APPEAL #C.A. 00357

IN THE COURT OF APPEAL OF THE NORTHWEST TERRITORIES

THE COURT:

The Honourable Mr. Justice Tallis
The Honourable Madam Justice Hetherington
The Honourable Mr. Justice Vertes

BETWEEN:

MARTSELOS SERVICES LIMITED

Respondent

- and -

ARCTIC COLLEGE

Appellant

APPEAL FROM THE JUDGMENT OF
THE HONOURABLE MR. JUSTICE M.M. de WEERDT
DATED MAY 8, 1992

REASONS FOR JUDGMENT OF THE HONOURABLE MR. JUSTICE VERTES
CONCURRED IN BY THE HONOURABLE MR. JUSTICE TALLIS
CONCURRED IN THE REASONS FOR JUDGMENT OF THE HONOURABLE MADAM JUSTICE HETHERINGTON

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R.A. Kasting & C.F. McGee
for the Appellant

D.M. Cooper, Q.C.
for the Respondent

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for the Respondent

4 It is not disputed that the tender call was governed by the Government Contract Regulations passed pursuant to the Financial Administration Act, R.S.N.W.T. 1988, c.F-4. The relevant sections of those Regulations were:

> 9. (1) A contract authority shall, before entering into any contract, issue an invitation to tender.
>
> (2) Every invitation to tender shall be issued so as to promote the submission of competitive tenders.
>
> ...
>
> 14. (1) A contract authority may refuse all tenders and award the contract to no one.
>
> (2) Subject to section 11, a contract authority shall only award a contract as a result of an invitation to tender to the tenderer who is responsive, responsible and has submitted a tender lower than that submitted by any other responsive and responsible tenderer.

Section 11 of the Regulations, noted in this extract, is not pertinent to this case.

5 The tender call also contained the following notice: "The lowest or any tender not necessarily accepted." This proviso is commonly referred to as a "privilege clause".

6 The respondent submitted a bid for this contract. A competing company, 862116 N.W.T. Limited (carrying on business as "P & A Security and Safety"), also submitted a bid. These were the only bids received in response to the tender call. When the bids were opened, it was revealed that the competitor was the low bidder.

7 After the opening of the bids, but before the contract was awarded, the owners of the respondent company complained to the officials of the appellant about a potential conflict of interest regarding P & A Security and Safety. It turned out that one of the two shareholders of that company was an employee of the appellant.

8 The substance of the complaint was that the employee was in breach of the conflict of interest provisions contained in the collective bargaining agreement between the government and its employees as well as those contained in the government's personnel policy. Further, it was alleged that because of the employee's particular job she could have exploited her knowledge to assist in the bid preparation.

9 It is not necessary to set out in detail the government's conflict of interest provisions. Suffice to say that employees are prohibited from carrying on any outside business or employment where there may be a conflict between the employee's regular work and his or her outside interest and where the employee is in a position to exploit knowledge or information gained in his or her employment for personal gain. There is a requirement for employees to notify the employer of any outside work. In this case, the employee had not notified the appellant of her outside business interest.

10 The appellant investigated the complaint and sought internal legal and personnel

relations advice. It concluded, based on the advice it received, that there was no conflict of interest because the employee did not have any private information that could be used to her company's advantage and did not have knowledge of competing bids. The appellant then awarded the contract to the low bidder.

TRIAL JUDGMENT

11 The learned trial judge found that there was a conflict of interest. He stated:

> **There is no evidence that the employee in fact took any advantage of her position as an accounts payable clerk in the defendant's office, by gathering information on payments made by the defendant under contracts for janitorial services then current, or on any other subject, and by making that information available to the competitor corporation (or her spouse). It was enough, for the purposes of the collective agreement, that she had a role as one of two directors of a corporation in business (or seeking to have business) with the defendant, at a time when she had access to information not available outside the office in which she was employed by the defendant, which information could, on the face of it, be exploited by her, through the corporation, for personal gain.**

12 Having found that there was a conflict of interest, the trial judge then went on to hold that the appellant should have acted on it. He held that there was a duty on the appellant to act fairly to all tenderers and that included an obligation to avoid even the suspicion of any unfair advantage being enjoyed by its employees.

13 The trial judge stated:

> **The fact that the defendant took no step to discipline the employee is beside the point. The fact that it was the employee's corporation and not the employee who contracted with the defendant is likewise irrelevant. What does matter is that the public, including the plaintiff, was entitled to expect that there was no possibility of "insider" knowledge or unfair advantage entering into the tendering process. The defendant had a clear duty to act in complete good faith with its tenderers so as to eliminate that possibility. Notwithstanding that the facts had been made known to it, the defendant chose to ignore that duty.**

14 As a result the trial judge held that the appellant was in breach of the "tendering contract". He then went on to consider whether the respondent was entitled to the contract.

15 The trial judge considered the requirement in the Regulations to award the contract to the lowest "responsive and responsible" bidder. He held that the employee's failure to disclose the potential conflict of interest was a sign of "bad faith" which disqualified the competitor from consideration as a "responsive and responsible" bidder. This left the respondent as the only eligible bidder. He then held:

> **The janitorial services contract should therefore have been awarded to it, as provided in the Financial Administration Act Regulations (and as was the industry practice and usage in such matters at the time in Fort Smith).**

As a result of that conclusion, the learned trial judge awarded damages amounting to the loss of anticipated profit by the respondent.

16 Several grounds of appeal were raised but, in my opinion, this appeal can be resolved by examining the effect of the privilege clause. In doing so, I have concluded, with respect, that the trial judge erred in holding that the appellant was obligated to award the contract to the respondent.

DISCUSSION

The learned trial judge held that the appellant had a duty to act fairly to all tenderers. He referred to the trial judgment in Gateway Realty Ltd. v. Arton Holdings Ltd. (No. 3) (1991), 106 N.S.R. (2d) 180 (S.C.), in saying that there was an obligation on the part of the appellant to contract in good faith. The trial judge held that, by failing to recognize a perceived conflict of interest and eliminating the offending bidder, the appellant breached its duty to contract in good faith and thereby the respondent was entitled to damages.

18 The Gateway decision has been viewed in many quarters as going beyond the current state of contract law. On appeal, the decision was upheld but there was no discussion about the extent of the "good faith" obligation: (1991) 112 N.S.R. (2d)

180 (C.A.).

19 There has been no authoritative recognition of the obligation to bargain in good faith. Some commentators suggest that it is only a matter of time before there is an express recognition of this principle: see J. Cassels, "Good Faith in Contract Bargaining" (1993), 15 Advocates' Quarterly 56.

20 In the area of contract tendering, the doctrine of good faith found some expression in the Supreme Court of Canada judgment in The Queen v. Ron Engineering & Construction (Eastern) Ltd., [1981] 1 S.C.R. 111. Writing on behalf of the court, Estey J. stated that "the integrity of the bidding system must be protected where under the law of contracts it is possible so to do" (p. 121). In my opinion this should be considered as a duty to treat all bidders equally but still with due regard for the contractual terms incorporated into the tender call.

21 Even if one can conclude that, in this case, the competing bidder did breach the conflict of interest guidelines, one cannot then conclude a breach of good faith by the appellant vis-à-vis the respondent. The trial judge found no "bad faith" on the part of the appellant. Any "bad faith" was held to be on the part of the competitor. I quote from the trial judgment:

> **The competitor did not disclose to the defendant that the defendant's employee was one of its two directors and owner of half its shares. It was left to the plaintiff to do that. And while the defendant sought and obtained advice on the matter, before awarding the janitorial services contract to the competitor, thereby acknowledging the existence of at least a perceived conflict of interest, the fact remains that neither the competitor nor the employee in question saw fit to make any disclosure of the situation. This, in my respectful view, demonstrated bad faith on their part to a degree which deprived the competitor of any valid claim to be either responsive or responsible as a tenderer for the contract in question, within the meaning of s.14 of the Regulations.**

The effect of this "bad faith" could only be the disqualification of the competitor's bid. It cannot create an obligation on the part of the appellant toward a third party, in this case the respondent.

22 I do not think it is necessary for me to discuss the conflict of interest issue further. The resolution of this appeal would be the same whether one assumes that the conflict of interest guidelines had been breached or not.

23 The trial judge found that the competing bid should have been disqualified and, since that left only the respondent's bid, the contract should have been awarded to the respondent. He based this on the Government Contract Regulations and on industry practice.

24 There was no obligation on the appellant to award the contract to any bidder. This is made clear in s.14(1) of the Regulations and was stated explicitly in the tender

call by use of the privilege clause. The Regulations do stipulate, in s.14(2), that if a contract is to be awarded it shall be awarded only as a result of a tender call and only to the lowest responsive and responsible bidder.

25 Much argument on the appeal was addressed to the issue of what obligations are imposed on an "owner", such as the appellant, when it issues a tender call. These arguments centred around the Ron Engineering decision. The learned trial judge referred to this decision when he held that once the respondent submitted its bid there arose a "tendering contract" between the parties.

26 In Ron Engineering, the Court was considering whether the tenderer could withdraw its tender after the bids were opened but before the owner accepted any one of them. The Court held that upon submission of the tender a unilateral contract ("Contract A") came into existence. The principal term of Contract A is the irrevocability of the bid and a corollary term was the obligation to both parties to enter into a contract ("Contract B") upon acceptance of the bid.

27 According to Ron Engineering, the obligation of the "owner", here the appellant, is to enter into a contract ("Contract B") upon acceptance of the tender. The owner also had "the qualified obligations ... to accept the lowest tender, and the degree of this obligation is controlled by the terms and conditions established in the call for

tenders" (p. 123).

28 This cannot be interpreted as imposing an obligation in all cases to award a contract. If that were the case, in the situation where there were several bidders, with each of whom the owner would have a Contract A, there would be an obligation to enter into a Contract B with each of them. This is not the case. The owner's obligation to enter into a Contract B arises only upon acceptance of a tender: M.S.K. Financial Services Ltd. v. Alberta (1987), 23 Constr.L.R. 172 (Alta.Q.B.).

29 Therefore, when the respondent submitted its tender, that gave rise to Contract A. As noted in Ron Engineering, in addition to the obligation to enter into Contract B on acceptance, the appellant had the qualified obligation to accept the lowest tender but subject to the "terms and conditions established in the call for tenders". One of the explicit terms of the tender call in this case was that the lowest or any tender would not necessarily be accepted.

30 As stated previously, there is nothing in the Regulations to obligate the appellant to accept any tender or award any contract. This is specifically provided for in s.14(1) where it stipulates that the appellant, as a contracting authority, may "refuse all tenders and award the contract to no one."

31 The respondent argues, however, that it was the industry practice or custom to award these contracts in the past to the low bidder. Indeed the evidence showed that the respondent had been the recipient of previous contracts. Canadian jurisprudence, however, has not recognized any precedence of industry practice or custom over the privilege clause, where the privilege clause is an explicit term of a tender call, except in special circumstances.

32 In Elgin Construction Co. v. Russell (1987), 24 Constr.L.R. 253 (Ont.H.C.), the court held that the privilege clause allowed the owner to reject the lowest tender and accept a higher one. The low bidder argued that, notwithstanding the privilege clause, it was the "custom of the trade" that the lowest bidder be awarded the contract unless it was not qualified. The court dismissed the claim and held that the express language contained in the instructions to bidders governed. White J. stated (at page 257):

> **It is my opinion that "no custom of the trade" can be deemed to qualify the most explicit words of the advertisement that "Tenders are subject to a formal contract being prepared and executed. The township reserves the right to reject any and all tenders and the lowest or any tender will not necessarily be accepted," and the equally explicit words in the "Information for Tenderers", as stated in para. 12, "The Corporation reserves the right to reject any or all tenders ... without stating the reasons and the lowest or any tender will not necessarily be accepted."**
>
> **Any "custom of the trade," as hitherto defined, is extirpated in its efficacy in the contractual relations of the parties by the explicit words in the advertisement and "Information to Tenderers," to which I have referred, which form a legal context in which the plaintiff's tender was submitted. As a matter of law, that context precludes the operability**

> of such "custom." To deny this would be to destroy the doctrine that contractual relations between parties are based on their objective manifestations of intent to exchange binding promises.

This reasoning has been applied to the same effect in numerous other cases: Megatech Contracting Ltd. v. Carleton (1989), 34 Constr.L.R. 35 (Ont.H.C.); Power Agencies Co. et al v. Newfoundland Hospital and Nursing Home Assoc. (1991), 44 Constr.L.R. 255 (Nfld. S.C.); and Glenview Corp. v. Canada (1990), 44 Admin.L.R. 97 (F.C.T.D.).

33 In the case of Acme Building & Construction Ltd. v. Newcastle (1990), 38 Constr.L.R. 56 (Ont.D.C.), an unsuccessful bidder, who was the low bidder on a municipal project, complained that the municipality used irrelevant criteria in assessing the various bids and argued that there was an accepted custom in the industry that the lowest qualifying bidder would be accepted. The trial judge rejected the evidence that such custom existed and concluded that the municipality's procedures were fair.

34 On appeal, the Ontario Court of Appeal upheld the trial judgment: (1993), 2 Constr.L.R. (2d) 308. The court held (at pages 309-310):

> In our opinion, even if there was acceptable evidence of custom and usage known to all the tendering parties, it could not prevail over the express language of the tender documents which constituted an irrevocable bid once submitted, and a contract, when and if accepted
> . . .
> With respect to accepting any given bid, the instructions to tenderers stated that the "[o]wner shall have the right not to accept lowest or any other tender". This gave the respondent the right to reject the lowest bid and accept another qualifying bid without giving any reasons.

An application for leave to appeal this judgment to the Supreme Court of Canada was dismissed on April 1, 1993.

35 Practice and custom have been held to over-ride the privilege clause only in specific cases with special circumstances. Those circumstances have been where an owner has relied on undisclosed criteria, or where the owner takes into account irrelevant or extraneous considerations, or where there are specific provisions in the tender specifications that are inconsistent with the general privilege clause, or where the tendering process was a sham. The cases where these situations have arisen are Chinook Aggregates Ltd. v. Abbotsford (1989), 40 B.C.L.R. (2d) 3456 (C.A.); Northeast Marine Services Ltd. v. Atlantic Pilotage Authority, [1992] F.C.J. No. 953 (T.D.); Canamerican Auto Lease and Rental Ltd. v. Canada, [1987] 3 F.C. 144 (C.A.); and Best Cleaners and Contractors Ltd. v. Canada, [1985] 2 F.C. 293 (C.A.).

36 In my opinion none of these situations arise in this case. That is not to say that there would not be other circumstances that would justify over-riding the privilege clause; it simply means that there is nothing in the circumstances of this case to warrant interfering with the explicit terms of the tender call. Even if it can be said that the industry practice was to award the contract to the lowest bidder --- and I am far from convinced that the evidence reveals such "practice" since there were occasions when the work was not done by the low bidder --- there was no evidence

that the appellant had done anything in assessing the two bids so as to jeopardize the integrity of the tendering process.

37 There was nothing in the tender documents to limit the scope of the privilege clause. The appellant was not applying undisclosed criteria. There was no evidence that the appellant gave some advantage or preference to the low bidder because of the employee's position. There is no evidence that the appellant used different standards in assessing the two bids. There is no evidence that the tendering process was a sham. And, it must be remembered, the competitor's bid was the low bid.

Even if we assume that the appellant should have eliminated the competing bid leaving only the respondent as an eligible bidder, can it be said that the appellant waived reliance on the privilege clause by awarding the contract to an ineligible bidder? I think not. The issue here is what was the appellant obligated to do. Even if it had an obligation to eliminate the competing bidder it does not follow that there was any obligation, either in law or according to industry practice, to award the contract to the respondent. This does not change simply because the respondent is the only eligible bidder. The appellant could have decided not to award any contract. It is no different if the competing bidder is disqualified after awarding the contract. The privilege clause, in these circumstances, is a complete answer to the respondent's claim.

DISPOSITION

39 I would allow the appeal, set aside the judgment appealed from, and dismiss the action.

40 Considering the fact that the problems resulting in this litigation were brought on by the appellant's failure to adequately address the conflict of interest complaint in the first place, I would direct that each party bear their own costs both here and in the court below.

Vertes, J.A.

I CONCUR:

Tallis, J.A.

DATED at Yellowknife, Northwest Territories,
this 19th day of January, 1994

REASONS FOR JUDGMENT OF THE HONOURABLE MADAM JUSTICE HETHERINGTON

1 Arctic College placed an advertisement in a newspaper inviting tenders for the provision of janitorial services. Two companies submitted tenders, 862116 N.W.T. Ltd. and Martselos Services Limited. After it opened the tenders, but before it awarded the contract for janitorial services, Arctic College became aware that one of its employees was a director and shareholder of 862116. However, it awarded the contract to 862116, which had submitted the lowest bid.

2 Martselos took action against Arctic College claiming damages for breach of its contract with the College. It complained that the College had not acted fairly in awarding the contract for janitorial services to 862116. The trial judge found in favour of Martselos, and gave it judgment against Arctic College in the amount of its anticipated profit from the contract for janitorial services ((1992), 5 BLR (2d) 204 (N.W.T. S.C.)). Arctic College appealed.

3 When Martselos submitted a tender in response to the invitation of Arctic College, a contract automatically came into being between them. In ***Her Majesty the Queen in Right of Ontario et al.*** v. ***Ron Engineering and Construction (Eastern) Ltd.***, [1981] 1 S.C.R. 111 at 119, Mr. Justice Estey referred to such a contract as contract

A, to distinguish it from the contract which arises on the acceptance of a tender, which he referred to as contract B. He said that the terms and conditions in the tender documents become part of the terms of contract A.

4 In this case the tender documents say nothing of a duty on Arctic College to act fairly. However, before us counsel for Arctic College conceded that it was an implied term of its contract with Martselos that it would act fairly. The case therefore raises the following issues:

(1) Did Arctic College breach its contract with Martselos in that it failed to act fairly in relation to that contract?

(2) If so, did Martselos suffer any loss as a result of the conduct of Arctic College?

(3) If so, is the appropriate measure of damages the amount of Martselos' anticipated profit from the contract for janitorial services?

Since in my view Martselos did not suffer any loss as a result of the conduct of Arctic College, and since its claim against the College must therefore fail, I will not deal with the other issues.

5 The trial judge found (at 210) that Arctic College should have awarded the contract for janitorial services to Martselos. He said that when it did not, Martselos lost the profit which it would have made from that contract. With respect, I do not agree.

6 As I indicated above the terms and conditions in the tender documents formed part of the terms of the contract which Martselos actually had with Arctic College. One of those documents was the invitation to tender. It contained the following statement:

> "The lowest or any tender not necessarily accepted."

In my view, as a result of this term of the contract, Arctic College was not in any way or in any event obliged to award the contract for janitorial services to Martselos. I agree with Mr. Justice Vertes that in the circumstances of this case industry practice and usage could not take precedence over this express term of the contract.

7 Since Arctic College was not obliged to award the contract for janitorial services to Martselos, that company failed to establish that it suffered any loss as a result of the conduct of the College in awarding the contract to 862116.

8 I would therefore allow the appeal and set aside the judgment of the trial judge in favour of Martselos.

"M.M. Hetherington" per JJ
Hetherington, J.A.
(authorized to sign)

DATED at Yellowknife, Northwest Territories
this 19 day of JAN., 1994

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