

9-1-2003

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Recommended Citation

Weitzman, Roy (2003) "Conduct unbecoming: Probity codes in tendering processes," *Public Infrastructure Bulletin*: Vol. 1: Iss. 2, Article 3.

Available at: <http://epublications.bond.edu.au/pib/vol1/iss2/3>

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CONDUCT UNBECOMING – PROBITY CODES IN TENDERING PROCESSES

Tender processes must be conducted properly if the private sector is to tender with confidence. The rules of probity establish a process for public tenders, but they might also leave governments open to challenges from disappointed tenderers. Roy Weitzman of Minter Ellison Lawyers outlines the rules and draws lessons from two recent cases.

Tender processes, and the open competition they produce, are extremely important to government, as they establish the environment in which governments achieve value for money outcomes through their interaction with the private sector. It is in this environment that rules on probity have been developed in the various Australian states and territories.

Unfortunately, the establishment of any code of conduct has consequences - probity rules both establish a process for conducting public tenders and provide a background against which disappointed losing tenderers may challenge the contract awarded. The stakes are high. The New South Wales and Victorian governments will both let contracts in excess of AUD\$2 billion in the next few years by way of public tender and if the tender processes are properly conducted, each project will represent value to the tax payer. If not, the states could be immersed in a sea of litigation.

THE RULES OF PROBITY

'Probity' means using honesty, integrity, uprightness, ethical conduct and propriety in dealings.¹ When used in a contractual sense, it means 'good process', conducted clearly, honestly, fairly, and impartially, without bias to any party.

The underlying principles of probity are:

- procedural fairness and integrity
- objectivity / independence of decision making
- confidentiality and
- accountability

The Commonwealth, and each of the states, has enacted rules to ensure that these principles are complied with.² The NSW Code establishes ten principles of probity are instructive, which are instructive.

1. Parties must conduct the tendering process with honesty and fairness at all levels.
2. Parties must conform to all legal obligations.
3. Parties must not seek or submit tenders without a firm intention to proceed.

4. Parties must not engage in any practice, including improper inducements, which gives one party an improper advantage over another.
5. Tenderers must be prepared to attest to their probity, and not engage in any form of collusive practice.
6. Conditions of tendering must be the same for each tenderer.
7. All requirements must be clearly specified in the tender documents and criteria for evaluation must be clearly indicated.
8. Evaluation of tenders must be based on the conditions of tendering and selection criteria defined in the tender documents.
9. Parties must not disclose confidential or proprietary information.
10. Any party with a conflict of interest must declare that interest as soon as the conflict is known to that party.³

The guidelines are, however, a matter between the government and its employees. Of themselves they do not provide a regime for the challenge of government decisions. However, they do provide a context within which the probity debate occurs and the rules themselves may, as we shall see below, be incorporated into the obligations between government and tenderers by virtue of tender documentation.

...probity rules both establish a process for conducting public tenders and provide a background against which disappointed losing tenderers may challenge the contract awarded.





...these documents must provide government with a flexible, yet sufficiently detailed framework to minimise potential legal challenges.

APPLYING THE RULES

The responsibility for establishing a good process in a transaction is with the project team within the department responsible for the project.

It is important to clearly define, before a tendering process gets underway, who is to make the important decisions at the various stages in the process. Organisational issues should be discussed, agreed and documented. Procedures and responsibility must be established for:

- authorising the documents which set the framework for the process
- analysing bids, making recommendations and finalising decisions on short-listing and bidder selection
- liaising with, negotiating with, and informing bidding parties
- consultation with Ministers and
- resolving probity and process issues as they arise

It is imperative that confidentiality be maintained during a tendering process to protect both the commercial interests of government, and the competitive position of each bidder. However, this need for confidentiality must be balanced with the need for government to be open and transparent in all its dealings.⁴

It is essential that during the tender process, competitors do not gain access to confidential bidder information. If bidders are not confident in government security mechanisms, they will refrain from providing the level of detail and volume of information required in bids, and may even be deterred from entering the tender process.

Sometimes the government may wish to allow bidders to compete on the basis of quality, design, and innovation, as well as price. Ground rules must be established to ensure bidders have confidence in the process, and the protection of their intellectual property, while still allowing government to share non-proprietary information with other bidders.

Bidders must have equal opportunity to access tender related information without discrimination. Processes must be established to monitor and control the provision of information to bidders, particularly where the need to amend tender documents arises.

DOCUMENTING THE RULES AND BID EVALUATION

The Registration of Interest (ROI) or Request for Tender (RFT) must document the rules governing the conduct of the tender process, and be provided to all bidders at the beginning of the process. As we shall

see, in the *Hughes Aircraft Case*⁵, it was held that these documents have legal status, and government will be bound by the enclosed terms. For this reason, these documents must provide government with a flexible, yet sufficiently detailed framework to minimise potential legal challenges.

The development and application of consistent, transparent, well-defined evaluation criteria is essential to a successful tendering process. Recommendations as to the successful bidder should be based on a comparative analysis of individual bid evaluation reports. Full records of how and why specific recommendations and decisions were made, should be documented.

Tender closing deadlines must be adhered to, as more time to prepare a bid would give a tenderer an unfair advantage. Nothing must be said to the successful bidder to indicate they have won until all approvals have been finalised, as there is a risk of 'drifting into a contract' through informal discussion with the bidder.⁶ All bidders should generally be notified at the same time of the result of a tendering process.

THE ROLE OF THE PROBITY AUDITOR

A probity auditor is an external consultant employed to provide independent insight into probity issues. An external probity auditor may be needed when a transaction is of a high value, if a matter is highly complex, and where bidder grievances are likely. During the tendering process, a probity auditor advises on any probity issues that arise and before a recommendation to sign and contract is made, the probity auditor provides a report that confirms the probity plan, and that all processes have been equitably followed. A probity auditor must be an integral part of the tender process, and not a last minute consideration.

PROCESS CONTRACTS – EXPRESS AND IMPLIED TERMS

Although not yet discussed in the High Court, recent cases have suggested an unsuccessful tenderer in Australia may assert that a contract existed between it and the tender inviter, governing the process leading to the formation of the ultimate contract.⁷ The terms and conditions in a public sector tender document outlining the process to be followed and the bid evaluation criteria may create a preliminary 'process' contract. This contract imposes a duty to deal fairly, and governs the conduct of the subsequent tender process leading to the ultimate formation of the contract for which the bids are being sought.⁸ Breach of a 'process' contract can give rise to a cause of action for damages, similar to the cause of action available for breach of contract generally.⁹

The express terms of a process contract will be those stated in the RFT (or equivalent) document and the documents incorporated in this part of the process.¹⁰ Depending on the terms of the RFT, the relevant codes and guidelines (outlined above) are likely to be incorporated into tender documents by reference, thereby also forming part of the express terms of a process contract.

The test for implying a term into a process contract is no different to the test for implication generally.¹¹

In *Hughes* the court was prepared to hold that a term of 'fair dealing' could be implied into all public sector process contracts within a certain class.¹²

The case examples that follow provide some practical guidelines as to the circumstances where process contracts may be shown to have been intended by the parties, as well as the type of terms that the courts have been prepared to imply into process contracts.

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CASES

Hughes Case

Facts

The Federal Court in this case considered the tender process leading to the award of the Australian Advanced Air Traffic Systems contract by the Civil Aviation Authority (CAA). Hughes, the applicant, was an unsuccessful tenderer in the two party tender process. The CAA had sought formal acceptance from the two parties of the evaluation criteria prior to the issue of the RFT, and it was asserted by Hughes that a process contract had been formed between the CAA and each tenderer.

The CAA changed the selection criteria after the bids had been submitted. More weight was given to one particular criteria, without telling the bidders and without offering them the opportunity to revise their bids to accord with the amended criterion. This became apparent to Hughes during a de-briefing.

Decision

Process contracts

The Court concluded that the CAA acted illegally by failing to adhere to the bid evaluation criteria described in the RFT. In his judgement, Finn J accepted that a simple, uncomplicated request for bids will generally be no more than an invitation to treat (although it may give rise to obligations to act fairly). However, the RFT may constitute a preliminary contract with the expectation that it will lead in defined circumstances to a second or Principal contract.

Finn J looked to the facts surrounding the tender process, and held that a preliminary 'process' contract was formed which was binding on the principal and the tenderers, as to the manner in which the tender process was to be conducted.¹³ It was held that the steps taken by CAA were such as "would convey to a reasonable person in Hughes'

position...that the CAA was intending to bind itself to comply with the procedures proposed."¹⁴

Trade practices

CAA was also found guilty of engaging in misleading and deceptive conduct under Section 52 of the Trade Practices Act 1974 (Cth). CAA failed to follow its representations as to how the tender process would proceed, and failed to notify the tenderers when they varied the implementation of the tender process.¹⁵

Terms of fair dealing

Finn J held that the RFT Contract between Hughes and CAA contained an implied term that the evaluation would be conducted fairly by CAA.¹⁶ He was of the view that: "...fair dealing is...a proper presupposition of a competitive tender process contract (especially one involving the disposition of public funds)".¹⁷ He also held that a: "...necessary incident of [a process] contract with a public body is...that it will deal fairly with tenderers in the performance of its tender process contracts with them".¹⁸

Cubic¹⁹

Facts

The New South Wales Department of Transport sought to facilitate the development and implementation of a new Integrated Ticketing System (ITS) for Sydney's public transport system. After a detailed call for proposals, four tenderers were short-listed, including Integrated Transport Solutions Pty Ltd (ITSL) and Cubic Transportation Systems (Australia) Pty Ltd (Cubic). The tender dispute arose under a 'Call for Revised Offers' document (Call) which was issued only to ITSL and Cubic. ITSL was the preferred proponent chosen by the project control group.²⁰

Cubic's case

Cubic commenced proceedings seeking to restrain the NSW government from entering into a



contract with ITSL. Cubic had two main arguments:

- the government failed to comply with the tendering procedure set out in the Call; and
- the tender evaluation and selection process was not fair and did not offer an equal opportunity to both tenderers, as it did not adhere to the requirements and procedures set out in the Call.²¹ Cubic relied on an implied term of fair dealing and the judgement of Finn J in the *Hughes Aircraft Case*.²²

Clause 3.1.1 of the Call stated that '*no contractual relationship exists between the Principal...and any Proponent in relation to the evaluation of revised Proposals, and otherwise dealing with a Proponent in relation to the ITS*'.²³ Further, Clause 3.1.17 stated '*each proposal submitted in response to this Call will comprise an irrevocable offer by the Proponent to perform the undertakings and observe the representations and warranties set out in the Proposal. The irrevocable offer shall be given in consideration for the Principal agreeing to consider the Proposal in accordance with this call*'.²⁴

These two clauses are inconsistent in that one expressly says no contractual relationship exists between the parties, while the other implies the creation of a contractual relationship.²⁵ Cubic alleged that, as a matter of contract under the terms of the Call, it was entitled to the specified process of evaluation. Cubic also made allegations of bias, as two members of the Evaluation Committee had previous involvement with Cubic which may have made them biased against Cubic. Further, Cubic alleged the legal adviser and probity auditors past involvement with ITSL raised a conflict of interest issue.

Decision

It was found that the government did not breach any obligations owed to Cubic.

Process Contracts

It was held that 'a contract of some kind was intended' based on the language of contract in clauses 3.1.1 and 3.1.17.²⁶ No contractual relationship was formed in relation to the evaluation of the bids, however the Call, in conjunction with the NSW tendering code did give rise to an implied term of fair dealing in relation to the tender process. Adams J stated that: "...the nature of the contractual obligations of the parties in the context of this tender requires the implication of a term of

reasonableness and good faith, especially because of the broad powers the Call reserves to it to vary the Call and the processes under it".²⁷ Unlike Finn J in the *Hughes Aircraft Case*²⁸, Adams J did not conclude there would be a preliminary 'process' contract in every government tender.

Implication of a term to act fairly

Adams J was willing to assume that the rules of procedural fairness are relevant to the procedures of government.²⁹ However he held that the content of such rules must be related to the nature of the exercise being undertaken, and should only be implied where it is both reasonable and necessary to do so. He did not consider that an implied obligation of fair dealing prevented a public agency from having regard to its own responsibilities on behalf of the State of New South Wales and entirely disregard the commercial interests of the tenderers.³⁰

Bias

The court followed the decision in the *Hughes Aircraft Case*³¹, concluding that the question to be asked was whether there was actual unfairness or actual bias.³² There must be more than a mere apprehension of bias, as 'where the question is one of contractual obligation, a breach must be proved and not merely apprehended'.³³ It was concluded there was no actual bias, nor were there any conflicts of interest.

Conflict of interest

Clayton Utz, a major law firm with offices in six Australian cities, was retained to advise the Department on the ITP and was also one of the members of a Legal and Commercial Sub-Committee responsible for assessing (but not selecting between) the revised offers of ITSL and Cubic.³⁴ At the time, the firm was also acting for one of ITSL's joint owners, ERG, in another unrelated matter. It was decided by the firm that there was 'no issue of legal conflict' however 'appropriate Chinese Walls' were erected to ensure confidentiality.³⁵

Cubic argued that the firm had a critical conflict of interest which affected the tender. Adams J held that more than an appearance of disloyalty, or conflict is required. The risk must be a real one (although it need not be substantial).³⁶ He concluded there was no unfairness, nor potential for unfairness, therefore no conflict of interest, and no grounds on which to oppose the firm's involvement in the tendering process existed.

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...while government may protect themselves from liability under contract with probity, there are still other avenues for bidders to disrupt the tender process and seek damages.



LESSONS FROM THE CASES

The *Hughes* case makes it clear that a process contract can exist, and that this contract can incorporate both explicit and implied terms. The existence of a process contract in public tenders will depend on the wording of the RFT documentation. *Hughes* also makes it clear that evaluation boards must be strictly educated about the rules of probity and must accept that the evaluation criteria, once published, cannot be altered without a rigorous process, potentially involving re-tendering.

Although not always bound by contract, government agencies may attract liability in other ways. In *Hughes Aircraft Case*, the government was liable under the *Trade Practices Act* for breaching their duty of confidentiality. Therefore, while government may protect themselves from liability under contract with probity, there are still other avenues for bidders to disrupt the tender process and seek damages.

Hughes also makes clear the legal risks which may arise in conducting de-briefings.

The *Cubic* case brings a different message. In the first place, it emphasises that courts will take a

common sense approach to probity issues (while nonetheless imposing strict standards of accountability on government). The clearest lesson from *Cubic*, is that tender documentation must be drafted with the strictest attention, whether they constitute a contract. It seems relatively clear that, had the government not insisted on bids constituting irrevocable offers, there was some prospect of no process contract arising. This, however, is not a conclusive matter determined by the case.

One matter which is brought to attention by the cases is the tactical matter of whether to have a process contract or not. It may appear obvious to government that if a process contract can be avoided it should be (as the process contract is the most substantive basis of challenge of tender outcomes), but another view can be advanced. One may suggest that it is worthwhile drafting the RFT documentation on the *assumption* that a process contract exists because:

- this avoids the risk that a process contract will be deemed to be in existence despite efforts to the contrary;
- this allows the government to attend to the consequences of the process contract existing and make specific provision for it (eg. limitation of liability or confining the circumstances in which a remedy is available). In each case a different policy outcome may justify a different conclusion.

The cases also show that the courts will take into account the behaviour of not only the government agency, but also the bidder. In *Cubic*, it was held that the questionable behaviour of a bidder could be grounds for denying a remedy. This will undoubtedly affect the behaviour of bidders in the future.

Current case law does not require a change the behaviour of government agencies that are already governed by numerous policies and guidelines. The main concern must be to ensure that the government agencies are aware of their obligation of probity and that this is enshrined in all tender processes.

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- 1 The Victorian government Purchasing Board, *Probity Guidelines for Tendering Projects in Victoria*, December 2001 <www.vgpb.vic.gov.au>
- 2 *Code of Tendering for NSW government Procurement* (NSW); The Victorian government Purchasing Board,

THERE'S MORE TO THIS CHICK THAN MEETS THE EYE

- Probity Guidelines for Tendering Projects in Victoria* December 2001 <www.vgpb.vic.gov.au> and *Ensuring Openness and Probity in Victorian government Contracts* [government Policy Document] (Vic); *State Purchasing Policy* (Qld); *Probity Guidelines for Tendering and Contracting* (Tas); *State Supply Board Policy* (SA) <www.statesupplyboard.sa.gov.au>; *State Supply Commission* (WA), *Guidelines for Assuring Quality in government Purchasing* <www.ssc.wa.gov.au>; *Commonwealth Procurement Guidelines & Best Practice Guidance* February 2002 (Cth)
- 3 *Code of Tendering for NSW government Procurement*
 - 4 In Victoria, for example, government must disclose details of the contract, excluding trade secrets and confidential business information, on the Victorian government Purchasing Board Website (see *Ensuring Openness and Probity in Victorian government Contracts*). For this reason, the government must restrain from providing bidders with absolute confidentiality assurances.
 - 5 *Hughes* (1997) 146 ALR 1
 - 6 The Victorian government Purchasing Board, *Probity Guidelines for Tendering Projects in Victoria* December 2001 <www.vgpb.vic.gov.au>
 - 7 *Hughes Aircraft Systems International v Airservices Australia* (1997) 146 ALR 1
 - 8 *Hughes* (1997) 146 ALR 1
 - 9 M. Bell, *From an invitation to treat to an invitation to treat...warily* (2003) 19 BCL 89 at 89
 - 10 *Transit New Zealand v Pratt Constructors Ltd* [2002] 2 NZLR 313 at 333
 - 11 See *BP Refinery West (Westenport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266 at 282-3. Cited with approval by the High Court in a number of cases, including *Codeffa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337 at 347 and *Hospital Products v United States Surgical Corp* (1984) 156 CLR 41 at 66
 - 12 The court thought there was '...much to be said for the view that, having no legitimate private interest in the performance of its functions, a public body (including a state owned company) should be required as of course to act fairly towards those with whom it deals at least in so far as this is consistent with its obligations to serve the public interest (or interests) for which it has been created.' (1997) 146 ALR 1 at 41
 - 13 *Hughes* (1997) 146 ALR 1 at 2
 - 14 *Hughes* (1997) 146 ALR 1 at 28
 - 15 *Hughes* (1997) 146 ALR 1 at 44
 - 16 *Hughes* (1997) 146 ALR 1 at 42
 - 17 *Hughes* (1997) 146 ALR 1 at 42
 - 18 *Hughes* (1997) 146 ALR 1 at 42
 - 19 *Cubic Transportation Systems Inc v New South Wales* [2002] NSWSC 656
 - 20 *Cubic Transportation Systems Inc v New South Wales* [2002] NSWSC 656 at para. [1] & [2]
 - 21 *Cubic* at para. [28]
 - 22 *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151 at 157
 - 23 *Cubic* at para. [6]
 - 24 *Cubic* at para. [6]
 - 25 *Cubic* at para. [16]
 - 26 *Cubic* at para. [44]
 - 27 *Cubic* at para. [44]
 - 28 *Hughes* (1997) 146 ALR 1
 - 29 *Cubic* at para. [58]
 - 30 *Cubic* at para. [58]
 - 31 *Hughes* (1997) 146 ALR 1
 - 32 *Cubic* at para. [43]
 - 33 *Cubic* at para. [163]
 - 34 *Cubic* at para. [131]
 - 35 *Cubic* at para. [132]
 - 36 *Cubic* at para. [138-139]



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