

TWO IMPORTANT PUBLIC CONTRACTING BIDDING CASES

By Howard B. Brown
Of Counsel, Lanak & Hanna, P.C.

Contractors bidding on public projects and their sureties know and understand the statutes, rules and regulations that affect their bids. No effort will be made here to repeat these. However, two California appellate courts have within the past few months rendered decisions that concern all those bidding on public projects. The decisions are *Schram Construction, Inc. v. Regents of the University of California* (August 24, 2010 and modified September 22, 2010) and *Great West Contractors, Inc. v. Irvine Unified School district* (August 31, 2010 and modified September 30, 2010).¹

In the *Schram* decision, the court was concerned with interpretation of a statute providing that an award of a contract for construction by the public body is to be based upon the “best value contractor.” The case directly affects only projects of the University of California, since the statute concerned was enacted as a pilot program and applies only to the University of California in San Francisco.² However, the case is important outside the context of a University bid, since it is possible or even probable that another court may apply the decision to *any* case where the award was given to the contractor who was deemed to be offering the *best value* to the public entity inviting bids. After *Schram*, it is reasonable to expect that if a contractor is bidding on a public project, this decision may guide and perhaps even control, the bidding process.

Most commonly in bidding procedures, the bidder on a project offering the lowest price is awarded the contract. However, an award may also be based on a district’s confidence in a particular contractor with which it has had previous, successful dealings. Perhaps for both of these reasons, the legislature has granted public entities the right to employ methods other than advertising and awarding the contract to the “*lowest* responsible bidder,” the “*most* responsible bidder,” or even to the “*best value* contractor” as provided in Public Contract

¹ *Schram Construction, Inc., v. The Regents of University of California*, 187 Cal. App. 4th 1040 (2010); *Great West Contractors, Inc. v. Irvine Unified School Dist.*, 187 Cal. App. 4th 1425 (2010). These cases are hereafter referred to as *Schram* and *Great West*, and jointly as “the decisions.” Although *Schram* did not a “lease-lease back” project in other respects its application may be applicable to all public projects.

² Public Contract Code § 10506.4.

Code § 10506.7. This was the situation in *Schram*, where, adopting the permission granted to it, the public entity awarded the contract based upon a bid upon what the agency considered to be the *lowest responsible bidder*. It did so using what is referred to as a “lease – lease back.” This procedure permits the school district or public agency to award a contract not to the lowest bidder, but that which the agency may consider to be the best value. On the surface, such a procedure appears susceptible to favoritism and paternalism.

The section for the construction of school buildings further provides that the lease for the construction “shall be with the lowest responsible bidder.” Although Education Code Section 17417 provides for “advertising for bids,” Section 17406(a) provides:

“Notwithstanding the provisions of Section 17417, the governing board of a school district, without advertising for bids, may let, for a minimum rental of one dollar (\$1.00) a year to any person, firm, corporation any real property that belongs to the district if the instrument by which such property is let requires the lease thereon to construct on the demised premises, or provide for the construction thereon of a building or buildings for the use by the school district during the terms thereof, and provides that title to the building shall vest in the school district at the expiration of that term.”

It is fair to assume that the result in the *Schram* decision, although concerning a construction project based upon “lease – lease back” and using a “best value” basis for selection of the contractor, will be applicable to any public entity awarding a contract to a contractor on a “best value” basis.

In *Schram*, the bidding contractor Schram appealed from a decision of a trial court affirming the University’s denial of the contractor’s demand to bid for a portion of a project. The hearing officer denied all protests, concluding that the University was not required to select bid packages based on “best value” but had reserved the option to select bid packages and disclosed this to prospective bidders. The hearing officer found that the University did not know the identity of the low bidder and had applied a blind bidding process. The hearing officer found no evidence of bias or favoritism in the bid package selection or low bidder

determination, and that it was in the University's best interest to award the contract to one contractor.³

After tracing the history of contract awards for public projects, the appellate court explained that the best value method requires that the contract be awarded to the bidder offering the best combination of price and qualifications, as based upon objective criteria including financial condition, relevant experience, previously demonstrated management competency, labor compliance, and safety record. The court explained, “[w]hen the University relies on the best value method, as it did in this case, it must ‘adopt and publish procedures and required criteria that ensure that all selections are conducted in a fair and impartial manner. . . . These procedures must comply with statutory provisions requiring: a bid solicitation that notifies prospective bidders of the ‘[c]riteria [the University] will consider in evaluating bids,’ the methodology it will use ‘in evaluating bids,’ and the relative importance of each of these criteria and the assignment of a qualifications score to each bid; and identification of the bidder determined to be the best value to the University (best value contractor) by dividing each bidder’s price by its qualifications score in order to determine the bid that provides ‘[t]he lowest resulting cost per quality point (best value ratio).’”

The court examined the statutes in light of “the purpose for which they were enacted: ‘[to invite] competition, to guard against favoritism, improvidence, extravagance, fraud and corruption, and to secure the best work or supplies at the lowest price practicable.” The court then carefully examined the objections raised by Schram, stating, “On its face, the statute mandates publication of the procedures and criteria necessary to ensure that all selections are conducted in a fair and impartial manner. It follows that information regarding the procedure and criteria for selecting bid packages . . . must be disclosed to the extent the bid selection would otherwise be unfair or its integrity would be compromised by nondisclosure. We conclude publication of the bid package selection information was necessary to a fair and impartial bid selection in this case.”

³ The project itself was extremely complex, consisting of six individual packages and three alternative combination packages. After learning which subcontractors had bid on each package, DPR—the contractor to whom the contract was awarded—and the University decided to change the various packages apparently to accommodate DPR. Such changes may very well have influenced the appellate court into believing that favoritism was reasonably established, although the court did not expressly comment on this aspect.

So why was the bid process flawed? The court explained that the bid selection turned on a criterion not disclosed to bidders, that is, the University's desire to award as much of the work as possible to a single subcontractor. This threshold criterion applied to all bids and was a major factor in identifying the best value bid. As a result, bidders were forced to guess at what would satisfy the University's needs. This information would also have been material to prospective bidders' decisions to participate in the bidding process in the first place. A contractor is at a competitive disadvantage, not only when undisclosed information undermines its ability to bid on same basis as others, but also when the undisclosed information is material in deciding whether to submit a bid in the first instance.

The court acknowledged that the hearing officer found no evidence of favoritism or bias, but said, "[r]egardless of whether the University acted with an improper motive, in our view, the [University's] knowledge of bidder identities permitted the University to control the results by its selection of the bid packages to be awarded. In requiring the University to adopt procedures that 'ensure' that the selection will be impartial, section 10506.4, subdivision (c) suggests it is not enough to simply refrain from favoritism; *the University must put affirmative safeguards in place to prevent bias and other arbitrary factors from influencing the bid selection.* We also conclude that the University's procedure here created an appearance of favoritism and undermined the integrity of the public bidding process, particularly since DPR had done a substantial amount of work with both Southland and ACCO in the previous five years." (Italics added.)

This decision will probably affect the conduct, drafting and award of contracts (not only for construction materials, but also for supplies) by public entities and those bidding on them. Clearly the award of the contract should not be affected by favoritism or bias for or against any bidder. Awarding entities must define the parameters and conditions upon which any award will be based. At the same time, contractors bidding on such projects should be aware of their right to protest an award based upon such favoritism. The *Schram* decision rested upon demonstrable evidence of bias that favored one bidder: such conduct is not acceptable. The evidence that it occurred, however, must be clear and unequivocal.

The *Great West* court began its decision by stating, "[t]his case is important for two reasons. First, it presents a challenging problem in public contracting law: How to distinguish a 'nonresponsive' bid from a de facto determination that the bidder is not a 'responsible' bidder. The difference is significant not only to the bidder, but to the taxpaying con-

stituency of the public entity: A truly nonresponsive bid may be summarily denied by a public entity even if the bid is otherwise monetarily the best for the entity. On the other hand, a determination of nonresponsibility entitles the bidder to a hearing where certain minimal elements of due process must be afforded before the contract can be awarded to the next-best bidder.”

The court continued, “The second major reason this case is important is that it presents an object lesson in how evidence that, at least on its face, tends to show favoritism—indeed, on this record, favoritism most foul—never got squarely presented to, or considered by, the trial court. The reason? An unfortunate combination of trial court calendaring beyond a petitioner’s control, and a public entity’s delay in complying with a request for information. (Readers can judge for themselves, when we recount the facts in detail in part II below, whether ‘stonewalling’ might not be a better word than ‘delay.’)”⁴

The decision is long and summarizes many prior court decisions. It, like *Schram*, also involves the issue of favoritism in the bidding process of public entities, in this case with a public school district. Some of the comments above regarding bidding by public entities—particularly schools and school districts—are applicable here, particularly references to the “lowest responsible” versus the “lowest” bidder.

The Irvine Unified School district [hereafter the district] was remodeling two elementary schools, and in 2008 sent out requests for bids for the work. The plaintiff, Great West Contractors, Inc., was the lowest bidder on both projects. However, the third-from-lowest bidders on each project, JRH Construction and Construct 1, were awarded the contracts. The decision by the court is 39 pages long and no attempt will be made to summarize all the facts or the basis for the court’s final decision. The appellate court relied heavily upon earlier case law,⁵ stating,

“Under the *D.H. Williams* rule, a public agency cannot reject the bid of the lowest bidder on a public works project on the theory that the *bid* is ‘nonresponsive’ to the agency’s request for bids when, *in substance*, the real reason for the rejection is that the

⁴ These are the court’s words—presumably every court decision is important!

⁵ *D.H. Williams Construction, Inc. v. Clovis Unified School District*, 146 Cal.App.4th 757 (2007).

agency thinks the lowest *bidder* is ‘not responsible’ – at least not without giving the lowest bidder the chance for a hearing on whether it really is ‘not responsible.’ On the record before us, because *D.H. Williams* was not followed, the Unified School district appears to have paid \$800,000 more than necessary to remodel two elementary schools.”

Nonresponsibility versus Nonresponsiveness

The court begins its discussion of the legal principles by noting the differences between “responsiveness” and “responsibility,” and stating that the rejection by the district of Great West’s bid was for “nonresponsibility,” not “nonresponsiveness.” This is the crux of the court’s argument and decision.

After the pre-qualifying process was completed, the district notified Great West in May 2008 that it was qualified to bid on the projects. Based upon this, Great West submitted its bids. It was, as previously noted, low bidder on both projects. The court noted on several occasions that, “[t]he exact differences between the winning bids and what lowest bidder Great West bid were \$323,673 on Northwood, \$486,000 on Eastshore. The total that the district paid for its decision to summarily reject Great West’s bid was \$809,673.”

Objections were made by Eastshore Contractors and Construct 1 [hereafter the objectors]. As noted above, these two objectors to whom the bids were eventually awarded were the two third-from-lowest bidders. No attempt will be made here to detail what objections were made or all the factors that were considered by the court. The objections included alleged mistakes in the statements of their licenses, including their license numbers, names and officers, or qualifiers on their behalf. Objections were also made to Great West’s bids based upon mistakes in its bids, including erroneous interpretations of the plans and specifications. The court rejected all of these objections on various grounds, including that some of the alleged errors and mistakes were the same as made by those objecting to the award to Great West.

The court also discussed certain actions taken by the district that indicated a failure to deal fairly and equally with all bidders. In particular, the court noted that the objectors were able to obtain copies of all bids from the district within 24 hours after the bids were submitted, as though the district were inviting objections.

The court discussed the factors that the district considered in not awarding the contract to Great West and rejected all of them, in stating:⁶

“The bottom line of the letter (literally) was that district staff were recommending the district’s board ‘reject your bid as non-responsive.’ As Great West’s opening brief now points out, the staff letter did not invite any response or suggest any opportunity for refutation or denial of its allegations. In any event, the board was due to award.”

Since the court was concerned with making its decision more understandable, the opinion discussed in great detail the legal processes that were employed by the parties. It focused on the district’s haste to get the process moving while Great West attempted to argue the legitimacy of its bids before the district, and before the courts could set them aside.⁷ It stated:

“It is established law that a contractor wrongfully denied a public contract by a public entity can only recover bid preparation costs but not lost profits. (*Kajima, supra*, 23 Cal.4th at p. 308 [‘We conclude bid preparation costs but not lost profits are available under a theory of promissory estoppel.’].) As Great West’s counsel pointed out in oral argument before this court, the rule has this effect: The main incentive for a bidder who has been wrongfully denied a public contract is to bring litigation that seeks to have the public contract ultimately awarded to it. And since such litigation is necessarily a prolonged process, which can entail a victory consisting of an order for a new request for bids and rebidding (as happened in *Konica, supra*, 206 Cal.App.3d 449 [where university had no discretion to excuse large deviation by winning bidder, university was required to publish new request for bids within 30 days of remittitur]), even more time will pass during which the relief request can be mooted.”

⁶ Although the court rejected the objections upon technical grounds, contractors bidding on a project should be very careful to make accurate statements to any owner or entity seeking bids.

⁷ The court’s discussion of the various petitions and writs will be of interest to attorneys but are not particularly significant to those employing the attorneys. However, the actions of the district were strange. According to the opinion of the court, the district ignored the court’s writ ordering it to stop work. In fact, the project was completed before the decision could be or was rendered!

The crux of the case was the distinction between the concepts of a “nonresponsive” and a “nonresponsible” bidder. The court explained, “[t]he nonresponsive versus nonresponsible issue is, however, a classic example of an issue capable of repetition yet likely to evade review. Consider: In public contracts of a short lead-time nature, like the ones here, an initial determination by the public agency that the lowest bid is “nonresponsive” allows for a summary rejection of that bid that may readily preclude effective judicial redress. ... Within a month, a little month, this case was effectively over as far as any practical possibility that the lowest bidder might actually obtain the contract was concerned.”

The court explained its distinction between the two concepts by explaining that this case “involving as it does the question of the difference between a nonresponsive and a nonresponsible bidder, does not implicate an issue of the public interest. But it obviously does. As the *D.H. Williams* court stated: ‘School districts, like most other public agencies, are required by law to award construction contracts (with certain narrow exceptions) to the lowest responsible bidder.’ Assuming that Great West is correct that its bid was not ‘nonresponsive,’ then this case represents an example of how the statutory mandate that public contracts be awarded to the lowest responsible bidder could be readily circumvented: The agency simply deems some aspect of the winning bidder’s bid package to be ‘nonresponsive’ in order to award the contract to the next (and perhaps favored) bidder.”

The district found that Great West’s bid was nonresponsive. The court distinguished between “nonresponsive” and “not responsive.” When the [trial] court observed during oral argument that “technically they [Great West] were responsive, they [the district] answered the question,” district counsel argued that not answering the question “truthfully” made it nonresponsive. The judge then asked, “Well, but are they not entitled to a hearing thereafter?” And counsel for the district said no – not when there is a “determination of nonresponsiveness.” The court, however, disagreed and said that,

“The definition of responsibility is fairly easy, because it is now statutory, set forth in section 1103 of the Public Contract Code. We now quote in full: ‘Responsible’ bidder, as used in this part, means a bidder who has demonstrated the attribute of trustworthiness, as well as quality, fitness, capacity, and experience to satisfactorily perform the public works contract.” Thus, “the statute speaks in terms of personal qualities that have been ‘demonstrated’ by the bidder. And the legislative emphasis on

responsibility going to the personal quality of the bidder is all the more significant when one recognizes the history of the case law on responsible bidding.”

The court discussed another case where it was found that the bidder was not responsible because it did a poor job in a prior job for the public entity. Thus, it determined that responsibility relates to such things as workmanship, where a school district had good reason not to trust the lowest bidder to do “even a halfway decent job.” For example, “a city could validly declare [a] contractor as irresponsible in wake of disputes over change orders and city utilities and a commission finding that [the] contractor knowingly and intentionally submitted false claims.”⁸

Based upon this analysis, the court concluded that the district was incorrect in rejecting Great West’s lowest bid as nonresponsive. The appellate court concluded that the trial court erred in agreeing with the district and reversed the trial court decision affirming the right of the district to ignore Great West’s bids.

Care to Be Taken By and Responsibility of Bidders

Although the court exonerated Great West from mistakes it made during the bidding process, it is worth noting that it is dangerous to be sloppy or careless. Contractors bidding upon projects, whether public or private, should be very careful to read the instructions for bidding and the plans, and be familiar with the site where the project is to be located. One of the reasons this appellate court ruled as it did was that it was clear from the outset that the district did not want Great West to be awarded the contracts. We don’t know the real reason for this, but in reading the opinion it is clear to the reader—as it was to the appellate court—that the awarding process was influenced by favoritism. Bidding agencies should be aware that the bidding process should not be taken lightly and favoritism should have no part of the bidding process.

The significance of this decision is similar to that noted above with *Schram*: those concerns and entities bidding upon public projects should be careful in their relationships with the bidding agencies. A close relationship will be carefully examined by other bidders upon the same project. Further, avoid any acts or conduct that could be viewed by others as

⁸ This subject, like all others, is extensively discussed by the court.

demonstrating favoritism or bias in the selection of the successful bidder. It would be much better to not make a bid than to make a bid and be assailed by others as having benefited from favoritism, bias, or even fraud. Parties should not, either before invitations or advertising for bids are sought or published, participate in any conduct that could be interpreted as improper.

Although not expressly referred to by either of the foregoing decisions, to avoid any hint of impropriety, bidders on public projects should avoid social relationships with those employed by a public entity engaged in preparing or requesting bids on public projects. Failure to do so may result in the disqualification of an otherwise prevailing bid. The disadvantages of litigation were obvious in the *Great West* case: legal costs and the lack of a remedy other than recovering the costs of preparing the bid.

0-0-0