

CASE COMMENT: *TERCON CONTRACTORS LTD. V. BRITISH COLUMBIA: THE FINAL NAIL IN THE COFFIN OF THE DOCTRINE OF FUNDAMENTAL BREACH?*

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The Supreme Court of Canada released its reasons in the much anticipated decision in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4 on February 12, 2010. In a five/four decision, the majority found in favour of Tercon, allowing the appeal. The Court agreed on the appropriate framework of the analysis as to the enforceability of the exclusion clause in issue, but were divided on the applicability of the relevant exclusion clause to the facts at hand.

The facts of Tercon arose out of a tendering contract between Tercon Constructors Ltd. ("Tercon") and Her Majesty the Queen in Right of the Province of British Columbia (the "Province") which issued the tender call. The key issue in the case was the interpretation of provisions in the contract relating to the eligibility to bid and a damages waiver which excluded compensation resulting from participation in the tendering process.

In 2000, the Ministry of Transportation and Highways for the Province issued a request for expressions of interest ("RFEI") for designing and building a highway in northwestern British Columbia. Six teams made submissions, including Tercon and Brentwood Enterprises Ltd. ("Brentwood"). Later in 2000, the Province informed the six proponents that it now intended to design the highway itself and would issue a request for proposal ("RFP"), which RFP in fact was issued on January 15, 2001. Under the terms of the RFP, **only** the six original proponents were eligible to submit a proposal. The RFP also included an exclusion clause which stated as follows:

2.10 ... Except as expressly and specifically permitted in these Instructions to Proponents, **no Proponent shall have any claim for 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. [Emphasis added] (para. 61)

Subsequent to the issuance of the RFP, Brentwood teamed up with Emil Anderson Construction Co. ("EAC") because it was unable to submit a competitive bid on its own. EAC was not one of the six qualified bidders. Together, Brentwood and EAC submitted a bid in Brentwood's name. Brentwood and Tercon were the two short-listed proponents. The Province ultimately selected Brentwood as the preferred proponent.

Tercon brought an action seeking damages, alleging that the Province had considered and accepted an ineligible bid and that, but for that breach, Tercon would have been awarded the contract. The trial judge agreed and awarded approximately \$3.5 million in damages and pre-judgment interest to Tercon.

The Court of Appeal reversed the trial judge's decision. Tercon sought and obtained leave to appeal to the Supreme Court of Canada. The Supreme Court found in favour of Tercon.

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Was the Brentwood Bid Ineligible?

The trial judge had found that the Brentwood bid was in substance, although not in form, from a joint venture of Brentwood and EAC and that it was, therefore, an ineligible bid. The British Columbia Court of Appeal concluded that it was unnecessary to address this issue.

The Province had submitted: (1) that a joint venture is not a legal person and that therefore the Province could not and did not contract with a joint venture; and (2) that the Province did not award the contract to EAC and EAC had no contractual responsibility to the Province for failure to perform the contract. These two arguments were not accepted by the Supreme Court. The majority noted that the issue was not, as these arguments assumed, whether the Province contracted with a joint venture or whether EAC had contractual obligations to the Province. The issue was whether the Province considered an ineligible bid.

The Province also took the position that there was no need to look beyond the face of the bid to determine who was bidding, arguing that the proposal was in the name of Brentwood and that therefore the bid was from a compliant bidder. The majority found that the trial judge, in rejecting this position, had made no error. Justice Cromwell stated that the trial judge's finding that the Brentwood bid was in fact on behalf of a joint venture was unassailable.

The Province's third argument was that there was no term in the RFP that restricted the right of proponents to enter into joint venture agreements with others; this arrangement left Brentwood, the original proponent, in place and allowed it to enhance its ability to perform the work. This submission was also rejected by the Supreme Court. The majority found that, when read as a whole, the provisions of the RFP did not permit the addition of a new entity, as occurred here. Furthermore, the Court noted that the Province never gave a written decision to permit this change as required by the RFP.

Both the majority and minority found no fault with the trial judge's conclusion that the bid was in fact submitted on the behalf of a joint venture of Brentwood and EAC which was an ineligible bidder under the terms of the RFP. The acceptance of Brentwood's bid breached not only the express eligibility provisions of the tender documents but also the implied duty to act fairly towards all bidders.

Was the Exclusion Clause Enforceable?

The Court then turned to consider the exclusion clause at issue. The consideration of the applicability of the exclusion clause is the most interesting element of the decision and will have far reaching implications for the tendering process and the construction industry in the future.

Both the majority and the dissenting Justices agreed that the doctrine of fundamental breach should be retired in respect of the enforceability of exclusion clauses. Justice Binnie, writing for the minority, stated "[o]n this occasion we should again attempt to shut the coffin on the jargon associated with 'fundamental breach' Categorizing a contract breach as 'fundamental' or 'immense' or 'colossal' is not particularly helpful."

In the result, Justice Binnie stated that the test as to the enforceability of an exclusion clause is comprised of three stages, pursuant to which the court asks itself:

1. Whether, as a matter of interpretation, the exclusion clause even *applies* to the circumstances established in evidence. This will depend on the Court's assessment of the intention of the parties as expressed in the contract.
2. If the exclusion clause applies, whether the exclusion clause was unconscionable at the time the contract was made, "as might arise from situations of unequal bargaining power between the parties" (*Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, at p. 462).
3. Whether the Court should nevertheless refuse to enforce the valid exclusion clause because of the existence of an overriding public policy, proof of which lies on the party seeking to avoid enforcement of the clause, that outweighs the very strong public interest in the enforcement of contracts.

Justice Cromwell, for the majority, agreed with the above three-stage test.

The Majority's Application of the Test to the Facts

The majority of the Supreme Court concluded that the exclusion clause did not cover the Province's breaches based on the facts before it. The majority found that the RFP process put in place by the Province was premised on a closed list of six bidders, and that, therefore, a contest with an ineligible bidder was not part of the RFP process and was, in fact, expressly precluded by its terms. The majority held that the "very premise of its own RFP process was missing" and that the work was awarded to a party that could not be a participant in the RFP process. Therefore, it was found that Tercon's claim was not barred by the exclusion clause because the clause only applied to claims arising "as a result of participating in [the] RFP" and not to claims resulting from the participation of other, ineligible parties. Furthermore, the words of the exclusion clause were found to be "not effective to limit liability for breach of the Province's duty of fairness to bidders."

The majority rejected the Province's argument about the commercial sophistication of Tercon, noting that this argument had two weaknesses:

1. It assumed the answer to the real question before the Court which was: What does the exclusion clause mean? The consequences of agreeing to the exclusion clause depend on its construction.
2. The Province overlooked its own commercial sophistication and the fact that sophisticated parties can draft very clear exclusion and limitation clauses.

The majority contrasted the exclusion clause at issue in the case before it with the limitation clause at issue in *Guarantee Company of North America v. Gordon Capital Corp.* [1999] 3 S.C.R. 423 ("*Gordon Capital*"), which provided that legal proceedings for the recovery of "any loss hereunder shall not be brought ... after the expiry of 24 months from the discovery of such loss." The Court found this language found in a fidelity bond to be clear. The Court used the

Gordon Capital case as an example which demonstrated that sophisticated parties are capable of drafting clear and comprehensive exclusion provisions.

The majority concluded that in attempting to determine whether or not an exclusion clause applies, a significant issue to be considered will be whether or not the defect in the tender calling authority's conduct is "such that it is completely outside ... [the RFP] process."

In reviewing the text of the exclusion clause within the context of the RFP as a whole, the majority found that it could not accept that the parties could have intended to "exclude a damages claim resulting from the Province unfairly permitting a bidder to participate who was not eligible to do so" (para. 78).

The Minority's Application of the Test to the Facts

In respect of applying the test to the facts of the case, the minority disagreed with the majority, finding that the exclusion clause did apply. In analysing the exclusion clause, Binnie J. accepted "the trial judge's view that the Ministry was at fault in its performance of the RFP, but the conclusion that the process thereby ceased to be the RFP process appears to me, with due respect to colleagues of a different view, to be a 'strained and artificial interpretatio[n] in order, indirectly and obliquely, to avoid the impact of what seems to them ex post facto to have been an unfair and unreasonable clause'" (para. 128).

In commenting on the bargaining power of the respective parties, Binnie J. referred to the fact that Tercon was a major contractor and was "well able to look after itself in a commercial context." Justice Binnie suggested that Tercon need not bid if it did not "like what [was] proposed"(para. 131).

Justice Binnie concluded that there was not any overriding public policy that would justify the Court's refusal to enforce the exclusion clause.

Justice Binnie concluded that while the Ministry's conduct was in breach of Contract A, that conduct was not so extreme as to engage an overriding and paramount public interest in curbing contractual abuse. It would appear that, here, Binnie J. was making an oblique reference to non-compliant bids. It remains to be seen whether or not the *Tercon* case will, in fact, open the floodgates in tendering cases involving non-complaint bids; however, inasmuch as no Contract A can be formed by the submission of a non-compliant bid, the issue is, in the result, arguable.

Conclusion

It is clear that the *Tercon* decision will have a significant effect on the construction industry and the tendering process in Canada. It is likely that tender calling authorities will give further consideration to drafting very carefully worded exclusion clauses. However, at least in the case of government tendering authorities, regard must be had to their obligation to draft such clauses such that any applicable policy mandate to provide for a fair and equitable tendering process is maintained.