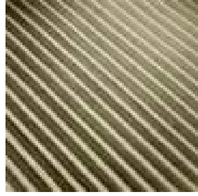

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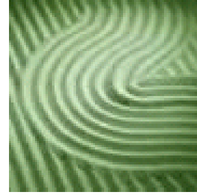
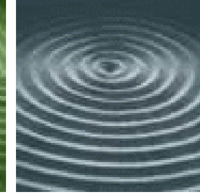
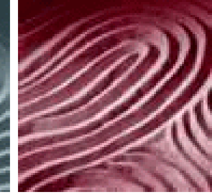

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"Contract A:" Sword or Ploughshare?

by William M. Pigott
November/December 2003

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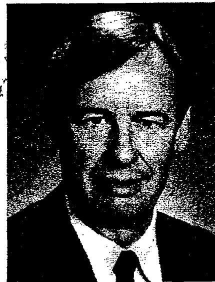

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...Ron Engineering flowered to address a chronic bid problem. How to reconcile an ostensibly "formal" irrevocable bid with the bidder's withdrawal on grounds that it made a serious mistake.

"CONTRACT A": SWORD OR PLOUGHSHARE?

Those less enamoured of the Supreme Court of Canada decision in *R. v. Ron Engineering & Construction (Eastern) Ltd.*, think of Contract A — created by *Ron Engineering* — as a drive-by shooting perpetrated on the law of mistake. After all, *Ron Engineering* flowered to address a chronic bid problem. How to reconcile an ostensibly "formal" irrevocable bid with the bidder's withdrawal on grounds that it made a serious mistake. Classic mistake theory meant that the owner could not accept a bid — even an irrevocable one with bid security — once advised of the mistake. Then came *Ron Engineering*.

The immediate reaction to *Ron Engineering* — apart from the shock of it all — was that contractors were walled off by Contract A from obtaining relief under the law of mistake. But, as time went by, the focus shifted from mistake to the other implications of Contract A. In a 22-year journey which has stretched from coast to coast and back, Contract A has been elaborated to define the obligations of both bidder and owner. Surprised, owners discovered that Contract A imposed obligations on them. And, potentially significant damages if those obligations were not met.

Followers of the *Ron Engineering* case law know that Contract A imposes an implied duty of fairness on the owner (*Martel Building Ltd. v. Canada*). They also

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know that the privilege clause (usually) places an obligation on the owner not to award the construction contract — Contract B under *Ron Engineering* — to a non-compliant bidder (*MJB Enterprises Ltd. v. Defence Construction (1951) Ltd.*).

Contract A also applies to the relationship between contractors and subtrades, arising if a trade is "carried". This genre of Contract A (usually) includes a prohibition on "bid shopping" (*Naylor Group Inc. v. Ellis-Don Construction Ltd.*). But, that is another story altogether.

No question about it, *Ron Engineering* — and the cases which have refined it — revolutionized the law of bidding.

New Law/Old Practice

One would think that the evolution of Contract A would spawn corresponding changes in the terms of bid documents. Wrong! At least, largely wrong.

Few owners issue bid documents (whether called bid documents or bids labelled something else — like a request for proposal) which speak of creating the process contract which is Contract A. Perhaps, that is not critical since Contract A is automatic if the right ingredients are present. But, reciting Contract A, in explicit bid provisions, might raise the awareness of both bidder and owner.

More fundamental, the industry still seems to view Contract A as a weapon — drawn during a bid dispute — rather than as a tool framing the bid process and controlling its outcomes.

Treating Contract A like a Contract

Consider a typical construction contract such as CCDC2-1994. The drafters of that contract took stock of the risks and obligations involved in executing a project. They set out the commercial terms — what is to be built, when, for how much. They also listed a series of obligations and identified contract risks. Then, they allocated the risks between the parties — or left them at large if that was the better decision — and then managed or insured them.

Why doesn't the construction industry take the same approach to Contract A? It's a mystery.

Telling it like it is

If bid documents expressly offered to enter Contract A (or, if you prefer the "process contract") with compliant bidders, a number of good things happen. First, both parties know that contract obligations are in the offing and that value is exchanged for the assumption and dis-

charge of those obligations. Second, a court or arbitrator would not be confused about whether this particular set of bid documents was, or was not, intended to create Contract A.

When you strip it down, a bid process is really two processes at once — one stacked on top of the other.

The invitation to bid is an invitation to the bidder to submit a price for the project — the bid is an offer for Contract B. This is so both before and after *Ron Engineering*.

But, the invitation to bid is now deemed to be — by the *Ron Engineering* case law — an offer. An offer by the owner to enter Contract A with each bidder who submits a bid which complies in all (substantial) respects with the bid documents. So, most bid documents have a public life and a secret life. The secret life leads to a separate Contract A between the owner and each compliant bidder.

Identifying and Allocating Risks

Most commercial contracts anticipate a breach of that contract and how the parties will behave if a breach occurs.

In Contract A, one of the principal risks is that the bidder will refuse an award of Contract B. Another risk is that — inadvertently or otherwise — the owner will breach its Contract A evaluation/award obligations.

Under most bid documents, a low compliant bidder who refuses to accept an award will be liable for the difference between its bid and the second low compliant bid. Potentially, a large amount of money — especially if a mistake has been made. Contracting being what it is, a substantial damage award can wipe out all but the most robust of contractors.

On the owner's side, a breach of Contract A can bring damages which range from the nominal (the cost of bid preparation) to the significant (the contractor's anticipated overhead and profit for the project).

Considering the nature and purpose of the bid exercise, the punishment may often be too harsh for the crime.

Consider a bid document — which identifies the "process contract" and includes a clause like the following:

> 1.1 *The Bidder acknowledges that by submitting a compliant bid, it has accepted an offer by the Owner to enter a "process contract" for the evaluation of bids and the award of the Contract, if an award is made. The Bidder acknowledges that the terms of the "process contract" are described in the Bid Documents.*
>
> 1.2 *The liability of the Bidder to the Owner for loss and damage arising out of the Bidder's breach of the "process contract" shall be limited to the lesser of the actual loss suffered by the Owner and the sum of One Hundred Thousand ($100,000.00) Dollars.*
>
> 1.3 *The liability of the Owner to any Bidder for the negligence of the Owner or for the breach by the Owner of the "process contract" shall be limited to the lesser of the sum of One Hundred Thousand ($100,000.00) Dollars and the reasonable cost to the Bidder of preparing its bid.*
>
> 1.4 *The limits of liability described in paragraphs 1.2 and 1.3 shall also apply to any claim for indemnity between the Owner and any Bidder in relation to this bid process.*

These clauses have not had the approval of a court yet. But, Contract A being a contract, the mutual limitation of liability should be effective.

If this clause — or one like it — is included in bid documents, it affects bid security. If the maximum damage for which the bidder can be liable for a breach of Contract A is $100,000, there is no point in requiring bid security which exceeds that amount. This may or may not produce savings in bid prices. It will help to reduce bid disputes. And, it will leave a contractor in business if it makes a bid mistake or decides to refuse an award.

The above example uses $100,000 as the limit of liability. But, the limit has to be assessed for each bid process. A balance should be struck between a number that is high enough to discourage anti-social bidder behaviour. Not so high as to inflict ruin. The corollary is that owners — by accepting these limits — give up the opportunity to reap a windfall from a contractor breach of Contract A.

Dispute Resolution

Over the last ten years, a great deal of effort has been devoted to alternative dispute resolution — meaning alternative to court. In Ontario, the court process now includes mandatory mediation (in all but a few areas). Most construction contracts — CCDC2-1994 being a prime example — include a negotiation/mediation/arbitration mechanism intended to keep construction

disputes out of court. And, in the hands of arbitrators who understand construction and its culture.

Contract A is not a one-on-one situation. In larger bid calls, there can be five to ten bidders all of whom may have Contract A with the bidding authority. If you use standard dispute resolution — like the CCDC2 model in such a bid context — how do you avoid creating a circus?

With multiple process contracts and a culture populated by people who are not shrinking violets, garden variety dispute resolution provisions don't work — at least they don't work for the owners who control the contents of bid documents. So, any dispute resolution provision must be attractive to owners.

Consider a dispute resolution provision such as this:

1. *In the event of a dispute arising in connection with this bid process, including a dispute as to whether the bid of any Bidder was submitted on time or whether a bid is compliant, the Owner, in its unqualified subjective discretion, may refer the dispute to a confidential arbitration before a single arbitrator with knowledge of procurement/bidding law and practice at Toronto, Ontario, pursuant to the* Arbitration Act, *1991, as amended. In the event that the Owner refers the dispute to arbitration, the Bidder agrees that it is bound to arbitrate such dispute with the Owner. Unless the Owner shall refer such dispute to arbitration, there shall be no arbitration of such dispute.*
2. *In the event the Owner refers the dispute to arbitration, the Owner and the Bidder agree that they shall exchange brief statements of their respective positions on the dispute, together with the relevant documents, and submit to an arbitration hearing which shall last no longer than two (2) days, subject to the discretion of the arbitrator to increase such time. The parties further agree that there shall be no appeal from the arbitrator's award.*

Some will argue that this clause is not fair because it is not symmetrical. It is not symmetrical because Contract A is not symmetrical either — one owner/several bidders. Besides, the damages that a bidder may recover in court — for a breach of Contract A — fall off dramatically if the complaining bidder is not the low compliant bidder. The bidder that finishes third, fourth or tenth in a large bid process may recover only nominal damages — perhaps the cost of bid preparation — because they never really had a chance — breach or no breach of Contract A. So, this dispute clause reflects "process contract" dynamics and a means to persuade the owner to include the clause in its bid documents. Unfair? Not at all. Any bidder still has its civil right to bring a lawsuit. If the damages at stake are minimal, contractors, being very smart people, will probably pass.

So, Where are We?

Most bid documents are prepared by consultants and their specification writers — without lawyer input on the "process contract" issues. Which may be why owners rarely use Contract A as a tool for allocating and managing some of the risks in bidding.

If the Contract A sword is to become a ploughshare, then owners or their consultants — at least from time to time — should collaborate with lawyers. And, between them treat Contract A like a contract. They should discover that Contract A is better used tilling fields than waging war.