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Construction Bidding and Tendering: Principles and Practice

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The law affecting the competitive process of bidding or tendering for a construction project was a sleepy legal backwater in Canada for at least a century or so – until 1981. A decision of the Supreme Court of Canada in that year turned things upside down and was followed by a flood of litigation, which now seems to be subsiding. What happened, and what has changed?

It is important to stress that the following overview is not an opinion regarding the correctness of the court decisions discussed, nor does it contain legal advice. It reviews the issues *exclusively* from the point of view of industry usage and common sense.

Reliance on common sense is supported by a statement made by Lord Atkin of the House of Lords back in 1932, in the famous *Donoghue v. Stevenson* decision. Talking about the English (and therefore also Canadian) Common Law, His Lordship said:

> *It will be an advantage to make it clear that the law in this matter, as in most other, is in accordance with sound common sense.*

This is something that the law and good construction practice have in common.

THE OPENING PHASE: MISTAKE IN BID

The starting point of the upheaval in 1981 was a deceptively simple question:

> *Should a bidder who submits a bid containing a significant but honest mistake be allowed to withdraw?*

An *"honest mistake"* is one where the bidder can prove to the owner that it has made a miscalculation or some such error affecting the bid price.

The construction industry's answer at the time was clearly expressed in the CCDC[2] 23 *"Guide to Calling Bids and Awarding Contracts"*:

> *If a bidder informs the [owner] promptly after bid closing and before acceptance that a serious and demonstrable mistake has been made in his bid and requests to withdraw, he should normally be allowed to do so without penalty.*

There are good and well known reasons for this recommendation as noted below.

The pre-1981 Common Law approach to this issue was set out in the case of *Belle River Community Arena Inc. v. W.J.C. Kaufmann Co. Ltd*. In 1973, Kaufmann submitted a bid to Belle River and soon after opening informed the owner that it wished to withdraw because there was a mistake in its bid. *Belle River* nevertheless accepted the bid. Kaufmann stood by its decision to withdraw. Belle River signed a contract with the next lowest bidder and sued Kaufmann for the difference in price. The trial judge wrote:

> *The authorities establish that an offeree [owner] cannot accept an offer which he knows has been made by mistake and which affects a fundamental term of the contract.*

In 1978, the Ontario Court of Appeal agreed with the trial judge. *"The purported offer, because of the mistake, is not the offer the offeror [bidder] intended to make, and the offeree [owner] knows that,"* said Justice Arnup, speaking for the Court.

So, the Common Law and the construction industry's common sense recommended practice were a good match – before the **Big Bang**, the first phase of a major expansion of the law of bidding and tendering.

THE BIG BANG

The law changed drastically in 1981 as a result of the decision of the Supreme Court of Canada in *R. v. Ron Engineering & Construction (Eastern) Ltd*.

The case involved essentially the same issue as in *Belle River*: Ron Engineering submitted a bid to Her Majesty the Queen in right of Ontario and the Water Resources Commission – the owner, for short. Ron's bid was the lowest but, soon after bid opening, Ron advised the owner that it contained an honest mistake. Still, the owner awarded the construction contract to Ron. When Ron refused to sign that contract, the owner retained Ron's bid deposit of $150,000 and awarded the contract to the second lowest bidder.

Ron sued but lost at trial, and appealed. The Ontario Court of Appeal followed its own decision in *Belle River*, so Ron won.

The Supreme Court of Canada had the last word. Justice Estey, writing for the Court, decided that much more was at stake than the bid bond the parties were arguing about:

> *… the integrity of the bidding system must be protected where under the law of contracts it is possible so to do.*

Until that fateful date in 1981, an owner's call for bids was simply an invitation to submit offers. If and when an offer (i.e. bid) was accepted by the owner, the parties entered into a construction contract.

Justice Estey discovered a new contract: the bidding contract. He called it Contract A to distinguish it from the construction contract, which he called Contract B:

> *Contract A … comes into being forthwith and without further formality upon the submission of the tender ...*
>
> *The principal term of contract A is the irrevocability of the bid, and the corollary term is the obligation in both parties to enter into a contract (contract B) upon the acceptance of the tender.*

In other words, submitting a bid in response to an owner's invitation creates a contractual relationship between bidder and owner. The construction contract may, or may not, follow.

Would Ron have submitted the same bid, or any bid at all, had it known that its bid was irrevocable even if it contained an honest mistake – never mind industry practice and the *Belle River* precedent? Perhaps. But that question never came up. Justice Estey took care of the mistake. He made it vanish:

> *There is no question of a mistake on the part of either party up to the moment in time when contract A came into existence. The [bidder] intended to submit the very tender submitted, including the price therein stipulated.*

Since there was no mistake, Ron had refused to enter into Contract B with Her Majesty for no valid reason. That was a breach of Contract A. The owner was entitled to keep Ron's bid deposit.

The Court allowed one exception to the general rule regarding the formation of Contract A: a mistaken bid can be withdrawn if the mistake is *"on the face of the bid"* i.e. if it is immediately apparent when the bid is opened.

On the other hand, even if the owner is made aware of a mistake in price moments after closing, and shown evidence that the mistake was an honest one, Contract A is in place and the bid cannot be withdrawn. The integrity of the process must be protected, even if the outcome does not rhyme with common sense.

WHAT ABOUT CONTRACT B?

A mistake in the bid price, invisible when Contract A comes into existence, inevitably reappears when the time comes to sign Contract B. Both parties know that the price is wrong, and the bidder wants out. How can there be a construction contract? Surely, this is an essential issue to consider before a drastic change in the law? But Justice Estey pushed it aside, to be decided at some future date:

> *The effect a mistake may have on the enforceability or interpretation [of Contract B] is an entirely different question, and one not before us. Neither are we here concerned with a question as to whether a construction contract can arise between parties in the presence of a mutually known error in a tender ...*

Almost seven years went by before this and related issues were finally addressed by the Supreme Court in *Calgary (City) v. Northern Construction Co*. In 1979, Northern had made a mistake in its bid. The owner agreed that there was *"no impropriety, dishonesty or fraudulent motive"* involved. When Northern refused to enter into Contract B, the owner claimed the difference between Northern's bid and that of the second lowest bidder. The trial judge found for Northern. The City appealed.

Justice McDermid of the Alberta Court of Appeal noted a problem facing the bidder as a result of the new law:

> *… the contractor is placed in a dilemma, for if he executes Contract B, I do not think he could then raise the question of mistake, while if he does not do so, he is in breach of Contract A.*

His colleague, Justice Kerans, had another question:

> *Would it be unconscionable for the city, in the circumstances of this case, to proceed to accept contract B after discovering that the offer was made as the result of an innocent and honest error of fact?*

Still, Northern lost in the Court of Appeal for reasons spelled out in the decision. Northern appealed to the Supreme Court,

but had no luck. In 1987, it took the Court all of four paragraphs to deal with Northern's arguments: the judgment in *Ron Engineering* governed. Appeal dismissed, with costs.

Contract A was thereby cemented in place – with steel reinforcement to be added over the following two decades.

A QUICK LOOK AT DAMAGES

In *Ron Engineering*, the bidder lost its bid deposit of $150,000 which was the limit of its liability under that particular set of bid documents. Fair enough: the owner could not have the work done for the price of the low bid, and one of the purposes of a bid deposit is to compensate the owner for just such an eventuality. In *Northern*, however, the owner successfully sued the bidder for the entire difference between the mistaken bid and the next lowest bid: $395,000.

Justice Kerans of the Court of Appeal observed that the only undeniable loss to the owner was just $213,726 – the difference between Northern's corrected bid and the next lowest bid. That was how much the owner had to pay out *extra* to have the work done. He continued:

> *The balance of the claim of the city, however, is a windfall: it is the $181,274 by which the tenderer's bid was reduced by reason of the innocent error. No loss to the city arises except the loss of the chance to take advantage of the mistakes of others.*

Sounds very reasonable, but still the City was awarded the full $395,000. Members of the construction industry interested in the rationale of this should read the full text of the decision.

So, in the years since *Belle River*, the cost of an honest mistake to the unfortunate bidder skyrocketed from nothing to several hundreds of thousands. A rather extreme example of how expensive a mistake can be for a bidder is the case of *City of Ottawa Non-Profit Housing Corp. v. Canvar Construction (1991) Inc*.

In 1991, Canvar[3] submitted to Ottawa a bid of $2.289 million. Soon after bid opening, Canvar informed the owner that its bid price contained a typo: it should be $2.989 million. Its bid bond was 5% of that amount, as required by the bid documents. The owner's cost estimate for the work was close to $3 million. The second lowest bid was over $3 million.

Canvar refused to sign Contract B. It lost at trial, and the mistake cost the bidder $841,000 on a job worth about $3 million, the difference between Canvar's bid and the second lowest. In 2000, the Ontario Court of Appeal found that the mistake was *"on the face of the bid,"* and that the bid should not have been accepted.

Too late for Canvar, though: it was no longer in business. Killed by a typo.

INDUSTRY STICKS TO COMMON SENSE

What has been the construction industry's reaction to the courts trying to protect the integrity of the bidding process? Apparently, the industry is not so keen to follow suit when it comes to mistaken bids. Almost three decades after *Ron Engineering*, the Canadian Handbook of Practice for Architects, edition 2009, recommends:

> *Infrequently, after the bid closing, a bidder may notify the architect or the client that a serious mistake has been made in the bid, and this contractor should be permitted to withdraw without penalty.*

The recommendation in the CCDC 23 *Guide* regarding mistaken bids has not changed much since the early 1980s. The 2005 edition provides:

> *… if the [Owner] is satisfied as to the existence of a genuine and significant mistake, the bid should not be accepted and the bidder should not be penalized even though the Owner may have the legal right to accept the bid.*

The Committee adds a practical, common sense justification of its position:

> *Forcing an unwilling bidder to perform the contract substantially increases the risk that the work will not be performed satisfactorily, and is therefore unlikely to be in the Owner's best interests, despite the lower initial price.*

It is fairly certain that the money-losing contractor will also vigorously pursue compensation for every perceived mistake in the drawings and specifications, and for every change or delay caused by the owner or its consultants, and rightly so.

CHANGE OF FOCUS

The nature of the bidding process is such that mistakes happen fairly often so the *Ron Engineering* decision caused quite a number of lawsuits but by now the supply of court cases dealing with mistaken bids has almost dried up. Perhaps mistaken bidders obey the law and no longer try to avoid Contract B. Perhaps most owners have decided to observe the practice recommended by the industry, and let the mistaken bidder go. Most likely, both of these responses are in play.

Does this truce mean that litigation in connection with bidding has stopped? Not at all. Only the opening phase is petering out. In 1999, the law entered a new phase, a logical extension of the reasoning in *Ron Engineering* but with a completely different focus.

In this phase, owners finally find out what Contract A requires of them – 18 years after the imposition of the Contract A / Contract B regime. A familiar name suggests itself for this new phase.

THE CLINTONIAN PHASE: NON-COMPLIANT BIDS

Remember Bill Clinton's famous response in 1998 when questioned whether he had improper relations with his intern? *"It all depends on what the meaning of the word 'is' is,"* declared the President. In this second

phase of the bidding and tendering litigation similar acts of verbal finesse play a crucial role, so let us call it the **Clintonian Phase**. The starting point, for this phase, was a question regarding an owner's actions:

> *Is the owner entitled to accept a bid that does not fully comply with the requirements of the bid documents?*

In 1999, the Supreme Court of Canada in *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd*. answered this question in no uncertain terms. Justice Iacobucci, speaking for a unanimous Court, said:

> *I find it reasonable, on the basis of the presumed intentions of the parties, to find an implied term [in Contract A] that only a compliant bid would be accepted.*

The routine privilege clause, found in most bid documents (*"Lowest or any tender not necessarily accepted"*) does not absolve the owner of its duty to accept only a compliant bid, decided the Supreme Court, it only allows it to reject the lowest bid in favour of a more attractive one.

Who can argue with the Court's conclusion, in principle? But the *practical* problem for owners is that, in most cases, a court's decision in a dispute over compliance depends on the exact meaning of some words – as understood or interpreted by a judge. Or the three judges of an appeal court. Or perhaps the nine judges of the Supreme Court of Canada.

The case of *Maystar General Contractors Inc. v. Newmarket (Town)* is an excellent example of the possible consequences.

ARE YOU SURE?

In 2005, the Town of Newmarket in Ontario issued a call for bids for the construction of a recreation facility. At bid opening, Maystar's bid was the lowest; Bondfield Construction Company Ltd. was a close second. The owner reviewed the bids and found that Bondfield had miscalculated the GST amount. The owner recalculated GST based on the bidder's stipulated price, a simple enough calculation. Bondfield's revised total price was now the lowest! The owner's officials and consultants were not sure how to proceed. Was Bondfield's revised bid compliant?

But then the owner's lawyers found a precedent decision: the same GST mistake had already been reviewed by the courts in another Ontario case. In that case, the trial judge found the GST amount *"superfluous and of no significance."* The Court of Appeal agreed with the trial judge:

> *The error in the calculation of the GST… did not make the bid price uncertain. That price was set out in the previous paragraph, and the [GST] calculation was, if not superfluous, at least subordinate.*

Bingo! Newmarket awarded the contract to Bondfield. Maystar sued. It claimed that Bondfield's price was uncertain, making the bid non-compliant. Maystar claimed loss of profit: $3.3 million. Who wouldn't sue?

A judge of the Ontario Superior Court of Justice very carefully examined the bid documents. He found that, in *this* case, the GST calculation was *"neither superfluous nor subordinate … [it was] an operative part of the bid."*

The three judges of the Court of Appeal agreed. Bondfield's bid should have been rejected. The owner settled with Maystar.

So, the owner made the wrong decision. But it was an honest mistake: in a difficult situation, Newmarket tried its best to be fair. Its lawyers relied on what appeared to be a clearly applicable decision of the Court of Appeal. Had the owner awarded to Maystar, Bondfield would most likely have sued and, possibly, won.

How can an owner ever be certain?

MORE ABOUT DAMAGES

In the Clintonian Phase of the bidding and tendering litigation, owners experienced the same upswing in damages as bidders did in the first stage after the *Ron Engineering* decision. The difference is that, for owners, the amount of damages is often in the millions: in most cases, the rejected bidder's recovery has amounted to most or all of its anticipated loss of profit on the contract which it was wrongly denied by the owner. A private owner could be wiped out as a result of an honest mistake!

Often, owners suffer a loss even if they win in court. Take, for example, the 2013 Newfoundland case *R. v. Derek Penney Electrical Ltd.*

The owner received eight bids but disqualified six of them, including the low bid, for non-compliance. Still, it got sued. Penney, the low bidder, took the owner to court and, at trial, argued that its bid was compliant and should not have been rejected. It lost. But the owner lost too, even before the trial started: It was left with only two bids out of eight from which to choose the best candidate for the project, and neither of them was the original low bid!

Or take *Rankin Construction Ltd. v. Ontario.* In 2005, Rankin submitted a bid to the Ontario Ministry of Transportation for a road-widening project. Its bid was lowest by about $1.7 million but it contained an irregularity worth $50,000. The Ministry, fearing a lawsuit by the second-lowest bidder, rejected Rankin's bid and was sued by Rankin for lost profits of $5 million. The Ministry won at trial and, in September 2014, it won again in the Court of Appeal. But was that really a win for an owner who overpaid $1.7 million – and then spent almost nine years defending that decision?

The *M.J.B.* decision of the Supreme Court of Canada was followed by a surge in litigation, probably inevitable in view of the rich prize.

DUTY OF FAIRNESS

The owner's obligations do not end with the requirement to consider only compliant bids. In 2000, the Supreme Court of Canada handed down its decision in *Martel Building*

Ltd. v. Canada, adding even more protection to the endangered species, the Canadian bidder. It found that there is also an implied duty of fairness:

> *… all bidders must be treated equally and fairly. Neither the privilege clause nor the other terms of Contract A nullify this duty.*

The duty of fairness is implied in the bidding process because *"such an implied contractual duty is necessary to promote and protect the integrity of the tender system … [and] to give business efficacy to the tendering process."*

No doubt, fairness is essential. But the *M.J.B.* decision and its legal offspring demand that owners go way beyond fairness. It is not enough for the owner to assess the bids *fairly*, in accordance with the criteria set out in the bid documents. The assessment must also be *correct* when examined by a judge, and conform to his or her interpretation of the criteria. The cost of an error in judgment by the owner is high. On the other hand, if a judge's assessment is found by an appellate court to be incorrect, the cost of the error will still be borne, one way or another, by the owner.

An incorrect decision is rarely the result of an act of unfairness. Most often, it is an honest mistake: a failed attempt to do it right, as in the *Newmarket* case discussed above. But in *M.J.B.*, Justice Iacobucci made it clear that an honest attempt to assess bids fairly is not enough:

> *Acting in good faith or thinking that one has interpreted the contract correctly are not valid defences to an action for breach of contract.*

In other words: You've made your bed, now lie in it. Makes sense, for a commercial contract. But the Court here is not discussing a real, voluntary contract. Contract A is *implied* by the courts based on the intentions of the parties – intentions *presumed* by the Court, that is. Did the parties really intend to turn the ancient practice of selecting a contractor for a construction project into a minefield for both owners and bidders?

Apparently not, considering the efforts made by the parties to escape the Contract A fallout. The law of bidding and tendering enters the Defensive Phase.

BUILDING A FIREWALL

Bidders have had very limited success in their efforts at self-protection but owners do have a strong remedy. Ever since *Ron Engineering*, the routine privilege clause has been growing in size and scope. In addition, the bid documents now also contain a discretion clause which gives the owner the right to waive minor bid irregularities. Most importantly, there is invariably an exclusion of liability (or exculpatory) clause. Or the three are combined in an "omnibus" clause.

An important step in the progress of the Defensive Phase for owners is the 2010 decision of the Supreme Court of Canada in *Tercon Contractors Ltd. v. British Columbia*.

In 2001, the B.C. Ministry of Transportation issued a request for proposals (RFP) for highway construction. The Ministry awarded the construction contract to a well-qualified but non-compliant proponent. Tercon, a compliant competitor, sued. But the RFP contained a strong exclusion of liability clause:

> *… no Proponent shall have any claim for any compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a proposal each proponent shall be deemed to have agreed that it has no claim.*

The trial judge found the exclusion of liability clause ambiguous, and decided in favour of Tercon. The proponent was awarded $3.5 million. The B.C. Court of Appeal disagreed. It found the words of the exclusion clause:

> *… so clear and unambiguous that it is inescapable that the parties intended it to cover all defaults, including fundamental breaches.*

Tercon appealed. Five of the nine judges of the Supreme Court found that the exclusion clause did not, "when properly interpreted," exclude Tercon's claim for damages. Four of the nine Supreme Court judges sided with the Court of Appeal. Their opinion, written by Justice Binnie, is strongly worded:

> *There is nothing inherently unreasonable about exclusion clauses. Tercon is a large and sophisticated corporation. … I would hold that the respondent Ministry's conduct, while in breach of its contractual obligations, fell within the terms of the exclusion clause. In turn, there is no reason why the clause should not be enforced. I would dismiss the appeal.*

In this case, thirteen judges in total reviewed the exclusion clause. Six of them interpreted it one way, seven the opposite way. That is as close as it can get. The six prevailed because five of them were with the top court.

When owners manage to get their exclusion of liability clauses so clearly worded that they can be interpreted only one way – no liability for the owner, no matter what – it is back to pre-*Ron Engineering* times for owners. Bidders, on the other hand, still have all of their Contract A obligations but no remedy against the immune owners.

Would it not be better for the fairness and reasonable certainty of the bidding process for owners to simply declare in the bid documents that they do not wish to enter into Contract A with bidders? That might leave both owners and bidders off the hook, and the industry itself would have to fight unfairness as it has been doing for decades before and after the Big Bang.

BACK TO BASICS – AND BEYOND

More than thirty years have passed since the Big Bang. It is now generally understood in industry that when a bidder submits a compliant bid, it has accepted the owner's offer of a potential Contract B, and so Contract A is in place. By contrast, a non-compliant bid is a counteroffer, and no Contract A is formed. This is a foundation

stone of the *Ron Engineering* edifice, under construction since 1981.

A facet of the already mentioned *Rankin* decision in 2014 may alter this structure and lead to some rebuilding from the ground up. Whether Contract A has arisen, and on what terms, are *"case-specific determinations,"* ruled the Court of Appeal. The terms and conditions of the bid documents must be scrutinized and their terms properly interpreted in each case to determine whether the parties intended contractual relations to arise on the submission of a bid. The Court carefully reviewed MTO's bid documents and found that

> *… it is clear that the parties intended that contractual relations would arise on the submission of Rankin's bid, even if Rankin's bid were non-compliant.*

The Court decided that non-compliance with the bid documents only meant that Rankin could not be awarded Contract B. The significance and implications of this decision, if any, will become clear in the next few months or years, or perhaps decades.

At the same time, courts across Canada will also be busy extending the requirement of good faith and honest performance to Contract B, following the decision, late in 2014, of the Supreme Court in *Bhasin v. Hrynew.*

We live in interesting times.

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* Any views expressed in this article are those of the author and may not necessarily reflect the views of the company.

1 A more detailed version of this Revay Report has appeared in the Construction Law Reports, published by Carswell/Thomson/Reuters, and in Legal Update, a publication of the Canadian College of Construction Lawyers.

2 The initials CCDC stand for Canadian Construction Documents Committee. Formed in 1974, the CCDC is a national joint committee responsible for the development, production and review of standard Canadian construction contracts and guides.

3 Not to be confused with Groupe Canvar Inc. in Montreal.

ERRATUM

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Quantification of Construction Claims – Page 2, Section 3.4 titled *"Measured Mile Method"* was not accurately translated from its original French version. The "measured mile" approach compares actual productivity achieved during unimpacted periods or "normal periods" with the actual productivity achieved during periods affected by the causes alleged. The claimant must demonstrate that the difference in productivity rates is the result of the alleged causes.

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