Scribbles Squibs* #62 (May 18, 2018):

A PUBLIC OWNER CAN CANCEL AN EXISTING CONTRACT TO GET A BETTER PRICE SAYS MASS. SUPREME JUDICIAL COURT

By Massachusetts Construction Attorney Jonathan Sauer

I. INTRODUCTION.

A very important – and a very disturbing - case has recently issued from the Massachusetts Supreme Judicial Court with regard to a public owner's right to exercise a termination for convenience clause for no other reason than to obtain a lower price. The Massachusetts Supreme Judicial Court ruled in the case of *A. L. Prime Energy Consultant, Inc. v. Massachusetts Bay Transportation Authority* that the MBTA could invoke a 'termination for convenience' clause to cancel a fuel supply contract after obtaining a better price from a different supplier under an available existing contract. (If you would like a copy of this decision, send us an email and we'll send it right along.)

This case is a disturbing movement away from traditional bid law principles that a public owner's receiving the lowest possible price in a procurement cannot be achieved at the expense of a process which is not open and honest with all bidders being in a position of equal footing. Certainly, no public entity would agree with a contractor's contention that it should be allowed to be excused from the performance of a publicly-bid contract because it could make more money elsewhere. Why, then, is what's good for the goose not also good for the gander?

II. WHAT HAPPENED WITH THE PROCUREMENT AND WHAT THE SUPREME JUDICIAL COURT DECIDED.

In January, 2015, the MBTA put out for bid a two year contract to supply it with ultra low sulphur diesel fuel (ULSD). The contract was supported with federal assistance.[1]

The contract included a termination for convenience clause under which the MBTA could "in its sole discretion" terminate the agreement "for the convenience and/or for any reason" with 30 days' notice and pay the contractor reasonable costs and profit on work done up to that point in accordance with principles set out in the Federal Acquisition Regulations.[2]

A. L. Prime Energy Consultant, Inc. (Prime) was awarded the contract in July, 2015.

Nearly a year later, the MBTA realized it could achieve cost savings by opting into a statewide contract with a different supplier that had been executed around the same time. The agency invoked the termination for convenience clause to sever its contract with Prime.[3]

Prime subsequently sued the MBTA in superior court for breach of contract. The MBTA moved to dismiss the complaint but a superior court judge denied that motion. That judge applied federal precedent, under which if an aggrieved contractor can show that a public entity has acted improperly by proving that it terminated a contract solely to obtain a better price elsewhere, it has a cause of action. Through the exercise of certain procedural mechanisms, the case ultimately found itself in front of the Supreme Judicial Court (SJC), which is Massachusetts' highest appellate court.

The SJC rejected Prime's argument that by referencing the Federal Acquisition Regulations, the contract incorporated federal case law, which requires a court, in construing a termination for convenience clause, to look into whether a public entity has abused its discretion or acted in bad faith. The SJC specifically stated that: "Massachusetts law must determine the proper construction of a termination for convenience clause."[4]

The language Prime was referring to "does no more than provide that, once the MBTA terminates for its convenience, Prime's reimbursement is to be determined under (federal regulation)," SJC Judge Lenk wrote. "The single reference to the Federal Acquisition Regulations does not incorporate the Federal standard for interpreting a termination for convenience clause. . . . .The MBTA's power to terminate is expressly defined by other language in the termination provision."

Applying, instead, general Massachusetts contract principles, the SJC found that, contrary to Prime's argument that only a funding loss or other change of circumstances would justify invocation of the termination for convenience clause, the contract indeed empowered the MBTA to terminate "for any reason".[5] [6]

The SJC further rejected Primer's arguments that construing the clause as written rendered the contract unenforceable for lack of consideration, particularly in light of the payments the MBTA was obligated to make if it were to invoke the clause, and that it rendered the contract illusory.[7]

Accordingly, the SJC concluded that the Superior Court Judge erred in denying the MBTA's motion to dismiss.[8] [9]

III. A CRITIQUE OF THE DECISION.

This decision misapplies what has historically been the rationale for termination for convenience clauses under federal procurement law. Because of how long it can take to both design a federal project and then get funding for it, by the time both design and funding come together, sometimes the project is no longer feasible or even necessary. It is for these reasons under federal procurement law that the concept of termination for convenience came into being. It was a mechanism by which the government could withdraw itself from unnecessary projects,

projects which became unnecessary not due to its own fault. A termination for convenience was never intended as being a vehicle for merely saving the government money. But, that is what the Court is attempting to do in this decision.

Although MGL C.30B is only referenced in one footnote in the decision, where this is purely a purchase of materials, it is probably the statutory scheme under which this procurement took place. How can a decision issue as to the interpretation of a statute without even *discussing* the statute?

Moreover, by failing to differentiate between a materials only procurement and construction procurements where there are both labor *and* materials, this decision, while probably only necessarily applicable to MGL C. 30B, might be later seen as authority for the application of its revised termination for convenience principles to MGL C. 149, s. 44A-H procurements (public buildings) and MGL C. 30, s. 39M procurements (public works) and construction management at risk projects pursuant to MGL C. 149A, where the numbers of such contracts are often sizably bigger and where the risks undertaken by public bidders are far greater than those merely vendors bidding only to supply materials.

One notes that there is no reference to *any* other Massachusetts procurement system until a reference to MGL C. 30, s. 39M - but only as a footnote - which does not appear in the decision until page 19. Massachusetts bid law is heavily statutory. Yet, in reaching its decision, the SJC only referenced two of the public bid statutes briefly in footnotes only with no discussion as to what either of those two statutes means or requires.

This decision, in my view, goes against several time-honored Massachusetts bid law principles.

The first is that in asking for bids, a public entity enters into an implied contract with the bidders that it will honor the terms of its own procurement. A bidder for public materials and, more especially for public construction - buildings or public works - puts a substantial amount of its own time and money in putting together a bid. And, in deciding to bid on one project, that bidder may be committing its resources for a number of years to follow and may be foregoing other potential opportunities under which greater profits were possible. The public owner and the public bidder enter into a symbiotic relationship - a form of procurement 'marriage' - where both are contemplating entering into a relationship based on good faith and honesty and some degree of trust. It's a relationship built upon mutual obligations and mutual respect. The public construction system can successfully operate no other way.

But, here, government is being rewarded for being inefficient, achieving a cost savings only at the expense of its public bidders. Would the Court let bidders for public procurements out of their ultimate contracts if they could demonstrate that they could make more money on other jobs? If this were allowed, there would simply be chaos in public procurement. And, yet, that is *exactly* what this decision is ultimately encouraging, its only ostensible saving grace being that it (apparently) is alright to be unfair when that unfairness saves the government money. As George Orwell said in *Animal Farm*, "All animals are equal but some animals are more equal than others." Isn't that, in the final analysis, what the Court is saying in this decision?

Massachusetts bid law precedents should be applied. And, those precedents say that in the public contracting domain, an invitation to bid upon certain conditions followed by submission of bids upon those conditions creates an implied contract obligating the bid solicitor (the government) to those conditions.

That's another way of saying that the government *should* and *will* honor the terms of its own procurements. And, without such a statement, what would induce private bidders to take their time and commit their own money and resources to bidding on Massachusetts public procurements if the government could cancel those procurements simply because a better deal came along? If, these become 'the new rules', the government will find that many former bidders on its projects will put their efforts towards more reasonable private construction, where the profit margins are generally greater and where parties breaking their contracts will not do so without potential consequences, such as the payment of damages.

For more than forty years, the law has been that there are the twin, *conjunctive* purposes to be accomplished by the competitive bid statutes, as as annunciated in decisions such as Interstate Engineering Corp. v Fitchburg, 367 Mass. 751, 757-758 (1975), which stated those purposes thusly: " . . . First, the statute enables the public contracting authority to obtain the lowest price for its work that competition among responsible contractors can secure. . . Second, the statute establishes an honest and open procedure for competition for public contracts and, in so doing, places all general contractors and subbidders on an equal footing in the competition to gain the contract." These principles have been interpreted in a variety of decisions as being *co-equal.*

The focus of this decision is solely on what might save the government money, only to be achieved at the expense of general contractors and subcontractors submitting bids, whose participation in the public procurement system is completely and utterly necessary to make it work *at all*.

The thrust of the decision is myopic because it focuses its attention upon just this *one* procurement: a saving of money for the procurement of fuel. But, it is illogical in the long term in that while it may save the government money for this *one* procurement, the net effect will be that fewer entities will be interested in bidding public projects if the government can cancel a job upon its finding a better price. And, with fewer entities bidding public projects, prices will go up, which makes what is arguably only a questionable gain as to this one purchase - fuel - become a long term loss with fewer bidders and higher prices as to a whole host of other publicly-bid projects.

If the government can get out of contracts because it discovers a better deal elsewhere, then why wouldn't that rationale also apply to the benefit of the other party to this partnership, the bidder for public procurement projects? Isn't what is good for the goose also good for the gander? Tyranny by the majority is no less tyranny.

IV. CONCLUSION.

I am not sure that there is any saving grace to this decision.

The Massachusetts Supreme Judicial Court is the oldest continuously functioning appellate court in the Americas. Its decisions typically demonstrate great legal sophistication and erudition. Perhaps this decision is the exception that proves the rule.

This decision, in my view, doesn't make any sense at all and doesn't follow a lengthy and broad series of Massachusetts cases defining various bid law principles, which this decision largely, if not studiously, ignores.

If there is any silver lining to what could appear otherwise to be a very dark cloud, it would appear that this is a decision based upon MGL C. 30B, which is the Massachusetts statute having to do with the procurement of materials only or for the procurement of relatively limited miscellaneous services. This is not a statute which governs the procurement of contracts for the construction of public buildings (MGL C. 149, s. 44A-H) or the procurement of contracts for the construction of public works (MGL C. 30, s. 39M) or the procurement of the construction of projects under the construction management at risk model (MGL C. 149A). With all three of these referenced statutes, there is a significant labor element in such procurements and such procurements necessarily are all involved with the construction of *something.* And, since all such projects involve the construction of a specific project and for the payment of prevailing wages which are uniquely determined for individual construction projects, it would seem highly unlikely that the circumstances underlying this decision could be found within the construction context without going out for an additional round of bids, which did not happen here. The provision of fuel oil is not directly or even necessarily construction-related and has no labor element involved with it at all. As such, this decision can easily be distinguished from being applicable to Massachusetts public construction projects, all of which will involve construction *something* using human labor.

But, at the same time, this is a very dangerous decision, in my view, as it might be cited in the future as legal authority for a public owner's terminating a *construction* contract to obtain better pricing elsewhere. This is neither fair to the subcontractors and general contractors participating in the public bidding process nor, in the final analysis, is it fair to the Massachusetts taxpayer, who will have to foot the bill for the higher prices that this decision almost necessarily will result in.

One must remember that Murphy's Law is, after all, a form of *law*.[10] It is not hard to imagine other courts interpreting what should be a very narrow decision applicable to the purchase of materials as being legal authority to be applied to Massachusetts construction projects. And, to summarize in one word, this would be a *disaster*.

Dear Reader, please keep in mind that some legislation results from citizen attempts to reverse what some consider to be poor judicial decisions. If you do not agree with this decision, you might consider contacting your local Representative or Senator in order to hopefully get

such a process started with regard to this decision. Organizations such as ABC, AGC and UCANE have a lot of influence on Beacon Hill. This might be a time to use it.

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* A 'squib' is defined as 'a short humorous or satiric writing or speech'. Wiktionary defines a 'squib' as: "a short article, often published in journals, that introduces empirical data problematic to linguistic theory or discusses an overlooked theoretical problem. In contrast to a typical linguistic article, a squib need not answer the questions that it poses."

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[1] It is a complicated legal issue as to when federal law will pre-empt or control Massachusetts law when a public procurement has both state and federal involvement. In this decision, the Court did not say that federal law pre-empted state bid law and bid law principles. In fact, the Court stated that it applied Massachusetts legal principles in its decision notwithstanding numerous references to various federal procurement regulations and to various federal court decisions.

[2] Many cases involving 'termination for convenience' clauses arose out of situations where due to a lengthy period of time passing between the original concept/design for a project and the ultimate funding of a project, by the time of the actual performance of a contract for a project, the need for the project no longer existed or the project required significant redesign, which made going forth with the project as designed impractical or unnecessary. In practice, such clauses have come to be used to terminate contracts between general contractors and subcontractors without fault so that such could be concluded for whatever reason in a way that litigation would not ensue. Neither purpose involves using such a clause as a vehicle to get a better price.

[3] The decision seems to make much of the fact that an existing contract would be used for the re-procurement and that the MBTA did not go out to bid for the purposes of attempting to obtain lower prices. This would seem to be a distinction without a difference, particularly as far as Prime is concerned.

[4] While stating that it would interpret the termination for convenience clause with reference to Massachusetts law, the SJC did not interpret such a clause with any appreciable reference to the public bid laws, the milieu out of which this case arises. And, further, having said that it would follow Massachusetts law, the SJC then went on to reference at least a dozen federal cases (in addition to various decisions from other states) and also made at least six references to one federal procurement regulation or another.

[5] The only Massachusetts case referenced with regard to a termination for convenience involved a situation where the public entity lost its funding, not a factor in this case.

[6] In construing a termination for convenience clause before this decision, it would not have occurred to any bidder on public work that the government's ability to terminate for convenience 'for any reason' would include finding a better price elsewhere. A marriage between two individuals is, first and foremost and from a legal standpoint, a contract. And, even applying society's current more relaxed approach to such matters, nonetheless, society still takes a dim view of one married partner's searching for a better spouse after having agreed to the first spouse. Why should the government be allowed to do otherwise?

[7] Those attending our Basic Construction Contract Law for Contractors know that 'consideration' is one of the three elements necessary to form a contract. Simply put, the 'consideration' is what each party to a contract is going to receive in exchange for its own performance. It is difficult to believe that consideration to a public bidder is anything less than its having the ability to be paid for its performance at agreed-to prices over the entire length of the contract, the term of which was determined by the public owner in soliciting bids. If a public owner can opt out when it finds a better price, then how does any bidder have anything other than the possibility of consideration, not its actual receipt? If a public owner is entitled to receive fuel oil over a period of two years for a fixed price from the public bidder, how can the bargain between the parties be seen as equal if a public owner can opt out of such a contract as soon as it finds a lower price? Prime having to perform for two years while the MBTA having to perform for as little as one day, *reductio ad absurdum.*

[8] One might question the level of concern the SJC demonstrated for the rights of Prime, including its contract right to the performance of its entire contract. In essence, with a court's review of the propriety of a government's actions, one has the government commenting on the correctness of the government's actions. For some disputes, including on what might be considered close calls, that sounds like one too many 'governments' involved in the equation. A bidder for public work is only able through successful competition to be in a position for its employees to feed their families. The successful competition should only be as to those directly competing for the same work,

for the same project. Here, the public bidder for *one* project is also being forced to have to compete with the bids of bidders bidding on *other* projects. All other arguments notwithstanding, this hardly seems fair.

[9] One of the few actual bid law cases referenced by the Court – the *Petricca* case – held that a public owner does not have the right to go out and rebid a contract to get a lower price. If such is true, then why this particular result which seems to be completely at odds with the *Petricca* holding?

[10] Charles Dickens stated in *Oliver Twist* that 'the law is an ass'. Humor being reason's last line of defense, his possibly less than sanguine disposition may have been caused, in part, by his habitation in a bleak house. The result of this decision is that the public bidder got . . . scrooged.