McMillan Binch LLP

# Working On A Tight RFP Deadline? Don't Forget The Legal Niceties

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# WORKING ON A TIGHT RFP DEADLINE? DON'T FORGET THE LEGAL NICETIES[1]

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## 1. INTRODUCTION

The Request for Proposal ("RFP") is a critical part of any large, complex procurement. It serves as the foundation not only for receiving and evaluating bids, but also sets the framework for the ultimate relationship between the parties. [3]

Typically, both issuers and bidders work to tight RFP deadlines. While the business and technical details of any given procurement are often paramount, the legal niceties (discussed below) are important too. Those who ignore them in the scramble to meet an RFP deadline do so at their peril and often trip up along the way.

### A. OVERVIEW

This paper addresses the main legal aspects of RFP's and responses. It discusses the model of a competitive, fair and transparent RFP process and provides practical tips on how to engage effectively in proposal solicitation and preparation, including:

(a) understanding the role of lawyers and distinguishing it from the roles of others on the team of either the issuer or bidder;

(b) developing an effective solicitation, by consulting prospective bidders and preparing the RFP and pro forma contract in advance;

(c) evaluating the RFP opportunity and preparing a successful response;

(d) conducting due diligence (both issuer and bidders) and getting the most out of data rooms and information meetings;

(e) complying with or clarifying mandatory terms and conditions in the RFP;

(f) selecting the preferred bidder and negotiating the contract;

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[1] This paper is based on presentations first made at the Winning the Request for Proposal Process conference organized by Federated Press held in Toronto, Canada, from October 19-20, 1999. The information in this paper is general in nature and should not be relied on or regarded as a substitute for specific and complete legal advice. Readers seeking such advice should consult their legal advisors.

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[3] For the purposes of this paper, the party issuing the RFP will be referred to as the "issuer", the party responding to the RFP will be referred to as the "bidder", and the successful bidder will be referred to as the "vendor".

(g) allocating and managing risks;

(h) monitoring performance of the contract;

(i) resolving disputes through litigation and other less traditional means;

(j) ensuring effective indemnities and remedies; and

(k) protecting rights on termination of the contract, including transition provisions.

While the comments in this paper relate primarily to large, complex government procurements, many will also be applicable to less complex procurements by corporate and other non-governmental organizations.

## B. ROLE OF ISSUER'S LAWYER

Successful RFP's and responses are the product of the combined talent, time and effort of a variety of individuals who, although working as a team, often possess different skills and priorities.

The issuer's lawyer is most often consulted to:

(a) advise on and ensure fairness, independence and objectivity in the development of the appropriate procurement process;

(b) draft sections of the RFP relating to the procurement process and ensure that the overall document is a clear, precise and complete description of the procurement opportunity;

(c) prepare the draft pro forma contract that may be attached to the RFP or at least those sections in the RFP that describe the legal issues that will likely find their way into the final contract;

(d) assist in the analysis and designation of certain provisions in the RFP and pro forma contract as "mandatory" (i.e., provisions that must be unconditionally complied with by bidders and that are not open to negotiation);

(e) assist in the conduct of certain due diligence and, if a data room and information meetings are to be used, assist in the organization of such room and meetings; and

(f) once the successful bidder has been selected, assist in the negotiation and finalization of the contract.

## C. ROLE OF BIDDER'S LAWYER

The bidders counsel is usually retained to:

(a) help review the RFP and assist the bidder in preparing its bid;

(b) review the draft pro forma contract and identify any legal issues that need to be addressed in the bid (such as seeking clarification of mandatory terms and providing alternatives to negotiable terms);

(c) if due diligence is to be conducted, provide assistance in the data room and at information meetings;

(d) assist the bidder to structure arrangements with others on the bidder's team (e.g., subcontractors and consortium members) in order to develop and implement the legal framework under which the bid will be made to the issuer. This may involve the development of joint venture or corporate structures where the "bidder" is a combination of bidders and suppliers. These situations are common in large procurements where one company may not have all of the specialized skills in order to deliver a complete bid; and

(e) if the bidder is successful and selected to negotiate the contract, play a role in negotiating and finalizing the contract.

The role of lawyers in the procurement process should obviously be distinguished from the role of the policy makers, business persons, technical experts and other individuals who contribute their expertise and experience to preparing parts of the RFP. At times, government issuers retain "fairness advisors", who are often lawyers and whose job it is to ensure that the procurement process and any consultations with prospective bidders remain impartial and transparent.

## 2. DEVELOPING AN EFFECTIVE SOLICITATION

An effective solicitation starts with the issuer consulting prospective bidders and preparing the RFP and pro forma contract well in advance. Early consultation by the issuer will accomplish several objectives, including:

(a) confirming that there will be a sufficient number of qualified issuers for a competitive procurement;

(b) ensuring that bidders have sufficient information to make reliable proposals;

(c) minimizing the amount of risk premium or number of conditional bids from bidders due to a lack of clarity in the RFP;

(d) providing sufficient time for bidders to form joint ventures or other business arrangements to make a complete response to the RFP; and

(e) ensuring real and perceived fairness in the procurement process.

## A. INITIAL CONSULTATION OF PROSPECTIVE BIDDERS

The issuer typically has several options for consulting prospective bidders. In complex procurements, as a first step, it may be useful for the issuer to release an information document as part of a general consultation with prospective bidders.

Such a document usually sets out the background, objectives, business models, assumptions and scope of the proposed procurement and seeks answers from prospective bidders to a series of questions proposed by the issuer. The main purpose of such a preliminary consultation is to give information to assist bidders in providing constructive feedback to the issuer's project team.

## B. REQUEST FOR EXPRESSION OF INTEREST

As a second step, the issuer may prepare a Request for Expression of Interest ("EOI") to provide prospective bidders with further information on the procurement opportunity. The EOI can also serve as a means to exchange information with prospective bidders in order to assist the issuer in finalizing its business analysis.

An EOI is typically issued with the caveats that it does not contain all of the information a prospective bidder needs to provide a full response and that it is not to be construed as an RFP. Furthermore, responses to an EOI usually are not used by the issuer to qualify or evaluate potential bidders in any way or with respect to any potential subsequent procurement process. In most cases, information provided by the issuer or the bidder is not considered to constitute an implied or expressed commitment.

As with the initial consultation, the benefit of a clear EOI is that it helps the issuer to obtain further feedback directly from prospective bidders on the procurement opportunity and it enables the potential bidders to determine whether they have a serious interest in preparing a proposal in response.

## C. REQUEST FOR QUALIFICATION

A separate Request for Qualification ("RFQ") is usually issued together with background discussion papers, the draft RFP and the draft pro forma contract. In this way, the RFQ helps potential bidders understand even more fully the nature of the business opportunity presented by the procurement.

It is common for respondents to an RFQ to be required to provide a deposit which is refundable if the bidder responds to a subsequent RFP or if no RFP is released. This deposit helps ensure that only serious bidders participate. The specific qualifications of prospective bidders is a matter to be determined primarily by the business and technical members of the issuer's procurement team.

Specific questions are often asked by and of bidders. In order to avoid the risk of appearing overly influenced by one particular bidder, the issuer usually (but not always) conducts bidder's meetings to obtain ideas collectively from prospective bidders. The issuer would also be well advised to conduct one-on-one consultations with prospective bidders before

issuing the final RFP. Such consultations may be preferred since group meetings run the risk of getting less valuable comments because individual bidders may be reluctant to share ideas with competitors.

The draft pro forma contract attached to the draft RFQ should indicate which terms and conditions the issuer proposes to make mandatory, and which will be subject to clarification or negotiation with the preferred bidder. The draft RFP usually includes proposed bidder qualification, due diligence and evaluation criteria.

One of the main advantages of full and early consultation with prospective issuers is that information gaps can be eliminated at the outset thereby reducing any risk premium in a bid or any delays or costs associated with the submission of conditional bids. In short, the bidders will better understand the issuer's requirements and this will usually result in better bids and a shortened contract negotiation process.

## D. REQUEST FOR PROPOSAL

A well structured and well organized RFP ensures that the procurement process is clear, accurate and fair to all bidders. It also provides an efficient and effective tool for communicating to multiple potential suppliers all at one time. A well drafted RFP will answer many of the potential bidder's questions and reduce the amount of administrative time the issuer is required to devote to answering such questions.

The RFP provides the issuer with the opportunity to set the terms and conditions of not only the procurement process, but also the main terms and conditions of the resulting contract. The RFP often takes on the role, format and appearance of a check list of the main business and legal issues that will be addressed in the contract.

### a) RFP RESPONSE DELIVERY AND TIMING

An important part of any RFP is setting out the terms and conditions for the bid procedure. This includes the delivery requirements, such as the time for delivery of the response, the address for delivery, the number of copies, the language of the response and any other special delivery details.

One of the fundamental principles for any RFP is the requirement that the bid be submitted on or before a specified time. The RFP should contain an express provision that any bid delivered after that time is disqualified and will be returned unopened. The acceptance by the issuer of a bid that has missed the deadline is only likely to lead to a dispute and the issuer is well advised to avoid such a dispute by strictly adhering to its own rules in the RFP.

Many RFP's contain a provision that requires all materials that are being delivered in respect of a proposal to be delivered by the deadline in order to avoid bidders forwarding supplementary material for consideration after the deadline. In addition to being a source of potential disputes, the receipt of supplementary material also interferes with the timeliness of the procurement process, since the supplementary material would then have to be evaluated and that bid reassessed.

An RFP should also have a provision indicating how long a bidder's offer must remain outstanding for consideration by the issuer.

**b) TIMETABLE**

The RFP usually contains a timetable that the issuer hopes to follow in the procurement process. An example of such a timetable is as follows:

| Event | Date |
|---|---|
| Distribution of RFP | Day 1 |
| Opening of Data Room | Day 2 |
| Data Room Reviews Completed | Day 15 |
| Date for Submission of Written Questions | Day 20 |
| Responses to Written Questions | Day 25 |
| Briefing Meeting for Proponents | Day 30 |
| Submission of Proposals | Day 45 |
| Evaluation of Bids Completed | Day 80 |
| Recommendation to Issuer's Board | Day 85 |
| Announcement of Short-Listed Bidders | Day 88 |
| Site Visits for Short-Listed Bidders | Day 89 |
| Negotiation of Contract | Day 90 |
| Announcement of Successful Bidder | Day 120 |

**c) BID FORMAT**

The RFP should also specify the prescribed format for the response, such as whether the bid may be submitted electronically and, if large number of copies are required, the designation of a "master copy" which would be deemed to be the "official" bid proposal.
In designing the prescribed format for the response, the issuer should attempt to solicit bids that may be easily compared and evaluated.

### d) SPECIFIC RULES, RESTRICTIONS AND RESERVATIONS (E.G., PRIVILEGE CLAUSES)

Depending on the particular procurement, the RFP may have provisions that specify that no representation is made as to the accuracy or completeness of any data in the RFP and the bidder has the onus of verifying such data. The RFP also usually provides that the bidder is not entitled to compensation from the issuer for any time, effort or expense in preparing its bid. Furthermore, the issuer usually reserves its right:

(a) not to award the contract;

(b) not to award the contract necessarily to the lowest priced bidder (but rather to the bidder offering the "best value");

(c) to conduct negotiations with one or more bidders in the event the negotiations with the first bidder are unsuccessful;

(d) to conduct a survey of potential bidders to obtain clarification of their proposals as part of the evaluation process;

(e) to cancel and reissue the RFP; and

(f) to extend any deadlines and amend the procurement process.

While such clauses are typically stated quite broadly in RFP's, they do have limits. The Supreme Court of Canada has recently told those who issue tenders for construction work that the clause, "The lowest or any tender shall not necessarily be accepted", often called the "privilege clause", cannot be used by issuers to accept a non-compliant bid over compliant bids.[4]

### e) QUALIFICATIONS

The RFP always specifies the technical qualifications required of prospective bidders. It also commonly includes financial qualifications. A similar pre-qualification requirement, although less common, involves pre-qualification relating to the bidder's management capability.

Depending on the type of procurement and the goods and services to be supplied, there may also be regulatory qualifications. These could include requirements to hold certain licences (for example, to provide gaming services in the case of procurement by a casino) or that relate to safety and security clearances for the bidder's premises or personnel.

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[4] *M.J.B. Enterprises Ltd.* v. *Defence Construction (1951) Ltd.* (1999), 170 D.L.R. (4th) 577 (SCC).

#### f) CONSORTIUM AGREEMENTS

If it is anticipated that the bidder will be a consortium, the RFP typically requires an executed copy of the bidder's joint venture agreement. Such an agreement will specify the establishment and mandate of the consortium, how the business of the joint venture will be structured, managed and financed, and who will be the bidder's key contact with the issuer.

## 3. ISSUER DUE DILIGENCE

### A. OBJECTIVES AND TIMING

As part of evaluating the written proposal of each bidder, the issuer usually performs due diligence to ensure that the bidder can implement its proposal. The RFP should require bidders to provide certain information that permits the issuer to verify that bidders have the expertise and financial resources to successfully complete the procurement project. In addition, before accepting a proposal and beginning contract negotiations, the issuer may wish to conduct further enquiries, such as security and reference checks on key officers and directors.

### B. CONFIDENTIALITY OBLIGATIONS

The issuer and its advisors should undertake in a confidentiality agreement or in the RFP not to disclose confidential information about the bidders, except as required by law. In Ontario government procurements, this means that the issuer usually provides a short summary of the application of the *Freedom of Information and Protection of Privacy Act* (Ontario).

### C. CRITERIA

The following factors should be the key due diligence criteria:

(a) financial strength;

(b) relevant experience; and

(c) relevant expertise.

It may be possible to define certain minimum criteria, such as expertise with particular systems or compliance with financial tests. In addition to minimum criteria, the issuer may be able to provide a sense of which supplementary criteria it considers the most important. To the extent that the issuer is able to do this, such information should be provided to all prospective bidders.

#### a) FINANCIAL INFORMATION

Reliable financial information is critical for the issuer to determine if the bidder (i) is likely to continue as a viable entity for the proposed life span of the procurement project and (ii) has the financial resources to complete the project. There are several ways in which the

issuer could become satisfied with the financial ability of the bidder. What the issuer will need to do by way of due diligence will depend on the nature of each bidder.

Obviously, if the bidder is a Schedule I Canadian Bank there will be limited need, beyond possibly a review of the latest publicly available financial information, to determine whether the Bank has the financial strength to take on the procurement project.

However, if the bidder is a newly incorporated company established to make the bid, then it will be necessary to assess the financial strength of the shareholder or shareholders. It will also be necessary to have such shareholder or shareholders become a party to the RFP contract in some manner (e.g., by way of guarantee of the obligations of the new subsidiary) to ensure that someone with financial strength is supporting the contractual obligations the successful bidder will assume in the contract.

The issuer needs to be satisfied that the prospective bidder and their guarantors have the financial strength to make the capital and other investments necessary to perform the contract, as well as the financial strength to compensate the issuer in the event a compensation claim is ever made because of the failure of the successful bidder to perform its obligations under the procurement contract. This can be achieved through conducting due diligence and through ensuring that there are back-up sources of financial compensation, particularly where the prospective bidder does not have significant financial resources of its own.

Some examples of back-up sources of financial support include letters of credit from banks, performance bonds from bonding insurance companies or guarantees from third parties (such as shareholders) with significant financial resources. Letters of credit and performance bonds cost money and these costs will be factored into the pricing of a bid.

To the extent the issuer wants to conduct detailed due diligence relating to the financial strength of prospective bidders, it could ask for some or all of the following:

(a) the last five years of audited financial statements for the bidder;

(b) if a company or division does not produce audited financial statements because it is a new entity (e.g., special purpose subsidiary established to make the bid) or because it is consolidated in a larger corporation, then the RFP could require unaudited divisional or subsidiary financial statements, plus audited consolidated financial statements of the parent;

(c) if the bidder is a partnership, joint venture or corporate entity established to make the bid, it will be important to see the corporate ownership chart indicating the percentage ownership of voting and equity shares along the ownership chain including the ultimate parent corporation – a copy of the financial statements for last five years of the ultimate parent corporation may also be appropriate in these circumstances;

(d) amount of capital expenditures that the prospective bidder anticipates it will have to make to implement the project (during first five years) and a business plan on how it will raise such capital, if it needs to do so;

(e) if capital will be raised from external sources (whether directly or through shareholders), letters from relevant bankers, investment bankers, and financial institutions confirming the availability of such financing; and

(f) an indication of the approximate percentage of the bidder's personnel that will be dedicated to the project.

**b) RELEVANT EXPERIENCE**

The issuer may need evidence that the bidder has experience in providing the services required in the procurement project. The issuer should specify the areas of experience in which it is interested. These areas could include experience in change management, outsourcing, government contracts, and labour management. The bidder should also be asked to provide three examples of relevant experience, summarizing in each case the project and personnel involved.

**c) RELEVANT EXPERTISE**

The issuer may wish to verify that the bidder will be able to assign to the procurement project individuals possessing the relevant expertise, keeping in mind that there can never be a guarantee that the proposed staffing will not change. If so, the following documentation should be requested:

(a) resumes of the members of the relevant bidder's management team who will be assigned to the procurement project if the bid is successful; and

(b) an organizational chart with the names, addresses and job descriptions of each member of the procurement project management team and their superiors up to the President and directors of the key operating entity.

It may also be prudent to conduct security checks on key officers and directors, including bankruptcy, criminal record, and litigation.

Once bidders have been short-listed, the issuer should verify with former clients of each bidder the names of the bidder's employees who were involved in completing a particular project for that client. By doing so, the issuer can be sure that members of the bidder management team who will be assigned to the procurement project have the relevant expertise.

**d) RELATIONSHIP BETWEEN PRIME CONTRACTOR AND SUBCONTRACTORS**

The issuer will also want to have a clear understanding of the contractual relationships between the prime contractor and any subcontractors, as well as relevant information about the subcontractor's experience and expertise. Although the prime contractor will be primarily responsible to the issuer, the strength of the prime contractor's consortium will be an important evaluation criterion.

### e) ABSENCE OF CONFLICT OF INTEREST OR UNFAIR ADVANTAGE

It is impossible to ensure with absolute certainty that a bidder does not have a conflict of interest or unfair advantage, or has not conducted inappropriate activity in connection with the bid. However, requiring a certificate under oath from a senior officer of the bidder causes the bidder to focus its mind on the issue and is a relatively easy way to do some due diligence on this issue. It also has the effect of emphasizing the importance which the issuer gives to the integrity of the bidding process.

Ontario government RFP's, for example, typically require that bidders:

(a) declare that they are not, and will not be in a conflict of interest; and

(b) do not have access to confidential information which would give them an unfair advantage or prejudice the Crown.

Bidders must provide the government, as issuer, with a list of the names of any individuals on the bidder's team who have worked for the Ontario public service (the "OPS"), together with the job classification and names of the particular ministry where each of these employees worked immediately prior to leaving the OPS.

The RFP should make it clear that if the issuer determines that the representations relating to appropriate conduct are untrue, it is grounds for the issuer to immediately disqualify the bidder from further negotiations.

### f) DUE DILIGENCE AFTER BIDDERS SHORT-LISTED

It is the interest of both the issuer and prospective bidders for the issuer to do as much due diligence as possible through the responses to the RFP. This keeps everyone on a level playing field to the greatest extent possible. However, in the same way that short-listed bidders may wish to supplement their due diligence with site visits or computer testing, so too may the issuer wish to do the same with respect to the short-listed bidders.

The issuer may wish to conduct some site visits or computer testing of the short-listed bidders' operations in order to give the issuer some additional comfort that its evaluation process did not result in any major gap. Such due diligence could also be helpful in building a common base of knowledge for the purposes of completing negotiations of the contract. In the event a contract is not successfully reached with the first successful bidder and negotiations then commence with a subsequent bidder, so long as that subsequent bidder is subjected to the same enquiries, the integrity of the issuer's due diligence process would be maintained.

## 4. EVALUATING THE RFP OPPORTUNITY AND PREPARING A SUCCESSFUL RESPONSE

### A. READ RFP CAREFULLY

While the observation is trite, in order to best evaluate a procurement opportunity, the specific RFP documentation must be read over and over again. It should also be reviewed in detail by the project team established by the bidder and its professional advisors.

An important part of evaluating the opportunity is bidder due diligence. The RFP usually has a communications section dealing with the process under which bidders can make enquiries. Typically, the RFP establishes a single point of contact as well as a process for dealing with responses so that each of the bidders has access to all of the responses that have been given to enquiries made. The ability of all potential bidders to receive and review the information is critical in that no one bidder should have an advantage having received specific information that was not available to the other bidders. This helps ensure a level playing field and to avoid potential complaints and disputes about the procurement process.

### B. ADHERE TO COMMUNICATIONS REQUIREMENTS

Another important component of the communication section of the RFP, particularly in highly sensitive government procurements, is the restriction that failure to adhere to the communications requirement is grounds for disqualification of the bidder. Such a provision usually specifies who may be contacted and who may not be contacted, and includes automatic disqualification upon contacting anyone about the RFP other than the specified contracting officers.

### C. MAKE PROPRIETARY ENQUIRIES

RFPs of a technical nature sometimes include an enquiry procedure that allows the bidder to specify its enquiry as “proprietary” versus “non-proprietary”. Proprietary enquiries are used when the nature of the bidder’s question is such that the bidder feels that it would not be appropriate to disclose its question (and possibly the issuer’s response) to its competing bidders, as this might put the bidder at a competitive disadvantage or require it to disclose proprietary or confidential information which would not be appropriate for competing bidders to see. These provisions permit the issuer to reject the status of the question as “proprietary” and provide the bidder the opportunity to withdraw its question, if it does not wish to proceed with the inquiry on a non-proprietary basis.

### D. ATTEND BIDDER INFORMATION MEETINGS

A bidder information meeting is an efficient way for the issuer to exchange information with all bidders. It also provides an opportunity for bidders to obtain additional clarification or information for preparing their response. In addition to the basic information of the time and place of such a meeting, the RFP may also specify the process for submitting questions to be answered at the meeting in order to help the issuer ensure that the appropriate persons are available to answer the questions. As well, the RFP should specify whether the information session is mandatory or optional. The RFP may also specify the number of

individuals from each bidder that can be in attendance and the process for notification of who will be attending. This may be helpful where there are a large number of bidders and capacity and time constraints exist.

## 5. BIDDER DUE DILIGENCE

### A. OBJECTIVES

The ultimate goal of the bidder's due diligence is to enable it to decide whether or not to bid on the procurement opportunity, and on what terms. Prospective bidders may wish to carry out due diligence to assist them in determining the value of the proposed transaction, identifying the issues that need to be addressed in the negotiation of the definitive agreement, and developing positions for negotiation of the definitive agreement. Well organized due diligence materials should give the prospective bidder confidence that it can appropriately cost and price the project and that the issuer is well organized with respect to the procurement project.

A due diligence process imposes an onus on the bidder to "satisfy itself" in respect of the information made available to it. In the absence of any contractual terms, the onus on the issuer will be to provide all relevant information and take steps to be satisfied that the information which is made available in the data room is generally accurate or true.

### B. USING REPRESENTATIONS AND WARRANTIES

Permitting a bidder to "satisfy itself", which is implicit in the due diligence process, is to be contrasted with relying on issuer representations and warranties in the procurement agreement.

A representation and warranty is a statement made by a party to a contract that a certain fact, circumstance or event is accurately represented in the contract (e.g., the issuer owns the assets proposed to be transferred and has the right to sell them free of encumbrances). If the issuer is giving the representation and warranty (i.e., making the statement on the basis that it is true and can be relied upon as being true), the onus shifts to the issuer to ensure its accuracy and truth.

It is common for the issuer to attempt to limit the extent to which it will give representations and warranties. This has the desired objective of "shifting the risk" to the bidder, but it comes at a cost. The additional risk being transferred to the bidders requires the bidders to be more careful and thorough in their due diligence and factor into their pricing a contingency for the "unknown". While shifting the risk to the other contracting party may be appropriate in some commercial relationships (e.g., the sale of a piece of equipment or property on a "as is/where is" basis) it may not be appropriate where the commercial relationship is more complex (such as where it involves a significant amount of business process integration).

In considering the extent to which the issuer should give representations and warranties, a distinction should be made between representations and warranties of a factual nature and those of a qualitative nature. For example, it is usually not onerous for the issuer to represent and warrant that:

(a) the assets to be transferred to the bidder are as set out in the list appended to the RFP;

(b) the employees to be transferred to the bidder are as set out in the list appended to the RFP; or

(c) the contracts to be assumed by the bidder are as set out in the list appended to the RFP.

These are factual representations which are relatively easy to give and are normally given in a commercial contract.

It is more difficult for the issuer to give representations and warranties that require an evaluation or judgement. For example:

(a) all of the contracts being transferred are in good standing and neither party thereto is in default, and there is no event or circumstance which has occurred which would result in such contracts being in default;

(b) the assets are in good operating condition and fit for the purpose for which they are intended to be used, reasonable wear and tear excepted; or

(c) the employees being transferred are the only employees the bidder will need to perform the contract.

These representations and warranties are typically "negotiated" in that the party giving the representation will try to qualify them or limit them and the party who is the recipient of the representation will try to keep them as broad and unqualified as reasonably possible.

The more judgement or evaluation which goes into the representation, the more risk of liability if the judgement or evaluation is wrong. There are ways to mitigate such risk by:

(a) not giving such representations;

(b) making such judgement representations subject to qualifications such as "to the issuer's knowledge after reasonable inquiry"; and

(c) limiting the period of time that the issuer would be at risk of a claim in the event such representation proved to be untrue (e.g., the claim has to be made within six months of the time the contract is signed).

## C. TIMING

The due diligence process should normally take place before the submission of bids. This will help to ensure high quality and compliant bids.

At times, due diligence can be conducted after a bid is accepted but before the final contract is fully settled. It is also possible (but usually not recommended) to have due

diligence conducted after the contract is signed but before the transactions set out in the contract are closed or consummated. Such due diligence, however, is generally restricted to verifying the accuracy of representations and warranties and compliance with covenants (i.e., promises) already contained in the agreement.

Where due diligence occurs after a contract is signed, there is a tendency on the party doing the due diligence to bring forward "issues" that arose "from the due diligence review" that "require the party to propose an amendment to the contract". In the worst case, the party's desire to complete the contract changes and the party withdraws from the contract.

## D. EXTENT

Generally, the extent of due diligence depends on the size and complexity of the procurement, the bidder's prior knowledge of the business or assets involved in the procurement, and the willingness of a prospective bidder and issuer to provide and rely upon representations, warranties and indemnities.

The nature of the obligations that a prospective bidder will assume under the contract will also be a key factor in determining the extent of due diligence it will wish to conduct. Prospective bidders are likely to be particularly interested in documentation relating to the costs and profitability of the various operations, historical and expected transaction volume growth, the nature of the technology and services in place, and the liabilities which are to be assumed (for example, material contracts, employee transfers and equipment transfers).

The issuer should be prepared to disclose all relevant material information. Material information is information which would reasonably be expected to be considered important or relevant to the prospective bidder. The level of detail should be sufficient to permit the prospective bidder to verify the statements made by the issuer in the RFP and to build the bidder's service, cost and pricing models.

The general rule of thumb is "if in doubt about whether to include information in the data room, then include it". This is because such information might be relevant to the prospective bidder and minimize the risk of the bidder saying after the contract is completed, "you had this information when we were conducting our due diligence but you did not share it with us and as a consequence we have suffered a loss". For example, financial information, technical information, business records and contracts that are of importance to the procurement opportunity should be provided for review.

Although the issuer should assist the prospective bidders to understand the information that is presented, the evaluation of the information is ultimately the responsibility of the bidder.

## E. ORGANIZATION

A well defined due diligence process will help to ensure that all bidders receive the same information in an efficient manner. Good organization not only increases the confidence of bidders in the materials provided, but also affects positively the perception that all bidders are receiving the same treatment. By contrast. disorganization may create the perception

that the process is not well developed and that all bidders are not receiving the same treatment. A disorganized data room and due diligence process may put seeds of doubt in the minds of the bidders relating to the issuer's ability to perform its side of the procurement project.

The reality and perception of an open, fair and transparent bidding process will be fostered by determining and communicating to bidders the due diligence process in advance of any disclosure. The due diligence timetable, the names of designated issuer contacts, the data room schedule, the information updating process, and the process for responding to bidders' questions should all be in place before due diligence begins.

## F. EQUAL ACCESS FOR ALL QUALIFIED BIDDERS

Once the identity of the qualified bidders has been determined, it is important to give each of them an equal opportunity to attend information sessions, to reserve time in the data room and to submit written enquiries. Equal and timely access to information in connection with the submission of the bids is a key component of an open, fair and transparent bidding process.

## G. CONFIDENTIALITY OBLIGATIONS

Before the issuer provides confidential information to prospective bidders and their advisors, the execution of a confidentiality agreement is usually required. It is common for the bidder and its advisors to undertake in such an agreement not to disclose:

(a) information provided by the issuer which is identified as confidential;

(b) any notes, analyses or other documents prepared by the bidder which reflect the confidential information; and

(c) the fact that the bidder is discussing the transaction with the issuer and has access to the confidential information.

It is usual to provide for the return or destruction of confidential documents by unsuccessful bidders upon execution of the definitive contract (or upon the termination of the RFP). The unsuccessful bidder should be required to certify that it has returned to the issuer or destroyed all such documents.

## H. MANAGEMENT OF INFORMATION

Generally, in many due diligence processes there will be written and oral sources of information, as well as information available from the inspection of property. To the greatest extent possible, the due diligence process should be through written documentation to ensure that all of the prospective bidders have equal access to the same information. Therefore, a system should be established for reducing to writing any important information provided to the prospective bidders.

## I. WRITTEN QUESTIONS RELATING TO RFP FROM PROSPECTIVE BIDDERS

Prospective bidders should be provided with an opportunity to submit questions relating to the RFP in writing by a particular date, prior to the end of the bid submission period. The issuer should circulate questions and answers to all prospective bidders with appropriate editorial changes to maintain the confidentiality of the enquiring bidder.

The written enquiry process should involve designating someone to receive the questions and circulate them to the issuer's procurement managers and key project employees. This individual would obtain undertakings from the relevant persons on the issuer's team to provide a written answer which would be returned to the manager of the written enquiry process for inclusion in a question and response package to be sent to all bidders and to the issuer's team.

## J. DATA ROOM ISSUES

### a) DESIGNATING MANAGER

The organization of data room information and procedures is a critical and potentially lengthy task of any procurement. The amount of documentation required and the current state of organization of that documentation will determine the resources and the time commitment required to organize the data room properly. In complex procurements, the issuer should designate a person to be the manager of the data room, to ensure that its organization proceeds on a timely basis.

### b) LOCATION AND SCHEDULING ACCESS

The data room must be located in premises that are large enough to accommodate the quantity of required documentation and that are available for the expected duration of the due diligence process. Often a conference room is used due to its size and its location which usually provides easy access to visitors without requiring them to pass through the heart of an office. There should be an efficient photocopying machine nearby if photocopying will be permitted.

Bidders should be given the opportunity to schedule blocks of time in the data room during which they can review materials, one bidder at a time. Sufficient time should be given to bidders to conduct a full review if they wish to do so.

If there are several bidders, it may be necessary to have at least one or two duplicate data rooms so as to give each bidder equal access. After the bids are submitted, access to the data room should end. It is not necessary to permit further access to the data room for the short-listed bidders or after the contract with the successful bidder is signed.

### c) ORGANIZING INFORMATION

There are many potential categories and sub-categories that could be used to organize the information in the data room. The best organizational approach will depend on the material available. Generally, data should be organized according to the type of information (for example, financial or technology-related) so that an expert in that area can easily review it. Organization by type of information also permits an efficient, methodical review. The reviewing

party can easily turn its mind to one key area at a time, rather than having to search for all the information related to a particular category.

### d) MAINTAINING CURRENCY OF INFORMATION

If new and material information in relation to the procurement is obtained after the due diligence review begins but before the bid closes, it should be added to the data room and an updated index, in blacklined form, or other notice of additions or changes, should be circulated to all prospective bidders. If the additions are minimal, it may be preferable to circulate the new documents to bidders if some of them have already conducted their due diligence review.

### e) PHOTOCOPYING DATA

There is no obligation to permit photocopying of data. However, it can reduce the amount of time that prospective bidders need to spend in the data room in order to make adequate notes.

To the extent that photocopying is permitted, it is best to provide an efficient photocopy machine close to the data room and to permit bidders to photocopy materials themselves on site, thus reducing the risk of loss of materials. In no circumstances should prospective bidders be permitted to remove data room documents from the premises.

If particular documents cannot be photocopied, they should be marked accordingly and placed in file folders of a different colour to remind the reviewer and the data room supervisor of the photocopying prohibition.

## K. BENEFITS: QUALITY OF BID AND EASE OF NEGOTIATION

The quality of bids will be related to the amount of pre-bid information provided to the bidders. The completeness of the bidder's proposal and the common understanding of the parties with respect to their objectives will provide a common point of departure in contract negotiations.

If disclosure is incomplete, then the successful proposal may have to be modified substantially, leading to increased costs and potential damage to relationships. In such circumstances, contract negotiations are likely to be lengthy and tense, given potential mistrust of information providers and anxiety over ultimate outcomes and benefits.

By contrast, complete disclosure should facilitate negotiation and improve the comfort level of the parties with respect to any representations and warranties included in the final contract. Where representations and warranties are included, the factual basis for their inclusion will have been verified by the representor. Furthermore, representations and warranties can potentially be minimized since the bidder will have "satisfied itself" with respect to particular issues.

Ultimately, there is a choice between a "front-load" or "end-load" due diligence process. If time and effort are invested at the beginning of the process to gather and make

available all relevant information, this should reduce the time, effort and cost of the subsequent stages of the process.

Issuers, however, should keep in mind that prospective bidders will be particularly sensitive to the cost of conducting due diligence before their bid is successful. This is not a reason to delay preparing due diligence materials since the issuer must be able to respond to the questions of prospective bidders and the successful bidder will usually wish to conduct due diligence before entering into the final contract. Rather, it is another reason to make sure that due diligence materials are relevant, well organized and user-friendly so that bidders will use them to their maximum advantage in preparing their bid.

If due diligence materials must be prepared at some stage, it makes sense to prepare them early and use them to inform all bidders as well as the issuer's representatives.

## 6. SELECTING THE PREFERRED BIDDER AND NEGOTIATING THE CONTRACT

### A. OBJECTIVES

The main objectives at this stage of the procurement process are:

(a) selecting the best value bid, based on quality of service and cost;

(b) securing the bidder's agreement to mandatory, non-negotiable contract terms and deliverables; and

(c) ensuring fairness in the procurement process.

In public sector procurements, the RFP often includes a description of the evaluation process and the criteria that will be used by the issuer in assessing the proposals received from bidders. The inclusion of an evaluation process and criteria is not commonly included in private sector RFP's.

### B. TWO-ENVELOPE BIDS

At times, it may be appropriate for the issuer to use a so-called "two envelope" bid approach to selecting the preferred proposal. By this approach, each bidder submits its bid in two parts, each part in its own envelope. One envelope is for the financial elements of the proposal, the other is for the non-financial elements.

If other financial proposals are within a specified percentage (e.g., 3%) of the preferred proposal, then all proponents are asked to reconsider their financial proposal and make their last and best offer. There are no opportunities given to change the non-financial elements of the proposal. In other words, a last and best financial proposal may be solicited from the preferred bidder and any other bidder whose financial offer is within the specified percentage.

### C. CONDITIONAL BIDS

Another important component in selecting the preferred bidder is determining how conditional bids should be treated. A conditional bid is one that the bidder will not commit to until the conditions attached to it have been met. The issuer should make all efforts to avoid such bids.

In complex procurements, it may be impractical simply to disqualify all conditional bids as this may limit unduly the number of qualified bidders. In order to minimize the need for conditional bids, clear instructions should be put in the RFP, bidders' conferences should be held, written answers to questions received should be given, data rooms should be organized and due diligence should be conducted.

A practical approach to dealing with conditional bids is to disqualify any bid which contains explicit conditions other than those that can be removed through clarification during the negotiation process. It is also important that all bidders make explicit all material assumptions made in formulating their proposals.

## 7. ALLOCATING AND MANAGING RISKS

An important part of any successful procurement is the identification, allocation and management of legal risks and potential liabilities. Effective solutions must address the legitimate and reasonable concerns of both the issuer and the vendor.

### A. TYPES OF LEGAL RISKS

Broadly speaking, the implementation of a large, complex procurement project gives rise to several types of legal risks, including:

(a) Direct Contractual Liability – liability of the vendor to the issuer (or vice versa) for breach of the contract between them;

(b) Third Party Liability – potential liability of the issuer and the vendor to persons who are not parties to the contract (i.e., "third parties");

(c) Early Termination – risks for the vendor as a result of termination for convenience by the issuer and risks for the issuer in the event the vendor prematurely terminates performance of its obligations under the contract;

(d) Limitation of Legal Recovery – risks that not all the losses suffered by the issuer or the vendor as a result of a breach of the contract by the other party of the contract will be legally recoverable from the party in breach as a result of the application of legal principles relating to the types of damages that may be recoverable for breach of contract or as a result of the terms of the contract itself; and

(e) Strength of Vendor Covenants – risks associated with the possibility that the vendor has, or will at some relevant time in the future have, insufficient assets to satisfy all of its legal obligations to the issuer.

In large, complex procurements, it is prudent for the issuer to develop a risk register to help it identify these risks and to keep track of how the risks are allocated and managed in the final contract.

### B. TYING LIABILITY TO RESPONSIBILITY AND CONTROL

One fair and common way to allocate and manage the proper level of liability risk a contracting party should bear is to tie the level of liability to the degree of responsibility and control assumed. To have one party assume a greater degree of liability than is commensurate with such party's responsibility adds a degree of risk transfer which will probably affect the economics of the transaction. If the issuer wishes to have the vendor assume liability for a risk which the vendor does not control, there will be a price to be paid for this, assuming the vendor is even prepared to assume the risk.

## 8. MONITORING PERFORMANCE OF THE CONTRACT

### A. ESTABLISHING MECHANISMS TO MONITOR PERFORMANCE

In complex long-term procurements, it is important that the issuer establish at the outset a clear mechanism to monitor contract performance on an ongoing basis. This mechanism may be as simple as having regular meetings of the issuer's and the vendor's key operational personnel.

### B. ESTABLISHING PERFORMANCE BENCHMARKS

Where possible, the contract should establish performance benchmarks and a means by which the parties can determine whether or not these benchmarks have been achieved. Often, procurement contracts require the vendor to provide for "continuous improvement" of increased service levels and reduced costs.

Ongoing monitoring of performance will act as an early warning system for potential breaches and will ultimately reduce the cost of performance and resolving disputes.

## 9. RESOLVING DISPUTES

For long term, complex procurements, it is often desirable that the contract specify a range of dispute resolution processes. This will maximize the likelihood that the parties will resolve disputes effectively and efficiently during the course of the procurement relationship.

### A. ALTERNATIVE DISPUTE RESOLUTION VS. COURT PROCEEDINGS

The term "alternative dispute resolution" or "ADR" is generally used to refer to any dispute resolution process outside the scope of a traditional lawsuit and traditional courtroom

proceedings. There have always been alternative dispute resolution processes. However, in recent times, these processes have gained in popularity and profile, and have, in some cases, become mandated as part of a traditional lawsuit or as a preliminary step before traditional litigation can proceed.

## B. CHOICE OF DISPUTE RESOLUTION PROCESS

The most appropriate dispute resolution process depends upon a number of factors, including the nature of the dispute, the desired degree of control by the parties over who should resolve the dispute, the relationship between the parties and the stage of the dispute (e.g., is it a new problem or have there already been several attempts to resolve it?).

Traditional litigation may be the most appropriate process where it is important for the issuer and for public policy reasons to have an open process and a decision that may serve as a useful precedent for the future. On the other hand, if a decision by an independent third party is required but the parties prefer to avoid the potentially negative publicity of open court litigation, then it may be appropriate to have the matter resolved by private arbitration.

The various dispute resolution processes are not mutually exclusive. If the dispute is not resolved by one process, the parties may agree to resort to another process.

## C. MODELS OF DISPUTE RESOLUTION

There is a full spectrum of dispute resolution processes available. At one end of the spectrum, negotiation, the parties have full control over the process and the crafting of the solution. At the other end, litigation, a third party has the authority to impose a solution.

The first step in most dispute resolution processes is to formulate a statement of the issues and facts as well as a list of relevant documents and other information. (This is known as the “Evaluation Statement” in the “Early Neutral Evaluation” process). This information should be provided to the persons evaluating the dispute.

Second, if information is to be provided to a third party or to the other party to the dispute in the course of the alternative dispute resolution process, then a confidentiality agreement is necessary. The agreement should state that all disclosures during the dispute resolution process will remain confidential and cannot be used in any subsequent dispute resolution proceeding, including arbitration and legal proceedings, without the consent of the parties.

Various disputes resolution processes are described below. Negotiation has been omitted as this term does not require explanation.

### a) INTERNAL RESOLUTION

It is frequently the case that persons who are involved at the hands-on operating level may be involved in a dispute and may not have either the authority or broader perspective to resolve the issue. Sometimes, emotions are also involved in causing deadlock.

It is often provided for in long term procurement contracts that, before any other form of ADR is attempted, the matter in dispute be "delegated up" to senior officers within the respective organizations who have the authority to resolve the dispute and a mutual commitment to try to make the overall relationship work.

**b) EARLY NEUTRAL EVALUATION**

If the senior officers cannot resolve the dispute, it may be appropriate to appoint a neutral third party to give an "expert opinion" on how the dispute should be resolved. The parties choose a neutral third party, usually an experienced and respected expert in the field if the dispute is technical in nature, or a lawyer if the dispute is one of contract interpretation.

The expert is provided with the Evaluation Statement prior to the "settlement conference". The disputants' goal in this process is to obtain an objective opinion about the merits of their respective positions.

The non-binding nature of early neutral evaluation may not always be appropriate if one party is more interested than the other in a speedy and final resolution of the dispute.

**c) FACT FINDING**

A fact finding process may be helpful where facts are vague or in dispute. A neutral third person or panel is appointed to determine the facts underlying the dispute and usually to assess the reasonableness of the disputants' positions given those facts.

The fact finder may be asked to produce a written report containing factual conclusions and, if desired, recommendations. The report can be accepted as binding or non-binding.

Alternatively, the fact finder may be asked to produce a report for each disputant, analyzing the strengths and weaknesses of their case.

Fact finding is most useful in the early stages of a dispute before the disputants become entrenched in their positions and unwilling to co-operate in any investigation that might disclose facts detrimental to their respective cases.

A determination of the facts may allow the disputants to subsequently negotiate a solution to their dispute on their own. If not, the parties may proceed to another dispute resolution process.

Where the parties proceed to voluntary mediation, they have the option of agreeing to make the fact finding report available to the mediator. If they do so, the mediation process is likely to be shorter.

If the parties ultimately proceed to litigation, any fact finding report will be admissible as evidence unless the parties have provided otherwise. There is a risk that parties will use the fact finding process to discover the strengths and weaknesses of the other side's case and will then "argue the facts that are found to be most damaging" in subsequent litigation.

Consequently, it is often prudent for the parties to execute a confidentiality agreement before beginning a fact finding process. It should stipulate that all discussions, notes, records and recollections provided to the fact finder or disclosed to the other side are confidential and may not be used at trial, except by the party who provided the information. Similarly, the confidentiality agreement should provide that any report by the fact finder may not be used at trial, except with the consent of both parties.

### d) MEDIATION

Mediation is a process which involves the appointment by the disputants of a completely neutral third party to assist them in reaching their own mutually acceptable solution. The ultimate goal is to produce a solution, recorded in a written contract, to which the disputants agree.

Mediation is often included in a contract as the first "outside" ADR process, since a mediator can be appointed relatively quickly, the process is relatively informal, and the parties retain control over the proceedings.

### e) MINI-TRIAL

"Mini-trial" is a term used to describe a proceeding created by the parties, and thus within their control, but which involves more formal presentations by each side. In a "mini-trial", lawyers usually make submissions to a panel of high-level representatives of the disputants who typically have settlement authority.

After listening to submissions, questioning the lawyers and negotiating a solution, the representatives may choose to enter into a binding agreement, if they have such authority. If they do not have such authority, any resolution must be ratified by both sides. The panel may also include a neutral third party who acts as an advisor/mediator/chairperson and who may or may not be authorized by the parties to issue a binding decision if the representatives do not agree on a solution.

The mini-trial process permits the disputants to find a creative solution, and is usually speedier and less expensive than a traditional trial.

### f) ARBITRATION

In a multi-stage dispute resolution process, arbitration is often used as the last resort. Alternatively, arbitration is stipulated for particular issues. In either case, the arbitration clause in the procurement contract must be carefully drafted since an agreement to submit a dispute to arbitration is binding under provincial law.

A general arbitration clause (providing that the parties may submit disputes under the agreement to arbitration) is usually not appropriate since it obliges the parties to submit any and all disputes to arbitration, on the initiative of either of the parties. In such a case, the obligation to arbitrate may only be avoided by mutual agreement.

The parties may stipulate in their contract a mechanism to appoint an arbitrator. Where the disputants appoint the arbitrator or panel, they have the flexibility of choosing an expert in the subject matter of the dispute, in contrast to litigation where the parties do not choose the judge. If an appointment procedure is not specified in the contract, and the disputants cannot agree, then the court may appoint the arbitrator, on application by a party.

Similarly, the parties may specify in the contract that particular rules of procedure will apply, usually the rules of a designated arbitration institute. Where no such provision is included in the contract and the parties do not otherwise agree on procedural rules, then the procedural rules under applicable legislation, such as the *Arbitration Act* (Ontario), will apply, supplemented by the rules of the particular arbitrator.

An arbitration decision is final unless the contract provides otherwise or unless a party obtains leave from the court to appeal on a question of law. Thus, arbitration can be used as a substitute for litigation or in addition to litigation. However, given the relatively high cost of arbitration, it is unusual for a procurement contract to provide for both arbitration and litigation of an issue.

Arbitration is usually a relatively formal proceeding and, depending on the rules adopted by the parties and the arbitrator, can be as lengthy as traditional litigation. The arbitration process resembles traditional litigation insofar as it usually includes opening statements, examination-in chief, cross-examination, re-examination, argument and reply. The arbitrator can award damages, specific performance or an injunction.

If necessary, an arbitration decision may be enforced by a court in the same way as a court order may be enforced. For example, a party may attempt to obtain an overdue payment of a monetary award by requesting a writ of seizure and sale of the assets of the party that owes the monetary award.

### g) LITIGATION

Traditional courtroom litigation is a formal process that in this province is governed by the Ontario Rules of Civil procedure. Particular documents must be filed with the court and delivered to the other side in order to commence a proceeding.

When both sides have completed their submissions, a judge or jury determines whether or not the complaining party has proved its case, on a balance of probabilities, and is entitled to the relief sought. The remedies that may be requested are limited, usually damages, specific performance or an injunction (see discussion in next section).

Litigation does not permit a party to claim remedies beyond those prescribed and does not provide a forum wherein the parties can create their own solution.

If the defendant does not comply with the remedy ordered by the court, enforcement mechanisms are available. Such mechanisms are relatively accessible and effective in the case of a claim for monies owed by a party whose location is known and whose assets may be seized.

Enforcement mechanisms may be more time-consuming and potentially less effective where such assets are not available or where specific performance of contractual provisions is sought.

## 10. ENSURING EFFECTIVE REMEDIES, INCLUDING INDEMNITIES AND PROTECTING RIGHTS ON TERMINATION

### A. TIERED REMEDIES

Remedies give the procurement contract its teeth. The promises in the contract are not worth the paper they are printed on unless they are enforceable. To address different levels of breach (relating to the character or severity of the breach), there should be different levels of remedies. Remedies that are tiered in accordance with the level of breach provide effective relief for the innocent party.

### B. INDEMNITIES

#### a) CLAIMS BY THIRD PARTIES AND CONTRACTING PARTY

The main purpose of an indemnity is to clearly stipulate the circumstances under which one party to the procurement contract can pursue a remedy from the other party. Typically, indemnity clauses specifically address the circumstances where one party to a contract will be entitled to seek recovery and protection against liability arising from claims by third parties due to the non-performance or negligence of the other party to the contract.

Indemnity provisions also typically reiterate the common law rule that the party in breach of contract will pay an amount of money damages to compensate the other party for the breaching party's defective performance.

In the case of indemnities from the Crown as issuer, the bidder should ensure that all statutory requirements to give effect to the indemnity have been met. For example, by section 28 of the *Financial Administration Act* (Ontario), where the issuer is the Ontario government, the issuer cannot enter into an indemnity unless it has obtained the written approval of the Minster of Finance.

#### b) TYPE OF LOSS

Indemnities may, by their express terms, address not only direct losses but also indirect or consequential losses suffered by the innocent party. They may also specifically require the indemnifying party to pay the innocent party's legal costs, in defending a third party claim or pursuing a claim against the breaching party.

The legal meaning of such terms as direct, indirect and consequential damage is, at best, unclear despite their frequent use in commercial contracts. If the issue becomes relevant in the course of a dispute, it is entirely possible that the vendor and the issuer will have different views about what constitutes direct as opposed to indirect or consequential damage.

As a practical matter, no contractual definition of what kinds of damages are and are not legally recoverable can be sufficiently specific to avoid all possibility of such disputes. Words are simply not capable of being used with a sufficient degree of precision to achieve such a result in all circumstances. Rather, there will often be room for some disagreement between the parties to a dispute.

#### c) LIMITATIONS ON LIABILITY

In complex, long-term procurement contracts, it is common for the liability of one or both parties under the indemnification provisions to be limited either by reference to a liquidated amount tied to the number of days the party is in default or to some other measure or by a cap on the maximum amount of liability a party may be required to incur. Some contracts have both liquidated damage clauses and a cap on liability. By quantifying and capping maximum liability, parties are able to estimate the amount of contingent liability they are assuming and to make the appropriate adjustments in the overall contract price or take other means to protect against risk of loss, such as purchasing insurance.

It is worth keeping in mind that whether the issuer agrees to or refuses to allow limits on the vendor's liability under the procurement contract is very likely to affect whether the vendor will agree to accept any limits on the issuer's liability. It is generally difficult for one party to negotiations to demand such a limitation from the other party when it is not prepared to accept a similar limitation itself.

#### d) CONTRIBUTORY BREACH OR NEGLIGENCE

Indemnities are usually subject to the exception that they do not operate to the extent that the losses are due to the act or neglect of the party seeking indemnification. A party should not be entitled to claim indemnification from another to the extent it is the author of its own misfortune.

### C. MONEY DAMAGES FOR BREACH

#### a) PRIMARY REMEDY

Generally speaking, the primary remedy at common law for breach of a procurement contract is the monetary award of damages. The purpose of this award is to put the innocent party in the same position as if the contract had been performed. In this way, the law of contracts protects the reasonable expectations of the parties, or the "loss of the bargain". This means that the innocent party will be entitled to damages which cover its out-of-pocket expenses and its reasonable expectation interest (usually the anticipated profits over the term of the contract). The law of contracts also protects the innocent party's restitution interest and, in order to avoid unjust enrichment, may require that monies be paid to the innocent party to compensate it for any benefit it has conferred on the breaching party under the contract.

### b) NO PUNITIVE DAMAGES

Generally speaking, the purpose of the law of contract is to compensate the innocent party, not to punish the breaching party. Therefore, only in very exceptional cases will the courts award exemplary or punitive damages for breach of contract.

### c) NO REMOTE DAMAGES

Another important principle in the awarding of damages is that of remoteness. Of course, the innocent party is entitled to be put in as good a position as would have been occupied had the innocent party received the performance promised. However, difficulties arise when the breach of contract causes a loss or deprives the innocent party of some anticipated gain from a separate transaction.

Indirect losses are usually only recoverable when they are reasonably foreseeable, which the courts have held may be the case when, at the time the contract was made, the special circumstances that gave rise to the indirect loss were known by the innocent party and communicated to the breaching party.

### d) NO AVOIDABLE DAMAGES

A further restriction on recoverable damages lies in the principle that the innocent party cannot recover for losses that could reasonably have been avoided. This is often described as the duty to mitigate. For instance, if the breaching party fails in breach of contract to deliver a machine essential to the innocent party's business, the innocent party is expected to go into the market and buy a substitute, not to let losses mount up for the lack of the machine.

### e) LIQUIDATED DAMAGES

Due to the difficulties inherent in ascertaining damages (such as remoteness) and the legal costs of proving them, the parties can agree in the procurement contract in advance to a genuine pre-estimate of damages for certain events of default. This pre-estimate could be negotiated by the parties and expressed in the procurement contract as a specific amount or by way of a formula. Such clauses are usually enforceable between commercial parties. However, they will not be enforceable if they operate as a penalty. To be enforceable, the clause must be reasonable, judged both at the time the contract was made and at the time it was breached. Again, this is because, as a matter of contract law, the purpose of damages is to compensate the innocent party, not to punish the party in breach.

## D. SECURITY FOR BIDDER'S PROMISES

For a procurement contract, the issuer will also need to consider whether it needs more than just the promise from the vendor to pay the issuer damages when the circumstances warrant. There are several ways the issuer can seek additional "security" to support this promise.

### a) GUARANTEES

The issuer may want to have guarantees from the shareholders of the vendor, particularly if the vendor does not have strong financial resources on its own. This can be quite effective in circumstances where the shareholders do have substantial financial resources.

### b) LETTERS OF CREDIT

The issuer could try to transfer certain financial risks from itself to a financial institution by requiring that a letter of credit from a bank or similar financial institution be delivered to it. Under a letter of credit, the bank promises to pay the issuer the face amount of the letter of credit as soon as the bank is satisfied that the triggering event has occurred (e.g., notice in writing from the issuer to the bank that the vendor has caused a loss and that the issuer is entitled to compensation under the letter of credit).

A letter of credit can be expensive for the vendor to maintain depending on its amount, the length of time it will be effective, and the circumstances under which it can be called. The bank usually requires the vendor to keep on deposit with the bank or to provide other security to backstop the bank in the event the letter of credit is called. Letters of credit can work quite effectively, but the security the bank may require to support the issuance of the letter of credit can be prohibitive to the vendor.

### c) PERFORMANCE BONDS

Performance bonds are issued by certain insurance companies who participate in this market. Under a performance bond, the insurance company promises the issuer that if the vendor fails to perform the obligations under the procurement contract, the insurance company will step in to cause the vendor or someone else to perform the vendor's obligations under the contract. The typical performance bond usually gives the insurance company the right to pay an amount as compensation in lieu of actually performing the relevant contract.

Performance bonds sound good in theory but are not that effective in practice, particularly where the performance obligations are sophisticated and cannot be easily substituted. It is also often difficult to negotiate the security which the insurance company will want from the vendor as consideration for issuing the performance bond.

### d) TRADITIONAL LIABILITY INSURANCE

Traditional liability insurance policies are not particularly effective as the primary solution to liability issues like those raised by the failure of the vendor to perform an obligation under a procurement contract. For recovery under the vendor's general liability insurance policy, it would be necessary to prove to the insurance company (or court) that the incident was an insured event under the policy and that the claimant (i.e., the issuer) is entitled to the proceeds of the insurance. The claim process can be complex, slow and expensive. Liability insurance policies are always needed for general liability concerns, but they do not usually cover contractual liabilities.

### e) NON-TRADITIONAL INSURANCE

There are non-traditional insurance products or methods that are available and could be designed to the particular facts of a large, complex procurement. For example, the issuer and the vendor could agree in the contract that the vendor would establish directly or through some form of specialized insurance product, a dedicated loss fund with a small portion of each transaction under the procurement contract being allocated to the loss fund to be available in the event the issuer suffers a loss and wants to receive compensation. The exact size and nature of the fund would depend on a variety of factors, circumstances, including the risk and likely size of claims.

## E. COURT ORDERS TO PERFORM

The courts also have the power to order specific performance of a contract, but will usually only do so if the subject matter of the contract is unique. For example, the court may order delivery of the Mona Lisa under a contract of sale, but it would not order specific performance of a contract for the sale of ordinary commercial goods.

The courts also have the power to order that a breach of contract be restrained. Such an order (called an injunction) could apply to certain provisions of a contract – for example, breach of confidentiality provisions – where an award in damages would not be sufficient to protect the business interests of the innocent party.

Still, specific performance, whether by way of an order of the court to do something or an order to refrain from doing something, is the exception. Generally speaking, absent express provisions in the procurement contract to the contrary, specific performance is the appropriate remedy only where an award of monetary damages would be insufficient.

## F. TERMINATION

Another type of remedy for breach of contract (apart from damages and specific performance) is termination. If a party breaches a term that is fundamental to the procurement contract, the other party may terminate its obligations under the contract as well as any of the breaching party's rights under the contract. Whether a term is fundamental or not depends on the seriousness of the breach.

## G. REMEDIES NOT EXCLUSIVE

A party's remedies are usually not exclusive. Subject to not putting the innocent party in a position better than would have been occupied had the contract been performed (by way of double compensation), it is also within the court's power to order a combination of performance (albeit defective) and a monetary award. So too, the innocent party can terminate the contract for cause and sue the breaching party for a monetary award of damages.

## H. FORCE MAJEURE

Contracts for long term procurement will often contain a force majeure clause, which is designed to address circumstances which are beyond the control of the issuer or the

vendor (such as floods, fires, ice storms, strikes). Events that constitute force majeure may, depending on their duration, lead either to termination of the procurement contract or suspension of the vendor's provision of services for some period of time. In either event, there would be risks to the issuer's ability to have services intended to be delivered pursuant to the procurement program provided during such events.

The issuer may wish to address what events will (and will not) constitute force majeure for the purposes of the procurement contract. Even more importantly, the issuer may wish to put in the contract that it has the right to provide services by some alternative means in the event that the vendor ceases, temporarily or permanently, to provide services under the contract. The issuer may wish to consider, as well, how and at whose expense it would be able, as a practical matter, to exercise any right to provide services by some alternative means, if the need to do so were to arise.

## I. RIGHT OF ISSUER TO TERMINATE THE CONTRACT

In order to protect the issuer's interest under the procurement contract, the following provisions setting out circumstances in which the issuer may terminate the contract are usually included:

(a) Termination Forthwith for Bankruptcy – In the event the vendor becomes bankrupt, insolvent, etc., the issuer may terminate the contract immediately. This right protects the issuer's interest vis-à-vis the vendor's creditors;

(b) Termination Upon Notice for Uncured Breach – The issuer should also have the right to terminate the contract in the event that the vendor breaches the agreement and, after a reasonable period of notice to cure the default, fails to do so. Termination in this case does not preclude the issuer from seeking a monetary award of damages;

(c) Termination Upon Notice for Fundamental Breach – The contract could also go on to stipulate fundamental terns, the breach of which entitles the issuer to terminate the contract without further notice, opportunity to cure given to the vendor, etc.;

(d) Termination Upon Notice for No Appropriation by Parliament or the Legislature – Where the government is the issuer, the procurement contract should also be clear that the government is entitled to terminate the agreement without further liability in the event it is unable to appropriate the necessary funds from Parliament or the Legislature, as the case may be. Such a clause usually provides that the government will use its reasonable efforts to obtain the appropriation sufficient to satisfy its obligations under the agreement and when it fails to do so, will notify the vendor in writing; and

(e) Termination Upon Notice for Convenience – Especially where the issuer is the government, the procurement contract should also give the issuer the right to terminate the agreement without cause, upon a period of notice and with provisions sufficient to protect the reliance interest of the vendor. For example,

the issuer is often required to at least reimburse the vendor its sunk costs. This is usually referred to as a right to terminate for convenience. Such a right gives the issuer the flexibility to cancel the project, with the appropriate notice and compensation to the vendor, if, for example, the project becomes obsolete or if there is a change in government policy.

Notwithstanding the inclusion of these rights in the procurement contract, it is usually the case that the issuer will not exercise the right of termination except in extreme cases.

### J. VENDOR'S RIGHT TO TERMINATE

The vendor may also have a right to terminate in certain circumstances (such as material default by the issuer in performing its obligations or if there is a material reduction in the scope of the project). In this case, the notice period would have to be sufficient to give the issuer enough time to transfer the contract to an alternative service provider.

### K. TRANSITION OBLIGATIONS UPON TERMINATION

In all cases of termination, the vendor must be obliged, by way of clear and detailed transition provisions in the procurement contract, to work with the issuer and the new vendor for a period of time and to facilitate the transfer of the procurement contract to the new vendor. This provision will be particularly important in the termination for convenience provisions. Practically speaking, however, these provisions may not be relied on when the issuer has terminated the agreement by reason of the vendor's breach.

As part of any transition provisions, the vendor should be required to deliver to the issuer all computer hardware, computer software, material, equipment, records and other property used to provide the services under the procurement contract.

## 11. SUMMARY AND CONCLUSION

### A. HALLMARKS OF SUCCESSFUL PROCUREMENT

While not an exhaustive list, as discussed in this paper, the hallmarks of a successful procurement are as follows:

(a) Issuer consults bidders early and often in open, fair and transparent manner;

(b) Issuer issues a well developed RFP and pro forma contract, specifying mandatory terms;

(c) Issuer conducts careful due diligence on bidders;

(d) Issuer provides organized data room, information meetings and other opportunities for bidders to conduct their due diligence;

(e) Bidders peruse RFP and review it thoroughly with their project team and professional advisors;

(f) Bidders conduct due diligence and ask issuer any questions they have about the procurement opportunity;

(g) Issuer selects “best value” bid;

(h) Negotiated procurement contract ties liability to responsibility and control;

(i) Parties monitor performance benchmarks, including those for continuous improvement;

(j) Disputes are resolved as they arise;

(k) Tiered remedies (including termination and transition) are effectively enforced to address different levels of breach.

## B. SKIPPING LEGAL NICETIES IS FALSE ECONOMY

While the pressure to meet a tight deadline in an RFP may tempt both the issuer and bidder to skip legal niceties, doing so is a false economy. Often, the legal principles and processes that must be respected for an open, fair and transparent procurement are just as important as the business and technical requirements of the RFP.

Well drafted RFP’s and responses form the foundation of successful procurements. They not only establish the framework for the business opportunity, they also are a useful tool for managing change and resolving disputes in the relationship between the parties.