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Broker Liability: A CANADIAN PERSPECTIVE, EH?

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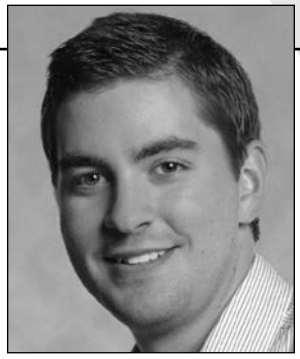

A. Introduction: In an Unregulated Industry, Self-regulation is the Key to Success

In Canada, the term "freight broker" or "load broker" refers to a party who arranges for the transportation of cargo from a shipper to a consignee and charges a commission on the shipping costs.[3] Brokers have special knowledge of routes, connections and destinations, and the availability and suitability of carriers.[4]

The regulations imposed upon freight brokers in Canada are limited: in Quebec, brokers must register with the *Commission des transports du Québec*, and in Ontario, any party who brokers freight, or arranges for a carrier to transport goods must maintain a trust account to hold monies payable to the carrier in trust for that carrier (those monies are deemed to be trust funds).[5] While brokers were previously required to register in Ontario, that requirement was eliminated several years ago.[6]

Therefore, aside from legislated trust obligations, freight brokers are essentially unregulated in Canada. Since there is no regulation in terms of limitation of liability or standard of care, freight brokers are subject generally to the laws of agency and negligence, and the contractual terms of any agreement entered into in respect of the brokerage services. In this regard, brokers can negotiate the terms of the contract to protect their interests. In order to thrive, a broker must self-regulate and follow regimented operations procedures or risk significant liability.

In this paper we will consider two areas of concern for brokers operating in Canada and their advisers:

1. The potential liability for officers and directors of a corporate broker arising from the failure to pay performing carriers; and
2. The potential liability for load brokers arising in our unregulated industry.

We conclude with general recommendations for brokers and their officers and directors that will help them avoid, or at least limit, liability in Canada.

B. The Laws Governing Broker's Liability

A broker in Canada, or a lawyer advising a broker in Canada, should take into account the following two legal regimes when determining the operations to be implemented into one's standard procedures and service conditions:

1. Section 190 of the *Highway Traffic Act*;[7] and
2. The common law principles governing the relationship of principal and agent, Negligence, and general Contract law.

1. Section 190 of the *Highway Traffic Act*

Several years ago, a new regime was enacted to regulate the obligation to hold monies in trust for a carrier. Subsection 191.0.1(3) of the *Highway Traffic Act*[8] states:

> **Contracts of Carriage**
>
> **Money for contract of carriage held in trust**
>
> 191.0.1 (3) A person who arranges with an operator to carry the goods of another person, for compensation and by commercial motor vehicle, shall hold any money received from the consignor or consignee of the goods in respect of the compensation owed to the operator in a trust account in trust for the operator until the money is paid to the operator.
>
> **Other rights unaffected**
>
> (4) Nothing in subsection (3) derogates from the contractual or other legal rights of the consignor, the consignee, the operator or the person who arranged for the carriage of the goods with respect to the money that is held in trust under that subsection.

This succinct statement of the broker's obligation to hold trust funds is clear: a carrier *will* be paid.

Our Courts have recently considered two cases regarding the personal liability of officers and directors for trust monies that were not paid to a carrier by the corporate broker. In those cases, the findings were mixed,

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but the Court's considerations provide useful guidance to avoid findings of personal and corporate liability.

In *Travelers Transportation v 1415557 Ontario Inc. c.o.b. as Platinum Express Worldwide*,[9] the plaintiff, Travelers, was a motor truck carrier. Travelers sued the defendant broker, Platinum Express Worldwide, and the directors and officers of Platinum, personally, for breach of trust arising from the failure of Platinum to pay Travelers for carriage services provided. In this case, there was a load brokerage agreement: Travelers provided motor truck carrier services to various shippers and consignees for the benefit of Platinum. Although Travelers performed its services as carrier, Platinum failed to pay invoices totalling more than $55,000.

Platinum claimed it was insolvent, however, it did not claim bankruptcy, nor did it take advantage of the considerable protection afforded by Canada's creditor-protection laws. Travelers obtained default judgment against the Platinum, and pursued claims against Platinum's officers and directors, ultimately settling with all but one, Mr. Persaud.

The Court considered Mr. Persaud's personal liability for the unpaid monies. While this case was decided under previous laws regarding brokers' trust obligations, the similarity in the statutory language preserves the relevance of this decision. The Court agreed that Platinum's obligation was to hold in trust any monies it received from the party holding the freight bill. Platinum was then obliged to pay the trust monies to the motor carrier as soon as the motor carrier had completed its services.

However, the Court rejected Traveler's argument, based upon the common law principle of breach of trust, that Mr. Persaud was personally liable. The Court rejected the argument that Mr. Persaud had actual knowledge of the alleged breach of trust or that he was reckless or wilfully blind to it.[10] Further, the Court rejected the argument that the alleged breach was part of the trustee's fraudulent and dishonest design.

We emphasize the "alleged breach" since there was no evidence that Platinum *was ever paid* and, therefore, the Court could not find that it breached its trust obligation. The Court did acknowledge, however, that had Platinum been paid, it would have been obligated under s. 191.0.1(3) of the *Highway Traffic Act* to keep a separate account for any funds received in payment and to hold those funds in trust.

A more recent case, *Tripar Transportation LP v U.S. Consolidators Inc., Linda Earle-Barron and Jonathan Turner*,[11] had a different result: the officers and directors of a corporate broker were held personally liable. The broker in this case, U.S. Consolidators, was no longer operating. Like Platinum, it had not declared bankruptcy nor sought protection from its creditors. Unlike Platinum, however, U.S. Consolidators had received monies from shippers and had deposited those monies into its own general account. Instead of paying the carrier for work performed and invoiced, U.S. Consolidators used the funds to pay other creditors including its landlord, the Hydro company and its directors.

The Court found U.S. Consolidators liable for breach of trust because the monies had not been deposited into a separate account and had been used to pay other creditors. In addition, the Court also found that while there was no evidence of fraud, two of the three directors of U.S. Consolidators were personally liable for the following reasons:

- The directors are deemed to have knowledge of the trust since it is imposed by statute and directors are deemed to have knowledge of the law;
- The corporation was a 'closely held' corporation;
- The directors were personally involved in day-to-day operations;
- The directors were personally aware of the broker's bank accounts and, specifically, the fact that no separate trust account was maintained;
- One director received payment of the trust funds to satisfy a contractual obligation to himself; and
- The second director was paid his salary from the general account, and knew that the funds received from the shippers were intended to be paid to the carriers, and that the carrier had not been paid.

In light of this evidence, and the statutory requirement that the carrier must be paid, U.S. Consolidators and its directors were found liable for breach of trust.

Three Lessons to Avoid Breach of Trust

There are three lessons to be learned from the above analysis:

1. If a broker faces financial instability and cannot pay its creditors, it must seek protection formally under the *Companies' Creditors Arrangement Act* (*the "CCAA")*,[12] a Federal Act that allows financially troubled corporations the opportunity to restructure their affairs and obtain a stay of actions against it by its creditors.
2. Every broker should create and maintain a trust account to ensure that funds received on behalf of a carrier are deposited in a separate account designated for trust monies. The broker must ensure that those trust funds are always treated as being separate from operating funds and are never co-mingled with the broker's funds for any reason.
3. Every director and officer should personally ensure (by implementing a system of accountability) that the corporate broker has implemented a separate trust account and that trust funds

are not paid to anyone other than the carrier as beneficiary. Where a director or officer is dissatisfied regarding the treatment of trust funds, the director or officer should resign.

2. The Potential Liability for Load Brokers in an Unregulated Industry

The second regime which a broker and its lawyer must be familiar with is the common law governing the principal-agent relationship, negligence, and breaches of contract. While many brokers do utilize contracts and agreements, a broker must be also be conscious of the laws governing undocumented transactions and/or communications (perhaps due to casual communications between a broker's representative and a shipper), and by which a broker can incur significant liability. Liability can arise due to negligence, negligent misrepresentation and breach of contract for example.

Allegations of negligence will often arise in claims against brokers, whether the claim itself is rooted in agency or breach of contract. Consider allegations that a broker gave incorrect instructions to the carrier, resulting in a shipment being delayed and the goods perishing. While the basis of the claim may be breach of contract, the allegations will surely include negligence on the part of the broker. In situations of cargo theft, the broker will often be accused of negligently selecting a carrier.

The nature of the broker's role as middle man between carrier and shipper, operating in a time-sensitive, low-profit environment, increases the likelihood that employees may fail to record instructions. It also promotes the use of documents not intended for the broker's specific purpose (such as a bill of lading where the broker's trademark is placed alongside the carrier's).

The liability of a freight broker has been likened to that of a travel agent:

> "If a person agrees to perform some work or service, he cannot escape contractual liability by delegating the performance to another. It is his contract. But if the contract is only to provide or arrange for the performance of services then he has fulfilled his contract if he has exercised due care in the selection of a competent contractor. He is not responsible if that contractor is negligent in the performance of the actual work or service, for the performance is not part of his contract..."[13]

Our Courts will accept the defence that if "the carrier defaults through no fault of the agent, surely the agent is not responsible."[14] As an agent, the true broker's function is simply to find a suitable carrier, enter into a contract for carriage as an agent of the shipper, and deliver the shipping instructions to the carrier. Thus, a broker can be exposed to liability for at least the selection of the carrier and the delivery of instructions to the carrier.[15] Recent case law in the United States makes it clear that brokers are also expected to ensure that the carrier is licensed to transport the cargo, and advise the carrier of the value of the shipment so that sufficient insurance can be purchased prior to transporting the load.[16] These expectations would apply to Canadian brokers.

The Broker Acting as Carrier: Any Limitation of Liability?

Additional obligations and liability may arise depending on how the broker has represented itself. For example, if the broker is found to have held itself out as a carrier it may be found liable as such, even if it only performed the duties of a broker.[17] In these circumstances, the liability can be significant, and the defences available to the broker are limited. Consider that where there is no declared value, a carrier can rely upon section 1 of the "Uniform Conditions of Carriage – General Freight,"[18] which provides: *"the carrier of the goods described in this contract is liable for any loss or damage to goods accepted by the carrier or the carrier's agent except as provided in this Schedule."* However, the issue of whether a broker who is alleged to be liable as a carrier can rely upon the Uniform Bill of Lading's limitation of liability, where it did not issue a bill of lading, or accept the goods, has not been judicially determined in Canada.

Likely, a broker would argue that the carrier was the agent of the broker to try to fall within limitations afforded by the Uniform Bill of Lading. However, while the carrier can take advantage of the defence of limitation of liability, would a Court agree that this limitation can benefit the broker? The plaintiff in that case would likely pursue the broker for the difference between the amount to be paid by the carrier, which is protected by a limitation of liability, and the actual loss. This places the broker in a precarious position as it would likely have insufficient insurance for the actual loss, since it would have expected the loss to be insured by either the shipper or the carrier or both (but not, of course, by the broker).

Further, if the relationship between the parties creates duties which extend beyond the traditional obligations of a broker, the broker will be liable for exercising those duties with reasonable skill and care.[19] For example, if the broker promises delivery by a certain date, he has undertaken more than just the supply of services, and may be responsible for late delivery on the grounds of breach of contract.[20]

Cargo Theft and Brokers

The continuing increase in cargo theft in Canada presents another area of potential liability.[21] Trucking represents a $65 billion industry in Canada and is the main target of cargo thieves and organized crime groups. Trucks transport about 90% of all consumer products and foodstuffs within Canada and almost two thirds (by value) of Canada's total trade with the U.S.[22]

The *Canadian Trucking Alliance's* "Report on Cargo Crime in Canada (2011)" advises that cargo theft

represents a $5 billion problem in Canada. In 2008 alone, $22 million worth of cargo was stolen in the Peel region of the Greater Toronto Area (the "GTA").[23] The GTA is known to have the "highest rates of cargo theft in Canada, rivaling the major supply chain crime areas of the United States, including Los Angeles, Dallas/Fort Worth and Miami,"[24] with around $500,000.00 of cargo disappearing every day.[25] This amounts to over $1 billion in losses and claims to Canadian carriers, annually.[26]

What responsibility might the freight broker bear: can it be held accountable for connecting the shipper with an unscrupulous carrier? Will the broker be liable for an unforeseen hi-jacking? Questions like these highlight the difficulties of operating in an unregulated sector.

In *Perfect Poultry v. Keltic Transportation*[27] our Court considered many issues relevant to brokers dealing with cargo theft. However, given the nature of the hearing (a pre-trial motion), the Court provided insight into the issues without conclusions. In this case, the defendant carrier "brokered-out" two loads to another carrier without the shipper's knowledge or consent. The shipper loaded the cargo onto trucks purportedly driven by the defendant's employees. It was alleged that the shipper did not adequately identify the drivers, who, along with the cargo, were never seen again. The factual record is unclear as to whether the drivers were unscrupulous employees of the third party carrier, or if they were complete strangers to the transaction who somehow learned of the shipment and masqueraded as employees of the defendant.

The past dealings between the parties were informal and the defendant argued that the history of informal communications led them to believe they were allowed to broker-out the loads. In previous dealings, the shipper might request services with just a one-line e-mail. The defendant argued that they had never taken possession of the loads and, therefore, they were simply a broker with no liability for the actions of the carrier.

This case questions the extent of a broker's obligation to "screen" a carrier, and the shipper's obligation to identify the drivers that attend to pick up the load. Both parties had arguably failed to discharge certain duties. Who was liable for the failure would determine who would bear the responsibility for the loss.

This case was scheduled to go to trial in the summer of 2012, but no decision has been reported as of May 2013. Had this case gone to trial, it is likely that the party with better records would have prevailed. If the defendant could show that it discharged its duty to exercise reasonable skill and care in selecting a carrier, the loss would likely fall on the shipper.

Due Diligence: Evaluating a Carrier's Performance

When selecting a carrier, a broker should consult the Ontario Ministry of Transportation's Commercial Vehicle Operators Registration (CVOR) System.[28] This system enables a broker to evaluate a carrier based on the events on its CVOR Record, including collisions, driver and carrier convictions, CVSA inspections and detentions, and the results of facility audits.

The first step in evaluating a carrier is to assess its on-road performance based on three separate safety indicators. These are the carrier's:

- Total collision points accumulated in (up to) a 24-month period (collision violation rate),
- Total conviction points accumulated in (up to) a 24-month period (conviction violation rate), and
- Total inspection points accumulated in (up to) a 24-month period, on CVSA inspections (inspection violation rate).

The points accumulated in each category are compared to the point threshold values listed in "Table of Threshold Values" to determine the Percentage of Threshold. Thresholds for collisions and convictions are based on the carrier's kilometric travel in Canada.[29] Thresholds for inspections are based on the total number of units (drivers and vehicles) inspected in Canada.[30] This is a measure of the carrier's performance in each of these categories.

The violation rate (Percentage of Threshold) in each category is combined to arrive at an overall violation rate. Collisions and convictions contribute at double the value of inspections towards the overall rate. Since they have been shown to be better predictors of future collisions than out of service defects, collisions and convictions are given more importance in determining the overall percentage of threshold.[31]

There are other factors to be considered when selecting a motor carrier, such as obtaining a corporate profile report to determine if the carrier is both in good standing for its tax filings, and a validly registered corporation, and any negative factors or detrimental ratings should be considered a warning that cannot be overlooked. The extent of investigation for a broker's due diligence can be expensive, but it is an expense that cannot be avoided. Some brokers have contracted out their due diligence with third parties, and many find that shifting the liability to the third parties willing to warrant the suitability of a carrier may be worth the investment.

Online Freight Matching

Rather than personally investigating carriers, there are companies that have developed products designed to address the needs of brokers and to assist them with meeting their standard of care. For example, TransCore Link Logistics® offers a fairly comprehensive set of services and solutions for brokers, such as confirmed insurance details and operating authorities for approved carriers. Transcore's Loadlink® is a network of information available to carriers, transportation

companies, owner-operators, load brokers, and other intermediaries in the U.S. and Canada. The participants post shipment information on the system which facilitates the matching of shippers and carriers. Similarly, LinkDispatch™ is a software program which enables carriers, brokers, shippers, and drivers to track their order, record accounts receivable and payable, communicate by electronic messaging, and generate personalized billing invoices.

C. Implementing a Sound Operating System and Record Management and Retention

As stated above, unlike carriers, brokers do not have statutory protection or statutory defences afforded by the Uniform Bill of Lading provisions.[32] The absence of regulation means that brokers must protect themselves from liability. This requires strategically crafted methods of operation that are clear and concise and which must be applied consistently to and for one's employees, contractors, agents and customers. Operations should also be designed to create a documentary record, or paper-trail, to protect the broker from liability. The record must be retained beyond the limitations of liability governing claims of negligence and breach of contract which is, generally, no less than two years from the date of the breach or negligent act.

The broker must be able to point to their records and operating system as proof that they exercised reasonable skill and care in the selection of the carrier as well as any other obligations present in the contract.

Conclusion: 10 Steps for Canadian Brokers

The following are a number of steps that brokers can take to protect themselves:

1. Generally, implement a consistent, standardized documentary management system to record preliminary details regarding the shipment, the provision of a quotation to a shipper, the procuring of the services of the motor carrier, and subsequently ensure that said details are fully recorded in the load confirmation sheet and rate agreement.
2. Create and use Service Conditions for the shipper which should include:
   a. definitions of terms which differentiate between carrier, shipper, and broker and which clearly delineate each party's respective role and obligations,
   b. a statement that the broker is the agent for the shipper,
   c. clear statements of limitations and exclusions of liability,
   d. a direction that quotations are not binding unless in writing,
   e. a process for declaring higher value to third parties, as well as the obligation of the customer to procure insurance, and
   f. formalized claim requirements with a prescribed limitation of time to make a claim, and the process for resolution of a claim.
3. A broker should also utilize a carrier confirmation and rate sheet which would include confirmation of the instructions for the carrier which are to be approved by the shipper.[33]
4. Post-delivery, a broker should review the carrier's invoice, ensure there is an appropriately recorded record of delivery, and review the invoice to the consignor or the consignee making sure all terms are consistent.
5. A broker should make its service conditions available on its website and instruct the shipper to advise in writing if there are service conditions which are unacceptable for the transaction before the delivery takes place in order to enable the broker to refuse the transaction, or amend its terms in writing for that delivery.
6. Avoid informality in your documentation and communications: ensure all contracts are in writing and use standard terms and conditions in all agreements.
7. Avoid publishing bills of ladings forms in which it appears (due to names and logos or trademarks) that the broker is the carrier.
8. Create and implement cargo theft policies in cooperation with shippers with whom the broker does business.
9. Anticipating that a broker may have to defend carrier selection, a broker should implement a written process to qualify motor carriers. Brokers should also perform due diligence before selecting a carrier including checking the CVOR and verifying the carrier's identity, safety rating, operating authority and insurance including the implementation of probationary periods with new carriers to ensure their performance and reliability.
10. Finally, trust monies must be held in a separate account, paid out only to the motor carrier that is the beneficiary, and all directors and officers should ensure that they are familiar with and approve of the accounting procedures governing the maintenance and pay out of such monies.

Endnotes

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2. Student-at-Law, Gowling Lafleur Henderson LLP, john.otoole@gowlings.com. Mr. O'Toole will be returning to Gowling Lafleur Henderson LLP as a transactional law Associate after his Call to the Bar in June, 2013.
3. John S. McNeil, *Motor Carrier Cargo Claims*, 5th ed. (Toronto: Thomson Canada Limited, 2007), ["*Motor Carrier Cargo Claims*"] at 307.
4. *Ibid*.
5. *Highway Traffic Act*, RSO 1990, c H.8 ["HTA"], s 191.0.1(3).
6. The previous Ontario Regulation 556/92 to the Truck Transportation Act was repealed effective January 1, 2006. Regulation 556/92 required an application to obtain a Load Brokerage Certificate, but the new legislation requires no such application or certificate, and universally applies to all companies who broker freight 'over-the-road' including motor carriers, warehousemen, customs brokers, freight forwarders, 3PLs and freight brokers.
7. *HTA, supra* note 5, s 190.
8. *HTA, supra* note 5, s 191.0.1.
9. *Travelers Transportation v 1415557 Ontario Inc. c.o.b. as Platinum Express Worldwide*, 2011 ONSC 44, [2011] O.J. No. 39 ["*Travelers Transportation*"].
10. The precedent in *Air Canada v M&L Travel Ltd*., [1993] SCJ 118, [1993] 3 SCR 787 provides that directors and officers of a corporation can be held personally liable for a corporation's breach of trust where the directors and officers knowingly directed or *knowingly* assisted in the corporation's breach of trust.
11. *Tripar Transportation LP v U.S. Consolidators Inc., Linda Earle-Barron and Jonathan Turner*, unreported decision, Court File No. SC-1100001987-0000 (August 23, 2012, Brampton) ["*Tripar Transportation*"].
12. *Companies' Creditors Arrangement Act*, RSC 1985, c C-36.
13. *Craven v Strand Holidays (Canada) Ltd.* (1982), 40 O.R. (2d) 186, 142 DLR (3d) 31 at 190, 191 (Ont. C.A.).
14. *J. Morgan Forwarding v Jupiter Developments* (1980), 3 A.C.W.S. (2d) 319 (Ont. H.C) (unreported).
15. *Motor Carrier Cargo Claims, supra* note 3 at 37, citing *Hillcrest General Leasing Ltd. v. Guelph Investments Ltd*., [1970] 3 O.R. 565 (Ont. Co. Ct.).
16. Gordon Hearn, *The Freight Broker in Canada: The Unregulated Field May Have Its Pitfalls* (January 2007), online: Fernandes Hearn LLP <http:www.fernandeshearn.com/newsletters>; and see also, Eric Zalud, "The Expansion of Negligent Selection Liability in the Transportation Arena: What You Don't Know About Whom You Select, May Hurt You" (Paper delivered at the Transportation Lawyers Association (TLA) 2013 Annual Conference & Canadian Transportation Lawyers Association (CTLA) Mid-Year Meeting, 30 April 2013)[unpublished].
17. *Motor Carrier Cargo Claims, supra* note 3 at 37, *citing Chubb, compagnie d'assurances du Canada c Logistique Trabspro inc*., 2006 QCCS 4001, [2006] Q.J. No. 7328 (Que. S.C.).
18. O Reg 642/05, Schedule 1, s 1. The Uniform Conditions of Carriage must be included as part of a contract for carriage as per s 4(n) of O Reg 642/05.
19. *Motor Carrier Cargo Claims, supra* note 3 at 38.
20. *See Jarvis v Swans Tours Ltd*., [1973] 1 All E.R. 71 (C.A.); *Jackson v Horizon Holidays Ltd*., [1975] 3 All E.R. 92 (C.A.); *Hadenko v Ernie Meissner Travel Agency Ltd.* (1982), 17 A.C.W.S. (26) 280 (Ont. Co. Ct.).
21. National Post, *Cargo thefts shift into high gear*, online: National Post, News <http://www.nationalpost.com > ("*National Post*").
22. Landsdowne Technologies Inc., *Study of Cargo Crime in Canada: Executive Summary* (April 2011), online: Ontario Trucking Association <http://www.ontruck.org/iMISpublic/Content/ContentFolders2/CTA/Operations/2011/StudyofCargoCrimeinCanadaExecutiveSummaryFinal.pdf>.
23. *National Post, supra* note 21.
24. FreightWatch International, FreightWatch *International Global Threat Assessment* (February 2011), online: FreightWatch International <http://www.freightwatchintl.com> at p. 9-11.
25. Jim Park, *Cargo Crime: Trucking's other dirty little secret* (27 February 2010), online: Today's Trucking <http://www.todaystrucking.com/cargo-crime>.
26. Stephanie Vescio, *An introduction to cargo theft in Canada: Reaching the breaking point and moving forward* (November 2012), online: McCague Borlack LLP <http://www.mccagueborlack.com> [the "Vescio Article"].
27. *Perfect Poultry v Keltic Transportation*, 2011 ONSC 7098, [2011] OJ No 5377.
28. More information is available at <http://www.mto.gov.on.ca>.
29. Carriers with vehicles plated in the USA are rated on kilometres travelled in Ontario only, and only for Ontario events.
30. For a copy of the threshold value tables, threshold formulas and sample calculations of kilometric rate of travel, violation rates, and percentages of threshold calculations of how you arrive at your violation rate, contact MTO Carrier Sanctions and Investigation Office

    Carrier Sanctions and Investigation Office
    Ministry of Transportation
    301 St. Paul Street, 3rd Floor
    St. Catharines, ON L2R 7R4
    Tel: 1-800-387-7736 (Ontario only) or 416-246-7166
    Fax: 905-704-2039 or 905-704-2525
31. Note: For an example of these calculations, or copy of the Table of Threshold Values please contact MTO Carrier Sanctions and Investigation Office (see address in Footnote 30).
32. *See Motor Carrier Cargo Claims, supra* note 3 at 158-185.
33. *See* the Broker-Carrier Agreement endorsed by the National Transportation Brokers Association at <http://www.ntba-brokers.com>.
34. *Vescio Article, supra* note 26.