

**Lexpert U.S. Cross-Border Litigation Guide
THE FEDERAL ACCOUNTABILITY ACT
AND DOING BUSINESS IN CANADA:
NEW LITIGATION POINTS TO PONDER**

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I. INTRODUCTION

Many international companies, particularly those based in the U.S., are important suppliers to the Canadian Government. As a result of international free trade agreements such as NAFTA and the *WTO Agreement on Government Procurement*, vendors outside of Canada generally have non-discriminatory access to a wide range of Canadian Government contracts. Recently, for example, the Canadian Government announced the purchase of four Boeing C-17 Globemaster transport planes, with related in-service support, at a cost of \$3.4 billion. More recently, the Government has reportedly decided to award a \$4.9 billion contract to Lockheed Martin for the purchase of 17 C-130J cargo aircraft and related support services².

However, the awarding of contracts by the Canadian Government has become increasingly litigious over the past few years. Many well known companies have shed their traditional reluctance to protest an unfair contracting process. This is due, in part, to the increased availability of remedies at the federal level through the Canadian International Trade Tribunal (CITT). Many bid protests have been successful before the CITT, and there is also a growing body of common law defining the Government's obligations of fairness during a tendering process.

Government servants are charged with a difficult task, and they do try to carry out their jobs correctly and with integrity. However, improprieties in the awarding of government contracts do occur, and they are unlikely to disappear. Such is human nature, and human error. In both the United States and Canada, there are extreme examples of individuals abusing the procurement process. These cases teach us something about why rules and processes that are intended to protect the integrity of government contracting seem inevitably to fail.

In July 2003, three units of Boeing were banned by the U.S. Air Force from seeking launch contracts because of their unlawful possession of thousands of pages of Lockheed Martin proprietary documents during the 1998 competition for the Evolved Expendable Launch Vehicle. Criminal charges were laid against two former Boeing officers³, and litigation ensued with Lockheed Martin. This infraction led Boeing to develop rigorous internal policies and protocols to ensure corporate oversight and accountability, the terms of which were set out in the 1995

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² Ottawa Citizen, April 4, 2007, "Lockheed Wins \$4.9 Billion Contract". It should be noted, however, that these contracts have not gone without controversy, including questions about the Government's need for such aircraft, and whether other qualified suppliers have not been given a fair opportunity to compete.

³ Statement of Deputy Attorney General Paul J. McNulty before the Senate Committee on Armed Services (2006).

*Interim Administrative Agreement Between The Boeing Company And The United States Department of The Air Force*⁴.

In another case, a former Chief Financial Officer of Boeing received a 4-month prison sentence for holding improper job talks with a senior acquisitions executive for the U.S. Air Force, Darleen Druyun, while she still had influence over contracts involving the company. Ms. Druyun pleaded guilty to charges of corruption for giving Boeing special treatment while negotiating jobs for herself and family members. Ms. Druyun received a prison term and other sanctions.⁵

In Canada, a massive federal government contracting scandal first came to light in 2002, and became known as the “sponsorship scandal”. The resulting investigations, and findings of individual fraud, dishonesty and widespread systemic failures, were very brutal for the Government.⁶ People were convicted of fraud, and the incumbent Government lost an election. After the election, Canada’s newly elected Government enacted the *Federal Accountability Act* (“*Fed AA*”) as one of its first priorities.⁷

The *Fed AA* is wide-ranging legislation whose ambitious goal, as described by the Prime Minister is nothing less than to “...change the way business is done in Ottawa [Canada] forever”⁸. This is perhaps a slight overstatement of the likely impact – there is an old saying that only diamonds are forever.⁹ However, the legislation is an ambitious attempt to address the systemic failures and ethical lapses in the Government’s management of public funds that the sponsorship scandal appeared to reveal.

A complete review of the litigation points arising under the *Fed AA* is far beyond the scope of this paper. However, this paper considers several points that should be of interest to potential suppliers:

- Commitment to fairness, openness and transparency
- The reach of the Auditor General into the private sector
- Anti-corruption and collusion measures to be promulgated in regulations
- Potential for litigation under the *Access to Information Act*
- Lobbying
- The creation of a Procurement Ombudsman as a potential remedy
- The proposed adoption of a *Code of Conduct for Procurement* and the legal implications for suppliers

⁴ U.S. Department of Defense News Transcript, March 4, 2005, presented by Acting Secretary of the Air Force Peter B. Teets.

⁵ Wall Street Journal, February 18, 2005.

⁶ See R. Lunau and P. Pompeo, “Government Accountability in Canadian Procurement: A Matter of Trust”, *International Government Contractor* (Thompson/West, Vol. 3, No. 5, May 2006).

⁷ The *Fed AA* was passed by Canada’s House of Commons on June 21, 2006 and received Royal Assent on December 12, 2006.

⁸ Quote from Stephen Harper, published in Government of Canada, *Federal Accountability Act and Action Plan: Turning a New Leaf* (pamphlet) (Ottawa: April 11, 2006).

⁹ I. Fleming, *Diamonds Are Forever* (Jonathan Cape, 1956).

II. WHAT THE CANADIAN GOVERNMENT BUYS

It is perhaps useful to begin with an overview of Canadian Government purchases. Procurement of goods and services represents a very significant portion of federal public spending overall. Many large federal contracts are governed by international treaties, such as NAFTA, which have the force of law in Canada and ensure that foreign-based suppliers have non-discriminatory access to a wide range of contracting opportunities.

The available figures are not entirely current, but the Canadian Government purchases approximately CDN\$13 billion a year in goods and services. Roughly CDN\$10 billion of these purchases is administered through the Government's central purchasing agency, the Department of Public Works and Government Services Canada ("PWGSC"). The Government uses the awarding of large contracts as leverage to promote its national industrial strategy, expecting vendors to generate offsetting benefits for Canadians, such as employment, investments, knowledge transfer, etc.

National defense represents the largest single area of expenditure. For example, in 2005/2006, the Department of National Defense accounted for more than 50% of federal government purchases, with the value of awarded contracts exceeding CDN\$7 billion.¹⁰ This trend appears set to continue into the foreseeable future, with the Government recently announcing major equipment acquisitions for the Army, Navy and Air Force.

The top ten goods and services purchased by the Canadian Government in 2005/06 included: firmware, software, supplies and support; communications, detection and coherent radiation equipment; aircraft and structural frame components; fuels, lubricants, oils and waxes; aircraft components and accessories; ground effect vehicles, motor vehicles, trailers and cycles; instruments and laboratory equipment; ammunitions and explosives; medical, dental and veterinary equipment and supplies; and clothing, individual equipment and insignia.

III. IMPACT OF THE FEDERAL ACCOUNTABILITY ACT

Even before the *Fed AA*, there was an increasing frequency of bid protests and related litigation over contract awards. This resulted in a procurement system that many suppliers and consultants felt had become too hide-bound and overly preoccupied with technicalities and formalities. The *Fed AA* adds a whole new overlay of restrictions, rules and regulations. It is therefore to be expected that the procurement process will continue to grow more legalistic, technical and lengthy. This trend can be seen in the increasing tendency of PWGSC to use third party fairness monitors and to obtain legal advice before announcing contract awards.

It is also quite possible that the *Fed AA* will result in more litigation rather than less, for the simple reasons that it provides new possible grounds for legal action, and that the more rules there are, the more likely it is that a rule will be broken.

¹⁰ PWGSC Procurement Statistics, FY 2005/2006

It is difficult to argue against the idea that if “accountability” in government contracting is good, then more accountability must be even better. Bringing a case before the Courts is one way that suppliers are able to hold governments accountable. The flip side of the coin, however, is that the fear of a legal challenge can virtually paralyze the procurement process with increased costs and delays.

IV. FED AA CHANGES THAT WILL AFFECT DOING BUSINESS IN CANADA

- **Fairness, Openness and Transparency**

Section 313 of the *Fed AA* adds a new section to the *Financial Administration Act* as follows:

The Government of Canada is committed to taking appropriate measures to promote fairness, openness and transparency in the bidding process for contracts with Her Majesty for the performance of work, the supply of goods or the rendering of services.

“Fairness, openness and transparency” are the traditional, overarching principles of Canadian Government procurement. What, then, does it mean to embody these principles in a statute?

The obligations of fairness, openness and transparency existed under administrative law before the *Fed AA* was enacted, and were embodied in the international trade agreements noted above. These principles were also contained in published Government policies such as the Supply Policy Manual of PWGSC and Treasury Board’s “Values and Ethics Code for the Public Service.”

Nonetheless, the above provision of the *Fed AA* enshrines this commitment into law, and this may be legally significant to suppliers for several reasons. First, and most obviously, by enacting this commitment in law, the Government makes a stronger statement of principle. Secondly, because the section is contained in a statute, it must have some legal significance. Courts may therefore be called on in future litigation to give content to this commitment to “fairness, openness and transparency in the bidding process...” Courts may have to decide important issues such as whether this commitment creates positive duties on the Government to take “appropriate measures”; whether a party can rely on this provision to compel the Government to take some action; what is the content of “fairness, openness and transparency”; whether the section is merely an unenforceable declaration of intent by the Government; and to whom any duty that arises under this provision is owed?

We expect that, in future Court challenges of contract awards, reliance will be placed on this section of the *Fed AA* to buttress arguments that the Government has a positive obligation to be fair, open and transparent to bidders.

- **Auditor General**

Of interest to entities that receive Canadian Government grants and contributions, is the expanded powers and immunities of the Auditor General of Canada. The *Auditor General Act*

has been amended to expand the powers and immunities of the Auditor General beyond examining Public Accounts and Crown corporations. While the *Fed AA* specifies that contracts for the performance of work, the supply of goods or the rendering of services are not subject to these expanded investigatory powers, the reach of the Auditor General's powers has been extended to include auditing the recipients of most government grants and contributions. Such audits include not only the keeping of adequate records and accounts, but also auditing value received for Government monies spent.

The Auditor General and her staff have been given corresponding immunity from criminal or civil proceedings, including protection from defamation suits. The ability of an organization to sue the Auditor General for statements made in a report is therefore limited to non-existent, despite the negative publicity that can result from an Auditor General investigation.

- **Anti-Corruption and Collusion Measures**

In addition to the existing prohibitions in the *Competition Act* against collusion in the submission of bids¹¹, the *Fed AA* allows Cabinet¹² to make regulations that, *inter alia*:

- prohibit payment of lobbyists by way of contingency fees;
- require public disclosure of information about contracts worth more than \$10,000;
- reduce corruption and collusion in the bidding process; and
- require bidders to declare that they have not committed certain criminal offences.

To date, no regulations have been published, but the Cabinet has been given broad powers to regulate in these areas. This is accordingly something to watch, to see what regulations the Cabinet may eventually promulgate.

- **Access to Information**

New legal rights and obligations have been conferred on suppliers who sell to Crown corporations and their subsidiaries. Federal Crown corporations, their subsidiaries, and certain other Government offices and entities, have been made subject to the *Access to Information Act*.

It is typical in Canada for competitors to request disclosure of successful bids under the *Access to Information Act*, including financial information contained in those bids. In the case of *Minister of Public Works and Government Services Canada v. Hi-Rise Group*¹³, the Federal Court of Appeal held that the confidentiality attaching to a bidding process ceases to apply once the process is completed, and that bidders should not expect the terms upon which they are prepared to contract will be insulated from the Government's disclosure obligations.

¹¹ *Competition Act*, R.S.C 1985 c. C-34, s. 47(2).

¹² In Canada, the Cabinet is composed of the high-ranking officials that are part of the Executive Branch of the federal government, i.e., Prime Minister and Ministers of federal government department appointed by the Prime Minister.

¹³ 2004 FCA 99. See also *Soci t  Gamma Inc. v. Canada* (1994), 56 C.P.R. (3d) 58, at 64.

By extending the applicability of the *Access to Information Act* to Crown corporations and other entities, the *Fed AA* not only creates the possibility for suppliers to seek information about these organizations, and about competing bids to these organizations, but also raises the possibility that suppliers will become involved in contesting the release of information relating to them. This accordingly has expanded the potential for bidders to be drawn into litigation over the disclosure of information under the *Access to Information Act*.

The *Fed AA* has also increased the scope of information that does not have to be disclosed under the *Access to Information Act*. This includes:

- information that could interfere with negotiations or injure the financial interests of a government institution;
- trade secrets or confidential financial, commercial, scientific or technical information belonging to Canada Post, Export Development Canada, Public Service Pension Investment Board, or Via Rail;
- information under the control of Atomic Energy Canada other than information about its general administration or the operation of a nuclear facility; and,
- information relating to an on-going investigation being conducted by the Auditor General, Information Commissioner, Privacy Commissioner, Official Languages Commissioner or Chief Electoral Officer.¹⁴

The meaning, scope and applicability of these exemptions will also have to be tested through future litigation.

- **Lobbying**

Businesses that use lobbyists (both in-house and consultants) have to take note that the *Fed AA* amends the *Lobbyists Registration Act* (renamed *Lobbying Act*) by requiring lobbyists not only to publicly disclose their clients, but also to provide monthly reports of their communications with designated public office holders (“DPOHs”). The Commissioner of Lobbying also has authority to verify a lobbyist’s monthly report by contacting DPOHs.

The penalties and sanctions under this new legislation have been increased from its predecessor legislation. Companies would therefore be wise to ensure that internal guidelines exist to properly track and record their dealings with government officials¹⁵.

- **Procurement Ombudsman**

¹⁴ However, information related to investigations can be disclosed once investigations or proceedings are concluded.

¹⁵ Sean Moore, Henry Brown, *The Federal Accountability Act and You*, Gowlings-Jarilowsky Chair in Public Management Seminars (slides), April 2007; T. Burke and P. Ngo, *The Federal Accountability Act And Doing Business In Canada: New Pitfalls?*, article to be published in International Bar Association, Summer 2007

One of the more innovative measures under the *Fed AA* is the creation of a Procurement Ombudsman¹⁶. The Ombudsman is responsible for reviewing the fairness, openness and transparency of departmental procurement practices. The Ombudsman can also review complaints from Canadian suppliers regarding the awarding or administration of contracts. The Ombudsman may then investigate such complaints and make recommendations to the Minister of Public Works.

Legal oversight of federal government contracting existed before the *Fed AA*, and obviously still exists. At the federal level, an independent, quasi-judicial tribunal, the CITT, has jurisdiction over a wide range of complaints about federal contracting irregularities. The Federal Courts also have a role to play in supervising the fairness of Government decisions and ensuring compliance with the legal obligations, express and implied, that surround tendering processes. The Ombudsman thus complements the existing legal mechanisms for Canadian suppliers to pursue complaints.

It must be noted, however, that the Ombudsman's role is essentially advisory, and not adjudicative. Nevertheless, the Ombudsman may, in some instances, provide a useful remedy where complaints fall outside the jurisdiction of the CITT for reasons such as the financial threshold of the contract, the expiry of the CITT's short limitation period to file a complaint¹⁷, or where the complaint relates to an issue of contract administration as opposed to the procurement process¹⁸.

It remains to be seen whether the Ombudsman's recommendations can be challenged in Court, or whether a decision by the Minister not to accept an Ombudsman's recommendation can be subjected to judicial review.

- **Code of Conduct for Procurement**

In conjunction with the *Fed AA*, the Canadian Government has promulgated a draft *Code of Conduct for Procurement* (the "*Code*"), for comments by suppliers¹⁹.

The proposed *Code* could have a very significant impact on suppliers from a litigation perspective. The draft *Code* would impose substantial obligations on bidders, and enforce compliance through conditions of contract.

Suppliers would be required to provide certification that they have complied with the requirements of the *Code*. These contractual certifications have been dubbed "integrity provisions". Proposed sanctions for non-compliance with the *Code* include bid exclusion, termination of a contract, and exclusion from future work.

¹⁶ Amendments to the *Department of Public Works and Government Services Act*. As of the date of this article, the Procurement Ombudsman has not been appointed.

¹⁷ The *Fed AA* leaves open the possibility for the government to enact regulations to impose a time period within which a complaint to the Ombudsman can be made.

¹⁸ *Re Complaint Filed by Liftow* (13 October 1999) (CITT)

¹⁹ The government has requested comments from suppliers regarding the *Code*, but it is not yet clear when the *Code* will be published officially or what its final contents will be.

The potential for implementation of the *Code* to result in litigation seems quite large, because it exposes suppliers to allegations of breach of contract and serious sanctions. Compliance with the *Code* would be a potentially costly business. For example, suppliers cannot simply assume that their normal business practices in the private sector (for example, offering gifts and hospitality to clients) are also acceptable when the client is the Government.

One can also foresee a host of legal issues related to enforcement of the *Code*, including the nature and extent of the obligations assumed by suppliers, what constitutes reasonable efforts to comply, the application of the rules of natural justice when sanctions are contemplated, the burden of proof that a breach has occurred, the supplier's lack of intention to breach the *Code*, etc.

The present version of the *Code* appears to leave many obligations only vaguely explained and understood, implementation by contractors would be difficult in practice, and the *Code* is perceived by some commentators as attempting to download responsibilities onto suppliers that properly belong to the Government.

As of now, this is a developing subject that suppliers should monitor.

VI. CONCLUSION

It remains to be seen whether human behavior can be changed by fiat alone. It is sometimes said of a lock on a door that it only keeps honest people honest. A strong legislative framework can certainly assist supervisors and managers in making concrete and tangible change by creating penalties that influence behavior, providing oversight mechanisms that bring problems to the attention of superiors or the public, and imposing negative career consequences on rule breakers.

However, as noted above, problems do not usually arise from the fact that there are not enough laws. For instance, in each of the Boeing, Druyun and "sponsorship" cases, the laws certainly existed to prohibit what happened and then to punish the offenders. However, in each of these cases the laws did not stop a handful of individuals from precipitating the events that occurred.

In the final analysis, the reach of the *Fed AA* may exceed its grasp. It probably won't change the way business is done in Canada forever, but it may do so for the time being at least.

July 20, 2007