

## The Facts on Fair and Open Contract Bidding

June 5, 2019

The Ontario Construction Secretariat (OCS) has released a twelve-page paper aimed at discrediting Cardus' work on open tendering in Ontario. Its paper comes just as the City of Toronto considers a June 2019 staff report that recommends the city finally adopt fair and open bidding for its construction projects. Sadly, the OCS response to that staff report, *Just Not Credible: Challenging Claims About Closed Tendering in Ontario*, is full of vague generalities, non-sequiturs, and inconsistencies, which will be addressed below. But the OCS paper is also notable as an example of what takes place when businesses that have become accustomed to government-backed privilege and immunity from competition in a diverse marketplace are suddenly faced with the prospect of having to earn their place in a market, rather than having a government secure their business for them.

The Economic Club of Canada hosted a conference in February 2019 that revolved around the question: "Is Construction in Ontario Open for Business?" In his address, Cardus Executive Vice President Ray Pennings noted that the assertions such as those made by the OCS about closed tendering, while cloaked in high-minded language, "are cover for brass-knuckles fights for market share and have very little to do with protecting working conditions for workers."<sup>1</sup>

We're seeing those brass knuckles in the new OCS report. Those brass knuckles are also aimed below the belt, not just at Cardus, but at other reputable organizations like the OECD, a community of economists and policy makers, and the municipalities that have experienced a significant reduction in the diversity of their bidding pools and decreased capacity in securing water treatment plants, city parks and recreation facilities, and other infrastructure.

Public infrastructure is paid for by all, and intended for the use of all in a given community. We all must pay for it, and we all can use it. What the OCS is asking is that only a select few can build it. Even apart from the economics, allowing select firms to benefit and penalizing other firms because of the private choices of their workers is fundamentally wrong as a matter of natural justice, and it is certainly out of step with the duty of government to not discriminate based on the private choices of its citizens. This is particularly true for a government like Toronto that "believes that the diversity among its people has strengthened Toronto" and that has committed to "equitably treating communities and employees, fairly providing services, by consulting with communities and making sure everyone can participate in decision-making."<sup>2</sup>

The OCS paper is a sucker punch aimed at workers who exercised their constitutionally-protected right to associate with an organization of their choosing; at taxpayers who are not able to benefit from the full diversity of Ontario's construction market; and ultimately at citizens who are faced with the choice of getting less infrastructure, paying more taxes, or seeing social programs robbed to pay more for the infrastructure that we all use.<sup>3</sup>

The economics, while they matter a great deal, are secondary to this important point. Government procurement should not discriminate against people because they make different choices about whom they

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<sup>1</sup> <https://www.cardus.ca/research/work-economics/articles/remarks-for-economic-club-of-canada-presentation/>

<sup>2</sup> <https://www.toronto.ca/city-government/accessibility-human-rights/equity-diversity-inclusion/>

<sup>3</sup> <https://www.thestar.com/opinion/commentary/2015/07/28/making-public-housing-dollars-go-further.html>

associate with. *That which is paid for by all, should be accessible to all who are qualified, regardless of their association.*<sup>4</sup>

Moreover, the assertions made by the OCS in its report suffer from a fundamental failure to understand why competitive procurement is valued by governments around the world, and why competition matters for the public good. We address these assertions in turn.

1. The OCS claims that the real objective of Cardus “is to transfer work from workers who belong to building trades unions to workers who belong to CLAC unions.” In fact, we make no pretense of knowing who will win the work in an open tendering environment, nor, frankly, do we have a preference. The point of open tendering, and why it is so valuable and integral to a democratic society, is that it allows the full diversity of firms to compete to meet the city’s needs without requiring city officials to make private judgments about which union they prefer. The city sets objective criteria, and firms must work within those criteria to provide the city what it needs at a reasonable cost. These criteria may include safety qualifications and other objectives. The firms that meet those criteria best, at the best price, have the privilege of completing the project. Procurement experts note that “membership in a particular trade union does not provide an objective criterion for the purposes of public procurement.”<sup>5</sup>
2. The OCS claims that our “purported basis for the 15% cost savings” is that “contractors who are not associated with the building trades are 2% to 40% cheaper.” Cardus says no such thing. In fact, we say the opposite. We note that “many projects completed by union, non-union, and alternative union firms are completed on time, and on budget, or even ahead of time and ahead of budget” and that “a variety of highly successful companies—all of which do public work in various jurisdictions across the country—work with a variety of labour models to deliver value to their customers.”<sup>6</sup> Open tendering is *not* about stacking the deck in any way; it is not even about saying that any given firm, with any given labour arrangement, at any given time, will be cheaper or better. That may change depending on the project or the situation. It is about ensuring a structure that will allow the greatest variety of qualified firms to bring their unique specialization and organization to bear on city work. Closed tendering diminishes the city’s choices and limits its options for no good reason.
3. The OCS asserts that achieving 15% cost savings would “require payroll costs to be reduced by almost half” and that “there is no other way to achieve cost reductions of that magnitude.” This assertion is particularly revealing, as it shows the extent to which the OCS is willfully ignoring the way that firms set prices. Firms do not compete simply on the price of labour, and to assume this is willfully ignorant of the realities of the marketplace and Toronto’s unique context. In fact, Toronto city staff in their own report note that a variety of factors go into the price offered by firms, including: “the overall state of the economy; the state of the construction industry specifically; *the amount of competition between firms*; the ability to negotiate on access to and prices for equipment, materials, and labour.”<sup>7</sup> Yet, *neither the OCS nor the city’s staff report account for any of these additional factors.*<sup>8</sup>
4. As a leading textbook on construction pricing and contracting notes: “When work is scarce in the submarket, the average number of bidders for projects will be larger than at times of plenty. The net result of scarcity is likely to be the increase in the number of bidders per project and

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<sup>4</sup> <https://www.cardus.ca/research/work-economics/reports/hiding-in-plain-sight-evaluating-closed-tendering-in-construction-markets/>

<sup>5</sup> <https://www.cardus.ca/research/work-economics/reports/hiding-in-plain-sight-evaluating-closed-tendering-in-construction-markets/>

<sup>6</sup> <https://www.cardus.ca/research/work-economics/reports/skimming-off-the-top/>

<sup>7</sup> City Manager’s Report to City of Toronto. *Labour and Training Costs in Construction Procurement*.

September 23, 2008. p. 15 <http://www.toronto.ca/legdocs/mmis/2008/ex/bgrd/backgroundfile-15927.pdf>

<sup>8</sup> For a full analysis of the City staff report, see <https://www.cardus.ca/research/work-economics/reports/tuning-up-ontarios-economic-engine-a-cardus-construction-competitiveness-monitor-brief/>

downward pressure on the bid price for each project in the submarket.”<sup>9</sup> This insight is corroborated in a study conducted by University of Toronto economist Dr. Morley Gunderson, Western New England University economist Dr. Tingting Zhang, and me that showed that restricted bidding placed “significant upward pressure” (gaps between bids increased by over 100% in closed environments) on prices in Ontario municipal construction markets that were closed.<sup>10</sup>

5. As we note, “the price for a given project is an emergent property of the workers doing the building, the engineers, the logistics planners, the state of the market, the profit motive of the company (private firms have different obligations than publicly traded ones), those who do the financing, safety records, insuring, and all other aspects of the hugely complicated business of building major infrastructure projects.”<sup>11</sup> The OCS asserts that the discrete expenses must be reduced, but fail to account for how those things work in tandem, and fail to account for the basic principle of competitive advantage: “Firms working in different sectors develop different specialities—some firms, for instance, may specialize in building hockey arenas. Others may excel at water treatment plants. And as the firms develop this expertise, they can tune their operational structures to lower costs for owners while still making a profit and offering high wages. Having a diversity of labour pools changes the composition of firms in ways that introduce unique possibilities for efficient, effective, safe work.”<sup>12</sup> Right now, the City of Toronto is prevented from accessing those unique competitive advantages that arise out of a diverse marketplace.
6. The OCS bandies about a purported mere 1.7% increase in costs because of closed tendering. But that figure does not account for all the factors that influence a project’s cost. The OCS’s figures simply are not credible. Indeed, it seems that on all matters in their paper, asserting something is the same as analyzing the work and methods of organizations such as the OECD and respected academics on the importance of fair, open, and competitive tendering. They are asking the City of Toronto to ignore the universally-recognized benefits of fair competition on prices in favour of baseless assertions and innuendo. They rightly note that Cardus is a faith-based think-tank, but it is they who are asking politicians to ignore the consensus and take their word on blind faith.
7. It is also important to note here that the OCS is not a disinterested party, but has a financial interest in the outcome of this decision. Its very reason for being is the “advancement of the unionized construction industry in Ontario,”<sup>13</sup> and it receives state support for advancing a particular subset of the whole industry in Ontario. They have a clear bias in favour of maintaining an environment where the firms and unions that pay their bills receive preferential treatment and do not have to compete for the privilege of earning money on projects that are paid for by all city taxpayers.
8. It is notable that the OCS does not address the importance of fair and open competitive bidding for preventing collusion. The OECD, for instance, draws a very clear line between the number of bidders and corruption, bluntly noting that “the fewer the number of sellers, the easier it is for them to reach an agreement on how to rig bids.”<sup>14</sup> Indeed, this is already an issue for the City of

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<sup>9</sup> Hendrickson, Chris. *Project Management for Construction: Fundamental Concepts for Owners, Engineers, Architects and Builders*. Carnegie Mellon University, Pittsburgh, PA. 2000.

[https://www.cmu.edu/cee/projects/PMbook/08\\_Construction\\_Pricing\\_and\\_Contracting.html#8.6%20Principles%20of%20Competitive%20Bidding](https://www.cmu.edu/cee/projects/PMbook/08_Construction_Pricing_and_Contracting.html#8.6%20Principles%20of%20Competitive%20Bidding)

<sup>10</sup> <https://www.cardus.ca/research/work-economics/reports/up-up-and-away/>

<sup>11</sup> <https://www.cardus.ca/research/work-economics/reports/skimming-off-the-top/>

<sup>12</sup> <https://www.cardus.ca/research/work-economics/reports/skimming-off-the-top/>

<sup>13</sup> <https://www.ontario.ca/laws/regulation/930187>

<sup>14</sup> “Guidelines for Fighting Bid Rigging in Public Procurement: Helping Governments to Obtain Best Value for Money.” OECD, n.d. <http://www.oecd.org/competition/cartels/42851044.pdf>

Toronto in a variety of sectors. Its auditor general noted that the city's procurement process had "telltale signs of bid-rigging and inflated pricing," and "even more concerning was the fact that most district contracts were consistently dominated by a small group of contractors over the past five years."<sup>15</sup> Maintaining a closed environment in the industrial, commercial, and institutional (ICI) sector is at odds with the city's overall strategy of broadening its contractor base in its procurement practices, and out of step with recommendations from the OECD and best practices recommended by the city's own procurement directives.

9. Toronto already notes that it wishes to maintain the integrity of its procurement process by ensuring that, "whenever possible, competitive methods of procurement will be used to obtain the best value for the City." It defines competitive procurement as a case where "suppliers are given an equal opportunity to bid, whether by invitation or by advertisement to the public, and which may include a process for conducting negotiations with one or more suppliers."<sup>16</sup> Choosing to restrict bidding based on union affiliation alone is at odds with the city's own understanding of equal opportunity to bid.
10. Finally, the OCS asserts that a move toward open tendering will weaken equity programs and labour force development, and will lead to a breakdown in safety on city jobs. Again, they do not make the case for how restricting tendering contributes to these outcomes, but simply assert that they are true. Nor do they make any case for why procurement—as opposed to another policy—is the optimal means for achieving these admirable objectives. However, the issue of safety, in particular, is worthy of a direct response.
11. They assert that union firms are safer, but fail to point out that, again, they have simply ignored hugely important variables in their analysis. There are public certifications given to firms (of all sorts) with strong safety records. The IHSA's Certification of Recognition (COR) is but one example.<sup>17</sup> The Infrastructure Health and Safety Association (open to all, regardless of union qualification) is "the only Authority having Jurisdiction to grant COR™ Certification [for safety] in the province of Ontario." Firms acquire this certification by being safe, regardless of their union status. Now, it's entirely possible that more unionized firms have COR certification than non-union firms, but in an open tendering situation, this would give unionized firms a competitive advantage regardless. Most, if not all, ICI projects in Toronto have safety as a criteria for firms to pre-qualify to bid. Pre-qualification is one method of screening out unsafe firms. That is, you have to be safe or you don't qualify to bid. Most municipalities are completely agnostic about whether a company is unionized or not, and this is how it should be. Owners care about good results and safe sites, not who workers choose to represent them. The paper cited by OCS argues that the unionization of a given firm is what makes the firm safe. But the paper does not include pre-qualification or COR certification as covariates in its analysis, or, worse from the point of view of credibility, included pre-qualification criteria for the union side only and not for the non-union side. It controls for firm size, but does not account at all for whether the project that a firm worked on did or did not have safety pre-qualification criteria or other safety requirements. This is a massively important variable, and not accounting for it could easily skew the numbers significantly. Given the prominence of public construction in Ontario's ICI construction market, it's likely the unionized sample is disproportionately weighted to public projects that have pre-qualification criteria. And this means that the so-called "union safety effect" is likely masking a more dominant "owners' commitment to safety" effect. Safety pre-qualification by public owners like the City of Toronto is the real safety driver in Ontario construction, and opening up the market to all firms would spread that commitment to safety across the industry as a whole, regardless of union affiliation.

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<sup>15</sup> <https://www.toronto.ca/legdocs/mmis/2017/au/bgrd/backgroundfile-102117.pdf>

<sup>16</sup> [https://www.toronto.ca/legdocs/municode/1184\\_195.pdf](https://www.toronto.ca/legdocs/municode/1184_195.pdf)

<sup>17</sup> <https://www.ihsa.ca/certificate-of-recognition/>

It is important to remember that closed tendering treats the City of Toronto like a private firm that is driven by the profit motive rather than public service. It is not. The City of Toronto is a corporation whose goal is to serve all of its citizens, regardless of their private beliefs, associations, and identities, and to provide them with an equal opportunity to build the beautiful city in which they live, work, play, and raise their families.

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