



# Newsletter



## New U.S. Food Safety Regulations Will Impact Canadian Food Haulers

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**CONTEST**

The U.S. Food Safety Modernization Act (“FSMA”) was enacted on January 4, 2011 but sat idle until after the U.S. election. Now, lawmakers in the U.S. are acting on the legislation and putting it into effect.

The FSMA gives the Food and Drug Administration (“FDA”) “sweeping new powers,” including the ability to send people to prison for felonies related to the careless or negligent handling of food.

Under the new rules, food companies will be required to demonstrate care of their products through the entire supply chain, or from “field to fork.” This, of course, extends to the transportation of their products.

Exactly two years after the FSMA enactment the FDA released two proposed Rules – one relating to the hazard analysis and risk-based preventive controls requirements of FSMA and the other relating to the establishment of science-based standards for growing, harvesting, packing and holding produce on domestic and foreign farms. Comments on both proposed rules are due by May 16, 2013.

### *Preventive Control Requirement*

One of the key aspects of the FSMA is the requirement that food facilities recognize and address risks associated with their product by implementing requirements for “hazard analyses” and “risk-based preventive controls”. Unfortunately, the FSMA doesn’t provide any insight into what these hazard analyses or

## FIRM AND INDUSTRY NEWS

- **Fernandes Hearn LLP** is pleased to announce that the Firm has been listed for inclusion in Chambers and Partners Global 2013 as one of the best "Shipping" Law Firms in Canada.
- **Gordon Hearn** was recently profiled as President of the Transportation Lawyers Association in its April edition of *Lawyer Monthly* magazine. The interview focused on the Association and developments in the area of Transportation Law.
- **Rui Fernandes** presented a paper on “*New Developments in Canadian Subrogation Law*” at the Recovery Forum in New York on April 11<sup>th</sup>, 2013 and presented a webinar for the Ontario Trucking Association on the *Kruger Products Limited v. First Choice Logistics Inc.* decision and implications for the trucking industry on April 25<sup>th</sup>, 2013.
- **Rui Fernandes, Gordon Hearn** and **Kim Stoll** will be representing the firm at the Transportation Lawyers Association Annual Conference and the Canadian Transport Lawyers’ Association Mid-Year Meeting in Napa, California on April 30<sup>th</sup> to May 4<sup>th</sup>, 2013. **Gordon Hearn** is the current President of the Transportation Lawyers’ Association and is running the conference in Napa and will be giving opening remarks. **Kim Stoll** will be moderating the Canadian Law Workshop where **Rui Fernandes** will be presenting a case review.



- **Kim Stoll** will be representing the firm at the annual conference of The Chartered Institute of Logistics and Transport in North America in Montreal, Quebec on May 7, 2013.
- **Rui Fernandes, Kim Stoll** and **Chris Afonso** will be representing the firm at the annual Canadian International Freight Forwarders Gala Dinner in Mississauga on May 9th, 2013.
- **Chris Afonso** will be presenting a paper on “Third Party Logistics Contracts: Avoiding Common Pitfalls” at the 46<sup>th</sup> Annual Conference for Supply Chain Canada in Mississauga on May 14<sup>th</sup>, 2013.
- **Rui Fernandes** and **Kim Stoll** will be representing the firm at the Semi-Annual Meeting of the Canadian Board of Marine Underwriters on May 22 and 23<sup>rd</sup>, 2013 at Manoir Saint-Sauveur Quebec.
- **Rui Fernandes** will be presenting on a panel on “Law & Order: Police and Criminal Investigation in the Boating and Small Vessel Sector” at the annual seminar of the Canadian Maritime Law Association on June 7<sup>th</sup>, 2013 in Toronto.
- **Rui Fernandes** will be presenting a paper on “Constitutional Jurisprudence in Transportation Law – Perspectives on Canadian Federalism and the Division of Powers” at the Commons Institute *Seminar on Supreme Court and Constitutional Litigation* in Toronto on June 27<sup>th</sup>, 2013.
- **LexisNexis Canada** has released its **Halsbury's Laws of Canada – Maritime Law** title. **Rui Fernandes** is the author of this new work. This completes Rui’s trilogy of works for LexisNexis’ Halsbury’s Laws of Canada. Last December his Transportation – Carriage of Goods and Transportation – Railway Law was published. The current work is described by LexisNexis with the following introduction:

“The globalization of the economy has ballooned the international shipping community in size, making the sea an integral means of modern trade. This title is a complete source of admiralty law across Canada. Covering both the general issues of maritime law, such as its legislative and constitutional framework, and the more specific issues, such as regulatory and safety requirements and the operation of ships, this title is essential for practitioners working in fields of trade, administrative and international law.”

risk-based preventive controls should look like.

The rule proposes to amend the FDA's regulation for Current Good Manufacturing Practice in Manufacturing, Packing, or Holding Human Food to modernize it and add requirements for the establishment and implementation of hazard analysis and risk-based preventive controls by domestic and foreign facilities.

These preventive controls would include requirements for food facilities (with limited exceptions) to maintain a food safety plan, perform a hazard analysis, and institute preventive controls for the mitigation of those hazards. Facilities would also be required to monitor their controls, verify that they were effective, take any appropriate corrective actions, and maintain records documenting these actions. All records have to be kept for two years and be available to the FDA. Trucking companies must now determine by asking their clients who ship food as to where they fit in the plan.

The new regulations will also require a product tracing system that can be used to track and trace all food products that are produced in or imported into the U.S. These requirements are likely to include a temperature traceability aspect, meaning that the FDA will want to see proof that food was transported at the proper temperature throughout its journey. Trucking companies will be a vital part of any compliance plan.

A final rule is expected to be published in 2014, with full enforcement in place by 2015. Trucking companies should be prepared to face shippers insisting on more transparency

and control over the transportation of their products. Costs to trucking companies may increase in order to upgrade fleets to provide more information. Trailer manufacturers may be required to provide some of the solutions including better locking doors, compartmentalizing product from various shippers, and temperature sensors that can send information remotely.

Within the next few months, the FDA hopes to issue a proposed rule on preventative safety controls for animal feed as well as proposed regulations related to importer accountability for food safety.

The FDA is also setting requirements for the safe transport of food and hopes to have a specific proposal out later this year. It is also working to set standards to prevent intentional contamination of food.

### *Growing, Harvesting, Packing and Holding Produce*

The proposed produce rule sets science-based standards for the safe production and harvesting of fruits and vegetables to minimize the risk of serious adverse health consequences or death.

FDA proposes to set standards associated with identified routes of microbial contamination of produce, including: agricultural water; biological soil amendments of animal origin; health and hygiene; animals in the growing area; and equipment, tools and buildings.

These new rules have been slow arriving. According to the FDA, roughly one in six Americans suffers from a food-borne illness

each year, and about 3,000 die. The U.S. has had numerous outbreaks from food-borne illnesses tied to salmonella, E. coli and listeria.

“We have one of the safest food supplies in the world, but we have work to do to stop food borne illnesses before they start,” Dr. Margaret Hamburg, commissioner of the FDA said in a press conference. “While the FDA responds very quickly and effectively in response to outbreaks, containing them and

finding their source and taking other necessary actions, we really need to do more than react after the fact. Preventing problems before they cause harm is not only common sense, it is the key to food safety in the 21st century.”

After a public comment period, the FDA will adjust the rules based on the feedback.

*Rui Fernandes*



## 2. U.S. Fifth Amendment Not Valid in Ontario

This case involved a proceeding which originated with a Letter of Request issued by the Superior Court of the State of California for the County of Los Angeles, in a civil action pending in California relating to the alleged fraudulent offer and sale of securities in California. The Letter of Request sought the assistance of the Ontario court in ordering Gertrude Barnhardt a resident of Ontario to provide testimony and documents relevant to the California Action, and specifically in relation to certain alleged fraudulent transfers of money from CanAm to a corporation known as Taurus Financial Advisors Ltd. of which Gertrude Barnhardt was the sole shareholder and only officer.

The issue in this reported decision (\*1) was whether a witness on an examination conducted in an Ontario proceeding, under Ontario law, was entitled to refuse to answer questions on the basis of the Fifth Amendment to the United States Constitution (the U.S. rule against self-incrimination). Put in the vernacular, would the Ontario Court permit a witness in Ontario to “plead the Fifth”?

The concern expressed by counsel for Ms. Barnhardt was that answers given by Ms. Barnhardt under oath in Ontario, and reduced to a transcript for use in the California action, could then be subsequently utilized by the FBI or investigators to found evidentiary support against or to bring to fruition; criminal charges against Ms. Barnhardt.

The Court noted that Ontario Courts have consistently held that the process of taking evidence under Letters of Request is not

governed by foreign law where fundamental values, such as the rights of witnesses, are concerned.

The Court also noted that Canadian courts, when asked to assist courts of the United States in procuring evidence for civil trials there, should be aware of the risk that might put citizens or residents of Canada in the worst of both worlds — compulsion to testify in Canada followed by use of the compelled material in the U.S.

The judge refused to permit Ms. Barnhardt to “plead the Fifth” and made several points outlining his reasoning:

- a) There was no evidence that an FBI investigation had proceeded or matured;
- b) The receiver in the U.S. action had given an undertaking not to make the information and evidence obtained available to third parties save as may be required by law; and
- c) In some respects, the sovereignty of a U.S. court can be impinged or underappreciated, if a Canadian court rules, under circumstances such as this, as to the validity or applicability of Ms. Barnhardt’s Fifth Amendment rights. Stated differently, the Court was satisfied that the admission of transcript evidence taken in Ontario, to be potentially utilized in an American criminal proceeding against Ms. Barnhardt, was properly a matter for the American court, not a Canadian court.

The judge stated: (\*2):

It is for an American court to determine (if such determination might ever be made), whether the admission of any compelled transcript evidence from Ms. Barnhardt

would shock the judicial conscience or violate baseline due-process requirements with respect to Ms. Barnhardt's Fifth Amendment rights. Any American court considering this matter will have available to it a full record as well as an appreciation of the fact that Ms. Barnhardt's evidence was compelled by a court order made by a Canadian judge. An American court will then apply its standards to American law in determining whether any potential use of self-incriminating transcript evidence provided by Ms. Barnhardt pursuant to a Canadian court order can be introduced and made applicable in American court proceedings.

The judge was of the view that arguments relating to the rights and protections afforded by the Fifth Amendment to the United States

Constitution remained available to Ms. Barnhardt, if and when she was required to rely upon such rights in proceedings in an American court, when attempts may be made to have her compelled transcript evidence used against her.

*Rui Fernandes*

Endnotes

(\*1) *Davidson v. Barnhardt et al.* (2012) 113 O.R. (3d) 475.

(\*2) *Ibid*, at paragraph 17.



### 3. Duty of Insurer on a Fleet Policy to Point Out Gaps in Coverage

In *Ostenda v. Miranda* (2012) ONSC 7346, the litigation had its origin in a motor vehicle accident that occurred on October 23, 2008 in Gurnee, Illinois, U.S.A. According to the statement of claim, on that occasion, the defendant Bahena Miranda was driving a car that struck the plaintiff Jan Ostenda, causing him catastrophic injuries. At the time, Mr. Ostenda was a truck driver employed by a transportation company known as Synergy Transportation System Inc. Zurich had issued a fleet motor vehicle coverage policy to Synergy, and thus Mr. Ostenda was covered by that policy.

The Zurich policy issued to Synergy did not contain a so-called "family protection coverage endorsement – OPCF44R". An OPCF44R endorsement, when included with an automobile insurance policy in Ontario, provides uninsured or underinsured coverage. Where an injured party is covered by such a policy (including an OPCF44R endorsement) and he or she is injured through the negligence of an uninsured or underinsured driver, the injured party may recover the balance of their monetary damage award against their own insurer (up to their own policy limits).

Bahena Miranda had either no insurance or very modest insurance coverage. Mr. Ostenda sued Zurich and his insurance broker for failing to include the OPCF44R endorsement. The statement of claim asserted that Zurich held out the broker as its agent and was, therefore, in law responsible for the negligence and breach of contract of the broker. The statement of claim further asserted that Zurich was negligent itself by reason of its failure to require the broker to

inform and advise Synergy and Ostenda of the availability and need to obtain underinsurance coverage.

The court held that it is well established that insurance brokers owe a duty to their customers to provide not only information about available coverage, but also to advise about which forms of coverage and the costs customers require in order to meet their needs. The court referred to the Supreme Court of Canada decision in *Fletcher v. Manitoba Insurance Co.* (\*1) and to the decision of the Ontario Court of Appeal in *Fine's Flowers Ltd. v. General Accident Assurance Co. of Canada* (\*2).

The court held that the broker was involved on behalf of the insured and had to meet duties as set out in *Fletcher* and in *Fine's Flowers*. The coverage that was offered by Zurich and the policy it ultimately issued were consistent with that requested by the broker, in that they did not reference or include OPCF44R coverage. The broker's liability was not in issue in this reported decision. The real issue was the liability of Zurich, if any.

After it received the application from the broker, Zurich conducted its own risk assessment of Synergy's operations, and it did so in relation to subsequent policy renewals. In the course of those risk assessments, Zurich's representatives interacted with Synergy's personnel and prepared and supplied risk assessment reports to Synergy. Mr. Ostenda submitted that this interaction and, in particular, Zurich's involvement and its advice to Synergy regarding risks, were such as to impose a duty upon Zurich to warn and counsel Synergy regarding potential gaps in its insurance coverage. The court

disagreed. Justice Stinson stated (\*3):

To extend the principle in *Fine's Flowers* to the present case would require the court to accept that Zurich was performing the same function as the broker and accordingly had the same duties. The extension of that principle, however, would require the court to accept that the customer looked to the insurer and placed reliance upon it in the same fashion as the customer in *Fine's Flowers* did in its broker, and further that the insurer knowingly and willingly undertook the responsibilities of a broker in the same fashion. In my view, the evidence in the present case fails to establish either premise.

The court added at paragraph 45:

From a public policy perspective, I reach the same conclusion. Professional insurance brokers are a regulated industry with codes of conduct and specific obligations. They perform specific services, including assessing customers' insurance needs, preparing and advising with respect to applications for insurance coverage and procuring insurance policies for the customer. For so doing, they are compensated, frequently on the basis of a commission paid by the insurer as a percentage of the policy premium. That commission income covers the costs of the services provided by the broker.

Interestingly, the judge also noted that if the law were to impose upon insurers a similar

duty to that undertaken by brokers – to explore and advise regarding a customer's insurance requirements – considerable duplication of effort would result. In effect, insurers would be required to perform virtually the same function as brokers. The result would be a duplication of effort and expense that would inevitably be passed on to the customer, thereby increasing the costs of insurance coverage.

The court also rejected the argument that Zurich should be responsible for the failure of the broker as its own agent. The evidence did not show that the broker had any legal authority to represent Zurich. There was no evidence that the broker had authority to bind Zurich in relation to the risk or to countersign the policy. Rather, the policy was issued by Zurich and not the broker.

*Rui Fernandes*

Endnotes

(\*1) [1990] S.C.J. No. 121

(\*2) 17 O.R. (2d) 529 (C.A.)

(\*3) at paragraph 37



#### 4. Punitive Damages Update: An Award of \$4.5 Million Against Two Insurers

There have been several cases recently where awards of punitive damages have been granted. The Supreme Court of Canada seminal case of *Pilot v Whiten*, cited below, was shocking both in facts and the penalty applied. The Supreme Court of Canada set out the parameters for consideration by courts for those situations where the actions of insurers in respect of their insureds were considered to be so outside the appropriate as to attract a punishing monetary award. With this in mind, the top award of punitive damages against an insurer as confirmed by the Supreme Court of Canada in *Pilot v Whiten* was \$1,000,000. The Saskatchewan Court of Queen's Bench has now weighed in with a possible new high-water mark. The case is under appeal and we will know in due course whether the award will stand or be over-turned.

This article will revisit the *Pilot v Whiten* case and review *Branco v. American Home Assurance Co.*, *infra* (a decision of the Saskatchewan Court of Queen's Bench).

##### *Punitive Damages Review: The Current High-Water Mark Case - Pilot v Whiten*

It is, of course, important to review where we have been in order to examine where we are going. The Supreme Court of Canada in the *Whiten v Pilot Insurance Corporation* [2002] 1 S.C.R.595 ("*Pilot v Whiten*") provided the standard that all insurers live by in terms of appropriate activity. Essentially, there is an implied obligation on the part of the insurer

to deal with claims of its insured with the utmost good faith.

*Pilot v. Whiten* was a shocking case. Binnie J.'s opening words in his reasons in the first paragraph of the case basically said it all.

1. This case raises once again the spectre of uncontrolled and uncontrollable awards of punitive damages in civil actions. The jury was clearly outraged by the high-handed tactics employed by the respondent, Pilot Insurance Company, following its unjustified refusal to pay the appellant's claim under a fire insurance policy (ultimately quantified at approximately \$345,000). Pilot forced an eight-week trial on an allegation of arson that the jury obviously considered trumped up. It forced her to put at risk her only remaining asset (the insurance claim) plus approximately \$320,000 in legal costs that she did not have. The denial of the claim was designed to force her to make an unfair settlement for less than she was entitled to. The conduct was planned and deliberate and continued for over two years, while the financial situation of the appellant grew increasingly desperate. Evidently concluding that the arson defence from the outset was unsustainable and made in bad faith, the jury added an award of punitive damages of \$1 million, in effect providing the appellant with a

“windfall” that added something less than treble damages to her actual out-of-pocket loss.”

The Court of Appeal had overturned the jury’s award of \$1,000,000 and reduced it to a more traditional and modest amount of \$100,000.

Binnie J. and the majority of the Supreme Court of Canada, however, reinstated the jury’s unprecedented award. Binnie J. noted the trial judge’s statement, when endorsing the jury’s decision, that a very substantial punitive damage award was required to “... punish the defendant and to effectively send the implied reminder to the defendant and to other insurers that they owe their insureds a duty of good faith in responding to claims made under policies of insurance issued by them.” The award, though high, was within “rational limits”. (\*1)

In its decision, the Supreme Court of Canada set out the principles governing punitive damages in a series of points:

- (1) Punitive damages are very much the exception rather than the rule
- (2) *they are imposed only if there has been high-handed, malicious, arbitrary or highly reprehensible misconduct that departs to a marked degree from ordinary standards of decent behaviour.*
- (3) Where they are awarded, punitive damages should be assessed in an amount reasonably proportionate to such factors as the harm caused, the degree of the misconduct, the relative

vulnerability of the plaintiff and any advantage or profit gained by the defendant.

(4) Having regard to any other fines or penalties suffered by the defendant for the misconduct in question.

(5) Punitive damages are generally given only where the misconduct would otherwise be unpunished or where other penalties are or are likely to be inadequate to achieve the objectives of retribution, deterrence and denunciation.

(6) Their purpose is not to compensate the plaintiff, but

(7) to give a defendant his or her just desert (retribution), to deter the defendant and others from similar misconduct in the future (deterrence), and to mark the community’s collective condemnation (denunciation) of what has happened.

(8) Punitive damages are awarded *only* where compensatory damages, which to some extent are punitive, are insufficient to accomplish these objectives, and

(9) they are given in an amount that is no greater than necessary to rationally accomplish their purpose.

(10) While normally the state would be the recipient of any fine or penalty for misconduct, the plaintiff will keep punitive damages as a “windfall” in addition to compensatory damages.

(11) Judges and juries in our system have usually found that moderate awards of punitive

damages, which inevitably carry a stigma in the broader community, are generally sufficient.

(emphasis added)

*Pilot v Whiten* is considered to be the “high-water mark”. There is now potentially a new high-water mark case that is making its way up the appeal ladder.

*Branco v American Home Assurance, Cameco Corporation, Kumtor Operating Company and Zurich Life Insurance Company, 2013 SKQB 98 (Saskatchewan Court of Queen’s Bench) March 21, 2013.*

#### *Facts*

Luciano Branco was employed by Kumtor Operating Company as a welder in Kyrgyzstan. He was described by the court as being an excellent employee with a perfect attendance record. Unfortunately, Mr. Branco suffered a work related injury to his foot. American Home provided insurance akin to Workers Compensation benefits (the “WCB insurer”). Zurich Life Insurance Company, located in Switzerland, provided long term disability benefits (the “LTD insurer”).

Even though Mr. Branco had surgery and took physiotherapy and rehabilitation therapy, according to his doctor, he was permanently disabled and unable to return to his employment. The WCB insurer, despite this confirmation of status, made a cash settlement offer of \$22,500 US. A comment was made in file by the handler:

I called the claimant and he did not accept our offer and said that

he was going to get an attorney. I hope he re-considers because he lives in Portugal and he will have to go back to Canada to get an attorney and this whole process is going to take years to settle. Here we go CANADA!!!!

It went downhill from there from requiring Mr. Branco to pay for his own rehabilitation and medical appointments to insistence on retraining at jobs well below his previous earning potential and incompatible with his then current physical ability. Mr. Branco went where he was directed to go including a vocational rehabilitation facility over three hours from his home in Portugal. Despite an opinion from the Saskatchewan Workers Compensation Board that Mr. Branco was not an appropriate candidate for retraining given his nearness to retirement of about 10 years, the insurer took this as a refusal to take rehabilitation and ultimately discontinued payment of benefits in 2004. Further, there was payment inconsistency over the years for no apparent reason. Even after agreement that Mr. Branco was entitled to various lifetime payments, these were not made until the day before trial. The WCB insurer was said to have engaged in court delay tactics.

With regard to the LTD Insurer, there were some difficulties with the proper submission of forms. The LTD insurer rather than paying benefits brought legal proceedings in the Canadian proceedings alleging that Switzerland was the more convenient forum. Costs were awarded against the LTD insurer. Even though the LTD insurer agreed that the first 24 months of benefits were payable (“disabled from his own occupation”), it refused to pay benefits after Mr. Branco would not accept an inappropriate reduction

of \$9,000 representing legal fees incurred even though there was the award of costs against the insurer. The payments were not made up until 9 years after the accident and nearly 6 years after litigation started and 1.5 years after the independent medical, which it eventually accepted. The LTD insurer instead engaged in low offers to settle and engaged in numerous court delay tactics. It failed to pay despite knowing there was an obligation to do so and when it knew that Mr. Branco was severely affected.

Throughout the years in which the case took to get to trial, Mr. Branco suffered financially to the point where he relied on family loans and borrowed clothing. His marriage was damaged and he was depressed. Mr. Branco was ashamed that he was unable to support himself and his family, which went to the root of his personal self-worth and integrity. He was put through many defence medicals and was diagnosed by 7 out of 10 doctors as having a rare disorder, Reflex Sympathetic Dystrophy or complex regional pain syndrome, which has a very poor success rate of rehabilitation.

#### *The Decision on Punitive Damages*

Acton J. cited *Pilot v Whiten* as the accepted law in Canada on punitive damages and quoted extensively from it, including the following excerpt from Binnie J.:

102. The respondent claims that an insurer is entirely within its rights to thoroughly investigate a claim and exercise caution in evaluating the circumstances. It is not required to accept the initial views of its investigators. It is

perfectly entitled to pursue further inquiries. I agree with these points. The problem here is that Pilot embarked on a “train of thought” as early as February 25, 1994 (see para. 7 above) that led to the arson trial, with nothing to go on except the fact that its policy holder had money problems.

103. The “train of thought” mentioned in the letter to Pilot from Derek Francis kept going long after the requirements of due diligence or prudent practice had been exhausted. There is a difference between due diligence and wilful tunnel vision. The jury obviously considered this case to be an outrageous example of the latter. In my view, an award of punitive damages (leaving aside the issue of quantum for the moment) was a rational response on the jury’s part to the evidence. It was not an inevitable or unavoidable response, but it was a *rational* response to what the jury had seen and heard. The jury was obviously incensed at the idea that the respondent would get away with paying no more than it ought to have paid after its initial investigation in 1994 (plus costs). It obviously felt that something more was required to demonstrate to Pilot that its bad faith dealing with this loss claim was not a wise or profitable course of action. The award answered a perceived need for retribution, denunciation and deterrence.

104. The intervener, the Insurance Council of Canada, argues that the award of punitive damages will over-deter insurers from reviewing claims with due diligence, thus lead to the payment of unmeritorious claims, and in the end drive up insurance premiums. This would only be true if the respondent's treatment of the appellant is not an isolated case but is widespread in the industry. If, as I prefer to believe, insurers generally take seriously their duty to act in good faith, it will only be rogue insurers or rogue files that will incur such a financial penalty, and the extra economic cost inflicted by punitive damages will either cause the delinquents to

mend their ways or, ultimately, move them on to lines of work that do not call for a good faith standard of behaviour.

105. The Ontario Court of Appeal was unanimous that punitive damages in some amount were justified and I agree with that conclusion. This was an exceptional case that justified an exceptional remedy. The respondent's cross-appeal will therefore be dismissed.

Acton J. went on to quote extensively from *Pilot v Whiten* on a number of bases including the concept of proportionality in the assessment of appropriate quantum; that is, the more reprehensible the nature of the



conduct, the higher the potential award as well as the factors involved in the assessment of blameworthiness (including planned and deliberate misconduct, awareness of the wrong, profit from the wrong, persistence in the wrong, intent and motive as well as whether the interest violated was deeply personal to the plaintiff and whether the plaintiff was vulnerable, financially or otherwise.) His Honour went on to quote Binnie J. on the issues of deterrence and rationality and appropriate quantum.

Unfortunately for the WCB insurer, Acton J. also noted a previous decision which awarded punitive damages against the WCB insurer, which case involved the same adjuster using the same tactics on another claimant worker in similar circumstances to Mr. Branco stating at paragraph 176 that the award of \$60,000 in that case was “not sufficient to prevent an immediate recurrence of the unacceptable technique.” (\*2)

Acton J. considered that the actions of both insurers had continued for over 8-13 years and that they were very aware of the hardship it was inflicting both through withholding funds and also that they engaged in litigation tactics such as numerous and expensive court applications. The actions of the insurers were considered planned and deliberate and meant to force Mr. Branco into an unreasonably low cash settlement. The insurers’ adjusters knew their actions were wrong and also took steps to ensure failure by Mr. Branco.

The award for punitive damages in *Pilot v Whiten* was \$1,000,000 for misconduct over two years. The misconduct here was over 8 to 13 years. Acton J. was not convinced that the \$1,000,000 as awarded was sufficient to stop

such misconduct as the *Pilot v. Whiten* decision was rendered during the time period that Mr. Branco’s case was being handled.

Acton J. awarded \$3,000,000 in punitive damages against the LTD insurer for behaviour that was “protracted and reprehensible” “nothing short of torturous on Branco.” He awarded \$1,500,000 in punitive damages against the WCB insurer for behaviour that was outrageous and similar in nature to previous conduct. Acton J. stated:

216. The court is cognizant of the fact that a punitive damages award of \$3 million may not be particularly significant to the financial bottom line of a successful worldwide insurance company. It is hoped that this award will gain the attention of the insurance industry. The industry must recognize the destruction and devastation that their actions cause in failing to honour their contractual policy commitments to the individuals insured.

217. Both AIG and Zurich failed to deal with Branco’s claim in good faith. Each tried to take advantage of Branco’s economic vulnerability to gain leverage in negotiating a settlement. The fact that Branco was able to continue to withstand this pressure for so many years from two different fronts is truly remarkable and almost superhuman, even though his resistance may have resulted in irreparable mental distress which may last for the remainder of his lifetime.

218. The court has grave concerns as to how often this type of action occurs in dealing with insurance claims. The court is only cognizant of the cases such as *Sarchuk*, *Whiten* and *Branco* which come before them. If *Whiten* (in the *Whiten* case) and *Branco*, in this case, had not been able to withstand the unbelievable pressure to settle on the terms and conditions originally offered these cases would not have received the attention of the courts either. The question remains: how many individuals have been unable to withstand the financial and psychological pressure of these tactics?

The highest award at any level is the award imposed in *Branco*. It appears that the “sticker shock” of the *Pilot v Whiten* case has dulled. The trial judge in *Branco* has made it

known that the court (at least at that level) will seek to punish with greater severity and has potentially opened the door to even higher awards if inappropriate conduct is as extended or more extended than that in the *Pilot v Whiten* case.

Both insurers have appealed to the Saskatchewan Court of Appeal.

Every insurer and insured should take note and watch with interest as the *Branco* case moves through the appeal process and we are witness to treatment by higher courts and whether the floodgates are indeed open.

*Kim E. Stoll*

#### ENDNOTES

(\*1) at para. 30

(\*2) *Sarchuk v Alto Construction Ltd.* 2003 SKQB 237



## 5. Aviation: Revisiting 261/04 – A Mixed Bag For Passengers and Airlines

In the January 2013 edition of the Fernandes Hearn LLP newsletter, when reviewing the 2012 *Nelson/TU* (\*1) judgments rendered by the European Court of Justice (“ECJ”) confirming the earlier *Sturgeon* (\*2) decision that EU Regulation 261/2004 (“261/04”) (\*3) afforded passengers a right to compensation in instances of delay as well as cancellation of flights, we alluded to the fact that the Commission was in the process of reviewing the infamous and broadly litigated European Union’s cornerstone legislation on air passenger rights (\*4).

After considering the outcome of a six-month stakeholder consultation process, the European Commission released on March 13, 2013 its proposal for a revision of 261/04 (\*5). The revised text seeks to redress certain imbalances created by the innovative jurisprudential law-making of the ECJ through its broad and teleological interpretation of 261/04, while broadening the Regulation’s scope to ensure passengers are protected in more circumstances. The new text reads more as a Charter of passenger rights, whereas the initial version of the Regulation was focused on delay, cancellation and denied boarding.

This overview of the key changes being proposed by the European Commission will be subdivided into the changes that benefit passengers and those that are to the advantage of the airlines.

### Pro-passenger

#### **Expansion of current benefits**

Right to care – This references the rights of passengers to access to telecommunications, refreshments, and – in case of lengthier delays – meals, accommodation and transportation to accommodation. Under the current Regulation, the time trigger for these duties to arise in cases of delay varies between two and four hours according to the flight distance. The proposal would unify the time trigger at two hours of delay. The current articulation translates a philosophy that the same delay duration to longer flights should be seen as a lesser inconvenience than for shorter operations. This approach lends itself better to differentiated rights to monetary compensation for inconvenience rather than the entitlement to alert family or friends, and to be nourished during the delay, thus this adaptation is rational.

### *Confirmation of pro-passenger jurisprudence*

In two key respects, the amended text will adopt the “pro-passengers” stances favoured by the ECJ in its case law.

Compensation for delay – Whether the omission in the drafting of the original 261/04 of a provision for compensation for lengthy delay was deliberate or inadvertent was consigned to history by the ECJ in its previously mentioned *Sturgeon* and *TUI/Nelson* decisions. A redrafted Article 6 of the Regulation will clearly provide for compensation due to passengers inconvenienced by long delays. However, the Commission proposes alternative and longer time lapses before passengers’ entitlement to compensation arises compared with those in force today under the court’s prescriptions in the *Sturgeon* case.

Extraordinary Circumstances – One of the most litigated points under the Regulation has been what constitutes extraordinary circumstances such as to exonerate a carrier from having to provide compensation to passengers. The ECJ in its *Wallentin-Herman* (\*6) decision offered a relatively restrictive interpretation of extraordinary circumstances, most notably excluding routine mechanical faults from constituting bases for exoneration. This position would be firmly adopted by the amended Regulation which would include an Annex 1 dedicated in a non-exhaustive manner to detailing what are and what are not “extraordinary circumstances”. It is also noteworthy that the airline would only be able to invoke the extraordinary circumstances where these affect the flight at issue or the flight operated immediately before by the aircraft. System-wide delays owing to extraordinary circumstances will not be a blanket catch-all defence without showing how those circumstances directly impacted the aircraft subject to delay or cancellation in its immediate operations.

### *New Rights*

*Re-routing* – Since the era of airline alliances, airlines have shown a markedly increased reluctance to rebook inconvenienced passengers on non-aligned carriers. Given the significant, and often punitive premium, placed by carriers on airfares booked at the last minute, an operator would frequently be financially better off by providing hotel accommodation and, where required, compensating passengers, as compared with rebooking them on a competitor’s service. The revised text at Article 8(5) seeks to redress this by granting inconvenienced passengers who elect to be rerouted the right

to be rebooked on a competing carrier’s flights where the operating carrier cannot make arrangements on its own services within twelve hours. This is bound to be a contentious provision given that it further imposes on the selling carrier the duty not to charge more than a recent average historical fare to the purchasing airline. This could not only lead to underpricing for the selling airline during peak season travel, but also raises issues of jurisdiction of the right of the Commission to impose fares on non-European carriers including when they are operating from their home jurisdictions.

*No-shows* - Carriers have traditionally viewed the contract of carriage as a strict sequential undertaking, which is voided by the failure of a passenger to present for any stage or leg of the flight. Given airlines’ preference that passengers purchase round-trips which allow the carrier to adjust pricing on presumptions of the nature of the travel as premised on the duration of stay, carriers have often applied prohibitive pricing to one way fares. One tool for enforcing this was by cancelling the return portion of a flight if the outbound were cancelled. The revised Article 4(4) of the Regulation prevents this practice by denying the right to carriers to cancel in-bound travel on the basis of failure to show for the out-bound leg. However, the text stops short of preventing carriers from cancelling flights within a leg of an itinerary for failure to use the flights sequentially. Hypothetical airline Air Paris may be prepared to offer a cheaper fare to fly London-Paris-Toronto than it would offer for the premium convenience of a direct Paris-Toronto leg. The Regulation, by omission of prescribing this, legitimizes Air Paris’s policy that the Paris-Toronto stage of the flight leg is

forfeited by failure to show for the preceding London-Paris stage.

*Information* – The Commission gives passengers under this draft a legislative right to information concerning their flight disruption at the soonest opportunity.

*Tarmac delays* – The new Article 6(5) legislates the rights of passengers to water and a climate controlled cabin once a tarmac delay reaches an hour, and passengers are entitled to disembark in cases of tarmac delays reaching five hours, save where safety concerns would preclude this.

*Name spelling changes* – Prohibiting the most egregious of administrative fees - reaching \$250 in the case of Ryanair - the new paragraph 4(5) proposes to require airlines to make changes to spellings of names which may lead to denied boarding situations on a gratuitous basis.

*Connecting Flights* – Passenger rights in cases of delay owing to a missed connection due to a late arrival of the preceding leg potentially by a different carrier, which were woefully overlooked in the drafting of the current 261/04, are addressed in the added Article 6a. The onward carrier would be responsible for rerouting the passenger and providing care to the passenger, whereas the airline whose late arrival caused the misconnect would owe compensation were this due. This provision will be particularly contentious owing to apparently applying to non-EU airlines where their operation from their home country into the EU is delayed, whereas these operations were previously not regulated by 261/04 as deemed *ultra petita* for the Community which could only regulate EU carriers and operations of non-EU carriers from EU airports. The provision

moreover only applied where the connection is pursuant to a single contract of carriage as the airlines have approbated the connection and submitted to the risk of misconnect. This could potentially lead to airlines increasing minimum connect times particularly where the onward flight leg is operated only once daily.

#### *Pro-airline*

Faced with the detailed onslaught of new duties, two significant concessions are afforded to airlines, in an explicit recognition that in certain instances the European Court of Justice has been overly favourable to passengers in its reading of 261/04.

*Cap on accommodation costs* – Recognizing that entirely unforeseeable conditions may arise, and with a clear hark to the Eyjafjallajökull eruption of 2010 and the contentious *McDonagh v. Ryanair* (\*7) ECJ judgment which ensued requiring low cost carriers to cover hotel accommodation for indefinite periods, a cap is set on the exposure of airlines to these expenses.

Under the proposal, the airline would not be responsible for accommodation beyond €100 per passenger and to a maximum of three nights. Some clarification in the drafting would assist here as all hotel accommodations have various rates adapted to supply and demand, and in case of extreme weather conditions or force majeure such as Eyjafjallajökull, demand can grow exponentially for airport lodgings. In these cases, airlines are best placed to obtain negotiated reasonable rates from the airport hotels and also benefit from volume booking discount, therefore it should remain incumbent upon airlines to make accommodation arrangements on behalf of

the passengers rather than simply providing €100 per passenger per night.

An additional carve out is made to exclude liability for lodgings where the flight stage is stand alone and less than 250kms.

The impact of these changes is mitigated by the new entitlement to be rerouted with competing carriers, hence in cases notably of industrial action which could create multi-day disruption, the passenger should usually be accommodated on another airline.

*Delay duration preceding compensation* – whereas the ECJ adopted in *Sturgeon* and reiterated in *Nelson/Tui* a bizarre calculation for the duration of a delay before the right to compensation arose (\*8), and the quantum of compensation owed, a more coherent, clear and restrictive prescription of delay duration is found in the draft revision at the amended Article 6(2). Delays must reach 5 hours for intra EU-journeys and journeys under 3,500 kms, 9 hours for journeys between 3,500 kms and 6,000 kms and 12 hours for journeys beyond 6,000 kms before an entitlement to compensation arises. Delay is now clearly defined as based upon arrival time compared with scheduled arrival, which means that tarmac delays may compound with push-back delays to trigger compensation rights.

It complicates matters that the time triggers for compensation for delay and for cancellation are now differentiated, especially given that the rationale for compensating delayed passengers was to ensure their equal treatment. Under this proposal it now becomes attractive for carriers to delay a flight extensively even when this could be cancelled and passengers

accommodated on other flights that it operates.

If “Air Alberta” cancelled a flight at 8AM out of London bound to Calgary, and it instead accommodated its passengers on its 11:30AM service, compensation would be due, whereas the 8AM flight could be delayed until 17:00PM without a right to compensation accruing. There should also be a single set of distance criteria to facilitate understanding and application of the Regulation. It unnecessarily complicates matters having the duration of delay triggering the right to compensation differentiated by one series of distances and the quantum of compensation due determined by a different set of distances.

In conclusion, the proposed amended Regulation elevates to legislation much of the ECJ case law interpreting the incumbent text, responds to certain iniquities which have arisen from circumstances not foreseen at the time of the 2004 draft thereby in limited circumstances capping airline exposure, prohibits certain publicized and maligned egregious practices particularly amongst the ultra low cost airlines of Europe, and creates an overall broader Charter of air passenger rights. Whereas there are improvements and clarifications, it is to be hoped that before adoption, the amendment will be subjected to a degree of legal scrutiny that was not exercised in the enactment of the incumbent 261/04.

*Mark Glynn*

## Endnotes:

(\*1) Case C-581/10 *Nelson v. Deutsche Lufthansa AG* & Case C-629/10 *TUI Travel plc et al v. Civil Aviation Authority*.

(\*2) Case C-402/07 *Sturgeon et al v. Condor Flugdienst GmbH*.

(\*3) REGULATION (EC) No 261/2004 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 11 February 2004 establishing common rules on compensation and assistance to passengers in the event of denied boarding and of cancellation or long delay of flights, and repealing Regulation (EEC) No 295/91.

(\*4) Mark Glynn, “Controversies under Regulation 261/2004 : The ECJ Reaffirms

Passenger Entitlement to Compensation for Long Delays to Flights in *Nelson v. Deutsche Lufthansa AG* and *TUI Travel plc et al v. Civil Aviation Authority*” (2013), Fernandes Hearn LLP Newsletter 2013:1.

(\*5) Online: European Commission <<http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0130:FIN:EN:PDF>>.

(\*6) Case C-549/07 *Wallentin-Hermann v. Alitalia SpA*.

(\*7) Case C-12/11, *McDonagh v. Ryanair Ltd*.

(\*8) For more detail, see Fernandes Hearn Newsletter 2013 Vol. 1 at 21.



## 6. *Unlu v Air Canada: Provincial Consumer Protection Law in a Federal Sphere*

On March 14, 2013, the British Columbia Court of Appeal upheld a ruling stating that certain sections of B.C.'s general consumer protection law are constitutionally applicable to international aviation ticketing practices and, as such, the airlines must comply with the provincial law. This decision is a boost to a potentially enormous class action involving almost every non-US international flight out of Vancouver sold by the defendant airlines. For their part, the airlines argued that the result of such a ruling would be regulatory overload, as businesses would be forced to comply with 11 different legislative regime: federal Parliament and each of the 10 provinces.

The Court of Appeal was alive to the concern of over-regulation, and the decision is narrow in scope; it constitutionally validated only one prohibition from a much broader law. Although narrow, however, the ruling provides insight into how courts in the future will treat litigation involving similar provisions of provincial consumer protection law as these laws are brought to bear on maritime, rail, and other transportation modes under the jurisdiction of the federal government.

### *Background*

Mr. Unlu launched his prospective class action lawsuits against, *inter alia*, Air Canada and Lufthansa ("the airlines") in relation to flights out of Vancouver International Airport. Each suit was based on an alleged violation of B.C.'s *Business Practices and Consumer*

*Protection Act* ("the *BPCPA*"), which states that a business must not commit or engage in a deceptive act or practice in respect of a consumer transaction. (\*1)

At issue was the classification of fuel surcharges as they appeared on the airline's electronic tickets. On these, the total cost paid was broken down into categories, such as base price and taxes. Mr. Unlu alleged that by including the cost of the fuel surcharge in the "Tax" category, the airlines were representing to customers that the fuel surcharge was an amount collected on behalf of a third party government. This representation was alleged to be deceptive, as the fuel surcharge was in fact retained by the airlines.

In addition to denying that this practice violated the *BPCPA*, the airlines asserted that as provincial legislation, the law was constitutionally inapplicable to airline ticketing practices. As such, each brought an application for a summary trial on the constitutional question.

### *The Constitutional Framework*

Federal Parliament has jurisdiction over aviation as part of its power to make laws respecting matters of national concern, for the peace, order and good government of Canada. This jurisdiction is independent of any international or interprovincial aspect – the BC Court of Appeal has ruled that it covers aircraft operating solely within a single province. (\*2) Even in circumstances of federal jurisdiction, however, provincial laws of general application apply unless violate the constitutional principles governing the division of powers between the

two levels of government. (\*3) The airlines argued that the *BPCPA* was inapplicable based on two such principles: paramountcy and interjurisdictional immunity.

Two types of conflicts between federal and provincial law trigger paramountcy. The first is simple: if the federal law says, “you must”, but the province says, “you cannot”, complying with one means violating the other. With the second type, complying with both laws is possible, but doing so would frustrate the underlying purpose of the federal law. There is a high threshold required to demonstrate that federal purpose has been frustrated. In either case, the provincial law is inoperative to the extent of the incompatibility. (\*4)

Interjurisdictional immunity is engaged when an otherwise valid provincial law: 1) intrudes on a protected “core” of federal jurisdiction, and 2) the effect of the intrusion is sufficiently serious. The core in question is defined as a vital part of the federal power – the basic, minimum and unassailable content. (\*5)

#### *The Decision of the Lower Court*

Justice Adair of the British Columbia Supreme Court dismissed the airlines’ applications. According to the judge, there was no conflict between the provincial consumer protection legislation and the relevant federal aviation legislation, the *Canada Transportation Act* and the *Air Transport Regulations*. In order for actual, operational conflict to exist with provincial legislation that prohibited deceptive practices, some section of federal law would have to require deceptive practices, or at the

minimum accept these practices as legitimate. There is no such section. It is true that the Canadian Transportation Agency (“CTA”) accepts the airlines’ tariffs, which in turn permits them to charge the international fuel surcharge and list it separately from the base fare. However, the lawsuit did not claim that the airlines’ did not have the right to impose a fuel surcharge. Rather, the claim was solely against the manner in which that surcharge was presented. Similarly, Justice Adair found that the onus on the airlines to demonstrate frustration of federal purpose was not met, as the claim did not intrude on areas where the CTA had authority.

Justice Adair also rejected the airlines’ argument that interjurisdictional immunity applied. The Supreme Court of Canada had previously concluded that the use of this constitutional doctrine to limit provincial law should be reserved for situations covered by precedent, and none were applicable to the present case. Moreover, on the second part of the test, the impact of the *BPCPA* on the federal sphere would be minimal. Compliance with the provincial act would not interfere with the CTA’s decision-making powers with regards to tariffs, fuel surcharges, and terms and conditions of carriage. If the case were successful on the merits, airlines simply would not be allowed to call a fuel surcharge a tax.

#### *The Decision at the Court of Appeal*

Both airlines appealed the decision to the British Columbia Court of Appeal. The appeals were dismissed, and the initial judgment was almost entirely affirmed.

The Court of Appeal agreed that there was no operational conflict between the relevant federal and provincial legislation. The Court was able to consider the impact of amendments to advertising regulations that were implemented after the lower court's decision was released. These regulations explicitly forbid the use of the term "tax" to describe an air transportation charge in any advertising. While the *Unlu* case dealt with tickets, not advertising, the Court found that in principle this was consistent with the plaintiff's assertion that non-third-party charges should not be shown in a way that suggests they are for the benefit of a third party. With regards to the frustration of federal purpose, the Court noted that the CTA itself stated that it is the airlines responsibility to ensure that they comply with all applicable legislation respecting advertising, including provincial legislation. This indicates that the CTA did not consider itself the sole authority regulating all aspects of aviation, and that federal purpose was not frustrated by provincial consumer protection legislation. (\*6)

The Court of Appeal found that Adair J. applied the correct principles and reached the correct conclusions with regard to interjurisdictional immunity. With regards to the airlines' argument that the application of the *BPCPA* would subject international aviation companies to the decisions of provincial regulators without expertise or knowledge of the airline industry, the Court found that these arguments addressed provisions of the provincial law that were not relevant to the specific provision at issue, being the prohibition on deceptive practices.

*The Effect of the Decision Going Forward*

The Court of Appeal decision in *Unlu* offers preview of how courts across the country might rule when provincial law meets federal undertakings. Indeed, several provinces have similar consumer protection legislation that prohibits misleading or deceptive practices by businesses operating in the province. (\*7) While a British Columbia Court of Appeal decision is not binding on the courts of the other provinces, other courts may find the reasoning persuasive and use it as a model. Likewise, while this case is concerned with the behaviour of international airlines, similar judicial reasoning might validate the applicability of provincial consumer protection legislation to other forms of transportation under federal jurisdiction.

Several factors will affect the breadth of the impact of the *Unlu* decision. First, the Court of Appeal narrowly focused on the exact circumstances of the case. The Court does not state that the provincial legislation is applicable to aviation; rather, that the three sections relied upon by Mr. Unlu are applicable to aviation (those being the definition of a deceptive practice, the prohibition of deceptive practices, and the grant of civil remedies for violations). This narrow focus was helpful to Mr. Unlu, as the onus was on the airlines to demonstrate an incompatibility between the laws. In a sense, they had to demonstrate that federal aviation law required airlines to mislead customers to the extent that the prohibition on misleading was in conflict. As Justice Adair stated in her decision, this would be absurd. For the broader group of consumers covered by provincial legislation, however, this narrow focus means that the question of whether any other section of the *BPCPA* can be applied to

aviation has been left for another day, another lawsuit, and another appeal. The Court of Appeal decision is more effective as a guideline for future justices than for transportation businesses attempting to determine which aspects of provincial consumer protection law apply.

Likewise, the Court's reasoning on interjurisdictional immunity will not make an easy transition from aviation to other areas of federal jurisdiction. As noted in the decision of first instance, interjurisdictional immunity should be invoked only in cases with firm precedents; here, none existed. Moreover, Justice Adair specifically carved out aviation as different from most other areas of federal jurisdiction, as the source of federal power comes from "peace, order, and good government". It is not a subject matter explicitly enumerated in the *Constitution Act, 1867*, and as such is distinguishable those areas which are, such as maritime shipping and navigation.

Finally, the Supreme Court of Canada recently allowed a number of appeals concerning the applicability of provincial consumer protection legislation to banks, another industry under federal jurisdiction. These appeals will be heard in the coming year. The B.C. Court of Appeal examined this

issue on a micro scale, but the Supreme Court will consider the wider picture. While the final decision in *Unlu* was narrow, the precedents as reviewed in that decision are the same ones that the Supreme Court will examine before refining and interpreting the broader principles.

*Terrence Laukkanen*

Endnotes:

(\*1) *Business Practices and Consumer Protection Act*, SBC 2004, c 2 at s. 5.

(\*2) *Jorgenson v North Vancouver Magistrate and North Vancouver (City)*, [1959] BCJ No. 80 (BCCA)

(\*3) *Ontario v Canadian Pacific Ltd*, [1993] OJ No 1082 (ONCA)

(\*4) *Quebec (Attorney General) v Canadian Owners and Pilots Association*, 2010 SCC 39 at para 64.

(\*5) Martin William Mason and Guy Regimbald, *Halbury's Laws of Canada – Constitutional Law (Division of Powers)*, at para HCL-102 (QL)

(\*6) *Unlu v Air Canada*, 2013 BCCA 112

(\*7) In Ontario, for example, *Consumer Protection Act, 2002*, SO 2002, c 30, Sch A at s. 14(1); in Alberta, *Fair Trading Act*, RSA 2000, ch F-2, at s. 6(4)(a)



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