MUNICIPAL GOVERNMENT LIABILITY AND LITIGATION

Osgoode Professional Development

June 17, 2014

CURRENT ENVIRONMENTAL LIABILITY ISSUES FOR MUNICIPALITIES

Graham Rempe, Lawyer Dianne Saxe, Lawyer

City of Toronto, Legal Services Saxe Law Office

The opinions expressed are those of the authors

Few topics evoke more concern about "vast" liability than environmental mishaps. Municipalities and their legal advisors are well advised to carefully monitor developments in this area, where liability is writ large. Memorable examples include the Mississauga train derailment of 1979, the Walkerton tainted water scandal of May 11, 2000 and of course the horrific tragedy at Lac-Mégantic, Quebec on July 6,

2013. In the wake of events like these, and many, many similar, though less dramatic examples, municipalities and other government bodies may be exposed to both civil and regulatory liability. The related costs or damages can be extensive, and expensive.

The environmental panel at this presentation will cover recent developments that merit attention, and offer comments on what they may mean for your practice.

Liability for Regulatory Orders

There are a breathtaking number of regulatory order powers within Ontario's environmental legislation. These powers are broad and apply to a wide range of people and activities. For example, s. 18 of Ontario's *Environmental Protection Act* ("EPA") applies to any person who "owns or owned or who has or had management or control of an undertaking or property". A wide range of potential orderees indeed! A s. 18 order provides for a number of measures, from monitoring and reporting, to planning and implementing remediation. The only precondition is a reasonable belief that the ordered activities will prevent or reduce contamination of the natural environment.

These orders can be and are issued to municipalities. A few recent cases show how these orders are being applied, and the consequences for orderees.

In the case *of Kawartha Lakes (City) v. Ontario (MOE),*[1] the Court of Appeal upheld an order against an innocent municipality whose property was contaminated by spilled fuel oil that migrated from the property next door. The spill was as a result of a discharge of heating fuel in a private residence. The spilled oil moved offsite, onto the neighbouring municipal property, and into Sturgeon Lake. The Ministry of the Environment ("MOE") had issued an order against the homeowner, who was taking steps through his insurer to clean up. The clean up stopped, though, when the insurance funds ran out.[2] The MOE's Provincial Officer then issued an order against Kawartha Lakes under s. 157.1 of the EPA (which has similar language to that of s. 18 above) to prevent further contamination of Sturgeon Lake.

The municipality appealed the order to the MOE Director, then the Environmental Review Tribunal, the Divisional Court, and the Court of Appeal, and lost at every step.

The undisputed fact was that Kawartha Lakes was completely innocent of any wrongdoing, unlike others that the MOE could have chosen. It was equally clear that the MOE could have forced Kawartha Lakes to clean up the spill in two ways. One type of order gave the city a clear right to compensation from the province; the one that the MOE chose did not. Kawartha Lakes argued that basic fairness should preclude such an order against the municipality, following earlier caselaw which established fairness as a consideration.

The issue was whether, in appealing the order, Kawartha Lakes could lead evidence to prove that it was not at fault, as it alleged others were (the homeowner, the fuel company, the remediation contractor, etc.). The ERT and the courts concluded that this was not relevant. The paramount concern for the Tribunal, and the courts, was whether the protection of the environment required the order, (by which they seemed to mean the cleanup) not whether it was fair to the orderee.

So the court set aside the principles of "fairness" and of "polluter pays", leaving Kawartha Lakes to seek compensation in civil court from everyone else associated with the incident.

Another regulatory liability case that is raising eyebrows among environmental lawyers is *Baker v. MOE.*[3]

In that case, Northstar Aerospace (Canada) had bought a manufacturing plant in 1985, without knowing that its soil and groundwater were contaminated with trichloroethylene ("TCE") and hexavalent chromium, both of which are known carcinogens. Northstar Canada discovered the contamination in late 2004, and started remediating voluntarily in 2005. Throughout the $20 million cleanup, the company was in great financial difficulty, and the MOE decided not to require financial assurance. In 2012, as it teetered on the edge of bankruptcy, under the control of the secured creditors, the MOE issued orders requiring both Northstar Canada and its US parent company to complete the remediation and to post cash financial assurance of $10 million. The lenders refused to put up the cash, and both companies immediately sought and received protection under the *Companies Creditors' Arrangement Act.* MOE then took over the remediation effort.

After all corporate assets had been distributed to the secured creditors, over MOE objection, the MOE issued a personal cleanup order under s. 17, 18 and 196 of the EPA against 13 former Directors and Officers of Northstar Canada and/or of its US parent company, without any evidence that any of them had anything to do with the site when the contamination took place.

Mr. Baker was a director of the US parent only, and only in the period after the Canadian site had shut down operations and was spending all its resources on cleanup under close MOE supervision. The directors and officers had no insurance against this type of order.

The order cost the individual directors and officers more than $100,000 every month, money that they could not recover even if the order were illegal and made without jurisdiction. They appealed the order to the ERT, and a motion was advanced to stay the order pending the hearing of the appeal.

Both the ERT and the Divisional Court refused to issue a stay. But, as the ERT and Court noted, s. 143(2) of the EPA prohibits stays for monitoring and remediation costs. Furthermore, the mere expenditure of money does not create a right to a stay, even if it may never be recovered. As the stay motion was interlocutory, there was no right of appeal in the EPA. The Court concluded that a judicial review was premature before the appeal had been argued on its merits before the ERT. The Court also noted that the applicant had failed to exhaust other legal remedies (a rehearing at the ERT based on new evidence) prior to applying for judicial review. The Court may also have been swayed by a paragraph in the order which implied that the contamination was due to a 1995 spill, during Northstar Canada's operations; the Crown withdrew this allegation, but not until after the stay had been refused.

Although the directors had a strong legal argument, the unrecoverable costs of the ongoing work and of the appeal were too great, especially since both sides threatened to go to the Supreme Court. The case was settled, before the ERT hearing on the merits was held, for $4.75 million. The MOE took back control of the cleanup, and immediately cut back on the work being done.

The panel will discuss the likelihood of orders like this and the precautions that can be taken to guard against liability.

Prosecution

Another route to liability is the quasi-criminal prosecution. Once again, there is a wide range of offences in Ontario's environmental legislation. Some of these are punishable by very large fines (or even imprisonment).

Of particular concern to municipalities, are ss. 187(3)-(4) and 188 of the EPA. The combined effect of these sections is to impose mandatory minimum fines for certain offences. The EPA provides that any prior conviction under a number of environmental statutes including the EPA, the *Ontario Water*

Resources Act, the *Pesticides Act*, and others, is considered, apparently regardless of how long ago, and how the activity relates to the subject matter before the court. As a result, municipalities can find themselves routinely exposed to mandatory minimum fines of $100,000 (and which may go as high as $10 million per offence).

A recent prosecution of note is *Castonguay Blasting Ltd. v. Ontario (MOE)*[4] which made its way up to the Supreme Court of Canada in 2013.

Castonguay was charged with failing to report the discharge of flyrock during blasting operations in Marmora in 2007 under s. 15 of the EPA. The flyrock damaged cars and nearby structures but had no impact on the natural environment. Castonguay had compensated the victims and reported the incident to the Ministry of Transportation (in accordance with its contract with that Ministry, for whom it was doing the blasting) and to the Ministry of Labour; however, no report was made to the MOE.

The Supreme Court of Canada concluded that this was, in fact, a reportable discharge, because it flew through the outside air. The Court rejected Castonguay's argument that harm to the natural environment must be "non-trivial". The Court resisted any notion that would require proof of environmental impairment as a precondition to reporting. In short, "… when in doubt, report."

To many, airborne rock fragments would not come immediately to mind as "contamination". There was no evidence that the MOE had given any prior warning to the blasting industry, or to the Ministry of Transportation, that the MOE wanted flyrock incidents reported to it. Nor was there any evidence that the MOE had any expertise or services to contribute to the response to flyrock incidents. Nonetheless, the MOE has aggressively pursued Castonguay. On top of the $25,000 fine imposed in the reported case, Castonguay was later fined $218,750 (including surcharge) for two similar incidents that took place in Sudbury in 2008. It was also fined $93,750 for an incident that took place in Magnetawan in 2010. Another blasting company, Austin Powder Ltd., was recently fined $130,000 for a fly rock discharge near Arnprior in 2009.

The panel will consider how this case could affect municipal and other government actors in dealing with their reporting procedures. In addition, the panel will speculate on the extent to which a baseball breaking a window is now a reportable discharge (and other fun hypotheticals).

Liability Through Arbitration – Blue Box Costs Arbitration

A battle royale is unfolding before an arbitrator as to the equitable distribution of the cost to run the blue box system in Ontario municipalities. The province requires municipalities to operate blue box systems.[5] The industries that generate blue box waste are required to contribute to the cost of the system. That contribution is governed by s. 25 of the *Waste Diversion Act, 2002*[6] ("WDA"), which provides that municipalities receive "fifty per cent of the total net costs incurred". "Total net costs incurred" is not a defined term.

The Association of Municipalities of Ontario and the City of Toronto are advancing the position in the arbitration that net cost is arrived at simply by deducting revenues from the sale of collected materials from the verified net costs that municipalities have incurred to divert Blue Box materials from landfill. Waste Diversion Ontario has verified the costs. The industry group takes the position that a "cost containment plan" approved by the Minister in 2005 caps industry liability at an amount that can be achieved using best practices, and that this amount must be calculated using a particular computer model. Nothing in the WDA or any regulation mentions best practices. Everything else is in dispute, except the fact that in several past years municipalities have agreed to accept millions less than a true 50% of verified reported costs, for those individual years. The cumulative shortfall for municipalities exceeds

$60 million.

The result could mean additional funds of tens of millions of dollars to municipalities each year. The panel will provide an update on the arbitration.

Recent developments in tort law and environmental liability

It was perhaps foreseeable that foreseeability has become a significant consideration, not only in negligence law, but in nuisance law as well. This is because many activities that took place long ago were not seen to be harmful at the time.

In *Berendsen v. Ontario,*[7] the issue was the effect of asphalt waste from highway repairs carried out fifty years ago. Waste asphalt was buried on farmland, with the agreement of the farmer. The plaintiff, a successor in title, experienced problems with cows which would not drink well water from the farm. The plaintiffs attributed this to water contamination caused by the asphalt waste.

The case made it all the way to the Supreme Court of Canada in 2001 on the question of whether the action was barred by the six month limitation in the *Public Authorities Protection Act*. The Supreme Court concluded that although the construction of the highway was a public act, the disposal of the asphalt waste was not, and the shorter limitation period did not apply. The Court sent the matter back for a trial.[8]

The trial was held in 2008, concluding with a finding of liability against the Province in the amount of $1.7 million, plus costs. The Province appealed, and the Court of Appeal set aside the decision. The Court had significant concerns about proof of causation. Nonetheless, it based its decision to allow Ontario's appeal on its analysis of the applicable standard of care. The Court noted that "foreseeability of harm is a crucial component".[9] The Court concluded that the Berendsens had not provided evidence to prove that, in 1960, when the asphalt was deposited, harm to cattle was a reasonably foreseeable risk. In fact, the Court concluded that the evidence pointed the other way: that risk was not foreseeable at that time.

The Berendsens sought leave to appeal, and the Supreme Court of Canada granted their application; however, on the threshold of a second visit to the Supreme Court of Canada, the case settled.

Smith v. Inco[10] is another storied environmental case that went to the Court of Appeal for Ontario – twice.[11]

The case involved the contamination of soils around residences with nickel. Inco operated a nickel refinery at the site from 1918 to 1984. Its emissions were never illegal or negligent, but they did deposit nickel on soil near the plant. After a Community Based Risk Assessment, the MOE ordered Inco to remediate soils around 25 residences in 2002 (this was done, except on the property of the representative plaintiff in the case, who refused to allow remediation).

Initially, the case was advanced as a class proceeding for health impacts and property damage alleged to have been caused by the pollution. Certification was denied by the class proceeding judge, and that order was upheld by the Divisional Court; however, the Court of Appeal reversed. The class was certified by the Court of Appeal on the basis of property damage claims alone. The health related claims had been withdrawn. The matter was sent back to trial, which resulted in a decision awarding damages in the amount of $36 million based on private nuisance and strict liability (i.e. the rule in *Rylands v. Fletcher*).

Inco appealed. Once again, the Court of Appeal reversed, this time in Inco's favour. The Court concluded

that the trial judge had erred in finding a private nuisance. The Court concluded that nuisance requires physical harm or damage to property, and that there was no evidence to substantiate that. The mere presence of metals in the soil would not suffice, even at levels higher than MOE generic criteria, and whether or not it generated concerns among neighbours, unless there was evidence that the metals were dangerous to human health, or otherwise prevented the residents from occupying their homes.

The Court also concluded that the trial judge had erred in finding strict liability. This tort traditionally applies to "non-natural" land use. The Court noted that the non-negligent operation of a refinery in a properly zoned, heavily industrialized area was not "non-natural". It was ordinary, and did not create a risk beyond those incidental to virtually any industrial operation. Finally, the Court ruled that there was no proof that the nickel had caused any loss in property value. The Supreme Court of Canada refused leave to appeal.

The Nova Scotia Court of Appeal has recently weighed in on these issues in *Sydney Steel Corporation v. MacQueen.*[12]

This case was a class proceeding against the federal and provincial governments, which involved historic airborne and waterborne emissions from steel and coke works, which operated from 1903 through 2000. The Nova Scotia Court of Appeal set aside the order certifying the action as a class proceeding. In so doing, the Court gave consideration to a number of torts.

The NSCA followed its Ontario counterpart in *Smith v. Inco*, and ruled that no cause of action was made out under the rule in *Rylands v. Fletcher*. The Court ruled that the use was not "non-natural" but rather an ordinary consequence of lawful activity (i.e. discharging pollution in an industrial area). Similarly, the routine discharge of contamination was not an "escape".

The NSCA also ruled that no cause of action was made out in trespass or battery, as the accumulation of contaminant was indirect and over the years, rather than direct and immediate as required in either tort.

The Court concluded that a cause of action in nuisance had been made out but went on, however, to conclude that neither nuisance, nor negligence claims should have been certified.

The NSCA concluded that many of the issues stated to be common, were not. For example, the Court noted that the nature of the impact of contamination on any of the individual class members whether in nuisance or negligence, would depend on the individual circumstances surrounding that impact. Accordingly, the Court's view was that there was no proper "common" issue in most cases. The few remaining common issues (such as whether defendants discharged contaminant) would not significantly advance all of the class members' claims at trial. Accordingly, for those common issues, the Court concluded that a class action was not the preferable procedure. The NSCA overturned the certification order.

The Alberta Court of Appeal most recently considered environmental tort issues in *Windsor v. Canadian Pacific Railway Ltd.*[13]

This was another TCE case. CPR operated an engine repair shop outside of Calgary. From the mid-50's to 1972, TCE was used as a degreasing solvent, and wastes were discharged into a settling pond, from which they leaked into groundwater. As a result of a contamination plume, CPR determined that some 70 neighbouring homes had indoor levels of TCE vapour above Health Canada thresholds, and installed ventilation systems. No remediation measures were taken on other homes in the area, as TCE levels were below the Health Canada thresholds. The action was certified as a class proceeding on behalf of both categories of neighbour.

Following *Inco* and *MacQueen*, the Alberta Court of Appeal concluded that the CPR shops were zoned for this type of industrial use and that the use was "appropriate to the place where it was maintained". Accordingly, the use was not "non-natural" or "special". The Court concluded that there was no "escape" within the meaning of *Rylands v. Fletcher* because the discharge of contamination was deliberate (which, the Court noted, seemed "surprising").

The ABCA referred to a House of Lords decision, *Cambridge Water Co. v. Eastern Counties Leather PLC*.[14] which introduced the notion of foreseeability in relation to an escape of TCE in the context of a strict liability claim. In *Windsor*, as in *Cambridge*, it was not until 10 years after the defendant's operation had ceased that it became known that TCE was more harmful than previously thought. It was almost 30 years later that it was first detected in the groundwater.

The Court also referred to the recent Supreme Court decision – *Antrim Truck Centre Ltd. v. Ontario (Transportation)*[15] - reiterating the requirement that damages in a nuisance claim not be nominal or trivial. The ABCA concluded that this was an issue which would have to be addressed at trial with respect to those homes with sub-slab ventilation. Those without ventilation (i.e. with levels lower than the Health Canada standard) had been carved out of the class on the certification motion.

These are recent cases which may significantly change the law associated with certain environmental torts. The panel will examine whether this is helpful to municipalities. Does it provide better protection against certain legacy problems (such as landfill methane or contaminated groundwater)?

Intervention in Regulatory Proceedings – Enbridge Line 9 Application

We all like to use oil. Few of us give a lot of thought to where it comes from, and how it arrives.

In 2013, we had a chance to investigate this issue. This, due to an Application by Enbridge Pipelines to reverse the flow of its Line 9B which runs from Hamilton to Montreal through the north end of the City of Toronto and through many other heavily populated municipalities.

Line 9 ran from west to east from 1976 to 1997. The direction of flow was reversed in 1997 to reflect market conditions. In late 2012, Enbridge applied to re-reverse the Line, to reflect market changes. The Application also sought an increase in capacity by 25% (without changing operating pressures) and to allow for the transport of heavier, tar sands crudes, including diluted bitumen (or "dilbit"). At the time of the Application, Line 9 had been operating for 38 years without major incident. Operation of the Line had been regulated by the National Energy Board through the entire time.

The Application was notorious for several reasons:

1. There were a number of controversial applications for new pipelines in North America (Keystone, Northern Gateway, Energy East, and others).

2. Serious spills had recently taken place in Kalamazoo, Michigan, where Enbridge's Line 6 ruptured in 2010; and in the Lac-Mégantic tragedy from 2013.

As a result, the Line 9 Application received considerable attention. A number of municipalities were

involved, including the City of Toronto. Issues raised by municipal intervenors (and others) included:

1. Pipeline integrity;
2. Emergency preparedness; and
3. Financial assurance.

Municipalities will be affected in the event of a major spill, including the costs incurred in responding to a spill, and, damage to municipal property and infrastructure. The Kalamazoo, Michigan incident is reported to have cost over $1 billion to date, and cleanup was still underway late in 2013.

At the end of the Line 9B Hearing, the project was approved with certain conditions. Some of the main outcomes of the Hearing included:

1. The conclusion that, with updated engineering measures, pipeline integrity can be managed.
2. The requirement that emergency plans be updated with input from municipal emergency responders and others.
3. The fact that NEB did not impose additional financial assurance requirements.

The City of Toronto and others had requested confirmation that up to $1 billion in financial assurance was available. The Government of Canada had indicated in 2013 that regulations to this effect would be promulgated. Nonetheless, the NEB did not impose that requirement on Enbridge (although one Board member dissented on this point). On May 14, 2014, the new Minister of Natural Resources, the Honourable Gregory Rickford, announced financial assurance and other measures to provide financial assurance. To date, no regulations or statutory amendments have been promulgated.

The panel will discuss the cost and value of intervention in these cases and, more generally, the scope of municipal liability in the event of a major spill. Clearly, there was and is a municipal interest in these issues. Participation in the NEB process comes at a price though, especially where it is necessary to retain expert assistance.

Liability Associated with the Management of Excess Soils

The proper transportation and management of excess soils and other fill materials provides a number of challenges:

1. Nuisance impact;
2. Potential environmental impact; and
3. The proper disposal of soil as waste where appropriate.

Nuisance impacts may be addressed through site alteration by-laws, which permit municipalities to govern the placement of fill within their jurisdiction.

Environmental impacts are generally addressed through the waste provisions contained within the Ontario *Environmental Protection Act*.

There has been a recognized need for some time to provide rules governing the management of excess soils. Although the Ministry of the Environment had been consulting on proposed regulatory amendments to address this issue since the late 1990s, these measures were not finalized until 2014. The long awaited regulation, though, came in the form of a guideline: Management of Excess Soil – A Guide for Best Management Practices[16] (the "Guide").

The Guide includes provisions applicable to:

- Source sites
- Receiving sites
- Auditable paper trails between the two

The Guide provides some welcome direction. Unfortunately, it leaves open several questions. Key is the extent to which a receiving site may "suitably" receive contaminated soils. In the past, the MOE had taken the position that soil with any contamination in excess of background levels[17] was a waste, as it may not meet the requirements of the (vague) definition of inert fill in Regulation 347 of the EPA. The Guide appears to leave that decision to the Qualified Person (as defined in Ontario Regulation 153/04). The regulatory provisions remain unchanged, however, leaving open arguments as to whether or not the disposal of soils which do not meet the definition of inert fill requires a Part V Environmental Compliance Approval.

Fill cases have been fertile ground for municipalities, which have tried to regulate the issue through fill placement by-laws. These by-laws have been subject to all manner of creative challenge.

In *Scugog (Township) v. 2241960 Ontario Inc.*,[18] the Divisional Court rejected the notion that the fill placement by-law did not apply because the owner was building an aerodrome. The Court concluded that the site was a fill site, not an aerodrome. In any event, as fill by-laws would not seriously impair aerodrome construction, interjurisdictional immunity would not preclude their application in this case.

In *Burlington Airpark Inc. v. Burlington (City),*[19] the receiving site was an airport that had been operated since 1962. The fill was being used for runway construction. The Court confirmed the *Scugog* decision, noting that "the by-law does not impact or intrude on the core of the Federal power".[20] Further, as Justice Swinton had concluded in *Scugog*, nothing suggested that the applicant "had been prevented from selecting appropriate materials to deposit on the property".

The case is scheduled to be argued at the Court of Appeal for Ontario on June 11, 2014. Stay tuned.

Meanwhile, in Alberta, the Court of Queens Bench reached a different conclusion in *Parkland Airport Development Corp. v. Parkland (County).*[21] In that case, the municipality required a development permit to allow for stripping and grading required to develop the airport. The Court concluded that this requirement was a significant intrusion on the exercise of the Federal aeronautics power.[22] Interestingly, the Court observed that everyone had agreed that municipal haul permits and fees could be required;[23] however, a development permit could not be a pre-condition to the issuance of these permits.

In another amusing line of cases, the disposal of fill on agricultural lands has been argued to be exempt from municipal regulation on the basis that it is a "normal farming practice". These arguments have had little success.[24]

Municipalities will now have to weigh what practices and procedures should be applied to their own activities, and how the existence of the Guide may affect any duty of care they are subject to.

Questions have also been raised as to potential municipal liability for soils exported from third party lands within the municipality. In *Northmarket Holdings Inc. v. Redvers et al,*[25] the Court of Appeal concluded that there is no private law duty to ensure that fill removed from a development site be directed to an approved disposal site. The Court specifically noted that the subdivision agreement did not refer to disposal at approved sites. One wonders what would have happened if it had, which is exactly what the MOE Guide promotes.

In the event that municipalities enact site alteration by-laws or requirements for developers to comply with the MOE Guide, they become exposed to potential liability for negligent implementation of these policies.

These schemes must therefore be considered in terms of the cost and staffing required.

Municipalities will certainly seek to insulate themselves from any such liability by relying, as a matter of policy, on the representations of Qualified Persons.[26] This will invariably lead into questions about reliance letters (get them) and consultant limitations (avoid them).

The panel will review liability trends in this area, especially in relation to implementation of the MOE Guide.