

GOVERNMENT



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Far-reaching implications for public sector from Auckland labs decision

The recent High Court decision on Auckland's lab testing contract has much wider implications for public sector procurement. In particular:

- Unsuccessful proposers will be in a stronger position to rely on both contractual and public law claims concurrently to challenge public procurement processes.
- The case sets very high expectations for communication to proposers of what an entity is looking for in its procurement. It leaves little or no room for subtlety or generality by a procurer when it comes to consulting on or communicating its procurement intentions.
- If entities are looking to make significant changes to the funding or service model through their procurement they need to be completely up front and "in your face" about it.
- Requests for Proposals (RFPs) and tenders may need to preserve the priority of public law obligations such as consultation more extensively than is currently the practice.
- The courts are intolerant of self-imposed time constraints from procurers as an excuse for failing to meet consultation obligations. Procurers may need to be more flexible in this regard.
- Obligations to consult can arise from a whole range of policy and framework

documents that may long pre-date, and not be closely connected to, the particular procurement, and which can therefore be easily overlooked.

- Conflict of interest disclosure needs to be much fuller and more explicit than is currently common practice.

Process contracts and judicial review

In the labs decision, Justice Asher considered that entering into service agreements under section 25 of the New Zealand Public Health and Disability Act 2000 (NZPHD Act) constituted the exercise of a statutory power and was therefore open to judicial review. The case indicates a major shift away from previous court decisions (in particular *Southern Community Laboratories Limited & Ors v Healthcare Otago Ltd & Ors* HC DUN CP30/96 19 December 1996) where tendering processes undertaken by public bodies were seen not to be amenable to judicial review given their highly commercial nature. Justice Asher justified his departure from the decision in *Southern Community Laboratories* on the basis that it was decided under the predecessor of the NZPHD Act, the Health and Disability Services Act 1993 (HDS Act) which "brought a commercial edge to public health". The judge considered that unlike the NZPHD Act, the

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HDS Act provided that Crown Health Enterprises should be as successful and efficient as comparable businesses. Notwithstanding the absence of a similar provision in the NZPHD Act, it is difficult to conceive of a more commercial decision than selecting a proposer under a competitive tendering process – not to mention for a half billion dollar contract.

Previous decisions involving the Ministry of Defence and the Auckland City Council conducting competitive procurement processes have analysed the status of an RFP or tender document and the management, through the use of exclusion clauses, of any contractual obligations and liability that arose. In these previous decisions the existence of a process contract has also led the court to conclude that judicial review was not appropriate.

Whereas the prior case law has generally chosen to give a remedy under either contract or judicial review, in this case Justice Asher seems to consider both are available. The decision seems to assume the existence of a process contract, with the judge regarding the RFP as having contractual force from the moment it was issued. At the same time Justice Asher states that legitimate expectations arise where a public authority promises to follow a certain procedure, and accepts in general terms that two of the three legitimate expectations claimed by the plaintiff could be seen as arising from the RFP.

The case puts unsuccessful proposers in public sector procurement processes in a better position to challenge those processes than they were previously. They can now more forcefully argue contractual and public law claims concurrently rather than having to choose between them.

Running procurement processes

The labs decision indicates organisations need to be very clear in the procurement

processes in the messages they give to proposers about what they are looking for.

The Auckland Regional district health boards (ARDHBs) were criticised for not being up front with Diagnostic Med Lab – the unsuccessful proposer – that they were looking for dramatic savings and possibly a radical change to the status quo (in that they were considering a different model of service supply).

If organisations want proposers to ‘think outside the square’ they have to convey this adequately, rather than allowing them to labour under the impression that incremental changes to an existing arrangement will suffice.

One onerous implication from the case is that the inclusion of unqualified confidentiality clauses in RFPs (agreeing not to disclose information contained in proposals) may be contrary to the obligation to consult. Justice Asher considered that the contractual constraints imposed by the RFP prohibiting release of proposers’ information without their consent could not excuse the DHBs from their duty to consult. Public sector procurement documentation may need to preserve the priority of public law obligations such as consultation more explicitly than is currently the practice.

Consultation

Tight timeframes contained in an RFP were seen as self-imposed constraints and did not excuse inadequate consultation. The court considered it was open to the DHBs to give Diagnostic Med Lab a further extension and suspend the RFP process in order to consult after the RFP proposals foreshadowed much more significant changes than had been signalled by the DHBs in their initial consultation.

Non-statutory guideline documents, especially those issued by Ministries, form part of the framework through which



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organisations must determine their public law obligations. To determine the DHBs' consultation obligations the court specifically relied upon the New Zealand Health Strategy, December 2000; the Consultation Guidelines for the Ministry of Health and District Health Boards, September 2002; the operational policy framework issued by the Ministry of Health, July 2005; and the Crown Funding Agreements between the DHBs and Ministry of Health. Justice Asher looked at these guideline documents as being binding on the DHBs and creating stringent public law obligations to consult.

A "bland" discussion document which needs to be closely analysed to appreciate the full significance of any potential changes will not be adequate consultation. Consultation needs to be more "in your face", and not just talk in generalities, so that consultees are aware if an organisation is seriously contemplating significant changes.

The urgency of the consultation was self-created given the impending contract end-date (which could have been extended) and consultation over the Christmas period was inadequate. By contrast, Justice Asher commented that the timeframe for some other DHB consultations of at least six working weeks, with a discussion document containing very detailed strategic options and a response template with particular questions, was adequate consultation.

Conflicts of interest

The court concluded that it is not sufficient simply to list the organisations a board member is involved in that could give rise to a conflict – the nature and effect of the potential conflict must be sufficiently disclosed so that other board members can understand the true nature of it and be able to respond to and deal with the conflict if it materialises.

In the court's view a strict approach to managing conflicts must be taken, with

rigorous exclusion from all relevant aspects of a process if any conflict of interest arises. The court was highly critical of the decision of the Auckland District Health Board not to exclude board member Dr Tony Bierre from the moment they realised he had a conflict of interest.

The onus on organisations is not limited to avoiding conflicts in its own decision-making process, it also extends to ensuring that proposers do not benefit from any conflict of interest. The judge considered that the knowledge, and therefore advantage, the Lab Tests consortium had gained through Dr Bierre's involvement meant that the proposal should have been excluded and the consortium should have been prevented from participating.

Watch this space

Given the wide-reaching implications of the judgment (e.g. a public body's decisions of an obviously commercial nature may be subject to judicial review) it will be interesting to see whether the DHBs appeal the case, at least in order to narrow and refine the legal precedent value of the decision.

The stark nature of the facts in the case probably influenced the judge to make stronger and more unqualified statements about the legal position than one might typically see in judgments. As a result there are likely to be statements and findings in the judgment that health providers and public sector tenderers will seize upon to support their arguments when future disputes arise in other procurement processes.

*For a full summary of the facts and findings of the case *Diagnostic Medlab Ltd v Auckland District Health Board, Waitemata District Health Board, Counties Manukau District Health Board and Ors* HC Auckland CIV 2006-404-4724, 20 March 2007, please see our Litigation Update (21 March 2007) at www.bellgully.com

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