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THE EVOLUTION OF TENDER CONTRACTS

By Chris Fellowes

In the world of contracting, you don't need a big bang to recreate the moment when contractual life starts. In theory it's very simple; fusion of offer and acceptance is achieved when a tender is accepted. In practice, however, the legal reality can be rather more complicated.

Public procurement

In the EU, the simple contractual model may be modified by the detailed regulations that govern public procurement. And they have teeth. Fail to comply and the consequences can be expensive in time and money. A dramatic recent illustration is the decision, by the High Court in Northern Ireland at the end of October 2008¹, to set aside an £800 million framework agreement because the Department of Finance and Personnel had failed to comply with the Public Contracts Regulations 2006.

But even if we leave the EU regulatory framework on one side, in a typical tendering arrangement we can expect to find not one, but two contracts. This was the analysis the English Court of Appeal adopted in **Blackpool and Fylde Aero Club Ltd v Blackpool BC**² in 1990. Blackpool Borough Council invited tenders for a concession to an air operator to operate pleasure flights from the local airport.

The invitation to tender said that tenders received after 12 noon on a specified date would not be considered. The Aero Club put their tender in the Town Hall letterbox at 11am but the letterbox was not cleared by the council staff at noon. The Aero Club tender was marked as received late and consequently not considered.

The club brought proceedings against the council claiming damages for breach of contract, contending that the council had warranted that if a tender was returned to the Town Hall before noon, it would be considered with all the other tenders duly returned when the decision to grant the concession was made.

The Court of Appeal agreed with this two contract analysis. Lord Justice Bingham said:

"I have no doubt that the parties did intend to create contractual relations to the limited extent contended for... I think it plain that the Council's invitation to tender was, to this limited extent, an offer, and the Club's submission of a timely and conforming tender an acceptance".

This contract was quite separate from the contract to be entered into by the council with the successful tenderer.

Blackpool was soon considered by the Court of Appeal in **Fairclough Building v Port Talbot BC**³ where, although **Blackpool** was



Chris Fellowes is a partner in the Construction & Engineering Group at Mayer Brown International LLP.

¹ *McLaughlin and Harvey Ltd v Department of Finance and Personnel* (No 3) [2008] NIQB 122

² [1990] 1 WLR 1195

³ (1992) 62 BLR 82

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distinguished, the Court found there was a contract to be implied from conduct that the Council would consider the aggrieved contractor's tender.

By the time that his His Honour Judge Humphrey Lloyd QC decided the marathon case of **Harmon CFEM Facades (UK) Ltd v The Corporate Officer of the House of Commons**⁴, in 1999 the **Blackpool** principle appeared to be settled:

"I consider that it is now clear in English law that in the public sector where competitive tenders are sought and responded to, a contract comes into existence whereby the prospective employer impliedly agrees to consider all tenders fairly (see the Blackpool and Fairclough cases)."

In 1981, the Supreme Court of Canada had established a two contract approach in **The Queen in Right of Ontario v Ron Engineering & Construction (Eastern) Limited (1981) 119 DLR (3d) 267**, where the lowest tenderer realised, after its bid had been opened and was found to be \$632,000 lower than the next lowest bidder, that it had made a mistake in its calculations, by failing to include a figure of approximately \$750,000. It did not withdraw its tender but said that, because notice of the error had been given to the owner before its tender was accepted, the tender could not be accepted. In the proceedings, it attempted to recover its tender deposit of \$150,000.

The Supreme Court said that a unilateral contract (contract A) arose automatically on the submission of a tender by the contractor and, under that contract, the tenderer could not withdraw the tender for a specified period of time, after which, if the tender had not been accepted, the deposit could be recovered by the tenderer.

The principal term of contract A was the irrevocability of the bid and the corollary term

was the obligation on both parties to enter into a construction contract, contract B, upon the acceptance of the tender. The deposit was required to ensure the performance of the tenderer of its obligations under contract A. The contractor's claim failed because no mistake existed which impeded the coming into existence of contract A.

In 2004 the tendering process and the treatment of tenderers came before the Privy Council on an appeal from the New Zealand Court of Appeal in **Pratt Contractors Limited v Transit New Zealand [2003] UKPC 83**. Transit, the New Zealand body with responsibility for maintenance and improvement of state highways and motorways, accepted, in the light of modern authority, that the request for tenders was not a mere invitation to treat and gave rise to a preliminary contract requiring it to comply with certain procedural obligations. It also accepted that the contract included an implied duty to act fairly and in good faith but the parties disagreed as to what the procedural obligations were and as to what counted as acting fairly and in good faith.

The nature of the implied duty to act fairly and in good faith had, said Lord Hoffman, been the subject of a good deal of discussion in Commonwealth authorities and he referred to the comments of Finn J in **Hughes Aircraft Systems International v Airservices Australia**⁵ to the effect that the duty, in cases of preliminary procedural contracts for dealing with tenders, is a manifestation of a more general obligation to perform any contract fairly and in good faith.

Lord Hoffman thought that was a "*somewhat controversial question*" which the Privy Council did not have to consider because Transit had accepted such a duty in the case.

More recently, in 2007 the issue appeared in the High Court of Northern Ireland in **Gerard Martin Scott v Belfast Education &**

4 (1999) 67 ConLR 1

5 (1997) 146 ALR 1

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Library Board⁶. Weatherup J said that an implied contract with implied terms of fairness and good faith could arise from the issue of tender documents for a public works contract, both from the scheme of the tendering process and the presumed intention of the parties.

Another decision of the High Court of Northern Ireland in the previous year, in **J & A Developments Ltd v Edina Manufacturing Ltd [2006] NIQB 85**, also made the point that a party inviting tenders may expressly bind themselves to follow a particular procedure, in that case, the 1996 Code of Procedure for single stage selective tendering. Ultimately the legal effect of the chosen tendering arrangements in each case will depend on exactly what is said.

Just public contracts?

In **Harmon**, as we have seen, His Honour Judge Humphrey Lloyd had said that the duty of the prospective employer to consider all tenders fairly arises “*in the public sector*”. But why is there any restriction of the analysis to public contracts?

If we go back to **Blackpool**, Lord Justice Bingham said:

“Had the club, before tendering, enquired of the council whether it could rely on any timely and conforming tender being considered along with others, I feel quite sure that the answer would have been ‘of course’.”

There is no obvious limitation to the arena of public contracts nor was there any similar limitation in **Fairclough** when Lord Justice Parker said that it was a “*question of a contract to be implied from conduct*”. In Canada, in the Supreme Court, in **Naylor Group Inc. v. Ellis-Don: [2001] 2 SCR 943**, Binnie J said that, as **Ron Engineering** and a subsequent Canadian decision made clear:

“...the Contract A/Contract B approach rests on ordinary principles of contract formation,

and there is no reason in principle why the same approach should not apply at this lower level. The existence and content of Contract A will depend on the facts of the particular case.”

The logic of applying the two contract analysis to private, as well as public, contracts, is attractive.

Is there a duty of care?

And now in 2008, and again in Canada, the subject has taken another turn. **Design Services Ltd v Canada**⁷ asked the question: If there is no contract A, does a prospective employer inviting tenders owe any duty of care in tort?

In **Blackpool**, the Aero Club had made a second claim in negligence against the council but the Court of Appeal had not needed to decide that because of its finding that the council was in breach of the implied contract. In **Design Services**, however, the Supreme Court of Canada did have to decide a claim by unsuccessful tendering parties in negligence.

Public Works and Government Services Canada (PW) launched a tendering process for a design and build project. Tenderers could bid alone or with others as a joint venture.

PW awarded the contract to a non-compliant bidder and one of the tenderers, Olympic Construction Limited, and certain sub-contractors associated with its bid, sued PW. Olympic settled with PW but the sub-contractors continued with the litigation. The Supreme Court had to decide whether an owner in a tendering process owed a duty of care in tort to sub-contractors.

Olympic had not entered into a partnership or joint venture with the sub-contractors and it was accepted there was no contract between the sub-contractors and PW. A contractual claim through the **Ron Engineering/Blackpool** route was not therefore open to

6 114 ConLR 209

7 [2008] BLR 571

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the sub-contractors. Which left the possibility of a duty in tort to be explored.

The first instance judge, Mosley J, thought that by reason of PW's "*close management*" of the participation of the sub-contractors in the tendering process, PW owed the Plaintiffs a duty of care in tort not to award the contract to a non-compliant bidder. The judge said:

"I conclude, therefore, that this is a case that cries out for a remedy."

His view was that, although Olympic and the sub-contractors did not enter into a form of joint venture, the process adopted by Olympic and the sub-contractors was "*analogous to a joint venture*". PW's requirements in the pre-qualification and tendering process therefore created a relationship between PW and the sub-contractors that met the proximity standard for a new duty of care.

Using the **Ron Engineering "Contract A/Contract B"** analysis the Supreme Court noted that PW had been in breach of its Contract A with Olympic by awarding Contract B to a non-compliant bidder. That breach had affected the subcontractors since their opportunity to recover their tendering costs and the opportunity to earn a profit from participating in the project depended on Olympic being awarded Contract B. The subcontractor's losses were, however, pure economic losses, unconnected to any physical injury or physical damage to their property (which might otherwise have enabled recovery in tort). Were the subcontractors owed a duty of care in respect of these losses?

The Canadian case of **Canadian National Railway Co v Norsk Pacific Steamship**⁸ had identified five different categories of negligence claims, where there was a duty of care in respect of pure economic losses:

- the independent liability of statutory public authorities;
- negligent misrepresentation;

- negligent performance of a service;
- negligent supply of shoddy goods or structures;
- relational economic loss, ie. where pure economic loss is suffered by virtue of some relationship, usually contractual, enjoyed with a personally injured third party or the damaged property.

No property of Olympic had been damaged and none of the five categories applied. So should a new duty of care be recognised?

The test to be applied in Canada was that in **Anns v Merton**⁹ (overruled in English law by the House of Lords in **Murphy v Brentwood District Council**¹⁰)

In **Anns**, Lord Wilberforce proposed a two-part duty of care test. The first part asked whether the relationship between the claimant and the defendant is close or "*proximate*" enough to give rise to a duty of care.

The Supreme Court noted that, from the perspective of the sub-contractors, several factors seemed to have led them to believe that their relationship with PW was closer than in the usual owner/sub-contractor situation:

- PW was selecting a design and build team;
- information on the roles and experience of the sub-contractors had to be provided to PW;
- the selection process was heavily reliant on the ability of the tenderer's team;
- at least 70 of the 150 points for an evaluation were directed at the team members' ability to do the work individually and as a team;
- the design and build team members and their key personnel could not be substituted without the express advance written consent of PW;
- the sub-contractors had to attend a "partnering" session with PW's project manager; and

8 Co (1992) 91 DLR (4th) 289

9 [1978] AC 728

10 [1991] 1 AC 398

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- the sub-contractors expended considerable time and energy in preparing their bids.

The Supreme Court concluded, however, that the fact that the sub-contractors had the opportunity to form a joint venture, and thereby be parties to the “*Contract A*” made between PW and Olympic, was:

“...an overriding policy reason that tort liability should not be recognised in these circumstances. Allowing the appellants to side-step the circumstances they participated in creating and make a claim in tort would be to ignore and circumvent the contractual rights and obligations that were, and were not, intended by PW, Olympic and the appellants. In essence, the appellants are attempting, after the fact, to substitute a claim in tort law for their own ability to claim under “Contract A”. After all, the obligations the appellants seek to enforce through tort exist only because of “Contract A” to which the appellants are not party.

...the appellants’ ability to foresee and protect themselves from the economic loss in question is an overriding policy reason why tort liability should not be recognised in these circumstances. The appellants had the opportunity to arrange their affairs in such a way as to be in privity of contract with PW relative to “Contract A”, but they chose not to do so and they are now trying to claim through tort law for lack of a contractual relationship with PW. Tort law should not be used as an after-the-fact insurer.”

The comments of Rothstein J. in **Design Services** echo the analysis of Lord Goff in **Henderson v Merrett**¹¹, a case that was not cited in **Design Services**. In his analysis of contractual and tortious responsibility under typical building contract arrangements, Lord Goff said:

“...there is generally no assumption of responsibility by the sub-contractor or

supplier direct to the building owner, the parties having so structured their relationship that it is inconsistent with any such assumption of responsibility.”

In **Design Services**, however, the responsibility being considered was, of course, that of the prospective employer, PW.

The second stage of the Anns test

The second stage of the Anns test asked whether there were countervailing policy considerations that negated the duty of care. Since the Supreme Court found there was no prima facie duty of care at the first stage, they did not need to continue with the second stage but, as a postscript, they found it useful to comment on one residual policy concern – indeterminate liability, which is a greater risk in cases of pure economic loss.

The recognition of a duty of care of an owner to sub-contractors in a tendering process could lead to what Cardozo C.J. of the New York Court of Appeals described as:

“...liability in an indeterminate amount for an indeterminate time to an indeterminate class.”

The trial judge had discounted the indeterminate liability concern but the Supreme Court said the facts suggested that the class of plaintiffs was not as well defined as found by the trial judge since a subsidiary of one of the design-build team members also made a claim and the class of plaintiffs therefore seemed to “...seep into the lower levels of the corporate structure of the design-build team members.”

The case thus had indications of indeterminate liability. Since the type of tendering process was not unique and there were many types of arrangements that could arise between owners and contractors and between contractors and subcontractors, recognition of an owner’s duty of care towards sub-contractors in these circumstances could therefore lead to a multiplicity of proceedings in tort, which was an undesirable result.

¹¹ [1995] 2 AC 145

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There was a more general concern in the construction contract field because of the chain of subcontractors and suppliers who might claim for economic loss if an employer wrongly failed to award the contract to the main contractor on whom they were all dependent. In the construction context the indeterminacy of the class of plaintiffs could readily be seen.

Even if a prima facie duty of care had been found in the first stage of the **Anns** test, it would have been negated at the second stage because of the indeterminate liability concern.

All of which must, no doubt, have left the unsuccessful subcontractors wishing they had tendered in a joint venture and secured the certainty of a contract A with PW.

And the way forward?

The case law may be fascinating for students of contract and tort law but what practical lessons can the commercial world take from all of this? Unsurprisingly, for those inviting public (and perhaps private) sector tenders, it is the good old-fashioned, but consistently effective, application of great care in putting together the tender invitation, which is where Contract A's DNA is formed. Just what form that life is to take will depend on what the tender documents say; as the Supreme Court of Canada pointed out in **Naylor Group v Ellis-Don**¹².

“The existence and content of Contract A will depend on the facts of the particular case.”

Which is another old-fashioned dose of advice worth repeating. The parties, in contract, you

might say, generally make their own law.

Moving forward to the assessment of tenders (and leaving aside the EU procurement regulations), if the invitation documents set out the basis of the assessment, then that procedure must be strictly followed. Ignoring the procedure can be unfair and, as we have seen, a theme of the cases is an implied duty to consider all tenders fairly. Keeping a careful note of a properly conducted assessment may also prove helpful, in case it is later necessary to demonstrate that the stated procedure has been fully and fairly followed.

Time spent in ensuring the process is properly and correctly set out and carried out (and in checking and double-checking the process) will be time well spent if it avoids the consequences headlined by the cases. Not only can those consequences be serious but the climate of the credit crunch is likely to encourage unsuccessful tenderers to look very hard for any failings in the tender process and, consequently, to put more pressure on those inviting tenders.

Bringing a Contract A into the world also brings responsibility. Those seeking tenders will want to ensure that the contractual big bang is on their terms.

¹² [2001] 2 SCR 943