



THE CONSTITUTIONAL COURT OF THE REPUBLIC OF LATVIA

JUDGEMENT

On Behalf of the Republic of Latvia

Riga, 3 November 2011

Case No. 2011-05-01

The Constitutional Court of the Republic of Latvia, composed of the Chairperson of the Court hearing Gunārs Kūtris, Justices Kaspars Balodis, Aija Branta, Kristīne Krūma, Uldis Ķinis and Sanita Osipova,

having regard to a constitutional complaint of a limited liability company “HansaWorld Latvia”,

according to Article 85 of the Satversme [*Constitution*] of the Republic of Latvia, Article 16 1st indent, Article 17 (1)11th indent and Article 19.² and Article 28.¹ of the Constitutional Court Law

on 4 October 2011 in writing examined the case

“On Compliance of Section 39 (1) Indent 6 of the Public Procurement Law with Article 91 and 105 of the Satversme of the Republic of Latvia”.

The Facts

1. On 6 April 2006, the Saeima [*Parliament*] of the Republic of Latvia adopted the Public Procurement Law.

By means of 20 May 2010 amendments, Section 39 (1) indent 6 of the Public Procurement Law (hereinafter – the Contested Norm) acquired a new wording.

The Contested Norm provides that the commissioning party shall exclude a candidate or applicant from further participation in a procurement procedure, as well as shall not review the tender of an applicant in case if average remuneration of employees of a candidate or applicant registered in Latvia (has its domicile in Latvia) for the first three quarters of the year during the last year consisting of four quarters before the date of submitting a tender offer of an application is less than 70 per cent of average employee remuneration in the State for the same period and in the same field pursuant to NACE 2.red. qualification level of two figures pursuant to data summarized by the State Revenue Service and published in the home page of the State Revenue Service. If the candidate or the applicant is registered as a tax payer during the last year consisting of four quarters before the date of submitting a tender offer or an application, average monthly salary of employees for the period starting on the second month after the registration up to the date of submitting a tender offer or the application is taken into account.

According to Para 17 of Transitional Provisions of the Public Procurement Law, the Contested Norm shall be applicable as from 1 October 2010, before which the non-amended wording of the norm shall remain in force.

2. The person who submitted the constitutional complaint, the limited liability company “**HansaWorld Latvia**” (hereinafter – the Applicant) asks the Constitutional

Court to assess compliance of the Contested Norm with Article 91 and Article 105 of the Satversme of the Republic of Latvia (hereinafter – the Satversme).

It is indicated in the application that the Applicant had participated in a public procurement tender of the Ministry of Finance (hereinafter – the Procurement Procedure). The Applicant has been excluded from the Procurement Procedure based on the Contested Norm because, in the particular period, average wage of its employees were less than 70 per cent of the average employee wage in the State in the respective field indicated by the taxpayer (NACE 2. red.) – “6202” (consulting services regarding use of computers).

The Applicant holds that the Contested Norm fails to comply with Article 91 of the Satversme. The Contested Norm establishes a differentiated attitude towards persons enjoying similar and, according to certain criteria, comparable conditions; moreover, measures selected by the legislator are not appropriate for reaching the aim of the Contested Norm. The Fact that the salary paid by the employee exceeds the 70 per cent of the average wage established in the Contested Norm does not mean that the respective person makes all stipulated tax payments into the State budget. Moreover, the Contested Norm restricts the rights of such persons to participate in procurement procedures that have fulfilled their fiscal commitments in front of the State but still meet the exclusion criteria established in the Contested Norm.

The Applicant is of the viewpoint that the Contested Norm does not comply with Article 105 of the Satversme because the restriction established therein is neither proportional nor assures reaching of the legitimate aim. It is possible to reach the aim of the Contested Norm by applying other less restrictive measures, for instance, control of enterprises to be carried out by the State Revenue Service [*Valsts ieņēmumu dienests*] in case of doubt regarding tax avoidance. The Applicant also provides arguments regarding non-compliance of the Contested Norm with the 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

(hereinafter – the Directive 2004/18/EC). The Applicant holds that Member States do not have the right to extend the list of cases established in Article 45 of the above mentioned directive, in which a participant may be excluded from procurement procedure. Member States have the right not to apply certain exclusion criteria or to interpret them in a restricted way only. However, extended interpretation of exclusion criteria or setting forth of other criteria is unacceptable. Moreover, according to argumentation of the Court of Justice of the European Union, participation in procurement procedures may not be restricted based on an indisputable presumption. The Applicant refers to application practice of an Estonian legal norm similar to the Contested Norm and indicates that such legal regulatory framework has been cancelled because it did not comply with Article 11 and Article 31 of the Constitution of the Republic of Estonia that regulate general restrictive provisions of rights and protection of freedom of entrepreneurship. In the annotation to the amendments to the Estonian Public Procurement Act it is indicated that the State does not have the right to interfere with private law relations and regulate wage to be paid to employees otherwise than by establishing the minimum wage rate.

3. The institution that adopted the Contested Norm, **the Saeima of the Republic of Latvia** (hereinafter – the Saeima) does not share the opinion of the Applicant and holds that the Contested Norm does comply with legal norms of a higher legal force. To characterize the legitimate aim of the Contested Norm, the Saeima refers to facilitating welfare of the society and protection of rights of other persons because the norm favours tax payment, registered and legal employment, as well as fair competition. Taking into account the high rate of illegal employment and “envelope salaries”, it was necessary to limit the rights of dishonest merchants to participate in procurement procedures in order to ensure participation of those merchants who fulfil their fiscal duties in good faith.

The Contested Norm is appropriate for reaching of the legitimate aim because it permits obtaining a clear percept of wages paid by a candidate or an applicant (hereinafter – an applicant) to its employees, which is a substantial security and reliability

factor when assessing compliance of an applicant with requirements set forth in procurement documentation.

The Saeima holds that the Contested Norm is necessary for reaching of the legitimate aim, and it is not possible to reach the aim by applying more lenient measures. Although the legal regulatory framework of the Contested Norm is not the only way how to eliminate problems of illegal employment and tax avoidance, alternative measures are still regarded as less effective. They require non-proportional expenses and time from the State. Therefore the most effective way of eliminating “envelope wages” is application of the regulatory framework established in the Contested Norm. It serves as a stimulus for merchants to fulfil their tax duties before the State.

The benefit gained by the society from the Contested Norm is greater than restriction of rights of an individual because, by means of public procurement, state administration ensures not only its own functioning but also fulfilment of services necessary for each inhabitant. The society is interested into effective use of State and local government resources. Effectiveness means not only ensuring public procurements for the lowest price possible but also payment of taxes by the supplier. Moreover, the Contested Norm protects fair competition among merchants who have fulfilled their tax duties before the State.

The Saeima indicates that the Contested Norm does not contradict requirements of the Directive 2004/18/EC and case-law of the Court of Justice of the European Union. Article 45 of the Directive 2004/18/EC permits applying its criteria insofar as they ensure equality in procurement procedures and transparency thereof. Consequently, the legislator has acted within its freedom of action and has not infringed requirements of the Directive 2004/18/EC.

4. A summoned person, **Ombudsman of the Republic of Latvia** (hereinafter – the Ombudsman) is of the viewpoint that the Contested Norm does not cause

infringement of the fundamental rights enshrined in Article 105 of the Satversme. Article 105 of the Satversme protects property already obtained, as well as assets, in respect to which a person has “legitimate expectations”. Effective legal norms do not entitle a person to count on the fact that a public procurement contract would be concluded with him or her in particular, in the result of which the person could gain material benefit.

Possible profit in the future cannot be regarded as property in the meaning of Article 105 of the Satversme and Article 1 of Protocol No. 1 of the European Convention for the Protection of Human Rights and Fundamental Freedoms (hereinafter – the Convention). Consequently, there is no reason to assess compliance of the Contested Norm with Article 105 of the Satversme.

The Ombudsman indicates that, pursuant to the equity principle established in Article 91 of the Satversme, every merchant has the right to agree with its employees on the amount of remuneration insofar as it complies with the minimum wage established in the State. Due to this reason, the Contested Norm can not be regarded as appropriate for reaching of the legitimate aim because requirements established therein might restrict rights of such merchants who have fulfilled their tax duties before the State. No legitimate aim for restriction of the fundamental rights of merchants can be established.

Consequently, the Ombudsman holds that the Contested Norm fails to comply with Article 91 of the Satversme.

5. A summoned person, **the Ministry of Finance** indicates that the Contested Norm is appropriate for reaching of the legitimate aim established by the legislator. The Contested Norm ensures that one and the same legal regulatory framework is applied in respect to all applicants who enjoy equal conditions, whilst a different legal regulatory framework is applied to those who enjoy different conditions. The Contested Norm also

ensures that all applicants participating in procurement procedures are equally treated based on the respective exclusion criterion.

The Ministry of Finance admits that the Contested Norm is not the only way how to eliminate problems of illegal employment and tax avoidance. However, other measures are rather ineffective because they are based on controlling and punishing merchants rather than on motivating them. Since capacity of the State Revenue Service is limited and there are many such merchants who pay rather low wages to their employees, it would require non-proportional expenses and time from the State. Consequently, it is not possible to reach the aim of the Contested Norm by applying other measures that would restrict rights of persons at a lesser extent.

The Ministry of Finance holds that the restriction of fundamental rights included into the Contested Norm shall be assessed in conjunction with 10 August 2010 Cabinet of Ministers Regulation No. 761 “Provisions regulating the Procedure for Gathering, Treating and Publishing information on Average Wage and Declared Taxed Annual Income” (hereinafter – the Regulation No. 761), which, in certain cases, permits performing re-calculation of wage paid by the employer. This permits avoiding application of the Contested Norm in case if payment of comparatively low wage within an enterprise is based on objective considerations.

The Ministry of Finance is of the viewpoint that limiting of range of applicants having the right to participate in a procurement procedure and selecting the most advantageous tender can not be opposed to ensuring of a fair competition and fulfilment of tax duties. The society is interested in effective use of State resources. This interest also includes criteria of tax payment by the applicants. Moreover, the Contested Norm protects those applicants of a procurement procedure who have fulfilled all tax duties before the State.

The Ministry of Finance indicates that the Directive 2004/18/EC does not prohibit the State to leave unamended or to adopt norms of substantive law, the purpose of which is ensuring observance of equal attitude and transparency principle in the field of public

procurement. By adopting the Contested Norm, the legislator has acted in the frameworks of Article 45 of the Directive 2004/18/EC and case-law of the Court of Justice of the European Union.

6. A summoned person, **the Ministry of Justice** holds that the measures included into the Contested Norm are appropriate for reaching of the legitimate aim of the norm because it facilitates payment of taxes into the State budget. The Ministry of Justice indicates that the Contested Norm includes only a motivating criterion, in case of compliance with which merchants obtain the necessary advantages for participation in a procurement procedure. Consequently, merchants who want to participate in procurement procedures, are motivated to pay taxes and make social insurance payments in respect to their employees at full extent. The Ministry of Justice also refers to statistical data that confirm that wage paid by employers generally is equal to the minimum wage or the State or less. This fact means that it is often the case that merchants pay “envelope wage” to their employees, they fail to pay taxes and social insurance contributions at full extent. Such merchants would thus gain more advantages in a procurement procedure since they can propose lower prices if compared to those who do pay full taxes.

The Ministry of Justice admits that the Contested Norm can restrict the possibilities of certain applicants to participate in a procurement procedure. However, it can not be considered that the Contested Norm restricts the range of possible applicants at such a large extent that this would contradict the purpose of the Public Procurement Law, which is to ensure free competition and equal and fair attitude in respect to competitors.

According to the Ministry of Justice, the Contested Norm does not contradict requirements of Article 45 of the Directive 2004/18/EC. When assessing norms of the Directive 2004/18/EC in conjunction with case-law of the Court of Justice of the European Union, it can be concluded that they do not even provide any list of applicant exclusion criteria. Thus the State preserves its freedom of action insofar as it is necessary to ensure observance of transparency and equal attitude principles.

7. A summoned person, **the Procurement Monitoring Bureau** [*Iepirkumu uzraudzības birojs*] (hereinafter – the PMB) indicates that the Contested Norm does comply with legal norms of a higher legal force. According to the PMB, the Contested Norm does have a legitimate aim, whilst measures selected by the legislator are appropriate for reaching of the legitimate aim.

It is reasonable to consider that applicants, the average wage of employees of whom is considerably lower than the average wage in the respective field, avoid tax payment duty. Consequently, such applicants obtain the possibility to propose lower prices in procurement procedures on unfair basis. Equally qualified and experienced employees are remunerated on equal basis. Moreover, the proportion of high and low qualified, as well as high and low remunerated employees in enterprises is similar.

The Contested Norm ensures that suppliers who work in one and the same field and participate in one and the same procurement procedures, ensure a comparable average wage to their employees. Although the Contested Norm can not fully ensure payment of taxes at full extent by all suppliers, the result of its adoption and application ensures that suppliers try to reach average tax payment indices of the respective field. Consequently, this ensures that, in procurement procedures, all applicants enjoy equal conditions in respect to tax payment duty fulfilment and none of them have obtained ungrounded advantages over others. The PMB admits that the Contested Norm seemingly restricts the possibility to choose the most advantageous and the cheapest tender. However, the PMB considers that it is not possible to oppose assurance of fair competition and tax payment duty. The Contested Norm ensures protection of interests of the entire society. When selecting an applicant who has made all tax payments, this ensures income of resources into the State budget and such benefit is more substantial for the society if compared to economy that could be made in case of accepting the cheapest tender.

The PMB holds that the Contested Norm does comply with requirements of the Directive 2004/18/EC. According to case-law of the Court of Justice of the European Union, Member States have the right to broaden the range of applicant exclusion criteria established in Article 45 of the above mentioned directive insofar as observance of equal attitude and transparency principles is ensured in respect to all applicants. Consequently, by adopting the Contested Norm, the legislator has observed the above mentioned principles.

8. A summoned person, the State Revenue Service [*Valsts ieņēmumu dienests*] (hereinafter – the SRS) explains motives for adoption of the Contested Norm and indicates that its legitimate aim is to ensure that those suppliers would become applicants in procurement procedures, in respect to which the probability of “envelope wages” is as low as possible. Since the appeal to pay taxes on voluntary basis and respective methods fail to ensure desired results, the Contested Norm stimulates merchants to eliminate all violations by themselves in order to obtain the right to participate in procurement procedures. The SRS indicates that the Applicant has been included into the high risk tax default list.

The SRS admits that it is rather likely that average wage of employees of an applicant to a procurement procedure who has fulfilled all tax duties might be lower than the one indicated in the Contested Norm. However, in certain cases, it is possible to carry out re-calculation of wage paid to employees of a merchant pursuant to norms of the Regulation No. 761 in order to admit participation of a particular applicant in procurement procedures.

9. The association “The Latvian Information and Communication Technology Association [*“Latvijas Informācijas un komunikāciju tehnoloģiju*

asociācija”] (**hereinafter – LIKTA**) is of the viewpoint that the Contested Norm does comply with Article 91 and Article 105 of the Satversme.

The LIKTA holds that the Contested Norm does not restrict economic activities and economic interests of the Applicant or its possibility to gain profit in State or local government procurement market. The Applicant has the right to participate in procurement procedures by proving that it has fulfilled its duties before the State. Consequently, infringement of the fundamental rights of the Applicant established in Article 105 of the Satversme can not be established and therefore compliance of the Contested Norm with Article 91 of the Satversme only should be assessed.

When committing applicants of a procurement procedure to ensure average wage for employees at, at least, 70 per cent of the average wage of the respective field, the applicant is motivated to pay wages at the respective level, as well as make all stipulated tax payments. Consequently, the Contested Norm is appropriate for reaching of the legitimate aim.

The LIKTA considers that it is possible to reach the legitimate aim of the Contested Norm by applying such measures that would restrict rights of an individual at a lesser extent. However, such measures are less effective and require non-proportional resources from the State. Exclusion of the Contested Norm from the Public Procurement Law would lead to non-observance of the equality principle and that of a fair competition in the field of public procurement. Consequently, the aim of the Contested Norm can not be reached at the same quality by applying less restrictive measures.

The benefit gained by the society from the Contested Norm is greater than the restriction of the fundamental rights of an individual. When assessing the Contested Norm in the context of Section 2 (3) of the Public Procurement Law, it can be concluded that the right to conclude a procurement contract should be granted to such applicants of procurement procedures that have fulfilled their tax duties and ensured benefit to the State. This ensures an effective use of public resources in the framework of a public procurement procedure.

10. The Association “Latvian Association of Construction Contractors” [*„Latvijas Būvnieku asociācija”*] holds that the Contested Norm does comply with legal norms of a higher legal force.

Inadequately low wages that are paid in order to avoid taxes distorts construction market at a considerable rate. Such actions result in advantage of dishonest merchants in procurement procedures, whilst the State incurs losses due to unpaid taxes. Consequently, the Contested norm should be preserved in the Public Procurement Law since it does not infringe the right of applicants of a procurement procedure to an equal attitude.

11. The Association “Latvian Forest Industry Federation” [*„Latvijas Kokrūpnieku federācija”*] indicates that the Contested Norm does comply with Article 91 and Article 105 of the Satversme.

The Latvian Forest Industry Federation is of the opinion that the aim of the Contested Norm is to ensure that the right to sign a public procurement contract is granted to such merchants, in respect to which the likelihood of “envelope wages” is as low as possible. This aim shall be regarded as a legitimate one in the context of the society in general and certain interest groups in particular.

The Contested Norm does comply with the principle of proportionality because the criterion of 70 per cent included therein is lenient enough for the majority of merchants that fulfil their fiscal duties before the State in good faith though pay comparatively low wages to be able to meet requirements of the Contested Norm and participate in public procurement procedures. In forest industry, application of the Contested Norm has had a positive trend. After coming into force of the Contested Norm, wages have increased in certain sectors of forest industry, which can be considered as a result of application of the Contested Norm. The trend was especially pronounced in enterprises that paid relatively low wages before.

12. The Latvian Chamber of Commerce and Industry [*Latvijas Tirdzniecības un rūpniecības kamera*] supports preservation of the Contested Norm in the Public Procurement Law. The application practice of the Contested Norm has ensured increase of wages in certain fields; thus the Contested Norm has a positive impact onto certain fields and the national economy in general. Before the Contested Norm was included into the Public Procurement Law, it was often the situation that applicants who were able to propose non-proportionally low prices were avoiding taxes. In such a situation, it was the State that was put in a disadvantageous position due to non-collected taxes, as well as merchants who paid their taxes though were not granted the right to sign tender contracts.

However, the Latvian Chamber of Commerce and Industry draws attention to the necessity to concretize the Contested Norm so that it would restrict the possibilities of dishonest merchants to participate in procurement procedures. The Latvian Chamber of Commerce and Industry has expressed such objections already when the Contested Norm was under elaboration by asking the Ministry of Finance to find a solution that would prevent all possible restrictions in respect to honest merchants.

13. The Latvian Association of Local and Regional Governments is rather concerned for the fact that the Contested Norm might restrict competition of merchants working in different regions of the State that are characterized by considerable differences in the living standard and amount of income. The Contested Norm might have a particularly negative impact on the possibilities of merchants working in less developed regions of the State to participate and win procurement procedures.

The Latvian Association of Local and Regional Governments questions appropriateness of the Contested Norm for reaching of its legitimate aim because it fails to fully eliminate “envelope wages”. Application of the Contested Norm might cause problems in respect to fair competition and cause the increase of offer prices. Moreover, the Contested Norm may turn out to be particularly disadvantageous in respect to those merchants who have had suspended their activities for a certain period of time in order

not to pay wages when idle standing. Due to the above mentioned reason, a limited range of applicants can take part in procurement procedures. It concerns only those merchants who fulfil their economic activity in an active way and have regular income.

The Findings

14. The Contested Norm is one of the criteria established in Section 39 (1) of the Public Procurement Law, according to which an applicant is excluded from further participation in a procurement procedure. The Contested Norm relates the amount of wage paid to employees of the company to average wage of employees of the respective field in the State by also establishing that an applicant would be excluded from further participation in a procurement procedure in case if the average wage of the employees is less than 70 per cent of the average indices of the respective field.

In case if an applicant complies with the exclusion criteria of the Contested Norm, it would lose the right to be awarded a procurement contract, whilst the tender of the applicant is not even considered.

In the present case, there is no dispute regarding the content of the fundamental rights included in Article 91 of the Satversme; therefore the Constitutional Court shall first of all assess whether the Contested Norm infringes the fundamental rights of the Applicant enshrined in Article 105 of the Satversme.

15. Article 105 of the Satversme provides: “Everyone has the right to own property. Property shall not be used contrary to the interests of the public. Property rights may be restricted only in accordance with law. Expropriation of property for public

purposes shall be allowed only in exceptional cases on the basis of a specific law and in return for fair compensation.”

15.1. It can be concluded from opinions provided by the parties and the summoned persons that viewpoints regarding the fact whether the Contested Norm infringes or not the fundamental rights enshrined in Article 105 of the Satversme differ. Justification of the constitutional complaint does not deal with the issue of compulsory alienation of property; therefore compliance of the Contested Norm with the first three sentences of Article 105 of the Satversme shall be assessed.

The Applicant holds that the Contested Norm restricts its economic interests related to gaining profit and protected by Article 105 of the Satversme. However, the Ombudsman is of the viewpoint that the Contested Norm should not be considered in the context of Article 105 of the Satversme because the effective legal norms does not give any legal grounds to a person to trust into the fact that he or she would be the one to whom a public procurement contract would be awarded and in the result of which profit would be gained. Article 105 of the Satversme does not protect all economic interests but only those, implementation of which is lawful and sure. Consequently, the Constitutional Court shall first establish the content of the fundamental rights included in Article 105 of the Satversme and assess whether the Contested Norm restricts these fundamental rights.

15.2. The Constitutional Court has already established in its case-law that Article 105 of the Satversme envisages undisturbed exercise of property right, as well as the right of the State to restrict use of property in accordance with the general interest (*see: Judgment of 20 May 2002 by the Constitutional Court in the case No. 2002-01-03, the concluding part*).

When establishing the content of the norms included in the Satversme, it is necessary to take into consideration international liabilities of Latvia in the field of human rights. International norms of human rights and the practice of their application serve as means of interpretation on the level of constitutional law to determine the contents and scope of fundamental rights and the principle of the law-governed state, as

far as it does not lead to decrease or limitation of fundamental rights included in the Satversme. The duty of the State to take into consideration the international liabilities in the field of human rights follow from Article 89 of the Satversme, which provides that the State shall recognize and protect fundamental human rights in accordance with this Constitutional, laws and international agreements binding upon Latvia (*see: Judgment of 16 December 2008 by the Constitutional Court in the case No. 2008-09-0106, Para 4*).

The Constitutional Court has also concluded that the most important international documents do not provide for the definition of the content of the notion “property”. However, lack of such definition cannot be regarded as a surprising fact because the content of this notion varies from one legal system to another. Consequently, the interpretation of this notion provided by the European institutions on human rights protection plays a great role in establishing the content of the notion of property (*see: Judgment of 4 February 2009 by the Constitutional Court in the case No. 2008-12-01, Para 8*).

It has been established in case-law of the European Court of Human Rights that Article 1 of Protocol No. 1 of the Convention includes three separate norms: first, the first sentence of the above mentioned article establishes the right to undisturbed enjoyment of property right; second, the second sentence of the same article establishes prohibition of deliberate alienation of property and conditions for alienation of property, and, third, the second part of the same article recognizes that the State has the right to use property in accordance with general interest (*see, e.g.: Judgment of 28 May 2009 by the Constitutional Court in the case No. 2010-47-01, Para 7.2, or Judgment of the European Court of Human Rights in the case AGOSI v. the United Kingdom, 24 October 1986, application No. 9118/80, Para. 48*).

Article 105 of the Satversme establishes a comprehensive guarantee of property law. “The right to property” means all property rights that a legitimate person can exercise in his or her own favour and according to his or her own will. The European Court of Human Rights has also concluded that, in the meaning of the Convention, many

claims can be regarded as property, namely, such claims, execution of which could be requested based on an apparent legal ground. Future income shall be regarded as property only in case if they have already been earned or a claim to be satisfied exists (*see, e.g.: Judgment of 27 October 2010 by the Constitutional Court in the case No. 2010-12-03, Para7, or Judgment of the European Court of Human Rights in the case Prince Hans-Adam II of Liechtenstein v. Germany, 12 July 2001, application No. 42527/98, Para 82 – 83*).

It follows from the aforesaid that the Applicant has not been granted any protected fundamental right to future profit following from participation in a procurement procedure. Neither Article 105 of the Satversme, nor Article 1 of Protocol No. 1 of the Convention provides protection of future possibilities of persons to gain profit if such possibility is not regarded as a subject-matter of property.

Consequently, the Contested Norm does not infringe the fundamental rights of the Applicant established in Article 105 of the Satversme; therefore proceedings in the present case insofar as it applies to compliance of the Contested Norm with Article 105 of the Satversme shall be terminated.

16. Article 91 of the Satversme provides : “All human beings in Latvia shall be equal before the law and the courts. Human rights shall be realised without discrimination of any kind.” It follows from the constitutional complaint that compliance of the Contested Norm with the first sentence of Article 91 of the Satversme only should be assessed, it guaranteeing equality of all persons before the law because, in the present case, there is no dispute regarding non-compliance of the Contested Norm with the principle of discrimination prohibition.

16.1. The task of the equality principle enshrined in the first sentence of Article 91 of the Satversme is to ensure that the demand of the law-governed state of an all-embracing influence of the law on all persons, as well as securing of applying the law

without any privileges is realized. It guarantees complete effect of the law, objectivity and impassiveness of its application as well as the fact that nobody is allowed not to observe the instructions of the law (*see: Judgment of 14 September 2005 by the Constitutional Court in the case No. 2005-02-0106, Para 9.1*). However, such unity of legal procedure does not mean leveling because “equality allows a differentiated approach, if it can be justified in a democratic society” (*see: Judgment of 26 June 2001 by the Constitutional Court in the case No. 2001-02-0106, Para 6*).

When interpreting Article 91 of the Satversme the Constitutional Court has recognized that the principle of equality forbids to the State institutions passing such norms, which without a reasonable ground permit a differentiated attitude to persons, who are in equal and under certain criteria comparable circumstances. The principle of equality permits and even requires a differentiated attitude towards persons, who are in different circumstances as well as permits a differentiated attitude towards persons, who are in equal circumstances, if there is an objective and reasonable basis for it (*see: Judgment of 3 April 2001 by the Constitutional Court in the case No. 2000-07-0409, Para 1 of the Findings, and Judgment of 29 December 2008 in the case No. 2008-37-03, Para 7*). A differentiated attitude is discriminating, if it does not have an objective and well-grounded reason, i.e. – a legitimate aim or if the chosen means and the advanced objectives are not proportionate (*see: Judgment of 23 December 2002 by the Constitutional Court in the case No. 2002-15-01, Para 3 of the Findings*).

16.2. Consequently, in order to assess whether the Contested Norms complies with the principle of equality included in the first sentence of Article 91 of the Satversme, it is necessary to establish:

- 1) whether and what persons (groups of person) enjoy equal and, according to certain criteria, comparable conditions;
- 2) whether the Contested Norm provides for an equal or different attitude towards these persons;

3) whether such attitude has an objective and well-grounded reason, namely, whether it has a legitimate objective and whether the principle of proportionality has been observed (*see, e.g.: Judgment of 2 February 2010 by the Constitutional Court in the case No. 2009-46-01, Para 7*).

17. In order to establish whether the Contested Norm complies with the equality principle enshrined in the first sentence of Article 91 of the Satversme, it is necessary to compare at least two groups of persons.

The Applicants draws attention to case-law of the Constitutional Court wherein it is recognized that participants of one and the same market enjoy equal and comparable conditions (*see: Judgment of 9 February 2004 by the Constitutional Court in the case No. 2003-21-0306, Para 9.2*). Consequently, the Applicant holds that all companies taking part or interested in taking part in procurement procedures on acquisition of right to provide information technology services enjoy equal and, according to certain criteria, comparable conditions. The Constitutional Court recognizes that the Contested Norm is applicable to all applicants of procurement procedures; however, negative consequences of its application occur only in respect to those applicants who comply with the exclusion criteria established in the Contested Norm.

In the present case, the average wage of employees of an applicant shall be regarded as the differentiation criteria. The Contested Norm prohibits taking part in a procurement procedure to those applicants, the average wage of employees of which is less than 70 per cent of the average indices of the respective field in the State. However, the Contested Norm does not restrict the right of other applicants to participate in a procurement procedure. In such a situation, it is possible to distinguish between two groups of applicants based on the wage paid by the employer to its employees and average indices of the respective field.

Disregarding the amount of remuneration paid to employees of both groups of applicants, all applicants participate or are interested in participation in procurement procedures granting the right to provide information technology services to State or local government institutions. Likewise, companies working in other fields and participating or being interested in participation in procurement procedures to win the right to conclude a public procurement contract enjoy equal and comparable conditions.

Consequently, the applicants, the average wage of employees of which is higher than the 70 per cent established in the Contested Norms, and applicants, the average wage of employees of which is lower than the 70 per cent established in the Contested Norm, enjoy equal and comparable circumstances.

18. The Contested Norm establishes a criterion that characterizes applicants of a procurement procedure. The criterion is applicable to all participants of a procurement procedure. However, when assessing the Contested Norm in conjunction with Section 39 (1) of the Public Procurement Law, it can be established that it serves as a criterion for exclusion of applications from a procurement procedure.

Consequently, merchants, the average monthly wage of which exceeds the threshold of 70 per cent established in the Contested Norm may proceed within a procurement procedure. However, applicants who meet the exclusion criteria established in the Contested Norm lose the right to participate in the procurement procedure.

Consequently, the Contested Norm establishes a differentiated attitude towards those groups of persons that enjoy equal and comparable circumstances.

19. The principle of equality permits and even demands a differentiated attitude to persons, who are in diverse circumstances as well as permits a differentiated attitude to persons, who are in equal circumstances if there is a reasonable and objective basis for it

(see: *Judgment of 11 December 2006 by the Constitutional Court in the case No. 2006-10-03, Para 17*).

The Saeima has indicated in its reply that the legitimate aim of the Contested Norm is facilitation of welfare of the society and protection of rights of other persons (see: *Case materials, Vol. 1, pp. 41*).

The Ministry of Finance, the proposition of which facilitated inclusion of the Contested Norm into the Saeima agenda, has indicated that elaboration of the Contested Norm was determined by problems related to tax payment, as well as the relatively high illegal employment rate in Latvia. Many employees avoid paying taxes for their employees or do not pay them at full extent. Thus they gain advantage in procurement procedures by proposing relatively lower prices. Consequently, it is necessary to provide stimulus to merchants to act in the frameworks of “formal economy” (see: *Case materials, Vol. 2, pp. 57*).

It is also indicated in the annotation to the Regulation no. 761, by means of which applicant of the Contested Norm is ensured, that the purpose of the Contested Norm is to ensure that procurement contracts would be signed by such suppliers, in respect to which “envelope wage” risk is as low as possible, as well as to facilitate payment of taxes, the State social insurance contributions included [see: *Cabinet of Ministers draft project “Provisions regulating the Procedure for Gathering, Treating and Publishing information on Average Wage and Declared Taxed Annual Income”, Para 3 of Section 2 of the initial impact assessment report (annotation), <http://www.mk.gov.lv/lv/mk/tap/?pid=40181902&mode=mk&date=2010-08-10>*].

Consequently, by adopting the Contested Norm, the legislator primarily wanted to exclude from participation in a procurement procedure all such applicants who have failed to fulfil their tax commitments at full extent. The Contested Norm stimulates tax payment by employers, as well as ensures fair competition among applicants in a procurement procedure.

Consequently, the legitimate aim of the Contested Norm is facilitation of welfare of the society and protection of rights of other persons by excluding from participation in procurement procedures all such applicants who have failed to fulfil their tax payment duties at full extent, as well as facilitation of comprehensive tax collection and assurance of fair competition in the frameworks of a procurement procedure.

20. In order to investigate whether the legal provision passed by the legislator complies with the principle of proportionality, the Constitutional Court shall investigate the following:

1) whether the means utilized by the legislator are suitable for achieving the legitimate objective or whether the aim set can be reached by the measure selected;

2) whether such action is indispensable, i.e., whether the objective can not be reached by other means that restrict the rights and legal interests of a persons at a lesser extent;

3) whether the action of the legislator is proportionate or commensurate, i.e., whether the benefit gained by the society is greater than the losses caused to the rights and legal interests of a person.

If, when assessing the legal provision, it is acknowledged that it is in conflict with at least one of the above criteria, then it is in conflict with the principle of proportionality and is unlawful (*see, e.g.: Judgment of 18 March 2011 by the Constitutional Court in the case No. 2010-50-03, Para 12*).

21. First of all, the Constitutional Court should investigate whether the measures selected by the legislator are appropriate for reaching of the legitimate aim and whether such measures restrict the rights of such persons that the legislator did not mean to address.

21.1. A low average wage of employees if compared to wage paid in other companies of the same field might be justified by the fact that an applicant avoids tax payment. Consequently, it is possible to agree with the opinion of the Saeima that a part of applicants who meet the criteria established in the Contested Norm do avoid tax payment.

As a result of the Contested Norm, applicants who meet the criteria established in the Contested Norm and avoid tax payment are excluded from a procurement procedure. Consequently, the legitimate aim of the Contested Norm is reached because the right to conclude a public procurement contract is not granted to such applicants who avoid tax payment. This assures fair competition among applicants because only those applicants who raise no doubt regarding fulfilment of their tax commitments can participate in a procurement procedure.

Consequently, the legitimate aim established by the legislator can be reached by measures established in the Contested Norm.

21.2. However, the question whether the Contested Norm reaches its legitimate aim shall be assessed in conjunction with application practice of the Contested Norm.

The Contested Norm is based on relation between the amount of wage paid to employees of a particular applicant to a procurement procedure and the average indices of merchants of the same field in the State. The Contested Norm does not require that persons applying the norm would verify whether a particular applicant of a procurement procedure who has met the exclusion criteria of the Contested Norm has or has not avoided paying taxes and whether its exclusion from the procurement procedure complies or not with the legitimate aim of the Contested Norm. Neither the Contested Norm, nor other norms of the Public Procurement Law establish the possibility to exclude such applicants from a procurement procedure, the average wage of employees of which exceeds the 70 per cent barrier established in the Contested Norm but who still have failed to fulfil their tax duties. Consequently, the Contested Norm might restrict the rights of such persons who have fulfilled all fiscal obligations; however, the norm does not

ensure that all applicants who have failed to pay taxes at full extent would be excluded from participation in a procurement procedure due to the fact that the exclusion criteria enshrined in the Contested Norm can not be applied to all applicants.

Consequently, by applying the Contested Norm, all those applicants who formally comply with the exclusion criteria established in the Contested Norm are excluded from participation in a procurement procedure. However, the fact whether an applicant to a procurement procedure has or has not made tax payments established in normative acts plays no role in application procedure of the Contested Norm. The SRS also admits that the Contested Norm might restrict the right to participate in procurement procedures of those applicants who have fulfilled their fiscal obligations at full extent (*see: Case materials, Vol. 2, pp. 104*).

It is possible to agree with the opinion of the Ombudsman that the legislator's purpose was not to restrict the rights of applicants who pay taxes because normative acts do not prohibit paying lower wage if compared to the average wage of the field or to employ subcontractors (*see: Case materials, Vol. 1, pp. 200*). According to opinions of the parties and the summoned persons, there are many reasons why an applicant might pay lower wage to its employees if compared to the average indices of the respective field. For instance, the Latvian Association of Local and Regional Governments has indicated that a relatively low wages dominate in recently founded companies or such companies that had suspended their activities for a certain period of time. Moreover, it draws attention to regional remuneration differences; namely, companies founded in Riga pay higher wages if compared to companies in other regions of the State (*see: Case materials, Vol. 2, pp. 54 – 55*).

Meanwhile the Latvian Chamber of Commerce and Industry indicated that part-time employment might result in reduced amount of average wage paid to employees of an applicant (*see: Case materials, Vol. 2, pp. 120*). Moreover, different ways of avoiding from the exclusion based on the Contested Norm exist, for instance, foundation of a new company or change in affiliation to a certain field of NACE 2. red.

Consequently, there are different reasons why an applicant might meet the exclusion criterion established in the Contested Norm even though it has made all stipulated tax payments. The legitimate aim of the Contested Norm is to restrict the rights of such applicants only that have failed to fulfil their fiscal obligations at full extent.

Consequently, the Contested Norm may restrict rights of such applicants that have paid all stipulated taxes to the State and not restrict the rights of such applicants who have done it only partially.

22. When assessing whether the legitimate aim of the Contested Norm can be reached by applying measures that would restrict the rights of individuals at a lesser extent, the Constitutional Court should first of all assess the nature of the restriction of rights established in the Contested Norm.

22.1. Upon ratification of the Treaty on Accession of Latvia to the European Union, the European Union law has become integral part of the Latvian legal system. Therefore, legal acts of the European Union and interpretation provided by case-law of the European Court of Justice should be taken into account when applying national law in order to avoid possible contradictions between Latvian national and European Union law (*see: Judgment of 17 January 2008 by the Constitutional Court in the case No. 2007-11-03, Para 24.2*).

Taking into account the fact that that procurement procedures are regulated not only by means of Public Procurement Law norms but also the European Union law, Latvian law must be interpreted so as to avoid any conflicts with the obligations of Latvia towards the European Union, unless the fundamental principles incorporated in the Satversme are affected. When assessing criteria for excluding applicants to procurement procedures, the requirements of the directives transposed by Latvia and interpretation of the directives established in the case law of the European Court of Justice should be

observed (*see: Judgment of 17 January 2008 by the Constitutional Court in the case No. 2007-11-03, Para 25.4*).

The Court of Justice of the European Union has recognized that Member States have the right to broaden the list of exclusion criteria in respect to applicants in procurement procedures. However, such right shall be exercised only insofar as it ensures observance of the principle of equal attitude and transparency (*see: Judgment of the Court of Justice of the European Union in the case Assitur, C-538/07, Para 23*). Moreover, such measures may not exceed the necessary limits to reach the legitimate aim of respective restrictions (*see: Judgment of the Court of Justice of the European Union in the case Michaniki, C-213/07, Para 48, and Judgment in the case Fabricom, C-21/03 and C-34/03, Para 34*).

Consequently, the Constitutional Court has to verify whether the legitimate aim of the Contested Norm can be reached by applying less restrictive measures. The Court of Justice of the European Union has indicated that the Community law must be interpreted as precluding a national provision, which, whilst pursuing the legitimate objectives of equal treatment of tenderers and of transparency in procedures for the award of public contracts, does not ensure observance of the principle of proportionality (*see: Judgment of the Court of Justice of the European Union in the case Michaniki, C-213/07, Para 69, judgment in the case Assitur, C-538/07, Para 30, and judgment in the case Fabricom, C-21/03 and C-34/03, Para 33 and 35*).

Although, in the above mentioned cases reviewed by the Court of Justice of the European Union, the investigated exclusion criteria were not analogous to those of the Contested Norm as to their content, it can still be concluded that restriction of rights based on an indisputable presumption is not admitted because it violates the principle of equality, of proportionality and of transparency. The formal nature of the exclusion criterion included in the Contested Norm and the application procedure does not permit persons applying it to verify whether a particular applicant has fulfilled its fiscal obligations and whether such exclusion is grounded. Consequently, the legislator has to

establish such measures for reaching of the legitimate aim of the Contested Norm that would permit verifying fulfillment of fiscal duties by an applicant.

Consequently, exclusion of an application from participation in a procurement procedure based on an indisputable presumption is prohibited.

22.2. The Constitutional Court has indicated that the Contested Norm includes a formal criterion that is applied to all applicants of a procurement procedure without verifying whether they have fulfilled their fiscal obligations. Consequently, an applicant who has made all tax payments at full extent can not prove that there is no reason to exclude it from the procurement procedure.

It is possible to agree with the opinion of the SRS that the Contested Norm shall be assessed in conjunction with norms of the Regulation No. 761. Section 11 of the above mentioned regulation establishes several conditions in respect to re-calculation of wages of applicant's employees, including, proportion of full-time employees in the company and their wage. However, application of the Regulation no. 761 permits preventing exclusion of applicants who have paid all taxes from participation in a procurement procedure only in exceptional cases. The Contested Norm may also restrict the right of applicants who have fulfilled their fiscal obligations to participate in procurement procedures in other cases when application of the Regulation No. 761 fails to solve the situation.

The Constitutional Court recognizes that the legislator enjoys freedom of action when establishing exclusion criteria of applicants to procurement procedures insofar as they would ensure observance of the principle of transparency of and equality in the field of public procurement. However, when taking advantage of such freedom of action, the legislator has to adopt such measures that would not restrict the rights of persons. The delinquency of the Contested Norm follows from its strictly formal application procedure, according to which the person applying the norm does not have the duty to verify whether doubt regarding partial fulfilment of fiscal obligations by an applicant is

grounded, whilst the applicant have no possibilities to prove that they have no debts to the State.

The Constitutional Court had already drawn attention to different reasons why average wage of applicant's employees might be lower than the threshold of 70 per cent established in the Contested Norm. If persons applying the Contested Norm would have been granted the freedom of action to assess the necessity of exclusion of an applicant from a procurement procedure and its compliance with the legitimate aim of the norm, the applicants would have the possibility to submit an explanation to the procurement procedure in respect to the comparatively low wages of their employees. After assessment of the explanations the procurement commission would decide whether the low wage of applicant's employees is based on objective reasons. In such a case, the commission could permit such applicants to continue participating in a procurement procedure that have fulfilled their tax obligations even if they meet the exclusion criterion established in the Contested Norm. Consequently, the legitimate aim of the Contested Norm would still be reached. The aforesaid does not exclude the right of the legislator to establish other less restrictive means to reach the aim of the Contested Norm provided that they would ensure the rights of the applicants to participate in procurement procedures.

Consequently, the legitimate aim of the Contested Norm can be reached by other means that would restrict the rights of individuals at a lesser extent.

23. If, when assessing the legal provision, it is acknowledged that it is in conflict with at least one of the above criteria, then it is in conflict with the principle of proportionality and is unlawful (*see, e.g.: Judgment of 16 May 2007 by the Constitutional Court in the case No. 2006-42-01, Para 11*). The measures included in the Contested Norm are not appropriate for reaching of its legitimate aim in respect to certain applicants because they restrict the right of applicants to participate in procurement procedures even if they have fulfilled all their fiscal obligations. Moreover, the legitimate aim of the

Contested Norm can be reached by other less restrictive measures. Consequently, the Constitutional Court does not have to assess whether the benefit gained by the society is greater than the detriment caused to rights of individuals. Consequently, the Contested Norm fails to comply with the principle of proportionality and with that of equality included in the first sentence of Article 91 of the Satversme. In addition, it should be assessed whether application of NACE 2.red classificatory for calculation of the average wage of the respective field can be considered as an objective criterion, based on which the right to participate in procurement procedures would be restricted.

The legislator is committed to selecting such measures that would ensure reaching of the legitimate aim of the Contested Norm, which in the present case is exclude merchants that have failed to fulfil their fiscal obligations from participation in procurement procedures. However, these measures may not restrict the rights of those applicants who have made all tax payments in good faith though they can not ensure the wage at the amount of 70 per cent of the average wage of the respective field to their employees. The legal regulatory framework of the Contested Norm restrict the rights of such persons who have made their tax payments in good faith, and no legitimate aim can be established in respect to restriction of rights of such persons. In order not to exceed the legitimate aim of the Contested Norm, the legislator either has to choose such measures that do not restrict the right of the applicants who have fulfilled their fiscal obligations to continue participating in procurement procedures, or to establish such legal procedure that would permit the applicants proving that they have made all stipulated tax payments. Consequently, the legislator enjoys freedom of action when selecting the most appropriate measures insofar as they do not apply the right of the applicants who have made all tax payments to participate in procurement procedures.

The Constitutional Court indicates that Section 39 (1) indent 7, 8 and 9 of the Public Procurement Law include applicant exclusion criteria that are similar to the Contested Norm. Although the above mentioned norms are not contested in the framework of the particular application and they are not being assessed in the

frameworks of the present case, the legislator is committed to verifying compliance of respective exclusion criteria with the considerations of the present judgment.

24. The Applicant asks the Constitutional Court to recognize the Contested Norm as null and void as from the date of its adoption (*see: Case materials, Vol. 1, pp. 11*). Such request is based on the consideration that, in such a case, all applicants that have been excluded from participation in procurement procedures would gain the possibility to bring an action to compensate losses, which would thus ensure protection of their infringed rights (*see: Case materials, Vol. 2, pp. 9*). According to Article 32 (3) of the Constitutional Court Law, a legal norm (act) that the Constitutional Court has declared as non-compliant with the norm of a higher legal force, shall be regarded as not in effect from the day of publication of the Constitutional Court judgment, if the Constitutional Court has not determined otherwise.

The procurement procedure, from which the Applicant was excluded based on the Contested Norm has been terminated, and restoration of the former situation without threatening successful fulfillment of public functions is impossible. The Constitutional Court has already concluded that recognition of a contested norm as null and void with retroactive force may not be applied in cases when it is not possible to restore the former legal situation (*see: Judgment of 19 October 2011 by the Constitutional Court in the case No. 2010-71-01, Para 26*). The Constitutional Court has concluded that the Applicant has not been conferred the fundamental right to gaining profit from participation in a public procurement procedure. Consequently, the infringement of rights of the Applicant shall not be regarded as serious enough to establish special provisions of validity of the Contested Norm in respect to the Applicant. Exercising the right established in Article 32 (3) of the Constitutional Court Law, the Constitutional Court shall see to it that the situation, which might develop from the moment the impugned norms lose validity, to the moment while the Saeima passes new norms, violates neither the fundamental rights of the submitters of the claim, guaranteed by the Satversme, nor creates relevant harm to

state or public interests (*see: Judgment of 16 December 2005 by the Constitutional Court in the case No. 2005-12-0103, Para 25*).

The Constitutional Court Law authorizes the Court to decide on ensuring the enforcement of their judgments, namely, authorize the Constitutional Court to decide important legal consequences of its judgments by itself. The law not only grants authorizations to the Constitutional Court but also makes it responsible for its judgments – so that they ensure legal stability, clarity and peacefulness in the public sphere (*see: Judgment of 21 December 2009 by the Constitutional Court in the case No. 2009-43-01, Para 35.1*).

By recognizing the Contested Norm as unconstitutional, the Constitutional Court did not recognize that the legislator has been denied the right to establish particular restrictions; instead, it has indicated that measures selected by the legislator may not restrict the rights of applicants to procurement procedures that have fulfilled their fiscal obligations at full extent. Consequently, the legislator has the possibility to improve the legal regulatory framework of the Contested Norm by establishing such mechanism that would not exceed the limits of the legitimate aim of the Contested Norm or infringe the rights of applicants who have made all their tax payments. Recognition of the Contested Norm as null and void as from the date of coming into force of the present judgment or with retroactive effect would render reaching of the legitimate aim established by the legislator impossible. Therefore, the most appropriate solution of the present case is recognition of the Contested Norm as null and void as from a particular moment in the future by giving the legislator time to improve the legal regulatory framework of the Contested Norm or assess the necessity to exclude the Contested Norm from the Public Procurement Law.

Consequently, the Constitutional Court shall rule that the Contested Norm shall become null and void as from 1 March 2012.

The Constitutional Court

Based on Article 30 – 32 of the Constitutional Court Law,

h o l d s :

- 1) proceedings in the present case insofar as it applies to compliance of Section 39 (1) indent 6 of the Public Procurement Law with Article 105 of the Satversme of the Republic of Latvia shall be terminated;**
- 2) Section 39 (1) indent 6 of the Public Procurement Law insofar as it restricts the rights of applicants and tenderers of procurement procedures that have made all tax payments shall not comply with Article 91 of the Satversme and become null and void on 1 March 2012.**

The Judgment is final and not subject to appeal.

The Judgment shall come into effect on the date of publishing it.

Presiding Judge

G. Kūtris

Translated by E. Labanovska, translator of the Constitutional Court