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CONSTRUCTION LAW BULLETIN

MORE ON TENDERS

Introduction

Usually tenders are attacked by an aggrieved tenderer who believes that the award made was wrong due to either procedural irregularities, corruption or otherwise.

What is the position if the organ of State who made the award itself recognises that it acted wrongly in making the award? Can it correct its mistake?

In December last year the Supreme Court of Appeal ("SCA") delivered a judgment[1] which provides the answer to this question.

Background

In November 2008 the North-West Department of Health and Social Development ("the Department"), represented by its then acting head, Ms Kgasi, entered into a five year lease with TEB Properties CC ("TEB"), represented by its managing member, Mr T E Bozwana, for office accommodation at a monthly rental of R3,2m excluding VAT.

Prior to the Department taking occupation of the leased premises, Ms Kgasi's successor as acting head of department, Mr Malaka, gave notice to TEB of the Department's summary termination of the lease agreement.

In his letter of termination Mr Malaka justified the termination on three grounds:

[1] TEB Properties CC v The MEC for Department of Health and Social Development, North West SCA Case No 792/10, date of judgment 1 December 2011, ZASCA 243.

- there had been no compliance with relevant statutory requirements;
- TEB had knowingly participated in an irregular process; and
- there had been no open bidding process.

TEB launched an application in the North-West High Court for an order declaring the Department's termination of the lease unlawful. The Department in turn filed a counter application in which it sought an order declaring the lease invalid.

The North-West High Court agreed with the Department and dismissed TEB's application and set the lease aside.

TEB appealed this decision to the SCA.

Legislative Backdrop

The SCA summarised the statutory matrix relevant to the issue and made reference to:

- section 217(1) of the Constitution which requires organs of State contracting for goods or services to do so in accordance with a system which is fair, equitable, transparent, competitive and cost-effective;
- section 4(1) of the North-West Tender Board Act which vests the power to procure supplies and services for government in the North-West Province in the Tender Board and stipulates that the Board must invite offers in connection with such procurement;
- section 38(1)(a)(iii) of the Public Finance Management Act ("PFMA") which requires departments to have an appropriate procurement system which is fair, equitable, transparent, competitive and cost-effective;
- Treasury Regulation 13.2 which grants to the accounting officer of a department the right to enter into operational lease transactions without limitations; and
- Treasury Regulation 16A.6.4 which provides that if it is impractical to invite competitive bids, an accounting officer may procure goods or services by other means subject to the obligation to record the reasons for not following a competitive bidding process.

Although not specifically referred to by the Court as relevant in this particular case, the Preferential Procurement Policy Framework Act ("PPPFA") is an important piece of legislation pertinent in the determination of the validity of any procurement process followed by an organ of State.

In relation to Regulation 16A.6.4 the Court noted that there must be a rational reason for not following a competitive bidding process and that the reasons concerned must be recorded so that National Treasury can review any such decision and determine whether there has been any financial misconduct by an organ of State.

The Facts

In June 2008 the Department commenced looking for new office accommodation for its head office personnel as its existing lease agreement was due to expire at the end of August 2008. Kgasi approached Bozwana and invited him to submit a rental proposal on behalf of TEB.

After a period of negotiations between Bozwana and a department task team headed by Kgasi, a lease agreement was concluded between the Department and TEB in November 2008. In terms of this lease agreement the Department leased premises comprising 21 612m² for a period of some 10 years at a monthly rental of R3,2m excluding VAT.

It was common cause that the lease agreement had been entered into without there having been any open and competitive bidding process.

Bozwana stated that during the negotiations Kgasi had reassured him that the procedure being followed was above board and regular and that any lease concluded would be valid because the need to conclude a new lease agreement was urgent as the Department's current lease was about to expire.

The Parties' Cases

The Department contended that the North-West High Court had made the correct decision and that the lease agreement was invalid for want of the required statutory procedures having been observed and most importantly the lack of an open bidding process.

TEB argued that despite the lack of an open bidding process the lease was valid because of the urgency of the situation and the power conferred on the Department in terms of Treasury Regulation 16A.6.4.

The Court held that this argument was unsustainable because, although the lease agreement was concluded in November 2008, it was only scheduled to commence on 1 December 2009 to enable TEB to construct the premises. The matter was therefore not urgent. The Department also contended that a lack of proper planning on its part could not create urgency for the purposes of Treasury Regulation 16A.6.4.

TEB also argued that Treasury Regulation 13.2.4 gave an accounting officer an unfettered right to enter into a lease agreement of the type concerned and she was not obliged to follow an open bidding process.

The Court ruled that Treasury Regulation 13.2.4 cannot be interpreted to give carte blanche to accounting officers to enter into lease agreements without following a competitive bidding process.

TEB complained that it was incumbent upon the Department to comply with the lease agreement until it had been set aside by a court and the Department had failed to do this.

The Court confirmed that contracts concluded by an organ of State, even where the organ of State has acted wrongly, do in fact remain valid and binding until set aside. However, when a court sets the contract aside, as in this case, the setting aside is effective right from the outset. In other words, it is as if there was no contract concluded at all.

The Court pointed out that the Department had acted correctly in seeking a court order setting aside the wrongful tender award.

TEB also argued that neither the Constitution nor the PFMA expressly require procurement via a competitive bidding process and that in any event it was not incumbent upon it to enquire and establish that the Department had complied with any relevant internal procedural requirements for procuring the lease without following a competitive bidding process.

The SCA held that this argument was also unsustainable. It pointed out further that the North-West Tender Board Act gave exclusive jurisdiction to the Tender Board to conclude lease agreements and preparatory to doing so to invite offers from tenderers.

Although not invoked by the SCA, it is clear from the provisions of the PPPFA and the Regulations promulgated in terms of the Act that government procurement must take place by means of an open and competitive tendering process.

Lastly TEB contended that the Department should be estopped from denying the existence and validity of the lease agreement.

The doctrine of estoppel is to the effect that if a party represents to another party that a state of affairs exists, even if that state of affairs does not in fact exist, if the other party acts to its prejudice on that representation, the representing party is bound by its representation and cannot rely on the true state of affairs being different.

In this case TEB, relying on the existence of the lease agreement, had procured a large bank loan to fund the construction of the office building and presumably had entered into a construction contract for that purpose. As such it had acted to its prejudice based in effect on the representation by the Department that a valid lease agreement had been concluded with it.

Unfortunately for TEB the State is not bound by the doctrine of estoppel where something is prohibited in law in the public interest. In this case clearly the prohibition against the procurement of goods and services by the State without following the statutory processes is in the public interest and as such the SCA ruled that TEB could not rely on estoppel.

Conclusion

Parties who conclude contracts with organs of State in dubious circumstances do so at their own peril. They could find themselves in a position where the contract concerned is set aside and they are left with various contractual commitments to third parties.

An organ of State can, on seeing the error of its ways, refuse to continue with an invalid tender award. It should however apply to court for an order setting aside its own wrongful award unless the tenderer concerned agrees to the cancellation of the award.

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