



California Supreme Court Rejects Claim by Second-Lowest Bidders on Public Works Contracts that Low Bidder Interfered with a Prospective Economic Advantage

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The California Supreme Court in *Roy Allan Slurry Seal, Inc. v. American Asphalt South, Inc.* (Feb. 16, 2017) Case No. S225398, --- Cal.3d ---, held that for public works contracts awarded to the lowest responsive, responsible bidder, the bidder has at most a hope for an economic relationship with the public entity and that relationship is insufficient to state a claim for intentional interference with prospective economic advantage.

Background:

The Plaintiffs in this litigation, Roy Allan Slurry Seal, Inc. (Allan) and Doug Martin Contracting, Inc. (Martin) (collectively, Plaintiffs) alleged that Defendant American Asphalt South, Inc. (American) outbid them on 23 public works contracts by failing to pay prevailing wages to its employees. As to the Riverside County contracts, Plaintiffs alleged that for the six public works contracts that the public agency awarded to American, either Allan or Martin was the second lowest bidder. Plaintiffs argued that American tortiously interfered with those contracts by illegally submitting deflated bids. Plaintiffs further argued that because they were the second lowest bidders, they would have been awarded those contracts if American had not submitted the illegally deflated bids.

Supreme Court's Analysis:

In this case, the Supreme Court considered whether a disappointed bidder on a public works contract [can] demonstrate the requisite economic relationship with the public entity? (*Id.* at p. 5.) It held in the negative.

The Supreme Court began its analysis by examining the tort – to state a claim for intentional interference with prospective economic advantage a plaintiff must establish: (1) the existence, between the plaintiff and some third party, of an economic relationship that contains the probability of future economic benefit to the plaintiff; (2) the defendant’s knowledge of the relationship; (3) intentionally wrongful acts designed to disrupt the relationship; (4) actual disruption of the relationship; and (5) economic harm proximately caused by the defendant’s action. (*Id.* at p. 5 [citing *Korea Supply Co. v. Lockheed Martin Corp.* (2003) 29 Cal.4th 1134, 1164-1165.]

The Supreme Court examined cases that focused on the first element of the tort, and particularly those decisions where a court found that either the economic relationship with the third party is too attenuated or the probability of economic benefit too speculative. (*Id.* at p. 9.) Themes throughout those decisions include a mere potential future relationship, a deal that is a mere expectancy, and potential economic relationships where one party has unfettered discretion to enter into the relationship. The Court concluded that these authorities counseled against recognizing the tort where there is a mere probability of future economic benefit. (*Id.* at p. 11 [quoting *Korea Supply Co.*, *supra*, 29 Cal.4th at 1164].)

The Supreme Court then examined the nature of public works contracts. It explained:

Public works contracts are a unique species of commercial dealings. In the contracts at issue here, the public entities retained broad discretion to reject all bids. The bids were sealed, and there were no postsubmission negotiations. In awarding the contracts, the public entities could give no preference to any bidder based on past dealings, and were required to accept the lowest responsible bid.

(*Id.* at pp. 1-2.) The Court also found significant that a bidder on a public works contract does not have a protectable expectancy because there is an insufficient degree of certainty that the second lowest bidder would receive the contract. (*Id.* at p. 12.)

Finally, the Court examined the public policy behind competitive bidding laws and emphasized that those laws are for the benefit of the public. It concluded:

Expanding tort liability to cover wrongful interference with the public contracts bid process would provide little additional benefit in light of the extensive statutory scheme. Conversely, an expansion has potentially significant public policy disadvantages. . . . The possibility of significant monetary gain may encourage frivolous litigation by second lowest bidders. . . . That litigation, in turn, may deter responsible bidders from participating in the process, thus undermining the Legislature’s goal of ‘stimulating competition in a manner conducive to sound fiscal practices.

(*Id.* at p. 18 [quoting Pub. Contract Code § 100, subd. (c).] Thus, the Supreme Court found that the Plaintiffs failed to state a claim for intentional interference with prospective economic advantage.

Concluding Remarks:

This decision is important for several reasons.

First, the Supreme Court solidified the rule that an unhappy bidder may only receive monetary damages in the amount of bid preparation costs, not lost profits, in civil litigation. It did so by quoting that rule and using the reasoning behind it—lost profits from a public works contract are highly speculative, not only because a bidder may bid at a loss, but also because typically a public entity has the discretion to reject all bids—to

support its conclusion that there is an insufficient economic relationship between a bidder and a public agency to state a claim for the tort.

Second, though this decision analyzed whether a bidder could state a claim for intentional interference with prospective economic advantage in the context of a low-bid procurement, it would make good sense for a court to apply the reasoning and result in this decision to other types of procurements as well. Alternative procurements, including design-build procurements, have many of the unique characteristics the Supreme Court pointed to in *Roy Allan Slurry Seal, Inc. v. American Asphalt South, Inc.* as the basis for its decision. For example, a public agency almost always has broad discretion to reject all bids regardless of the type of procurement. Moreover, public agencies must award contracts based on the invitation for bids or invitation for proposals; thus, public entities usually give no preference to any bidder based on past dealings. The policy underpinnings of the decision, that the purpose of the Public Contract Code is to encourage competition, would likewise be equally applicable in the context of an alternative procurement.

Finally, the Supreme Court was clearly concerned about the future impacts on public procurements of a rule that permitted an unsuccessful bidder to sue the successful bidder for monetary damages, raising the potential of draining government resources and potentially interfering with the public's interest in having its contracts promptly awarded and performed. That concern was in addition to the concern that permitting an unsuccessful bidder to sue for lost profits would discourage bidding on public contracts and increase the cost of the project.