May 5, 2004

Dear Purchasing Officer:

You have the following question: Is it lawful for the city to base the award of competitive bids on the preference for local contractors or providers of goods and services?

An important federal case almost incidentally addresses that question. I have been unable to find any cases in Tennessee directly on that question, but a Tennessee state case defines "competitive bidding." Those cases, and the case law in other jurisdictions, indicate that the answer is probably that local preferences as a general policy are probably not legal, but that local preferences supported by some reason or reasons related to the quality of the bid at issue may be legal.

The courts in most jurisdictions have repeatedly declared that local governments have broad discretion in determining what are the lowest and best bids on public contracts of various kinds, and that the courts generally will not interfere with the exercise of that discretion. However, that discretion is considerably more limited where under the state law or local government charter, contracts must be "competitively bid."

Competitive Bidding Generally

The Municipal Purchasing Law requires that contracts over a certain amount be competitively bid. [Tennessee Code Annotated, ' 6-56-304] What does the term "competitive bidding" in the Municipal Purchasing Law mean? The Tennessee Supreme Court in State ex rel. Wright v. Leech, 622 S.W.2d 807 (Tenn. 1981), answered that question:

1. "The request for bids must not unduly restrict competition. All persons or corporations having the ability to furnish the supplies or materials needed, to perform the work to be done, should be allowed to compete freely without any unreasonable restrictions."

2. "It is essential that bidders, so far as possible, be put on terms of perfect equality so that they may bid on substantially the same proposition and on the same terms."

3. "In order to attain competitive bidding in its true sense, *proposals for bids must be invited under fair circumstances which afford a fair and reasonable opportunity for competition.*" [Emphasis is mine.]

4. Among other things, the advertisement for bids should include "[s]pecifications of the supplies or equipment to be purchased and the quantity thereof."

Those standards are not optional, continued the Court, they must be followed.

The obvious fundamental principles of Leech are that all bidders must be put on a level playing field, and that the bidding process actually be competitive. In fact, it is further said in Metropolitan Air Research Testing Authority, Inc. v. Metro. Government of Nashville & Davidson County, 842 S.W.2d 611 (Tenn. Ct. App. 1992), that:

> One of the purposes of competitive bidding is to provide bidders with a fair opportunity to compete for public contracts. State ex rel. Leech v. Wright [citation omitted]. Thus, the courts have recognized that *the statutes and ordinance requiring competitive bidding impose upon the government an implied obligation to consider all bids honestly and fairly*. [Citations omitted.] [At 616] [Emphasis is mine.]

In addition, ' 23 of the City Charter, provides that with respect to all contracts for "work, improvements, supplies, materials or machinery," that exceed the amount that triggers the application of the Municipal Purchasing Law, "it shall be the duty of the council to let such contracts to the lowest and best bidder after due notice for competitive bids. This action may be dispensed with only where one source supply exists."

If the city lets bids to bidders based on a general policy of local preference, it seems difficult to argue that the city's bid process is fair or that it promotes competition. But here, let us also turn to examination of whether the "lowest and best bid" standard contemplates local preferences.

The Lowest Responsible Bidder

As indicated above, generally, a government body has considerable discretion in determining what is the lowest responsible bidder, but that discretion is not unlimited. It is said in 10 McQuillin, Municipal Corporations, ' 29.73, that there must be a *plausible* reason for a rejection of the lowest bid. Owen of Georgia, Inc. v. Shelby County, 648 F.2d 1084, 1992 (6th Cir. 1981), is even more clear. There, Shelby County, Tennessee, rejected the lowest bid on a certain contract on the grounds that the second lowest bidder was a local firm, and had a better minority hiring record. Shelby County argued that the "good cause" provision of the statute that governed the county's competitive bidding gave it grounds to reject the lowest bid. The good cause provision read:

> All open market purchase orders or contracts shall be awarded to the lowest bidder who is financially responsible, taking into

> consideration the qualities of the articles to be supplied, their conformity to specifications, their suitability to the requirements of the County government and the delivery terms. And any and all bids may be rejected for good cause. [At 1088]

The Court rejected Shelby County's argument, reasoning that:

> While a bid may be rejected for reasons other than those enumerated, the County must cite factors similar to the ones listed, i.e. factors which go to the heart of the contract. In order for rejection to be based on "good cause," the proffered reason must be related to something which affects the County bargain to substantially the same degree that, for example, inferior quality goods or non-conforming goods affect it. Poor workmanship on a previous job is one example of such a factor.
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> *The reasons cited by the County in the present case "that Pidgeon Thomas employs a higher proportion of minorities and is a local concern" do not constitute "good cause" for rejecting the other bid*. These factors simply do not affect the County's bargain to the same extent that factors such as those specifically enumerated affect it. [At 1092] [Emphasis is mine.]

As pointed out above, under the competitive bidding requirements contained in the City's own charter, the city is obligated to award bids to the "lowest and best bidder." Under Owen of Georgia, Inc. v. Shelby County, cited above, the rejection of the lowest bid is required to be supported by some reason related to the bidder's responsibility. Indeed, it may be that in some cases a local preference is in fact related to the bidder's responsibility, or otherwise to the quality of the bid, presumably if it affects the ability of the bidder to perform the contract.

The heavy weight of authority in other states appears to be in accord with that principle. For example in Scandrick v. City of Dayton, 423 N.E.2d (1095), the City of Dayton's Code of Ordinance required awarding bids to the "lowest and best bidder." The Ohio Supreme Court held that a local preference granted to one bidder on a construction contract was an abuse of discretion on the part of the city, for what appear to be three reasons:

1. In spite of what the city claimed was a "primacy of the policy to prefer resident bidders," the city

> ....did not announce or disclose the existence of such a policy to the bidders until after the bids were opened. It appears, therefore, that appellants made a conscious decision to withhold this pertinent

> information until after they had actual knowledge of the amounts of the bid. In effect, appellant's modified their requirements without notice. This action tended to undermine the integrity of the competitive bidding process. [Citations omitted.] [At 1097]

2. There was "no logical nexus" between the city's goal of increasing its tax base and its decision to award the contract to the next lowest bidder.

In the trial court the city tried to justify the award of the bid based on residency. The city's witness testified that in awarding the bid, the city considered the location of the successful bidder's home office, and the fact that he employed a work force year round within the city. However, the city could offer no proof of where the successful bidder's employees lived, and apparently could not even prove that the successful bidder's company was actually a city resident. In short, it could not point to a good reason for the local preference.

3. "The evil" said the Court, was not necessarily that resident bidders are preferred, but that:

> there are absolutely no guidelines or established standards for deciding by how "many percentages" a bid may exceed the lowest bid and yet still qualify as the "lowest and best" bid. Absent such standards, the bidding process becomes an uncharted desert, without landmarks or guideposts, and subject to a city officials' shifting definition of what constitutes "many percentages." Neither contractors nor the public are well served by such a situation. [At 1098]

The third reason seems to require Ohio cities to adopt standards under which local preferences will be granted, and to make all bidders aware of them. I doubt the Tennessee Courts would go that far, but it does appear to me that they would require that a local preference in the award of local government contracts be supported by some reason related to the ability of the bidder to perform the contract, on a case-by-case basis.

Similarly, in Marriott Corporation v. Metropolitan Dade County, 383 So.2d 662 (1980), a Florida District Court of Appeals overturned the award of a contract by Dade County to Jerry's rather than Marriot. The county awarded the contract to Jerry's because it was a local corporation, notwithstanding the fact, that Marriot's bid would have returned to the county a greater percentage of the revenues it would have earned under the contract. A county resolution required bids to be awarded on the basis of the best financial interest to the county.

Holding that the award of the bid to Jerry's was an abuse of discretion on the part of the county, the Court reasoned that "Under competitive bidding, the contract must be awarded as a

function of the reasonable exercise of power by municipal government authorities, as a matter of public policy and fidelity to the public trust." [At 667] The standard for deciding whether there is an abuse of discretion, said the Court is:

> While the law imposes no mandatory obligation upon a public agency in respect to the letting of competitive contracts that will require the agency in every case to consider the lowest dollars and cents bid as being "the lowest responsible bid" to the exclusion of all other pertinent factors that may be taken into consideration, the law does require that where discretion is vested in a public agency with respect to letting public contracts on a competitive basis, the discretion may not be exercised arbitrarily or capriciously but must be based upon facts reasonably tending to support the conclusions reached by such agency. [At 668]

That case appears to be saying the same thing as does Owen of Georgia, Inc. v. Shelby County, cited above.

Remedies for Improper Bid Process

It is clear in Tennessee that any unhappy bidder has standing to challenge the award of a bid on the ground that the bid process was illegal in some manner. [See Metropolitan Air Research Testing Authority, Inc. v. Metro. Government of Nashville & Davidson County, 842 S.W.2d 611 (Tenn. Ct. App. 1992); Browning-Ferris Industries of Tennessee, Inc. v. City of Oak Ridge, 644 S.W.2d 400 (Tenn. App. 1983); Owen of Georgia, Inc. v. Shelby County, 648 F.2d 1084 (6thCir. 1981)]. It is also said in Browning-Ferris Industries of Tennessee, Inc., above, that:

> A contract entered in violation of bidding statutes or ordinances is void and it is not necessary to show that the governmental authority acted in bad faith or fraud was involved. Johnson City Realty Co., 166 Tenn. 655, 64 S.W.2d 507 (1933). [At 403]

In Tennessee, that does not mean that the unhappy bidder gets the contract. The unhappy bidder's remedy when a bid is set aside is apparently at least the cost of preparing his bid, and perhaps the cost of his lawsuit. In Browning-Ferris Industries v. City of Oak Ridge, 644 S.W.2d 400 (Tenn. Ct. App. 1982), the Court awarded the unhappy bidder for the reasonable expenses for preparing and presenting its bid. In Owen of Georgia, Inc. v. Shelby County, the Court found the County liable on the theory of promissory estoppel, reasoning that, "In its solicitation of bids pursuant to the Restructure Act, Shelby County clearly promised to award the contract to the lowest financially responsible bidder if it awarded the contract at all." [At 1095] The measure of damages, continued the Court, was "the expenses it incurred in its unsuccessful participation in the competitive bidding process as well as the costs incurred in its successful attempt to have the

award to Pidgeon-Thomas rescinded as having been made in the violation of the statute." [At 1096]

Sincerely,

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