

Contract law and public procurement

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1 Money

In 2014, the European Union's GDP was almost € 14 trillion.¹ Its public procurement was estimated to account for 16 percent of the GDP.² 16 percent of € 14 trillion is € 2, 24 trillion.

A € 10 bill is approximately 0,1 mm thick. Thus, in € 10 bills, tightly packed together, the money spent on public procurement in the EU each year would, with a ten percent margin, reach halfway around the world.

Consequently, we have good reasons to make sure that our public procurement is efficient. Even a marginal improvement – let's say two percent – will provide access to vast sums of money to be used in a better way than on inefficient procurements. Two percent of € 2,24 trillion – that is about 450 km in € 10 bills – equals e.g. most of Sweden's yearly spend on public procurement. It is my firm belief that this article is worth at least that much!

2 Contract law and public procurement law

The structures of contract law and of public procurement law are fundamentally different. While contract law regulates the relationship between the parties to a contract – and nothing else – public procurement law regulates the relationships between a contracting authority and all suppliers, in practice primarily those who are not awarded a contract.

Although fundamentally different, the two structures meet and must coexist in public procurement. On a timeline, public procurement law primarily regulates events prior to the conclusion of the contract, while contract law starts when the offers³ are submitted and continues way past the immediate relevance of public procurement law.

In a more practical sense, they affect each other greatly. Public procurement law limits the freedom of contract, both regarding the right to conclude contracts with whomever the contracting authority wants and in some regards the

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¹ See http://europa.eu/about-eu/facts-figures/economy/index_en.htm (2015-09-29).

² See <http://ec.europa.eu/trade/policy/accessing-markets/public-procurement/> (2015-09-29).

³ I will use the "contractual" term "offer" rather than the term "tender", which is used in e.g. dir. 2004/18/EU. At least for the purpose of this article, there is no difference between them.

content of contracts. It also limits the right to change an existing contract. The reason is that a changed contract really is a new contract and, as such, shall be procured in accordance with public procurement legislation. These limitations are in a way the backbone of public procurement: They are if not the purpose, at least the immediate effect of the purpose of the legislation.

Major parts of *the legislation* regarding public procurement more or less disregards the existence of contract law. Instead of focusing on the performance of a contract, it focuses on formalities and underlying EU principles in order to promote objectivity and fairness as well as the free movement of goods and services. That is natural, since that is part of the structure and purpose of that type of regulations.

However, that does not mean that *contracting authorities* shall disregard the existence of contract law and focus only on formalities. If they do, they waste money. Our money. Instead, contracting authorities shall conduct their businesses as efficiently as possible. That shall, of course, be done within the boundaries of public procurement law. In many minds, that seems to create a conflict. In my mind, that conflict hardly ever exists: The public procurement legislation is much more forgiving than what most people believe. A great part of common procurement problems are easy to handle. The key factor is to keep things simple. The tool is contract law.

In this article I will discuss some aspects of public procurement law and practices where contract law and contractual solutions provide alternatives to the common procurement practices. I am certain that the contractual solutions in most cases will provide higher value to the contracting authority and – in its extension – the taxpayers.

The article is based on Swedish law. For public procurement, it is limited to LOU (lagen (2007:1091) om offentlig upphandling), which is based on primarily dir. 2004/18/EU.⁴ Since my purpose is to discuss the relationship between public procurement law and contract law, I have simply assumed that LOU corresponds to the underlying directives.

3 The purpose of contract law and the purposes of contract terms

Contract law is relatively simple. The overall purpose is to create value for the parties. Contracts are concluded because their parties believe that they will be better off with the contracts than without them. If they don't, it does not make any sense to contract at all. Instead, it is better for the buyer to do the work or produce the goods itself and for the supplier simply not to sell.

⁴ <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32004L0018&from=en>.

Contract terms – or clauses – on the other hand, can be divided into four separate categories, with distinctive and separate purposes. The purpose of the first category is to create order. The second and third categories are reflections of each other. They divide values and risks. The fourth category summarizes the division of values and risks.

3.1 To create order

Some clauses have as their sole purpose to create order. Typical clauses within this category are choice of law clauses, clauses determining where and how conflicts shall be resolved – forum and primarily arbitration clauses – entire agreement or merger clauses⁵ and written modification clauses.⁶

In contrast to clauses within the second and third categories, clauses within the first category are not necessarily beneficial to one of the parties, even though they in a specific situation can prove to be so. Choice of law clauses provide a good example. Parties and their lawyers tend to believe that their own national legislation is a supreme choice: Swedish lawyers prefer Swedish law, German lawyers prefer German law etc. Large corporations often seem to take pride in enforcing their own legislation in contracts: “We are a large Swedish legal entity. Of course we shall have Swedish law in our contracts.” However, at the end of the day, that could very well be the single reason why a case is lost, since the solution provided in the chosen legislation may prove to be detrimental to the party who insisted on it. But that is a consequence, not the purpose, of the clause.

3.2 To divide values

A few clauses divide values between the parties. Most prominent among them is the description of the object of the contract: In most peoples’ minds, “champagne” provide the buyer with a higher value than simple “sparkling wine”. Consequently, if the object is described as “champagne” the buyer is entitled to a higher value than if it were only described as “sparkling wine”. Some sparkling wines are quite horrible, while champagne rarely tastes anything but well.

Another aspect of dividing values shows itself when the outcome of the contract is better than anticipated. If e.g. the object of the contract is more valuable than anticipated, it will usually benefit the buyer. But nothing prevents the parties from agreeing on another division of that possible additional value, so that it partly or wholly shall benefit the supplier.

⁵ See e.g. art. 2.1.17 Unidroit Principles of International Commercial Contracts (2010).

⁶ See e.g. art. 2.1.18 Unidroit Principles.

3.3 To divide risks

The mirror image of dividing values is the division of risks. Almost all contract terms worth mentioning fall into this category.

The description of the contract's object is one of them.⁷ It allocates values, but even more so risks. A buyer of "food" may assume that it is edible, but stands the risk that it does not taste very well. The buyer of a "boat" may assume that it floats, but stands the risk that it is not very fast. And of course, the buyer of "sparkling wine" stands the risk that it is horrible.

Other examples of terms that divide risks are all terms relating to delivery⁸ and the passing of risk,⁹ non-disclosure and competition, definitions of obligations¹⁰ and – of course – remedies for non-performance,¹¹ including notices of non-performances.¹²

3.3.1 *Division of risk and economy*

The sum of the division of risk always amounts to 100 percent. All risk that is not borne by one of the parties, must by necessity be borne by the other party (or other parties). Parties cannot – at least not in a way that affects anyone else – agree that a certain risk shall be borne by a third party. That requires the consent of that third party, who then is no longer a "third party".

It is simple economy that risks are costs. Every change in risk affects a party's costs. As a consequence, it also affects the price that a buyer is willing to pay, or the price that a supplier charges.

3.4 To summarize the division of values and risks

The fourth category has only one clause: The price. The price summarizes the division of values and risks. Most people are willing to pay more for a bottle of wine if it is a champagne – regardless of whether they know what champagne it is – than for a bottle of sparkling wine, at least as long as they do not know what sparkling wine it is. The reason is simple: The possibility that it tastes well is higher, and the risk that it tastes horribly is lower, with the champagne than with the sparkling wine.

The same reasoning is true for other clauses. For a buyer with a tight time schedule, time is more valuable than it is for other buyers. Therefore, a contract

⁷ See e.g. art. 35 CISG (the UN Convention on Contracts for the International Sale of Goods).

⁸ See e.g. art. 30–33 CISG.

⁹ See e.g. art. 66–70 CISG.

¹⁰ See e.g. specifically art. 31 and art. 33 CISG.

¹¹ See e.g. art. 45–52 CISG.

¹² See e.g. art. 38–39 CISG.

with liquidated damages amounting to e.g. 5 percent of the price per day has higher value for that buyer than a contract with liquidated damages amounting to 1 percent of the price per week. Consequently, that buyer shall be prepared to pay more for the former contract term than for the latter. And a buyer of an object that is anticipated to last for at least ten years, shall be prepared to pay more, if the supplier in the contract agrees to be responsible for lacks of conformity during that time, instead of what follows from non-mandatory law, which usually is one or two years.¹³

3.4.1 *“Supplier friendly” and “buyer friendly” contracts or clauses*

A well-established misunderstanding is that contracts or contractual clauses can be “supplier (or seller) friendly” or “buyer friendly”. That may be true, but only when the parties don’t know what they are doing. To professional parties, a “supplier friendly” clause or contract – i.e. one that places most values with the supplier or most risks with the buyer – has lower value to the buyer than it would have had with other regulations. Professional parties will let that be reflected in the price. And a low price is hardly “supplier friendly”. On the other hand will a “buyer friendly” clause or contract place most values with the buyer and most risks with the supplier. To professional parties, that will raise the price. And high prices are usually not regarded as “buyer friendly”.

3.4.2 *Establishment of price*

The purpose of the price is to summarize the values attributed to and the risks assumed by each party. The more value attributed to it and the less risk borne by it, the higher price shall the buyer be willing to pay. And of course, with a lower value and a higher risk, a buyer shall not be willing to pay as much.

4 The description of the supplier’s obligations

The single most important clause in any contract is the description of its object. On a good second place comes clauses specifying other obligations of the supplier, primarily the time and place for performance.

The object shall be described as well as possible under the circumstances at hand. If the contracting authority has the technical expertise, it shall describe the technical solutions in detail. If, on the other hand, the technical expertise is with the supplier, the contracting authority shall only describe the functions that it wants to achieve and let the supplier choose the most appropriate technical solution.

¹³ See e.g. art. 39 (2) CISG.

If the descriptions are adequate, the supplier stands a good chance to calculate a “correct” price and the buyer stands a good chance to have remedies if the supplier does not perform. If, on the other hand, the descriptions are not adequate, the supplier cannot correctly calculate a price, but must to a greater or lesser extent *guess* what it will be required to perform. From a legal point of view, that may be OK. Nothing prevents parties from contracting for the sale of “a thing”¹⁴ that shall be delivered “later”¹⁵ and “somewhere”.¹⁶ The contract will still be valid. But there are definitely better solutions, both legally and commercially.

With uncertainties – even if not as extreme as in the paragraph above – the buyer will not be able to know what rights it may have. The risk that the buyer will be dissatisfied is higher. Therefore, the risk for litigation is higher. Since the burden of proof in litigation primarily will be on the buyer – at least regarding the conformity of the goods – it is in the buyer’s best interest to avoid that situation. The best way to do that is to improve the description of the object. That can only be done before the contract is concluded.

The description of the object of a contract is of paramount importance. With a poor description, it is pure luck if the contract will be performed correctly (whatever that may be under the circumstances). With an adequate description, the contract will stand a good chance to actually function. Although slightly less important, this is true for the description of other obligations as well. The contract will certainly work better if e.g. the time and place for performance is specified, than if they aren’t.

5 Remedies for non-performance

The description of the supplier’s obligations is the most important part of almost any contract. Without it, it usually doesn’t matter what the rest of the contract looks like. This is primarily due to the fact that a great part of most contracts contains remedies for non-performance. And if it cannot be established whether or not an obligation has been performed, there is no need for any remedies.

But after the description of the obligations, the most important part of any contract contains the remedies for non-performance (or breaches of contract). They have two purposes. One is to correct the effects of a party’s – usually but not always the supplier – non-performance. The other – and from a practical point of view much more important – purpose is to give primarily the supplier *good incentives* to do what the buyer wants.

¹⁴ Cf. art. 35 CISG.

¹⁵ Cf. art. 33 CISG.

¹⁶ Cf. art. 31 CISG.

5.1 *Pacta sunt servanda*

Contracts must be honored: *Pacta sunt servanda*. That is, however, not the whole truth. In many contracts, it is actually quite far from the truth. In practice, it is only true to the extent that it is supported by remedies for non-performance of contractual obligations. More than anything else, the true meaning of *pacta sunt servanda* is a matter of liability to pay damages for the non-performance of contractual obligations. In e.g. CISG and Unidroit Principles, a non-performance by one party usually leads to the obligation of that party to pay damages to its counterparty. The damages shall cover all loss, including – or rather primarily – loss of profit.¹⁷ In that setting, the concept of *pacta sunt servanda* is a true reflection of reality.

But when – as is often the case – a non-performing party's liability is limited, one may argue that the concept of *pacta sunt servanda* is only partially true: Is it e.g. still correct to say that the (whole) contract must be honored, when the liability is limited to only “direct loss”, to the price for the performance or a certain fraction of it, or liquidated, so that the loss – regardless of how high it actually is – is agreed to equal a certain fraction of the price per time unit? In such cases, a part – often a major part – of the negative effects of a non-performance will be borne by the aggrieved party. To that extent, it does not cost a non-performing party anything if it does not perform. And as a consequence: To that extent, the idea of *pacta sunt servanda* may very well be said to not apply.

This is – of course – theory with little practical importance in itself. It is, however, important to raise the issue, since it emphasizes the importance of the remedies available to one party in case of the other party's non-performance. If they do not support the obligations to perform, it is relatively easy to choose not to perform the obligations. And then, the contract is not worth much for the aggrieved party.

5.2 Remedies as incentives

It is not uncommon that parties emphasize how important certain aspects of the other party's obligations are, and then let the remedies speak a totally different language. Contracts state that “time is of the essence” and at the same time state that a late delivery will entitle the buyer to liquidated damages that will amount to only a minor portion of its actual loss. They will underline the paramount importance of quality, and at the same time state that non-conforming objects shall be repaired “within a reasonable time” – and without any economic pressure on the supplier – and that the buyer, if the supplier does not repair within that

¹⁷ See art. 74 CISG and art. 7.4.1. and 7.4.2. Unidroit Principles.

time, will be entitled to a relatively modest price reduction. Such constructions are not good incentives. If anything, they are counter-productive.

A buyer shall always ask itself *how important* different aspects of a contract are. The amount of importance shall be reflected in the contract. If time is important, it shall be relatively expensive for a supplier to perform late: If Christmas presents are bought, the purchaser must have the right to terminate¹⁸ the contract at least a day or two before Christmas and to – on the supplier's expense¹⁹ – purchase new presents. If quality – or a certain level of quality – is important, it must be expensive for the supplier not to perform on that level. Every obligation of the supplier has a price. That price depends on the risk that a non-performance occurs and the remedy for such non-performance.

Remedies for non-performances shall be regarded primarily as an *incentive program*. The contracting authority shall ask itself: How do I create a situation where I can be as sure as possible to receive performance, and how do I achieve that without having to pay more than necessary?

6 Fundamental and other non-performances

Termination of a contract is usually regarded as the ultimate remedy for a breach of contract. If a contract is terminated, both parties are released from their obligations under the contract, except the obligation of the non-performing party – the party in breach of contract – to pay damages.²⁰ The standard prerequisite for termination is that the non-performance is *fundamental*. Non-performances that do not reach that threshold, will still entitle the aggrieved party to remedies, but the contract will remain intact. The definitions of the concept of *fundamental non-performances* are at best vague.²¹ That is a problem when a conflict needs to be solved. But it does not need to be a problem for the drafter of a contract.

A party needs to be able to terminate a contract only if it would not have concluded it at all – not even on different terms – if it at the time of the conclusion of the contract had known that the other party would not perform. In all other situations, other remedies are sufficient. If the party had been willing to purchase at a lower price if it had been aware of the non-performance, combinations of a later performance, repair, delivery of substitute goods or services, price reduction and damages will reestablish the contractual equilibrium.

¹⁸ The contractual terminology is not consequent. In CISG, the term “avoidance” is used, while other international sets of rules – e.g. Unidroit Principles or PECL (Principles of European Contract Law) – use the term “termination” for the same purpose. I will use the term “termination” in this article.

¹⁹ Cf. art. 75 CISG.

²⁰ Cf. art. 81 CISG and art. 7.3.5 Unidroit Principles.

²¹ See e.g. art. 25 CISG, art. 7.3.1 Unidroit Principles and art. 8:103 PECL.

In public procurement, contracts are almost always drafted by the contracting authority. Therefore, the drafter may – shall – ask itself when a possible non-performance would lead to the choice to not purchase at all, primarily at any price. Only then, does the contracting authority need the right to terminate the contract.

7 Qualification and evaluation

The distinction between fundamental and other non-performances corresponds in part to the distinction between criteria for qualitative selection and criteria for awarding the contract. The former are absolute – if not fulfilled, the supplier will not stand a chance – while the latter reflect an evaluation of the criteria: The contracting authority is willing to accept e.g. a lower quality, a longer delivery time or a lower service level, if that is reflected in the price or in some other aspect of the offer benefits the contracting authority.

8 Selection of suppliers

8.1 Selection of suppliers and termination of the contract

A selection of suppliers – or rather the decision to exclude a supplier – corresponds to the termination of a contract. From the supplier's point of view, it hardly matters whether it is not selected at all or if it is thrown out at a later stage. In both cases, it will not be allowed to perform. If anything, it is better for the supplier to be excluded at an early stage, since it may then be able to focus on other businesses.

From the contracting authority's point of view, the effect of excluding a supplier or of selecting it and then terminating the contract, is basically the same: At the end of the day, that supplier will not be allowed to perform. Since the effect is the same, the criteria should also be the same. Contracts need only be terminated when the contracting authority would not have purchased – not at any price – if it at the time of the conclusion of the contract had been aware of the future non-performance. Consequently, criteria for the selection of suppliers should be limited in a corresponding way. When defining criteria for the selection of suppliers, the contracting authority shall ask itself if non-compliance with the criteria shall lead to the choice to not purchase at all, primarily at any price. Only then, is it beneficial to the contracting authority to use the criteria. In all other situations, the exclusion of a supplier may be a waste of money.

8.2 Mandatory criteria – taxes and corresponding issues

More than anything else, the selection criteria that relate to public obligations – payment of taxes etc. – can be described as “hygiene factors” in public procurement. They do not primarily relate to the relationship between the contracting authority and its suppliers, but rather to the relationship between society as such and the entire body of suppliers. Therefore, such requirements are mandatory: A supplier shall be excluded, if it does not comply with the criteria.²²

8.3 Non-mandatory criteria

While criteria that are for the benefit of society as such, rather than of the contracting authority, are mandatory, other criteria are not mandatory. They apply only when the contracting authority chooses to include them in a procurement. While the contracting authority according to chapter 10 § 1 LOU “shall” exclude a supplier, it “may” according to other regulations create grounds for the exclusion of a supplier, but it may also abstain from creating such grounds. Two examples may illustrate this.

8.3.1 *Technical and professional capacity*

According to chapter 11 § 10 LOU, a contracting authority *shall* assess a supplier’s technical and professional capacity. However, this applies *only if the contracting authority has requested proof of such capacity*.²³ If – but only if – such proof has been requested, shall the capacity be proved in accordance with chapter 11 § 11 LOU.

8.3.2 *Sub-suppliers and outsourcing of obligations*

Chapter 11 § 12 LOU applies when a supplier *relies* on the capacity of other entities.²⁴ In practice, the rule only needs to be applied *when the contracting authority has requested proof of capacity*.²⁵ If no such proof is requested, there is no reason for a supplier to state that it relies on another entity’s capacity.

The specific mentioning of reliance on other entities may possibly be explained by the relatively common misunderstanding that a contracting party can outsource not only the performance of an obligation to others – which in itself is no problem – but also the obligation as such. In most – if not all – jurisdictions, that is a misunderstanding. Rights may as a rule be transferred to others without the promisor’s consent. Obligations, on the other hand, may not be transferred.²⁶

²² See chapter 10 § 1 LOU, cf. art. 45 dir. 2004/18/EC and art. 57 dir. 2014/24/EU.

²³ Cf. art. 44 (2) dir. 2004/18/EC and art. 58 dir. 2014/24/EU.

²⁴ Cf. art. 47 (2) dir. 2004/18/EC and art. 63 dir. 2014/24/EU.

²⁵ Cf. chapter 11 § 10 LOU.

²⁶ Cf. e.g. art. 9.2.3 Unidroit Principles.

8.4 When is the important important?

The selection of suppliers has one major – and many minor – drawback. The major drawback is that it is based on historical facts. At best, it will therefore only provide the contracting authority with a forecast of the supplier's future performance if it is selected. As all forecasts, it may be wrong.

The question whether historical facts are more important than the actual performance is easy to answer: Of course historical facts are of no importance whatsoever, if the performance happens to be perfect. Therefore, it would be better if “selection criteria” – if at all – focused on the actual performance rather than on the history of the supplier. That causes a problem, since it cannot be done as a matter of selection. It can only be done with the aid of contractual terms, since the contract focuses on the actual performance of the supplier's obligations.

8.5 Let the suppliers select or exclude themselves

In almost all situations, the contracting authority writes the contract. If the terms were not set already from the start, the suppliers would not be competing for the contract on equal terms. Instead, they would each suggest their own terms, with different divisions of both values and risks. That would not be a fair competition and, therefore, not conform to the principles underlying the public procurement regulations, primarily the principle of transparency.

8.5.1 “Selection” through contract terms

Contracting authorities have a golden situation. They can monopolize the drafting of contracts. They can in any given situation, before they actually buy, decide the terms on which they are willing to buy. If the time of performance is important, they may select contractual remedies that reflect that importance. If quality is important, they may describe that quality in an appropriate manner – without having to haggle with suppliers' contradicting views on what they want to deliver – and set remedies for non-performances. And on and on. In short: Contracting authorities have the opportunity to draft contracts that are perfectly fitted for their needs. And no one can interfere.

With the use of contract terms, a contracting authority can eliminate most – if not all – of the selection process. In most contracts, technical and professional capacity, use of sub-suppliers and other common selection criteria are of no real importance. Instead, the outcome of the contract – the result – is what matters.

If the contracting authority describes its needs in an appropriate manner and selects remedies for non-performance that reflect those needs, it creates a situation where suppliers that would be excluded in a “normal” selection process must ask themselves what would happen if they were awarded the contract: “We

don't have the capacity to perform. God forbid that we win! Let's not submit any offer." With appropriate definitions of the supplier's obligations and appropriate remedies, the selection will take care of itself.

8.5.2 *Don't ask!*

The use of contract terms instead of selection criteria shifts the procurement's focus. Today, it is common that contracting authorities don't dare to believe that suppliers will actually be able to perform. Therefore, contracting authorities ask if the suppliers have the technical, personal and financial ability to actually perform, if they need other entities resources to perform and – if so – if they have contracts with those entities etc. And once the contracting authority has asked, it is stuck with the regulations of the selection of suppliers.

With appropriate remedies for non-performances, such controls are unnecessary. The suppliers will assess their abilities and submit offers if they believe that they will be able to perform. Therefore, a contracting authority shall as a rule not ask if a supplier *is able* to perform or *how* it will perform. It shall only ask *if the supplier will perform*. Once the obligation to perform is established, the how and the ability is strictly the supplier's responsibility.

8.5.3 *The non-use of remedies*

It is common that purchasers don't use the remedies that they are entitled to. Outside of the scope of public procurement, that may be bad economy, but it is not a legal problem. In public procurement, a legal aspect is added: Does the non-use of remedies constitute a new contract and – if that is so – may that contract be procured without the formalities stated in public procurement legislation?

The distinction between changed contracts and new contracts does not make much sense. In contract law, it is of no importance, unless parties in a contract have attached certain importance to it. But for what it is worth, there is no such thing as a changed contract. Instead, the parties agree – in a new contract – to exchange – or substitute – the old contract for the new.

For the purpose of public procurement law, the reasoning must be the same: A changed contract is a new contract. As soon as another supplier would have submitted its offer on different terms – primarily at a lower price – or for that matter submitted an offer at all, if it had known that there in fact were no remedies for non-performances, the formalities should have been used. Changes – or rather exchanges – may only be allowed, when there would be no such effect. And to not use ones contracted rights is definitely a change of an existing contract, or rather an exchange of the old contract for a new.²⁷

²⁷ See e.g. art. 4.3 (c) Unidroit Principles.

8.5.4 *The use of remedies*

The use of contractual remedies instead of a “normal” selection requires that suppliers believe that the remedies will be used. That may not be the case the first times around. The fact that available remedies have not been used, creates a pedagogical problem. It is, however, easy to solve, even if it takes some time: Just start using the available remedies! That will probably cause a bankruptcy or a few before the suppliers catch on. That may be sad, but it is in my opinion a very low price to pay for a more efficient use of public money.

8.6 Do not exclude any suppliers

If all important aspects of a contract are adequately reflected in it, there is no need to select – or rather exclude – suppliers. One may as well evaluate the offers of all suppliers. That will increase competition: A greater number of offers will be evaluated. If basic market economy theory is correct – and the assumption that it is, is the foundation of public procurement as such, so we better believe it – that will lead to either a higher quality (in a broad sense) or a lower price. As a bonus, there will be less work for the contracting authorities and the suppliers and – since there will not be much to complain about regarding the selection – the courts. That can’t be bad.

9 Evaluation of offers

In public procurement law, the selection of suppliers is separated from the evaluation of offers. They may not be mixed. From a contractual point of view, on the other hand, there is no reason to make any distinction between the selection process – if any – and the evaluation of offers, at least not to the extent that selection criteria have been made into contractual terms. The only difference would be that the non-performance of such obligations by definition shall result in a right to terminate the contract, while the non-performance of other obligations may lead to less dramatic effects.

9.1 Evaluation criteria

There are two distinct evaluation criteria. Offers may be chosen either based on price (the lowest price wins) or based on which offer is the economically most advantageous to the contracting authority. Since the latter specifically states that only *economic advantages* may be evaluated – as opposed to advantages *in general* – it is hard to see how there could possibly be any difference between the two. In practice, however, courts seem to allow possible advantages that are relatively far from economical. That practice is not supported by the legislation.

9.1.1 *The object of the contract and other performance obligations*

If you want champagne and state in a contract that you want it, you can be sure that one of two things will happen: Either champagne will be delivered, or the supplier will be in breach of contract. There are no other alternatives. If you, however, only state that you want sparkling wine – even though you want champagne – there is no support in the contract for your wish to receive champagne. In that situation, you will have to either use selection criteria (the supplier must produce the wine in the district of Champagne) – or evaluate the quality so that wine from Champagne allows a higher price. The selection criteria is at best legally shaky and may be challenged in court. And it is absolutely questionable if the evaluative preference for champagne is a correct reflection of the criteria “economically most advantageous”. That is, however, not the point. The point is that if you say that you want champagne, both the selection process and the evaluation of quality are unnecessary. And you will most probably not have to wait for your champagne while the courts decide if you have procured it correctly.

9.1.2 *The remedies for non-performance*

Remedies for non-performance divide risks between the parties. They are always to a greater or lesser extent supplemented by the underlying contractual legislation. In e.g. most international purchases of goods, that underlying legislation is CISG.

The division of risks shall affect the price. If a major part of the risks is borne by the supplier – which increases the probability that the supplier will perform correctly – the price will be higher. And if most risks are borne by the buyer, the probability for a correct performance is lower.

9.1.3 *Lowest price or economically most advantageous?*

Since the price is a summary of all other terms of the contract, there is never – or at least hardly ever – any need to evaluate offers in any other way than to select the offer with the lowest price. The only situation when it would be preferable to use the other criteria is when the terms of the contract do not reflect the needs of the contracting authority. But then, there is something very wrong with the proposed contract terms.

It is often argued that the evaluation criteria “economically most advantageous” is superior to “the lowest price”. The argument is based on the assumption that “the lowest price” automatically corresponds to “the lowest quality”. Nothing could be more wrong. Persons who argue that, do not understand the simple correspondence between the price and all other parts of a contract. The argument disregards the fact that a contracting authority not only may, but shall, define what it wants to purchase. Maybe more than anything else, that includes the

quality wanted by the contracting authority. Once that is done, a contract shall entitle the contracting authority to a delivery of i.a. the quality described in the contract. Champagne, anyone?

10 Buy what you need and select appropriate remedies for non-performance

The simple fact that the price reflects all other aspects of a contract does not only mean that the price will be “right” if the object is appropriately described and the remedies also are appropriate. It will also mean that the price will be *too high*, if the contracting authority has asked for a higher quality than needed, an earlier performance than needed, a higher service level than needed etc. and has required more dramatic remedies than needed. All such – unnecessary – additions to the supplier’s risk will – without adding any corresponding value to the contracting authority – be reflected in a higher price.

11 Simple suggestions for public procurements

This article boils down to five simple suggestions for public procurements.

11.1 Selection and exclusion of suppliers

Don’t select or exclude suppliers. Let them select or exclude themselves. They know their business much better than you do. As a consequence, they also know much better than you whether or not they have e.g. the capacity to perform. If they promise to perform, it is assumable that they can.

The benefits are obvious: The contracting authority does not have to deal with selection criteria, or for that matter with selections at all. And the suppliers don’t have to deal with them. It is highly likely that that fact in itself will increase the amount of offers. To some purchasers, many offers mean more work. But if the rest of the process is easily manageable, that is not much of a problem. More important is the simple fact that more offers mean more competition.

A simpler process for tendering with less formalities is also likely to attract smaller – primarily local – enterprises. That is not in any way contrary to the law. And it will make local politicians happy.

Many cases in court are about selection criteria. Without such criteria – or at least when they have been reduced to a minimum – the amount of cases will diminish. That is at least highly likely. That will save time and money for everybody involved, primarily contracting authorities, suppliers and courts. And with less cases, there will be more contracts that will be performed when they

were meant to be performed. That certainly benefits the users of whatever was purchased.

11.2 The object of the contract and other performance obligations

If you don't know what you want – don't buy. Do your homework and wait until you know what you want. Then state that, and let the suppliers offer their best solution to your needs. If these simple rules are not followed, it is pure luck if the performance corresponds to what the contracting authority needs.

The contracting authority shall also describe all other obligations that it wants to place on the supplier. Once the contract is concluded, it cannot – and to at least a great extent may not – add new requests.

In short: Contracting authorities shall let the contract's description of the obligations of the supplier paint a picture of what it wants to happen. If it accomplishes that, chances are that the contract will actually work well.

11.3 The remedies for non-performance

Those chances will increase tremendously if the picture is supported by appropriate remedies for the non-performance of the obligations. Whatever is important to the contracting authority, must be made important to the supplier. The use of contractual remedies is the most efficient way to communicate to the suppliers what the contracting authority thinks is important (and for that matter what it considers to be less important).

From a legal point of view, it does not matter if the remedies are unbalanced in favor of either party, primarily the contracting authority. The risk that they will be adjusted by a court shall not be exaggerated.

However, there is also money involved. From an economic point of view, it does not make any sense to buy something better than what one needs and to place risks at the other party that do not correspond to an equivalent value to oneself. Therefore, a contracting authority shall strive for contractual terms that are balanced, i.e. that correctly reflects its needs.

11.4 Lowest price

A contract's price is a summary of all other parts of the contract. Therefore, an offer's price is a summary of all other parts of the offer. If the contracting authority has done its job when preparing the contract, the offer's only addition shall be a price. In all other respects, all offers shall be equal. Therefore, there is no reason to evaluate anything but the price.

Again, the benefits are obvious. More or less strange criteria for the evaluation of offers give incentives for "tactical pricing", where criteria that do not reflect

reality will be over- or underpriced in offers and corrupt the evaluation. More important, however, is that such criteria tend to be challenged in court. That takes time and money away from all involved parties, including the courts. The evaluation criteria “lowest price” is totally transparent. That will greatly limit the amount of court cases regarding the evaluation of offers.

11.5 Use your rights

A chain is not stronger than its weakest link. In public procurement – as in any procurement – one possibly weak link is the follow up of contracts. It is not uncommon that contracts are not used the way they should be used. Once they have been concluded, they are filed deep in a drawer and never looked upon again. Instead, businesses are conducted in a more or less false assumption that they reflect the contract’s terms. In particular, this is often true for remedies. Quite often, purchasing authorities – just like other purchasers – do not use the remedies that are available to them. They are at best saved for a rainier day.

The pedagogical effect of this is devastating to purchasing authorities and, therefore, to public procurement as such. Suppliers learn that they don’t have to bother with remedies when they set the price of their offers. Inappropriate suppliers – i.e. suppliers that would not pass a selection process – will submit offers. And they will sometimes win, since their cost for quality is lower than the corresponding cost for suppliers that would pass the process. For a contracting authority, it is, therefore, crucial that it imposes all available remedies on suppliers who do not perform. Always.

12 Final words

This does not always work. There are rare procurement situations that do not fit into this pattern. One such situation is when it actually is prudent to purchase even when the contracting authority does not know what it wants. Another is when the supplier’s person – rather than the result of its delivery – actually is important.

However, such situations are relatively rare. It is almost always both possible and advisable for a contracting authority to actually describe what it wants and on what terms it wants it. For a contracting authority that does so, that chooses to move its focus from the purchasing as such – with selection and evaluations criteria and formalities – to the actual performance of a contract, there is a bright light at the end of the tunnel: The purchasing will be easier and the contracts will to a greater extent be correctly performed. There is no doubt in my mind that a shift of focus *from procurement to performance* will add tremendous value to any contracting authority.