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TRANSPORTATION NOTES

Legal Decisions and Developments Affecting the Transportation Industry in Canada

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Class Action for Collection of US Transportation Taxes Partially Stayed

Teri Prince, a resident of the United States, has, on several occasions, purchased tickets on the Air Canada website for travel exclusively within Canada. On each occasion she was charged a "U.S.A. Transportation Charge" and a "U.S. Flight Segment Tax" because she resides in the U.S.

Matthew Wallach, another Air Canada customer, booked a ticket from Los Angeles to Calgary while he was in Canada. He was charged a "USA Transportation Charge" and a "U.S. Passenger Facility Service Charge" (although the latter charge should have been identified as an "International Travel Facilities Tax").

It is important to understand that:

- the U.S.A. Transportation Tax and the U.S. Flight Segment Tax are imposed under ss. 4261(a) and (b) of the *United States Internal Revenue Code* (the "*Code*") on "taxable transportation";
- "taxable transportation" is defined as transportation that begins and ends in the U.S. or the 225-mile zone. The term "225-mile zone" means that portion of Canada and Mexico that is not more than 225 miles from the nearest point in the continental United States; and
- s. 4261(e)(2) of the *Code* provides that where amounts are "paid outside the United States for taxable transportation, the taxes imposed by subsections (a) and (b) shall apply only if such transportation begins and ends in the United States."

The plaintiffs commenced a prospective class action, alleging that:

With respect to tickets purchased in Canada, (a) Air Canada collected taxes under the *Code* when flights did not begin and end in the United States (the "Improper Collection Argument"); and (b) Air Canada collected U.S. taxes on tickets purchased in Canada, thereby giving unlawful extra-territorial effect to the U.S. tax laws in Canada (the "Extra-Territorial Argument").

With respect to tickets purchased in the United States, only the Extra-Territorial Argument was advanced.

The plaintiffs further alleged that Air Canada negligently misrepresented that the U.S. taxes had to be paid as a condition of carriage.

In response, Air Canada brought a motion before the Ontario Superior Court of Justice seeking a declaration that that court does not have the jurisdiction to adjudicate the dispute and, in the alternative, that it should exercise its discretion to decline jurisdiction.

In making this argument, Air Canada conceded that it carries on business in Ontario and that there is a real and substantial connection to Ontario such that the Court could assume jurisdiction (per *Club Resorts Ltd. v. Van Breda*, 2012 SCC 17).

However, Air Canada argued that the Court is precluded from hearing the case as a result of the "revenue rule" which arose in *United States of America v. Harden* [1963] S.C.R. 366. In that case, the Supreme Court of Canada held that Canadian courts should not enforce foreign revenue laws or judgments either directly or indirectly.

The Court did not accept Air Canada's argument. Rather, it held that *Harden* was an "enforcement rule" and that it stood only for the proposition that foreign states may not sue in Canada for taxes due under the law of a foreign state.

As a result, the Court held that the revenue rule does not apply because the Court is not being asked to enforce a claim by the U.S. government for the recovery of taxes. Rather, the issue is whether Air Canada is entitled to and has properly collected amounts from its customers on ticket purchasers.

The issue then turned to whether the action should be stayed in any event on the basis of *forum non conveniens*. Air Canada argued that the case should be dealt with by the U.S. courts because they are the experts in their own tax legislation. The Court noted that this was no different from other cases where a Canadian court is called upon to consider a foreign law to determine a Canadian dispute.

In any event, the Court conducted a *Van Breda* analysis to determine this portion of the motion.

In the case of tickets that were purchased in Canada, the Court found that the action could proceed before the Ontario Courts because:

- it is not more appropriate for a foreign court to determine whether Air Canada's charges to its customers in Canada are lawful in Canada;
- the Court found that a U.S. Court would not be better suited to determine

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> ers to maximize the use of aircraft, and also allow passengers to utilize a booking regime with the flexibility to alter or cancel reservations without notice and possibly without charge depending on the type of airfare purchased.

The Agency then went on the consider the issue of whether Air Canada's Tariff Rule 45 (E)(1)(b)(iv) is reasonable. According to Mr. Lukács, this tariff provision acts as a blanket exclusion from liability that exonerates Air Canada from compensating passengers who are denied boarding because of Air Canada's "poor planning and/or inadequate maintenance of its equipment" when aircraft with smaller capacity are substituted, on missions requiring larger equipment, due to technical failures on the aircraft originally assigned to the flight.

While Mr. Lukács acknowledged that Air Canada should not imperil the safety of its passengers, he argued that the phrase "operational safety reasons" (which appear in the impugned tariff provision) could be "arbitrarily stretched" to benefit only Air Canada's interests.

Air Canada argued that the USDOT does not require air carriers to provide denied boarding compensation in "downguage" situations — and that it is of utmost importance that Air Canada be able to decide, for operational and safety reasons, when aircraft should be substituted. Such decisions should not have negative commercial repercussions on the air carrier, nor should they require compensation to passengers.

Air Canada then provided examples of "downguage" situations that may not be readily apparent, including:

- weather conditions that could make certain aircraft unsuitable for a flight due to the absence of Instrument Landing Systems at certain airports;
- where there were no suitable aircraft with GPS capabilities;
- unplanned mechanical issues with the aircraft assigned to the flight in question (e.g. as a result of bird strike); and
- locating aircraft that can operate within the noise curfews at destination airports.

In the case of commercially-driven downguages, Air Canada submitted that these only occur in exceptional circumstances, such as the reduced demand that resulted during the 2003 SARS outbreak. Even then, Air Canada argued that downguaged equipment would not be assigned if it resulted in a passenger being denied boarding.

Mr. Lukács argued that the term "operational and safety reasons" should not be allowed in the tariff as it amounts to a "catch-all excuse" for not paying denied boarding compensation on downguaged flights. He noted that his concern was shared in the EU. To demonstrate this, he pointed to the restrictive manner in which the European Court of Justice interpreted the term "extraordinary circumstances" (in the operational context) in *Wallentin-Hermann v. Alitalia*, Case C-549/07. Mr. Lukács argued that the Court in that case struck the right balance between the carrier and the passenger by holding that while technical or mechanical problems on their own are not extraordinary circumstances that relieve the carrier from paying denied boarding compensation, if such causes occur from causes entirely outside a carrier's control (e.g. a bird strike), no compensation is due.

In deciding the complaint, the Agency preferred the approach taken from *Wallentin-Hermann*, described above. More specifically, where a denied boarding situation occurs as a result of a downguage, the responsibility rests with the carrier to establish that the events in question were beyond its control and that it took all reasonable measures to avoid the downguage.

As a result, the Agency found this portion of Air Canada's tariff to be unreasonable.

Next, the Agency went on to consider whether Air Canada's Tariff Rule 245(E)(2) was unreasonable. This provision permits Air Canada to limit denied compensation to the amount of CAD$100 or provide a voucher in the amount of CAD$200 for flights within Canada or to the U.S. or Mexico. Mr. Lukács argued that this amount has not been updated over time and is now insufficient to compensate passengers for being denied boarding.

In making his argument, Mr. Lukács noted that the regimes in the US and the EU are significantly more generous to the passenger. In the US, compensation is based on the fare paid as well as the length of delay — with a maximum amount payable of US$1,300. In the EU, the compensation is based on the length of the delay and, inexplicably, the distance of the flight in question, to a maximum of €600.

Air Canada argued that the Agency had already decided in *Anderson, supra*, that Tariff Rule 245(E)(2) was reasonable. Moreover, it argued that from 2004 to 2012, its average fare was ~CAD$180 — and, as a result, the compensation offered was in line with average fares. (Incidentally, Mr. Lukács challenged this on the basis that Air Canada counted flight segments, rather than one-way trips. He argued that this artificially increased the number of data entries and this deflated the value of the average fares).

Air Canada also pointed out that where a passenger is denied boarding in these circumstances, not only does it provide an alternative flight, it also provides accommodations, meal vouchers and other incidentals, as the situation requires. Therefore, argued Air Canada, the amount paid was above and beyond the actual out-of-pocket expenses incurred by the passenger.

Finally, Air Canada argued that because of the extensive nature of its domestic route network, passengers are frequently re-protected within narrow timeframes.

Mr. Lukács proposed the following regime for compensating delayed passengers, founded upon on a base amount intended to reflect the inconvenience suffered as a result of a denied boarding, as calculated by Mr. Lukács:

Length of Delay	***Compensation***
Less than 2 hours	50% base amount =CAD$200
2 hours, but less than 6 hours	100% base amount =CAD$400
6 hours of more	200% base amount =CAD$800

The Agency considered the various arguments and, in the end, held that, although it had found Tariff Rule 254(E)(2) reasonable in *Anderson, supra*, the level of denied boarding compensation that was approved in that decision was now 12 years old and therefore due for review.

The Agency also found that, notwithstanding the fact that Air Canada pays delayed passengers' accommodations, meals and other incidentals — in addition to the compensation set out in Tariff Rule 245(E)(2), it was not persuaded that these payments "entirely or sufficiently mitigate the damages experienced by [a delayed] passenger."

The Agency found Tariff Rule 245(E)(2) unreasonable, but noted that the U.S. denied compensation regime, as well as that which was proposed by Mr. Lukács were reasonable. It also held that the E.U. mechanism was unreasonable because the distance to be travelled is not necessarily relevant to the inconvenience suffered by a delayed passenger.

Lukács v. Air Canada,
CTA Decision No. 204-C-A-2013

Transportation Tax (cont'd)

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whether the amounts collected were "paid outside the United States" or whether "transportation begins and ends in the United States";

- Air Canada is located in Canada and carries on business in Ontario;
- one of the plaintiffs is a Canadian resident;
- witnesses are located in both Canada and the United States;
- the tickets were purchased in Ontario; and
- Air Canada's expert testified that if the case were transferred to the United States, each of the plaintiffs and each of the class members would have to apply for an administrative refund from the Internal Revenue Service — which would subject them to an additional procedural step before they could commence their Improper Collection portion of the claim.

As a result, the Court found that the claims for the tickets purchased in Canada could proceed in the Ontario courts.

As to the claims for tickets purchased in the United States, the Court came to a different conclusion. Recall that these claims advance only the Extra-Territorial Argument.

The plaintiffs argued, with no supporting jurisprudential authority, that the matter was suitable for the Canadian courts because the ticket related to travel within Canada. Moreover, the issue of whether Air Canada has authority to collect this tax was a matter of Canadian law.

The Court rejected the plaintiffs' framing of issues in this manner and held that:

> … a Canadian court should not be adjudicating any matters relating to the imposition and collection of taxes on transactions occurring within the United States. To do so would constitute an interference with U.S. tax sovereignty.

The Court also rejected the argument that the Extra-Territorial Argument should also be heard in Canada to avoid a multiplicity of proceedings. The Court found that the Improper Collection and Extra-Territorial Arguments were fundamentally different—and therefore there was no unfairness in severing them. The claims relating to tickets purchased in the United States was stayed.

Prince and Walach v. ACE Aviation and Air Canada
2013 ONSC 2906 (CanLII)

Disclosure Sufficient in Rail Blockade Case

The "Idle No More" protest movement, which began in November 2012 and originated among Aboriginal peoples in Canada comprised many different kinds of political actions across the country. Marches through cities and towns, social media campaigns and liquid diet hunger strikes were all associated with the movement through the winter of 2013. In addition, in December 2012 certain protesters blockaded the Canadian National Railway Company's (CN) St. Clair Industrial Spur Line near Sarnia, Ontario at its crossing on the reserve of the Aamjiwnaang First Nation (also known as Chippewas of Sarnia First Nation).

On December 21, 2012, Justice David Brown of the Superior Court of Justice granted CN an interim injunction, which ordered the removal of all obstructions and restrained any further blockade. Despite this, the blockade continued and, less than one week later, CN was before Justice Brown again, seeking a continuation of the injunction order until it was varied or discharged by further order of the court. The injunction was renewed.

On January 2, 2013, CN brought a motion seeking an order of civil contempt against one of the protesters, Ron Plain, for his alleged continued blockade of the CN Spur Line in contravention of the injunction. The court ordered Plain not to go within 100 feet of the rail line and authorized his arrest where there were reasonable and probable grounds to believe that he had contravened court orders.

On May 24, 2013, Plain's counsel brought a motion seeking extensive disclosure. On June 10, 2013, Justice Thomas released his reasons on Plain's motion for disclosure.

Taking up nearly four full pages of his reasons, Justice Thomas set out the disclosure requested by counsel to Plain. The list comprised 33 requests, including "all documents that form the basis for CN's right to use the lands for the Spur Line," several more particularized requests for documentation relevant to the blockade and to the motion brought before Justice Brown, as well as a series of questions related to "what might loosely be viewed as the appropriateness of Brown J. hearing the injunction application," like, "over what period of time did now-Justice D.M. Brown act as counsel for CN?"

In addition, Justice Thomas noted that Mr. Rosenthal submitted that the disclosure requested was relevant to many aspects of his client's defence, including the "anticipated novel argument that the principles of fundamental justice preclude convicting [Plain] of contempt if the injunction order was invalid."

Justice Thomas first dealt with Mr. Rosenthal's submission that a narrow exception to the law prohibiting collateral attacks on court orders law should be created for Aboriginal persons. This would allow Mr. Plain to attack the validity of the injunction order directly and without an appeal of the order itself. Mr. Rosenthal sought to argue that the injunction order was invalid based on an argument that CN's use of the land in question was not authorized, which would involve examination of treaty and other related rights. Counsel argued that this exception would validate Plain's s. 7 *Charter* guarantees, which protect an individual's right to life, liberty and security of the person and the right not to be deprived of these except in accordance with the principles of fundamental justice.

Justice Thomas held that public order demands that a court order only be negated by due process of law and not by disobedience and cited an Ontario Court of Appeal decision in which a *Charter*-fuelled collateral attack on a court order was considered and rejected. He found that there was no evidence that the principles of fundamental justice had been impacted and that there was no merit to the s. 7 argument.

Based on previous case law, Justice Thomas adopted a contextual approach to determine the nature and extent of disclosure required in the contempt motion. The factors to be considered included: (1) the relief being sought by the party bringing the motion; (2) whether the alleged contempt is ongoing; (3) the nature of the conduct alleged; and (4) the nature and extent of the materials being sought in disclosure.

CN was seeking only a costs sanction against Plain. Though by the time of the hearing in May the Spur Line was operational again, in view of the nature and extent of the materials being sought, Justice Thomas said he was "unable to find that the ends of justice would be met" by ordering the disclosure requested. In addition, because no appeal of the injunction order had been commenced, the detailed disclosure requested was held to have little relevance to the narrow issue of the civil contempt allegation.

It was therefore decided that no further disclosure was necessary and the contempt application was ordered to proceed.

Canadian National Railway Co v Plain,
2013 ONSC 3212

End of the Line *(Overselling)*

Readers of this newsletter will be familiar with Gábor Lukács, a former university professor and prolific air passenger rights activist in Canada. In May 2013, the Canadian Transportation Agency released another decision arising from one of his complaints — this time on the issue of overbooking.

In this complaint, Mr. Lukács sought an order from the Agency:

- directing Air Canada to stop overselling its domestic flights;
- disallowing a provision in Air Canada's tariffs that relieves it from compensating a passenger if, for "operational and safety" concerns, the aircraft on which the passenger had a confirmed reservation is substituted with an aircraft of lesser capacity, thereby preventing Air Canada from accommodating the passenger on the new aircraft due to lack of capacity; and
- disallowing a provision in Air Canada's tariffs that in certain situations provides that passengers compensation for denied boarding be limited to payment of CAD$100 or be given a travel voucher in the amount of CAD$200 for travel within Canada, the United States and Mexico.

The Agency began its analysis by noting that s. 67 of the *Canada Transportation Act*, S.C. 1996, C.10 requires that air carriers' domestic tariffs not be "unreasonable". The test for "reasonableness" had been decided in *Anderson v. Air Canada* (CTA Decision No. 666-C-A-2001). In the matter at hand, the Agency decided the test:

> … requires that a balance be struck between the rights of passengers to be subject to reasonable terms and conditions of carriage and the particular air carrier's statutory, commercial and operational obligations.

The Agency also noted, as a preliminary matter, that there is no presumption that a tariff is reasonable.

The Agency then considered the issue of overbooking. Mr. Lukács argued that while this may have been an industry practice in the 20th century, it is no longer so today. He pointed to WestJet (Air Canada's main domestic competitor) — an airline which, as a matter of practice does not overbook its flights, yet remains profitable. In fact, Mr. Lukács argued that Air Canada is the only Canadian domestic carrier that engages in the practice — and as a result he argued that it would not be subject to a competitive disadvantage should it be prohibiting from overbooking its flights.

Air Canada responded by arguing that overbooking is common in the industry and permits carriers to offer flexible fares where passengers can change itineraries at the last minute, resulting in 'no-shows' for a flight. Air Canada argued that if the process is managed in a reasonable manner through its sophisticated systems that analyze no-shows and booking patterns, the disruption to passengers could be minimized. Air Canada also argued that the Agency had already recognized the reasonableness of overbooking in *Simcock v. Air Canada* (CTA Decision No. 181-C-A-2005).

As further support for its position, Air Canada cited the Agency's *Fly Smart* publication where overbooking is recognized as being reasonable, as well as jurisprudence from the US Supreme Court in *Nader v. Allegheny Airlines Inc.*, US 290 [1976] where overbooking was described as "common industry practice". Finally, Air Canada noted that the USDOT has acknowledged "the legitimacy of a well-controlled over-sale system" even though the overbooking levels for American carriers are double those of Air Canada.

As to the argument that WestJet does not engage in overselling, Air Canada distinguished its business model by arguing that, unlike WestJet, Air Canada does offer some fares that are fully refundable — so the two airlines could not be fairly compared on their differences in their over-sale policies.

Air Canada argued that some of its customers place a high value on refundable tickets and, given the nature of these tickets, it is much more exposed to no-shows on refundable fares. Moreover, as an international carrier involved in a global alliance, Air Canada has much more connecting traffic and is therefore exposed to misconnections, which result in additional no-shows.

In short, the practice of overbooking allows Air Canada to absorb some of the these risks and, as a result, is a net benefit to its passengers.

The Agency accepted Air Canada's arguments. It held that:

> …[overbooking] is commonplace among air carriers. The Agency is of the opinion that, in general, the practices serves the interests of both the carriers and the travelling public because carriers are able to operate at maximum capacity, which should result in reduced fares. The systems employed by carriers to forecast the number of reservations for particular flights, and the potential number of "no-shows" for those flights, allow carri-

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