

Blakes Bulletin

Procurement / Litigation

Design Services Ltd. v. Canada

DAVID TUPPER, JASON HOLOWACHUK, JOEL RICHLER AND JUDY WILSON

Summary

In *Design Services Ltd. v. Canada* 2008 SCC 22, the Supreme Court of Canada considered whether an owner owes a duty of care to subcontractors in the tendering context, and found that this type of claim cannot be justified as a new category of negligence for reasons of proximity and indeterminate liability. In reaching this conclusion, the Supreme Court placed particular emphasis on what contracting options would have been available to the subcontractors under the owner's tender documentation, had the subcontractors chosen to utilize them.

This decision has a number of important implications relative to limitation of an owner's liability under the terms of its tender documentation and in relation to the need for subcontractors to secure adequate contractual protections for themselves.

Facts

Design Services Ltd. and other plaintiffs were subcontractors assembled by the general contractor Olympic Construction Limited, to submit a bid proposal for the construction of a naval reserve building, HMCS Cabot, at St. John's Newfoundland.

Olympic's bid was submitted pursuant to a design-build tender process, issued by the Department of Public Works and Government Services Canada. The tender documentation required Olympic to assemble a team of subcontractors for a design-build process each of whom had to be pre-approved by Public Works and could not be substituted without specific authorization. Stage one of the two-stage process involved a request for statement of qualifications (SOQ). Public Works required the SOQ to contain significant detail concerning the role, relationship and experience of each member of the design-build team. Public Works also required each team to attend a "partnering session" between its project manager and all constituents. Stage two involved a request for proposal (RFP), whereby prequalified applicants could reply to the RFP. The RFP provided that a reply could either be submitted by a single proponent (i.e., the general contractor) or by a joint venture consisting of the team pre-qualified under the SOQ process.

Members of Olympic's team, including Design Services and other subcontractors, entered into various agreements among each other, including confidentiality and non-disclosure agreements, but decided that Olympic would be the sole proponent in the response to the RFP. If Olympic was awarded the contract, it would then enter into subcontracts with members of its design-build team. Public Works was not involved in any of the negotiations between Olympic and the members of its design-build team.

Public Works approved Olympic's SOQ. Olympic submitted its reply to the RFP as the sole proponent. Public Works awarded the contract to a non-compliant bidder and litigation ensued. Olympic settled with Public Works. Design Services and other constituents of Olympic's design-build team (the "Design-Build Plaintiffs") continued to advance their own claims following the settlement. In doing so, they had to overcome the fact that they had no contractual relationship with Public Works.

Arguments

The Design-Build Plaintiffs contended that Public Works invited not just a general contractor to participate in the design-build competition but also the constituents of its design-build team, each of whom spent a considerable amount of effort to prepare designs and plans and submit a price. Public Works stood to gain a great deal by this effort so that it would be unconscionable and contrary to the integrity of the bidding system to allow Public Works to limit its liability to Olympic alone, where it had breached a duty of fairness to the design-build team as a whole by awarding the construction contract to a non-compliant bidder.

Public Works did not dispute that it breached its duty of fairness to Olympic by awarding the contract to a non-compliant bidder or that if the contract had been properly awarded to Olympic, the Design-Build Plaintiffs would have been paid for their work on the project, including the cost of preparing the bid documents. However, Public Works contended that the Design-Build Plaintiffs had no legal status in the process because it was open to them to organize their affairs as joint venturers for purposes of the SOQ and reply to the RFP, but they had chosen not

Procurement / Litigation

to do so. Further, it was argued, theirs were claims for pure economic loss that did not fall under any established duty of care and could not become a new category of negligence because, among other things, this would open the door to indeterminate liability by encouraging further claims from sub-subcontractors, suppliers, their employees and the like.

Background to Tendering: The Contract A and B Framework

The general framework for analyzing the construction tendering process was set out in *Ontario v. Ron Engineering & Construction (Eastern) Ltd.* [1981] S.C.J. No. 13 and recently reviewed by Binnie J. in *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, [2001] 2 S.C.R. 943. Upon the submission of a tender in response to an owner's call for tenders, a unilateral contract is formed between the bidder and the owner. This is known as "Contract A." Depending on its terms (expressed and implied), Contract A binds owners in several ways. Principally, owners must treat all bidders fairly and equally, and they can only accept compliant bids (*Martel Building Ltd. v. Canada*, [2002] 2 S.C.R. 860). The successful bidder is required, as a condition of Contract A, to enter into the construction contract with the owner (Contract B).

Supreme Court of Canada [2008] S.C.J. No. 22

The Supreme Court of Canada unanimously affirmed the decision of the Federal Court of Appeal (which overturned the trial judgment). Rothstein J., for the court, concluded that a new duty of care should not be recognized. The Design-Build Plaintiffs were claiming pure economic loss that did not fall within a pre-existing category of a duty of care. Although it was reasonably foreseeable to Public Works that the Design-Build Plaintiffs would suffer harm from a contract award to a non-compliant bidder, the second aspect of the test for establishing a new duty of care – sufficient proximity – could not be established. Public Works maintained a distance between itself and members of design-build teams that were not proponents through the terms of its tendering documents.

Furthermore, a new duty of care between an owner and a subcontractor in a tendering context was not justifiable. Contrary to the finding at trial, the issue of indeterminate liability was problematic. While it was true that the subcontractors were known to Public Works by reason of its prequalification SOQ process, the contractual context led to the indeterminacy of the class of plaintiffs that could

readily be determined. The concern was that holding Public Works to a duty of care in respect of those subcontractors would actually open the door to a potentially indeterminate number of claims for economic loss by further suppliers and employees working under those subcontractors. The Design-Build Plaintiffs could have protected themselves by making themselves parties to Contract A, but chose not to do so. The Supreme Court concluded in this regard that tort law should not be used as an after-the-fact insurer.

Application

Whether an owner could owe a duty of care to its subcontractors was a question left open in *Martel Building Ltd. v. Canada*, [2000] 2 S.C.R. 860. In *Design Services*, the issue was resolved. Thus, in the absence of damage to property (which may engage existing principles of relational economic loss), no duty of care exists. The position taken by the Supreme Court on indeterminate liability recognizes the reality that construction contracting typically involves a very long and complex supply chain, making it difficult or impossible to draw the line between claims of subcontractors versus their respective suppliers and employees. In the result, future cases claiming economic loss against owners in the construction context are more likely to focus on the terms of the owner's tender documentation, having regard to whether the subcontractors had reasonable opportunities to protect themselves by contract with the owner. Owners who have taken the time to carefully structure their tender documentation with regard to the involvement of subcontractors may realize a significant mitigation of risk in this regard.

For subcontractors, this decision should serve as a stark reminder of the importance of performing comprehensive due diligence independently of the general contractor, both to understand the owner's tender documentation and to obtain adequate legal protection. Simply working closely with a general contractor will not create legal contractual benefits for the subcontractor.

For further details, or if you have any questions concerning this bulletin, please contact [David Tupper](mailto:David.Tupper@blakes.com) at 403-260-9722 or david.tupper@blakes.com, [Jason Holowachuk](mailto:Jason.Holowachuk@blakes.com) at 403-260-9776 or jason.holowachuk@blakes.com, [Joel Richler](mailto:Joel.Richler@blakes.com) at 416-863-2735 or jr@blakes.com, [Judy L. Wilson](mailto:Judy.L.Wilson@blakes.com) at 416-863-5820 or judy.wilson@blakes.com or any other member of our [Litigation](#) or [Procurement](#) Groups.

Go to blakes.com/english/subscribe.asp to subscribe to other Blakes Bulletins.

Blakes periodically provides materials on our services and developments in the law to interested persons. If you do not wish to receive further bulletins or other materials from Blakes, please contact Blakes Marketing Department at 416.863.3036 or dorothy.byers@blakes.com. For additional information on our privacy practices, please contact us at privacyofficer@blakes.com. Blakes Bulletin is intended for informational purposes only and does not create a lawyer-client relationship. The transmission of this information does not suggest Blakes or any of its lawyers are practising law of any jurisdiction other than Canada. The information provided in this bulletin is summary in nature and does not constitute legal advice. We would be pleased to provide additional details or advice about specific situations if desired. For permission to reprint articles, please contact Blakes Marketing Department at 416.863.2403 or lynn.spencer@blakes.com. ©2008 Blake, Cassels & Graydon LLP.