

WHITEPAPER 2020

LOW TENDERS

1 INTRODUCTION

- 1.1 The topic of this talk is Low Tenders: The question the Whitepaper has asked me to address is: “If you know a tender is low because of a previous experience and have written to the tenderer but to no avail, how do you disqualify because of price.
- 1.2 This question is concerned with quite a nuclear option at a particular stage in the procurement process: actually rejecting a tender during evaluation stage for being too low. This tenderer may have passed qualification and selection stages with flying colours; it may in fact be the highest scoring bidder on both price and quality, but the price rings alarm bells. This raises quite challenging issues: Firstly, do you have to set a test in advance so that you can **spot** an abnormally low tender? Secondly, if you do spot an abnormally low tender, do you **have to** investigate it? Lastly, what questions should you ask and what do you do with the information you get back?
- 1.3 Notably there is no definition of what “abnormally low” means in our legislation. One of the original reasons for the requirement to check apparently low tenders prior to rejection was of course to build the common market, to prevent discrimination against suppliers from other member states who might genuinely have lower overheads or costs. With the advent of the 2014 Directive and surrounding guidance, the purpose does seem to have evolved to include the benefits of ensuring that the bid is economically, technically and legally sound.
- 1.4 I will be suggesting that it is at least good practice to have pre-defined measures of when an apparently low tender should be investigated, and that authorities should investigate suspect tenders to ensure that they are economically, technically and legally sound. This view is not on all four corners with the case law in England and Wales, so I will be explaining my reasoning for it.
- 1.5 I will be referencing the inherent risk in rejecting a tender *merely* because it has a low price, providing the tender is compliant with applicable laws, meets the specification, and has addressed costings accurately.
- 1.6 I will be concluding that the state of the law on Regulation 69 is to be treated with some caution, and a better tool to ensure inherent economic sustainability of bids is to build in evaluation criteria and evaluation models which cannot be gamed and which guard against overly aggressive pricing.

2 QUESTION 1: THE EXTENT OF THE OBLIGATION TO IDENTIFY AND INVESTIGATE A TENDER WHICH APPEARS TO BE ABNORMALLY LOW

- 2.1 The current legal position in England and Wales is that there is **only** a duty to investigate an abnormally low tender where you intend to reject the tender on the basis that it is abnormally low. This is the conclusion reached by the Court in a case called *SRCL Limited v NHS England*¹. In this case the Court held that there is a duty to investigate abnormally low tenders, but **only** where you intend to reject the tender on the basis that it is abnormally low, not a general duty to investigate abnormally low tenders to check that they are sound.
- 2.2 The SRCL case involved a reverse auction run by NHSE for clinical waste collection services. SRCL was the incumbent provider and argued that NHSE should have investigated the price submitted by Healthcare Environmental Services on the basis that the price was so low as to indicate that the waste could not be collected in a clinically safe or compliant way. The Court rejected that submission and held that there is no general duty to investigate an apparently low tender – the Judge (Mr Justice Fraser) said that to impose such a duty would be too onerous a burden on public bodies. In short, it was up to contracting authorities to decide whether they wanted to investigate. A **duty** to investigate only arose where the contracting authority was intending to reject a tender for being abnormally low.

¹ [2018] EWHC 1985 (TCC)

2.3 I would argue that there is room for a different interpretation of when a duty to investigate an abnormally low tender arises. This is for four reasons:

- 2.3.1 the wording in the applicable Regulation,
- 2.3.2 the recitals to the 2014 Directive²,
- 2.3.3 the views of Professor Arrowsmith; and
- 2.3.4 guidance which suggests it is good practice to do so.

2.4 **The applicable Regulation:** The applicable Regulation regarding abnormally low tenders is Regulation 69 of the Public Contracts Regulations 2015. This provides as follows:

“Abnormally low tenders

*69. – (1) Contracting authorities **shall** require tenderers to explain the price or costs proposed in the tender **where tenders appear to be abnormally low** in relation to the works, supplies or services.”*

2.5 I would emphasise in particular that the wording states that contracting authorities **shall** require tenderers to explain their price, not “may” or “have a discretion to”, but “shall”. Elsewhere in the 2014 Directive and Regulations, we see that “shall” is synonymous with “must”. For example:

- 2.5.1 A contracting authority “shall” base the award of contracts on the most economically advantageous tender (Regulation 67(1)).
- 2.5.2 A contracting authority “shall” specify the weightings for criteria (Regulation 67(9)).

2.6 These are widely understood to be fundamental mandatory obligations; why then does “shall” suddenly become less mandatory in Regulation 69?

2.7 Indeed, further down in Regulation 69 itself a contracting authority “shall” reject a tender where the investigation establishes that the tender is legally non-compliant. In *SRCL* Mr Justice Fraser recognised that this duty is mandatory³. So it would seem that “shall investigate where the tender appears to be abnormally low” should be mandatory too.

2.8 In terms of the intention behind the provisions, the wording of the 2015 Regulations is notably different to the wording of the 2006 Regulations which stated as follows:

“30(6) – If an offer for a public contract is abnormally low the Contracting Authority may reject that offer but only if it has -

- (a) Requested in writing an explanation of the offer or of those parts which it considers contribute to the offer being abnormally low;*
- (b) Taken account of the evidence provided in response to a request in writing; and*
- (c) Subsequently verified the offer or parts of the offer being abnormally low with the economic operator”.*

2.9 So the duty to investigate was very much tied to potential rejection in the 2006 Regulations. The 2015 Regulations state instead that contracting authorities shall require tenderers to explain the price or costs where tenders appear to be abnormally low, without that being tied to proposed rejection of the bid. Why do we have this different structure? For that it is instructive to look at the Recitals to the 2014 Directive which the 2015 Regulations implemented. Recital 103 provides that: “*Tenders that appear abnormally low in relation to the works, supplies or services might be based on technically, economically or legally unsound assumptions or practices. Where the tenderer cannot provide a*

² 2014/24/EU

³ [190]

sufficient explanation, the contracting authority should be entitled to reject the tender” – and it goes on to say when rejection should be mandatory if the low price results from non-compliance with law.

- 2.10 In *SRCL* Mr Justice Fraser did consider but was not persuaded by the changes in the wording between the 2006 and 2015 Regulations. He also considered but was not persuaded by the views of Professor Arrowsmith who prefers the interpretation that there is a general duty to investigate abnormally low tenders based on European case law which she describes the 2014 Directive as codifying⁴. Professor Arrowsmith considers that it is this interpretation which is best supported by the wording of the Directive and its recitals⁵.
- 2.11 However, Mr Justice Fraser preferred the conclusion reached by Mr Justice Flaux in *Varney*⁶ that an authority is not under a general duty to investigate “suspect” tenders.
- 2.12 Interestingly he does equate the duty to ensure that the bid is economically sustainable with the duty to award to the most economically advantageous tender under Regulation 67. I will return later to the theme of using the evaluation criteria to check sustainability rather than the mechanism in Regulation 69 itself, which is perhaps a more practical approach.

3 THE IMPORTANCE OF MODELLING

- 3.1 In terms of guidance, in February 2019 the Cabinet Office published the “Outsourcing Playbook” and updated it again recently in June 2020. The Outsourcing Playbook focusses on how central government works with private companies, and specifically how to avoid a similar situation to the collapse of Carillion. The Outsourcing Playbook applies to all outsourced services (but not works or supplies), with additional requirements applicable to complex outsourced services.
- 3.2 That is what the Outsourcing Playbook says: “Where a bid appears to be abnormally low, the department must require the bidder to explain their proposed price”⁷.
- 3.3 To identify what is likely to be an unsustainable bid, the Outsourcing Playbook recommends producing a “Should Cost Model” or “Expected Market Cost” model at the start of a process, and this is mandatory for complex outsourced services. The Guidance states that by knowing what the expected market cost is, an authority can identify what is an apparently low tender and interrogate it.
- 3.4 The Guidance also warns against low cost bias and states that central government departments are required to refer any abnormally low bid that is 10% lower than the average of all bids or the Should Cost Model to a Continuous Commercial Improvement Team. So I referred earlier to the suggestion that contacting authorities pre-determine what triggers an investigation – this is an example of two such measures which could be pre-set in advance to trigger an investigation. But contracting authorities will need to give careful consideration to what is the right measure or measures and not fettering their discretion.
- 3.5 This percentage threshold anomaly method of determining what is abnormally low, is just one of a range of techniques identified by the European Commission in its guidance dated 24 July 2019⁸ on participation of third country bidders. Other techniques mentioned include arithmetical methods based on an assessment of the deviation of a tender from the average price of all tenders, or from a pre-determined benchmark.
- 3.6 So what is the legal position regarding whether or not all authorities should benchmark in this way at the start of a process? In *SRCL*, Mr Justice Fraser said that there is “no definition of what the words “abnormally low” mean⁹. He said that a contracting authority has a discretion as to what test it uses for identifying what may be an abnormally low tender and that an “anomaly threshold”, such as a

⁴ *SAG ELV Slovensko* [2012] ECR I-10873

⁵ 7-268: *The Law of Public and Utilities Procurement, Volume 1*, Third Ed.

⁶ *J Varney & Sons Waste Management Ltd –v- Hertfordshire County Council* [2010] EWHC 1404 (QB)

⁷ Page 20 of the Bid Evaluation Guidance Note published in June 2020.

⁸ https://ec.europa.eu/growth/content/new-guidance-participation-third-country-bidders-eu-procurement-market_en

⁹ Paragraph 204

comparison of the consistency with other tenders, is a perfectly permissible approach. He said that an authority should **not** be required to form its own free-standing view in advance of what would or could constitute abnormally low.

- 3.7 Based on central government guidance and what the European Commission says however, it would seem that considering what could constitute an abnormally low tender in advance of a procurement process is advisable. Careful consideration needs to be given to what would be a reliable indicator of that¹⁰.

4 WHAT FORM SHOULD AN INVESTIGATION INTO AN ABNORMALLY LOW TENDER TAKE?

- 4.1 Assuming that an authority does wish to investigate an apparently abnormally low tender, what questions should or can it ask? Whilst it is not an exhaustive list, regulation 69 is explicit that you **can** ask questions about the following:

4.1.1 Economics of the manufacturing process, of the services provided or of the construction method.

4.1.2 The technical solutions chosen or any exceptionally favourable conditions available to the tenderer for the supply of the products or services or for the execution of the work.

4.1.3 The originality of the work, supplies or services proposed by the tender

4.1.4 Compliance with applicable obligations in the field of environmental, social and labour law

4.1.5 Compliance with sub-contracting requirements including transparency and exclusion provisions

4.1.6 Whether or not the tenderer has obtained state aid.

- 4.2 **Are you able to ask other questions?** Regulation 69 does not **limit** the questions you can ask to these factors alone, so there may be other questions that you want to ask and could ask providing they are relevant and proportionate. If the purpose of the abnormally low tender provisions is to ensure that the tender is “sound” (which the recital to the Directive suggests the purpose includes) then it would seem permissible to ask the tenderer to confirm a range of questions.

- 4.3 **Are you able to ask for documentary evidence?** Regulation 69 refers to the bidder providing explanations, information and evidence. The European Commission guidance emphasises that the bidder should provide all the evidence necessary to provide a sufficient explanation, which may include detailed information accompanied by appropriate documentation on the production process, facilities, social conditions, certificates and environmental standards. So it would seem that the authority is entitled to ask the bidder to back up its explanation with evidence.

- 4.4 **Are you able to verify compliance with the terms of the tender?** The European Commission guidance goes on to say that the reasons provided by the bidder to justify the viability of the offer must comply with the terms of the initial tender¹¹, and that in this regard, contracting authorities should not limit themselves to requesting solemn declarations from the bidder that it intends to comply with those obligations. So it would seem that the authority is entitled to request evidence to verify compliance

¹⁰ In *Impresa Lombardini (joined cases C-285/99 and C-286/99)* the CJEU said an authority is required to seek an explanation in relation to abnormally low tenders (points 43 and 51), and that a mathematical criterion such as an anomaly threshold was permissible (although note Advocate General Ruiz-Jarabo Colomer, ECLI:EU:C:2001:314, paragraph 36 recognises that there is no one will know at the outset what that threshold will be).

¹¹ CFI, Case T-422/11, *Computer Resources International*, point 87

with the tender, and this overlaps with an authority's ability to verify that the tenderer has understood and can meet technical specifications under Regulation 67(7)¹².

- 4.5 **What questions might you ask?** You may wish to ask for a detailed explanation, with supporting evidence of the following, anticipating potential commercial sensitivity concerns by providing appropriate reassurances in advance:
- How did the bidder calculate the prices and costs overall? Is the calculation sound?
 - How did the bidder arrive at a specific price for a specific item?
 - Does the price allow for fulfilling all legal and contractual requirements (referring to any in particular that you are concerned about)?
 - Does the price allow for fulfilling all required labour and environmental standards (again raising any you are particularly concerned about)?
 - How is the tender financed?
 - Any other particular questions about the solution or deliverability that you are particularly concerned about in view of the price.
- 4.6 **What if the explanations raise further questions or are unclear?** Should you go back to the bidder? Providing an authority is acting in accordance with general principles, an authority is likely to have discretion to go back to the bidder to ask further questions if anything remains unclear, or if further questions emerge, and this is confirmed by the European Commission guidance. It is however less clear whether an authority has to ask for clarification or further information if the explanation is insufficient before rejecting or accepting the tender. Where the cause of the deficient explanation could be said to be attributable to fault on the part of the contracting authority (for example, the authority did not make clear what had to be provided) then it may be disproportionate to reject. Equally, there may be a risk that repeated communications with the tenderer amount to allowing it to improve its bid, which may be at risk of challenge from other bidders.
- 4.7 **Should you be concerned about asking whether the contract is profitable or makes a certain margin?** There is no explicit reason why you cannot ask this question – your purpose in asking it may be to ascertain whether the contract is inherently financially sustainable. Query however, what you do if the tenderer responds that it is deliberately buying the work at a loss in order to improve its market positioning. Does this mean that the tender is not economically sound and should be rejected? Does the price payable under the contract have to deliver a sustainable margin, or can you accept an explanation from a robust bidder who says it is prepared to subsidise this contract from other books of business.
- 4.8 Regulation 69(5) provides the contracting authority must reject the tender where it is abnormally low because it does not comply with social, environmental or labour laws, or where the tenderer is in receipt of incompatible state aid.
- 4.9 Other than that, the authority “may only reject the tender where the evidence supplied does not **satisfactorily account for** the low level of price or costs proposed, taking into account the elements referred to in paragraph (2)”. It is therefore not obvious from this what you should do if a tenderer is deliberately pricing low – given that it has passed economic and financial standing tests is this necessarily economically unsustainable?
- 4.10 Professor Arrowsmith suggests that there is no duty to reject in any situation other than those defined in Regulation 69(5) but she does go on to identify that it is possible to interpret the ruling in *SAG Elv-Slovensko*¹³ as imposing a duty to reject “when a tender presents an unacceptable risk of default”¹⁴.

¹² Of interest here is the judgment of the EFTA Court in *Fosen-Linjen I* - E-16/15

¹³ *SAG ELV Slovensko a.s. and others v Úrad pre verejné obstarávanie C-599/10*

¹⁴ [814].

- 4.11 Does not making a margin on the work necessarily mean that there is a risk of default? There is no explicit obligation for a tenderer to demonstrate that it will make a margin or profit on its bid, and providing it is lawful under the competition regime to do so, it may be open to a tenderer to undercut other bidders by “buying” work. Were a contracting authority to reject such a tender, there could be an argument (which would depend on the facts of the case) that to reject merely on the grounds of insufficient margin is unlawful, for example that it is disproportionate. Might there not be a risk of challenge in itself in an authority deciding what is or is not an acceptable margin for an operator to make?
- 4.12 In summary therefore, if there is evidence of non-compliance with certain laws, the authority must reject. Where the authority considers that the evidence supplied does not satisfactorily account for the low level of price or costs proposed, it has a discretion to reject, but any decision to reject therefore needs to be very carefully considered and documented in accordance with the principles of equal treatment, transparency, proportionality and non-discrimination. It may be advisable to try to avoid the use of one measure only to reject a bidder, and instead to carry out a more sophisticated assessment, consistent with previous guidelines on financial standing at SQ stage as well.

5 **GIVEN THE LACK OF CLARITY REGARDING THE ABNORMALLY LOW TENDER PROVISIONS, IS A BETTER APPROACH TO BUILD IN ECONOMIC SUSTAINABILITY AS PART OF THE EVALUATION CRITERIA INSTEAD?**

- 5.1 Methods of doing so would include:
- 5.1.1 A sufficiently high quality weighting so that emphasis is placed on deliverability, a high level of confidence in meeting the criteria and specification.
 - 5.1.2 Building in two stage assessments – having a quality threshold first and then competing on price alone.
 - 5.1.3 Identifying bids which offer the highest value and lowest delivery risk in the areas that are the most critical to successful delivery.
 - 5.1.4 Building in a formula for evaluation to guard against excessive pricing or aggressive pricing. The range of evaluation methodologies is vast, and formula exist which build in protection against aggressive pricing – in fact again this is an area which has attracted interest at previous Whitepaper conferences, and in a talk I gave a few years ago I covered some of the techniques available¹⁵.

6 **CONCLUSION**

- 6.1 To conclude this talk, the question asked by the Whitepaper was – when you know a tender is low because of previous experience, you write to the tenderer but “to no avail” – how do you disqualify because of price?
- 6.1.1 In summary, it would be good practice at least to consider in advance what measures you will use to identify what is an apparently abnormally low tender.
 - 6.1.2 If a bidder is apparently abnormally low, and if you get no answer at all, you are entitled to disqualify.
 - 6.1.3 If a bidder is apparently abnormally low and you establish that the tender is not compliant with applicable labour, environmental or social laws, you are **obliged** to reject the tender.
 - 6.1.4 If you establish that the tender does not meet your tender requirements, it may be unequal treatment to award to that bidder in any event.
 - 6.1.5 You are entitled to ask a wide range of questions and make request for supporting evidence. Plan this stage carefully and document it fully so that the decision you take is

transparent and proportionate – whilst you have discretion about what is “satisfactory” evidence from the supplier, you need to be mindful not to reject a sustainable tender simply because it is a low price without adequate justification.

- 6.2 Finally, if you do decide to reject a tender on the basis that it is an abnormally low, the careful audit trail you have prepared to document your decision making process will enable you to provide adequate and transparent reasons to the bidder affected for its rejection, and will also of course discharge your obligations to record any decision to reject in a Regulation 84 report.
- 6.3 The issue of economic sustainability therefore continues to be an important one, and whilst the abnormally low tender provisions create uncertainty, many contracting authorities are avoiding the problem through greater agility in use of innovative and sophisticated evaluation criteria and methodologies to ensure their procurement is fit for purpose.