 10.77 (all the institutions);
— Annual Report concerning the financial year 1992, paragraphs 15.7 to 15.9 (Parliament);
— Annual Report concerning the financial year 1993, paragraphs 17.1 to 17.38 (Parliament) and 18.1 to 18.19 (Council);
— Annual Report concerning the financial year 1995, paragraphs 13.16 to 13.39 (Commission);
— Special Report No 5/95 concerning the signing without prior approval of the contract for the building of the European Parliament's new chamber in Strasbourg, paragraphs 5.1 to 5.16 (OJ C 27, 31.1.1996);
— Annual Report concerning the financial year 1998, paragraphs 6.13 to 6.17 (Commission).

THE COURT OF JUSTICE'S REPLIES

The Court of Justice wishes to state, at the outset, that it endorses the finding made by the Court of Auditors, following its examination of the Court of Justice's expenditure on buildings, that the budgetary and financial framework within which the European institutions have to meet their accommodation requirements is inappropriate; it therefore fully concurs with the recommendations made by the Court of Auditors with a view to remedying the situation.

Nevertheless, it is within that framework that the Court of Justice, in collaboration with the Luxembourg authorities, has been constrained, over the last twenty years, to take steps to cope with its constantly and rapidly growing accommodation requirements, which have been determined by a substantial increase in its caseload, the creation of the Court of First Instance and the growth in the number of staff employed in the institution.

The Court of Justice wishes to emphasise that it has no control over the number of cases to be dealt with or over the amount of work which those cases generate, and that, if it is to ensure continuity in the judicial task entrusted to it by the Treaties, it must have the necessary premises and infrastructures to enable the administration of justice to function properly.

It is against that background — which is, in essence, common to all the institutions but which is also characterised by certain specific factors peculiar to the Court of Justice — that the comments set out below, which are submitted in response to the report of the Court of Auditors on the Court of Justice's expenditure on buildings (hereinafter referred to as 'the Court of Auditors' report'), need to be read. Those comments deal with the following topics:

1. Changes in the accommodation requirements of the Court of Justice between 1979 and 1994, and the ways in which those requirements have been met;
2. The occupation of the annexes to the Palais without a written contract;
3. The relations between the Court of Justice and the Budgetary Authority;
4. Monitoring of the cost of constructing and financing the buildings annexed to the Palais;
5. The lease-option agreement of 15 November 1994;
6. Conclusion.

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1. *Changes in the accommodation requirements of the Court of Justice between 1979 and 1994, and the ways in which those requirements were met*

For the purposes of considering the remarks made in the Court of Auditors' report, it is necessary briefly to recall the context in which the accommodation requirements of the Court of Justice evolved between 1979 and 1994 (see the annexed brief chronology).

1.1. **Provisional solutions in response to constantly and rapidly evolving requirements**

It became apparent as early as 1979 that the main building of the Court of Justice (the Palais) was inadequate to accommodate all the staff of the institution, which was growing rapidly. As a result of the 1981 and 1986 enlargements and the setting-up of the Court of First Instance in 1989, the number of members of staff of the Court of Justice increased from 363 in 1980 to 733 in 1989 — a rise of 102 %. In order to cope with that increase, it became necessary to rent 40 offices in the Jean Monnet building in 1979, followed by a further 80 in 1980. Towards the end of 1985, 140 offices were installed in prefabricated huts at Weimershof. Following the 1986 enlargement and the abandonment of the prefabricated buildings on the Weimershof site in 1988, it became necessary to rent a further 150 offices in the BAK building.

1.2. **An unsatisfactory state of affairs**

The renting of those various office premises outside the precincts of the institution, at locations some distance from the Palais, was unsatisfactory from a functional standpoint; for an institution such as the Court of Justice, whose activities are closely interconnected, the scattering of its departments over a number of different sites gives rise to a substantial loss of time and efficiency.

Moreover, the prefabricated buildings rented at Weimershof did not fulfil current criteria in terms of hygiene and comfort.

It further became apparent, from 1985 onwards, that the Palais was inadequate not only as regards office space but also, and above all, as regards the institution's requirements with respect to courtrooms equipped with interpreters' booths, particularly in anticipation of the creation of the Court of First Instance.

1.3. **An appropriate response: the construction of the annexes**

The first annexe (Annexe A or the Erasmus building), the construction of which was decided in 1984, was handed over in October 1988, nine years after the Court of Justice had formally notified the Council of its accommodation problems. The further space provided by Annexe A, amounting to some 300 offices, meant that the prefabricated premises in Weimershof could be vacated; in addition, it comprised the offices and courtrooms

needed for the activities of the Court of First Instance, which had been created in the interim and was inaugurated in September 1989.

Annexe B (the Thomas More building), the construction of which commenced when the Financing Law was passed in June 1989, was handed over in 1992, enabling the requirements arising from the 1986 enlargement to be met in part.

Annexe C was completed and occupied in October 1994; its construction had been decided on in 1989 and the corresponding financing law was passed in December 1990, not only with a view to coping with the future enlargement in 1995 but also on account of the presence of asbestos in the Palais and the European Parliament's insistence on recovering possession of the premises occupied by the Court of Justice in the BAK building. It was not until that building was handed over that it became possible, for the first time in 15 years, to accommodate all the staff within one and the same complex of buildings.

The annexes to the Palais, successively constructed and handed over as described above, have therefore replaced a series of make-shift facilities, thereby providing the Court of Justice with premises suitable for its task and its operation. As indicated in paragraph 2 of the Court of Auditors' report, those buildings were constructed one after the other in order to meet constantly evolving requirements. They have not from the outset formed part of a comprehensive building programme.

1.4. **A buildings policy evolving in parallel with that of the other Community institutions**

In seeking to resolve its accommodation problems in such a way as to enable it to perform its judicial functions to the best of its ability, the Court of Justice, like all the other Community institutions, initially chose the option of renting, having considered and then rejected the idea of financing certain buildings itself. Prior to 1992, at a time when the seats of the Community institutions had not been definitively fixed and the Budgetary Authority had not yet adopted its policy in favour of the purchase of premises, the Court of Justice was not in a position to spearhead a new buildings policy, which it was for the political institutions of the Community to define.

Thus, it was only when that new buildings policy had been clearly defined by the Budgetary Authority in 1992 that the Court of Justice could begin to consider the possibility of purchasing the annexes.

The observations contained in the Court of Auditors' report must be read in the light of that situation.

2. **The occupation of the annexes to the Palais without a written contract**

In paragraph 9 of its report, the Court of Auditors criticises the Court of Justice for having entered into occupation of the annexes

to the Palais without first signing a written contract. The following comments need to be made in that regard.

Once the plans for the construction and leasing of a first annexe had taken shape, the Court of Justice informed the Luxembourg authorities of its wish to reach agreement as to the rent to be paid by the institution.

However, it was not possible to enter into proper negotiations concerning the precise amount of the rent until 1989, six months after the entry into occupation of Annexe A, when the Court of Justice received from the *Comité de Coordination pour l'Installation d'Institutions et Organismes Européens à Luxembourg* (CCIOE), the relevant Luxembourg interministerial coordinating body, a draft lease in respect of that annexe. The Court of Justice thereupon insisted on the conclusion of a lease of Annexe A as soon as possible and on the immediate opening of discussions concerning the terms for the letting of the future Annexes B and C, with a view to avoiding the occupation of those buildings without any written agreement (letter from the Registrar to the President of the CCIOE of 8 May 1989).

The discussions were initially concerned exclusively with the amount of rent. To that end, comparative studies were prepared showing, in particular, the rents charged for the buildings occupied by the other institutions in the Kirchberg area. The representatives of the Court of Justice and the Luxembourg authorities reached agreement on the rent for Annexe A in May 1992.

The Court of Justice had meanwhile received draft lease agreements in respect of Annexes B and C. The rent per square metre was much higher than that agreed for Annexe A, and was well in excess of the rents charged in the Kirchberg area. The Court of Justice was concerned, first, to conclude agreements which accorded with the principles of sound financial management, particularly those of economy and cost-effectiveness (see Article 2 of the Financial Regulation of 21 December 1977 applicable to the general budget of the European Communities (OJ L 356, 31.12.1977, p. 1)), and, second, to follow the course outlined by the Court of Auditors in its 1979 report ⁽¹⁾ by ensuring that the lease included a purchase option. It therefore rejected those draft lease agreements.

As the policy that the Community institutions should purchase their buildings was firmed up, the thinking of the Court of Justice at this juncture was directed to the prospect of purchasing, which warranted the inclusion in the contract under discussion of a clause permitting deferred purchase. Since that clause necessitated negotiations between the Court of Justice and the Luxembourg State, the signature of a lease was postponed.

⁽¹⁾ Special Report of the Court of Auditors on accommodation policies of the institutions of the European Communities, in particular point 7.5.3 (OJ C 221, 3.9.1979, p. 1).

In the circumstances described above, the Court of Justice was faced with the choice of either:

- sacrificing the requirements of sound financial management by signing contracts at any price (that is to say, accepting without demur the firm and elevated demands put forward by the other contracting party); or
- allowing the ad hoc arrangements referred to in 1.1 and 1.2 above to continue, with the disadvantages that these entailed in terms of continuing and increasing disruption of its functioning; or
- meeting the most pressing requirement by entering into occupation of the annexes.

Mindful of its duty under the Treaties to ensure the continuity of its judicial task, and faced with the impossibility of concluding written leases on favourable terms, the Court thought it best to opt for the third of the above solutions pending the conclusion, on 15 November 1994, of the lease-option agreement (see point 5).

In the view of the Court of Justice, the formal irregularity resulting from the occupation of buildings without a written lease must be considered in the light of the constraints described above.

Occupation of the annexes without a written lease justified the payment of some financial consideration. This took the form of advances on rent, calculated on the basis of market rental levels and by reference to the rents paid by the other Community institutions in the Kirchberg area. The advances paid between 1988 and 1994 were taken into account as accrued instalments of the purchase price of the annexes (see point 5.3.2).

In paragraph 11 of its report, the Court of Auditors states that those advances were paid in accordance with the availability of budgetary funds and not on the basis of verified economic parameters. In actual fact, for as long as the Court of Justice remained in a renting situation, the advances paid by it were calculated by reference to the rents charged for comparable buildings occupied by the other institutions in the Kirchberg area ⁽²⁾. It was only when the Court of Justice envisaged the purchase of accommodation that the advance payments exceeded the rents charged for comparable premises in the Kirchberg area, in such a way as to correspond to the appropriations granted by the Budgetary Authority.

The Court of Auditors also states in paragraph 11 that the advances were not fixed on the basis of a prior, bilaterally negotiated assessment of the true costs of each of the buildings. However, for as long as the parties were in a lessor/lessee situation, the Court of Justice, as a mere lessee, was not in a position to require information as to the total construction cost and the financial arrangements adopted by the Luxembourg authorities, particularly as

⁽²⁾ See, in particular, the Annual Report of the Court of Auditors concerning the financial year 1987, point 10.50 (OJ C 316, 12.12.1988, p. 1).

regards the period of amortisation of the capital sums invested ⁽¹⁾. As a lessee, it sought to negotiate an acceptable rent. It was legitimately entitled to assume that the host country would choose an adequate amortisation period and that the amount of the rent would remain reasonable and at a level commensurate with that which a Community institution may expect from a host country which is seeking to develop a policy of providing seats for international organisations.

In those circumstances, the Financial Controller felt obliged to approve the proposals for expenditure commitments and the corresponding payment orders in respect of those advances.

3. *The relations between the Court of Justice and the Budgetary Authority*

At paragraph 4 of its report, the Court of Auditors expresses the criticism that the Budgetary Authority was not provided with prior information and that no prior authorisation was given for the conclusion of contracts in respect of premises, of whatever kind (renting, purchase or lease-option).

The question of the involvement of the Budgetary Authority in decisions of the Court of Justice in regard to premises arose in different ways, depending on whether those decisions related to renting or purchasing. Consequently, a distinction must be drawn between straightforward lettings (see point 3.1) and the lease-option agreement concluded in 1994 (see point 3.2).

3.1. *Straightforward lettings*

The Budgetary Authority was not only informed of the Court of Justice's intention to occupy new premises as a lessee (point 3.1.1); it invariably granted the appropriations needed to cover those letting costs (point 3.1.2).

3.1.1. *Information regarding the intention of the Court of Justice to occupy the new premises as a lessee, and the consequences arising from this*

At the beginning of 1979 the Court of Justice made the Budgetary Authority aware of its accommodation requirements; the Council then entered additional appropriations in the budget of the Court of Justice for the financial year 1980, with a view to the renting of additional offices.

⁽¹⁾ There was, moreover, nothing extraordinary about the fact that the Court of Justice was ignorant of the financial arrangements of the owners of the rented premises, particularly as regards amortisation of the capital invested, as is apparent from the answer given by Mr Burke on behalf of the Commission to a question from Mr Tyrell, a Member of the European Parliament (Written question No 2039/83 (OJ C 194 23.7.1984, p. 1)).

With respect to the same financial year, the Council also granted appropriations for the financing of studies concerning the possibility of accommodating certain departments of the Court of Justice in a building to be constructed in the immediate vicinity of the Palais. Subsequently, in May 1984 (see letters from the President of the Court of Justice to the President of the Council and from the Registrar to the Chairman of the Permanent Representatives Committee and to the Chairwoman of the Council's Budgetary Policy Committee), the Council was informed of the Court of Justice's intention to rent an annexe to be constructed. The Council indicated its agreement to this. Although that letting was special in that the context was that of a building to be constructed in order to meet the specific requirements of the Court of Justice, the Budgetary Authority could not have been under any misapprehension as to the intention of the Court of Justice to rent that building. That intention was clearly indicated in the letters sent by the Court of Justice and, later on, in the Luxembourg Financing Law of 1985 authorising the construction of the first annexe, in which those offices were to be located. That law stated that 'the best way of achieving the proposed extension within a short space of time was for the Luxembourg Government to construct an annexe to the Palais of the Court of Justice, to be let to the Court, like the Palais itself, once it was completed'.

The Council was also informed of the Court of Justice's view that the renting option was not to result in any increase in its budget within the immediate future and of the Court of Justice's intention of approaching the Budgetary Authority as soon as any increase in the budget proved to be necessary on account of changes in its requirements. The view expressed by the Court of Justice was based on the consideration that the costs of renting the first annexe would be covered in the immediate future by the appropriations granted for the renting of offices outside the Palais. At no time did the Court of Justice conceal the fact that its budget resources would have to be adjusted to meet its accommodation requirements, which were constantly and rapidly evolving.

The Council endorsed the solution proposed by the Court of Justice.

3.1.2. *The grant by the Budgetary Authority of the appropriations needed to cover the costs of renting*

The appropriations needed to cover expenditure in respect of the renting of premises were granted by the Budgetary Authority within the context of the drawing up of the annual budget (see point 3.1.2.1). The Budgetary Authority was also informed of the multiannual forecasts of the Court of Justice as soon as an appropriate framework was set up to that end (see point 3.1.2.2).

3.1.2.1. *The involvement of the Budgetary Authority in the drawing up of the annual budget*

Where increased appropriations proved necessary in order to meet the costs arising from existing or planned lettings, the Budgetary Authority was invariably given due notice to that effect, within the context of the drawing up of the annual budget.

The requests for budget appropriations, accompanied by supporting documentation, which the Court of Justice submitted to the

Budgetary Authority with a view to covering rental costs were the subject, throughout the period under consideration, of systematic and thorough discussion within the Budgetary Committee of the Council and the Committee on Budgets of the European Parliament, on the occasion of the examination of each draft budget submitted by the institution. Up until 1997, the Budgetary Committee of the Council carried out an examination of each heading of the draft budget, and the heading entitled 'Rent' generally gave rise to detailed debate, particularly between the representative of the Grand Duchy of Luxembourg and the representatives of the other Member States.

As regards, more particularly, the first financial year during which the cost of renting the first annexe was incurred (1988), the estimates showed, under heading 200 ('Rent'), the amount needed for 'rent of the new annexe to the Court building for four months, less the rent of the Jean Monnet building for the same period'. The fact that the appropriations in question were granted can be taken to signify the agreement of the Budgetary Authority to the renting of that first annexe. The Budgetary Authority had received a request for appropriations in the spring of 1987, and had had the opportunity to express its comments throughout the course of the procedure for approval of the 1988 budget. Thus, the resolution of the European Parliament on the draft budget for 1988 notes that 'the occupation by the Court of its new annexe, the floor area of which is the same as that of its current premises, will inevitably lead to a significant increase in its financial requirements' and the Rapporteur proposes that 'the expenditure connected with the occupation of its new building by the Court of Justice should be covered by the allocation of adequate funds'.

3.1.2.2. The information provided to the Budgetary Authority within the framework of multiannual estimates

Despite the absence of any appropriate framework for the submission of multiannual budget estimates, the Court of Justice kept the Council constantly informed of the foreseeable course of its development and of its accommodation requirements, having regard, in particular, to the increase in its workload, the successive enlargements of the Community, the extension of its jurisdiction, the creation of the Court of First Instance and the growth in the number of staff.

When, following a decision of the Group of the Heads of Administration, the appropriate framework for the submission of multiannual budget estimates of administrative expenditure was set up in 1988, the Court of Justice, like the other institutions, submitted such estimates, including those relating to expenditure on rent over the period from 1989 to 1992, to the Budgetary Authority. Those estimates were accepted by the Budgetary Authority on the basis of a communication from the Commission. They did not, however, prompt the Budgetary Authority to establish a multiannual investment budget endowed with differentiated appropriations.

3.2. The lease-option agreement of 1994

In 1979 the Court of Auditors published a report recommending that premises occupied by the Community institutions should be

purchased rather than leased. In 1981 the Council stated that it was not opposed in principle to the purchase of premises by the institutions. However, as noted by the Court of Auditors, the Council refused, as budgetary authority, 'to provide the necessary financial resources' for the purchase of premises (Council Decision of 14 December 1981, cited in points 10.62 to 10.66 of the Court of Auditors' Annual Report concerning the financial year 1987 (OJ C 316, 12.12.1988, p. 1)). In July 1990 the Rapporteur of the Committee on Budgets of the European Parliament contemplated, in the context of that committee's examination of the 1991 budget of the Court of Justice, the entry in that budget of the appropriations needed for the purchase of the Palais and Erasmus buildings. However, that idea never bore fruit, since, despite the wording of Resolution A3-360/90 of the European Parliament, the appropriations entered in the 1991 budget were only those intended to cover the rent for the two buildings in question.

Although the construction of Annexes A, B and C had taken place with a view to the conclusion of a lease, and while the Court of Justice was persevering with its attempts to obtain the host country's agreement to a reasonable rent, the new circumstances described above prompted the Court of Justice to contemplate the inclusion of a purchase option in the lease under discussion.

In 1992, as indicated above, the Budgetary Authority established a policy in the matter of premises which unequivocally advocated the purchase by the institutions of the buildings occupied or to be occupied by them.

The consolidation of that new policy of the Community institutions with respect to premises and the increasingly favourable reception given by the Budgetary Authority to the idea of purchasing Annexes A, B and C, coupled with the Luxembourg authorities' wish to calculate the rent on the basis of amortisation of the capital sums invested over a 20-year period, speeded up the negotiation of an agreement by which the payment of rent was to be combined with the deferred purchase of the buildings.

That change in approach led to increased contact between the Court of Justice and the two branches of the Budgetary Authority.

The Budgetary Authority was of course duly informed that an agreement was being negotiated with the Luxembourg authorities; indeed, it decided in 1994, by way of a supplementary and amending budget, to allocate the sum of ECU 9,476 million to the Court of Justice before the end of the current financial year, with a view to 'partially covering the difference between the rent demanded by the Luxembourg State for the Court's new complex of buildings, on the basis of a lease incorporating a purchase option, and the amount which can be paid under the budget of the institution'. Since the use of those appropriations presupposed the conclusion of a lease containing a purchase option, the European Communities, represented by the Court of Justice, and the Luxembourg State signed a lease-option agreement on 15 November 1994, following several years of negotiations.

The text of the lease-option agreement was communicated to the Budgetary Authority.

In 1996 the Budgetary Authority requested and obtained from the Court of Auditors a technical opinion concerning the financial commitments governing the premises of the Court of Justice. That opinion contained no criticism of the legal and financial arrangements set up by the agreement, or any reservations regarding the advance payment of the purchase price in addition to the annual rental payments contemplated (see in that regard point 5.2). In consequence of that opinion, the sum of ECU 50 million was made available to the Court of Justice in order to enable it to make an advance payment pursuant to the agreement.

It is clear, therefore, that the Budgetary Authority was involved in the plans for the purchase of buildings by the Court of Justice pursuant to the lease-option agreement.

4. Monitoring the cost of constructing and financing the buildings annexed to the Palais

The Court of Auditors expresses the criticism that there was a lack of monitoring of the implementation of the building projects and the constituent elements of the construction costs (see paragraphs 5, 7, 11 and 20(c) of the Court of Auditors' report).

It is necessary to draw attention to the conditions in which monitoring could be carried out (see point 4.1) and the gradual intensification of monitoring (see point 4.2).

4.1. The conditions in which monitoring was carried out

Monitoring was subject, first, to internal constraints (see point 4.1.1) and, second, to the nature of the relations between the institution and the Luxembourg authorities (see point 4.1.2).

4.1.1. Internal conditions

The task of the administrative departments of the Court of Justice is to provide support for its judicial activities and to undertake the day-to-day management of the institution. The staff of those departments, relatively few in number, do not possess the extensive range of skills that are necessary to ensure detailed and extensive monitoring, from a technical and financial standpoint, of construction operations on such a large scale. This led the Court of Justice in 1986 to sign a contract with Bouwcentrum, a Netherlands firm of experts; however, that firm was unable to perform its task properly.

It was in those conditions, and at times in circumstances demanding urgent action, that the Court of Justice was constrained to take decisions in order to meet its accommodation requirements and that the expenditure in that respect was monitored.

4.1.2. Relations with the Luxembourg authorities

In addition, monitoring by the Court of Justice was circumscribed by the nature of its relations with the Luxembourg authorities.

The relationship, in the matter of land and buildings, between a Community institution and the Member State in which the seat of that institution is located cannot be judged by the yardstick of a contractual relationship between a private lessee and a private lessor.

The Court of Justice is in a special position as a lessee, in that it has specific requirements in terms of construction (buildings accessible to the public, courtrooms equipped with interpreters' booths, etc.) which go beyond a mere need for office space. The Luxembourg authorities used that special position as an argument for fixing the rent in accordance with the cost of construction. The Court of Auditors' report contends that such a method of proceeding should have prompted the Court of Justice to envisage monitoring the cost of the construction and to require that the detailed arrangements of the building programme be formally set down in writing. It is further claimed that, while the parties were in a lessor/lessee situation, the Luxembourg authorities should have agreed to involve the Court of Justice in the definition of those arrangements.

The Luxembourg authorities did not however feel bound to involve the Court of Justice in the working out of the financial arrangements criticised in the Court of Auditors' report, or in the selection of the architect, the property developer and the main contractor.

It was not until the Court of Justice was called on to assume ownership of the premises that it was able to learn of the financial arrangements. However, its relations with the Luxembourg authorities continued to be affected by the situation obtaining at the outset. It experienced recurrent problems in obtaining the information needed for monitoring, whether in relation to the amount of the rent, exemption from VAT or the purchase of the land, and in obtaining explanations concerning certain alterations and additional works. A typical example of the ambiguity characterising the relations with the Luxembourg authorities is to be found in the fact that, despite their agreement to transfer ownership of the annexes on a non-profit basis, they continued to demand rent for the Palais notwithstanding that the cost of that building had been amortised a long time previously and despite the undertaking given by them in 1984 to reduce the rent in question in line with the amortisation of the cost of the building.

4.2. A gradual intensification of monitoring

Monitoring by the Court of Justice gradually increased in intensity (see point 4.2.1) and was ultimately placed on a systematic footing within the framework of the lease-option agreement (see point 4.2.2).

4.2.1. The intensification of monitoring

The representatives of the Court of Justice attempted on several occasions to influence the choices made by the Luxembourg authorities, but without ever obtaining a satisfactory result. During the period in which the Court of Justice was in the position of a future lessee, the points which it raised related in essence to its operational requirements, and even they were not always acted on.

Following its entry into occupation of the first annexe (the Erasmus building) in the autumn of 1988, the Court of Justice put forward numerous demands with a view to ensuring that that building should be rendered more fit for its intended purpose and that the matters thus raised should be taken into account in the early stages of the drawing up of plans for the construction of other buildings in the future. Those demands were intended to avoid the substantial additional costs brought about by works of rectification.

Once it was established that the Court of Justice was to become the owner of the buildings, it submitted observations on the various aspects of the cost of their construction. This was particularly the case as regards Annexe C, the construction of which commenced in February 1992 and the original plans for which were significantly modified at the behest of the Court of Justice. At that juncture, however, the financial arrangements had already been put in place by the Luxembourg authorities and the essential elements of the construction programme were fixed.

As regards the financial expenditure, it proved possible, following difficult negotiations entered into after the agreement had been signed, to persuade the Banque et Caisse d'Épargne de l'État ('BCEE') to agree to new terms of a more favourable nature. The Court of Justice took the view that, in the context of the lease-option agreement, it ought to attempt, in the interests of sound management, to renegotiate, through a representative of the Luxembourg Finance Ministry, the loan terms agreed between the Luxembourg State and the BCEE.

4.2.2. *The control mechanism introduced by the lease-option agreement*

The agreement provided for a mechanism of control (see point 5).

In response to paragraph 16 of the Court of Auditors' report, it should be noted that, in certain instances, the fact that the initial financial estimates were exceeded is due to demands made by the Court of Justice which were justified by changes in its requirements (e.g. the construction of an additional storey in Annexe C, an increase in the number of interpreters' booths needed, etc.).

5. *The lease-option agreement of 15 November 1994*

The lease-option agreement, which was adopted following lengthy negotiations (see point 5.1), establishes a mechanism (point 5.2) and lays down the constituent elements of the final purchase price of the buildings (point 5.3), which does not include certain items of expenditure which the Luxembourg authorities had undertaken to bear in 1983 and 1984 (point 5.4); it was negotiated independently of the lease of the Palais (point 5.5). Lastly, it safeguards the financial interests of the Communities (point 5.6).

5.1. **The genesis of the agreement**

Reference should be made in this connection to point 3.2.

The agreement represents a compromise resulting from protracted negotiations between the Court of Justice and the Luxembourg authorities, rather than the ideal form of contract which the Court of Justice aspired to conclude.

5.2. **The mechanism set up**

The Court of Auditors is fully aware of the mechanism set up by the agreement, which it described in its technical opinion of 30 May 1996 regarding the financial commitments governing the premises of the Court of Justice. The features of that mechanism may be summarised as follows.

The agreement does not fall within any specific category of contracts. It is *sui generis*, combining elements of a lease and of sale and purchase. Under its terms, the Luxembourg State covenants in particular to transfer ownership of the buildings to the Court of Justice (following the transfer of those buildings to the State by the property company responsible for their construction). For its part, the Court of Justice covenants, by paying annual instalments, to reimburse to the State, at cost price, the investment made by the latter, without any profit or loss to the State. The annual instalments are treated as advance payments towards the purchase of the buildings by the European Communities (Article 8(1) of the agreement). They continue to be payable until such time as the total amount paid out corresponds, in the aggregate, to the purchase price less VAT.

Although the effects of the agreement extend from 1 August 1988 (the date on which occupation of (part of) the premises first commenced) until the date on which the European Communities become the owners of all three annexes, namely 31 December 2015 at the latest, the annual instalments became payable only from 1 January 1995. The sums paid in respect of the occupation of the buildings between 1988 and 1994 were treated as accrued instalments of the purchase price (see point 5.3.2).

The amount of each annual instalment may be adjusted to take into account any advance payments made, over and above the annual instalments, towards the purchase price (Article 8(2) of the agreement). The amount in question was initially fixed in the sum of LUF 633 520 000 (ECU 16,3 million). Following the advance payment of ECU 50 million made in October 1996 in pursuance of the abovementioned opinion of the Court of Auditors, the amount of the annual instalments was reduced to LUF 405 000 000. That amount is subject to adjustment in the event of a significant increase in the rates of interest applicable to the loans used to finance the annexes.

5.3. **The purchase price**

5.3.1. *The constituent elements of the purchase price*

The agreement does not specify the purchase price; instead, it lists the factors by which that price may be determined.

The reasons for this are threefold: first, the rate at which the loans were granted is not fixed throughout the entire financing term, which means that the financing costs may vary in line with changes in the rate; second, certain construction costs were not yet known by the parties when the agreement was concluded; and, third, certain construction costs were, and still are, the subject of disputes between the Court of Justice and the Luxembourg authorities (design faults and poor workmanship).

The purchase price of the buildings is determined by reference to the expenditure incurred, whether that expenditure is financed direct by the State or by the developer (Article 8(1) of the agreement). The expenditure in question is made up of the cost of construction, architects' and engineers' fees, costs relating to the financing of expenditure (commissions, guarantees and interest charges) and expenses incurred by the State as lessor.

5.3.2. *The inclusion of payments on account of rent made between 1988 and 1994 in the absence of a written contract*

Because of the absence of any written lease stipulating the terms of occupation of the annexes, the parties to the lease-option agreement found it necessary to depart from concepts strictly specific to a lease in deciding how the sums paid on account of rent between 1988 and 1994 should be characterised. In contrast to the situation prevailing in respect of the Palais, the occupation of which is governed by a written lease, the Luxembourg authorities acknowledged that it was legitimate to treat the sums paid on account between 1988 and 1994 (see points 2 and 5.2) as accrued instalments of the purchase price (Article 6 of the agreement) rather than as 'irrecoverable' rent.

5.3.3. *The procedures for determining the purchase price and the task of the independent expert*

Article 9 of the agreement provides that, on its entry into force, the parties are to appoint an independent expert whose tasks include, *inter alia*, calculation of the purchase price of the buildings. The expert's fees are to be borne in equal shares by the State and by the Court of Justice. An expert was appointed pursuant to that Article in February 1995.

The tender submitted by the expert, which was accepted by the Court of Justice and by the Luxembourg authorities and which thus forms the contractual framework of his task, provides for the submission by him of a report dealing in turn with four matters: first, the determination of the calculation parameters, second, the determination of the purchase price as at 31 December 1994, third, the annual determination of the flow of funds (financing costs, expenditure incurred by the Luxembourg State as lessor and VAT) and the annual updating of the purchase price and the balance payable and, fourth, the drawing up of the final statement of account.

The tender stipulates that the information needed to determine the purchase price as at 31 December 1994 is to be made available to the expert by the Luxembourg Ministry of Finance and Ministry of Public Works. According to the tender, 'the costs specified are to be determined and checked on the basis of the information received by the Ministries concerned. An audit is to be carried out on the basis of supporting documentation' (point 2.2 of the tender).

It can therefore be seen that the means placed at the expert's disposal for making a correct determination of the construction cost and for verifying that the purchase price reflected the actual costs of the operation were provided for under the agreement.

The amount thus determined is then to be used as the basis for working out the annually updated amount of the purchase price from 1988 onwards and the balance remaining payable. To that end, account is to be taken, first, of the sums paid in respect of annual instalments or advance payments and, second, of the costs and expenses incurred. The total balance payable by the Communities is to be shown for each year in the form of the updated purchase price of the buildings less the updated amount of the instalments paid by the Court of Justice and less VAT (Article 8(1) of the agreement).

In order to determine the flow of funds and the balance payable, the independent expert bases his calculations, first, on the data produced by the accounting system of the State's accounts department and, second, on the data provided by the bank statements relating to the BCEE loan accounts or other bank accounts relating to the agreement (point 2.3 of the tender).

The Court of Justice considers that, since the cost of construction, which serves as the basis for calculating the balance payable, is to be determined by reference to supporting documentation (that is to say, documents proving that the expenditure has been incurred pursuant to Article 8(1) of the agreement), the independent expert's task is not merely to check the expenditure in purely accounting terms but also to verify that that expenditure is justified. In the event that the construction cost appears to have been wrongly determined or the purchase price does not reflect the construction cost, it is to be rectified and a corresponding correction is to be made to the balance payable (see the first paragraph of point 5.6). The Court of Justice therefore considers that guarantees are in place to ensure that only the expenditure to be borne by the institution under the agreement is in fact borne by it.

5.4. **The treatment of the undertakings given by the Luxembourg authorities in 1984**

The Court of Auditors regrets that the agreement does not exclude from the total price items of expenditure which the Luxembourg authorities had unilaterally undertaken to bear in June 1983 and at the sitting of the Government Council on 30 March 1984.

It should be noted, first, that, as the Court of Auditors states in paragraph 14 of its report, those unilateral undertakings were given in a context which was totally different from the situation prevailing at the time of the conclusion of the lease-option agreement in 1994. That agreement was the outcome of a compromise based not on the unilateral undertakings given in 1983 and 1984 but, in essence, on negotiating points of a different nature, such as the classification of the sums paid on account of rent between 1988 and 1994 (see point 5.3.2).

Be that as it may, the lease-option agreement exempts the Court of Justice from having to bear various items of expenditure which the Luxembourg authorities had undertaken to bear in 1983 and 1984, such as those relating to the occupation of the land (point 5.4.1) and the construction of public roads (point 5.4.2).

5.4.1. *The problems connected with the land*

When, on 14 March 1994, the Luxembourg authorities submitted their initial draft agreement setting out the conditions governing the occupation of the annexes, the plan being, at that time, that ownership of the buildings should in due course be transferred (which was not the case in 1984), they stated that 'the price of the land is fixed at LUF 200 000 000 per hectare'.

The Court of Justice rejected that proposal, since it had at all times taken the view that a host country which is seeking to develop a policy of providing seats for international organisations should include in its offer the land on which the buildings to be purchased by the institution in question are located. It proved impossible to secure that result, since the Luxembourg authorities pointed out that the Court of Auditors had purchased the land on which its building was constructed. The Luxembourg authorities ultimately granted the Court of Justice a surface right by which it was to have free use of the land for a term of 98 years. The Court of Justice took the view that this was economically the most favourable arrangement, having regard to the purchase price proposed by the Luxembourg authorities.

Thus, under the 1994 lease-option agreement, the Court of Justice has free use, pursuant to a surface right, of the land on which the annexes are located. It is true to say, however, that it is not the owner of that land and that it will need to become the owner of it prior to the expiry of the surface right if it wishes to prevent ownership of the buildings from being transferred to the Luxembourg State.

It will be noted in that regard that the surface right leaves open, throughout the period of its currency, the possibility of negotiating the transfer of ownership of the land free of charge.

5.4.2. *The road system*

The subject-matter of the agreement is set out in detail in Article 1. It comprises the buildings and the appurtenances and annexes thereto registered in section E C (Weimerskirch) of the cadastral register of the municipality of Luxembourg under plot numbers 840/4284, 871/4923 and 871/4983.

The public roads are not covered by the agreement. Consequently, the cost of building those roads does not in any way constitute an item of expenditure to be taken into account in the calculation of the purchase price as determined in accordance with Article 8(1) of the agreement.

In response to paragraphs 8 and 14 of the Court of Auditors' report, it should be noted that Article 8(1) of the agreement enables the Court to exclude from the final price of the premises the cost of providing public roads such as the link road between the Boulevard Konrad Adenauer and the Rue du Fort Niedergrünwald, despite the fact that that road, which is designed to facilitate the flow of traffic, was built at the suggestion of the Court of Justice.

5.5. **The rent payable for the Palais**

In response to the final sentence of paragraph 19 of the Court of Auditors' report, the Court of Justice would point out that the rent for the Palais is fixed in point III of the lease concluded on 5 June 1973 between the Luxembourg State and the Court of Justice.

The Court of Justice has merely requested from the Budgetary Authority the appropriations needed in order to pay the rent contractually due, and has paid that rent by means of those appropriations.

5.6. **Preservation of the financial interests of the Communities**

It is apparent from the scheme of the lease-option agreement, from its preamble, from Article 8(1) and from the circumstances in which it was concluded (which involved a number of items of expenditure being challenged even before the agreement was signed: see the second paragraph of point 5.3.1) that the balance payable, as established on an annual basis by the expert, is merely an estimate which is subject to adjustment in the light of fresh information received, information not produced by the Ministries referred to (see 5.3.3 above) in the performance of their duties or fresh assessments of existing information.

Consequently, it cannot be concluded that the Court of Justice agreed to bear items of expenditure which should not be taken into account for the purposes of calculating the purchase price in the manner laid down by Article 8(1) of the agreement. On the contrary, the Court contested from the outset the inclusion of certain expenditure in that calculation (see the second paragraph of point 5.3.1).

As matters currently stand, there still exists a long list of points in dispute, and the Court of Justice is continuing its negotiations with the Luxembourg authorities with a view to excluding certain items of expenditure from the final statement of account.

The Court of Auditors points out, first, various inadequacies in the checks carried out both by the Luxembourg Government and by the independent expert (see paragraphs 17 and 18 of the Court of Auditors' report) and, second, the improper allocation of certain costs which has occurred as a result (see paragraphs 8, 14 and 20(f) of the Court of Auditors' report).

In order to ascertain the extent of the invoicing anomalies found to have occurred and of the financial costs which are not directly linked to the financing of the building works, the Court of Justice proposes to request the Luxembourg authorities, first, to carry out, or arrange to have carried out, further detailed investigations and, second, to give it access, either directly or through the intermediary of an external auditor, to all documents which may be of assistance for the purposes of determining the purchase price as defined in Article 8(1) of the agreement.

Clarification regarding that price must be provided by no later than the date on which the agreement expires, which is currently expected to be in 2007. Until then, indeed, until the two parties concerned have agreed the final statement of account, *any estimate of any loss suffered by the Communities can amount to no more than pure conjecture.*

The Court of Justice has no reason to think that performance of the agreement will not be in conformity with the principle of good faith in the performance of agreements, as laid down in the third paragraph of Article 1134 of the Luxembourg Civil Code, applicable pursuant to Article 19 of the agreement, according to which the agreement is to be governed by Luxembourg law.

There is even less reason to think that performance of that agreement is founded otherwise than on the principle of collaboration between the Community and the Member States laid down in the EC Treaty, of which the protection of the financial interests of the Communities forms part.

6. Conclusion

- From the outset, the building of each of the three annexes to the Palais has not formed part of any comprehensive construction programme; instead, each of those annexes has been built in turn in order to meet constantly evolving requirements,
- At the point in time at which the various building works were undertaken, renting was the sole solution foreseeable for the Court of Justice in view of the policy which the Community institutions were then pursuing in the matter of buildings,
- Whenever it requested appropriations in order to meet the rental obligations envisaged, the Court of Justice provided the Budgetary Authority with all the information which it itself possessed,
- The Court of Justice was not fully informed of the financial arrangements adopted by the Luxembourg authorities until it considered purchasing the buildings; as a lessee, it could not demand to be so informed,
- The Court found itself constrained to occupy the buildings without a written contract, and, having regard to the *de facto* occupation which resulted, it considers that the Luxembourg authorities were entitled to demand a *quid pro quo* and that the Court of Justice was consequently bound to make 'payments on account',
- Following the adoption by the Budgetary Authority of a buildings policy favouring the purchase of premises occupied by the Community institutions, the Court of Justice planned to purchase the annexes occupied by it; to that end, it signed a lease-option agreement which was the result of a compromise reached after lengthy and difficult negotiations,
- The Court of Justice considers that the task entrusted to the independent expert pursuant to that agreement involves not merely checking the expenditure in purely accounting terms but also verifying that that expenditure is justified,
- The Court of Justice further considers that the balance payable, as established on an annual basis by the independent expert, is merely an estimate which is subject to adjustment,
- The terms laid down by the lease-option agreement regarding the purchase price payable by the Court guarantee that the expenditure which the institution is actually required to bear is limited to that to be borne by it under the agreement,
- The Court of Justice will make further inquiries without delay, in order to satisfy itself that there has been no irregularity adversely affecting the financial interests of the Communities.

ANNEX

BRIEF CHRONOLOGY

1972	August	Occupation of the Palais
1973	January	Accession of Denmark, Ireland and the United Kingdom
1979	January	Communication from the Court of Justice to the Council concerning its long-term accommodation requirements (10 years)
	November	Occupation of 40 offices in the Jean Monnet building
1980	July	Occupation of a further 80 offices in the Jean Monnet building
1981	January	Accession of Greece
1982	May	Deferral by the Council of its examination of a buildings project for the Court
1984	May	In response to a proposal submitted by the Court, the Council agrees to the construction of a building containing 300 offices
1985	July	Law for the financing of the Erasmus annexe
	December	Occupation of 140 offices in huts at Weimershof
1986	January	Accession of Spain and Portugal
	September	Work commences on the construction of the Erasmus annexe
1988	October	Decision establishing a Court of First Instance of the EC
		Evacuation of the Jean Monnet building
		Partial evacuation of the huts at Weimershof
		Occupation of the Erasmus annexe
1989	February	Commencement of work on the construction of the Thomas More annexe
	June	Law for the financing of the Thomas More annexe
	September	Commencement of the activities of the Court of First Instance
		Occupation of the BAK building
		Total evacuation of the huts at Weimershof
1990	December	Law for the financing of Annexe C
1992	February	Commencement of work on the construction of Annexe C
	September	Completion of work on the construction of the Thomas More annexe
		Partial evacuation of the BAK building
1994	October	Completion of work on the construction of Annexe C
		Occupation of Annexe C by the Court of First Instance
		Evacuation of the BAK building
	November	Lease-option agreement concluded between the Court of Justice and the Luxembourg State
1995	January	Accession of Austria, Finland and Sweden
1996	November	Report on asbestos in the Palais
1998	September	Announcement by the Court of Auditors of the audit concerning the expenditure of the Court of Justice on accommodation
1999	January	Occupation of the T building (temporary alternative premises)
	July	Evacuation of the Palais