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Briefing note

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The Rules of Engagement: Private Sector Procurement and the Common Law

Construction tender processes run by public bodies are usually subject to statutory procedures and requirements intended to promote transparency and competition. This has increasingly led to legal challenges from unsuccessful bidders seeking to challenge the propriety of award decisions. However, in common law countries, the legal principles governing procurement in the private sector have, to date, been considerably less developed and investigated[1].

Inevitably, the growth in procurement challenges to regulated public sector tenders has also lead to developing interest in the legal duties implied into private procurements. An understanding of the extent of any such duties is clearly important in successfully navigating a world of increasingly sophisticated bid documentation, processes and tactics.

Key issues

- Although considerably less developed than the rules governing the public sector, there are important legal principles of application to private sector procurements.
- The law in this area is developing and an increase in disputes is anticipated prompted by the growth in public sector challenges.
- There are plenty of pitfalls for the unwary – the potential for claims is wider than cases of fraud or misrepresentation.
- Exclusions of liability may be construed strictly so need to be drafted carefully.
- Bid bonds may be making a comeback – but are they worthwhile or appropriate?

The basic legal relationship

It is generally considered nowadays that a contractual relationship may be implied into most formal tender arrangements where statements are made as to how the tender process will be carried out. This is usually called a "tendering contract" or "process contract"[2]. In English law, such a contract is still regarded as a limited exception to the general principle that there is no contractual relationship formed until a person asking for tenders accepts one of them.

[1] This briefing focuses on private sector tender processes - although many of the principles are derived from disputes involving and are therefore also relevant to public sector procurements, we do not cover the application of specific public sector procurement regulations and rules in this paper.

[2] See for example the leading decision of the Supreme Court of Canada in *The Queen in Right of Ontario v Ron Engineering & Construction (Eastern) Ltd (1981)*, which distinguishes the "advance" tendering/process contract arising on the submission of a tender in response to the invitation to tender and governing the tendering process (Contract 'A'), from the terms of the "principal" construction contract which was the subject of the procurement ('Contract B').

Even in Canada, Australia and New Zealand, where the concept has been considerably expanded, a contract does not arise with every invitation to tender ("ITT"). In these jurisdictions there is still a requirement to show that the parties intended to create a tendering contract on submission of the tender.

Some English law commentators continue to contend that a tendering contract relationship is more likely to be implied in a formal public sector context, or alternatively, that a court will be less inclined to imply such a relationship in the case of a private procuring entity (in this briefing an "employer"), who has not indicated any desire to fetter its discretion to make subjective choices.[3] However, it is submitted that on major projects, where there is formal ITT documentation, that distinction is nowadays likely to be less relevant.

In practice, and to avoid both express commitments and implied duties on their part, it has become commonplace for well-advised employers to include exclusion clauses in ITT documentation. That said, there are often exceptions where it remains important for certain aspects of the ITT process to be binding and enforceable (for example, provisions dealing with confidentiality, withdrawal, cancellation and liabilities) and these aspects are therefore usually carved out of any exclusion clause.

In any event, and notwithstanding general exclusionary statements, that is not the end of the story. The law may yet import other duties into the tendering relationship - breaching those duties might generate claims from disappointed bidders to recover bid expenses and, if relevant, loss of profit.

Governing law

Before considering those areas where claims may arise in connection with tendering arrangements, if there is a cross-jurisdictional aspect, we may need to determine first the legal system that will deal with these issues.

Helpfully, on major projects with an international dimension, the ITT documentation will invariably state an express choice of law. That choice will therefore usually be enforced and govern claims in respect of a tendering contract. Moreover, if there is a dispute in connection with determining whether a tendering contract exists or not, it will still usually be applied as the putative choice of law of the contract.

However, as with all choices of law for contractual and non-contractual arrangements, limits apply, not least if the parties and the country to which the tender relates are not bound by the same international treaty arrangements, or alternative systems of law are advanced in bidder responses.

In any event, it should always be remembered that an express choice of law which is not connected with the country where the project is located will not prejudice the application of any relevant mandatory provisions of the law of that country. In complex scenarios, this may bring into consideration different legal regimes' treatment of the tender process.

Potential areas of claim: (1) No prospect of award from the outset and cancelled procurements

If it can be shown that there was never any intention of letting a contract to any or all of the bidders invited to submit a tender, then the process is at risk of being deemed to be fraudulent and relevant bidders should be able to bring an action to recover their bid expenses.[4]

However, the position is quite different for tender processes which are genuinely cancelled. It is clear that unless it has committed to do so, a private sector employer is not required by law to accept the lowest or any other type of bid[5] and even

[3] For example, Hudson (Twelfth Edition at para. 3-036). This may simply reflect the less developed English case law in this area compared to the position in Canada and Australia.

[4] Canadian courts have also found that 'bid-shopping' (soliciting bids from tenderers with whom one has no intention of dealing to drive down prices) constitutes a breach of the tendering contract (see *Naylor Group v Ellis-Don Construction (2001)*).

[5] For such a situation to arise, one would have to envisage an arrangement where the employer had somehow managed to contractually bind itself to accept a certain type of bid (e.g. the lowest price) and managed its bid documentation in such a way that the bid was deemed to be accepted as soon as communicated.

though it is recommended that ITT documentation normally make this point clear, it is generally thought that it is unnecessary for the employer to include a statement to preserve this discretion. It follows from this that the employer is free to cancel a tender process and, again, ITT documentation will usually expressly permit cancellation at any stage without liability, in order to remove any doubt on the issue.[6]

However, cancellation of a bid process can lead to a breach of an implied contractual duty to consider compliant bids at all and/or to consider them 'fairly' (see below).

Potential areas of claim: (2) Failure to consider a compliant bid at all

English and Commonwealth courts have implied duties into tendering arrangements obliging employers at least to open and consider conforming bids[7]. It is considered that the very clearest and most specific language would need to be used if it is intended to completely exclude this basic obligation (for example, a 'privilege' statement entitling rejection of the lowest or any tender may be insufficient to oust the implied duty to consider bids in the first place).

However, even this limited rule may be subject to exceptions where it is reasonable, for example due to supervening circumstances, to exclude that bidder from the tender.[8]

What is less clear is if the bidder must comply absolutely with the rules of the bid process in order to enjoy the right to have its bid considered. This is likely to turn on the express requirements of the ITT. As a matter of good practice, employers will typically expressly exclude any legal or binding obligation to consider non-compliant bids, even if seeking to encourage variant offers.[9]

Potential areas of claim: (3) Failure to treat compliant bidders fairly

A common complaint in bid processes is of unbalanced treatment, where one bidder is seen to have the 'inside track' or to be treated favourably, for example, by having access to data that other bidders do not. More seriously, it may be alleged that an award has been made to an unqualified bidder who should have been excluded from the process.

If the unbalanced treatment is the result of some form of corruption or bribery,[10] this can of course invalidate the whole process. Where secret commissions have been paid to advisors and agents, the employer is free to rescind the tender process and any contract resulting from it and recover damages. The employer may, however, lose that right if it has affirmed the contract or acquiesced in the receipt of the bribe/commission.[11] Losing bidders will of course also be entitled to bring actions in deceit or fraud.[12]

Where a tendering contract contains express statements on how the bid process will be organised, these may also cover the nature of the employer's obligations in evaluating and considering tenders. For this reason, employers are usually circumspect about including their assessment criteria and even general statements of intent - so where this is included (for example, to guide bidders) it is normally advisable for this to be non-binding and for the employer to retain discretionary rights to award as it sees fit (and not to award at all).

Absent specific and binding obligations on assessment and evaluation, the question then arises as to what extent a tendering contract will be deemed to include an implied term to act 'fairly' in considering tenders and, if so, what this entails.

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[6] Exceptions may include design competitions or specialist projects, where the employer may agree to underwrite certain bidder costs to maximise the prospect of receiving the best bids and ideas.

[7] *Blackpool & Fylde Aero Club Ltd v Blackpool Borough Council (1990).*

[8] *Fairclough Building Ltd v Port Talbot Borough Council (1992).*

[9] This is invariably best described as a right to reject non-compliant submissions. Requiring absolute compliance can be problematic where the employer wishes to retain flexibility (or there is a possibility that no bidder will be able to achieve full compliance).

[10] Laws dealing with bribery and corruption affecting parties may have extra-jurisdictional effect. Please contact us if you would like to receive our latest guidance on the UK Bribery Act.

[11] *Bartram and Sons v Lloyd (1904).*

[12] *Richardson v Silvester (1873).*

It is in relation to this question that the practice between common law countries differs. At its widest, in certain Commonwealth countries a duty to act 'fairly' appears to be considered part of a broader duty of 'good faith' in performance of contract. In contrast, in English law the textbooks tend to restrict implication of tendering contract obligations to the duty to consider compliant bids - it seems that currently a duty to consider bids fairly is more likely to be implied in the sphere of public sector procurement[13] (for example, where contractors are not allowed to compete on similar terms) and the applicability of any such duty to purely private sector procurements remains doubtful.

Where it is held that there is a duty to act fairly and treat tenderers equally, it is unlikely that the strict administrative standards of procedural fairness would be held to apply in the context of a private sector procurement.[14] That said, it is of course conceivable that in future this may change and come under examination in particularly egregious cases of partiality. In Canada, the courts have reinforced an implied duty of fairness by reference to the policy goal of protecting and promoting the integrity of the tender process, holding that without the implied term tenderers would either incur significant expenses in preparing futile bids or ultimately avoid participating in the tender process.[15]

The uncertainty in the scope of such implied obligations has inevitably led to well-advised employers including both 'privilege' clauses preserving discretionary rights in their ITT documentation and exclusions of liability. The latter need careful drafting as they may be construed narrowly. In a recent leading Canadian case,[16] a 'losing' bidder claimant succeeded in a claim for loss of profit despite an exclusion clause purporting to prohibit such liability. It was held in this case that the relevant exclusion clause was not intended to cover a situation where a contract was 'unfairly' awarded to a party who should never have been allowed to participate.

Potential areas of claim: (4) Misrepresentation

ITT documentation will also typically disavow responsibility for the accuracy of statements of fact and information provided therein. Exceptions to such an exclusion may eventually emerge in respect of key data in the ultimate contract documentation, but not ordinarily within the tender process itself. However, it should be noted:

1. An exclusion of responsibility cannot succeed where a misrepresentation is fraudulent. For example, if an employer fraudulently misrepresents its own status in order to attract bids, it will be liable to bidders who have relied on that representation.
2. Where a misrepresentation is made negligently and reliance is placed on it by a bidder, it may be able to bring a claim in tort. Exclusion clauses purporting to avoid this liability will be construed narrowly and may have to satisfy a test of reasonableness, so employers will wish to ensure that their ITT documentation seeks to protect against this potential independent tortious liability.
3. In non-common law countries, there may additionally be liability associated with failures to disclose important relevant information held by the employer. It is considered that in a tendering context this is highly unlikely to apply in common law jurisdictions, except where that information is required to be disclosed by statute (for example, for safety reasons).

Potential areas of claim: (5) Other liability for specific lost bid costs

The general assumption in most competitive tendering scenarios is that bidders take full risk for their bid costs, absent either fraud, a failure to properly consider the bid, or actionable misrepresentation as mentioned above.

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[13] For example in *Harmon CFEM Facades (UK) Ltd v The Corporate Officer of the House of Commons (1999)*. Public sector cases may also involve claims for misfeasance, concerned with the abuse of public office.

[14] In other words the standards are likely to be of 'good faith' and 'fair dealing' rather than requiring the employer to act judicially, for example *Pratt Contractors Ltd v Transit New Zealand (2003)*. In other Commonwealth cases, it has been held the duty does not include having to comply with internal procurement policies or having to investigate tenderers' commitment and ability to deliver their tender promises.

[15] *Martel Building Ltd v Canada (2000)*, mentioned in *Tercon Contractors Ltd v British Columbia (2010)*.

[16] *Tercon Contractors Ltd v British Columbia (2010)*.

However, where a bidder provides particular services which are outside 'usual' tender submission services in the expectation (and not the mere hope) of receiving a contract, it may also be entitled to recovery of the relevant expenses incurred in carrying out these services. In very clear-cut cases (for example, where a contractor is asked to carry out initial preparatory works with nothing said as to payment or price), this may take the form of implying a full contractual promise to pay reasonable remuneration, whether as part of the tendering contract or separately as an independent contractual commitment.

Alternatively, where the dispute concerns a reasonable expectation of payment, liability may be deemed to be 'quasi-contractual'[17]. This introduces a technical but important legal distinction, as in such cases compensation will only be for the benefit received by the employer (the so-called principle of 'unjust enrichment') which may be less than the cost of providing the services or ultimately be assessed as having no value.

Changing the rules of the game

ITT documentation will usually permit changes by the employer without compensation. In the absence of such language, it is possible there could be an opportunity for bidders to try to recover wasted costs (for example if a bidder can show it relied on a misrepresentation), though the general principle will continue to apply that the bidder is responsible for its own costs and is not required to continue to bid if the ITT is amended. Needless to say, a tendency to change the ITT can disincentivise bidders and either lead to withdrawal or uncompetitive responses.

Changes in the nature of the ITT are likely to generate more controversy if they are the result of adopting ideas generated by one of the bidders. For example, a client may wish to adopt the variant proposals of a bidder but compete other bidders on it, in order to be able to compare properly. This may open up questions on the licensing/ownership of intellectual property as well as issues as to whether the original competition was ever genuine.

Locking-in, withdrawal and bid bonds

The 'flip-side' of the general principle that a bidder is at risk for its bid costs is that it is also free to withdraw a bid at any time before it has been formally accepted and a contract concluded. This is obviously of considerable concern to an employer wishing to preserve a competitive bidding environment and/or wishing to avoid the delay and costs of a failed procurement process. The position becomes even more acute once a preferred bidder is selected, so ITT documentation will invariably provide for a binding commitment that bids will be available for acceptance for a minimum period.[18]

The enforceability of an irrevocable commitment given by a bidder is not however a straightforward matter. In larger commercial procurements there is often significant to-ing and fro-ing between the parties with changes agreed and negotiation of terms. It is common for bids to reserve or condition certain positions so that the overall bid is not capable of immediate acceptance in any event (and common law systems notoriously will not enforce 'agreements-to-agree' in respect of the remaining terms of a contract if these are sufficiently significant to prevent a contract existing at that juncture). Also, it would not be unusual during a procurement process for there not to be a valid responding bid on the table to the latest updates sought by the employer from time to time. These changes and outstanding issues may mean any bid commitment is unenforceable and indeed this may be a deliberate tactic on the part of bidding parties to stall discussion on certain topics until they are the preferred bidder.

A related tactic used to avoid bid commitments is for the tenderer to argue that its own bid is non-compliant so that no tendering contract is capable of being formed in the first place. This argument has been used in a number of Canadian cases with varying degrees of success, often when a tenderer has made an error in its formal bid.

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[17] Arising in restitution, for example *Sabemo Pty Ltd v North Sydney Municipal Corporation (1977)*.

[18] The Canadian cases advancing contractual liability in tenders initially considered contractor obligations not to revoke or change bids, for example, *The Queen in Right of Ontario v Ron Engineering & Construction (Eastern) Ltd (1981)*. In this case, the Supreme Court of Canada upheld the enforceability of a requirement that bids could not be revoked for 60 days after tenders. It went on to state the contractor could not avoid liability on the grounds of a mistake in its tender, unless the mistake was apparent on the face of the tender.

Concern over enforcing bid commitments occasionally leads to requests for bidders to provide bid bonds either on submission of the bid or on selection as a preferred bidder pending finalisation of the ultimate contract (in order to mitigate the employer's costs of retendering). For many years these instruments became rare in the UK - aside from being seen as onerous (a bidder will not, after all, withdraw lightly from a process to which it has committed effort and expenditure), they began to depart from a strict on-demand format, incorporating conditions which raised precisely the same concerns over enforceability as applied to the bid commitment in the first place. Moreover, if required at an early stage, they may limit the number of bidders (because of the impact on bidders' bonding and other banking facilities) without necessarily providing any real valuable security to the employer. However, more recently we have seen a return to bid bonds being actively considered on major projects, usually focused on trying to prevent changes in bid position (as well as withdrawal) after a preferred bidder decision is made but before the full ultimate contract can be concluded (for example, within a knowledge tendering process).

Collusive bidding practices

Collusive tendering or 'bid-rigging' are terms used to describe unlawful arrangements between bidders that seek to prevent or limit competitive tendering in an attempt to guarantee certain bids are accepted and/or artificially to inflate tendered prices. As well as fines levied by government competition authorities, bidders may face employer action for damages either for breach of express binding terms of a tendering contract or potentially in tort for breach of statutory duty.[19]

Summary

The law concerning tendering contracts continues to develop quickly and whilst the major driver for this is public procurement regulation, it is increasingly likely that this will migrate and encourage disputes in connection with private sector tenders. Although the general principle remains that bidders are at risk for their bid costs, employers will wish to ensure that their ITT documentation is carefully drafted to avoid the pitfalls for the unwary highlighted above. That said, courts will look askance at structures which are designed to require bidders to submit irrevocable tenders but seek to avoid all employer obligations and liabilities. Moreover, when ITT documentation becomes onerous and too one-sided, the potential bidding market tends to react predictably (for example, by shrinking or responding in kind). The bidding process is, after all, the initial period of familiarisation between the parties and should therefore be engendering the kind of co-operative behaviour from the outset which will best deliver the project in future.

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[19] This may arise as a direct claim or by way of 'follow-on' actions following an infringement decision by the regulator.

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