THE NEW COMPETITION ACT

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In this article, the authors examine the most significant changes to Canada's competition law, introduced by the enactment of the Competition Act and the Competition Tribunal Act in June, 1986. Among the key provisions are those providing for the review of mergers and monopolies on a civil rather than a criminal standard, and the creation of the Competition Tribunal empowered to issue orders in respect of these and other reviewable trade practices. The authors argue that the new law may signal a more sophisticated economic analysis in competition matters and that the availability of consent orders and advance clearance of mergers should strengthen both the role of the Director and the role of negotiation in respect of matters arising under the legislation.

Dans cet article, les auteurs analysent les modifications les plus importantes apportées au droit canadien relatif à la concurrence qui ont étés introduites au mois de juin 1986 lors de la mise en vigueur de la Loi sur la concurrence et de la Loi sur le Tribunal de la concurrence. Parmi les dipositions-clé se trouvent celles qui prévoient l'examen préalable des fusions et des monopoles d'après des normes de droit civil plutôt que pénal ainsi que celles qui créent le Tribunal de la concurrence ayant pouvoir de rendre des ordonnances sur ces pratiques commerciales comme sur toutes celles qu'il a le droit d'examiner. Les auteurs avancent qu'il est fort possible que ces nouvelles mesures marquent l'avènement d'une analyse économique plus sophistiquée en matière de concurrence et que le rôle du Directeur comme celui de la négociation relative aux questions émanant de la législation, soient renforcés par les moyens tels qu'ordonnances sur consentement et examens préalables des fusions.

Introduction

With the enactment of the Competition Act[1] and the Competition Tribunal Act[2] in June, 1986, the federal Parliament not only completed an amendment process that was twenty years in gestation but it reformed the law fundamentally. Instead of a prosecutorial, court system based on the criminal law power, we now have the beginning of a new regulatory

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[1] S.C. 1986, Part II, c. 26, s. 19 renames the Combines Investigation Act, R.S.C. 1970, c. C-23, the Competition Act. Part II of the 1986 Act contains extensive amendments to the legislation.

[2] S.C. 1986, c. 26, Part I.

system, complete with its own Tribunal, based on the federal power to regulate trade and commerce.[3]

The statute contains provisions for consent orders and advance ruling certificates which effectively permit settlement of all issues that can be tested before the Tribunal. The focus may change from litigation to negotiation. The provisions relating to mergers and abuse of dominant position, which are heard by the Tribunal, may well usurp the old conspiratorial offences as the prime focus of the statute. This is a new world of competition law and will be of signal importance to commercial lawyers. In this article we have tried to explain the major new provisions, with particular reference to similar provisions in the laws of the United States and the European Community, from which the Canadian provisions seem to have been borrowed.

I. *The Competition Tribunal*

Since its inception in Canada in 1889, competition law has been framed in terms of criminal law, in contrast to the civil law approach used in Europe and the mixture of civil and criminal jurisdictions used in the United States.[4] While most of the recent proposals have favoured a change to some form of civil basis, at least as a complement to the criminal provisions, there have been mixed opinions on the appropriate adjudicative body to impose civil remedies.[5]

The Competition Tribunal Act establishes a hybrid specialized tribunal composed of both judges and lay persons empowered to hear applications and issue orders in respect of the reviewable matters contained in Part VII of the Competition Act. Part VII includes the provisions in respect of mergers, abuse of dominant position, specialization agreements, delivered pricing, the reviewable trade practices previously contained in Part IV.1 of the Combines Investigation Act,[6] and other matters.[7] The Tribunal is constituted as a court of record consisting of up to four judges of the Federal Court Trial Division and up to eight lay members

[3] See C.S. Goldman, The Constitutionality of the Combines Investigation Act Civil Damages Remedy (1986), 11 C.B.L.J. 385.

[4] Economic Council of Canada, Interim Report on Competition Policy, Ottawa: Information Canada (1969), p. 107ff.

[5] L. Skeoch and B. McDonald, Dynamic Change and Accountability in a Canadian Market Economy, Ottawa: Minister of Supply and Services, Canada (1976), p. 39ff.; Interim Report on Competition Policy, *supra*, footnote 4, p. 110; Minutes of Proceedings and Evidence of the Standing Committee on Finance, Trade and Economic Affairs, Issue #66 (June 27, 1977), p. 66A:96, submission of the Canadian Petroleum Association.

[6] *Supra*, footnote 1.

[7] Part VII of the Competition Act also includes provisions in respect of foreign laws and directives (ss. 54 and 55), and a provision (s. 56) concerning refusals to supply by foreign suppliers.

appointed by the Governor in Council, on the recommendation of the Minister of Consumer and Corporate Affairs.[8]

It is axiomatic that the Tribunal can only be as good as its appointees, and although the Act provides no specific criteria in respect of the qualifications of lay members who sit on the Tribunal, section 3(3) of the Act permits the Governor in Council to establish an advisory council to advise the Minister with respect to the appointment of lay members. The advisory council would be composed of up to ten members "knowledgeable in industry, commerce or public affairs" who may include representatives of the business community, the legal community, consumer groups or labour.[9] If an advisory council is established, and it has been, it must be consulted by the Minister before any recommendation with respect to the appointment of a lay member is made to Cabinet,[10] which should go some way toward alleviating concerns with respect to the qualifications of those sitting on the Tribunal.

Four judicial members and one lay member were appointed initially, with Madam Justice Reed being appointed the Chairman. At least one judicial member must hear every application and, in general, the panel must consist of no less than three and no more than five members, at least one of whom is a lay member.[11] In respect of applications for interim orders, however, a single judicial member may sit alone.[12] In proceedings before the Tribunal, questions of law are to be determined exclusively by the judicial members of the panel while questions of fact or mixed law and fact are to be determined by all the members, both lay and judicial.[13]

Unlike the Restrictive Trade Practices Commission, which it replaced, the Competition Tribunal exercises no investigative or inquiry functions, but is strictly an adjudicative body empowered to make findings and issue remedial orders. The separation of all investigative or prosecutorial powers from the adjudicative function is consistent with the Supreme Court of Canada's ruling in the *Southam*[14] case in which the court held that some investigative functions vested in the Restrictive Trade Practices Commission ill accorded with the neutrality and detachment expected of the members of the Commission. While proceedings before the Tribunal are

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[8] Competition Tribunal Act, s. 3(2).

[9] *Ibid.*, s. 3(3).

[10] *Ibid.*, s. 3(4). Skeoch and McDonald, *op. cit.*, footnote 5, p. 295, pointed out that "the government does not enjoy an altogether distinguished reputation for its appointments to boards and commissions in the past".

[11] Competition Tribunal Act, s. 10.

[12] *Ibid.*, s. 11.

[13] *Ibid.*, s. 12(1)(a) and (b).

[14] *Hunter* v. *Southam Inc.*, [1984] 2 S.C.R. 145, (1984), 11 D.L.R. (4th) 641, [1984] 6 W.W.R. 577.

intended to be informal and expeditious, the Tribunal has the same powers as a court with respect to the examination of witnesses, the production and inspection of documents, the enforcement of its orders and other matters.[15]

Although the Competition Tribunal is a unique judicial institution in Canada, it shares some similarities with the Restrictive Practices Court, the adjudicative body given responsibility in respect of the United Kingdom Restrictive Trade Practices Act.[16] The Restrictive Practices Court is composed of five judges (three from the High Court, one from the Court of Session and one from the Northern Ireland Supreme Court) and up to ten non-judicial members. However, the legislation it administers is not comparable to the Competition Act, dealing mainly with the registration of restrictive agreements if certain "gateways" are available.[17]

Only the Director may bring applications before the Tribunal,[18] but the statute provides a panoply of remedies, including the divestiture of assets or shares, the dissolution of an amalgamation, the prohibition of a proposed merger or the allowance of a proposed merger to be completed only on specified conditions.[19] Interim orders, either on notice, or in limited circumstances, on an *ex parte* basis, are available to prevent mergers that would be difficult to undo subsequently after a lengthy proceeding or where there has been a failure to comply with the pre-merger notification requirements. Interim orders have effect for ten days in respect of *ex parte* orders and twenty-one days in respect of orders obtained on notice.[20] Interim orders may also be obtained outside of the merger context on the usual basis used by the courts. Where such an order is granted, the Director is required to proceed as expeditiously as possible with the main application.[21]

Probably the most important remedy is the availability of consent orders.[22] The provision allows the Tribunal to accept an order on terms agreed upon by the parties without hearing further evidence. This obvi-

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[15] Competition Tribunal Act, s. 9(2) and s. 8(2).

[16] Restrictive Practices Court Act, 1976 (24 Eliz. 2, c. 33).

[17] See R. Merkin and K. Williams, Competition Law: Antitrust Policy in the U.K. and the E.E.C. (1984); R. Whish, Competition Law (1985).

[18] The provisions in respect of specialization agreements (s.58(1)) being the one exception, although the Director must be given an opportunity to be heard. In addition, s. 7(1) of the Competition Act continues the procedure enabling any six Canadian residents not less than 18 years of age to apply to the Director to commence an inquiry where such persons believe, *inter alia*, that grounds exist for the making of an order under part VII of the Act.

[19] The major remedies are found in the Competition Act, ss. 51 and 64.

[20] *Ibid.*, s.72.

[21] *Ibid.*, s.76.

[22] *Ibid.*, s.77.

ously points to the likelihood of negotiated settlements. Consent decrees have played a major role in United States civil antitrust enforcement, with the majority of government civil antitrust suits being settled on a consent basis.[23] Before entering a consent judgment in the United States, the court must consider any comments received in respect of the proposal and must determine that the entry of such a judgment is in the public interest. In Canada, although the Tribunal's authority to grant consent orders is discretionary, the Act provides no guidelines and there is no suggestion of any public interest criterion.[24] Orders of the Tribunal are not cast in stone and can be rescinded or varied on application by the Director.[25] Also any order of the Tribunal whether final, interlocutory or interim, may be appealed to the Federal Court of Appeal, as if it were a judgment of the Federal Court Trial Division but leave to appeal is required if the appeal relates to a question of fact.[26]

Many commentators would have given Cabinet the authority to annul certain decisions of the Competition Board.[27] The Royal Commission on Corporate Concentration, however, took a different view, stating that cabinet review was a worse alternative than review of the specialized tribunals by the ordinary superior courts. ''If anything'', the Commission stated, ''it displaces open standards with hidden discretion. It will stultify the development of the law and it will create suspicion about the integrity with which it is administered''.[28] Apparently the government accepted this approach as the Competition Act contains no Cabinet over-ride. The elected Ministers will not have an opportunity to determine that a merger, even if found by the Tribunal to limit competition substantially, is nevertheless in the interest of Canada as viewed from the perspective of wider government policy, such as full employment or national defence.

II. *Mergers*

The new Competition Act, realizing on almost twenty years of government commissioned reports, expert opinion and failed legislative reform,[29]

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[23] See S.C. Oppenheim, G.E. Weston and J.T. McCarthy, Federal Antitrust Laws (4th ed., 1981), p. 1033ff.

[24] Earlier versions of the Competition Act required publication of proposed consent orders prior to final adoption in order to allow inputs from interested parties. Now there is no suggestion of any public interest input as the Tribunal need hear no evidence. Section 9(3) of the Competition Tribunal Act does permit the Tribunal to hear intervenors but that does not appear to relate to consent orders.

[25] Competition Act, s. 78.

[26] Competition Tribunal Act, s. 13.

[27] See, for example, Skeoch and McDonald, *op. cit.*, footnote 5, p. 314.

[28] Report of the Royal Commission on Corporate Concentration, Ottawa: Ministry of Supply and Services (1978), p. 163.

[29] Economic Council of Canada, *op. cit.*, footnote 4; Skeoch and McDonald, *op. cit.*, footnote 5; Report of the Royal Commission on Corporate Concentration, *op. cit.*,

repeals the criminal offence of merger and delivers merger adjudication to the civil jurisdiction of the Competition Tribunal. The merger provisions reflect Parliament's intention to regard mergers as neither inherently good nor inherently evil and direct the Tribunal to consider the likely competitive impact of mergers on the industrial, trading or professional markets in which they occur. Orders in respect of an impugned merger may be made where the Tribunal finds that the transaction "prevents or lessens, or is likely to prevent or lessen, competition substantially".

The substantial lessening of competition test, which is new to merger adjudication in Canada, closely resembles the United States standard in section 7 of the Clayton Act, which prohibits acquisitions where, "the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly".[30] This similarity of wording invites the importation of concepts of United States law into Canada.[31] Since the adoption of its new merger concepts in 1950, the struggle in the United States has been waged between standards inviting an open-ended inquiry into all the various factors that may be economically relevant[32] and the adoption of "simple rules" that focus on a few critical facts, such as market shares. The factors considered relevant under the open-ended approach include the market shares resulting from the merger, the existing degree of concentration in the industry, any trend toward concentration, the purpose of the merger and the history of the acquired and acquiring firms. However, in the early cases, particularly when one passes beyond the rhetoric of the opinions to the record of what was done, the conviction grows that the courts acted differently than they spoke; they invalidated rather slight and unimportant mergers in competitive industries on the basis of modest increases in concentration.[33] We hope that this will not be our experience in Canada.

An effective merger policy demands the enunciation of standards that at once check harmful mergers, bypass the harmless ones and provide

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footnote 28; A Report of the Task Force on Competition Policy of the Business Council on National Issues (1981); Bill C-256 (28th Parl., 3rd Sess., 1st Reading June 29, 1971); Bill C-42 (30th Parl., 2nd Sess., 1st Reading March 16, 1977); Consumer and Corporate Affairs, Proposals for a New Competition Policy for Canada, Second Stage, Ottawa: Minister of Supply and Services (1977); Bill C-13 (30th Parl., 3rd Sess., 1st Reading November 18, 1977); Bill C-29 (32nd Parl., 2nd Sess., 1st Reading April 2, 1984).

[30] 15 U.S.C.A., s. 18 (1980).

[31] As has been done in the Securities Law field when Canada adopted a system similar to the U.S. system; see *Pacific Coast Coin Exchange* v. *Ontario Securities Commission*, [1978] 2 S.C.R. 112, (1977), 80 D.L.R. (3d) 529.

[32] The seminal case adopting this approach, at least in theory, is *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 82 S.Ct. 1502 (1962).

[33] See L.A. Sullivan, Handbook of the Law of Antitrust (1977), p.59. The high water mark likely came in *United States* v. *Von's Grocery Co.*, 384 U.S. 270, 86 S.Ct. 1478 (1965), where the market shares were less than 10% but the merger was condemned.

a reasonable level of predictability to parties contemplating a business acquisition. This is a tall order. Whether broad or narrow criteria are adopted, identification of the pertinent market in which the merger occurs is central to the analysis. The boundaries of the product and geographic market define the extent of the industry in which structural change and competitive impact are examined. The outward boundaries of the market expand or contract as emphasis is given to factors such as product substitutability and the possible influence of actual or potential competition.[34] This is easiest to visualize in horizontal mergers where the merging entities are in direct competition at the same level of business within an industry.

Some guidance as to how markets are to be defined for Canadian purposes can be found in the factors listed in the statute that the Tribunal may have regard to in considering whether or not a merger is likely to lessen competition substantially. These include "the extent to which acceptable substitutes for products supplied by the parties to the merger or proposed merger are or are likely to be available".[35] This provision invites the Tribunal to consider products to which buyers might turn in response to a price increase in the principal product.[36] But the inquiry into the presence or absence of such substitutes in the market signals a considerably more complex (and more costly) economic analysis.

The United States Department of Justice introduced new Merger Guidelines in 1984 that attempt to use bright-line tests to replace the *ad hoc* basis upon which markets have often been defined. In summary, the Guidelines define a market as a product or a group of products and a

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[34] See *R.* v. *J.W. Mills & Son Ltd. et al.* (1968), 56 C.P.R. 1, at p.35, a conspiracy case, in which the Exchequer Court of Canada endorsed the necessity of a careful market analysis as a predicate to examining the anti-competitive effect of impugned conduct.

[35] Competition Act, s. 65(1)(c).

[36] Where consumers are highly responsive to price changes among products which are reasonably interchangeable, the market is described as demonstrating high "cross-elasticity of demand". The greater the cross-elasticity of demand that exists between two products, the more closely "substitutable" are those products. The leading U.S. case on product demand substitutability is *United States* v. *E.I. Du Pont de Nemours & Co.*, 351 U.S. 377, 76 S.Ct. 994 (1956). In *Eddy Match Company* v. *The Queen* (1953), 18 C.R. 357, 109 C.C.C. 1, 20 C.P.R. 107 (Que. Q.B. App. Side), app. for leave to appeal refused (1953), 109 C.C.C. 26 (S.C.C.), the Quebec Court of Queen's Bench Appeal Side rejected an argument by the appellants that paper matches and mechanical lighters were product substitutes of wooden matches and ought therefore to be considered in determining the issue of "control of a class or species of business". In *R.* v. *J.W. Mills*, *supra*, footnote 34, the Exchequer Court of Canada recognized product substitutability as a relevant factor in market definition. "Cross-elasticity of supply" may also be relevant to market definition. This principle posits the potential for suppliers of similar products to devote resources to the production of a certain product in response to a price increase in respect of that product.

geographic area in which the product or products are sold such that a hypothetical, non-regulated, profit maximizing monopolist could profitably impose a non-transitory five per cent increase in prevailing prices.[37] Concerns have been raised both with respect to the dependence of the analysis upon hypothetical constructs and the potential costs of obtaining the requisite information.[38] However, before rejecting the United States approach, the Tribunal will need a viable alternative to define the relevant market that is not so vague as to defy articulation.

Mergers are conventionally divided into three categories and subject to differing competitive concerns. Mergers between directly competing firms (such as supplier-supplier) are described as horizontal; mergers between firms in a buyer-supplier relationship are described as vertical; the term conglomerate merger is generally used to describe mergers that are neither horizontal nor vertical.

The merger provisions of the Competition Act clearly apply to horizontal and vertical mergers and appear broad enough to catch other forms of business structure, for example, joint ventures.[39] Whether the reference to acquisitions of "other persons" is intended to bring conglomerate mergers within the scope of the Act is not clear. Assuming a market has been defined, the Tribunal must then consider the likely impact on competition within that market by the merging of the entities. That impact and the tests used will differ depending on the type of merger under consideration.

A. *Horizontal Mergers*

Horizontal mergers are generally considered to be of the most competitive significance, and in recent years, enforcement in the United States has focused almost exclusively on horizontal mergers, in the belief that they pose the greatest potential harm to consumers.[40] Although serious anti-competitive effects may result from horizontal mergers between significant competitors, it is equally clear that horizontal mergers may be of significant economic benefit. The Economic Council of Canada noted in its 1969 Interim Report on Competition Policy:[41]

> On the good side, mergers may be an important means by which owners who wish to divest themselves of a business or a part of a business can do so with a minimum of disruptive economic effects. They may also be the most appropriate means of

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[37] U.S. Department of Justice Merger Guidelines, s.2.

[38] See D. Boies and R.L. Goss, Relevant Geographic Markets, in 22nd Annual Advanced Antitrust Seminar (Practising Law Institute, 1982), p. 51ff; R.H. Sayler, The Justice Department's 1982 Merger Guidelines, *ibid.*, p. 543.

[39] Because of the word "establishment" in s. 63.

[40] See J.E. McCarty, Merger Enforcement at the Federal Trade Commission, in The F.T.C. 1984 (Practising Law Institute, 1984), p. 222.

[41] *Op. cit.*, footnote 4, p. 113.

achieving certain cost savings, or bringing about industrial reorganizations made necessary by changes in patterns of demand or in the technical conditions of production.

Further, horizontal mergers may have a pro-competitive effect, where, for example, the combination of two insignificant firms facilitates competition with a market giant.[42]

In *United States* v. *Philadelphia National Bank*,[43] the United States Supreme Court adopted a test of presumptive illegality in respect of horizontal mergers that would be met if a merger produced a firm controlling an undue percentage share of the relevant market and resulted in a significant increase in concentration. The court added that where concentration was already great, "even slight increases in concentration" could satisfy the presumptive test. This cast a sharp focus on market shares which is still very dominant in United States thinking, although there are now signs of a broader approach. Since 1974, the United States Supreme Court and the enforcement authorities have adopted a framework that takes into account efficiencies, market dynamics, longer term industry characteristics and other economic variables. In the pivotal case of *United States* v. *General Dynamics Corp.*,[44] the Supreme Court upheld a merger between competing coal companies, notwithstanding market shares above levels previously found to be unlawful. Nevertheless, market share analysis and concentration ratios are still a primary focus.

In the Department of Justice 1984 Merger Guidelines the Herfindahl-Hirschmann Index (HHI) has replaced the older concentration ratios as a measure of market concentration. Concentration ratios represent the aggregate percentage share of market sales accounted for by a specified number of the largest firms (generally four) in the market. In a market, for example, where the top four firms hold ten per cent, the four firm concentration ratio would be forty per cent. The HHI however, measures the sum of the squares of the market share of *each* firm in the market. For example, a market of ten firms, each with ten per cent of the market would have an HHI of 1,000. Using this system, it is alleged that a more accurate impact of a horizontal merger can be obtained. For example, a merger will have the same effect on the Index regardless of the number of firms in the market. The guidelines establish thresholds that will normally govern the Department's response to any particular merger. The Depart-

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[42] See J.E. Kwoka, The Effect of Market Share Distribution on Industry Performance (1979), 61 Rev. Econ. & Stat., at pp. 101-109. In the 1982 Merger Guidelines, the Department of Justice stated: "There is some economic evidence that, where one or two firms dominate a market, the creation of a strong third firm enhances competition. The Department has considered this evidence but is not presently prepared to balance this possible gain against the certainty of substantially increased concentration in the market." This reference was omitted from the 1984 Guidelines.

[43] 374 U.S. 321, 83 S.Ct. 1715 (1963).

[44] 415 U.S. 486, 94 S.Ct. 1186 (1974).

ment is not likely to challenge mergers that result in a post merger HHI of less than 1,000, and is likely to challenge if the post merger HHI exceeds 1,800 *and* the increase in the HHI is more than 100 points. For example, in a market where the two largest concerns each had twenty per cent of the market, there were two fifteen per cent holders and three ten per cent holders, any merger of a ten per cent holder with a fifteen per cent holder would trigger action.

In the Canadian context, the new Competition Act includes a number of factors which the Tribunal should consider and which should ensure that no presumptions based on a Canadianized HHI will arise.[45] The Tribunal may have regard to foreign competition, the possibility that either of the companies is failing, the existence of entry barriers, as well as the extent to which effective competition remains or would remain in the market. In addition, the Act recognizes a limited "efficiencies defence" where the merger is likely to result in gains in efficiency that will be greater than, and offset, any adverse effect on competition in the relevant market.[46]

The inclusion in the listed considerations of a "failing company" concept suggests that an acquisition that might otherwise be challenged because of increased concentration, should be spared on the basis that any anti-competitive effects are outweighed by the public interest in protecting employees, shareholders, creditors and the community from the detrimental effects of a business failure. The doctrine was first raised by the United States Supreme Court in *International Shoe Company* v. *Federal Trade Commission*,[47] but the American courts have only resorted to it when the prospect of rehabilitation was so remote that the company faced the grave probability of business failure and there was no other available purchaser that provided a less anti-competitive alternative.[48] While the Canadian approach has been more liberal, it is clear that the new Act does not view the failing company concept as an absolute defence but simply as a factor to be balanced in weighing a merger's effect on competition.[49]

Among the barriers to entry that may protect a business from new competitors entering its market are tariffs, regulatory restrictions, significant start-up costs and specialized technologies or know-how that cannot

[45] Section 64(2) of the Competition Act prohibits the Tribunal from focusing on market share alone.

[46] Competition Act, s.68(1).

[47] 280 U.S. 291, 50 S.Ct. 89 (1930).

[48] *Citizen Publishing Co.* v. *United States*, 394 U.S. 131, at p. 138, 89 S.Ct. 927, at p.931 (1969).

[49] See Skeoch and McDonald, *op. cit.*, footnote 5, p. 87; see also Restrictive Trade Practice Commission, Report Concerning the Manufacture, Distribution and Sale of Yeast, Ottawa: Dept. of Justice (1958), and the Competition Act, s. 65(1)(b).

be easily obtained. High barriers to entry that would discourage *de novo* entry into a market may accentuate the possible anti-competitive effects of a market entry by merger. Accordingly, this is an important factor for the Tribunal to consider. Whether fortunately or not, there are no additional indices that attempt to give mathematical precision to the height of entry barriers. Accordingly, a qualitative approach will need to be developed, which gives great scope for economic evidence to be introduced.

There are a number of possible "efficiencies" typically associated with mergers, including those that may result from plant size economies, superior management, research and development, finance and control, advertising and distribution, risk taking for large or unique projects, and overhead expenses such as insurance and legal services. American courts have traditionally been unsympathetic to the efficiencies defence. In *Federal Trade Commission* v. *Proctor and Gamble*,[50] for example, the United States Supreme Court stated:

> Possible economies cannot be used as a defence to illegality. Congress was aware that some mergers which lessened competition may also result in economies but it struck the balance in favour of protecting competition.

The efficiencies defence has, however, received considerable attention in the literature and more recently the Department of Justice has agreed to consider significant net efficiencies, if the parties to the merger establish them by clear and convincing evidence.

From a Canadian perspective, despite doubts expressed by Professor Thompson,[51] the Act gives express recognition to an efficiencies argument in section 68(1):[52]

> The Tribunal shall not make an order under section 64 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.

Subsection 68(2) provides, however, that in determining whether an efficiencies argument has been made out, the Tribunal *shall* consider whether the efficiencies put forward will result in "a significant increase in the real value of exports; or a significant substitution of domestic products for imported products". This may represent a significant limitation on the availability of an efficiencies argument, where a transaction is likely to have an entirely domestic effect. It is submitted, however, that the factors

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[50] 386 U.S. 568, at p. 580, 87 S.Ct. 1224, at p. 1231 (1967).

[51] See D.N. Thompson, Mergers, Effects and Competition Policy: Some Empirical Evidence, in J.R. Prichard, W.T. Stanbury, and T.A. Wilson (eds), Canadian Competition Policy: Essays in Law and Economics (1979), p. 297.

[52] Competition Act. s. 68(1).

enumerated in 68(2) are not the only factors that the Tribunal may have regard to in considering offsetting efficiencies, but only two key factors that the Tribunal must take into consideration. The dual burden of demonstrating not only that efficiencies are likely to occur, but further, that such efficiencies would not likely be gained if the transaction were disallowed, further attenuates the efficiency defence.

B. *Vertical Mergers*

Vertical integration may be of significant economic benefit to the transacting parties. Greater efficiencies and cost reductions may result and, moreover, the arrangement may be used defensively to protect the parties from the predatory policies of competitors in either an "upstream" or "downstream" market. The effect of a vertical merger in such instances may be competitively neutral or even pro-competitive. The concerns traditionally arising from vertical mergers are the potential for such arrangements to foreclose markets and facilitate the exercise of predatory or other anti-competitive practices.[53]

Section 63 of the Competition Act defines "merger" to include the acquisition of a supplier or customer and therefore clearly applies to vertical mergers. In American antitrust law, vertical mergers have principally been challenged on the basis that integration will foreclose a market for competitors. In *Brown Shoe Company*,[54] Chief Justice Warren identified the foreclosing of competitors of either party from a segment of the market otherwise open to them as the "primary vice of a vertical merger". The earlier United States cases, which generally applied the market share analysis familiar to horizontal mergers, tended to focus on the percentage of the upstream or downstream market foreclosed by the merger, in determining legality.[55] More recent cases[56] and academic authorities[57] have associated other factors with vertical integration, including "squeezing" competitors through price or supply manipulation, restricting outlets or sources of supply so as to require two-level entry by potential competitors, facilitating false product differentiation and removal of barriers to oligopolistic pricing practices.

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[53] See R.H. Bork, The Antitrust Paradox (1978), p. 225ff. Judge Bork is among the strongest opponents of antitrust concern with vertical mergers. For a different view, see W. Mueller, Public Policy Toward Vertical Mergers, in J. Weston and S. Peltzman (eds.), Public Policy Toward Mergers (1969), p. 150ff.

[54] *Supra*, footnote 32.

[55] See *United States* v. *Kennecott Copper Corporation*, 249 F. Supp. 154 (S.D.N.Y., 1965), aff'd *per curiam* 381 U.S. 414 (1965); *United States* v. *Aluminum Company of America*, 233 F. Supp. 718 (E.D. Mo. 1964), aff'd *per curiam* 382 U.S. 12 (1965).

[56] See *Fruehauf Corp.* v. *F.T.C.*, 603 F. 2d 345 (2d Cir., 1979); *United States* v. *Hammermill Paper Co.*, 429 F. Supp. 1271 (W.D.Pa., 1977).

[57] See, generally, P. Areeda and D.F. Turner, Anti-Trust Law (1980), Chapter 10.

While some academic writers have been very critical of the foreclosure theory and competition policy concern with vertical acquisitions generally, United States courts have not necessarily been ready to abandon the traditional foreclosure theory.[58] In 1983, the Second Circuit Court of Appeals berated a lower court for rejecting the foreclosure analysis in favour of "contemporary economic theory". However, the approach taken by the courts is only relevant if the enforcement agency decides to attack and, in the United States at least, there is evidence that the enforcement agencies are prepared to judge vertical mergers by considerably more lenient standards than those expressed in the case law.

In the 1984 Merger Guidelines, the elevation of entry barriers, rather than foreclosure, is at the heart of the approach. The Guidelines state that competitively objectionable barriers will not be found to exist unless, first, the degree of vertical integration is so extensive that potential entrants must enter at both the primary and secondary level; second, two-level entry is substantially more difficult than primary entry; and finally, overall concentration of the primary market is above 1800 HHI, reflecting a market structurally conducive to non-competitive performance. In addition, the Guidelines state that the enforcement agency may challenge a vertical merger that facilitates collusion through integration to the retail level, elimination of a disruptive buyer or the evasion of rate regulation.

The approaches set out in the Guidelines may be useful to Canadian lawyers who are attempting to convince the Director not to act, but the United States court decisions are likely to find more acceptance before a Tribunal charged with interpreting the statute. Again this marshalls the lawyer toward negotiation rather than confrontation.

C. *Conglomerate Mergers*

Conglomerate mergers raise competitive concerns normally in the arena of potential competition. The basic doctrine was described by the United States Supreme Court in *U.S.* v. *Falstaff Brewing Corporation*:[59]

> Suspect also is the acquisition by a company not competing in the market but so situated as to be a potential competitor and likely to exercise substantial influence on market behavior. Entry through merger by such a company, although its competitive conduct in the market may be the mirror image of that of the acquired company, may nevertheless violate section 7 because the entry eliminates a potential competitor exercising present influence on the market.

American case law since *Falstaff* has developed two "limbs" to the potential competition doctrine: the "perceived potential entrant" theory and the "actual potential entrant" theory.

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[58] *United States* v. *American Cyanamid Co.*, 719 F. 2d 558 (2d Cir. 1983), *cert.* denied, 104 S.Ct. 1596 (1984).

[59] 410 U.S. 526, at pp. 531-532, 93 S.Ct. 1096, at p. 1100 (1973).

The "perceived potential entrant" theory assumes that a significant potential competitor "waiting in the wings" of a market constitutes a present competitive force within that market. Fearing entry by a new and powerful competitor, firms are forced to behave in a competitive, efficient manner to protect their market. If the potential entrant enters the market by merger, the threat is eliminated without the concomitant benefit of an additional player entering the market as a new, independent competitor.

The "actual potential entrant" theory assumes not that the potential entrant *presently* exerts any competitive influence, but rather that such influence would be exerted if the firm actually entered the market as an independent entity. The United States Supreme Court has yet to sanction the "actual" potential competition theory but did discuss it in *Marine Bancorporation*.[60] The court there stated that it would be necessary to show that the relevant market is oligopolistic, that absent acquisition by merger the acquirer would likely have entered the market in the near future and that such entry would have a substantial likelihood of ultimately producing deconcentration of the market or other significant procompetitive effects.

From a Canadian perspective, the 1978 Report of the Royal Commission on Corporate Concentration concluded that "conglomerate mergers have not in general decreased competition within industries by increasing their concentration or by ceasing to be potential competitors by means of internal expansion".[61] Professor Thompson has expressed similar reservations with respect to the application of the potential entrant doctrine in the Canadian context. He has noted: ". . . potential entry seems only a minor factor in conglomerate situations, and the possibility of conglomerate mergers foreclosing potential competition is rather unlikely."[62]

The merger provisions of the new Competition Act do not expressly refer to conglomerate mergers. An argument against such application may perhaps be founded on the basis that one might have expected to find language drawn from the specialized doctrines that have been associated with conglomerate mergers included in the factors listed in section 65(1) of the Act. For example, the Tribunal could have been directed to have regard to the likelihood that the transaction would give rise to reciprocal arrangements, or eliminate potential competition. However, the remedial rather than penal character of the new merger provisions may leave little scope for a narrow construction argument.

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[60] 418 U.S. 602, 94 S.Ct. 2856 (1974). See also *Tenneco, Inc.* v. *F.T.C.*, 689 F. 2d 346 (2d Cir., 1982). Other leading cases include *F.T.C.* v. *Procter and Gamble Company*, *supra*, footnote 50; *Federal Trade Com.* v. *Consolidated Foods Corp.*, 380 U.S. 592, 85 S.Ct. 1220 (1965); *United States* v. *Northwest Industries Inc.*, 301 F.Supp. 1066 (N.D.Ill., 1969).

[61] *Op. cit.*, footnote 28, p. 124.

[62] *Op. cit.*, footnote 51, p. 323.

D. *Joint Ventures*

Section 67(1) of the Act provides a very limited exemption from the application of the merger provisions for certain types of joint venture. The exemption only applies to unincorporated joint ventures to undertake a specific project or a program for research and development. The joint venture must be pursuant to a written agreement that requires one or more of the parties to contribute assets to the combination, restricts the range of activities that may be engaged in by the joint venture and stipulates that the combination will terminate on completion of the program or project. In addition, it must be shown that the program or project would not have been likely to occur but for the joint venture, and finally, that the joint venture is not likely to lessen or eliminate competition except to the extent reasonably necessary to complete the program or project. The obvious corollary to the limited exemption is that joint ventures not falling within the narrow terms of the exception will be subject to evaluation under the merger provisions to determine whether such joint ventures lessen competition substantially.

In 1964, the United States Supreme Court resolved that the merger provisions of the Clayton Act did apply to joint ventures. In *United States* v. *Penn-Olin Chemical Company*,[63] the court held that Pennsalt and Olin, two firms involved or potentially involved in the manufacture and distribution of certain chemicals, were both capable and likely entrants into the sodium chlorate market in the southeastern United States. The court held that even if only one of the companies would have actually entered the sodium chlorate market, the joint venture eliminated the competitive force that would have been exerted by the remaining company anxiously waiting on the wings of the market. The lower court decisions subsequent to *Penn-Olin* have relied on the potential entrant doctrine, striking down joint ventures where one of the parties was a potential entrant and allowing those where separate entry was unlikely.[64] The Federal Trade Commission, however, recently approved a joint venture between General Motors and Toyota on the basis of a balancing of potential efficiencies against antitrust concerns.[65]

One possible implication of the application of the merger provisions to joint ventures may be that, if the *Penn-Olin* doctrine is the appropriate basis upon which a substantial lessening of competition may be found, it

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[63] 378 U.S. 158, 84 S.Ct. 1710 (1964).

[64] *Yamaha Motor Co., Ltd.* v. *F.T.C.*, 657 F. 2d 971 (8th Cir., 1981), *cert.* denied 456 U.S. 915, 102 S. Ct. 1768 (1982); *Northern Natural Gas Co.* v. *Federal Power Com'n.*, 399 F. 2d 953 (D.C. Cir., 1968); *United States* v. *F.C.C.*, 652 F. 2d 72 (D.C. Cir., 1980).

[65] See J.F. Brodley, The Limited Scope and Precedential Value of the FTC's GM-Toyota Decision, in Antitrust and Trade Policy in International Trade (Corporate Law Institute, 1984), p. 223.

may be illogical to deny that the Act applies to conglomerate mergers. Simply stated, the potential competition doctrine is only "half" as applicable to joint ventures as it is to conglomerates. A joint venture may at least add one new competitor to the market. Finally, if potential efficiencies should be a significant factor in the consideration of joint ventures, the attenuated efficiencies defence provided for in the Act may impede the development of a sound policy in this area.

III. *Pre-Merger Notification*

The concept of merger registration or prior notification has had a long history in the United States, culminating with the enactement of the Hart-Scott-Rodino Antitrust Improvements Act of 1976.[66] The Federal Trade Commission actually implemented a pre-merger notification program in 1969. The rules required reporting of both large asset acquisitions and stock purchases resulting in control of the target company. The obligation to report, however, was the beginning and end of the Federal Trade Commission requirements. No waiting period was imposed and, accordingly, while the rules kept the government informed of merger activity, the rules did not meet the key objective of providing the government with time to intervene in merger cases prior to consummation. The Federal Trade Commission has also established special reporting requirements for particular industries including grocery, dairy and cement. These rules continue in full force notwithstanding the requirements of Hart-Scott-Rodino.[67] The Hart-Scott-Rodino Act imposed prior notification and waiting period requirements for certain large mergers. It has long been recognized that any harmful effects of mergers can be extremely difficult to reverse or offset once the merger has been completed.[68] Accordingly, pre-merger notification is intended to give the authorities an opportunity to act before the merger is consummated.

In concept, both the existing United States and the new Canadian pre-merger notification systems are similar. The coverage criteria of both programs are based on a three part test which enquires into the nature of the persons, the size of the persons and the size of the transaction. Persons to whom the rules apply are required to provide such information in respect of the parties and the transaction as is required and to wait out a specified time period prior to consummating the transaction. Notification is not specifically limited to "mergers" and accordingly, notification must be given in respect of all share or asset acquisitions covered by the

[66] 15 U.S.C.S. ss. 1311-1314.

[67] P.D. Standish, Acquisitions and Mergers Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976: Pre-Merger Notification and Waiting Requirements, in 18th Annual Advanced Antitrust Seminar (Practising Law Institute, 1978), p. 237.

[68] Economic Council of Canada, *op. cit.*, footnote 4, p. 113.

three-fold test and not otherwise exempt. Despite these general similarities, however, there are significant differences between the two systems both in terms of coverage and operation.

A. *The Thresholds*

The Competition Act defines the term "person" broadly to include individuals and both incorporated and unincorporated entities. The obligation to notify, however, is only triggered by the acquisition of the assets or shares of an "operating business", which is defined as "a business undertaking in Canada to which employees employed in connection with the undertaking ordinarily report for work". This could eliminate notification of acquisition of certain portfolio companies.. Notification is also not required in respect of the acquisition of foreign assets and is only required in respect of the acquisition of foreign securities if they constitute voting shares of a foreign corporation that either carries on or controls a corporation that carries on an operating business in Canada.

The size of each party to the transaction is determined under Hart-Scott-Rodino by including all entities controlled by an entity that is not itself controlled by any other entity (the "ultimate parent entity"). The basic threshold is satisfied if one party to the transaction has annual net sales or assets of $100,000,000 and the other party has net annual sales or assets of $10,000.00. The size of each "ultimate parent entity" is considered separately. Accordingly, where the acquiring person has sales or assets of $99,000,000 and the acquired person has sales or assets of $99,000,000, the "size-of-the-persons" test would not be satisfied.

The Competition Act adopts a combined assets or combined gross revenues from sales formula for determining the size of the parties to which the pre-merger notification rules apply. Only where the parties to the proposed transaction, together with their affiliates, have assets in Canada, or gross revenue from sales in, from or into Canada that exceed $400,000,000 is the merger notifiable.[69]

B. *Size of the Transaction*

Under Hart-Scott-Rodino, the "size-of-the transaction" test is satisfied if, as a result of the acquisition, the acquiring person would hold *either* fifteen per cent of the voting securities of the acquired person or an aggregate total amount of voting securities or assets of the acquired person in excess of $15,000,000. The Federal Trade Commission Rules, however (Rule 8.02.20) have changed the basic test to prevent the fifteen per cent rule from sweeping in asset or share acquisitions of relatively low

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[69] The method of calculating the value of assets or gross sales is prescribed in regulations that were first released in February, 1987.

value, or share acquisitions involving relatively small issuers. Unless as a result of the acquisition the acquiring person would hold assets or voting securities of the acquired person valued at more than $15,000,000 or voting securities which confer control of an issuer which, together with all entities which it controls, has annual net sales or total assets of $25,000,000 or more, the transaction is exempt from the pre-merger notification requirements.

The pre-merger notification requirements of the Competition Act apply in respect of a proposed asset acquisition where the aggregate value of the assets to be acquired exceeds $35,000,000. With respect to the acquisition of voting securities, section 82(3) requires that the issuer corporation have assets or gross revenues from sales exceeding $35,000,000. Assuming that the latter criterion has been met, the provisions will apply where as a result of the proposed acquisition of voting shares the acquirer would own voting shares carrying more than twenty per cent of all outstanding votes in respect of a public company, or thirty five per cent of the outstanding votes in respect of a private company.

It is arguable that neither the acquisition of non-voting convertible preferred shares nor their conversion at a later time would trigger the notification requirements under the statute. Section 80(1) defines "voting share" as "any share that carries voting rights under all circumstances or by reason of an event that has occurred and is continuing". The Federal Trade Commission Rules specifically exempt the acquisition of non-voting convertibles from the operation of the United States statute but they define the exercise of the conversion right as an acquisition and accordingly the exercise of such right may require pre-merger notification. It may be that regulations will be issued to clarify this point in the Canadian context.

The Competition Act provides special size-of-the transaction rules for amalgamations. Notification would be required in respect of a proposed amalgamation where the continuing corporation would own assets or have gross revenues from sales in excess of $70,000,000. In addition, notification would be required in respect of an unincorporated combination that involves the contribution by one or more persons of assets of an operating business, where the revenues from sales generated by such assets that are the subject matter of the combination exceed $35,000,000.

D. *Additional Acquisitions*

The statute provides an additional acquisition threshold at which further filings are required. Further notification is required upon an acquisition by the acquiring party of additional voting shares giving the acquiring party fifty per cent of the votes attached to all outstanding voting shares of the target corporation. The fifty per cent threshold applies to both public and private corporations.

E. *Filing of Notice and Waiting Periods*

The Competition Act establishes two options available to persons required to comply with the pre-merger notification provisions. Section 93 allows a "short-form" filing requiring the filing party or parties to provide somewhat less detailed information with respect to the proposed transaction than would be required under section 94, the "long-form" filing provision. Although parties are at liberty to choose either the long or short form filing, the Director has the absolute discretion to require any party that has elected to file the short-form to provide the more detailed information required under section 94. This is the only jurisdiction given to the Director to request further information. The Director must make such a request within seven days of the original filing. The waiting period is seven days for the short-form filing and twenty-one days for the long-form filing. It has been suggested that as a practical matter, many parties may elect the long-form unless the obvious effects of the transaction are relatively minor or preliminary discussions with the Director indicate that the short-term filing would be sufficient.[65] The Director may terminate the waiting period prior to its expiration where he has decided that no application under the substantive merger section will be made in respect of the proposed transaction. In addition, parties need not comply with the pre-merger notification provisions at all if an Advance Ruling Certificate has been obtained. This is a most important provision and will be extensively relied upon if the Director is liberal in his approach.

A separate waiting period is established in respect of an acquisition of voting shares through a Canadian stock exchange. Provided that a "long-form" filing is done, the waiting period is ten trading days or such longer period, not exceeding twenty-one days, as may be allowed by the rules of the stock exchange before shares must be taken up.

F. *Exemptions*

The Competition Act lists eight specific transactions that are exempt from pre-merger notification. A ninth exemption is provided for "such other classes of transactions as may be prescribed". Five of the exemptions appear in one form or another in the United States' legislation. These are:

(1) Acquisitions of real property or goods in the ordinary course of business if as a result of the acquisition the acquiring person would not hold all or substantially all of the assets of a business.

(2) Acquisition of voting shares for the purpose of underwriting.

[70] J.C. Baillie, R.J. Holsten and K.E. Thomson, Structural Rationalization: An Analysis of the Specialization Agreement, Merger and Pre-Merger Notification Provisions of Bill C-91, in Competition Law in Canada, Insight (1986)

(3) Acquisition of voting shares resulting from a gift, intestate succession or testamentary disposition.

(4) Acquisition of collateral or receivables, or an acquisition resulting from a foreclosure or default made by a creditor in good faith in the ordinary course of business.

(5) A transaction between affiliates.

In addition, the Canadian statute exempts a Canadian resource property or share acquisition, pursuant to an agreement to carry out exploration or development activities; a transaction in respect of which the Director has provided an Advance Ruling Certificate; and a transaction pursuant to an agreement entered into before the coming into force of the pre-merger notification provisions and substantially completed within one year of their coming into force.

Because the exemptions, as presently proposed, are not co-extensive with the exemptions stipulated in the substantive merger provisions, there exists the anomaly that notification would appear to be required in respect of transactions that would not otherwise be susceptible to attack under the Act. Amalgamations under the Bank Act,[71] the desirability of which the Minister of Finance has certified, provide the best example.

G. *Content of Required Information*

The information required to be filed is extensive but is the type of information that a purchaser normally has available by the time an agreement to acquire has been finalized. As compared to the information requirements in the United States the Canadian provisions do not require information as to prior, industry related, acquisitions, nor is there a specific request as to any "vendor/vendee" relationships between the parties.

The Competition Act exempts from the pre-merger notification requirements all persons agreeing in writing to form a "combination" that imposes on one or more of the parties an obligation to contribute assets, where the agreement will govern a continuing relationship between the parties, no change in control over any party to the combination would result and the agreement restricts the range of activities that may have been carried on pursuant to the combination and contains provisions allowing for its orderly termination. This exemption from pre-merger notification may be broader than the substantive joint venture exemption discussed earlier.

H. *Penalties*

The Competition Act repeals section 42(2) of the Combines Investigation Act[72] and substitutes therefore:

[71] R.S.C. 1970, c. B-1.

[72] *Supra*, footnote 1.

> (2) Every person who, without good and sufficient cause, the proof of which lies on him, fails to comply with [the notification provisions] is guilty of an offence and is liable on summary conviction or on conviction on indictment to a fine not exceeding five thousand dollars or to imprisonment for a term not exceeding two years or to both.

It is somewhat surprising to find a "reverse onus" provision in legislation passed subsequent to the Charter of Rights and Freedoms[73] and it seems unlikely that this provision will survive in its present form. Alternative relief is provided in the form of an interim injunction.

IV. *Abuse of Dominant Position*

The criminal offence of monopoly, a component of Canadian competition law since the first Combines Investigation Act[74] has been replaced with a procedure empowering the Tribunal to review the abusive trade practices of dominant firms and prohibit the continued practice of anti-competitive behaviour or, where necessary to restore competition in an affected market, even order the divestiture of assets or shares.[75] If an order is to be issued three conditions must be satisfied:

(1) The persons involved must substantially control a class or species of business throughout Canada or any area thereof;

(2) Such persons must have engaged in a practice of anti-competitive acts; and

(3) Such practice has or is likely to have the effect of lessening competition substantially in a market.

A. *Control and Practice*

The concept of abuse of dominant position appears to be derived from Article 86 of the Treaty of Rome. In the *United Brands*[76] case, the European Court of Justice said:

> The dominant position referred to in this article relates to a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained in the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers.

Whether the Canadian test of control of a "class or species of business" is coextensive with or something less than control of "a market" is an open question. In *Eddy Match Company* v. *The Queen*[77] the Quebec Court of Appeal held that wooden matches were a separate species of

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[73] Constitution Act, 1982, Part 1.

[74] S.C. 1910, c.9.

[75] Competition Act, s.51(1).

[76] *United Brands* v. *Commission*, [1978] E.C.R. 207, [1978] 1 C.M.L.R. 429.

[77] *Supra*, footnote 36.

business from paper matches and mechanical lighters, even though all were lighting devices and might reasonably have been considered substitute products within a single market.

Assuming that the Tribunal finds "control of a class or species of business", it must then find that the firms making up the dominant group have "engaged in a practice" of anti-competitive acts. In *R.* v. *William E. Coutts Company Limited*,[78] the Ontario courts considered the concept of a "practice" as it related to loss-leaders. Two of Coutts' dealers each conducted one deep-discounting sale, lasting approximately one week. Coutts refused them further supplies and, when charged under the Combines Investigation Act, relied on the statutory defence that the dealers had engaged in the "practice" of using its greeting cards as loss-leaders. The Crown argued that a "practice" required a habitual or constant sale, but the court disagreed, holding that a practice denotes only something more than an isolated act or acts. Though there had been only two sales of short duration, there was uniformity and consistency for the term of each sale and that constituted a practice.[79]

B. *Anti-Competitive Act*

Control of a "class or species of business", and a *practice* of injurious acts, however, are not sufficient to prompt a Tribunal order. There must also be proof that the practice related to an "anti-competitive act" and that there was substantial lessening of competition in the market under review.[80]

With respect to anti-competitive acts, section 50 of the Act provides a non-exhaustive list of nine examples that the Tribunal may have regard to in considering whether a dominant firm has abused its market position. The list appears to have been drawn from anti-competitive conduct considered in Canadian and American monopoly cases rather than from the list of examples found in the European statute.[81] The application of Article 86 of the Treaty of Rome has not, however, been restricted to the four

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[78] [1968] 1 O.R. 549, at p.550, (1966), 52 C.P.R. 21 (Ont. H.C.), aff'd [1968] 1 O.R. 549, [1968] 2 C.C.C. 221, (1968), 54 C.P.R. 60 (Ont. C.A.).

[79] It is difficult to relate the concept of a "practice" to enumerated acts such as the acquisition by a supplier of a customer. Does the complainant have to show a series of such acquisitions?

[80] There are United States antitrust cases to the effect that the market analysis appropriate in merger analysis may not be appropriate in monopoly cases. See *United States* v. *Mrs. Smith's Pie Co.*, 440 F. Supp. 220 (E.D.Pa., 1976). Other cases, however, take the view that the same concepts are involved. See *Twin City Sportservice, Inc.* v. *Charles O. Finley & Company, Inc.*, 512 F. 2d 1264 (9th Cir., 1975).

[81] Thus the regulation of prices and output, which are two of the practices in the list provided in the Treaty of Rome, are not included in the Canadian list. Indeed any concept of "fair prices" has been denied in Canadian jurisprudence to date; see *Weidman* v. *Shragge* (1912), 46 S.C.R. 1, 2 D.L.R. 734; Restrictive Trade Practices Commission,

expressly stated examples of anti-competitive conduct. The Article has been considered applicable to a variety of forms of anti-competitive conduct including acquisitions that increase market dominance, refusals to deal and predatory pricing. Accordingly, both the existing and developing case law in respect of Article 86 will likely be of some interpretative value with respect to the abuse of dominant position provisions of the Competition Act.

The nine anti-competitive acts listed in section 50 all require some element of anti-competitive intent or purpose. Some of these, such as the use of fighting brands, have a history in Canadian case law while others, such as the adoption of incompatible product specifications, have been the subject of comment in American jurisprudence, but have yet to receive consideration by Canadian courts. Because the list is non-exhaustive, it is dangerous to infer a "safe haven" for anti-competitive conduct that falls outside the nine specific examples. A consideration of the listed examples, however, provides a framework within which to examine situations that have been recognized by authorities in Canada and other jurisdictions as representing unlawful exercises of market dominance. In addition, the list itself may provide some guidance as to the type of conduct, in general, that may be found by the Tribunal to violate the abuse of dominant position provisions. For example, the inclusion in all nine examples of a reference to some purpose, object, or design may suggest that an element of intent must be demonstrated in respect of all forms of conduct alleged to constitute an anti-competitive practice.

The first listed example, a vertical price squeeze, is premised on the ability of a dominant supplier, who deals at two levels of a distribution chain (for example wholesale and retail) to "squeeze" its unintegrated competitors in the retail market by raising the wholesale price of the product and maintaining the price charged by its integrated concern for the end product in the retail market.[82] Unintegrated purchasers, required to lower or maintain their selling prices to remain competitive in the secondary market, may find their profit margins squeezed or even eliminated.

A "price squeeze" allegation was considered in *Kaiser Aluminium and Chemical Corp*. v. *Bonjorno*,[83] a private antitrust action for damages

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Competition in the Petroleum Industry, Ottawa: Minister of Supply and Services (1986), p. 14. Discriminatory trade practices and tied selling are expressly addressed in ss. 34 and 49 of the Competition Act. This does not, however, preclude their status as a potential anti-competitive act under s. 50.

[82] See generally Oppenheim, Weston and McCarthy, *op. cit.*, footnote 23, p. 356ff; G. Birrel, The Integrated Company and the Price Squeeze Under the Sherman Act and Section 2(a) of the Clayton Act, As Amended (1956), 32 Notre Dame L. Rev. 5; Areeda and Turner, *op. cit.*, footnote 57, par. 728ff.

[83] 752 F. 2d 802 (3rd Cir., 1985), aff'ng 559 F. Supp. 922 (E.D.Pa., 1983), *cert.* denied 106 S.Ct. 3284 (1986).

based on violation of the monopolization provisions of the Sherman Act.[84] Kaiser was a major supplier of aluminium coil and sheet, the raw materials used by the plaintiff to manufacture aluminium pipe. Kaiser established a pipe manufacturing facility in close proximity to the plaintiff's plant and thereafter, so the plaintiff alleged, Kaiser deliberately raised the price of the raw aluminium to the same level as the price it charged for its finished pipe. The plaintiff was successful before a jury and this verdict was upheld by the Third Circuit Court of Appeals. The court cited Kaiser's deliberate withdrawal of an existing price structure that had moderated prices to the independent fabricators, the fact that Kaiser's price of pipe was often below the cost of the raw material and a system that enabled Kaiser's integrated fabricator to set the raw material prices for its competitors without affecting its own finished pipe costs, in determining that Kaiser had deliberately implemented the price squeeze "to destroy its competition".[85]

Price squeeze allegations were also raised in the Restrictive Trade Practices Commission Inquiry into the State of Competition in the Canadian Petroleum Industry,[86] but were not found to be substantial. The Commission, however, noting that "motives are notoriously difficult to decipher and objective tests are desirable",[87] recommended a two-part cost based test for identifying predation in the context of the dual distribution system employed in the petroleum industry. The thrust of the tests proposed by the Commission is that the squeeze is not predatory, and therefore not unlawful, unless the independent retailer's margin is compressed below zero when compared to the integrated supplier's retail price.

There does not appear to have been a decision under Article 86 in which a "price squeeze" constituted the abuse of dominant position alleged. However, in the *Commercial Solvents*[88] case, the European Court considered a "supply squeeze" pursuant to which Commercial Solvents forwardly integrated into the finished product market and refused to supply the raw materials to its prior customers (now its competitors) in the end product market. The company argued that it did not have sufficient capacity to produce raw materials for both its own integrated concern and

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[84] 15 U.S.C.S., ss. 1-7 (1890).

[85] *Ibid.* Apparently, the plaintiff was not in fact purchasing its raw aluminum from Kaiser at the material time. The plaintiff argued and the court accepted, however, the proposition that Kaiser was the price leader for raw aluminum in the market and accordingly, although the plaintiff did not make its purchases directly from Kaiser, the latter in fact controlled the price of raw aluminum.

[86] *Op. cit.*, footnote 81.

[87] *Ibid.*, p. 285.

[88] *ICI and Commercial Solvents Corporation* v. *E.C. Commission*, [1974] E.C.R. 223, [1974] 1 C.M.L.R. 309.

competing manufacturers. The Court of Justice rejected this argument and found against Commercial Solvents.

The "supply squeeze" though not included among the list of anti-competitive acts in section 50 of the Act, would likely be reached by the reviewable practice of "Refusal to Deal", provided for in section 47(1) of the Act. This example, in fact, points up one of the anomalies of the Act. A "supply squeeze", whether effected by a dominant firm or otherwise, would likely be subject to review under section 47(1), but, unlike the closely related "price squeeze", the Director need not demonstrate any anti-competitive purpose or intent to obtain an order from the Tribunal under this provision.

The second listed example in the statute involves the acquisition by an enterprise at one market level of either a customer or supplier for the purpose of impeding a competitors's entry into the market. While we know of no case directly on point in Europe, a horizontal merger has been held to be an abuse of a dominant position under the Treaty of Rome, which has no separate specific merger offence.[89]

There have been no vertical merger decisions in Canada and relatively few in the United States. The decision of the Second Circuit Court of Appeals in *American Cyanamid*[90] however, does illustrate a situation in which a vertical acquisition represented an alleged abuse of monopoly power. The recent litigation arose out of a 1981 application by Cyanamid to terminate the remaining provisions of a consent decree entered in 1964. The consent decree settled a Government complaint against Cyanamid in which the latter was said to control the entire domestic supply of melamine, a powder used in the production of plastic laminates. Formica Co. was the principal domestic user of melamine in the production of plastic laminates, and in 1956 Cyanamid acquired Formica Co. The government attack alleged that Cyanamid made the acquisition for the purpose of foreclosing others from selling melamine to Formica Co, and eliminating a substantial independent competitive factor in the manufacture of laminating resins and laminates. The consent decree required the continuation of outside purchases of melamine by Formica Co. When requested to lift the consent decree the lower court found that vertical integration would not produce any anti-competitive effects. On appeal to the Second Circuit it was held that the lower court had erred in applying "contemporary economic theory", rather than the previously developed court tests. The court therefore refused to lift the consent decree.

The third example in the statute involves the use of freight equalization against the plant of a competitor. Freight equalization, whether part

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[89] *Europemballage and Continental Can* v. *Commission*, [1973] E.C.R. 215, [1973] C.M.L.R. 199.

[90] *Supra*, footnote 58.

of an industry-wide delivered pricing scheme, or used selectively to meet or better the offerings of a freight advantaged competitor, typically involves the designation of one or more artificial "basing points" from which freight charges are calculated, regardless of the actual origin of goods sold.[91] If the customer is closer to the actual source of the goods than the designated basing point, it will pay an element of "phantom freight". Conversely, the supplier must "absorb" freight costs in those cases where the customer is nearer the base point than the actual plant of origin. In the Dynamic Change Report, Skeoch and McDonald drew a clear distinction between co-operative formula pricing and unsystematic area pricing employed as an individual effort to expand sales. The authors considered that "the latter category raises no policy issues", but added "except, of course, in cases where unsystematic area pricing may be part of a predatory pricing plan".[92] The practice of freight equalization can eliminate any competitive price advantage that a firm might have enjoyed in respect of customers close to its plant, and may give rise to allegations of abusive predation if exercised by a dominant firm against a smaller, "freight advantaged" rival.

Predatory intent can be defined generally as a dominant firm's deliberate sacrifice of current revenues through lower prices for the purpose of driving rivals out of the market.[93] The line between predation and acceptable anti-competitive conduct has been considered extensively in the context of predatory pricing, the anti-competitive conduct referred to in section 50(i) of the Act (and also a criminal offence under section 34(1)(c) of the Act).[94] Predation, however, still remains an elusive concept. In an influential 1975 article, Areeda and Turner posited an entirely "cost-

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[91] See *Corn Products Refining Co. et al.* v. *Federal Trade Commission*, 324 U.S. 726, 65 S.Ct. 961 (1945) (use of single basing point pricing system found to violate s. 2(a) of the Robinson-Patman Act as unlawful price discrimination); *American Chain & Cable Co.* v. *Federal Trade Com'n*, 139 F. 2d 622 (4th Cir., 1944) (delivered pricing system found unlawful on basis of conspiracy); see also *R.* v. *Armco Canada Ltd.* (1974), 6 O.R. (2d) 521, 17 C.P.R. (2d) 211 (Ont. H.C.) (delivered pricing system adopted by manufacturers of metal culverts found to be unlawful conspiracy). It will be noted that ss. 52 and 53 of the Competition Act make delivered pricing a reviewable practice. The effect of the provisions is to require a supplier to make delivery to a customer at any point requested by that customer, provided that the supplier makes a practice of ordinarily making deliveries at that point. The customer is entitled to the same terms that would be available if his place of business were located at the place of delivery. See also, *Boise Cascade Corp.* v. *Federal Trade Commission*, 637 F. 2d 573 (9th Cir., 1980).

[92] Skeoch and McDonald, *op. cit.*, footnote 5, p. 233.

[93] See *MCI Communications Corp.* v. *AT&T*, 708 F. 2d 1081, 112 (1982), *cert.* denied 104 S.Ct. 234 (1983).

[94] See *R.* v. *Consumers Glass Co. Ltd.* (1981), 33 O.R. (2d) 228, 57 C.P.R. (2d) 1 (Ont. H.C.), where O'Leary J. cited with approval the approach taken in *Re IBM Peripheral EDP Devices, Etc.*, 481 F. Supp. 965 (N.D. Cal., 1979).

based'' measure of predatory behaviour.[95] They suggested that any price below short-term marginal cost (the additional cost incurred to produce one additional unit) should be presumptively unlawful, while any price above short-term marginal cost should be presumed conclusively lawful.[96] This approach reflects a belief that so long as a company makes some profit, however small, the firm is operating efficiently and should not be subjected to antitrust scrutiny. If a dominant firm drops its price to the point where it loses money on the sale of each additional unit produced, it can be presumed that it is doing so for anti-competitive reasons. Although many United States courts have accepted elements of the Areeda-Turner test and have regarded pricing below marginal or average variable cost as a key indicator of predatory conduct,[97] there has been a general reluctance to rely entirely on cost-based criteria, to the exclusion of all other factors.[98]

The relevance of cost-based criteria to the issue of predatory pricing has been considered in a number of Canadian authorities. The Dynamic Change Report,[99] for example, was extremely critical of the Areeda-Turner test, focusing primarily on the shortcomings of short-run cost analysis. In the *Hoffman-LaRoche Limited*[100] case, the defendant pharmaceutical company was accused and convicted of selling tranquilizers to hospitals at predatory prices. Linden J. endorsed an expansive test for determining unreasonableness, in which the ''actual difference between the production cost or accounting cost and the sale price''[101] would be just one important factor among many. He accepted that pricing below ''cost''

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[95] P. Areeda and D.F. Turner, Predatory Pricing and Related Practices Under Section 2 of the Sherman Act (1975), 88 Harv. L. Rev. 697.

[96] The authors were also prepared to accept ''average variable cost'' as an acceptable surrogate.

[97] See *Northeastern Tel. Co. v. Am. Tel. & Tel. Co.*, 651 F. 2d 76, at pp.87-88 (2d Cir., 1981), *cert.* denied 455 U.S. 973 (1982); *Pacific Engineering & Production Company of Nevada* v. *Kerr-McGee Corp.*, 551 F. 2d 790, at p. 797 (10th Cir., 1977), *cert.* denied 434 U.S. 879 (1977); *Barry Wright Corp.* v. *ITT Grinnell Corp.*, 724 F. 2d 227 (1st Cir., 1983).

[98] See *Chillicothe Sand and Gravel* v. *Martin Marietta Corp.*, 615 F. 2d 427 (7th Cir., 1980); *Jays Foods, Inc.* v. *Frito-Lay Inc.*, 1985-2 Trade Cases par. 66/745; *Transamerica Computer Co., Inc.* v. *IBM Corp.*, 698 F. 2d 1377 (9th Cir., 1983), *cert.* denied 464 U.S. 955 (1983). The Ninth Circuit eschews the cost-based approach and has suggested that it may be open to the plaintiff to demonstrate predatory intent even where prices are actually above average total costs, but the First Circuit has rejected the Ninth Circuit's approach; see *Barry Wright Corp.* v. *ITT Grinnell Corp.*, *supra*, footnote 97.

[99] Skeoch and McDonald, *op. cit.*, footnote 5.

[100] *R.* v. *Hoffman-La-Roche Ltd.* (1980), 109 D.L.R. (3d) 5, 28 O.R. (2d) 164, 53 C.C.C. (2d) 1 (Ont. H.C.). The trial decision was affirmed by the Ontario Court of Appeal (1981), 125 D.L.R. (3d) 607 in a judgment that discussed mainly constitutional law points. See also J.P. Cairns, Predatory Pricing: Notes on Hoffman-LaRoche (1984), 9 C.B.L.J. 242.

[101] *Ibid.*, at pp.40 (D.L.R.), 200 (O.R.), 38 (C.C.C.).

would not be unreasonable where the sale was of short duration, the price cut was introduced defensively, or where long term economic benefits might accrue to the seller by reducing prices below cost. Linden J. also held that a price above "cost" can never be held to be unreasonable.

In *Consumers Glass Co. Limited*[102] O'Leary J. accepted the Areeda-Turner test as the appropriate standard for determining the existence of predatory conduct in a dominant supplier situation. There, Portion, a subsidiary of Consumers Glass, was the only supplier of small plastic lids in Canada. When, in 1975, a second company, Amhil, entered the small lid market offering lower prices, Portion responded by offering discounts to all customers. The Crown alleged that the discounts were introduced to eliminate Amhil from the market and amounted to predatory pricing. However, the court found that both Portion and Amhil could each have supplied the entire Canadian market for small plastic lids and considered it inevitable that one or the other would be forced from the market. The court also accepted as fact that at no time had Portion sold lids for less than the variable cost of producing them. Although Portion was not "profit maximizing" the evidence suggested that it was at least "loss minimizing" and accordingly, its conduct was not predatory, regardless of Portion's intent.

Section 50(i) requires that sales below "acquisition cost" must be for the purpose of eliminating or disciplining a competitor; below cost sales alone are not enough to establish predatory intent on the part of dominant firms. Accordingly, an objective cost-based test will not be the only factor considered by the Tribunal. Two observations may be made based on existing jurisprudence:

(1) Parliament appears to have endorsed a test for predatory pricing that should take into account both cost and non-cost factors; and

(2) A sale above "cost" cannot be an anti-competitive act.

Another defined anti-competitive act is the use of fighting brands introduced selectively on a temporary basis to discipline or eliminate a competitor. Fighting brands were a central issue in the monopoly conviction in the *Eddy Match*[103] case, where there was evidence of repeated use of fighting brands to force bankruptcy or absorption on new entrants. Contrasted to this is the allegation of the use of fighting brands in the Petroleum Industry.[104] There the Restrictive Trade Practices Commission did not characterize the practice as predatory or anti-competitive, concluding only:[105]

> Second brands appear to have helped give the integrated marketers time to adjust

[102] *Supra*, footnote 94.

[103] *Supra*, footnote 36.

[104] Restrictive Trade Practices Commission, *op. cit.*, footnote 81.

[105] *Ibid.*, p. 432.

their offerings without, as a group, sacrificing market share. Now that the integrated marketers' major brands are better positioned. . .second brands apparently are being withdrawn.

The anti-competitive acts listed in section 50(c) and (f), the pre-emption of scarce resources required by a competitor and the buying up of products to prevent the erosion of existing price levels, both focus on abuses of purchasing power by dominant firms. The Act recognizes supply pre-emption as an abuse only where practised with the "object of withholding the resources from a market". The few relevant American antitrust cases have also focused on exclusionary intent in determining the legality of alleged excessive purchases. In *United States* v. *Aluminum Co. of America*,[106] for example, it was alleged that the Aluminum Co. of America (Alcoa) had made pre-emptive purchases of certain bauxite deposits, not for the purpose of securing an adequate future supply, but only in order to seize upon any available supply and so to ensure its monopoly. Judge Hand noted:[107]

The very statement of this charge shows that it depends upon "Alcoa's" intent, for, if the purchases provided for the future needs of the business, or for what "Alcoa" honestly believed where its future needs, they were innocent.

Judge Hand was satisfied that the government had not shown the required unlawful intent and upheld the dismissal of this aspect of the complaint. It was further alleged that Alcoa had unlawfully pre-empted certain water power facilities, but this complaint too was dismissed by the court for want of proof of an unlawful purpose.

The law's concern with the buying up of products, so as to command higher prices, goes back to the early 16th century, when statutes were passed in England outlawing the practices of "engrossing" (the buying up of large quantities of foodstuffs or "cornering the market", to resell them at higher prices) and "forestalling" (the purchasing of goods before they came to market with the intention of selling them at higher prices).[108] In a recent British case, *Potato Marketing Board* v. *Robertsons*,[109] an independent potato farming concern alleged that the periodic buying up of potatoes by the Potato Marketing Board to support price levels contravened Article 86 of the Treaty of Rome. The Court rejected the argument, and stated in respect of the "support buying" issue:[110]

. . . the consumer derives substantial long-term advantages from the system oper-

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[106] 148 F. 2d 416 (2nd Cir., 1945); see also *American Tobacco Co. et al.* v. *United States*, 328 U.S. 781 (1946).

[107] *Ibid.*, at pp. 432-433.

[108] See J. Magwood, Competition Law of Canada (1981), p. 7ff; F.D. Jones, Historical Development of the Law of Business Competition (1926), 35 Yale L.J. 905; Combines and Fair Prices Act, 1919 S.C. 1919, c. 45, s. 17.

[109] [1983] 1 C.M.L.R. 93 (Co. Ct.).

[110] *Ibid.*, at p. 144.

ated by the Board. It is true that in the short term consumers could in years of surplus buy their potatoes cheaper if there were no support buying. Indeed, the evidence shows that in years of surplus without support buying they would sometimes be able to buy potatoes priced well below the cost of production but it does not follow that it would be in their long-term interest to do so or that they are prejudiced by their not being able to do so.

The *Potato Marketing* case underscores an important distinction between Article 86 and the abuse of dominant position provisions of the Competition Act. Article 86(b), the provision under which the court analyzed the support buying allegation, defines the unlawful effect of the limitation of production in terms of "prejudice to consumers". This is not the test under the Competition Act, which requires the Tribunal to evaluate the effect of anti-competitive practices upon competition, rather than the impact on the public as was the case under the monopoly provisions of the Combines Investigation Act.

The adoption of incompatible product specifications designed to prevent entry into, or to eliminate a competitor from a market, is another listed abuse. This type of conduct has been considered in several cases in the United States. In *Berkey Photo, Inc.* v. *Eastman Kodak Company*,[110] the court rejected the plaintiff's claim for pre-disclosure to competitors of Kodak's new camera system, but it did hold that if Kodak's decision to produce its new film in a format compatible only with its own newly introduced camera was justified not by the nature of the film, but motivated by a desire to impede competition in the manufacture of cameras capable of using the new film, Kodak would have been guilty of an antitrust offence. It is precisely the latter type of conduct at which section 50(g) of the Competition Act would appear to be directed. It might be noted as well that the court in *Berkey Photo* suggested, with some caution, that while the plaintiff was not entitled to damages for the failure of Kodak to pre-disclose, if the plaintiff had still been in the camera business, it may have been entitled to prospective relief requiring Kodak to disclose *future* innovations. In this regard, it may be considered whether such an order might be obtained under section 51(2) of the Act, which authorizes the Tribunal to make such orders "as are reasonable and necessary" to overcome the effects in a market of the anti-competitive practice.

Finally, the statute castigates requiring a supplier to sell only to certain customers with the object of preventing a competitor's entry into a market. This anti-competitive conduct may be compared with the reviewable practice of "exclusive dealing" which addresses downward restrictions imposed upon distributors by suppliers.

Only one case involving exclusive dealing has been decided under the Combines Investigation Act. In *Director of Investigation and Research*

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[111] 603 F. 2d 263 (2nd Cir. 1979), *cert.* denied 444 U.S. 1093 (1980).

v. *Bombardier Limited*,[112] the Restrictive Trade Practices Commission refused to prohibit the exclusive dealing practices of Bombardier, a snowmobile manufacturer and distributor. In determining whether Bombardier's exclusive dealing policy lessened or was likely to lessen competition substantially, the Commission considered the likely effect of the policy on Bombardier's competitors at the manufacturing, distribution and retail levels. The Commission found no evidence that the policy would have any effect in the manufacturing sector of the snowmobile market. Bombardier continued to face strong competition from competing manufacturers, a factor cited by the Commission as indicating, "that the most serious potential effects of an exclusive-dealing policy are not present".[113]

Limiting the customers of a supplier has been analyzed in United States case law as a form of vertical conspiracy. In *Klor's Inc.* v. *Broadway-Hale Stores Inc*,[114] for example, the United States Supreme Court accepted Klor's allegations that Broadway-Hale had exercised its "monopolistic" buying power to induce major manufacturers and distributors of electrical appliances to refuse supplies to Klor's and convicted Broadway-Hale as a conspirator.

C. *Lessening Competition Substantially in the Market and Superior Economic Performance: The "Zero Defences"*

The final aspect of the abuse of dominant position provisions requires that the abuse must have or be likely to have the effect of substantially lessening competition in a market. Once the Tribunal has found "dominance", which by definition posits a market completely or substantially devoid of competition, and a practice of anti-competitive acts, it is unclear what additional relevance the "substantial lessening of competition" factor could have to the Tribunal's determination as to the existence of abusive conduct. Similarly, there would not appear to be any scope for section 51(4) of the Act, which requires the Tribunal to consider whether a practice of anti-competitive acts is the result of superior competitive performance. Any suggestion of superior competitive performance would seem inferentially rebutted by proof of an anti-competitive practice, particularly as such proof appears, under the Act, to be predicated on a showing of predatory or anti-competitive intent.

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[112] 53 C.P.R. (2d) 47 (R.T.P.C.); see G. Takach, Exclusive Dealing After Bombardier: The Law is Not a Great Deal Clearer Than Before (1983), 8 C.B.L.J. 226.

[113] *Ibid.*, at p. 56.

[114] 359 U.S. 207, 79 S.Ct. 705 (1959). See also *Oreck Corp.* v. *Whirlpool Corp.*, 579 F. 2d 126 (2nd Cir., 1978), *cert.* denied 439 U.S. 946, 99 S.Ct. 340 (1978), where a rule of reason approach resulted in an acquittal.

D. *Joint Monopolization*

The reality of the Canadian marketplace is that oligopolies rather than single firm monopolies prevail. Typically, tightly concentrated oligopolies, particularly in industries involving relatively undifferentiated products, display a marked uniformity of performance among the firms within the oligopolistic structure. Each trader is aware that any attempt to enlarge its market share by price cutting will immediately lead to retaliation and likely deterioration of price stability and the substantial reduction of profits. This process of "conscious parallelism" may continue without actual collusion among competing firms. The Report of the Royal Commission on Corporate Concentration[115] noted, however:

> While the practice of conscious parallelism may lack all the customary elements of a formal agreement as defined by the courts in conspiracy cases, the economic effects may be just as pernicious as those associated with a conspiracy. Prices may be maintained, over a long time, at levels significantly above those that would exist under competitive conditions. Innovations and technological change may be initiated or introduced at a slower rate. Excess capacity may continue to exist over long periods, not only constituting a burden to the customers of the industry's output, but also acting as a barrier to the entry of new competitors. In addition, conscious parallelism may shift the major firms's cost curves upwards because of inefficiency in production and distribution in the absence of competitive pressures to be efficient. This inefficiency involves a waste of valuable resources and a loss to society as a whole.

In the *Large Lamps*[116] case, Pennel J. expressly held that the Combines Investigation Act's definition of monopoly could include a situation of "shared monopoly", between or among independent business entities. The court, however, found sufficient evidence to support an inference of express agreement among the accused, and accordingly, did not find it necessary to rule on the issue of whether "conscious parallelism" alone could support an offence under the Act.

Although United States antitrust law has long recognized the possibility of monopolization through conspiratorial action, no United States court has condemned monopolization through consciously parallel, but non-collusive, actions of firms within a tightly oligopolistic market. In 1982, the Federal Trade Commission dismissed a complaint against *Kellog Co., et al.*[117] on the basis that the evidence with respect to "shared

[115] *Op. cit.*, footnote 28, pp. 85-86; see also, Symposium on the Report of the Royal Commission on Corporate Concentration (1979), 3 C.B.L.J. 239, at p. 287.

[116] *R.* v. *Canadian General Electric Co. Ltd.* (1976), 15 O.R. (2d) 360, 34 C.C.C. (2d) 489, 29 C.P.R. (2d) 1 (Ont. H.C.); see F.H. Webber, Oligopoly and the Combines Investigation Act (1982), 6 C.B.L.J. 453.

[117] C.C.H. Trade Reg. Rep. Transfer Binder, FTC Complaints and Orders 1979-1983, par. 21, 899 (1982), p. 22,244; 42 ATRR 182. The FTC did condemn parallel behaviour in the *Antiknock Compound* case but was reversed on appeal; see *Ethyl Corporation* v. *F.T.C.*, 46 ATRR 347 (2nd Cir., 1984).

monopoly" would not support the issuance of a divestiture order. In reference to the "shared monopoly" theory, Commissioner Clanton, stated:[118]

> . . . I do not believe such a theory, however characterized, can serve as a predicate for the Commission to restructure an industry, at least in the absence of clear predatory behaviour, which is not claimed here. I do want to emphasize, however, that Section 5 may well provide the Commission with sufficient authority to attack non-collusive behaviour that contributes to or enhances anti-competitive conduct, and which is without compelling business justification. In such circumstances, the principal remedial tool for dealing with this kind of behaviour would be a conduct order.

Article 86 of the Treaty of Rome refers, as well, to the abuse of dominant position by "one or more" undertakings. The European Court of Justice, however, has refused to interpret this provision to control oligopolistic behaviour. In *Hoffman-LaRoche*,[119] for example, the European Court of Justice stated:

> A dominant position must also be distinguished from parallel courses of conduct which are peculiar to oligopolies in that in an oligopoly the courses of conduct interact, while in the case of an undertaking occupying a dominant position, the conduct of the undertaking which derives profits from that position is to a great extent determined unilaterally.

The Competition Act makes no reference to conscious parallelism. In the Guide[120] accompanying Bill C-91, the Minister states only that consideration was given to restricting the application of the law to a single firm, but "with an appropriately lower threshold of market power such as 'dominant market position'". Recognizing, however, that there are very few industries in Canada in which one firm controls its market, the joint dominance concept was maintained along with the higher "substantial or complete control" threshold. The Guide makes no reference to conscious parallelism, either in its comments with respect to abuse of dominant position or those in respect of the changes to the conspiracy section. In short, the Act leaves us no further ahead on the issue of conscious parallelism in the context of abuses of market dominance.

V. *Specialization and Export Agreements*

A. *Specialization Agreements*

The Competition Act creates a limited exemption for qualifying specialization agreements, from the Act's general prohibitions against conspiracy and exclusive dealing. A "Specialization Agreement" is defined as an agreement under which each party mutually agrees to discontinue

[118] *Ibid.*, at p.22,244.

[119] *Hoffmann-La Roche AG* v. *E.C. Commission*, [1979] 3 C.M.L.R. 211, at p. 275.

[120] Competition Law Amendments: A Guide, Ottawa: Minister of Supply and Services, Canada (1985), p. 22.

producing an article or service that each is engaged in producing at the time the agreement is entered into.[121]

The Economic Council of Canada observed that inadequate specialization in many Canadian industries had prevented firms marketing a multiplicity of products from achieving maximum plant efficiency through longer production runs. Although greater specialization could in some instances increase efficiency, the Council recognized that it may, nevertheless, not be in an individual firm's interest to make the independent decision to specialize and that market forces alone cannot always be relied upon to bring about the opportunities for greater economic efficiency obtainable through specialization.[122] The provisions of the Act allowing competing firms to enter into qualifying specialization agreements are intended to facilitate this process of "structural rationalization" of industries, that might not otherwise occur.

The price of greater efficiency, however, may be a lessening of competition. Accordingly, the statute imposes limitations on the availability of specialization agreements and requires the Competition Tribunal to balance the rewards of efficiency against the restrictions on competition that may result from such agreements. It must be shown that the gains in efficiency "would not likely be attained if the agreement were not implemented".[123] Section 58(2) of the Act further directs the Tribunal to consider whether gains from the agreement will result in a significant increase in the real value of exports or a significant substitution of domestic articles or services for imported articles or services. If the Tribunal is satisfied that the agreement or proposed agreement meets the requisite conditions, it may make an order directing the registration of the agreement for a period specified in the order. In contrast with earlier proposals, it falls to the Tribunal to determine appropriate time limits for each agreement.

The prescribed time period, however, does not necessarily entail that the agreement will remain in force for the period specified. Section 59(2) provides that the Tribunal may order the removal of an agreement from the register or the modification thereof. The section speaks in terms of the

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[121] Competition Act, s. 57.

[122] Interim Report on Competition Policy, *op. cit.*, footnote 4, pp. 74ff and 118ff.

[123] Competition Act, s.58(1)(a). Dr. Skeoch criticized a similarly worded efficiency test. Skeoch stated: "The additional requirement that the efficiency gains must not reasonably be expected to be attained by means other than the merger represents a concept of economic causation that must cause serious concern. To meet this requirement successfully would demand techniques of economic analysis that are so far unknown. The number of issues in economic history or in recent economic policy to which it would be possible to assign sole determinants or for which it would not be possible to reasonably ascribe alternative determinants must be very few, indeed.;" see (1984), Canadian Competition Policy Record, Volume 5, No. 2, p. 5.

agreement no longer meeting the requirements of the Act, rather than the parties no longer living up to the terms of their agreement. Accordingly, changes in market conditions, entirely beyond the control of the parties, might cause the agreement to fail to meet the requisite conditions. In addition, registration of an agreement may be made conditional upon the occurrence of any of five events:

(1) the divestiture of particular assets, specified in the order;

(2) a wider licensing of patents;

(3) a reduction in tariffs;

(4) the making of an Order in Council under section 17 of the Financial Administration Act[125] affecting a remission or remissions specified in the Order of the Tribunal of any customs duties on an article that is subject to the agreement; or

(5) the removal of import quotas or import licensing requirements.

It should be noted that the specialization agreement provisions are entirely permissive and create no offences or penalties. Non-registered specialization agreements are not unlawful *per se*; they simply do not enjoy the immunity from possible prosecution under the relevant sections of the Act that is obtained by registration.

The competition law of the European Economic Community also makes provision for the immunization of specialization agreements in certain circumstances.[125] Pursuant to this general exempting authority, Article 1 of the regulations creates what is known as a "block exemption" for specialization agreements of the type contemplated by the Canadian legislation. Block exemptions remove agreements from the operation of Article 85 on a generic basis and agreements that conform to the block exemption are inherently valid and require no further authorization.

The European Commission may also authorize specialization agreements on an individual basis where such agreements would not otherwise come within the terms of the block exemption. Professor Whish notes:[126]

> [T]he Commission has been consistently favourable towards specialization agreements which encourage the achievement of economies of scale and production thus lowering costs; even if an agreement falls outside the block exemption which exists, there is a good chance that an individual exemption will be given, although the Commission will look beyond the façade of an agreement to ensure that specialization really is its objective.

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[124] R.S.C. 1970, C.F-10.

[125] In addition to the exemption created under Article 85 of the EEC Treaty, Article 65(2) of the Treaty establishing the European Coal and Steel Community also provides an exemption for specialization agreements.

[126] *Op. cit.*, footnote 17, p. 336.

In *Re Italian Cast Glass*[127] the Commission denied a specialization agreement exemption in respect of agreements entered into by three Italian cast glass producers to divide among themselves the production of different types of glass. The arrangements, though structured as specialization agreements in form, were found by the Commission to be, in substance, agreements to divide the market and fix quotas among the participating producers.

Italian Cast Glass points out a number of issues relevant to a consideration of the specialization agreement provisions of the Competition Act. The Competition Tribunal might, for example, as did the Commission, look to the significance of the articles in respect of which the parties have agreed to cease production. Parties ought not be able to shield conspiracies that unduly restrict competition behind token attempts at specialization. Also, the manner in which productive capacity is divided pursuant to the arrangements may suggest to the Tribunal that any "specialization" that occurred had very little to do with achieving greater efficiency and everything to do with stifling competition.

B. *Export Agreements*

The Competition Act retains and broadens the export agreement exemption to the conspiracy offence by replacing the "volume of exports" test with a standard based on the "real value of exports". Under the new provisions, the agreements may have the effect of reducing the volume of exports, provided that price increases offset any reduction in the net value of such exports that may result. More significantly, the possible effect of the agreement on the domestic market for the exported product or products need no longer be considered by the parties. Section 32(5)(c) does, however, disallow the availability of the export agreement defence where the agreement is likely to prevent or lessen competition unduly in the supply of services facilitating the export of products from Canada. A conspiracy, for example, that unduly limited competition with respect to shipping facilities or insurance may not qualify for the export agreement exemption and may, therefore, subject the parties to possible prosecution.

Parties to an agreement that comes within the exemption provided by section 32(4) of the Act must nevertheless consider any possible impact that the antitrust laws of another jurisdiction may have upon the export arrangement. The extra-territoriality of United States antitrust laws has long been recognized. In *Timberlane Lumber Co.* v. *Bank of America*,[128] the Ninth Circuit Court of Appeals introduced a "jurisdictional rule of

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[127] [1982] 2 C.M.L.R. 61 (E.C. Commission). See also *Re Papeteries Bolloré SA and Braunstein Frères SA*, [1972] C.M.L.R. D94 (E.C. Commission).

[128] 549 F. 2d 597 (9th Cir., 1976).

reason'' test for determining the extra-territorial application of United States antitrust law. Stated briefly, the test addresses three factors:

(1) Does the restraint affect the foreign commerce of the United States;

(2) Is it of such a type and magnitude as to be cognizable as a violation of the Sherman Act;

(3) As a matter of international comity and fairness should the extra-territorial jurisdiction of the United States be asserted to cover the restraint.

In the United States, the Webb-Pomerene Act[129] provides an antitrust exemption for associations entered into for ''the sole purpose of engaging in export trade and actually engaged solely in such export trade'' and for ''an agreement made or act done in the course of export trade by such association''. The statute has been very narrowly interpreted and has done little to help the export trade. As a result, in 1982, the United States enacted the Export Trading Company Act,[130] Titles III and IV of which reduce the uncertainty regarding the jurisdictional reach of United States antitrust laws in respect of export agreements. Title IV of the Act provides that United States antitrust jurisdiction over export related activities is limited to conduct that has a direct, substantial and reasonably foreseeable effect on domestic commerce or on the export trade of a United States resident. The Title makes it clear that American antitrust concern with export arrangements is to be focused not on the possible competitive impact in foreign markets, but only on competition at home. Title III of the Act enables United States exporters to apply for a certificate of review issued by the Department of Commerce with the concurrence of the Department of Justice. This certificate provides virtual immunity from federal or state antitrust action in respect of the export arrangement covered by the certificate.[131] In addition, the provisions significantly limit the rights available to a private litigant to bring suit in respect of the conduct covered by the certificate.

While foreign companies may not apply for a certificate of review under Title III, United States subsidiaries of foreign firms are eligible, however, and foreign companies may receive the protection of a certificate by becoming members of a United States trading entity which receives

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[129] 15 U.S.C.S. ss. 61-65. The major cases interpreting the Act (and which considerably narrowed its scope) are *United States Alkali Export Association Inc.* v. *United States*, 325 U.S. 196, 65 S.Ct. 1120 (1945); *United States* v. *Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947 (Mass. Dist. Ct., 1950). See also *United States* v. *Concentrated Phosphate Export Association, Inc., et al.*, 393 U.S. 199, 89 S.Ct. 361 (1968).

[130] 15 U.S.C.S. ss. 4001-4003, 96 Stat. 1233 (1982).

[131] The lone exception being that the U.S. Attorney General may bring an injunctive suit against conduct threatening clear and irreparable harm to the national interest.

a certificate.[132] Accordingly, a Canadian export cartel may find shelter under a Certificate of Review and avoid the reach of United States antitrust laws, if it is composed of members having United States subsidiaries or, by becoming a member of a United States trading entity. The Canadian export cartel will be able to obtain the benefit of the certificate so long as the goods pass through the United States or through a United States territory at some stage during the course of the export operation. This may represent an important opportunity for Canadian exporters to make use creatively of the antitrust laws of the United States.

Conclusion

In conclusion, there are two other changes in the Competition Act that deserve at least brief recognition.[133] First, the statute now applies to Crown corporations in respect of commercial activities to the same extent as it applies to their competitors.[134] This change was required as a result of the Supreme Court of Canada decision in the *Eldorado*[135] case which held that the statute did not bind the Crown at all. Secondly, the collusive offence provisions that were contained in section 309 of the Bank Act[136] have been shifted to the Competition Act,[118] although the approval of bank mergers is still left with the Minister of Finance.[138]

Both these changes complement the fundamentally new approach of an economically sophisticated analysis of broad application directed through a central regulatory system. The Director's role is strengthened. Negotiation, not litigation, becomes the focus. It is an exciting development for those who support the concept of a competitive environment as essential to the future development of Canada in the global market-place of the next century.

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[132] U.S. Department of Commerce, Guidelines for the Issuance of Export Trade Certificates of Review (Second Edition), 5 CCH, Current Comment, par. 50,471 (1985), pp. 56, 149.

[133] We have not dealt with the new Tribunal jurisdiction over delivered pricing due to space limitations; see Competition Act, s. 52.

[134] *Ibid.*, s.2.1.

[135] *R.* v. *Eldorado Nuclear Ltd.*; *R.* v. *Uranium Canada Ltd.*, [1983] 2 S.C.R. 551, (1983), 4 D.L.R. (4th) 193.

[136] Banks & Banking Law Revision Act, S.C. 1980-81-82-83, c. 40.

[137] Competition Act, s. 33.

[138] *Ibid.*, s. 66(b).