# The Long and Winding *Road Tunnel Case*: Compensation for Procurement Damage in Icelandic Law

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## 1 Introduction

For almost a decade an important case on compensation for public procurement damage has been on-going in Iceland. More precisely the case regards a claim for loss of profit due to termination of a tender procedure in 2003 that concerned the making of a road tunnel in northern Iceland (here after referred to as the *Road Tunnel Case*). The case has already led to three district court's rulings and two Supreme Court judgments and is still pending for the third one.[1]

Although the final judgment is still to come, it is worthwhile to reflect shortly on the case. It is the leading Icelandic case on the subject and a description of it thus serves as a complement to Kai Krüger's comprehensive article on compensation for procurement damage, also to be found in this volume. Moreover the case regards interesting questions about tenderers' options to sue for loss of profit and the burden of proof in such cases. Finally the case mirrors an increasing trend in how claims for compensation, in the field of pure economic damage (n. *rene formuestap*), are pursued in Iceland.

## 2 Background

The rules on government procurement in Iceland are laid down in the Act on Public Procurement, No. 84/2007, which implemented Directive 2004/18/EU. When the events of the *Road Tunnel Case* took place in 2003 the act in force was Act No. 94/2001 but the articles on compensation are substantially the same in both acts,[2] i.e. article 84 in the old act and article 101 in the new act. It should also be mentioned that there is a more general act in force, Act No. 65/1993, which is not limited to public procurement procedures. This article however focuses on liability in the public procurement context.

Article 101 of Act No. 84/2007 consists of two sections. Section 1 concerns tenderers' negative interests, i.e. their cost of participating in the procedure (reliance damage), whereas section 2 has bearing on their positive interests, i.e. loss of profit (pecuniary damage).

Section 1 is as follows:[3]

> A contracting authority is liable for damages that violations of this Act, including the provisions of the Directive referred to in the Act, and rules established herein, may cause to economic operators. An economic operator need only prove that it had a realistic possibility of winning a contract and that this possibility was prejudiced by the violation. The amount of compensation

1 It should be mentioned that from 2002 to 2007 the author worked at the law firm representing the claimants in the *Road Tunnel Case*.

2 Parliamentary Record 2006-2007, A-section, p. 1609.

3 Direct quotes from the act are from a translation available at the website of the Ministry of Finance, "www.ministryoffinance.is/media/adrarskyrslur/Act-nr-84-2007-on-Public-Procurement.pdf." Other direct quotes in this article are translated by the author.

> shall be based on the cost of preparing a tender and participating in the tender procedure.

As the text directly indicates the requirements for such compensation are more relaxed than in general and the legislative material directly states that the contracting authority has the burden to proof that a violation has not caused damage to the tenderer.[4] This means, for example, that if it is established that the Act has been violated in the evaluation of tenders, the authority has to prove that it would have been impossible for the relevant tenderer to win the contract. This also means that more than one operator may be able to obtain compensation for the same unlawful action.[5] According to article 97 of the Act, the Public Procurement Complaints Commission, which economic operators may appeal to, "may express its opinion on the liability of the defendant for damages towards the complainant, but shall not express itself concerning the amount of damages". The Commission has often expressed its view that a contracting authority is liable under section 1 of article 101.[6]
Section 2 of article 101 is as follows:

> In other respects, damages resulting from violations of this Act and rules established hereunder shall be governed by general rules of law.

The legislative material states that section 2 is intended to iterate that section 1 does not preclude that tenderers can claim higher compensation than for preparing a tender and participating in the procedure. It goes on:

> More precisely section 1 does not preclude that a tenderer can claim compensation that aims at putting him in the same situation as if the contract had been carried through. In other words it would embody compensation for pecuniary damage, even though contract was never made, and what primarily comes here to inspection is a tenderer's damage due to loss of profit.[7]

The legislative material then refers to a longstanding debate among Nordic academics on the question of whether it is possible to reward damages for positive interests in the case of violation of public procurement rules. It states that the view of limiting a tenderer's right to compensation to his negative interests has generally been rejected and that his right to obtain compensation

4 Parliamentary Record 2000-2001, A-section, p. 4539.

5 *Handbók um opinber innkaup*, Reykjavík 2008, p. 114. Available at the website of the State Trading Centre (Ríkiskaup), "www.rikiskaup.is/media/eplica-uppsetning/HandbokOI_Final.pdf".

6 *See* for example the following recent rulings: *PPCC (Public Procurement Complaint Commission 17 October 2011 (Case No. 20/2011)*, and *PPCC 8 April 2011 (Case No. 27/2010)*.

7 Parliamentary Record 2000-2001, A-section, p. 4539. The legislative material cited here concerns the enactment of article 84 in Act No. 94/2011, but it is also fully relevant to the article now in force (article 101 of Act No. 84/2007), since the articles are substantially the same.

for loss of profit has been recognized. In that respect, it refers to *SC (Supreme Court of Iceland) 18 November 1999 (Case No. 169/1998)*, where the Court awarded a sum of compensation for loss of profit by discretion (it awarded 1.850.000 ISK whereas 4.289.440 ISK was claimed). The legislative material then states that contrary to claims under section 1, a tenderer has to prove such damage in accordance with general rules. It goes on:

> This means, firstly, that he has to prove that he would have been awarded the contract, if there had not been a culpable violation on behalf of the buyer. Not only does this require that a tenderer proves that his tender was the most economically advantageous, but also that the buyer would not have rejected all offers… Secondly, the tenderer has to prove the extent of his damage, for example that he would have made profit from a contract with the buyer. In light of this it is clear that it can involve many complications for a tenderer to litigate a claim like this.[8]

Contrary to section 1, the Public Procurement Complaints Commission has refrained from expressing its view on liability under section 2.[9] The only way to pursue claims for loss of profit is therefore generally before the courts.

In sum, the text of section 2, refers to damages "governed by general rules of law". Although these general rules were not perfectly clear when the article was enacted in 2001, there was a judgment from 1999 that awarded compensation by discretion for loss of profit and the legislative material provided further guidance as to the substance of the general rules. This was the situation when the *Road Tunnel Case* came to play in 2003.[10]

Two more things shall be mentioned before moving to the case and its special features. Firstly, the existence of damage is a peremptory condition of liability for damages in Icelandic law, whether in or out of contract.[11] Secondly, the general way to pursue compensation claims before the Icelandic courts is to claim a certain amount of money. The Act on Civil Procedure, No. 91/1991, however provides an exception in article 25, section 2, which allows plaintiffs to seek judgments of acknowledgement, on the condition that they have legitimate interests in seeking such a ruling.

8 Parliamentary Record 2000-2001, A-section, p. 4339-4540.

9 The *Road Tunnel Case* is a clear example of this, as will be explained in chapter 3.1.

10 It should however be mentioned that the Supreme Court handed down one judgment regarding section 2 in the period between the events of the *Road Tunnel Case* and until the case reached the Supreme Court. This judgment is *SC 26 February 2004 (Case No. 347/2003)*, where the tenderer was not considered to have proven that he would have been awarded the contract in a flawless procedure.

11 *See* for example Örlygsson, Þorgeir, Bogason Benedikt and G. Gunnarsson Eyvindur: *Kröfuréttur II – Vanefndaúrræði*, Reykjavík 2011, p. 188, and Matthíasson, Viðar Már *Skaðabótaréttur*, Reykjavík 2005, p. 595.

## 3 The *Road Tunnel Case*

### *3.1 Generally*

In March 2003 the Icelandic Road Administration invited operators that had been pre-selected to participate in a procedure regarding a road tunnel in northern Iceland (the Héðinsfjarðargöng). The contract specifications stated that the comparison of tenders would be financial only. Four tenders were submitted, the lowest one a joint tender from Íslenskir aðalverktakar hf. (an Icelandic corporation) and NCC International AS (a Norwegian corporation), which was 3,2% higher than the authority's estimated cost. On a meeting of the Icelandic government on July 1, 2003 the government decided to postpone the road tunnel project and with a letter July 8, 2003 the Road Administration announced that it would reject all tenders. The reason given was an "expansionary situation" which was under way in Icelandic society.

The two corporations resorted to the Public Procurement Complaints Commission that declared the decision to reject all tenders unlawful and expressed its view on liability under article 84, section 1, of Act No. 94/2001.[12] It however refrained from doing the same with regard to section 2 of the same article so the corporations resorted to the Icelandic courts.

### *3.2 Round 1 – Claim for an Acknowledgement of Liability*

The corporation filed suit in the District Court of Reykjavík and claimed an acknowledgement of the Road Administration's liability for the corporations' loss of profit due to the rejection of their offer. No particular amount of compensation was claimed at this time. The District Court came to the conclusion that Act No. 94/2001 had been violated. The Road Administration was however acquitted since the corporations had not proven that this caused them damage.[13]

The corporations appealed to the Supreme Court which, in *SC 17 November 2005 (Case No. 182/2005)*, overturned the District Court judgment and found in favour of the corporations. The Supreme Court made it clear that although legal provisions assumed that it might be permissible for a buyer to reject all tenders, and although the contract specifications in this particular procedure expressly reserved such right, this right could not be used unless there were objective and well-founded reasons for doing so. Since this was not the case the decision was considered to have violated Act No. 94/2001. The Court went on to state that in light of the legislative material, article 84, section 2 of the Act had to be interpreted in that way that a buyer which violates the Act might be obliged to pay an operator compensation for loss of profit, on the condition that the operator proves sufficiently that he would have been awarded the

12 *See PPCC 19 August 2003 (Case No. 18/2003)*.

13 *See DCR (District Court of Reykjavík) 15 April 2005*.

contract if the Act had not been violated and that the violation thereby has caused him damage.

The Court referred to the provision in the contract specifications stating that the comparison of tenders would be financial only. It went on by noting that the two corporations had submitted the lowest tender, which was significantly lower than the second one, and that there was nothing to indicate that the authority would have had reason to reject the tender on the grounds of price. And by choosing this particular operators for participation in the procedure, the authority had taken the view that they were generally competent to take on the project. In light of this and the provision of the contract specifications, the burden of proof had to be shifted to the authority, which needed to prove that the corporations would not have been awarded the contract if the procedure had not been terminated. The authority had not proven this and for that part the conditions of article 84, section 2 were met. The Court went on:

> By this lawsuit [the corporations] have used the possibility in article 25, section 2 of the Act on Civil Procedure, No. 91/1991, to seek for the time being only an acknowledgement of [the authority's] liability. Before the Supreme court [the corporations] have brought forward source material concerning premises for the calculations of their tender […], which expected a certain profit of the project. It has also to be considered that the tender was higher than [the authority's] estimated cost, but the estimate must have presumed that the prospective contractor would have some profit from carrying through the project. By this, [the corporations] have adequately brought forth a probability of damage which article 84 can cover. Article 25 of Act No. 91/1991 does not preclude an acceptance of their claim, but this only resolves the legality of [the authority's] actions without any ruling on to what extent the action has caused [the corporations] damage.

The conclusion of the judgment started like this:

> The [authority's] liability towards [the corporations], due to loss of profit that they might have enjoyed if [the authority's decision] had not been taken, is acknowledged.

### *3.3 Round 2 – Claim for a Certain Amount of Compensation*

Following the Supreme Court judgment the parties engaged in negotiations that proved not to be successful. The corporations therefore filed another suit (this time against the Icelandic state) in the District Court of Reykjavík and now claimed a certain amount of compensation. They mainly claimed 478.868.309 ISK (in solidum), on the grounds of their calculations based on the contract specifications. More precisely the corporations estimated the cost of the project on the one hand and the income of the project on the other hand and claimed the disparity. They also set forth a second claim, 258.955.156 ISK, on the grounds of a valuation performed by two experts (one engineer and one accountant), who were appointed by the District Court at the corporations' request. The state objected that the corporation had suffered damage. Among

other things the state contested the valuation of the experts, referred to the fact that the Norwegian corporation did not participate when the procedure was repeated, that the Icelandic corporation had carried through other large projects at the relevant time etc.

In a ruling in 2010, the District Court of Reykjavík dismissed the case on the grounds that the source material provided was utterly inadequate for passing a substantial judgment on the corporations' claims.[14] The corporations appealed this ruling and in February 2011, in *SC 4 February 2011 (Case No. 718/2011)*, the Supreme Court overturned it and prescribed the District Court to address the case substantially. Subsequently the District Court delivered a judgment in June 2011, where the Icelandic state was acquitted.[15]

The District Court firstly explained that its understanding of *SC 17 November 2005 (Case No. 182/2005)* was that the corporations had adequately brought forth a probability of damage and that the state was obliged to pay compensation for the loss of profit that the corporations might have gained had the decision not been taken. However, nothing had been declared as to what extent the corporations had sustained damage and it was up to them to prove the damage's extent, in this case their presumed loss of profit due to the rejection of their offer. The District Court also stated that it followed from article 84, section 2 of Act No. 94/2011, that general rules of compensation had to been taken into account, including the rule that the claimant has to mitigate his damage and should not be put in a better position than if the damage had not occurred.

The Court then turned to evaluation of the corporations' claims. It first rejected the main claim on the grounds that the corporations' estimate and the related calculations were not sufficient evidence of the corporations' damage, and were even further away from proving that the damage measured up to the specific amount claimed. The Court then rejected the second claim on the grounds that the two experts who performed the valuation had relied on the same insufficient source material and that their method for calculating loss of profit was precarious. In this respect the District Court referred to the experts' presumption that the profit would have been the same as shown in the Icelandic corporation's financial statement 2004. However, no information had been made available on the corporation's projects this particular year or on whether this profit would have been gained in other projects that could in some respect be considered comparable to this one. In addition, no information had been made available on the Norwegian corporation's projects or profit this particular year. Taking this into consideration the District Court came to the conclusion that it could not rely on the two experts' valuation. At the end of the judgment the Court remarked:

> The plaintiffs' view can be sustained, that it is difficult for them to prove their veritable damage due to the defendant's decision to reject their tender for the making of Héðinsfjarðargöng. Notwithstanding their statement that it is

14 *DCR 9 December 2010 (Case No. E-7123/2007)*.

15 *DCR 28 June 2011 (Case No. E-7123/2007).*

> impossible to acquire more material and that their claim cannot be arranged in another way than described above, the Court nevertheless considers that both plaintiffs possess various information and material about their operation, projects and profit at the relevant time, including from their accounting, which can be assumed to have been better suited for supporting their claims and other pleadings. Not least, the Court in this respect takes into view that no information is available about NCC International AS's projects at the relevant time, nor about the corporation's experience in the field of building tunnels or similar projects, let alone its profit from such projects. The plaintiffs could easily have acquired and provided such material. They did, however, not do so, but chose instead to found their claims on the material that has been provided. As a consequence it has to be considered as not proven that the plaintiffs suffered damage due to the defendant's decision to reject their tender for the making of Héðinsfjarðargöng. For the same reason there is not a ground to determine compensation to the plaintiffs by discretion. The defendant will therefore be acquitted of all the plaintiffs' claims.

The corporations appealed this District Court Judgment and litigation will soon take place before the Supreme Court.

## 4 Remarks

In addition to being the leading case in the field of public procurement damage, the *Road Tunnel Case* can be seen as one of the leading cases in an increasing trend in Iceland in the field of pure economic damage. More precisely the trend is to suit first for an acknowledgment of liability, before claiming a certain amount of compensation (both in and out of contract). This was not the first case where the Supreme Court acknowledged liability in that way,[16] but it is an important case in the line of such judgments, which have grown significantly in number after the 2005[17] judgment.[18] Importantly, many big cases related to the bank collapse in 2008 seem to be framed in this manner, i.e. the claimants start by pursuing an acknowledgment of liability, before claiming a certain amount of compensation.[19]

The possibility to suit for an acknowledgement of liability can in many ways be beneficial to claimants. It can allow them to obtain results on the legality of their counterpart's actions, without first having to undertake the often complicated and expensive process of proving a certain amount of damage (which often would be done by obtaining valuation by experts). It must however be stressed that although this might be seen as a fairway in

16 *See* for example *SC 13 February 2003 (Case No. 384/2002).*

17 *SC 17 November 2005 (Case No. 182/2005)*.

18 Later judgments are for example *SC 23 February 2006 (Case No. 371/2005)*, *SC 8 May 2008 (Case No. 450/2007)*, *SC 3 June 2010 (Case No. 43/2010)* and *SC 17 November 2011 (Case No. 87/2011)*.

19 Some of these cases have already reached the Supreme Court, see *SC 25 November 2009 (Case No. 600/2009)* and *SC 25 November 2009 (Case No. 601/2009)*.

comparison to some other jurisdictions, at least in the field of compensation for positive interests in public procurement procedures, the claimant nevertheless must overcome severe obstacles before being awarded a certain amount of compensation. Firstly, he must prove damage to a certain extent to be able to obtain an acknowledgment of liability. Secondly, after receiving such an acknowledgement, he still has to prove the amount of his damage. Some remarks on the burden of proof at both stages are appropriate.

As regards the former stage, the first Supreme Court judgment in the *Road Tunnel Case*, i.e. *SC 17 November 2005 (Case No. 182/2005)*, illustrates that the requirement to prove damage is more relaxed in a case of an acknowledgment than in general. Thus, the Court declared that the corporations had brought forth a probability of damage that was adequate for acknowledging liability. The Court has elaborated further on the requirement of proof in later cases and these judgments make it clear that although this requirement only concerns probability, it can preclude claimants from seeking an acknowledgment. A clear case on that point is *SC 19 February 2010 (Case No. 68/2010)*, where an Icelandic corporation sued for an acknowledgment of the State Trading Centre's liability for rejecting its tender in a procedure. The Supreme Court remarked that according to its case law article 25, section 2 of the Act on Civil Procedure, No. 91/1991, requires that the claimant adequately bring forth a probability of damage which he has suffered and explains what this damage consists of. Since the claimant had not done so, the case was dismissed. Similar judgments in other cases of pure economic loss, outside the field of public procurement, can also be found.[20] These judgments make clear that this requirement is in fact a procedural one, linked to article 25 of Act No. 91/1991. If the claimant fails to adequately bring forth a probability of damage the result is therefore a dismissal of the claim, rather than an acquittal.[21]

In regards the latter stage, the most recent District Court judgment in the *Road Tunnel Case*, i.e. *DCR 28 June 2011 (Case No. E-7123/2007)*, illustrates that a judgment of acknowledgement does not leave the claimant with an easy task to obtain a particular amount of compensation. The claimant still has to prove that he has suffered damage of that amount and the case is informative on the problems he may face and the complicated questions that can arise in the assessment of damage. The District Court placed high demands on the plaintiff. High demands are in line with the general approach in the field of pure economic loss, where claims are often rejected on the grounds that damage has not been proven. It remains to be seen whether the Supreme Court will adhere to the District Court's approach or whether it will accept the plaintiffs' argument that is impossible to acquire better evidence or arrange the claims in another way. The Court might also take some kind of an intermediate position

20 See for example *SC 25 November 2009 (Case No. 600/2009)*, *SC 25 November 2009 (Case No. 601/2009)*, *SC 17 December 2009 (Case No. 698/2009)*, *SC 20 August 2010 (Case No. 435/2010)*, *SC 11 April 2011 (Case No. 187/2011)* and *SC 12 April 2011 (Case No. 188/2011)*. On the other hand this requirement was met in *SC 19 March 2010 (Case No. 129/2010)* and *SC 10 March 2011 (Case No. 57/2011)*.

21 This was expressly stated in *SC 17 November 2011 (Case No. 87/2011)*.

by awarding a lower sum of compensation by discretion, along the lines of *SC 18 November 1999 (Case No. 169/1998)*.

Although it is clearly the plaintiff who bears the burden of proof, and the defendant must be acquitted if the plaintiff cannot prove damage, such an end to the longstanding *Road Tunnel Case* might be seen as somewhat peculiar, bearing in mind that the existence of damage is a peremptory condition of liability for damages. The courts would then first have acknowledged an existence of liability, but then rejected compensation since damage was not proven – notwithstanding that the existence of damage is a general precondition for the existence of liability. [22]

22 It should however be mentioned that there are judgments in the field of pure economic loss where the Supreme Court has first declared that liability for damages exists, if the plaintiff can prove damage, but has then acquitted the defendant on the grounds that damage has not been proven. *See* for example *SC 18 October 2007 (Case No. 141/2007)* and *SC 22 January 2008 (Case No. 239/2008)*. Although it is therefore not unprecedented that the Court first declares liability but then denies compensation due to lack of proof, the wording in the 2005 *Road Tunnel judgment* can be seen as little bit different than in the two cases mentioned above, as well as in an older judgments of acknowledgment, i.e. *SC 13 February 2003 (Case No. 384/2002)*. In the 2003 judgment the Supreme Court thus stated that the judgment only concerned the legality of the relevant actions, without any ruling on "whether" these actions caused damage to the plaintiff, whereas in the 2005 judgment the Court stated that there was no ruling on "to what extent" the action caused damage to the plaintiffs.