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# Can a Local Government Rescind Its Award of a Contract Under North Carolina's Formal Bidding Statute?

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Suppose a local governing board has received bids on a construction contract and has awarded the contract to the "lowest responsible bidder" under North Carolina's formal bidding statute (North Carolina General Statute § 143-129). After the award *but before the parties have executed a written contract,* the board determines that it is not in the governmental unit's best interest to go forward with the contract. Perhaps a question has arisen about the qualifications of the contractor, a funding source is lost, or the board decides to redesign the project. Does the award obligate the board to go forward with the contract, or can it rescind its award without incurring any liability to the contractor?

This bulletin examines the issue of when a public contract governed by North Carolina's competitive bidding requirements becomes binding on the governmental unit. There are no North Carolina cases that address this subject directly. Courts in other jurisdictions have held that where a statute establishes special procedures or requirements as prerequisites to a valid public contract, no binding obligation exists until *all* of those requirements have been met, even though the actions undertaken would otherwise constitute offer and acceptance under basic contract law principles.[1] However, some of these cases, under various legal theories, also limit the circumstances that justify the awarding authority's failure to go forward with a contract after it has been awarded.

## Offer and Acceptance

A basic tenet of contract law is that the acceptance of a valid offer creates a contractual obligation.[2] This maxim typically applies in the context of public contracts as well, so that the "acceptance of a valid bid by the proper municipal authorities, where all legal requirements are observed, constitutes a binding contract."[3]

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1. *See generally* J. D. Emerich, Annotation, *Revocation, Prior to Execution of Formal Written Contract, of Vote or Decision of Public Body Awarding Contract to Bidder*, 3 A.L.R.3d 864 (1965); State v. Johnson, 779 P.2d 778, 780 n.2 (Alaska 1989)(summarizing cases addressing this issue).

2. JOHN D. CALAMARI and JOSEPH M. PERILLO, THE LAW OF CONTRACTS §§ 2–5 (3d ed. 1987). *See* Henderson & Corbin, Inc. v. West Carteret Water Corp., 107 N.C. App. 740, 421 S.E.2d 792 (1992).

3. 10 EUGENE MCQUILLAN, THE LAW OF MUNICIPAL CORPORATIONS § 29.80 (Charles R. Keating ed., 3d ed. 1987). It is well established that, in the context of a competitive bidding procedure, the bid constitutes an "offer" and the award of the contract constitutes an "acceptance" for purposes of contract law analysis. CONSTRUCTION BIDDING LAW § 1.3 (Robert F. Cushman and William J. Doyle eds., 1990); 10 MCQUILLAN, *supra*, § 29.65. A bidder may sometimes argue that the solicitation of bids constitutes an offer by the contracting authority and that a responsive bid therefore constitutes an acceptance. However, this formulation is simply inconsistent with the competitive bidding process. This is especially true in North Carolina, where the awarding authority

Under many competitive bidding statutes, there are statutory requirements that must be completed *after* the governing body has voted to award a contract and accept a particular bid. For example, North Carolina's formal bidding statute requires that all contracts within its scope must be executed in writing.[4] In addition, that statute requires the successful bidder to provide satisfactory performance and payment bonds and to execute the contract within ten days after it is awarded.[5] When these types of requirements apply, "even after acceptance of the bid has occurred, no contract is formed until the requisite formality has been complied with."[6]

The only North Carolina cases concerning this subject involved situations in which the bidder, rather than the awarding authority, sought to withdraw from the award. There is language in these cases suggesting that a binding contract is created when it is awarded, although the holdings turned on other factors. Furthermore, as will be shown below, the obligations of the bidder and the awarding authority under competitive bidding statutes are not parallel. Thus the determination that a bidder is bound by the award of the contract does not necessarily extend to the awarding authority.

In *Wm. Muirhead Construction Company v. Housing Authority,*[7] the defendant awarded a contract under the formal bidding statute, but a dispute arose about whether a certain part of the work was covered in the contractor's bid or was to be negotiated on a unit-price basis. The Housing Authority argued that, under the competitive bidding law, "once an award is made there is a binding contract."[8] Without specifically ruling on that contention, the court concluded that no contract existed, because the bid documents were ambiguous and there was no "meeting of the minds" between the parties.

A similar result was reached in a case involving a private, nonprofit water corporation's "tentative" award of a contract subject to Federal Housing Authority (FHA) approval.[9] The corporation argued that the award created a binding contract and that the bidder was unable to withdraw its bid after that point. The court of appeals held that the tentative or conditional acceptance of a bid does not create a contract, because acceptance must be "unequivocal and unqualified."[10] The opinion recites the basic rule of offer and acceptance and seems to suggest that had the award not been conditional, it would have constituted a valid acceptance. The facts before the court, however (especially the lack of a valid acceptance and perhaps the fact that the awarding authority was not a public entity), did not require the court to address the question of whether statutory requirements to be met following the award would have affected the parties' respective obligations.

## Bidder's Obligation

Competitive bidding statutes alter the typical contract formation process and establish different requirements for offer and acceptance. For example, under basic contract principles, an offer is revocable until it is accepted or rejected. However, competitive bidding statutes impose an obligation upon a bidder, from the time the bid is submitted, to execute a contract if the bid is accepted. This obligation typically is secured by a bid deposit or bid bond. Under the formal bidding statute, a bid must be accompanied by a bid deposit or bond of at least 5 percent of the bid amount. According to the statute, the bond is forfeited if the successful

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has discretion in awarding contracts and reserves the right to reject any and all bids. N.C. GEN. STAT. § 143-129.

4. N.C. GEN. STAT. § 143-129; *see* Styers v. Gastonia, 252 N.C. 572, 114 S.E.2d 348 (1960) (holding that contract for construction or repair within scope of bidding statute was unenforceable against the city because it was not in writing).

5. The ten-day time period is often extended by the governmental unit to allow sufficient time for the preparation and signing of contract documents. In addition, § 143-129 authorizes the governing board to waive the performance and payment bond requirements for contracts for the purchase of apparatus, supplies, materials, or equipment.

6. SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 4:10 (Richard A. Lord ed., 4th ed. 1990).

7. 1 N.C. App. 181, 160 S.E.2d 542 (1968).

8. *Id.* at 187, 160 S.E.2d at 547.

9. Henderson & Corbin, Inc. v. West Carteret Water Corp., 107 N.C. App. 740, 421 S.E.2d 792 (1992).

10. *Id.* at 743, 421 S.E.2d at 794. *But c.f.* City of Merrill v. Wenzel Bros., 277 N.W.2d 799, 802 (Wis. 1979) (holding that award contingent on EPA approval was binding on both parties from point when approval, received after award, was communicated to bidder).

bidder "fails to execute the contract within ten days after the award or fails to give satisfactory surety."[11]

Litigation involving obligations after the award of a contract often involves the question of whether a contractor is entitled to withdraw a bid (e.g., due to a mistake justifying withdrawal)[12] or, if not, whether the contractor must forfeit the bid bond. This was the posture of the cases described earlier. In these cases, the bid bond provision makes clear that once bids are opened, unless legal grounds for withdrawal exist, the successful bidder is obligated to go forward with the contract or forfeit the bid bond.

## Awarding Authority's Obligation

As noted above, the bidder's obligation under competitive bidding laws is greater than that of a person making an offer under traditional contract law. The following discussion demonstrates that the bidding statutes do not impose comparable obligations upon the awarding authority.

Unlike the bidder withdrawal situation, award rescission is not addressed in the bidding statutes. As outlined in the first section of this bulletin, standard contract law provides that a contract is binding upon acceptance. Indeed, a number of cases from other jurisdictions have held that acceptance occurs and the contract is binding on both parties as of the award, even where some formalities occur after that time.[13] As stated in *City of Susanville v. Hess*:[14]

> [I]n letting of contracts for the doing of public works where the legislative body or the administrative officer is required by statute to call for bids and must under competitive bidding conditions let the contract to the lowest responsible bidder, *the making of the award* gives rise to the contract between the public body or agent and the successful bidder.

This rule also was applied in *Lord Electric Co. v. Litke*,[15] where the awarding authority rescinded its award of a contract after the indictment of the successful bidder on bid rigging charges. The court held that the rescission was invalid, because the award of the contract created a binding obligation on both the bidder and the awarding agency.[16] As stated in another case:

> The time to exercise discretion is when the bids are opened as advertised and the public body makes the award. After that decision the body is without discretion.[17]

In contrast, other jurisdictions have ruled that the awarding authority is not bound until both parties have complied with all applicable statutory procedures. For example, in *Mann v. Incorporated Town of Rochester*,[18] the Indiana Appellate Court held that the bidder does not acquire any right to perform the work simply by being determined to be the lowest bidder. Instead, the awarding authority's discretion to make or not to make the contract remains until it is exhausted by the exe-

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11. The statute authorizes the governing board to waive the bid bond requirement for contracts for the purchase of apparatus, supplies, materials, or equipment estimated to cost less than $100,000.

12. *See* N.C. GEN. STAT. § 143-129.1 (providing that bidder may withdraw a bid only if a written request is presented within seventy-two hours after the bid opening and upon proof that error is substantial and due to clerical, unintentional error or omission, as opposed to a mistake in judgment).

13. *See* United States v. Purcel Envelope Co., 249 U.S. 313 (1919) (recognizing binding contract upon formal order of acceptance and before signing and approval of contract) [relying on Garfielde v. United States, 93 U.S. 242 (1876)].

14. 290 P.2d 520, 526 (Cal. 1955) (emphasis added).

15. 469 N.Y.S.2d 846, 848 (N.Y. Sup. Ct. 1983).

16. The court noted, however, that the formation of the contract did not preclude the awarding authority from convening to determine whether it wished to *perform* the contract, or to determine whether valid grounds for rescission of the contract might exist.

17. Robert W. Anderson Housewrecking & Excavating v. Board of Trustees, 681 P.2d 1326, 1331 (Wyo. 1984) (holding that award created binding obligation on both parties, because statute did not require a writing, and recognizing rule that no contract exists until there is a writing only where the statute requires a writing).

18. 63 N.E. 874 (Ind. Ct. App. 1902).

cution of a contract.[19] Similarly, as recognized in *Covington v. Basich Bros. Construction Co.*:[20]

> The proposal and award were preliminaries looking toward execution of a formal contract. . . . The commission then revoked its award so that the preliminaries were wiped out and the parties were in the same position as before the award was made. The commission had the right to revoke its award at any time before a formal contract was entered into because a contract with a public agency is not binding on the public agency until a formal contract is executed.

The South Dakota Supreme Court applied this rule in *Schull Construction Co. v. Board of Regents of Education*, in which the awarding authority rescinded and revised a resolution that awarded a construction contract "pending the signing of contracts and the furnishing of performance and payment bonds."[21] The applicable bidding statutes contained a requirement that contracts "shall be made and set forth in writing and signed on behalf of the public corporation by the proper officials thereof." Although the contractor argued that the resolution approving the bid created a binding contract, the court held that until the contract was signed by the awarding authority, no binding contract existed and the board had the power to rescind its award.[22]

The basic result in these cases is not surprising: clearly, where a statute requires a written contract, there is no binding obligation on the parties until the writing is executed. The result is unusual, however, in that the respective obligations of the bidder and the awarding authority are not equivalent. The bidder is bound to go forward with a contract before the awarding authority is and, indeed, before an enforceable contract exists.

## Discretion to Rescind Award of a Contract

Even in jurisdictions holding that the governmental unit is not bound until all formal requirements are met, the legal doctrines on which some of the cases rely limit the awarding authority's discretion in completing those formal requirements. Thus, although the award does not necessarily create a contract, the awarding authority may not have the same degree of discretion (either as to a particular bidder or the decision to contract at all) after the award has been made. In large measure, these cases turn on how the courts characterize the formal requirements that must be satisfied after an award.

Some courts have held that the execution of a contract or compliance with other statutory formalities are ministerial acts and that there is no discretion as to their completion.[23] Indeed, units commonly rely on the detailed bidding instructions, specifications, award notices, and other preliminary documents for the terms of the contract. The formal contract is often a relatively brief document (sometimes just a purchase order) that incorporates the earlier documents by reference.[24] Viewed in this light, the process is reasonably characterized as ministerial.

Similarly, several courts have characterized an award as an agreement to contract subject to a specific condition or, stated another way, a contract subject to a condition precedent to formation.[25] Under this formulation, a binding contract does not exist upon award, but the authority has no discretion to rescind its award if the relevant conditions (e.g., contractor delivery of a signed contract and acceptable bonds) are satisfied.

In contrast, the *Schull* case, summarized above, held that a board has the power to recon-

19. *Id.* at 876.

20. 223 P.2d 837, 840 (Ariz. 1951).

21. 113 N.W.2d at 665.

22. *Accord* State v. Johnson, 779 P.2d 778 (Alaska 1989); Village of Woodbridge v. Bohnen Int., Inc., 377 N.E.2d 121, 123 (Ill. Ct. App. 1978); MacKinnon-Parker, Inc. v. Lucas Metro. Housing, 616 N.E.2d 1204 (Ohio App. 1992); Philadelphia v. Canteen Div. of TW Services, 581 A.2d 1009 (Pa. Commw. Ct. 1990) [relying on Wayne Crouse, Inc. v. School Dist., 19 A.2d 843 (Pa. 1941), and Chilli v. School Dist., 6 A.2d 99 (Pa. 1939)].

23. Brophy v. City of Joliet, 144 N.E.2d 816, 822 (Ill. Ct. App. 1957).

24. *See* City of Susanville v. Hess, 290 P.2d 520, 526 (Cal. 1955).

25. K. L. Conwell Corp. v. City of Albuquerque, 802 P.2d 634, 639 (N.M. 1990) (distinguishing between conditions precedent to formation and conditions precedent to performance); Anderson v. Board of Trustees, 681 P.2d 1326, 1331 (Wyo. 1984).

sider and rescind its award of a contract and that, in the absence of fraud or arbitrary action, a court may not interfere with that discretion.[26] Other cases have characterized the award as a "preliminary declaration of intent to enter into a formal contract" that does not in any way limit the unit's future actions or discretion to revoke the award.[27]

## Conclusion

It is not clear which of these approaches North Carolina courts would apply. Several North Carolina cases seem to assume that a contract is binding from the point of the award. These cases dealt with the obligations of the bidder, however, not the awarding authority. As has been shown, these obligations are not identical under the competitive bidding statutes.

Clearly, the formal bidding statute establishes several requirements that occur after the award of the contract: the bidder must provide acceptable bonds, and both parties must execute a written contract.[28] Thus, the rule that the governmental unit is not bound until all of the statutory formalities are completed could be applied in this state. Given the nature of the post-award requirements under the North Carolina statute, however, a bidder could argue that if he or she provides acceptable bonds and executes the contract within the specified period, the awarding authority and its agents lack discretion not to execute the contract.

The question of whether a contractor could recover damages for rescission of a contract award flows from the interpretation of when the contract is formed. If the execution of the contract is a ministerial act, then upon submission of satisfactory bonds and an executed contract, a contractor reasonably may incur expenses (for example, ordering supplies or subcontracting portions of the work) in reliance on the inevitable execution of the contract by the governmental unit. If, on the other hand, the board retains discretion to rescind the award until all of the formalities are completed, it could be argued that a contractor cannot recover any costs incurred before the contract is executed by both parties. Even under these circumstances, a contractor might be able to recover under equitable theories of estoppel or *quantum meruit* if the awarding authority encourages the contractor to incur the expenses or benefits from labor or materials received prior to execution.

A court's analysis of whether a governmental unit is bound by the award of a contract might be influenced by its perception of the unit's reasons for rescinding the award. For example, if the award were rescinded because the successful bidder turned out not to be "responsible" within the meaning of the bidding statute, a court might look more favorably upon the unit's decision not to go forward with the contract. On the other hand, a court might be more inclined to find that the unit is bound by the award if the authority simply changed its mind for reasons unrelated to the actions of the bidder, in effect weighing the asserted reason for rescission against the reasonable expectations of the successful bidder.[29]

To avoid liability and perhaps to clarify the unit's intent, standard language could be incorpo-

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26. Schull Constr. Co. v. Board of Regents of Educ., 113 N.W.2d 663, 665 (S.D. 1962). This standard of review is similar to the one the North Carolina Court of Appeals recently endorsed for review of the award decision itself. *See* Kinsey Contracting Co. v. City of Fayetteville, 106 N.C. App. 383, 416 S.E.2d 607 (1992).

27. *See* Philadelphia v. Canteen Div. of TW Services, 581 A.2d 1009, 1012 [citing Wayne Crouse, Inc. v. School Dist., 19 A.2d 843 (Pa. 1941), and Chilli v. School Dist., 6 A.2d 99 (Pa. 1939)].

28. One could argue that the statutory writing requirement is satisfied by the bid documents, together with the written manifestation of the contract award (usually the minutes of the meeting at which the award was made and the written notice thereof delivered to the successful bidder). However, the language in N.C. GEN. STAT. § 143-129 requiring the bidder to provide sufficient bonds and to execute a contract within ten days of the award clearly indicates that additional acts must occur after the award. It also seems to suggest that a separate contract document (in addition to the bid documents and award decision documentation) must be executed.

29. *Compare* Dedmond v. Escambia County, 244 So. 2d 758, 760 (Fla. 1971) (change of mind by board members held insufficient basis for rescission of lease award) *with* Mann v. Rochester, 63 N.E. 874, 876 (Ind. Ct. App. 1902) (after award and before execution of contract, board retains discretion to act on opinion as to contractor's ability, promptness, and fidelity).

rated into the award resolution and bidder instructions specifying that the award represents a preliminary determination as to the qualification of the bidder, and that no legally binding acceptance of the offer occurs until the awarding authority executes the contract.

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