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Thomas Heintzman is the author of Goldsmith & Heintzman on Canadian Building Contracts, 4th Edition which provides an analysis of the law of contracts as it applies to building contracts in Canada.

Goldsmith & Heintzman on Canadian Building Contracts has been cited in over 183 judicial decisions including the two leading Supreme Court of Canada decisions on the law of tendering:

M.J.B. Enterprises Ltd. v. Defence Construction (1951), [1999] 1 S.C.R. 619 and
Double N Earthmovers Ltd. v. Edmonton (City),[2007] 1 S.C.R. 116

An Owner Owes No Duty Of Care To A Subcontractor In A Bid Depository System

The Newfoundland and Labrador Court of Appeal has recently held that an owner does not owe a duty of care to a subcontractor arising from the normal operation of a bid depository system: ***Defence Construction (1951) Limited v. Air-Tite Sheet Metal Limited***.

The Background:

The owner, Defence Construction, a wholly owned subsidiary of the government of Canada, entered into a contract with N. M. Dobbin Limited for the construction of an aircraft hanger in Labrador. Dobbin in turn entered into a subcontract with Air-Tite for the installation of the heating system. Those contracts were awarded through a bid depository system. The heating system was designed by Shawmont Newfoundland Design Associates.

The heating system did not work properly. As a result, Dobbin terminated Air-Tite's subcontract and retained another company to perform corrective work. Later, it was determined that the fault was due to the negligent design of Shawmont, not the defective work of Air-Tite.

Defence Construction sued Shawmont and Dobbin for damages and Dobbin commenced third party proceedings against Air-Tite. In a separate action, Air-Tite sued Dobbin and Defence Construction for damages as a result of the wrongful termination of Air-Tite's contract with Dobbin and the failure of Dobbin to award the corrective work to Air-Tite.

The Trial:

The trial judge held that Shawmont had been negligent in the design of the air conditioning system and awarded damages in favour of Defence Construction against Shawmont. The trial judge dismissed Defence Construction's claim against Dobbin on the ground that Dobbin had followed the Shawmont design and had not itself been negligent.

The trial judge also held that Defence Construction was negligent in the supervision of the contract between Dobbin and Air-Tite and awarded Air-Tite damages against Dobbin and Defence Construction. The negligence alleged against Defence Construction was that it granted permission to Dobbin to terminate the sub-contract to Air-Tite and award the corrective work to the third party without taking reasonable care to inquire as to whether the failings in the heating system were due to the fault of Air-Tite.

The Court of Appeal:

The Newfoundland and Labrador Court of Appeal allowed the appeal so far as Air-Tite's claim in negligence against Defence Construction. Applying the decision of the Supreme Court of Canada in ***Design Services Ltd. v. Canada***, [2008] 1 S.C.R. 737, the Court held that the owner, Defence Construction, owed no duty of care to the subcontractor Air-Tite.

The Court held that subcontractors do not fall within a recognized category of persons to whom a duty of care in negligence is owed by owners. Nor were there good policy reasons to create a new category of persons, namely subcontractors, to which owners owed a duty of care.

Main Contract Creates No Duty Of Care

Air-Tite relied upon a provision in the main contract between Defence Construction and Dobbin (Article 4.6) which prohibited Dobbin from changing the subcontractor without the permission of Defence Construction.

The terms of the main contract were incorporated into the contract between Air-Tite and Dobbin. The trial judge had held that Article 4.6 created a duty of care between Defence Construction, as owner, and Air-Tite, as subcontractor, requring Defence Construction to use reasonable care in consenting to Dobbin terminating the subcontract with Air-Tite and replacing it with another subcontractor.

The Court of Appeal rejected this proposition. The Court of Appeal held that the terms of the main contract could not, by themselves, create a duty of care by the owner to the subcontractor. Rather those terms were the "means for Defence Construction to oversee the manner in which Dobbin executed its part of the bargain." These considerations worked against, not for, a conclusion that the main contract created proximity of relationship between the owner and the subcontractor. In the Court's view, Air-Tite's arguments were an attempt "to shift responsibility for Dobbin's wrongful termination of its contract with Air-Tite to Defence Construction when the latter was not privy to the subcontract."

Bid Depository System Creates No Duty Of Care

The Court of Appeal also rejected that Air-Tite's submission that a duty of fairness arose from the tender process and created a duty of care from the owner to the subcontractor.

As the Court said:

"While such a duty of fairness may have been a general expectation of Air Tite, there is no basis on which to conclude that Defence Construction and Air-Tite had a relationship that, as between those parties, created expectations or reliance which would impose the duties suggested by Air-Tite on Defence Construction."

Nor could the bid depository system, without more, establish subcontractors as a new class of persons to whom owners owe a duty of care, particularly in relation to the alleged wrongful termination by the contractor.

The Court continued:

"This is not a situation that fits within or is analogous to a relationship previously recognized as imposing a duty of care between the parties. Neither is it a situation where a new duty of care should be established."

Damages For Breach Of The Subcontract

The Court of Appeal also dismissed Dobbins appeal from the trial judgment holding it liable to Air-Tite for not retaining Air-Tite to perform the additional remedial work. The Court held that Air-Tite had no right to be awarded that work as Dobbin's contractual right to make changes in the work encompassed the right to assign the remedial work to another subcontractor and not Air-Tite. Nevertheless, the Court held that Dobbin had wrongfully terminated the subcontract and that, had that not occurred, Air-Tite "would have been retained to do the work that was contracted" to the third party.

This latter conclusion is open to question. The amount of damages to be awarded for breach of contract is not based upon the probabilities of what the defendant "would have done" but upon what the defendant was <u>entitled</u> to do. Even if Dobbin wrongfully terminated the subcontract, its liability for damages cannot be greater than the amount it would have had to pay Air-Tite had it acted in accordance with the subcontract: ***Hamilton v. Open Window Baker***

Ltd., [2004] 1 S.C.R. 303. Accordingly, if Dobbin was entitled to award the additional work to another subcontractor – as the court found – then it should not have been liable to Air-Tite based upon whether or not it might have or would have awarded the additional work to Air-Tite.

The Important Issue: No duty of care by an owner to a tendering subcontract

The first point in this decision is of considerable importance. The Newfoundland and Labrador Court of Appeal has held that, as a matter of principle, a bid depository system does not create a duty of care by the owner in favour of the subcontractor. This decision extends and solidifies the decision by the Supreme Court of Canada in ***Design Services***. In the latter case, the subcontractor was given the option to join a joint venture with the contractor. The Supreme Court of Canada held that, in that circumstance and when the subcontractor did not take up that option, there could be no duty of care between the subcontractor and the owner.

The decision of the Newfoundland and Labrador Court of Appeal shows that the principle in ***Design Services*** is of general application. In the absence of specific facts giving rise to a special relationship, an owner has no duty of care to a subcontractor arising from a bid depository system.

Construction Law - Duty of Owner to Subcontractor - Tendering

Defence Construction (1951) Limited v. Air-Tite Sheet Metal Limited, 2011 NLCA 67

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