Tendering Basics

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This paper provides an overview of several important concepts in the law of tendering.

Four areas are examined. First, the Contract A/Contract B analysis. Second, the emergence in the jurisprudence of the ‘nuanced’ approach to costs in bids. Third, the distinctions between a tender and a request for proposal. Finally, the assessment of damages in tendering cases.
I. Contract A/Contract B

In Canada, the tendering process is governed by the Contract A/Contract B analysis established by the Supreme Court of Canada in *R. (Ont.) v. Ron Engineering and Construction (Eastern) Ltd.*, [1981] 1 S.C.R. 111.

“Contract A” is the name given to the contract that comes into existence between a bidder and an owner upon the submission of a compliant bid by a contractor to an owner in response to a tender call.

“Contract B” is the construction contract itself, which comes into existence upon the acceptance by an owner of the lowest compliant bid made by the contractor.

A more in depth discussion of the case that transformed the law of tendering follows.


In *Ron Engineering*, a contractor submitted its tender with a certified cheque for $150,000, as required by the owner’s tender documents. This $150,000 tender deposit was to be returned after the execution of the construction contract and the receipt by the owner of the performance bond and payment bond. The tender documents stated that the tender deposit could be retained if the tender were withdrawn or the contractor refused to execute the construction contract.

After the tenders were opened by the owner, the contractor realized that it had omitted to include over $750,000 from its tender. This error resulted in a bid that was $632,000 lower than the next lowest bid. The contractor immediately forwarded a telex to the owner requesting to withdraw the tender without penalty.

The contractor subsequently maintained that it had not withdrawn the tender, but that the offer was not capable of being accepted because the owner received notice of the error prior to acceptance of the tender. The contractor asserted that it was therefore entitled to recover the tender deposit.

In response to the contractor’s assertion that the tender was not withdrawn, the owner accepted the bid and submitted the construction contract to the contractor. When the contractor refused to enter the construction contract, the owner retained the tender deposit, and accepted the second lowest bid. The contractor commenced an action to recover the tender deposit, and the owner counter-claimed for damages occasioned by the contractor’s refusal to carry out the terms of the tender call.

The trial judge found the owner entitled to keep the tender deposit and dismissed the counter-claim. The Court of Appeal, however, reversed this decision on the basis that the owner could not accept an offer which it knew was made by mistake and which affected a fundamental term of the contract.

The Supreme Court of Canada allowed the appeal from the decision of the Court of Appeal, and restored the trial judge’s decision to allow the owner to retain the deposit. In reaching this decision, the Court looked to the tender documents and determined that there were two contracts created within the tendering process: Contract A and Contract B.

Contract A came into existence automatically when the tender was submitted in response to the tender call. The terms and conditions of the tender documents, including the provisions regarding the withdrawal of tenders, became terms of Contract A. The construction contract, or Contract B, would come into existence when the tender was accepted.

The tender submitted by the contractor complied with the terms of the tender call. The contractor did not submit the tender or its contents by mistake, and nothing on the face of the tender revealed an error. Therefore, there was no mistake or non-compliance to prevent Contract A from forming at the moment the tender was submitted.
The question of whether the tender deposit was rightfully retained by the owner was therefore answered with reference to the forfeiture provisions in the contract. Because Contract A specified the conditions under which the tender deposit was recoverable, and none of these were met, the owner was entitled to keep the tender deposit. The Court acknowledged that the mistake in the calculation of the bid might be relevant to Contract B, however, the issue of Contract B was not before the Court.

In *Ron Engineering*, the Court not only redefined the approach to the tendering law, but also established the irrevocability of tendered bids and the obligation on both parties to enter Contract B upon acceptance of a bid. Further, the Court confirmed an obligation on the owner to accept the lowest compliant tender.

## II. Nuanced View of Costs

Typically a tender will contain a clause known as a “privilege clause.” A privilege clause is designed to provide an owner with greater flexibility with respect to its obligation to accept the lowest compliant bid. The use of privilege clauses was approved by the Supreme Court of Canada in *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] 1 S.C.R. 619.

In *M.J.B.*, an owner invited tenders for the construction of a pump house, the installation of a water distribution system, and the dismantling of a water tank. The tender documents required a lump sum price for the pump house construction and water tank demolition, and a per lineal metre price for the water system construction.

One of the four tenders submitted contained a qualification as to the lineal metre price, such that it offered two price options rather than one. This tender was also the lowest bid, and was accepted by the owner. The second lowest bidder, M.J.B., alleged that the qualification to the price disqualified the tender. M.J.B. commenced an action for breach of contract, claiming that its bid should have been accepted as the lowest compliant bid.

In defending its acceptance of the qualified bid, the owner relied on a privilege clause in the tender documents which stated that “the lowest or any tender would not necessarily be accepted.”

The trial judge found that the qualification invalidated the tender, but that the privilege clause excused the owner from the obligation to award the construction contract to the next lowest bidder. As such, M.J.B. could not claim that it would have been awarded the contract but for the breach.

The trial judge did find, however, that the acceptance of a non-compliant bid was a breach of the obligation to treat all bidders fairly. This decision was upheld by the Court of Appeal, and the owner was ordered to reimburse M.J.B. for the costs of preparing its rejected tender.

At the Supreme Court of Canada, the central issue was whether the privilege clause allowed the owner to disregard the lowest bid in favour of another tender, including a non-compliant bid. The Court held that it was an implied term that only compliant bids could be accepted but that the privilege clause precluded an implied term that the lowest bid had to be accepted.

In discussing the effect of the privilege clause, Mr. Justice Iacobucci stated at para. 46:

> The discretion to accept not necessarily the lowest bid, retained by the owner through the privilege clause, is a discretion to take a more nuanced view of “cost” than the prices quoted in the tenders.

The Court went on to find that the owner breached Contract A by accepting a non-compliant bid, and that M.J.B. would have been awarded the contract had the non-compliant bid been properly disqualified. However, precisely what was meant by a “nuanced view of cost” was left for subsequent cases to consider.

The first important case in this regard was *Sound Contracting Ltd. v. Nanaimo.*
A. Sound Contracting Ltd. v. Nanaimo (City), 2000 BCCA 312

1. Facts

The City of Nanaimo put out a tender for the “Hammond Bay Project.” Sound Contracting had the numerically lowest bid for the project by over $30,000. However, after analysis, the City chose the second lowest bid.

The City had used the services of Sound Contracting on a number of previous occasions. However, one year before this particular contract, the parties had a disagreement over a similar contract that resulted in an arbitration award in Sound Contracting’s favour, which required the City to make an additional payment of over $22,000. As a result, when staff analyzed the tenders on the current project, they were concerned that awarding the contract to Sound Contracting would not result in the best value for the City. After considering the need for on-site supervision, the risk of running legal costs, arbitration expenses, and other additional payments, the staff concluded that the second lowest bidder constituted the best value for the City.

2. Trial

At trial, the judge performed her own analysis of the competing bids and, by applying the same consideration to each contract, concluded that Sound Contracting’s bid was in fact the lowest bid. The trial judge made the assumption that the second lowest bidder would also make the same types of claims as Sound Contracting. The trial judge held that it was improper for the City to conclude that one bidder would claim indirect costs and another one would not. As such, this assumption was certainly an application of an undisclosed criterion and also an inappropriately uneven treatment of the bidders. Accordingly, at trial, Sound Contracting was awarded damages.

3. Court of Appeal

The Court of Appeal overturned the trial judge’s decision. The Court held that the privilege clauses contained in the request for tenders released the City from its obligation to award the work to the lowest bidder. The Court concluded that a higher bidder might be accepted if there are valid, objective reasons for concluding that a better value may be obtained by doing so.

The Court further concluded that whether previous dealings between the parties provided a proper indicator of how a proposed relationship will work out in practice was not up to the Court to decide. The Court should not be substituting its own analysis for that of the owner or staff of the company as long as they have acted fairly and in good faith in determining which tender provided the greatest value based on quality, service and price.

However, the Court warned that the discretion offered by privilege clauses should not be used in such a way to punish or get even for past differences. Whenever the low bidder was not the successful tenderer, additional factors in the analysis must be shown to be reasonable and relevant. As such, the Court concluded that the City acted in good faith and was fair to all bidders and accordingly they were allowed to select the second lowest bidder.

4. Commentary

Sound Contracting confirmed that, where a privilege clause is employed, an owner need not necessarily select the lowest bid submitted, but can take other factors into account in choosing the successful bidder.

While a privilege clause permits the owner greater flexibility in assessing the ‘cost’ of a bid beyond the price, it does not allow an owner to award the contract to anyone. M.J.B. established that while
privilege clauses may allow an owner to accept bids other than the lowest by taking a “nuanced view of cost,” various implied terms restrict the owner’s discretion. For example, an owner can only rely on a privilege clause if there are legitimate business reasons behind the owner’s decision. If the owner’s motivation can be shown to have been unfair or motivated by inappropriate intent, the owner will not be able to rely on the privilege clause.

In the next case, Continental Steel sought to establish that Mierau Contractors did not evaluate the bids fairly and appropriately, and therefore was not entitled to rely on the privilege clause.

B. Continental Steel Ltd. v. Mierau Contractors Ltd., 2007 BCCA 292

1. Facts

Mierau Contractors was bidding on a new construction project and invited subcontractors to bid on steel work. The lowest bid was from Continental Steel, followed by PMC Builders and Developers Ltd. A clause in the tendering invitation stated that the lowest bid would not necessarily be accepted. Ultimately, Mierau selected PMC, the second lowest bidder, to complete the steel work on the project.

Mierau’s choice was based in part on negative experiences it had while working with Continental in the past and on negative things it had heard about Continental. Mierau decided that the second lowest bid from PMC represented a better value. The difference in costs between the bids of PMC and Continental was $5,229. Mierau decided that the degree of risk in using Continental was far greater than the extra costs associated with PMC’s bid.

Upon being told that it did not get the contract despite being the lowest bidder, Continental threatened legal action. Mierau’s response was to review their decision to determine if they had made a mistake. They obtained four references from other contractors that had past dealings with Continental (one was positive, one refused to comment, and two were negative). On the basis of these findings, they concluded that they had made the right business decision in selecting PMC.

2. Trial

At trial, the judge concluded that Mierau had treated Continental unfairly in the bidding process as Mierau’s concerns were unjustified. The judge ruled that the evidence that two contractors had negative comments regarding Continental was not relevant to the issue of the plaintiff’s rights to be chosen as a low bidder, and that the evidence was “completely insufficient to form any fair, good faith basis for rejecting the bid.” The trial judge held that Mierau breached its duties of fairness and good faith in the consideration of Continental’s bid and as such, they were liable for damages.

3. Court of Appeal

In a unanimous decision, the BC Court of Appeal overturned the trial judge’s decision. Mr. Justice Low stated at para. 26:

> Once the bids were in the appellant had to make a business decision and in doing so it had to be fair to all bidders. On the one hand, it could not be arbitrary. But, on the other hand, the appellant was not obliged to blindly accept the lowest bid. It was entitled to act in its own best financial interest so long as its decision was not unfair to any bidder.

The Court held that in contacting other contractors to confirm their concerns about using Continental, Mierau acted in a “business like way.” The Court stated that Mierau did not need to prove that Continental had a bad reputation, it only needed to prove that it had treated Continental fairly.
The Court confirmed that a contractor has an obligation to be fair when choosing a bid, even with the privilege clause in place. However, the Court concluded that the test was met in this case. In considering all the factors, the Court found that Mierau’s decision was a reasonable exercise of business judgment and the choice to select PMC’s bid was made on the basis of an honest business assessment.

Another recent case that touches on the issue of the “nuanced view of costs” is the Double N Earthmovers decision. In this case the courts were asked to determine to what extent there is a positive duty on owners to investigate and confirm factors other than price in evaluating bids.

C. Double N Earthmovers Ltd. v. Edmonton (City), 2007 SCC 3

1. Facts

The City of Edmonton issued a call for tenders to supply equipment and operators to move refuse at a landfill. The tender forms specifically stated that all equipment must have been manufactured in 1980 or later. The City awarded the contract to Sureway Construction, but permitted them to supply equipment that was manufactured prior to 1980. In response, Double N Earthmovers, a rival bidder, sued the City. It argued that the City breached the duties owed to Double N under Contract A in a number of ways and, as a result, Double N was entitled to profits it would have realized had it been awarded the contract.

2. Trial

Double N’s claim was dismissed at trial. The Court held that Sureway’s bid was compliant and that Contract B came into being when the City accepted Sureway’s tender. The Court found no duty on the part of the City to investigate Sureway’s tender. Further, the Court found that the City was not in breach of Double N’s Contract A by deciding, after accepting Sureway’s bid, to let Sureway use equipment older than 1980. In the trial judge’s view, all the Contract As came to an end upon the valid formation of Contract B with Sureway and the City could not be liable to Double N for its post-Contract B dealings with Sureway.

3. Court of Appeal

In a unanimous decision, the Alberta Court of Appeal agreed with the trial judge that Sureway’s bid was compliant on its face and that an owner is not subject to a duty to investigate suspicions of potential non-compliance. The Court also rejected Double N’s argument that the City’s Contract A obligations with an unsuccessful bidder could survive the formation of Contract B with a compliant bidder.

4. Supreme Court of Canada

The majority upheld the Court of Appeal’s decision. The Court had to decide whether the problems with the bids constituted non-compliance such as to be a breach of Contract A between Double N and the City. The majority found that the City was not aware that Sureway’s bid was not compliant and that there was no obligation to investigate the bid to ensure that it was. As such, there was no breach of the contract between Double N and the City.

a. Was the Bid Non-Compliant?

Double N argued that the failure to include the specifications for the machine on Sureway’s bid rendered it non-compliant. However, the Court held that the tender included a clause that permitted the City to “waive any informality.” The Court held that the definition of an informality would be something that did not “materially affect the price or performance of Contract B.” As such, the absence of serial numbers and license registration were considered to be informalities.
b. Did the City have an Obligation to Investigate Sureway’s Bid?

Double N argued that the City had a duty to investigate whether the equipment Sureway was bidding with met the City’s specifications. Double N argued that it had made complaints to the City regarding the need to investigate Sureway’s equipment and there had also been allegations raised by other rival bidders regarding non-compliance. The Court held that the wording in the tender document provided a right to inspect equipment but did not impose a duty to do so. The Court found no express or implied obligation to investigate the equipment bid prior to acceptance. The Court held at para. 51:

There is no reason why the parties would expect an owner to investigate whether a bidder will comply, when each bidder is legally obliged to comply in the event its bid is accepted. Whether or not the bidder is, at the time of tender, capable of performing as promised is irrelevant in light of the bidder’s legal obligation to do so once its bid is accepted.

c. Did the City Engage in “Bid Shopping”?

The Court held that the City’s pre-award negotiations with Double N and with Sureway did not amount to impermissible bid shopping and that the tender documents clearly indicated that some measure of negotiation was anticipated. The provision permitted negotiation with the lowest evaluated tenderer. Pursuant to the wording of the tender, the Court held that the City was specifically entitled to negotiate with Sureway, as they were the lowest bidder offering compliant units after the City’s initial evaluation. In obiter, the Court stated that if the City was to be criticized at all it should have been for conducting negotiations with Double N when they knew they were not the lowest evaluated tenderer.

d. Did the City Award the Contract on Terms Other than those Set Out in the Tender?

Sureway’s bid stated that the unit it offered in respect of the first item was a 1980 Caterpillar D8K, but was in fact a 1979 unit. Double N argued that this deceit prevented Sureway and the City from forming Contract B on the day the City accepted their bid. The Court held that the City was unaware of Sureway’s deceit until after it accepted the tender. In other words, there was no collusion between the City and Sureway to disregard the tender terms. As such, the City did not enter into a contract in terms other than as set out in the bidding documents and therefore did not violate any duties owed to Double N.

e. Did the City Violate its Duties by Permitting the Supply of Equipment Manufactured Prior to 1980?

The issue the Court considered in this context was whether the owner’s obligation under Contract A to treat all bidders fairly survived the creation of Contract B with the successful bidder. The Court held that it did not.

As the Court stated at para. 71:

Where an owner undertakes a fair evaluation and enters into Contract B on the terms set out in the tender document, Contract A is fully performed. Thus any obligations on the part of the owner to unsuccessful bidders have been fully discharged. Contract B is a distinct contract which the unsuccessful bidders are not privy.
f. Minority Decision

In a strong dissent, four of the nine Supreme Court justices would have allowed the appeal. Speaking for the minority, Madam Justice Charron opened her decision with the following statement at para. 76:

... the dismissal of the action and third party claim by the courts below not only results in Sureway Construction of Alberta Ltd.’s reaping the profits of its deceit, but also enables the City to escape entirely from its implied obligations. Far from preserving the integrity of the tendering process, this result seriously undermines it.

The minority held that the City had breached its obligations to Double N under Contract A by failing to ensure that Sureway’s bid was compliant. Further, the minority held that the City had breached its obligation to Double N to accept only compliant bids and to treat all bidders fairly and equally when it accepted a bid that was, on its face, non-compliant. The minority did not address the issue of bid shopping.

5. Commentary

The following general principles can be gleaned from the cases in this section:

1. Absent a privilege clause, Contract A generally includes an implied term that the lowest compliant bid will be accepted.

2. An owner can rely on a privilege clause to take a broader view of costs and is not necessarily required to award the contract to the lowest compliant bid.

3. An owner can only rely on a privilege clause if there are legitimate business reasons behind the owner’s decision. If the owner’s motivation or intent can be shown to have been unfair, the owner will not be able to rely on the privilege clause.

4. Absent a showing of unfair treatment or inappropriate intent, the courts should not go too far in second-guessing the business decisions of owners.

5. There is generally no implied duty requiring an owner to investigate to see if bidders will really do what they promised in their tender. Owners are entitled to rely on the tender forms in conducting their evaluation of the bids.

III. The Distinction Between RFPs and Tenders

A basic explanation of the difference between a request for proposal (“RFP”) and an invitation to tender was described by the Court in Socanav Inc. v. Northwest Territories (Commissioner), [1993] N.W.T.R. 369 at para. 21:

If there is a distinction between the two forms of soliciting offers, it may be this. When the government knows what it wants done and how it should be done (such as a construction project), it will already have its plans and specifications and is looking simply for the best price. On the other hand, when the government knows what it wants done, but not how to go about doing it, it seeks proposals on methods, ability, and price. Then it can negotiate on the best method to achieve the best value.

In other words, an offer to negotiate is generally not considered to give rise to contractual relations. An RFP is just that—a non-binding invitation to enter into negotiations with the owner. Negotiations may or may not result in a contract, and thus no legal obligation is created requiring that a contract be awarded to a successful bidder. This is clearly contrasted with a tendering process, which creates a legal relationship (Contract A) when a compliant bid is submitted, and impresses the party receiving bids with duties of fairness and good faith. Contract A requires that the owner must enter into Contract B with a successful compliant bidder.
However, simply calling a document an RFP is not enough to protect someone from the obligations arising out of a tender. The BC Supreme Court in *Tercon Contractors Ltd. v. British Columbia*, 2006 BCSC 499 provided a list of factors that will be used by the courts to determine whether an RFP will create a Contract A:

- the formality of the RFP process;
- whether there is a deadline for submission;
- whether bid/proposals are required to be irrevocable;
- whether there is a duty to award Contract B;
- whether Contract B has specific conditions not open to negotiation; and
- whether there is a statement that the RFP was not a tender call.

Where the court finds, on balance, that the terms of the RFP indicate that the “invitation to negotiate” is in fact a tender call, the submission of a compliant tender will result in the creation of a Contract A, and the usual tendering obligations will follow.

**IV. Damages**

Before a contractor responding to a call for tenders will be entitled to damages, it must establish the following on the balance of probabilities:

- the existence of Contract A;
- breach of a term of Contract A (often a breach of the duty of good faith);
- but for the breach of Contract A the contractor would have been awarded Contract B; and
- the damages claimed are not otherwise too remote.

In *M.J.B.*, *supra*, the Court described the general measure of damages as “expectation damages” and determined that the key question was whether on a balance of probabilities, the appellant would have been awarded Contract B.

In *Tercon*, *supra*, the Court concluded that the analysis of damages based on the difference between the revenue that the plaintiff would have received had it been awarded the contract and the cost that it would have incurred in performing work was a proper method for assessment in that case. In other words, the proper damages in tendering cases is the loss of expected profit had the contract been awarded.

Where the plaintiff is an owner and is suing a contractor for refusing to enter Contract B, the proper measure of damages is the actual loss to the tenderee: *Sound Contracting Ltd. v. Nanaimo (City)*, [1997] B.C.J. No. 1749 at para. 55.

**V. Commentary**

From the perspective of an owner, an award of damages for breach of its tendering obligations can be a bitter pill to swallow. Not only must it pay the successful bidder to actually complete the work, it must also pay damages to the aggrieved bidder for its lost profits.

Conversely, for the plaintiff contractor, there is minimal downside risk in bringing a tendering lawsuit and a potentially huge upside. The issues in tendering cases tend to be reasonably straightforward and the cases can be tried far more easily than most construction issues. Cost is therefore not nearly the deterrent to litigation that it is on other construction disputes.
The upside for a contractor in pursuing a tendering claim is an award of damages for the plaintiff contractor’s entire profit for the job—not bad for not doing the work or taking the construction risk. It is, therefore, crucial that tendering documents are drafted with care and that the established tendering process be followed precisely and fairly.