

**LEGISLATIVE FRAMEWORK FOR AMENDING
SECTION 45 OF THE *COMPETITION ACT***

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I. EXECUTIVE SUMMARY

This report examines various legislative frameworks which could provide a basis for amending section 45 of the *Competition Act*. The main objective of such amendments would be to create a system which efficiently and effectively proscribes hard-core cartel behaviour, while encouraging strategic alliances and collaborations among competitors that produce pro-competitive benefits. Ancillary to this objective is the desire to harmonize Canada's laws with that of its major trading partners and, to the extent possible, provide a similar policy framework for competitor collaborations and mergers.

To determine the appropriate legislative model to meet the above objectives, we have examined the approach taken in a number of jurisdictions; specifically: the European Community, Germany, Italy, the United States, Australia, New Zealand and South Africa. The results of this review reveal a number of unique features and contrasting approaches. For example, section 1 of the U.S. *Sherman Act* is a broad provision with judge-made categories of *per se* prohibitions and no competitive effects test for hard-core cartel activity. For other types of arrangements examined under section 1 of the *Sherman Act*, the courts have applied a rule of reason analysis to determine if the prohibition is violated. In comparison, Article 81 of the European Community Treaty (the "EC Treaty") does not include any *per se* prohibitions, but relies on a broad prohibition and a system of individual or block exemptions that, in principle, could result in exemption for arrangements that would fall within the *per se* prohibitions implied under the *Sherman Act*. The Australian *Trade Practices Act* contains very specific *per se* prohibitions against price-fixing arrangements, while others rely upon broader and more general prohibitions, similar to Article 81 of the EC Treaty.

Section 45 of the *Competition Act* is unique in a number of respects in comparison to its foreign counterparts. For example, unlike the rule of reason analysis applied under section 1 of the *Sherman Act* and Article 81(3) of the EC Treaty, section 45 includes only a "partial" rule of reason. Further, unlike the *Sherman Act*, as interpreted and applied by the U.S. judiciary, there are no *per se* prohibitions under section 45. Various commentators have criticized section 45 on the basis that it is both underinclusive, because it can allow manifestly anti-competitive arrangements to escape condemnation, and overinclusive, because it subjects all horizontal arrangements to criminal prohibitions, even where these may potentially increase welfare. Also, the record of enforcement of section 45 in contested proceedings demonstrates that the failure to establish either that the arrangement unduly lessened competition or that the parties' intended that the agreement should have this effect, has become a significant obstacle to the effective enforcement of this provision against hard-core cartel behaviour.

In addressing this deficiency, reference may be made to the experience under section 1 of the *Sherman Act*, which demonstrates that a *per se* prohibition may provide an effective means of deterring and remedying hard-core, cartel behaviour. In particular, *per se* prohibitions are less costly to enforce and promise increased certainty and predictability. However, the U.S. experience also demonstrates that the significant disadvantage of a *per se* restriction is the inflexibility of such a provision, which may result in the prohibition of beneficial competitor collaborations.

To ensure that potentially pro-competitive arrangements are not inhibited, it is necessary to provide an exception for the limited class of agreements that, strictly speaking, violate these prohibitions, but

which are nevertheless desirable due to their pro-competitive benefits. One option is to adopt a rule of reason analysis. Under such an analysis, a court would have the flexibility required to differentiate pro-competitive, welfare enhancing collaborations from those which are not. However, the rule of reason may only be implemented gradually through successive cases and would not provide a practical solution to the Competition Bureau's enforcement concerns. Further, a rule of reason approach arguably leads to greater uncertainty and reduces the effectiveness of enforcement due to the need in each case to undertake a complex market assessment and analysis in order to determine whether the anti-competitive effects of the arrangement in question are outweighed by its pro-competitive benefits.

A notification, authorization or exemption mechanism avoids several of the shortcomings associated with the American approach to rule of reason analysis. Article 81(3) of the EC Treaty utilizes this approach, as do the Australian and New Zealand statutes. Like the American model, a full rule of reason analysis is applied. Enforcement authorities are given a broad discretion to immunize arrangements based on the particular circumstances of each case. In terms of process, it is the relevant enforcement agency, and not the courts (or an administrative tribunal), that has exclusive authority (at least at first instance) to authorize or exempt an agreement that would otherwise contravene a statutory prohibition. As a result, antitrust authorities are able to control the development of competition policy as it relates to competitors collaborations without the cost and delay associated with full administrative proceedings and without having to rely on the unpredictable direction of caselaw.

To be effective, such a notification and exemption regime should not, as a rule, exclude hard-core cartel behaviour and should not involve a cumbersome or lengthy procedure. In this regard, we have proposed two models: (i) a system whereby the Commissioner would be able to either grant an exemption or institute civil or criminal proceedings in respect of an existing or proposed arrangement for which an exemption has been sought (the "discretionary track model"); and (ii) an identical model, with two exceptions: first, only those arrangements that are notified prior to time they are entered into or given effect would be eligible for exemption; and second the Commissioner would not be authorized to institute proceedings under the criminal prohibition in respect of a notified arrangement (the "civil track model"). We believe that the latter approach is somewhat problematic because naked, hard-core cartel behaviour that is more effectively and more appropriately addressed through the application of a *per se* criminal prohibition, would be subject to a full-blown competitive effects analysis under the civil provision. Also, the effectiveness in terms of cost and time would be lost because a competitive effects analysis would be required even for an arrangement that otherwise clearly falls afoul of a *per se* prohibition. For all these reasons, we believe that the civil track model may reduce the efficiency and effectiveness with which the Commissioner would be able to "prosecute" naked, hard-core cartel behaviour. In addition, there is a risk under the civil track model that parties would utilize the exemption procedure to insulate hard-core, cartel behaviour from criminal prosecution. However, these weaknesses are significantly reduced by limiting notification to proposed arrangements that have not yet been implemented.

Under either model proposed in this report, agreements that do not violate the *per se* prohibitions would be examined under a civil provision. The establishment of a civil regime has a number of advantages, including harmonization of the treatment of mergers and strategic alliances. Further, the examination of potential anti-competitive effects and corresponding benefits, are matters in respect of which the specialized experience of the Tribunal and the lower standard of proof applied in Tribunal proceedings may be more appropriate.

We believe that a “dual track” approach strikes an appropriate balance between the competing objectives of, on the one hand, effective deterrence and punishment of hard-core cartel behaviour and, on the other hand, the need for a forum in which pro-competitive, welfare enhancing collaborations can be effectively differentiated from those which are not.

II. BACKGROUND

As part of the Competition Bureau's on-going legislative development initiative, we have been asked to consider potential amendments to section 45 of the *Competition Act*. Section 45 has been described as the "cornerstone" or "central provision" of Canada's competition laws. The harm to which section 45 is directed, such as price-fixing and other anti-competitive horizontal arrangements, has been characterized as the "antithesis of open competition" that "tear[s] at the economic fabric of our society". However, despite its central importance to the Canadian competition law regime, the conspiracy provision has remained largely unchanged since its introduction under the original 1889 *Act for the Prevention or Suppression of Trade*.

Notwithstanding its longevity, several commentators have made a case for amending section 45. As outlined below, recent studies and a number of high-profile prosecutions conducted in the United States, Canada, the European Community and elsewhere demonstrate that hard-core cartels are more prevalent and more harmful than previously believed. For example, in last two years alone, Canadian courts have levied over \$126 million in fines under section 45 in relation to hard-core cartel behaviour.

At the same time, however, there is a growing consensus on the need to encourage the pro-competitive benefits that may arise from certain strategic alliances or competitor collaborations. The Federal Trade Commission-Department of Justice *Antitrust Guidelines for Collaborations Among Competitors* and European Commission *Guidelines on the Applicability of Article 81 of the EC Treaty to Horizontal Cooperation* both recognize the substantial benefits that arise from such collaborations and the need to ensure that they are encouraged.

These commentators have also argued that section 45 permits neither effective prosecution of plainly anti-competitive arrangements nor effective differentiation between arrangements that raise social welfare by creating efficiencies that outweigh anti-competitive harm and those that do not. In this light, those advocating the amendment of section 45 suggest that the main objective of any changes must be to make section 45 more effective against arrangements which have the most significant potential to distort competition, such as hard-core cartels, while, at the same time, ensuring that pro-competitive strategic alliances are not discouraged.

In furtherance of this objective, significant amendments were proposed to section 45 of the *Competition Act* through Bill C-472.¹ Bill C-472 would have created a *per se* prohibition against certain types of arrangements, including price fixing, market allocation, restrictions on production and boycotts, which, at present, constitute offences under section 45 only where they are proved to "unduly prevent or lessen competition". Also, this Bill proposed the introduction of a companion

¹ *An Act to amend the Competition Act (conspiracy agreements and right to make private applications), the Competition Tribunal Act (costs and summary dispositions) and the Criminal Code as a consequence*, 2nd Session, 36th Parliament, 48-49 Elizabeth II, 1999-2000.

civil provision that would have allowed the Commissioner to seek remedial orders from the Tribunal in relation to all other arrangements, where these were shown to substantially lessen competition. Finally, Bill C-472 proposed the establishment of a clearance process for strategic alliances that would have allowed parties to obtain immunity from civil action.

In evaluating proposals, such as Bill C-472, it is useful to have regard to the approaches adopted in other jurisdictions. In this report, we provide a comparative review of the approach to competitor collaborations taken in a number of jurisdictions and propose legislation that incorporates elements of these models. Specifically, this report examines each of the following areas:

- (i) the need to encourage strategic alliances while deterring hard-core cartel behaviour;
- (ii) the need to harmonize the conspiracy provision with that of Canada's major trading partners;
- (iii) the approach to competitor collaborations in the European Community, Germany, Italy, the United States, Australia, New Zealand and South Africa and the respective merits and weaknesses of these regimes;
- (iv) the elements of the current section 45 and its weaknesses; and
- (v) proposed legislative models.

III. STRATEGIC ALLIANCES AND HARD-CORE CARTELS

As noted above, one of the main objectives of the proposed amendments to section 45 is to provide a flexible mechanism that will effectively deter hard-core cartel behaviour while ensuring that parties are not discouraged from engaging in potentially beneficial strategic alliances. The benefits flowing from such strategic alliances between competitors have been expressly recognized by a number of competition authorities. For example, the Federal Trade Commission-Department of Justice *Antitrust Guidelines for Collaborations Among Competitors* state:

In order to compete in modern markets, competitors sometimes need to collaborate. Competitive forces are driving firms toward complex collaborations to achieve goals such as expanding into foreign markets, funding expensive innovation efforts, and lowering production and other costs.

Such collaborations often are not only benign but procompetitive. Indeed, in the last two decades, the federal antitrust agencies have brought relatively few civil cases against competitor collaborations. Nevertheless, a perception that antitrust laws are

sceptical about agreements among actual or potential competitors may deter the development of procompetitive collaborations.²

The Joint Guidelines further recognize that consumers may benefit from competitor collaborations in a variety of ways; such as, where cooperation enables participants to offer goods or services that are cheaper, more valuable to consumers, or brought to market faster than would be possible absent cooperation. Further, such collaborations may allow participants to make more efficient use of their existing resources or derive other potential benefits not achievable without some form of collaboration. The Joint Guidelines state:

Efficiency gains from competitor collaborations often stem from combinations of different capabilities or resources. For example, one participant may have special technical expertise that usefully complements another participant's manufacturing process, allowing the latter participant to lower its production cost or improve the quality of its product. In other instances, a collaboration may facilitate the attainment of scale or scope economies beyond the reach of any single participant. For example, two firms may be able to combine their research or marketing activities to lower their cost of bringing their products to market, or reduce the time needed to develop and begin commercial sales of new products.³

A copy of the Joint Guidelines is attached at Schedule "T". The European Commission has also recognized that horizontal cooperation may be beneficial in certain circumstances:

[H]orizontal cooperation can lead to substantial economic benefits. Companies need to respond to increasing competitive pressure and a changing market place driven by globalization, the speed of technological progress and the generally more dynamic nature of markets. Cooperation can be a means to share risk, save costs, pool know-how and launch innovation faster. In particular for small and medium-sized enterprises cooperation is an important means to adapt to the changing market place.⁴

Nevertheless, despite the benefits that may result from strategic alliances, it is also clear that cooperation among competitors that constitutes "hard-core cartel" behaviour may result in significant distortions of competition. A recent Organisation for Economic Co-operation and Development ("OECD") report on hard core cartels defines these as "anticompetitive agreements by competitors to fix prices, restrict output, submit collusive tenders, or divide or share markets" and notes that such

² Federal Trade Commission and U.S. Department of Justice, *Antitrust Guidelines for Collaborations Among Competitors* (April, 2000) at page 1, Schedule I [hereinafter "Joint Guidelines"]

³ Joint Guidelines, *supra* note 2 at 6.

⁴ *Guidelines on the Applicability of Article 81 of the EC Treaty to Horizontal Cooperation* (2001/C3/02) at C 3/2. [hereinafter "Guidelines"]

agreements “are much more prevalent and harmful to the global economy than previously believed”.⁵ To address this concern, the OECD has urged each member country to:

...ensure that its competition laws effectively halt and deter hard core cartels. Members are urged to ensure that their sanctions and investigatory powers are adequate and that their exclusions and authorizations of what would otherwise be hard core cartels are both necessary and not broader than necessary to achieve their overriding policy objectives.⁶

Apart from hard core cartel behaviour, otherwise pro-competitive collaborations among competitors may facilitate tacit collusion through practices such as the exchange and disclosure of competitively sensitive information.

Given the significance of the potential benefits and detriments arising from collaboration among competitors, it is commonly recognized that any system directed at regulating such arrangements must be able to effectively deter and prohibit cartel behaviour, while remaining flexible enough so as not to dissuade competitors from entering into potentially beneficial strategic alliances. Further, statutory provisions must be clear and easy to enforce, facilitating consistent and inexpensive enforcement as well as providing a reasonable degree of predictability to those whose conduct may be subject to scrutiny.⁷ In our view, any reforms of the conspiracy provision must be consistent with these objectives. Bill C-472 and the proposed amendment described in the Terms of Reference address this objective through a dual-track approach whereby only the most harmful types of agreements would be subject to criminal sanctions, while other agreements would be assessed on the basis of a civil standard. The merits of this approach are discussed in further detail below.

IV. THE NEED FOR HARMONIZATION

One objective expressed during the public consultations concerning Bill C-472 as well as in the Terms of Reference, is the need to harmonize the conspiracy provision with those of the U.S., Europe and Canada’s other major trading partners. The approach to collaborations among competitors applied in many of these jurisdictions is discussed below. A number of advantages arise from convergence in the field of competition law. For example, it has been noted that: “a lack of convergence constitutes a trade barrier”, “convergence reduces compliance costs for companies conducting international business” and “convergence ends the need for states to apply their competition laws extraterritorially, and the corresponding need of target states to enact blocking or

⁵ Organisation for Economic Co-operation and Development, *Hard Core Cartels* (2000) at 6 and 11. [hereinafter *Cartels*]

⁶ *Ibid* at 14.

⁷ See Thomas W. Ross, “Proposals for a New Canadian Competition Law on Conspiracy” (1991) 36 *Antitrust Bulletin* 851 at 869-70.

claw-back statutes”.⁸ These advantages have prompted a number of attempts at harmonization of international competition laws, including: the *United Nations Conference on Trade and Development Restrictive Business Practices Code*, the *Organization for Economic Cooperation and Development 1994 Interim Report on Convergence of Competition Policies* and the *Draft International Antitrust Code*. These measures have to date been largely unsuccessful.⁹

As will be demonstrated from the discussion below, the difficulty in promoting “harmonization with Canada’s major trading partners” is the divergence in the models applied by many of Canada’s trading partners. For example, section 1 of the U.S. *Sherman Act*, as interpreted and applied by the U.S. judiciary, establishes *per se* prohibitions, without a competitive effects test, for hard-core cartel activity. For other types of arrangements examined under that section, a rule of reason analysis has been applied to determine if the prohibition against unreasonable restraints of trade is violated. In contrast, Article 81 of the European Community Treaty does not incorporate a *per se* approach relying instead upon a broad prohibition and a system of individual or block exemptions that, in principle, could provide an exemption for arrangements that would fall within the *per se* prohibitions implied under the *Sherman Act*. As a result, the objective of harmonization, particularly with Canada’s largest trading partners, necessarily raises the question as to which model Canada should harmonize its competition laws? Further, as discussed in greater detail below, full harmonization with Canada’s trading partners may not be desirable given that many of these foreign jurisdictions consider social or other non-economic considerations as relevant to the determination of whether collaborations are permissible.

V. ARTICLE 81 OF THE EUROPEAN COMMUNITY TREATY

(a) Introduction

Article 81 (formerly Article 85) of the Treaty on the European Union (the “EC Treaty”) prohibits as incompatible with the common market a broad range of anti-competitive agreements, decisions and practices. Article 81(1) applies to “agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Members States and which have as their object or effect the prevention, restriction or distortion of competition...”. Agreements caught under Article 81(1) are automatically void by virtue of Article 81(2), unless exempted under Article 81(3). In addition, violations of Article 81 may result in the imposition of significant fines of up to 10% of the previous year’s turnover of the firms involved. The full text of Article 81 is attached at Schedule “II”.

⁸ Daniel Steiner, “The International Convergence of Competition Laws” (1997), 24 *Man. L.J.* 577 at 581.

⁹ *Ibid* at 578.

(b) Application of Article 81

In determining whether an agreement, decision or practice violates Article 81(1), there are two requirements that must be satisfied:

- the prohibited agreement, decision or practice must be shown to be liable to affect trade between members states; and
- the agreements, decisions or practices must have as their object or effect the prevention, restriction or distortion of competition within the common market.

As noted above, an agreement may be prohibited under Article 81 if it has either the object or effect of preventing, restricting or distorting competition within the common market. As such, where parties enter into an arrangement with the object of restricting or distorting competition, such conduct is prohibited under Article 81(1) irrespective of its effect on competition. Conversely, agreements or arrangements which have the effect of distorting competition are prohibited regardless of the parties' intentions. This approach was confirmed by the European Court of Justice in *Société Technique Minière v. Maschinenbau Ulm GmbH*¹⁰ where the Court held that the words "object or effect" must be read disjunctively such that it was necessary to first consider what the purpose of an agreement was and if it was clear that the object of the agreement was to harm competition, there was no need to consider the effect of the agreement. The approach used to determine the "object" and "effect" of an arrangement for the purpose of Article 81(1) is described below.

(c) Object of the Agreement

The European Court of Justice has confirmed that the term "object" does not mean the subjective intent of the parties. Rather, the object of the agreement is the purpose of the agreement as may be determined from the words of the agreement itself, considered in the context in which the agreement would be applied.¹¹ An interesting consequence of this interpretation is the potential application of a *quasi per se* approach to Article 81(1) for certain agreements which are obviously restrictive of competition, such as naked price-fixing arrangements. As the Commission states in its recently published *Guidelines on the Applicability of Article 81 of the EC Treaty to Horizontal Cooperation*:¹²

In some cases the nature of a cooperation indicates from the outset the applicability of Article 81(1). This is the case for agreements that have as their object a restriction of competition by means of price fixing, output limitation or sharing of markets or

¹⁰ [1966] ECR 235, [1966] CMLR 357 (ECJ). [hereinafter *Maschinenbau Ulm*]

¹¹ *Compagnie Royale Asturienne des Mines SA and Rheinzink GmbH v. Commission*, [1984] ECR 1679. [1985] 1 CMLR 688 at paras. 25-26.

¹² *Guidelines*, *supra* note 4.

customers. These agreements are presumed to have negative market effects. **It is therefore not necessary to examine their actual effects on competition and the market in order to establish that they fall within Article 81(1).**

...

Another category of agreements can be assessed from the outset as normally falling under Article 81(1). This concerns cooperation agreements that have the object to restrict competition by means of price fixing, output limitation or sharing of markets or customers. These restrictions are considered to be the most harmful, because they directly interfere with the outcome of the competitive process. Price fixing and output limitation directly lead to customers paying higher prices or not receiving the desired quantities. The sharing of markets or customers reduces the choice available to customers and therefore also leads to higher prices or reduced output. **It can therefore be presumed that these restrictions have negative market effects. They are therefore almost always prohibited.**¹³ [emphasis added]

For these types of agreements, the Commission may simply assume that their object is to reduce competition and that, therefore, there is no need to have regard to the actual effect on competition of the agreement. In its *10th Annual Report*, the Commission expressed the view that price-fixing agreements fall into “the category of manifest infringements under Article [81(1)] which it is always impossible to exempt under Article [81(3)] because of the total lack of benefit to the consumer”.¹⁴ However, despite this broad statement by the Commission, it would be incorrect to suggest that Article 81 includes a full *per se* prohibition, even against such price fixing arrangements. Unlike the *per se* prohibitions implied under section 1 of the *Sherman Act*, an agreement that is caught under Article 81(1) (even a naked price-fixing arrangement) may qualify for an exemption under Article 81(3) based on its pro-competitive benefits. In fact, the Commission has been prepared to accept restrictions on pricing where these were considered essential in the circumstances and did not lead to an elimination of competition.¹⁵ The Court of First Instance described the approach to Article 81 in the case of *European Night Services v. EC Commission*:

Before any examination of the parties’ arguments as to whether the Commission’s analysis as regards restrictions of competition was correct, it must be borne in mind that in assessing an agreement under Article 81(1) of the Treaty, account should be taken of the actual conditions in which it functions, in particular the economic context in which the undertakings operate, the products or services covered by the agreement and the actual structure of the market concerned, . . . **unless it is an agreement containing obvious restrictions of competition such as price-fixing,**

¹³ *Ibid* at paras. 18 and 25.

¹⁴ Available online at <http://europa.eu.int/comm/competition/publications/publications/#ports>.

¹⁵ For example, through Regulation 4056/86, the Commission implemented a block exemption for certain liner conference agreements. See also *Eurocheque: Helsinki Agreement*, OJ [1992] 95/50.

market-sharing or the control of outlets . . . In the latter case, such restrictions may be weighed against their claimed pro-competitive effects only in the context of Article 81(3) of the Treaty, with a view to granting an exemption from the prohibition in Article 81(1).¹⁶

(d) Effect of the Agreement

Where the object of the arrangement cannot be said to restrict competition, an examination of the effect of the arrangement becomes crucial. This requires a full analysis of the market in which the arrangement will be implemented. In particular, as the Court of First Instance held in the above passage from *European Night Services*, account must be taken of “the economic context in which the undertakings operate, the products or services covered by the agreement and the actual structure of the market concerned”. Further, the Court in that case emphasized that the prescribed examination of the conditions of competition had to be based not only on existing competition between undertakings currently in the relevant market, but also on potential competition. This was necessary “in order to ascertain whether, in the light of the structure of the market and the economic and legal context within which it functions, there are real and concrete possibilities for the undertakings concerned to compete among themselves or for a new competitor to penetrate the relevant market and compete with the undertakings already established”.¹⁷

(e) Guidelines on the Applicability of Article 81 to Horizontal Cooperation

As noted above, the Commission has issued guidelines on horizontal co-operation which describe the Commission’s analytical framework for the examination of many forms of horizontal arrangements.¹⁸ In the Guidelines, the Commission recognizes that horizontal cooperation may lead to competition problems where, for example, parties agree to fix prices or output, to share markets or if cooperation enables the parties to maintain, gain or increase market power. However, the Commission also recognizes that most horizontal co-operation agreements do not have as their object a restriction of competition and therefore, regard must be had to the effect of the agreement within its economic context.¹⁹

The Commission emphasizes in the Guidelines that arrangements between parties which do not have a significant share of the relevant market are unlikely to have a restrictive effect.²⁰ In addition to examining market power, the Guidelines state that the Commission will examine the level of

¹⁶ [1998] ECR II - 3141, [1998] 5 CMLR 138, at para. 136 (ECJ).[hereinafter “*European Night Services*”] [emphasis added]

¹⁷ *Ibid* at para. 137.

¹⁸ *Guidelines, supra* note 5.

¹⁹ *Ibid* at para. 19.

²⁰ *Ibid* at para. 20.

concentration within the relevant market, barriers and the likelihood of market entry, the countervailing power of buyer/suppliers and the nature of the products.²¹

The Guidelines also contain specific provisions describing the treatment of agreements that may not be prohibited under Article 81, including: agreements on research and development,²² joint production agreements,²³ specialization agreements (*i.e.*, where parties agree unilaterally or reciprocally to cease production of a product and to purchase it from another party),²⁴ subcontracting agreements (*i.e.*, where one party entrusts to another party the production of a product),²⁵ joint purchasing agreements,²⁶ agreements on standards,²⁷ environmental agreements²⁸ and others. A copy of the Guidelines is attached at Schedule “III”.

(f) Article 81 and the Rule of Reason

Despite these attempts to limit the application of Article 81, the Commission has often been criticized for adopting an extremely broad interpretation of Article 81(1).²⁹ Some critics suggest that much of the analysis of the pro-competitive benefits of an arrangement carried out under Article 81(3) should be conducted under Article 81(1) in deciding whether the agreement is in fact restrictive of competition.³⁰ However, as discussed below, the exemption process under Article 81(3) results in significant delay and expense to the parties. Consequently, a broad interpretation of Article 81(1) may have the result of discouraging parties from engaging in potentially beneficial arrangements.

The disadvantages of a liberal interpretation of Article 81(1) has prompted some critics to suggest that the Commission adopt a “rule of reason” approach to Article 81(1).³¹ As discussed more fully

²¹ *Ibid* at para. 30.

²² *Ibid* at section 2.

²³ *Ibid* at section 3.

²⁴ *Ibid* at para. 79.

²⁵ *Ibid* at para. 80.

²⁶ *Ibid* at section 4.

²⁷ *Ibid* at section 6.

²⁸ *Ibid* at section 7.

²⁹ *See, e.g.*, Peter Freeman and Richard Whish (ed.), *Butterworths Competition Law* (2000) at para. 188 [hereinafter *Butterworths*]; A. Jones, *EC Competition Law* (2001) at paras. 1-065 ; Alexander Schaub, “EC Competition System - Proposals for Reform”, (1999) 22 *Fordham Int’l L.J.* 853 at 880.

³⁰ *See* Jones, *supra* note 29 at para. 1-068.

³¹ Schaub, *supra* note 29.

in the section below describing the *Sherman Act*, a rule of reason approach requires a balancing of the pro-competitive aspects of an agreement against its anti-competitive effect. The result of adopting the foregoing recommendation would be that fewer agreements would be caught under Article 81(1).

There is some limited support within the European Community caselaw for the adoption of a “rule of reason” analysis under Article 81(1). For example, in *Maschinenbau Ulm* the European Court of Justice held that a term conferring exclusivity on a distributor might not infringe Article 81(1) where it was a vital element in the distributor’s decision to market a particular supplier’s goods. Further, Advocate-General Roemer stated as follows in *Etablissements Consten and Grundig v. EEC Commission*:

Next, I have already indicated in another case that American law (the “White Motor Case”) requires for situations of the type before us a comprehensive examination of their economic repercussions. Clearly I do not mean to say that we should imitate in all respects the principles of American procedure in the field of cartels. This would not in fact be justified by reason of the essential differences between the systems (prohibition *per se* in American law; possibility of exemption under Article 85(3) of the EEC Treaty). But such a reference is useful nevertheless in so far as it shows that in respect of Article 85(1) also it is not possible to dispense with observing the market *in concreto*. It seems to me wrong to have regard to such observation only for the application of paragraph (3) of Article 85, because that paragraph requires an examination from other points of view which are special and different. But in particular (as is shown by *Société Technique Minière v Maschinenbau Ulm GmbH*) **it would be artificial to apply Article 85(1), on the basis of purely theoretical considerations, to situations which upon closer inspection would reveal no appreciable adverse effects on competition, in order then to grant exemption on the basis of Article 85(3).**³²

(g) Ancillary Restraints

Rather than adopting a rule of reason approach, others suggest that the Commission should apply the doctrine of “ancillary restraints” more liberally. Pursuant to this doctrine, restrictions on competition are held to fall outside Article 81(1) where they are objectively necessary for the performance of a specific type of pro-competitive agreement or are essential to induce a party to a contract to take on the commercial risk inherent in the agreement.³³

A common example of an ancillary restraint is a restrictive covenant found in an agreement regarding the sale of a business. Both the European Court of Justice and the Commission have

³² [1966] ECR 299 at 358 (ECJ). [emphasis added]

³³ Schaub, *supra* note 28.

accepted that Article 81(1) does not apply to non-competition clauses and other restrictions on the commercial freedom of undertakings when these restrictions are imposed in the context of the sale of a business. For example, in *Reuter/BASF* the Commission held as follows:

It is recognized that it may be necessary in certain cases to provide safeguards to ensure the effective performance of an agreement. These may take the form of a contractual non-competition clause in cases where not only the material assets of a undertaking but also its commercial goodwill, including relations with customers, are to be transferred to the purchaser. In such cases it is essential to prevent a seller from re-acquiring his old customers either directly or indirectly through cooperation with the purchaser's competitors in the period following the transfer. Compliance by the seller with such a non-competition clause means no more than that he must respect his obligation under the agreement to transfer full value of the undertaking. Application of Article 85(1) to such a non-competition clause in an agreement can be excluded in such cases, since it would make more difficult or even impossible transactions which are generally recognized as legitimate.³⁴

Other forms of ancillary restraints accepted by the Commission include provisions protecting a franchisor's rights,³⁵ restrictions on licensees of patented products³⁶ and provisions relating to products requiring an exclusive and selective distribution arrangement.³⁷

In 1990, the Commission issued a Notice regarding the ancillary restraints doctrine in the context of the review of mergers. The Notice defined the eligible restraints as follows:

The "restrictions" meant are those agreed on between the parties to the concentration which limit their own freedom of action in the market. They do not include restrictions to the detriment of third parties. If such restrictions are the inevitable consequence of the concentration itself, they must be assessed together with it under the provisions of Article 2 of the Regulation. If, on the contrary, such restrictive effects on third parties are separable from the concentration they may, if appropriate, be the subject of an assessment of compatibility with Articles 85 and 86 of the EEC Treaty.³⁸

Further, sections 5 and 6 of the Notice describe the notion that these restraints must be "necessary":

³⁴ O.J. L54/40, [1976] 2 C.M.L.R. at D56-57.

³⁵ *Pronuptia*, [1986] E.C.R. 353, [1986] 1 C.M.L.R. 414.

³⁶ *Burroughs/Geha*, O.J. L13/53, [1972] 2 C.M.L.R. D127.

³⁷ Commission Decision No. 85/616/EEC. [1988] 4 C.M.L.R. 461.

³⁸ *Notice on Restrictions Ancillary to Concentrations*, OJ [1990] C203/5 at s. 3.

The restrictions must likewise be “necessary to the implementation of the concentration”, which means that in their absence the concentration could not be implemented or could only be implemented under more uncertain conditions, at substantially higher cost, over an appreciably longer period or with considerably less probability of success. This must be judged as an objective basis.

The question of whether a restriction meets those conditions cannot be answered in general terms. In particular as concerns the necessity of the restriction, it is proper not only to take account of its nature, but equally to ensure, in applying the rule of proportionality, that its duration and subject matter, and geographic field of application, do not exceed what the implementation of the concentration reasonably requires. If alternatives are available for the attainment of the legitimate aim pursued, the undertakings must choose the one which is objectively the least restrictive of competition.³⁹

(h) The *De Minimus* Rule

To further reduce the breadth of Article 81(1), the Commission has adopted a *de minimus* rule that exempts agreements which do not have a significant impact on competition.⁴⁰ The *Notice on Agreements of Minor Importance Which do not Fall Within the Meaning of Article 85(1) of the Treaty*⁴¹ provides guidance in respect of the application of the *de minimus* doctrine. Pursuant to this doctrine, agreements which affect competition may nevertheless be considered to fall outside of Article 81 because they do not have an appreciable impact either on competition or on inter-state trade. In the Commission’s opinion, agreements whose effects on trade between Member States or on competition are negligible do not fall under the prohibition on restrictive agreements. Only those agreements which have an appreciable impact on market conditions are prohibited.

The Notice also provides guidance on the nature of agreements that may fall outside of Article 81(1) based upon the aggregate market share of the parties. Specifically, the Notice indicates that the Commission will not apply Article 81 in respect of arrangements between undertakings engaged in the production or distribution of goods or in the provision of services where the aggregate market share held by all of the participating undertakings does not exceed, in any of the relevant markets:

- (a) a 5% market share threshold, where the agreement is between undertakings operating at the same level of production (*i.e.*, horizontal agreements); or

³⁹ *Ibid* at ss. 5-6.

⁴⁰ The *de minimus* doctrine was formulated by the European Court of Justice in *Volk v. Vervaecke*, [1969] ECR 295, [1969] CMLR 273.

⁴¹ OJ [1997] C 372/13.

- (b) a 10% market share threshold, where the agreement is made between undertakings operating at different economic levels (*i.e.*, vertical agreements).⁴²

However, both horizontal and vertical agreements which have the effect of fixing prices, limiting production or sales, or sharing markets or sources of supply or, in the case of vertical agreements, conferring territorial protection on the participating undertakings or third party undertakings may not benefit from this exclusion regardless of the market share of the participants.⁴³

The Commission Notice provides an additional exception for agreements between small and medium sized businesses, defined as undertakings with gross revenues less than 40 million ECU that employ less than 250 people. This exception applies irrespective of the market share of the parties, except that the Commission has reserved the right to seek a remedy where the agreements involve a large number of smaller undertakings such that the cumulative effect may be unduly restrictive.⁴⁴

(i) The Exemption Under Article 81(3)

Despite the Commission Notices described above, and the application of the ancillary restraints doctrine, a large number of agreements continue to fall within the scope of the prohibition in Article 81(1). As a consequence, the focus of the inquiry under Article 81 is typically on whether the agreement may be exempted pursuant to Article 81(3). Article 81(3) allows the Commission to declare Article 81(1) inapplicable in various situations. In general, Article 81(3) provides an exemption where the impugned agreement:

- (a) contributes to:
 - (i) improving production or distribution, or
 - (ii) promoting technical or economic progress,
 - (iii) while allowing consumers a fair share of the resulting benefit;
 but
- (b) does not:
 - (i) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; or

⁴² *Ibid* at para. 9.

⁴³ *Ibid* at para. 11.

⁴⁴ *Ibid* at para. 19.

- (ii) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

Overall, Article 81(3) is an extremely flexible provision that permits the Commission to exercise its discretion in determining whether an agreement is permissible.

In terms of procedure, an exemption may be obtained in two ways: the parties may submit a “notification” requesting an individual exemption for a particular agreement; or, the parties may draft the agreement in a manner that will be exempted pursuant to one of the “block exemptions” issued by the Commission. These options are discussed below.

The procedure governing individual exemptions under Article 81(3) is found in Regulation 17/62.⁴⁵ Pursuant to this Regulation, parties may apply for an exemption under Article 81(3) by submitting a notification to the Commission. While the Commission, national courts and national authorities can all apply Article 81(1), Regulation 17 stipulates that the power to grant exemptions under Article 81(3) is exclusively the Commission’s. As such, Regulation 17 establishes the Commission as the centralized authorization body for the exemption of practices or agreements that infringe Article 81(1).

One of the principal advantages to the parties of submitting a notification is that it has the effect of “stopping the clock” for the purpose of the imposition of a fine for any infringement. Pursuant to Article 15(5) of Regulation 17, the Commission may not impose a fine for the period between the date of notification and the final decision by the Commission. To avoid abuse of this provisional immunity, the Commission retains the discretion to impose a fine retrospectively where it is clear that the agreement infringes Article 81(1). As such, a notification in respect of a price-fixing agreement or other restrictive arrangements is unlikely to trigger immunity from fines.

Unfortunately, the notification scheme is prone to abuse by parties wishing to delay or hinder litigation before the national courts under Article 81. As noted above, national courts have the jurisdiction to apply Article 81(1), but may not grant exemptions under Article 81(3). In litigation before national courts where it is alleged that an agreement violates Article 81(1), the court may decline to hear the matter pending the determination of whether the agreement is exempt under Article 81(3). As a result, defendants in proceedings before the national courts may submit notifications solely with a view to delay proceedings before the national courts.⁴⁶

The vast majority of notifications seeking an individual exemption are resolved informally through the use of “comfort letters”.⁴⁷ Similar to “no action” letters issued by the Canadian Competition

⁴⁵ Council Regulation (EEC) No 17/62, OJ Sp Ed [1962] No 204/62.

⁴⁶ *White Paper on Modernisation of the Rules Implementing Articles 85 and 86 of the EC Treaty* (1999) at 4. [hereinafter *White Paper on Modernisation*]

⁴⁷ *Ibid* at para. 34.

Bureau, these letters indicate that the file has been closed, but without a formal decision having been made. In 1999, of the 582 cases closed, only 68 were closed by formal decisions, as compared with 514 cases closed by various informal means.⁴⁸

An alternative to the individual exemptions described above is to draft the agreement in a manner that will take advantage of the block exemptions issued by the Commission. Agreements which fall within the scope of the block exemptions do not need to be notified, and are valid without authorization from the Commission. In general, block exemptions are structured in the following manner:

- (a) clarification of the categories of agreements or practices to which the exemption relates;
- (b) restrictions which will often be acceptable (often referred to as the “white list”); and
- (c) restrictions which will take the agreement outside of the scope of the exemption (often referred to as the “black list”).⁴⁹

Such exemptions may be withdrawn by the Commission and are limited in duration. A further alternative is available under certain block exemptions which provide an “opposition procedure”. Pursuant to this procedure, agreements that fall outside of the relevant block exemption may be notified individually. If the Commission fails to oppose the agreement within a specified period (usually between 4 to 6 months), the agreement is deemed to be exempted.⁵⁰

(j) Critique of European Community Treaty System

As noted above, the main criticism of the EC Treaty system is that due to the Commission’s broad interpretation of Article 81(1), agreements with little or no risk of being economically anti-competitive are caught by Article 81(1). Further, Article 81(2) deems all forms of agreements which fall within the broad scope of Article 81(1) void and unenforceable, unless the agreement is subject to an exemption.⁵¹ As a result, parties are required to submit a notification to secure an individual exemption or are required to “fit” the arrangement within the scope of a block exemption. More generally, the result is that companies are required to notify a large number of agreements that do

⁴⁸ European Commission, *XXIXth Report on Competition Policy* (1999) available online at: http://europa.eu.int/comm/competition/annual_reports/1999/en.pdf at 20. [hereinafter *Report*]

⁴⁹ *Butterworths, supra* note 29 at I/165.

⁵⁰ *Ibid* at I/179.

⁵¹ Mario Siragusa, “The Millenium Approaches: Rethinking Article 85 and the Problems and Challenges in the Design and Enforcement of the EC Competition Rules” (1998) 21 *Fordham Int’l L. J.* 650 at 660.

not raise serious competition issues. Such notifications are also encouraged by the availability of provisional immunity from fines.

The significant number of notifications imposes a large administrative burden on the Commission. For example, in 1999 alone, the Commission received 162 notifications.⁵² This administrative burden is exacerbated by the fact that pursuant to Regulation 17/62, only the Commission has the power to grant exemptions under Article 81(3). Recognizing these deficiencies, the Commission published a White Paper⁵³ in 1999 discussing modernization of the rules implementing Articles 81 and 82 and EC Treaty. Comments submitted during the public consultation surrounding the White Paper indicated almost universal dissatisfaction with the current regime. A copy of the White Paper is attached at Schedule “IV”.

Among the proposals considered by the legislators was the suggestion to incorporate a rule of reason into Article 81(1), in order to increase the number of arrangements that would be permitted, without the necessity of resorting to an exemption under Article 81(3).⁵⁴ Supporters of this approach note that Article 81(1) is drafted in a manner similar to the broad language found in section 1 of the *Sherman Act* and that, therefore, a rule of reason may be implied without the necessity of redrafting the existing legislation.⁵⁵

However, some commentators have argued against incorporating a U.S. rule of reason into EC law on the basis that it is problematic and difficult to define.⁵⁶ As the Commission notes in its White Paper, the importation of a rule of reason analysis into Article 81(1) would effectively nullify Article 81(3) of the Treaty.⁵⁷ In addition, the Commission expressed the concern that the substance of such an approach would have to be developed through caselaw, in a manner similar to the gradual definition and development of the rule of reason in U.S. jurisprudence. It stated:

It would moreover be dangerous if modernisation of the competition rules were to be based on developments in decision-making practice, subject to such developments being upheld by the Community Courts. Any such approach would mean that modernisation was contingent upon the cases submitted to the Commission and could take many years. Lastly, this option would run the risk of diverting Article 85(3) [now Art. 81(3)] from its purpose, which is to provide a legal framework for the

⁵² *Report*, *supra* note 48 at 20.

⁵³ *White Paper on Modernisation*, *supra* note 46.

⁵⁴ Jones, *supra* note 29 at paras. 1-068 to 1-070; Schaub, *supra* note 29 at 880

⁵⁵ Siragusa, *supra* note 51 at 664-65.

⁵⁶ Jones, *supra* note 29 at para. 1-071; *Butterworths*, *supra* note 29 at I/99-I/103;

⁵⁷ *White Paper on Modernisation*, *supra* note 46 at para. 57.

economic assessment of restrictive practices, not to allow application of competition rules to be set aside because of political considerations.⁵⁸

These concerns have been echoed by others. For example, in “EC Competition System - Proposals for Reform”, Alexander Schaub, the then Director-General of DGIV states:

Another drawback is that a switch to a rule of reason approach, which the Commission could only implement gradually, i.e., step by step, would probably be too slow to provide effective remedies for the weaknesses of the present system. Moreover, in such a process, the Commission would have limited steering powers, as the evolution of this approach would depend on confirmation by the Court of Justice, which is difficult to predict.

Further, Professor Alison Jones states:

A rule of reason approach to Article 81(1) arguably leads to greater uncertainty for parties to agreements who must, in every case, have to undertake complex market assessments and analyses in order to determine whether or not their agreement could be said to have as its object or effect the prevention, restriction or distortion of competition. Further, Article 81(1) is directly effective and can therefore be applied by national courts or, in some Member States, national competition authorities. It is not necessarily the case that national courts or competition authorities are suitable for the sophisticated analysis of agreements under Article 81(1) that some critics call for, and there must at least be a danger that the analysis might vary from one Member State to another.⁵⁹

Due to the unwillingness to implement a rule of reason analysis in Article 81(1), EC legislators have been faced with two fundamentally different options for reform: the adoption of a modified authorization system (e.g., an altered system of notification); or, a directly applicable exception (i.e., an exemption that is applicable without prior notification or administrative authorization).

In examining whether the notification and authorization regime should be abolished, commentators identified at least five disadvantages to the notification regime as it is currently applied under Article 81(3):

- (i) due to the high number of notifications received by the Commission and the significant time required to review such notifications, the Commission is unable to focus its limited resources on dealing with the most significant restrictions on competition;

⁵⁸ *Ibid.*

⁵⁹ Jones, *supra* note 29 at para. 1-071.

- (ii) experience has indicated that notifications do not reveal serious threats to competition such as cartels, which are almost never notified, and in fact, dealing with notifications diverts resources away from investigating such conduct;
- (iii) due to the administrative burden resulting from such notifications, the Commission is unable to respond in a timely manner to the parties;
- (iv) the costs of preparing the notifications required are significant and may discourage parties from engaging in potentially beneficial alliances or arrangements, particularly where the parties are small or medium sized enterprises; and
- (v) parties may improperly rely upon the notification system to prevent or delay litigation under Article 81 before the national courts.⁶⁰

The Commission itself has expressly recognized the above deficiencies of the notification regime. In a recent proposal to amend Regulation 17, the Commission stated:

The Commission's monopoly on the application of Article 81(3) is a significant obstacle to the effective application of the rules by national competition authorities and courts. ... Furthermore, the notification regime no longer constitutes an effective tool for the protection of competition. It only rarely reveals cases that pose a real threat to competition. In fact, the notification system prevents the Commission's resources from being used for the detection and punishment of serious infringements.⁶¹

In fact, in the 40 years since the enactment of Regulation 17, there have been only 9 decisions in which a notified agreement was prohibited without a complaint being lodged against it. The Commission has also recognized the burdens of the notification system on industry, particularly small- and medium-sized enterprises:

The second deficiency of the current system is that it imposes an excessive burden on industry by increasing compliance costs and preventing companies from enforcing their agreements without notifying them to the Commission even if they fulfil the conditions of Article 81(3). This is particularly detrimental to [small and medium sized enterprises] for whom the cost of notification and in the absence of notification,

⁶⁰ *White Paper on Modernisation*, *supra* note 46 at para. 44; *see also White Paper on the Reform of Regulation 17 - Summary of the Observations* (DG Document 29.02.2000) [hereinafter "*White Paper on Reform*"]; Siragus, *supra* note 51 at. 657-64.

⁶¹ *Proposal for a Council Regulation on the Implementation of the Rules on Competition Laid Down in Articles 81 and 82 of the Treaty and Amending Regulations (EEC) No 1017/68, (EEC) No. 2988/74, (EEC) No. 4056/86 and (EEC) No 3975/87, 2000/0243 (CNS) (27.9.2000) at 2.*

the difficulty of enforcing their agreements can constitute a competitive disadvantage compared with larger firms.⁶²

On the other hand, the notification regime offers a number of advantages, including:

- (i) it has enabled the Commission to build a coherent body of precedent decisions through the issuance of formal determinations granting or denying exemptions;
- (ii) the centralized authorization system has permitted the Commission to ensure that competition rules have been applied consistently across the EC;
- (iii) a determination by the Commission as to whether an exemption is available provides legal certainty for the parties; and
- (iv) the notification and authorization regime is extremely flexible and, in principle, permits the Commission to exempt agreements that are *prima facie* violations of Article 81(1).

Notwithstanding these advantages, the Commission has expressly supported the abolishment of the notification and authorization regime currently applied in Article 81(3). If the proposed Council Regulation implementing Articles 81 and 82 of the Treaty is accepted, a new enforcement regime will be implemented under which the Commission will no longer have the exclusive authority to apply Article 81(3). Rather, both the prohibition set out in Article 81(1) and the exception contained in Article 81(3) would be directly applied by not only the Commission, but also by national courts and national competition authorities. The proposed system is anticipated to increase the effective enforcement of the Community competition rules by allowing national competition authorities and courts to apply Articles 81 and 82 in their entirety.⁶³ Furthermore, by abolishing the notification system, the Commission will be able to focus on complaints and on proceedings that are instituted on its own initiative. This is to be coupled with increased powers of investigation for Commission officials.⁶⁴

A concern expressed during the consultation process for the White Paper was whether the abolition of the notification regime would destroy the legal certainty that exists under the current notification and authorization regime. Under the proposed Council Regulation, all agreements that satisfy the conditions of Article 81(3) would be considered valid and enforceable, without the necessity of any authorization from the Commission or a court. However, even though the applicable criteria would be established through prior decisions or administrative guidelines, it is possible that parties would experience difficulty in determining whether particular arrangements fall within Article 81. As noted

⁶² *Ibid.*

⁶³ *See ibid* at 6.

⁶⁴ *See ibid* at 7.

in paragraph 77 of the White Paper: “undertakings would have to make their own assessment of the compatibility of their restrictive practices with Community law, in the light of the legislation in force and the case-law”.

The lack of certainty resulting from the abolishment of the notification and authorization regime was described by Professor Whish as follows:

The White Paper proposals are radical. The willingness of the Commission to volunteer the abandonment of its monopoly over the granting of exemptions under Regulation 17/62 is in some respects the most radical proposition. However, for companies and their advisers the ending of the notification and authorisation system may be the most important feature of what is proposed. Under the existing system, the problem has been that, for most agreements, an individual exemption required pre-notification to the Commission, and **yet the Commission did not have the staff or resources to deal with the large number of agreements it received.** The system is flawed, but at least it offers the possibility of notification to those that wish to notify. Under the proposals in the White Paper, the Commission will scrap the system of notification altogether. It will not be possible to notify at all: the safe-haven, or fairly safe haven, of sending in a Form A/B to the Commission and relying on immunity from being fined will no longer be available.

Assuming that the idea of abandoning notification prevails, this will present significant challenges to companies and their advisers. The position will be a lot closer to that in the US, where companies have to be more self-reliant.⁶⁵

To attempt to address these concerns, the Commission has also expressed its commitment to introduce block exemptions and guidelines that will assist in the enforcement of the rules. In addition, the Commission has noted that with a larger number of decision-makers applying Article 81(3), case-law and practice on the interpretation of this Article will develop more rapidly.

(k) Other European Community Jurisdictions

The above provisions are similar to the legislation found throughout the EC and applied by various national authorities. In Germany, the *Act Against Restraints of Competition*⁶⁶ contains a broad prohibition in section 1 that is similar to Article 81(1). Section 1 provides:

Agreements between competing undertakings, decisions by associations of undertakings and concerted practices which have as their object or effect the prevention, restriction or distortion of competition shall be prohibited.

⁶⁵ Richard Whish, *EC Competition Law* (2001) at paras. 2-095 to 2-090. [emphasis added]

⁶⁶ GWB-Übersetzung, Endfassung 09.03.1999 BkarsA.

Unlike the EC Treaty however, the German legislation identifies a number of potential exemptions to the general prohibition set out above, including: agreements whose subject matter is merely the uniform application of standards or types, and agreements whose subject matter is the uniform application of general terms of business, delivery and payment.

For example, Section 3 provides an exemption for “specialisation cartels”:

Agreements and decisions whose subject matter is the rationalisation of economic activities through specialisation may be exempted from the prohibition under Section 1 provided the restraint of competition does not lead to the creation or strengthening of a dominant position.

Section 4 contains an exemption for agreements between small or medium sized businesses for the rationalization of economic activities provided that competition in the market is not substantially impaired and the agreement serves to improve the competitiveness of the small or medium sized enterprises.

In addition to further exemptions for “rationalisation cartels” and “structural crisis cartels”, section 7 provides the following general exemption:

Agreements and decisions which contribute to improving the development, production, distribution, procurement, taking back or disposal of goods or services, while allowing consumers a fair share of the resulting benefit, may be exempted from the prohibition under Section 1 provided the improvement cannot be achieved otherwise by the participating undertakings and is of sufficient importance when compared with the restraint of competition connected with it, and the restraint of competition does not result in the creation or strengthening of a dominant position.

Agreements and decisions whose subject matter is the rationalisation of economic activities through specialisation or in some other way, the joint purchasing of goods or the joint procurement of commercial services, or the uniform application of terms and conditions, may be exempted from the prohibition under Section 1...

Similar to the EC regime, to secure an exemption, the parties to the agreement are required to submit a notification to the cartel authority. Also, like the opposition procedure found in the EC regime, certain types of agreements shall be “exempt from the prohibition under section 1 and shall take effect unless the cartel authority objects within a period of three months from receipt of the notification”. For other types of agreements, such as structural crisis cartels, the exemption may only be granted through a decision of the cartel authority.

As a further example of European Community legislation, reference may be made to the Italian anti-trust regime. Article 2 of *Law No. 287 of October 10, 1990*⁶⁷ prohibits agreements restricting freedom of competition in a manner similar to Article 81(1) of the EC Treaty:

1. The following shall be regarded as agreements: accords and/or concerted practices between undertakings, and any decisions, even if adopted pursuant to their Articles or Bylaws, taken by consortia, associations of undertakings and other similar entities.
2. Agreements are prohibited between undertakings which have as their object or effect appreciable prevention, restriction or distortion of competition within the national market or within a substantial part of it, including those that:
 - (a) directly or indirectly fix purchase or selling prices or other contractual conditions;
 - (b) limit or restrict production, market outlets or market access, investment, technical development or technological progress;
 - (c) share markets or sources of supply;
 - (d) apply to other trading partners objectively dissimilar conditions for equivalent transactions, thereby placing them at an unjustifiable competitive disadvantage;
 - (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.
3. Prohibited agreements are null and void.

Similarly, the exemptions contained in Article 4 correspond to the exemptions found in Article 81(3):

1. The Authority may authorize, for a limited period, agreements or categories of agreements prohibited under section 2 which have the effect of improving the conditions of supply in the market, leading to substantial benefits for consumers. Such improvements shall be identified taking also into account the need to guarantee the undertakings the necessary level of international competitiveness and shall be related, in particular, with increases of production, improvements in the quality of production or distribution, or with technical and technological progress. The

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Available online at http://www.agcm.it/AGCM_ENG/NORMATIV/E_NORMNA.NSF/09b5eea8ea4739cec12564d1004837ee/d9221ec1a3ef3879802564a30066bc40?OpenDocument.

exemption may not permit restrictions that are not strictly necessary for the purposes of this subsection, and may not permit competition to be eliminated in a substantial part of the market.

2. The Authority may subsequently, after giving notice, revoke the exemption referred to in subsection (1) in cases where the party concerned abuses it, or when any of the conditions on which the exemption was based no longer obtain.

3. Requests for exemption shall be submitted to the Authority, which shall avail itself of the powers of investigation referred to in section 14 and decide within a period from 120 days of the date on which the application is filed.

It is interesting to note that despite the similarity in the wording between the Italian and EC regimes, the Italian Antitrust Authority has implied a form of the “rule of reason” analysis into Article 2 of its legislation. For example, in *Autorita Garante della Concorrenza e del Mercato, Relazione Annuale Sull’attività Svolta*⁶⁸ the Court held that in general, consistent with the European Community approach, after an agreement is found to have a restrictive object, an assessment of the restrictive nature of its effect is not necessary for purposes of establishing a violation of Article 2(2), since the two prerequisites laid down in this provision are alternative. However, the Court went further to describe the following additional considerations:

As a qualification to the above, however, . . . it cannot be ruled out that, even if an agreement is found to have a restrictive object, the analysis of its effects, as a possible indicator of the agreement’s restrictive nature with respect to the structure of the relevant market, may become appropriate. The agreement’s effects may become relevant for the purpose of establishing possible external factors, which must be taken into account in the whole assessment, with particular respect to the agreement’s appreciability. Under the settled case law of the Court of Justice, the effects of an agreement must be assessed in its legal and economic context. Therefore, the way in which market relationships would have developed in the absence of the agreement in question must be taken into account; furthermore, the agreement must be assessed jointly with any other similar agreements existing in the same market. Where scrutiny of an agreement’s effects appears necessary, an economic analysis of the markets, which must take into account such elements as the existence of intellectual property rights, the existing degree of competition and the competitor’s reaction to the agreement’s effects, will thus be indispensable.⁶⁹

⁶⁸ See *Annual Report* (1994) at 129.

⁶⁹ *Ibid* at 129.

(I) Conclusion in respect of European Community Systems

There are a number of advantages to the approach adopted under the EC Treaty and in the legislation of other EC jurisdictions as described above. Applying a broad interpretation to Article 81(1), and its counterparts found in national legislation, ensures that these provisions are applicable to all forms of anti-competitive horizontal arrangements, including price-fixing and other hard-core cartel behaviour. To ensure that the broad prohibition found in Article 81(1) does not dissuade parties from engaging in potentially pro-competitive arrangements, Article 81(3) provides a broad discretion to the Commission to grant exemptions.

The benefit of the broad and liberal interpretation of Article 81 is also its greatest weakness. Given its breadth, Article 81(1) is applicable to agreements with little or no risk of being economically anti-competitive. Also, Article 81(2) renders agreements which fall within the broad scope of Article 81(1) void and unenforceable, unless an individual exemption is obtained or the agreement falls with the block exemptions. This, in turn, results in a heavy reliance by industry and the Commission upon the notification and exemption regime found in Article 81(3). Therefore, from a practical perspective, the Commission works reactively, dealing only with notifications from industry participants as opposed to focusing its efforts and resources on proactively addressing significant distortions of competition, such as hard-core cartels, which are almost never the subject of notification. Further, the legal certainty created by the exemption process is eroded due to excessive delay in the processing of notifications. Finally, the high cost of such notifications is potentially prohibitive, particularly for small- and medium-sized enterprises. The overall result is that parties may be dissuaded from engaging in potentially beneficial strategic alliances which do not fall within the strict terms of the block exemptions. As noted by Presley Warner and Michael Trebilcock:

The mere availability of an authorization mechanism may not be sufficient to encourage parties to proceed with potentially competitive arrangements, since parties to arrangements which may trigger the prohibition will be reluctant to proceed with their arrangements if they must submit to cumbersome procedures to protect themselves from sanctions.... the mechanism must be simple to invoke and must provide legal certainty to the parties.⁷⁰

The proposed abolition of the notification and authorization regime, as outlined in the draft Council Regulation discussed above, will certainly reduce the administrative burden on the Commission and the costs to industry participants. However, these benefits will come at the expense of legal certainty. Similar to the U.S. model, parties will be forced to resort to their own assessment of their agreement's compliance, or lack thereof, with provisions of Article 81.

⁷⁰ Presley L. Warner and Michael J. Trebilcock, "Rethinking Price-Fixing Law" (1993) 38 McGill L.J. 679 at 710. [hereinafter "Warner et al."]

It is noteworthy that unlike some of the other regimes canvassed herein, the European Community approach utilizes a “single track” notification system. This places heavy emphasis on notification and creates potential for abuse. As discussed below, limiting the requirement for notifications to those agreements falling within category of *per se* prohibition would significantly lower the number of notifications. Similarly, making all agreements - not just *per se* illegal agreements - unenforceable absent a notification, requires parties to submit notifications for agreements for which there is little risk of opposition by competition authorities.

VI. UNITED STATES

Section 1 of the *Sherman Act*⁷¹ sets out a prohibition against contracts, combinations, and conspiracies (collectively “agreement”) “in restraint of trade or commerce among the several States or with foreign nations”. Violations of section 1 may be prosecuted civilly or as criminal offences. Criminal enforcement of section 1 – the preserve of the Department of Justice (“DOJ”) – is limited to traditional *per se* offences of the law. Criminal violation of section 1 is a felony punishable by maximum fines of \$10 million in the case of corporate defendants and \$350,000 in the case of all other defendants.⁷² Individual offenders may also be imprisoned for up to 3 years.

Civilly, there are three possible plaintiff-side actors – the DOJ, Federal Trade Commission (“FTC”) (collectively the “Agencies”), and private plaintiffs. The DOJ may obtain injunctive relief restraining or enjoining an agreement or it may file suit to amend it.⁷³ It may also recover treble damages if the U.S. government is the purchaser of the affected goods or services.⁷⁴ Private plaintiffs may also obtain injunctive relief⁷⁵ or bring suit for treble damages.⁷⁶ In private actions, a prior conviction flowing from a related criminal prosecution may serve as *prima facie* evidence of

⁷¹ 15 U.S.C. § 1.

⁷² See Gary R. Spratling, “The Trend Toward Higher Corporate Fines: It’s a Whole New Ball Game” in *National Institute on White Collar Crime Presented by the ABA’s Criminal Justice Section* (March, 1997) for a discussion of the manner in which fines are calculated under the *Sentencing Guidelines*. Notably, the “double the gain/double the loss standard” in 18 U.S.C. § 3571(d) has been successfully employed to fine defendants in excess of the \$10 million *Sherman Act* cap. This standard provides for an “alternative maximum fine for an antitrust violation [equal to] twice the gross gain derived from the crime [*i.e.*, total gain derived by all persons from the offense] or twice the gross loss [*i.e.*, the total loss suffered by all persons other than the defendant as a result of the offense] caused by, *the cartel, not the defendant*”. Spratling, *supra* at 5. [emphasis in the original]

⁷³ See 15 U.S.C. §§ 4, 25.

⁷⁴ See § 4A *Clayton Act*, 15 U.S.C. § 15a.

⁷⁵ See *Clayton Act*, 15 U.S.C. § 26. Plaintiffs must establish “threatened loss or damage”. See, e.g., *Hawaii v. Standard Oil Co. of California*, 405 U.S. 251, 260-64 (1972).

⁷⁶ See § 5(a) *Clayton Act*, 15 U.S.C. § 15. Plaintiffs must establish both standing to sue and actual injury as a result of the alleged antitrust violation. See also 54 Am. Jur. 2d *Monopolies, Restraints of Trade, and Unfair Trade Practices* (1996) at § 50.

the alleged civil wrongdoing.⁷⁷ Finally, the FTC may institute civil proceedings under section 5 (*i.e.*, “unfair methods of competition”) of the *Federal Trade Commission Act*⁷⁸ in respect of an agreement that violates section 1.⁷⁹

As a general matter, the type of agreement at issue will be determinative of the DOJ’s decision to proceed civilly or criminally.

[C]urrent [Antitrust] Division policy is to proceed by criminal investigation and prosecution in cases involving horizontal, *per se* unlawful agreements such as price fixing, bid rigging and horizontal customer and territorial allocations. Civil process and, if necessary, civil prosecution is used with respect to other suspected antitrust violations, including those that require analysis under the rule of reason as well as some offenses that historically have been labelled “*per se*” by the courts.⁸⁰

There are, however, circumstances in which criminal investigation and/or prosecution may not be pursued, despite the fact that an agreement may appear to be *per se* illegal.

These ... may include cases in which: (1) there is confusion in the law; (2) there are truly novel issues of law or fact presented; (3) confusion reasonably may have been caused by past prosecutorial decisions; [and] (4) there is clear evidence that the subjects of the investigation were not aware of, or did not appreciate, the consequences of their action.⁸¹

⁷⁷ See § 4(a) *Clayton Act*, 15 U.S.C. § 15.

⁷⁸ 15 U.S.C.S §§ 41 et seq.

⁷⁹ See Warner et al., *supra* note 70 at 699 for a fuller discussion of the details of antitrust enforcement by the FTC.

⁸⁰ U.S. Department of Justice, Antitrust Division, *Antitrust Division Manual* available at <http://www.usdoj.gov/atr/foia/divisionmanual/ch3.htm>. It should be noted that the phrase “some offenses that historically have been labeled ‘*per se*’ by the courts” refers to certain categories of agreements (*e.g.*, agreement to price fix or boycott) that have traditionally been treated as *per se* illegal but which, under current Supreme Court jurisprudence, may now be subject to review according to a rule of reason standard where they are shown to be ancillary to a productive transaction.

⁸¹ *Ibid.*

(a) Modern American Approach to Horizontal Agreements

Read literally, section 1’s broad, unqualified language “would condemn all contracts affecting interstate commerce”.⁸² For this reason, the provision has been construed by the United States Supreme Court as proscribing agreements only where they are “unreasonably restrictive of competitive conditions”.⁸³ As applied by the U.S. judiciary, a section 1 violation, in respect of a competitor collaboration, thus has three elements:

- there must be a contract, combination or conspiracy (“agreement”) between two or more competitors;
- the agreement must affect interstate or foreign commerce; and
- the agreement must have as its object or effect the unreasonable restraint of trade.⁸⁴

Specific intent must also be proved where Section 1 is enforced criminally. On the civil side, although an anti-competitive intent cannot by itself found an antitrust violation, pro-competitive intent will not necessarily negate a violation. However, “extrinsic evidence of intent may aid in evaluating market power, the likelihood of anticompetitive harm, and claimed procompetitive justifications [under a rule of reason review] where an agreement’s effects are otherwise ambiguous”.⁸⁵

Under U.S. law, there are three categories of horizontal agreement – *per se* illegal agreements, rule of reason agreements and *per se* legal agreements. In general, the label of “*per se* illegality” applies to an agreement coming within one of the judicially-determined categories of agreement that is conclusively presumed to be anti-competitive and is thus summarily condemned as unlawful (*e.g.*, price fixing⁸⁶ and output fixing agreements as well as agreements to divide territories or customers⁸⁷

⁸² Thomas C. Arthur, “Farewell to the Sea of Doubt: Jettisoning the Constitutional Sherman Act” (1986) 74 Calif. L. Rev. 266 at 268.

⁸³ *Standard Oil Co. v. United States*, 221 U.S. 1, 58 (1911).

⁸⁴ *See Times-Picayune Pub. Co. v. United States*, 345 U.S. 594 (1953).

⁸⁵ Joint Guidelines, *supra* note 2 at 12.

⁸⁶ *See, e.g., United States v. Trenton Potteries*, 273 U.S. 392 (1927) [hereinafter *Trenton Potteries*]; *U.S. v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) [hereinafter *Socony-Vacuum*]; *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951). [hereinafter *Kiefer-Stewart*]

⁸⁷ *See, e.g., U.S. v. Topco Assocs. Inc.*, 405 U.S. 596 (1972) [hereinafter *Topco Assocs. Inc.*]; *U.S. v. Sealy, Inc.*, 388 U.S. 350 (1967) [hereinafter *Sealy, Inc.*]; *Timken Roller Bearing Co. v. U.S.*, 341 U.S. 593 (1951). [hereinafter *Timken*]

or to boycott customers and suppliers⁸⁸). Rule of reason agreements are those agreements that are thought to be potentially pro-competitive, and are thus subject to review according to the rule of reason standard which requires that, in order to avoid condemnation, an impugned agreement be shown to have a net pro-competitive effect within the relevant market.

(b) The Rule of Reason Standard

The rule of reason is the presumptive standard according to which the “reasonableness”, and hence the legality, of competitor collaborations is determined.⁸⁹ As noted above, the factual inquiry mandated by the rule of reason is whether, on balance, the impugned agreement promotes or suppresses competition.⁹⁰ In practical terms, this involves as many as four different inquiries.

(i) Anti-Competitive Harm

Courts first ask whether the agreement harms competition. Here, the plaintiff must establish the likelihood that some anti-competitive harm will result from the impugned agreement. Output reduction, likely or actual, is used as a measure of anti-competitive harm.⁹¹ Market power, which acts as a surrogate for an agreement’s output-reducing effects, may also be used due to “the inherent difficulty of measuring the effects of [an agreement] on output”.⁹² The Joint Guidelines identify four factors relevant to the question of anti-competitive harm. These are:

- the nature of the agreement (*i.e.*, whether it limits independent decision-making or combines control or financial interests);

⁸⁸ See *Klor’s, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959) [hereinafter *Klor’s*]; *Fashion Originators’ Guild of America, Inc. v. Federal Trade Commission*, 312 U.S. 457 (1941) [hereinafter *Fashion Originators’*]; *Eastern States Lumber Dealers’ Assoc. v. U.S.*, 234 U.S. 600 (1914). [hereinafter *Eastern States Lumber Dealers’ Assoc.*]

⁸⁹ See *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 59 (1977) [hereinafter *GTE Sylvania*]; *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988); *National Collegiate Athletic Assn. v. Board of Regents of the University of Oklahoma*, 468 U.S. 85 (1984) [hereinafter *NCAA*]; see also *Martin B. Glauzer Dodge Co. v. Chrysler Corp.*, 570 F.2d 72 (CA3 NJ 1977).

⁹⁰ See *National Society of Prof’l Eng’rs v. United States*, 435 U.S. 679, 691 (1978). [hereinafter *Prof’l Eng’rs*]

⁹¹ See *Broadcast Music, Inc. v. Columbia Broadcasting System*, 441 U.S. 1, 20 (1979). [hereinafter *Broadcast Music*]

⁹² Warner et al., *supra* note 70 at 694. Notably, according to Warner et al. (at 694) “[t]here is no consensus among either courts or academics on the degree of market power that parties must possess for courts to conclude that their [agreements] reduce output”.

- relatedly, the ability and incentive of participants to compete independently;⁹³
- the likelihood, timing and sufficiency of entry;⁹⁴ and
- more generally, the market circumstances.⁹⁵

(ii) Efficiency Justification

At the second stage, the burden of proof shifts to the defendant who is required to proffer an efficiency justification for the impugned agreement. For example, an agreement may permit competitors with differing capabilities and resources to act jointly or collectively “to offer goods or services that are cheaper, more valuable to consumers, or brought to the market faster than would be possible absent the collaboration”.⁹⁶ The Joint Guidelines refer to the foregoing as “cognizable efficiencies”, defined as verifiable – as opposed to vague or speculative – efficiencies “not arising from anti-competitive reductions in output or service, and that cannot be achieved through, practical, significantly less restrictive means”.⁹⁷ Where the implausibility of an alleged efficiency justification is obvious, the agreement will be summarily condemned.⁹⁸

There is some uncertainty as to the proper scope and limits of the justification inquiry. The question is whether economic efficiency alone, as opposed to a balance of efficiency and non-economic considerations, is the proper focus of the rule of reason justification analysis. In the *Professional Engineers* case,⁹⁹ the Supreme Court appeared to strictly limit the justification analysis to

⁹³ The Joint Guidelines review six factors relevant to the ability and incentive of participants and the collaborations to compete – exclusivity, control over assets, financial interests in the collaboration or in other participants, control of the collaboration’s competitively significant decision-making, likelihood of anti-competitive information sharing, and the duration of the collaboration – at 18-21.

⁹⁴ Entry is discussed at 21-23 of the Joint Guidelines.

⁹⁵ Joint Guidelines, *supra* note 2 at 11; *see also* Joint Guidelines, *supra* note 2 at 13-15 for a discussion of the manner in which independent decision-making may be limited by various kinds of collaborations (*e.g.*, production collaborations, R&D collaborations, buying collaborations, and marketing collaborations) and the resulting anti-competitive harm.

⁹⁶ Joint Guidelines, *supra* note 2 at 6.

⁹⁷ Joint Guidelines, *supra* note 2 at 23. Note that “cognizable efficiencies are assessed net of costs produced by the competitor collaboration or incurred in achieving those efficiencies”.

⁹⁸ *NCAA*, *supra* note 89 at 111 (quoting Areeda).

⁹⁹ *See Prof'l Eng's*, *supra* note 90 at 693-95.

consideration of a challenged agreement’s effect on competition. Thus, it has been suggested that non-economic considerations are not cognizable for the purpose of the justification analysis.¹⁰⁰ However, it has been argued that the Court has failed, either in *Professional Engineers* and/or in subsequent cases, to “squarely indicate whether [and, if so, precisely in what manner] social concerns are relevant to the validity of” horizontal restraints.¹⁰¹

(iii) Reasonable Necessity

Assuming that the defendant has successfully demonstrated that a plausible efficiency justification exists for the impugned agreement, courts move to the third stage of rule of reason inquiry where the defendant is required to establish the justification’s “reasonable necessity”. Notably, the manner in which the necessity of a restraint, or the lack thereof, is to be judged has not been determined authoritatively.¹⁰²

The Joint Guidelines establish that “reasonable necessity” does not require a showing that the restraint is “essential”. Instead, where an equivalent or comparable efficiency-enhancing integration could practically be realized through “significantly less restrictive means”, an impugned restraint will not be considered to be “reasonably necessary”.¹⁰³ The Joint Guidelines also indicate that “reasonable necessity” will also turn on the market context (*e.g.*, new entrant versus established competitor), the duration of the agreement, and the extent to which the collaboration is structured so as to deter free riding or opportunistic conduct that could ultimately diminish promised efficiencies.¹⁰⁴

(iv) Net Effect

As described in the Joint Guidelines, the final stage of the rule of reason analysis involves a comparison of the “likelihood and relative magnitude of cognizable efficiencies and anticompetitive harms to determine the agreement’s overall actual or likely effect on competition in the relevant market”.¹⁰⁵ The actual or likely short-term effects of the agreement are the principal focus here .

¹⁰⁰ See Warner et al., *supra* note 70 at 694.

¹⁰¹ See Arthur, *supra* note 82 at 365-66; see generally Barry Wertheimer, “Rethinking the Rule of Reason: From Professional Engineers to NCAA” (1984) Duke L.J. 1297.

¹⁰² See James T. Halverson, “The Direction of Antitrust in the Decade Ahead: Some Predictions: The Future of Horizontal Restraints Analysis” (1988) 57 Antitrust L.J. 33 at 46; Arthur, *supra* note 82 at 360.

¹⁰³ See Joint Guidelines, *supra* note 2 at 9.

¹⁰⁴ See Joint Guidelines, *supra* note 2 at 24.

¹⁰⁵ Joint Guidelines, *supra* note 2 at 25.

While “delayed benefits” may also be taken into account, the Joint Guidelines indicate that these are given less weight “because they are less proximate and more difficult to predict”.¹⁰⁶

(c) *Per Se Illegality*

As noted at the outset, in principle, American law designates certain agreements as unreasonable *per se* and hence illegal under section 1. Historically, where judicial experience has demonstrated that a specific type of agreement is “so ‘plainly anticompetitive’ and so often ‘lacking ... any redeeming virtue’”¹⁰⁷ (e.g., it is solely a means of restricting output and increasing prices) the Court’s jurisprudence establishes that an agreement falling into that category will be conclusively presumed to be illegal, without the necessity of an inquiry into its:

- net competitive effect,
- claimed business purpose, or
- possible non-economic justifications (*viz.* its reasonableness).¹⁰⁸

As a general rule, U.S. law summarily proscribes price fixing¹⁰⁹ and output fixing agreements as well as agreements to divide territories or customers¹¹⁰ or to boycott customers and suppliers¹¹¹ on this basis. Consequently, the mere fact of agreeing to fix prices, for example, is a sufficient basis for liability.¹¹² The business purpose or effects of an agreement of this kind have no place in the summary *per se* analysis.

¹⁰⁶ Joint Guidelines, *supra* note 2 at 25.

¹⁰⁷ Halverson, *supra* note 102 at 35 (quoting *Prof'l Eng'rs*, *supra* note 90 at 692; *GTE Sylvania*, *supra* note 89 at 50; *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958) [hereinafter *Northern Pac. Ry.*]).

¹⁰⁸ See, e.g., *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 351 (1982). [The anticompetitive potential inherent in all price-fixing agreements justifies their facial invalidation even if pro-competitive justifications are offered for some] [hereinafter *Maricopa*]

¹⁰⁹ See, e.g., *Trenton Potteries*, *supra* note 86.; *Socony-Vacuum*, *supra* note 86; *Kiefer-Stewart*, *supra* note 86.

¹¹⁰ See, e.g., *Topco Assocs. Inc.*, *supra* note 87; *Sealy, Inc.*, *supra* note 87; *Timken*, *supra* note 87.

¹¹¹ See *Klor's*, *supra* note 88; *Fashion Originators'*, *supra* note 88; *Eastern States Lumber Dealers' Assoc.*, *supra* note 88.

¹¹² See T. Webb, “Fixing the Price Fixing Confusion: A Rule of Reason Approach” (1993) Yale L.J. 706 at 708.

The *per se* analysis has three rationales – economic reliability, ease of judicial administration, and predictability.¹¹³ *Per se* illegality reflects the judgment that the economic theory underpinning price fixing, for example, is “sufficiently well developed to obviate the need for consideration of [a price-fixing agreement’s] positive effects in particular instances”.¹¹⁴ Relatedly, the *per se* rules also reflect the judgment that the likelihood of anti-competitive harm is so great (and the likelihood of pro-competitive benefits so minute) in relation to certain categories of agreement that the costly and time-consuming rule of reason inquiry may justifiably be foregone.¹¹⁵ Finally, assuming that the proscribed conduct is capable of clear definition, the *per se* rules also rest on the judgment that they increase the consistency and predictability of anti-trust enforcement and judicial decision-making.¹¹⁶

In the 1980s and 1990s, however, significant criticism of the economics underpinning most of the categories of *per se* illegal agreements cast doubt on the economic reliability rationale and has inevitably, given the inter-relatedness of the three rationales discussed above, led to a diminution in the *per se* rules’ ease of administration and predictability.¹¹⁷ “Only the rules against cartel activities have escaped without serious challenge”.¹¹⁸ The result has been abandonment, both by the Supreme Court and U.S. Circuit Courts, of strict *per se* treatment of certain categories of agreement historically thought to produce consequences necessarily violative of the statute. These include tying agreements,¹¹⁹ agreements to price fix,¹²⁰ to allocate customers or markets,¹²¹ and to boycott.¹²²

The Courts’ recent approach to the *per se* rule against price-fixing is illustrative of the foregoing trend. “Under the Sherman Act, a combination formed for the purpose and with the effect of raising,

¹¹³ *Ibid* at 708.

¹¹⁴ *Ibid* at 709.

¹¹⁵ *Ibid* at 709; *see also* *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2, 15-16 n. 25 (1984). [hereinafter *Hyde*]

¹¹⁶ *See* *Webb*, *supra* note 112 at 710.

¹¹⁷ *See* *Arthur*, *supra* note 82 at 316-17 and n. 288.

¹¹⁸ *Arthur*, *supra* note 82 at 316.

¹¹⁹ *See* *Hyde*, *supra* note 115.

¹²⁰ *Board of Regents v. NCAA*, 104 S. Ct. 2948, 2960-62 (1984); *Broadcast Music*, *supra* note 91 at 8-10, 16-24.

¹²¹ The trend is now to evaluate market-division agreements using a rule of reason standard. “There is now strong authority for the proposition that defendant’s must have market power for their market-sharing arrangements to be condemned”. Warner et al., *supra* note 70 at 696 n. 92 (citing *NCAA*, 468 U.S.; *Polk Brothers Inc. v. Forest City Enterprises Inc.*, 776 F.2d 185 (7th Cir. 1985); *Rothery Storage & Van Co. v. Atlas Van Lines Inc.*, 792 F.2d 210 (D.C. Cir. 1986); *General Leaseways, Inc. v. National Truck Leasing Assoc.*, 74 F.2d 588 (7th Cir. 1984)).

¹²² *See* *Johnston; Northwest Wholesale Stationers Inc. v. Pacific Stationary & Printing Co.*, 472 U.S. 284 (1985); *Maricopa*, *supra* note 108.

depressing, fixing or pegging, or stabilizing the price of a commodity . . . is illegal per se”.¹²³ The *per se* rule against price fixing, as historically articulated and applied by the Supreme Court, catches maximum as well as minimum price agreements, agreements involving contractual terms which affect price (*e.g.*, credit terms), agreements on final price, agreements to force other to raise their prices and even agreements that only indirectly interfere with free market pricing decisions.¹²⁴ However, the historic rule which condemns any combination that literally raises, depresses, fixes, pegs, or stabilizes no longer holds in all cases. In *Broadcast Music*, the Supreme Court abandoned the literal *per se* rule, distinguishing “price fixing agreements” and “*per se* price fixing” in recognition of the fact that “agreements which literally ‘fix’ prices may under some circumstances be lawful, in particular, where ancillary to legitimate joint activity”.¹²⁵

The current approach to price fixing relies on the distinction between “naked” restraints – agreements between competitors not reasonably necessary to a *bona fide* collaboration or productive transaction – and “ancillary” restraints – agreements that aid some valid business transaction and thus create “integrative efficiencies”.¹²⁶ Naked restraints are *per se* illegal and subject to summary condemnation, while ancillary restraints are subject to evaluation pursuant to the rule of reason standard, where market definition and power issues are considered.

The Joint Guidelines indicate that “[i]f ... participants in an efficiency-enhancing integration of economic activity enter into an agreement that is reasonably related to the integration and reasonably necessary to achieve its procompetitive benefits, the Agencies [will] analyze the agreement under the rule of reason, **even if** it is of a type that might otherwise be considered per se illegal”.¹²⁷ The Joint Guidelines define “efficiency enhancing integration” as follows:

In an efficiency-enhancing integration, participants collaborate to perform or cause to be performed (by a joint venture entirely created by the collaboration or by one or more participants or third parties acting on behalf of other participants) one or more business functions, such as production, distribution, marketing, purchasing or R&D, and thereby benefit, or potentially benefit, consumers by expanding output, reducing price, or enhancing quality, service, or innovation. Participants in an efficiency-enhancing integration typically combine, by contract or otherwise, significant capital, technology, or other complementary assets to achieve procompetitive benefits that

¹²³ *Socony-Vacuum*, *supra* note 86 at 223.

¹²⁴ See M. Elaine Johnston, “Horizontal Restraints” in *The 47th Annual Spring Meeting: Antitrust Fundamentals* (1999) at 7-8.

¹²⁵ *Ibid* at 8.

¹²⁶ Warner et al., *supra* note 70 at 697; see also Halverson, *supra* note 102 at 46 [ancillary restraints are those that are “subordinate and collateral to a separate, legitimate transaction ... [serving] to make the main transaction more effective...” ((quoting *National Bancard Corp. (NaBanco) v. Visa U.S.A., Inc.*, 779 F.2d 592 (11th Cir.), cert. denied, 107 S. Ct. 329 (1986)).

¹²⁷ Joint Guidelines, *supra* note 2 at 8. [emphasis added]

participants could not achieve separately ... The integration must be of a type that **plausibly** would generate procompetitive benefits cognizable under the efficiencies analysis.¹²⁸

(d) Conclusion in Respect of the US Regime

(i) Macro Advantages

The U.S. model, to a considerable extent, permits differentiation between competitor collaborations that reduce social welfare and those that raise social welfare by creating efficiencies that exceed and compensate for any resultant anti-competitive harm.¹²⁹ The American regime, at least in principle, builds in the aforementioned distinction on two levels:

- the rule of reason/*per se* illegality dichotomy; and
- the rule of reason review itself, which, of course, permits a comprehensive assessment of the alleged pro-competitive benefits of an impugned agreement prior to deciding its legality.

Further, it is arguable that the Supreme Court’s recent relaxation of the *per se* rules has enhanced, rather than diminished, the ability of regulatory and judicial decision-makers to differentiate between collaborations in the manner described above.

(ii) Macro Disadvantages

As a result of section 1’s broad, standardless language the current state of American conspiracy law has been one hundred years of jurisprudence in the making. Even now, however, some suggest that the absence of a singular operational standard “to guide the decision of hard cases” has “permit[ted] courts to reappraise and reshape the basic policies of antitrust law” with the result that “[a]ntitrust litigation [in the U.S.] remains notoriously costly and unpredictable, despite repeated efforts to simplify both the doctrine and the litigation process”.¹³⁰

Recent developments in American law (described above) have created uncertainty in relation to the circumstances in which a *per se* rule or rule of reason analysis will be applied by the courts. For example, in relation to “agreements that concern price in some way”, Webb argues that there is uncertainty in predicting which analysis will be adopted by the courts in a given case.¹³¹ In this

¹²⁸ Joint Guidelines, *supra* note 2 at 8. [emphasis added]

¹²⁹ See Ross, *supra* note 7.

¹³⁰ Arthur, *supra* note 82 at 268 and 270; see also Webb, *supra* note 112 at 706.

¹³¹ See Webb, *supra* note 112 at 720.

regard, he points to the inconsistent results in the *Broadcast Music* and *Maricopa* cases despite broadly similar facts. In both cases, the defendants were engaged in marketing a new product – “blanket licenses” in *Broadcast Music* and low-cost, full coverage health insurance in *Maricopa* – and in both cases “the new product was a ‘blanket’ response to the high transaction costs of per-use purchases”.¹³² However, the Court applied the *per se* rule in *Maricopa* and the rule of reason in *Broadcast Music*. Webb contends that there is no principled basis for distinguishing these cases.¹³³

(iii) Micro Advantages and Disadvantages

The respective advantages and disadvantages of each of the constituent elements of the relevant American regime will be considered next.

(1) Per Se Illegality

In principle, the strict variant of the *per se* rule offers at least two inter-related advantages:

- it is relatively less costly; and
- it promises increased certainty and predictability.¹³⁴

Because the sole question under a *per se* analysis is whether the unlawful conduct has taken place, logically *per se* rules should be less costly, as a matter of time and expense, to enforce and apply than the rule of reason’s in-depth comparative inquiry into the net competitive effect of the same conduct.¹³⁵ Similarly, the *per se* rules’ categorical approach, which purports to make the types of the agreements that are proscribed more certain, promises greater consistency and predictability, to the benefit of business planners.

However, the efficiency and clarity of the *per se* rule may be more apparent than real. In practice, application of a *per se* rule involves a threshold inquiry, namely whether the impugned agreement may be properly characterized as falling within the *per se* rule in question. Characterizing an agreement “can be very difficult, and may involve a fair amount of sophisticated economic inquiry”.¹³⁶ Consequently, as the Supreme Court has recognized, “there is often no bright line

¹³² Webb, *supra* note 112 at 721-22.

¹³³ See Webb, *supra* note 112 at 722.

¹³⁴ See Webb, *supra* note 112 at 708.

¹³⁵ See *Northern Pac. Ry.*, *supra* note 109 at 5 [A *per se* rule avoids the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries].

¹³⁶ H. Hovenkamp, *Economics and Federal Antitrust Law* (1985), at 128-29.

separating *per se* from Rule of Reason analysis”.¹³⁷ The cost advantages, both to the administration of justice and litigants, of the *per se* rule are, of course, lost if a full-blown or even a partial rule of reason analysis is required prior to condemning an agreement as *per se* illegal.

Relatedly, this characterization problem has negative consequences for the vaunted certainty and predictability of the *per se* rule. For example, “an uncertain definition of price fixing cannot provide businessmen with a reliable standard by which to guide their conduct”.¹³⁸ The chilling effect flowing from the uncertain application of the *per se* rule arguably inhibits efficient competitor collaborations, ultimately diminishing social welfare.

More fundamentally, as noted above, the *per se* rules are premised on the related assumptions that:

- the economic theory underpinning the conclusion that a category of agreements is invariably injurious to competition is sound and, consequently,
- that the burdensome rule of reason inquiry may justifiably be avoided in relation to certain categories of agreements.

The *per se* rule against price fixing illustrates the problematic nature of the foregoing assumptions.

Webb argues that “as a legal category [the *per se* rule] has no coherent economic rationale” (apart from the harms from anti-competitive cartels).¹³⁹ Pointing to the well-known exceptions for joint ventures and partnerships, he argues that it is not every “agreement concerning price” that is “economically invidious but rather agreements by producers with market power to restrict output and raise price to above competitive levels”.¹⁴⁰ The result of American law’s historically mechanical interdiction against any combination that raises, depresses, fixes, pegs, or stabilizes prices (*i.e.*, without regard to market power and economic effects) has ultimately been, he suggests, to undermine competition and consumer welfare.¹⁴¹

¹³⁷ *NCAA*, *supra* note 89 at 104 n. 26.

¹³⁸ *Webb*, *supra* note 112 at 711.

¹³⁹ *Webb*, *supra* note 112 at 715.

¹⁴⁰ *Webb*, *supra* note 112 at 715.

¹⁴¹ *See Webb*, *supra* note 112 at 714. *Webb* holds out *Boise Cascade v. FTC*, 693 F.2d 573 (9th Cir. 1980) as an example of the overbreadth of the traditional *per se* rule against price fixing. In that case, three Southern plywood manufacturers were found guilty of *per se* violations of section 1 for conspiring to maintain a uniform system of “delivered” pricing (*i.e.*, a method of price quotation). In keeping with the *per se* rule, no adverse effect on total prices was found or even considered. The defendants had standardized delivery charges, as between Southern and Western producers, by quoting a mill price adjusted to reflect the higher delivery charges from West Coast producers. *Webb* doubts whether, in the absence of evidence that total price was affected, an agreement of this kind actually results in anti-competitive harm. On the contrary, he suggests that the price quoting system had a clear pro-competitive justification, namely “[it] reduce[d] information costs to consumers comparing Southern

Similarly, Ross suggests that “even a practice as notorious [and as inimical to competition] as price fixing can be part of a socially efficient arrangement”.¹⁴² By way of illustration, he points to a hypothetical agreement among a number of small retail pharmacists in a large city to jointly advertise and honour the prices listed. He notes that “[w]hile this is no doubt (in part) an agreement to fix price, the arrangement can have no negative effect on competition (since the retailers together represent a tiny fraction of sales in the city) and will in fact be beneficial to the extent that it improves information in the market and lowers the cost of advertising” through the realization of scale economies.¹⁴³

A final arguable disadvantage of *per se* illegality is its effect on the flow of information to judicial decision-makers. “It is difficult enough for judges to inform themselves about business practices without shutting off the information flow before it begins, by prematurely adopting a rule of blanket illegality”.¹⁴⁴

(2) Rule of Reason

As noted above, the fundamental advantage offered by the rule of reason standard is flexibility, permitting courts to differentiate between pro-competitive, welfare enhancing collaborations from those which are not. Flexibility comes at a price, however. The rule of reason is an imprecise standard requiring a case-by-case weighing of all the relevant circumstances before a determination regarding the reasonableness of an impugned agreement can be made. The complicated and prolonged economic investigation necessitated by the rule of reason standard often entails significant time and expense.

The other difficulty associated with the rule of reason arises from the task of comparing the relevant pro-competitive and anti-competitive effects. Where the two effects are disproportionate the net effect is plain. However, close cases are more problematic. According to Arthur, Supreme Court jurisprudence provides “neither a methodology for case-by-case weighing of restrictive and efficiency effects, nor a set of rules with which to avoid such a case-[by]-case inquiry”.¹⁴⁵

and Western plywood by enabling them to compare the respective mill prices directly and to determine the total delivered price simply by adding the same standard freight charge to each mill quotation. The result was increased competition among all plywood producers and reduced search costs for plywood consumers”. Webb, *supra* note 112 at 718-19.

¹⁴² Ross, *supra* note 7 at 866.

¹⁴³ Ross, *supra* note 7 at 862.

¹⁴⁴ *Vogel v. American Society of Appraisers*, 744 F.2d 598, 604 (7th Cir. 1984) (quoted in Halverson, *supra* note 102 at 43).

¹⁴⁵ Arthur, *supra* note 82 at 362.

Finally, it has also been suggested that under the current rule of reason approach “defendants will find it hard to prevail”.¹⁴⁶ This of course raises the spectre of over-deterrence, with its attendant harm to consumer and, ultimately, social welfare.

VII. AUSTRALIA

Australia’s first antitrust statute “closely followed the terms of the *Sherman Act* 1890” and did not provide an authorization mechanism.¹⁴⁷ However, the current Part IV of the Australian *Trade Practices Act* includes a number of different elements from the U.S. and European Community regimes discussed above, along with other aspects which are unique to Australia. Specifically, the *Act* incorporates detailed *per se* prohibitions against agreements to fix prices or engage in other forms of hard-core cartel behaviour. The *Act* also contains a broad proscription that relies on a partial rule of reason analysis, similar to section 45 of the Canadian *Competition Act*, to prohibit agreements or arrangements which have the purpose or effect of substantially lessening competition. Similar to Article 81(3) of the EC Treaty, the *Act* permits the Australian Competition and Consumer Commission (the “ACCC”) to grant “authorizations” to “make” or “give effect to” agreements, even for those agreements which fall within the *per se* prohibitions. A copy of the relevant provisions is attached at Schedule “V”.

Section 45 proscribes agreements, arrangements and understandings which have as their purpose, effect or likely effect the substantial lessening of competition.¹⁴⁸ Section 45 also prohibits corporations from giving effect to such agreements. The *per se* prohibitions are found in section 45A of the *Act*. Section 45A states as follows:

Without limiting the generality of section 45, a provision of a contract, arrangement or understanding, or of a proposed contract, arrangement or understanding, shall be deemed for the purposes of that section to have the purpose, or to have or to be likely to have the effect, of substantially lessening competition if the provision has the purpose, or has or is likely to have the effect, as the case may be, of fixing, controlling or maintaining, or providing for the fixing, controlling or maintaining of, the price for, or a discount, allowance, rebate or credit in relation to, goods or services supplied or acquired or to be supplied or acquired by the parties to the contract, arrangement or understanding or the proposed parties to the proposed contract, arrangement or understanding, or by any of them, or by any bodies corporate that are related to any of them, in competition with each other.

As noted above, section 45A prohibits agreements between actual or likely competitors, that have the purpose, effect, or likely effect of fixing prices in relation to the supply of products. Pursuant

¹⁴⁶ Arthur, *supra* note 82 at 364.

¹⁴⁷ John Duns, “Competition Law and Public Benefits” (1994) 16 *Adel L.R.* 245 at 248.

¹⁴⁸ See s. 45(2)(a)(ii).

to section 45(1), agreements to fix prices are deemed to have the purpose or effect of substantially lessening competition and therefore, are contrary to section 45. Despite the express wording of the statute however, the Australian courts have diluted the “*per se*” nature of the proscription by interpreting s. 45A as requiring proof of an “intention or likelihood to affect price competition”.¹⁴⁹

In a report published by an Independent Committee of Inquiry following a review of Australian competition policy conducted in 1993, it was recommended that exemptions should generally not be permitted for horizontal price-fixing on the basis that it will “undermine the message that price competition is central to effective competition...”.¹⁵⁰ Contrary to this recommendation however, the legislation recognizes that certain types of price-fixing or other agreements which fall within the *per se* prohibitions may result in pro-competitive benefits and therefore should be exempted. For example, section 45A contains a number of exceptions for agreements relating to combined purchasing, joint supply and joint advertising among competitors in certain circumstances. Specifically, section 45A(4) states that the prohibition does not apply to agreements “in relation to the price for goods or services to be collectively acquired” or “for the joint advertising of the price for the re-supply of goods or services so acquired”. Although such agreements are not subject to the *per se* prohibition, they remain subject to the general prohibition found in section 45 where it is established that the agreement has the purpose or effect of substantially lessening competition.

Section 45 and the related prohibitions are enforced by the national courts within Australia. Similar to the EC regime, violations of section 45 are only punishable by fines, referred to as “pecuniary penalties”. However, as with the EC regime, the fines that may be imposed by the Australian Courts are significant. Section 76 authorizes the courts to impose fines against a corporation of up to \$10 million (approximately C\$8 million) for conduct contrary to section 45. Secondary boycotts, which are also prohibited under section 45, may result in fines of up to \$750,000. In addition, individuals may be fined up to \$500,000 in respect of any of conduct contrary to section 45. Pursuant to s. 82, private plaintiffs are permitted to bring suit to recover damages for loss or injury suffered as a result of acts or omissions in breach of Part IV. Notably, half the litigation under the Act is commenced by non-governmental plaintiffs.¹⁵¹

¹⁴⁹ Lynden Griggs, “Compliance with Section 45 of the Trade Practices Act: A Plan” (1997) 15 Australian Bar Rev. 149 at 156 (citing *Radio 2UE Sydney Pty Ltd Stereo FM Pty Ltd* (1983) 68 FLR 70 at 72).

¹⁵⁰ Maureen Brunt, “The Australian Antitrust Law After 20 Years – A Stocktake” in David K. Round, ed., *The Australian Trade Practices Act 1974* (1994) 483 at 509 (quoting *The Hilmer Report* (National Competition Policy Review (1993)) at 39).

¹⁵¹ Allan Fels, “The Trade Practices Act 1974 – Twenty Years On” (1994) 16:2 Competition and Consumer L.J. 1 at 4.

Despite the availability of significant fines, it is noteworthy that the Commission spent \$12 million on litigation in 1999-2000 in order to secure only roughly \$14 million in penalties against companies that were found to have contravened the Act.¹⁵²

(a) Authorizations

Under s. 88 of the Act, the ACCC has the power to grant “authorizations” to “make” or “give effect to” agreements that would or might be contrary to Part IV of the Act, including agreements that substantially lessen competition and even price fixing agreements falling within the *per se* prohibitions. Authorization has the effect of insulating successful applicants from legal action by the ACCC or any other party. At the ACCC’s discretion, authorizations may be granted subject to conditions, undertakings¹⁵³ and time-limitations.¹⁵⁴ Authorizations are generally only available where the agreement has not yet been concluded. Specifically, unless the parties make the agreement subject to a condition that the provisions will not come into effect until an authorization is granted and an application is made to the ACCC, an agreement that “has been made” or an “understanding has been arrived at” before the ACCC makes a determination in respect of the application, is not eligible for an authorization.¹⁵⁵

The issue of delay that has plagued the European Community regime appears to have been avoided under the Australian legislation through the imposition of a fixed deadline within which the ACCC must grant or deny an authorization. Subject to certain minor exceptions, the ACCC has four months in which to grant or refuse an authorization, failing which, at the expiry of this period, it is deemed to have granted the authorization.¹⁵⁶ Statistics specific to the authorization of competitor collaborations under the Act are unavailable. Nevertheless, global statistics relating to both mergers and anti-competitive conduct found in the ACCC’s 1999-2000 *Annual Report* are available. In 1999 - 2000, 160 authorization applications were subject to consideration by the ACCC. Of these, 78 authorization applications were carried forward from the previous year, while 82 were new applications. Over a 12 month period ending June 30, 2000, seven applications were withdrawn and 72, or roughly 45% of the total applications subject to ACCC consideration, were decided.¹⁵⁷ In assessing these figures, however, it should be noted that the *Report* does not reveal the proportion

¹⁵² Australian Competition & Consumer Commission, *Annual Report 1999-2000* at 2.

¹⁵³ *See* s. 87B.

¹⁵⁴ *See* ss. 90(3) and 91(1).

¹⁵⁵ *See* s. 88(12).

¹⁵⁶ *See* s. 90(10A).

¹⁵⁷ *Ibid* at 45.

of decided applications that fell into the “carried forward” category. Nor does it indicate the average processing time for an application.

Two different tests govern the ACCC’s decision to grant an authorization, the first resembles the comparative inquiry mandated by the American rule of reason standard. In the case of agreements and covenants that may substantially lessen competition, the ACCC is not permitted to grant an authorization unless it is satisfied that the proposed agreement would or is likely to result in a net benefit to the public (*i.e.*, benefit in excess of detriment due to any resultant lessening of competition).¹⁵⁸ A causal relationship between the claimed public benefit and the agreement must be shown to exist.¹⁵⁹ The applicant is not required, however, to establish that the benefit would not otherwise be available, but for the impugned agreement.¹⁶⁰ On a practical note, Adhar suggests that the burden on applicants is a heavy one.¹⁶¹ In fact, between 1974 and 1983 only 1.65% of authorization applications were granted.¹⁶²

Eligible “benefits to the public” have been defined broadly by the ACCC and the Australian Competition Tribunal. Unlike the inquiry under the *Sherman Act*, the ACCC and Tribunal are not limited to economic considerations, but may also examine a number of non-economic factors, such as the following:

- fostering business efficiency, especially when this results in improved international competitiveness;
- industry rationalisation resulting in more efficient allocation of resources and in lower or contained unit production costs;
- expansion of employment or prevention of unemployment in efficient industries or employment growth in particular regions;
- promotion of industry cost savings resulting in contained or lower prices at all levels in the supply chain;

¹⁵⁸ See ss. 90(6) and (7).

¹⁵⁹ Rex J. Adhar, “Authorisation and Public Benefit Under the Commerce Act 1986: Some Emerging Principles” (1988) 16 Australian B.L.R. 128 at 142.

¹⁶⁰ *Ibid* at 143.

¹⁶¹ *Ibid* at 147.

¹⁶² See Warren Pengilly, “Comparative Approaches to the Enforcement of Antitrust Laws Against Price-Fixing Arrangements (with Special Emphasis on the Lessons Learned from the Antitrust Law and Enforcement in Australia)” (1983) 28 Antitrust Bulletin 882 at 884 and 917.

- promotion of competition in industry;
- promotion of equitable dealings in the market;
- growth in exports;
- development of import replacements;
- economic development, *e.g.*, of natural resources through encouraging exploration, research and capital investment;
- assistance to efficient small business, *e.g.*, guidance on costing and pricing or marketing initiatives which promote competitiveness;
- industrial harmony;
- improvement in the quality and safety of goods and services and expansion of consumer choice; and
- supply of better information to consumers and business to permit informed choices in their dealings.¹⁶³

On the breadth of the “relevant considerations” under the authorization procedure, Duns confirms that “[n]o attempt has been made to limit consideration of benefits to what might be considered directly economic benefits and certainly not to efficiency criteria”.¹⁶⁴ However, in practice, according to Duns, economic analysis dominates the authorization process under the Act, although there are a number of examples where the ACCC or the Tribunal have given weight to non-efficiency factors.¹⁶⁵

Further, where the analysis of the foregoing non-economic factors reveals a detriment, rather than a benefit, these factors may be considered in determining the magnitude of the anti-competitive harm produced by an impugned agreement. It should be noted that the task of evaluating whether the public benefits flowing from proposed anti-competitive agreements does not rest with the courts, which under the Australian regime are charged with applying the foregoing legislative prohibitions, but with the ACCC. The courts consider only the purpose and effect – actual, likely or deemed –

¹⁶³ Jones, *supra* note 29.

¹⁶⁴ Duns, *supra* note 147 at 256 (quoting *Queensland Co-operative* at 17,242: a public benefit may constitute “anything of value to the community generally, any contribution to the aims pursued by the society”).

¹⁶⁵ See Duns, *supra* note 147 at 260 and 262.

of the relevant agreement on competition; their task does not extend to assessing any other effects, efficiency-enhancing or otherwise, of the impugned agreement. The notification and authorization process before the ACCC constitutes the institutional mechanism for ensuring that net pro-competitive competitor collaborations are not deterred.¹⁶⁶

Authorizations are subject to variation, revocation and/or the substitution of a replacement authorization by the ACCC where, for example, the person to whom the authorization was granted has failed to comply with a condition thereof or there has been a material change in circumstances.¹⁶⁷ Determinations by the ACCC to grant, vary, revoke or substitute authorizations are also subject to review by the Australian Competition Tribunal (the “Tribunal”) under s. 101 at the instance of any “dissatisfied person” having a “sufficient interest” in the determination in question.

VIII. NEW ZEALAND

The *Commerce Act* (1986) (the “Act”), reflects New Zealand’s adoption, albeit modified, of the Australian competition law regime, in furtherance of the governments’ pledge, as part of the 1983 Closer Economic Relations Treaty, to harmonize their respective competition legislation.¹⁶⁸ As such, the general approach and basic elements of the *Commerce Act* are very similar to those reviewed above in respect of Australia’s *Trade Practices Act*.

(a) **Substantive Provisions**

Like the Australian *Trade Practices Act*, the *Commerce Act* combines a general prohibition, specific *per se* proscriptions and an authorization or exemption scheme. The general prohibition is found in section 27 which declares contracts, arrangements or understandings the purpose, effect or likely effect of which is to substantially lessen competition in a market, or which attempt to so lessen competition, illegal and unenforceable.¹⁶⁹ A copy of the relevant provisions is attached at Schedule “VI”.

Sections 30 and 34 make “price fixing” agreements *per se* illegal. Under s. 30, agreements among competitors to “fix” the prices for goods or services are deemed to substantially lessen competition. “Price fixing” is defined broadly by s. 30 to include the fixing, controlling or maintaining the price of goods or services or any discount, allowance, rebate, or credit in relation to goods or services. According to the Commission, s. 30 is likely to catch agreements to:

¹⁶⁶ See Karen Yeung, “Quantifying Regulatory Penalties: Australian Competition Law Penalties in Perspective” (1999) 23 Melbourne U. L.R. 444 at 466.

¹⁶⁷ See ss. 91B(3) and 91C(3).

¹⁶⁸ Adhar, *supra* note 159 at 129.

¹⁶⁹ See <http://www.comcom.govt.nz/acts/comact/3restrictive.cfm>.

- create a price range;
- create a price or discount formula or system;
- set credit and rebate levels;
- set prices or discount levels; or
- control the elements that contribute to prices.¹⁷⁰

As with the Australian statute, the *per se* prohibition found in s. 30 is subject to three exemptions: joint ventures (s. 31), recommended price (s. 32) and joint buying and advertising arrangements (s. 33). However, in all three of these cases, the parties' agreement remains subject to the general prohibition found in section 27 against agreements which have as their purpose or effect the substantial lessening of competition.¹⁷¹

Under the Act, the Commerce Commission (the "Commission") may also obtain an injunction restraining conduct as described above¹⁷² or negotiate administrative settlements resulting in signed undertakings.¹⁷³ Further, the Commission, as well as private plaintiffs are entitled to bring suit in the High Court of New Zealand against those allegedly in breach of the statute. Acts or omissions contrary to the above prohibitions are punishable by fines of up to \$5 million (approximately Cdn. \$3.2 million) for a corporation and \$500,000 in the case of individuals.¹⁷⁴ However, as of August 1998, the highest penalty imposed under Act totalled only \$300,000 or 6 per cent of the \$5 million statutory maximum fine which may be imposed on corporations that have contravened the Act.¹⁷⁵ The Commission has expressed concern, from both a deterrence and an enforcement standpoint, about the courts' reluctance to impose significant penalties, relative to the costs incurred by firms in defending an action brought by the Commission.¹⁷⁶ It notes that the small size of court-awarded

¹⁷⁰ *Ibid.*

¹⁷¹ See www.comcom.govt.nz/acts/comact/3restrictive.cfm.

¹⁷² See s. 81.

¹⁷³ *Ibid.*

¹⁷⁴ *Ibid*; see s. 80. It should be noted that recently proposed amendments to the Act would increase the maximum corporate fine to \$10 million, introduce an alternative maximum penalty equal to three times the value of the illegal gain and clarify the availability of exemplary damages in private actions. See OECD Annual Report on Competition Law and Policy - New Zealand (1999-2000) available at <http://www.oecd.org/daf/clp/annrep.htm>.

¹⁷⁵ *Ibid* at 275.

¹⁷⁶ *Ibid.*

penalties has hindered it in penalty negotiations with defendants. The Commission also suggests that, to this time, courts have not set penalties at deterrent levels. As regards the appropriate starting point, the Commission maintains that:

To be effective deterrents should eliminate any profit incentive to engage in illegal activity ... includ[ing] taking into account the expected future net gains from the contravention, and the probability of detection and prosecution.

At times it is totally appropriate for penalties to be far higher than the actual gain made by the firms involved.

... [E]xpected gains are likely to be higher than the profits made up to the time when the contravention was detected; and in cases which are difficult to detect, such as hard core conspiracies, the optimal deterrent penalty would be some multiple of the expected illegal gain.

... for the civil standard under the Act, a suitable proxy would be a range of five per cent to 40 per cent of turnover for a minimum one year.¹⁷⁷

Pointing to the “overwhelmingly positive” experience in the U.S. from a compliance perspective, the Commission also advocates the inclusion of criminal sanctions under the Act.¹⁷⁸

(b) Authorisations and Exemptions

As with the Australian statute, the New Zealand regime provides for “authorisations” for agreements which contravene the above provisions, even including those agreements which fall within the *per se* prohibition against price-fixing.¹⁷⁹ As a general rule, such authorisations are available only where the impugned agreement has not yet been concluded.¹⁸⁰ However, agreements may be authorised, despite having been already concluded, so long as they contain an exclusionary provision delaying their force and effect until an authorisation is secured. It should also be noted that the Commission’s jurisprudence establishes that the “mere making of an application [for an authorisation] is not

¹⁷⁷ *Ibid* at 275-76.

¹⁷⁸ *Ibid* at 276; *see also* Stephen Corones, “Penalties for Price-Fixing: A Built-In Feature of How we do Business in Australia?” (1996) 24 Australian Business L. Rev. 160 (advocating use of criminal sanctions to punish serious contraventions of Part IV of the *Trade Practices Act*).

¹⁷⁹ *See* s. 61(6) [“or is deemed to result therefrom”]; *see also* Adhar, *supra* note 159 at 131 (citing *Re New Zealand Vegetable Growers Federation*, Unreported, 9 July 1987, no. 206).

¹⁸⁰ *See* s. 59.

necessarily an admission that the [agreement in question] is one to which section 27 or other appropriate section applie[s]”.¹⁸¹

The Commission is not entitled to grant an authorisation unless it is satisfied that an agreement will in all the circumstances result, or is likely to result, in a “net public benefit”.¹⁸² Like the American model, the Commission must undertake a form of rule of reason review where the benefit enuring to the public from the impugned agreement is weighed against its anti-competitive effects. Significantly, the Act does not identify or define those considerations which are properly examined in assessing the benefit to the public. Consequently, in *Weddel*,¹⁸³ the Commission gave the phrase “public benefit” a broad and liberal interpretation: “The Act is worded broadly and there appears to be no limitation as to the nature of the public benefit which may be claimed ... A benefit is something of value to the public”. Further, Adhar notes that it “has been stressed that notwithstanding the importance given economic efficiency through the promotion of competition, the types of public benefit are not confined to economic benefits”.¹⁸⁴ To date, accepted “benefits to the public” have included:

- productive efficiencies;
- economies of scale;
- cost savings;
- lower unit wage costs;
- enhanced job security;
- increased utilization of New Zealand resources; and
- improved road safety.¹⁸⁵

A former Chairman of the Commission suggested that eligible public benefits may also include regional development, enhancement of work skills and employment opportunities, the interests of employees and “any other effect aiding the well-being of the people of New Zealand” (*e.g.*, freedom

¹⁸¹ *Weddel Crown* Unreported, 22 July 1987, no. 205 at 10 (quoted in Miriam R. Dean, “Collective Pricing - A Practical Guide to Section 30 of the Commerce Act 1986” (1990) 20 Victoria University of Wellington L.R. 1 at 19). [hereinafter *Weddel*]

¹⁸² *See* ss. 61(6).

¹⁸³ *Supra*, note 181 at para. 25(ii)-(iii).

¹⁸⁴ Adhar, *supra* note 159 at 139.

¹⁸⁵ Adhar, *supra* note 159 at 139.

of the press).¹⁸⁶ As with the Australian regime, the task of evaluating the public benefits from proposed anti-competitive agreements does not rest with the High Court of New Zealand, which is charged with applying the foregoing legislative prohibitions, but with the Commission. The Court considers only the purpose and effect – actual, likely or deemed – of the relevant agreement on competition; its task does not extend to assessing any other effects, efficiency-enhancing or otherwise, of the impugned agreement. The notification and authorisation process constitutes the institutional mechanism for ensuring that net pro-competitive competitor collaborations are not deterred.

Pursuant to s. 61, the burden throughout the authorisation process is on the applicant to establish a “causal nexus” between the agreement and the alleged public benefit.¹⁸⁷ While the applicant is not required to establish that the benefit would not otherwise be available, but for the impugned agreement, the Commission will take into account evidence that the benefit in question could be achieved through less harmful means in assessing the weight to be given to the benefit claimed.¹⁸⁸ Further, any detriment flowing from a claimed benefit will be netted from the benefit before the ultimate weighing takes place.¹⁸⁹ From an evidentiary standpoint, the Commission has stated the following guidelines as to proof:

- the need for specific reasoned, as opposed to conclusory or general, claims;
- the need for evidence to show that the claimed beneficial effects are likely to eventuate;
- demonstration that the benefits will actually flow from the proposal or conduct;
- demonstration that the New Zealand public will benefit;
- the desirability of demonstrating that sections of the public which will benefit;
- the need, where possible, to provide some quantification of the benefit, whilst recognising the difficulty of quantifying the benefit in monetary terms;

¹⁸⁶ *Ibid.*

¹⁸⁷ *Ibid* at 142.

¹⁸⁸ Adhar, *supra* note 159 at 143.

¹⁸⁹ *Ibid* at 146.

- the irrelevancy of motives or objectives, except to assist in ascertaining where the benefit is likely to flow.¹⁹⁰

On a practical note, at least in the early stages of the Act's operation, authorisations were granted sparingly, with the Commission refusing applications in the first five of six cases. Adhar suggests that, like in Australia, the burden on applicants is a heavy one.¹⁹¹ In fact, the Commission received no restrictive trade practices authorisation applications in 1999-2000. Further, the Commission's annual report for that year reveals that since 1996, only seven applications have been received – four in 1996-97 and three in 1998-99.¹⁹²

IX. SOUTH AFRICA

(a) Substantive Provisions

Similar to the Australian and New Zealand statutes, South Africa's recently enacted *Competition Act* (the "Act") includes a combination of specific *per se* prohibitions, a general prohibition for agreements that substantially lessen competition and a system for granting authorizations and exemptions. Horizontal agreements to price fix, allocate markets or customers and rig bids are *per se* illegal.¹⁹³ For all other agreements, the Act requires a rule of reason analysis to determine whether the agreement in question substantially prevents or lessens competition in a market and whether the pro-competitive benefits flowing from the agreement (*i.e.*, technology, efficiency or other pro-competitive gains) outweigh the resulting anti-competitive harm.¹⁹⁴

For violations of the *per se* prohibitions, the Competition Tribunal may impose administrative fines. Such fines "may not exceed 10% of the firm's annual turnover in the Republic and its exports from the Republic during the firm's preceding financial year".¹⁹⁵ For violations of the general prohibition, the Tribunal may order that the agreement is void or restrain the parties from engaging in any practice that is contrary to the Act. The Commissioner of Competition (the "Commissioner") may

¹⁹⁰ *Ancor Ltd./N.Z. Forest Products Ltd.* (unreported, 21 August 1987, no. 208 at para. 53) (quoted in Adhar, *supra* note 168 at 144); *see also Goodman Fiedler Ltd/Wattie Industries Ltd.* (1987), 6 N.Z.A.R. 446 at 449 (quoted in Adhar, *supra* note 159 at 144).

¹⁹¹ Adhar, *supra* note 159 at 147.

¹⁹² *Report of the Commerce Commission for the Year Ended 30 June 2000* at 34.

¹⁹³ *See* s. 4(1)(b).

¹⁹⁴ *See* s. 4(1)(a); Competition Commission South Africa, *General Brochure - 2000* available at <http://www.compcom.co.za/publications/LatestPublications.asp>.

¹⁹⁵ *See* s. 61(2).

also negotiate and obtain consent orders.¹⁹⁶ Notably, a consent order may, if the complainant agrees, include an award of damages to the latter.

(b) Exemptions

Like Australia and New Zealand's respective regimes, the Act provides a form of authorization, termed "exemption".¹⁹⁷ However, unlike the former two regimes, where authorization performs a task similar to the American rule of reason standard (albeit with reference to a broader set of considerations), the South African exemption is concerned almost purely with the public policy (*e.g.*, social and economic democratization), as opposed to the economic implications of an impugned agreement. This is not surprising, given that the Act's objectives include diversification of ownership in favour of members of historically disadvantaged communities, promotion of the social and economic welfare of South Africans, and the creation of new employment opportunities.¹⁹⁸ An exemption may be granted, with or without conditions,¹⁹⁹ where an agreement that is otherwise in breach of the Act is necessary to attain one or more of the following objectives:

- maintenance or promotion of exports;
- promotion of the competitiveness of small businesses or firms controlled or owned by historically disadvantaged persons;
- changing the productive capacity to stop decline in an industry; and
- maintaining economic stability in an industry designated by the Minister of Trade and Industry.²⁰⁰

Notably, the Act is silent as to whether, assuming that an agreement is in fact shown to be required to achieve one of the foregoing objectives, the Commission may nevertheless decline to grant an exemption because, for example, the nature and magnitude of the agreement's contribution to the realization of the one of the foregoing objectives is outstripped by its anti-competitive harm. As with the other two models, an exemption is subject to being revoked where it is determined that it was granted on the basis of false or incorrect information, a condition imposed by the Commission has not been fulfilled or the reason for granting the exemption has ceased to exist.²⁰¹ Like the New

¹⁹⁶ See s. 63.

¹⁹⁷ See s. 10 (Part C - Exemptions from Application of Chapter)

¹⁹⁸ See s. 2.

¹⁹⁹ See s. 10(2)(b).

²⁰⁰ See s. 10(3)(a) and (b); *Ibid.*

²⁰¹ See s. 10(5).

Zealand statute, the Act does not set any time limit for determination of an application for an exemption.

X. ADVANTAGES AND DISADVANTAGES OF THE AUSTRALIAN, NEW ZEALAND AND SOUTH AFRICAN REGIMES

Similar to the American regime, these regimes are all subject to the same generic pros and cons of *per se* rules and the rule of reason standard.

In relation to *per se* illegality, Warner et al. assert that in applying their respective deeming provisions,

Australian and New Zealand courts have apparently experienced the same difficulties as American courts have had in applying the *per se* illegal rule. In at least some cases, Australian courts have been unable to apply the deeming provision to price-fixing arrangements in such a way as to avoid inquiring into the surrounding circumstances of those arrangements.²⁰²

However, the authors leave unanswered the more important question of whether the detailed and precise (relative to section 1 of the *Sherman Act*) statutory language of the relevant Australian provisions has, to any appreciable degree, reduced the relative frequency with which Australian courts have been confronted with the “characterization” problem that plagues their American counterparts. South Africa’s *Competition Act* which came into force on September 1, 1999 has not yet been the subject of relevant academic commentary or critique. There is, however, no reason to believe, based on statutory language or otherwise, that the challenges and difficulties experienced in the United States, New Zealand, and Australia will be avoided in South Africa. In fact, assuming that the magnitude of the characterization problem is a direct function of drafting precision, it is arguable that the South African statute, which identifies the restrictive horizontal practices it proscribes on a *per se* basis in general terms, will present significant problems from a characterization perspective.

As regards the rule of reason, it appears that non-economic considerations are relevant and admissible in all three regimes, be it as part of a review resembling the American rule of reason analysis (*see* Australia and perhaps New Zealand) or as a condition precedent for the issuance of a “public policy” exemption (*see* South Africa). The South African public policy exemption, in particular, is uncharted territory as far as the validity and importance of non-economic considerations is concerned. It is arguable that the South African exemption, which applies to all manner of restrictive horizontal practices, reflects a legislative judgment that South Africans are or should be willing to tolerate supra-competitive prices for goods and services as the cost of advancing economic and social democratization and enfranchisement. It remains to be seen how broadly the South

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Warner et al., *supra* note 70 at 713. Note, however, that the authors do not cite any cases in support of this assertion.

African Commission will construe its exemption power. More generally, in respect of all three mechanisms, it is arguable²⁰³ that the absence of a principled basis for courts to accept or reject non-economic considerations will lead to inconsistency and unpredictability in the law. Also, multiple objectives and, in particular, the combination of economic and non-economic objectives in a single policy tool is a recipe for policy failure. As the New Zealand Commission has observed: “It is not easy to make a judgment between two public policies”.²⁰⁴ This is particularly so where the public policies being compared and weighed against one another are different in kind.

Finally, in relation to authorizations/exemptions, the failure of the New Zealand and South African statutes to limit the time available to their respective Commissions for determination of an application may result in businesses being placed in a legal limbo as they await approval. This is of course creates uncertainty, thereby undermining effective business planning.

XI. FOREIGN APPROACHES TO HORIZONTAL RESTRAINTS SUMMARIZED

Although each of the jurisdictions examined in this report have adopted prohibitions against horizontal restraints, there are important differences in relation to the source and nature of the relevant proscription. Section 1 of the *Sherman Act* states a broad, standardless prohibition against restrictive horizontal trade practices. Due to the absence of specific statutory proscriptions within section 1, the scope and limits of the prohibition are defined through judge-made rules. In contrast, New Zealand and Australia’s respective regimes employ both a general prohibition along with precise statutory *per se* prohibitions against price-fixing, as well as other forms of restrictive conduct. Similarly, Article 81 of the EC Treaty combines a general prohibition against agreements that have the purpose or effect of distorting competition, together with a non-exhaustive list of prohibited arrangements. Finally, the South African statute provides an exhaustive list of *per se* illegal arrangements as well as a general statutory prohibition against all other arrangements that have the effect of substantially preventing or lessening competition.

The various regimes also display important differences in relation to the standard used to determine whether an arrangement is prohibited. The American and South African regimes apply a *per se* rule to certain categories of arrangements and a rule of reason analysis to all other arrangements. As noted above, the EC Treaty prohibits arrangements that have the object or effect of distorting or restricting competition, but allows for the application of a full rule of reason analysis where parties have submitted a request for an exemption. Australia and New Zealand combine *per se* prohibitions with a general prohibition, subject to authorization, against arrangements that substantially lessen competition.

²⁰³ Please note that there is a dearth or complete absence of commentary and criticism in relation to the Australian, New Zealand and South African models.

²⁰⁴ *Amcor*, *supra* note 190 at para. 75 (quoted in Adhar, *supra* note 159 at 146). In that case, the Commission was asked to weigh the benefit of “utilization of resources and the flow-on effects” against the detriment to competition.

Only the United States lacks some form of notification, exemption or authorization system. The EC, South African, Australian and New Zealand models all have similar notification and authorization regimes which permit regulators to grant immunity to certain forms of pro-competitive arrangements, even for price-fixing or similar agreements. Subject to certain limited exceptions, these regimes also provide that applications for authorizations will be granted with prospective effect. The consequences of notification, authorization or exemption are significant in the four regimes with such a mechanism. As noted above, under the EC Treaty as well as the Australian, New Zealand and South African statutes, notification, authorization or exemption is the condition precedent for immunity from liability.

The basis upon which exemptions will be granted also varies among the various jurisdictions. Except in rare cases, the decision to grant or refuse an application for an exemption under the EC regime is based solely on economic considerations. In both Australia and New Zealand, economic and non-economic considerations are accepted as relevant to the determination of an application for authorization. In South Africa however, exemptions are granted or refused exclusively with reference to non-economic considerations. In determining whether an authorization may be granted under the EC, Australian, South African and New Zealand legislation, a rule of reason analysis is applied to determine the benefits and detriments of an impugned arrangement.

In terms of a dual-track approach, only the American regime provides the option of either criminal or civil review of impugned arrangements. As a general rule, the nature of the arrangement will govern whether the arrangement is subject to criminal or civil review. The other regimes examined in this report rely exclusively on a single-track civil review mechanism. However, under each of these single-track civil regimes, significant fines may be imposed which, although they do not carry the same social stigma as a criminal conviction, result in significant deterrence.

From a remedial perspective, the American and South African models have unique elements. The American regime alone authorizes the recovery of treble damages and provides for the incarceration of individuals convicted of criminal violation of the proscription against horizontal restraints. Similarly, only the South African statute contemplates the making of an order akin to specific performance (*i.e.*, directing a party found to have engaged in a prohibited practice to supply or distribute goods or services to another). Notably, all five regimes permit private enforcement of the prohibitions against competitor collaborations.

Our review also reveals the significant structural differences in the competition regimes of these jurisdictions. The United States has a dual criminal/civil regime which relies on adjudicative models of decision making, as opposed to the administrative decision makers which predominate in Europe, at least in respect of the granting of exemptions. Notably, it is these structural differences that are often the source of criticism in each jurisdiction. The American system is criticized for being expensive and uncertain, whereas the European system is criticized for being bureaucratic and slow. Canada has chosen a compromise between these two extremes.

XII. LESSONS FROM THE COMPARATIVE REVIEW

(a) Defining the Prohibition

The American experience under section 1 of the *Sherman Act* suggests that *per se* prohibitions provide an effective means of deterring and remedying hard-core cartel behaviour. In particular, it indicates that *per se* prohibitions are less costly to enforce and promise increased certainty and predictability. As noted above, the *per se* inquiry into whether the unlawful conduct has taken place at all – the sole question under a *per se* analysis – requires less time and expense, than the in-depth inquiry into competitive effects required under a rule of reason. Further, the *per se* rule’s categorical approach promises greater consistency and predictability in judicial decision-making and thus increased certainty for industry. In addition to the increased expense and time, as noted in respect of proposed amendments of the EC Treaty, utilizing a rule of reason analysis also runs the risk that competition rules may be set aside because of political considerations.

However, the U.S. experience also demonstrates the disadvantage of *per se* restrictions; namely, the inflexibility of such restrictions may result in the condemnation of beneficial competitor collaborations. As noted by Warner et al., “[even] a *per se* criminal prohibition for naked price-fixing cannot be formulated with complete precision, and will unavoidably target potentially pro-competitive arrangements”.²⁰⁵ Further, the application of a *per se* rule involves a threshold inquiry, namely whether the impugned agreement may be properly characterized as falling within the *per se* prohibition in question. The cost advantages, both to the administration of justice and litigants, of the *per se* rule are, of course, lost if a full-blown or even a partial rule of reason analysis is required prior to condemning an agreement as *per se* illegal. Further, the characterization problem has negative consequences for the desired certainty and predictability of the *per se* rule. In sum, the efficiency and clarity of the American *per se* approach may be, to an unspecifiable degree, more apparent than real.

Our comparative review suggests that the inefficiency and uncertainty resulting from the above-mentioned characterization problem may be reduced by a statutory provision that specifically and precisely identifies (and, to the extent possible, describes) the types of arrangements that are proscribed on a *per se* basis, such as section 45A of the Australian *Trade Practices Act* and section 30 of New Zealand’s *Commerce Act*. Our review also indicates that the overbreadth that results from the inflexibility of *per se* prohibitions can be limited by providing some means of exempting the limited class of agreements that, strictly speaking, violate these prohibitions, but which, due to their potentially pro-competitive benefits, should not be condemned summarily, if at all.

One option, based on the American model, is simply to review impugned arrangements thought to be potentially pro-competitive using a rule of reason analysis. Under a rule of reason analysis, the Tribunal (or the courts) would have the flexibility required to differentiate pro-competitive, welfare enhancing collaborations from those which are not. However, as noted by the European

²⁰⁵ Warner et al. *supra* note 70 at 716.

Commission and other commentators, in rejecting a rule of reason approach to Article 81(1) of the EC Treaty, the rule of reason can only be implemented gradually through successive cases and, consequently, would not provide a quick answer to the Competition Bureau's enforcement concerns. Further, a rule of reason approach arguably leads to greater uncertainty because, in each case, a complex market assessment and analysis would have to be undertaken in order to determine whether the pro-competitive benefits of the impugned arrangement outweigh its anti-competitive effects. Of course, an analysis of this kind would also increase the time, cost and complexity of enforcement. Relatedly, because the evolution of the rule of reason analysis would be determined by the courts, its development would be difficult to predict and potentially inconsistent with the Commissioner's policy objectives.

A notification, authorization or exemption mechanism offers a second option and, as will be explained, one that avoids several of the shortcomings associated with the American approach to rule of reason analysis. As noted above, Article 81(3) of the EC Treaty provides a mechanism of this kind, as do the Australian and New Zealand statutes. Like the American model, a full rule of reason analysis is applied in considering whether an exemption should be granted. However, in contrast to the American model, these mechanisms truly exempt arrangements from statutory prohibitions, *per se* or otherwise. Under Article 81(3) of the EC Treaty, s. 88 of the *Trade Practices Act* and ss. 58 and 61 of the *Commerce Act*, enforcement authorities are given a broad discretion to immunize arrangements based on the particular circumstances of each case. In further contrast to the American model, it is the relevant enforcement agency, and not the courts, that has exclusive authority (at least at first instance) to authorize or exempt an agreement that would otherwise contravene a statutory prohibition. This administrative model for exemptions avoids the problems identified with the US system, including the costs and uncertainty of purely adjudicative model. Notably, industry participants in the EC have expressed support for the existing notification and exemption regime based on the legal certainty it provides.

However, based on the experience in the EC, we note that, to maximize its effectiveness, a notification or authorization regime must not involve a cumbersome or lengthy procedure. In the EC, a backlog of notifications has produced significant delays which may have discouraged parties from pursuing potentially pro-competitive alliances. This appears to be the result of an over-inclusive notification regime which, as a result of Article 81(2), voids all forms of agreements that fall within the broad scope of Article 81(1) and for which no notification has been submitted. As outlined below, a more manageable notification system would likely result if only those agreements which contain price-fixing or other similar provisions required notification to retain provisional validity.

(b) Dual Track Regime

The U.S. experience demonstrates the advantages of maintaining both a civil and criminal review process for competitor collaborations. Deterrence is the least expensive method of enforcement and criminal penalties provide a powerful deterrent. Also, criminal sanctions are unquestionably appropriate for hard-core cartel behaviour that is, by definition, harmful to consumers. As noted

above, the effectiveness of criminal penalties from a compliance perspective has prompted the New Zealand Commerce Commission to advocate the inclusion of criminal sanctions within the New Zealand statute. Further, as stated by the Assistant Attorney General, in describing the core mission of the Department of Justice - Criminal Antitrust Enforcement division:

Price fixing and other criminal violations of the Sherman Act are the antithesis of open competition. They are criminal precisely because they raise prices, they lower quality and they reduce choice. In a narrow sense, as I have said, they take money from Americans. In a broader sense – and equally important – criminal antitrust violations tear at the economic fabric of our society. Antitrust crimes are antisocial, just as fraud and robbery are antisocial. A society that tolerated such crimes could no longer maintain its economic freedom, any more than a society that tolerated murder could long maintain its physical freedom.²⁰⁶

On the other hand, as noted above, the DOJ also recognizes that where a legitimate disagreement exists as to whether the pro-competitive benefits of an arrangement outweigh its anti-competitive effects, criminal prosecution is inappropriate. In those cases, it has acknowledged that civil review may be preferable to criminal review, even for arrangements that have customarily been labeled *per se* illegal.²⁰⁷ In the same vein, noting that reasonable disagreements often exist about the net competitive effect of competitor collaborations, Ross has remarked that “it seems difficult to support the threat of criminal prosecution with the possibility of imprisonment and accompanying social stigma” in respect of any and all horizontal restraints.²⁰⁸ It must also be remembered that the criminal law process, with its stringent burden of proof, may entail high cost and delay to the disadvantage of enforcers and those whose conduct is subject to prosecution.

(c) **Social and Other Non-Economic Considerations**

To a greater or lesser extent, the European, Australian, New Zealand and South African models admit social and other “non-economic” considerations (*i.e.*, considerations unrelated to economic efficiency) as relevant to the determination of whether an exemption or authorization should be granted. For example, the ACCC has expressly stated that in determining whether an arrangement is to be authorized, it will have regard to non-economic benefits, such as “employment growth in particular regions” or “industrial harmony”. As discussed below, the inclusion of such non-economic factors arguably leads to inconsistency and unpredictability in the law, due to the absence of any principled basis for accepting and rejecting factors of this nature. Furthermore, while recognizing that, in its present form, s. 45 of the *Competition Act* expressly admits a narrowly cast

²⁰⁶ Anne K. Bingman and Gary R. Spratling, “Criminal Antitrust Enforcement” (February, 1995) available online at <http://www.usdoj.gov/atr/public/speeches/95-02-23.htm>.

²⁰⁷ See *Antitrust Division Manual*, *supra* note 80.

²⁰⁸ Ross, *supra* note 7 at 867.

exception for arrangements relating only to the export of products from this country,²⁰⁹ we believe that the unrestricted introduction of non-economic factors into the s. 45 analysis would mark a major policy shift that risks politicizing competition policy in this country. We also note the absence, among Canadian competition policy commentators, of any support for an expanded rule of reason analysis which would include non-economic considerations. It may be however that increased globalization may place some pressure on competition policy to balance the global competitiveness of Canadian businesses, against short term anticompetitive effects in domestic Canadian markets.

(d) The Core Elements for an Amended Section 45

The foregoing review supports the following attributes and core elements for an amended section 45:

- the section should prohibit hard-core cartel behaviour through a *per se* criminal provision;
- the section should precisely enumerate the types of arrangements that are subject to the *per se* prohibition;
- arrangements that do not fall within the *per se* prohibitions would be subject to a full rule of reason analysis pursuant to a civil provision; and
- parties would be able to seek an exemption from the *per se* criminal provisions on the basis that the pro-competitive benefits of the potentially criminal arrangement outweigh its anti-competitive effects.

XIII. CRITIQUE OF SECTION 45: THE CASE FOR REFORM

There are certain notable differences between section 45 of the *Competition Act* and the other regimes described above. For example, unlike the rule of reason analysis applied under section 1 of the *Sherman Act* and Article 81(3) of the EC Treaty, section 45 includes only a “partial” rule of reason. As the Supreme Court of Canada confirmed in *R. v. Nova Scotia Pharmaceutical Society et al.*:

Section 32(1)(c) [now section 45] lies somewhere on the continuum between a *per se* rule and a rule of reason. It does allow for discussion of the anti-competitive effects of the agreement, unlike a *per se* rule, which might dictate that all agreements that lessen competition attract liability. On the other hand, it does not permit a full-

²⁰⁹ See ss. 45(5) and (6); see also s. 49(2)(a).

blown discussion of the economic advantages and disadvantages of the agreement, like a rule of reason would.²¹⁰

Further, unlike the *Sherman Act*, as interpreted and applied by the U.S. judiciary, there are no *per se* prohibitions implied under section 45. Under Canadian law, it is insufficient for the Crown to establish that the proscribed agreement was entered into or given effect. Rather, as part of the *actus reus* of the offence, the Crown must establish that if the agreement were carried out it would likely lessen competition unduly in a relevant market. This may be contrasted with sections 47 and 49 of the *Competition Act* which create *per se* offences for bid-rigging and agreements between federal financial institutions respectively. In addition, section 45 contains two separate *mens rea* requirements:

- (i) a subjective *mens rea* requirement - the accused must have had a subjective intent to enter into the impugned agreement and had knowledge of its terms; and
- (ii) an objective *mens rea* requirement - the accused must have known, or ought to have known, that the effect of the agreement would be to lessen competition unduly.²¹¹

In relation to the objective *mens rea* element, in *R. v. Nova Scotia Pharmaceutical Society et al.* Gonthier J. stated that:

In order to satisfy the objective element of the offense, the Crown must establish that on an objective view of the evidence adduced the accused intended to lessen competition unduly. ... [I]t would be a logical inference to draw that a reasonable business person who can be presumed to be familiar with the business in which he or she engages would or should have known that the likely effect of such an agreement would be to unduly lessen competition.²¹²

Academic commentators have criticized section 45 on the basis that it is vague and economically unsound. For example, in “Rethinking Price Fixing Law”, Warner et al. describe the disadvantages of the current regime as follows:

The current prohibition is underinclusive because it can allow manifestly anti-competitive arrangements to escape condemnation. ...the current prohibition, which requires the Crown to prove on a criminal burden of proof that an arrangement has lessened competition “unduly” can allow price-fixers to escape conviction...

²¹⁰ [1992] 2 S.C.R. 606 at 650.

²¹¹ Davies, Ward & Beck, *Competition Law of Canada* (2000) at 8-7.

²¹² *Supra* note 210 at 660.

At the same time, the current prohibition is overinclusive because it subjects all horizontal arrangements to criminal prohibitions and casts a shadow over many arrangements that may potentially increase welfare. Apart from the obvious price-fixing case, the welfare effects of many horizontal arrangements are ambiguous, and arrangements with ambiguous welfare effects should not be deterred and do not require criminal sanctions.²¹³

The record of enforcement of section 45 also supports the need for reform. In “Beyond Merriment and Diversion: The Treatment of Conspiracies under Canada’s Competition Act”,²¹⁴ Robert Jackson and Harry Chandler examine the historical record of enforcement of s. 45. As noted above, of the 51 cases brought under section 45 since 1980, 29 of these cases resulted in guilty pleas. However, the most striking statistic from the report is that of the 22 contested cases under section 45, the Crown has succeeded in only three. Of the 17 cases involving acquittals or discharges, Jackson and Chandler report that 6 were due to a failure to establish the existence of an agreement and the remaining 11 were due to a failure to establish either that the arrangement unduly lessened competition or that the parties’ intended that the agreement should have this effect. This is of particular concern considering that all of these prosecutions involved hard-core cartel behaviour, such as agreements to fix prices or share markets. As Jackson and Chandler note:

A review of all the cases listed in Appendix I reveals that every single case involved blatant hard-core anticompetitive behaviour - primarily price-fixing, market-sharing or bid-rigging. None involved what are sometimes called strategic alliances, for example, competing firms entering into partnerships to facilitate the transfer of knowledge, skills and technologies; to enter new markets at a lower cost and with less risk; to enhance innovation and growth; to bring products to the market more quickly; to overcome legal or trade barriers; to realize economies of scale and scope; or to be more competitive against larger rivals with wider product lines.²¹⁵

They conclude that “the results suggest that the ‘undueness’ element poses the greatest obstacle to achieving convictions under section 45”.²¹⁶

XIV. PROPOSALS FOR REFORM

(a) Statutory Objectives

²¹³ Warner et al., *supra* note 70 at 690-91.

²¹⁴ Available online at: <http://strategis.ic.gc.ca>.

²¹⁵ *Ibid* at 5-6 of 23.

²¹⁶ *Ibid* at 7 of 23.

In examining proposals for reform, we believe that any model proffered should be evaluated based on the extent to which it achieves the following objectives:

- consistent and cost-effective enforcement;
- certainty and predictability for both enforcement authorities and those whose conduct may be subject to scrutiny;
- flexibility, sufficient to permit differentiation between pro-competitive and anti-competitive competitor collaborations;
- adequate punishment of economically harmful collaborations without deterring efforts to develop new, pro-competitive cooperative arrangements; and
- harmonization of the treatment of competitor collaborations and mergers.²¹⁷

(b) Previously Proposed Models

Two prior legislative models for section 45 have been advanced. In “Rethinking Price Fixing Law”, Presley Warner and Michael Trebilcock propose a dual-track model (the “Trebilcock-Warner Model”) with four basic components: (a) a redefined criminal, *per se* prohibition that targets only naked (and covert) price-fixing arrangements; (b) an *ex ante* notification system which offers “immediate and permanent immunity from criminal liability”²¹⁸ to parties that notify the Competition Bureau “prior to the time at which the arrangement takes effect, or within 30 days of the execution of the arrangement”;²¹⁹ (c) a civil review process for notified arrangements which the Commissioner believes to be anti-competitive; and (d) collateral amendments to the Act, the purpose of which would be to adopt the procedural protections and devices available in relation to merger review in respect of the review of horizontal arrangements.

Under the Trebilcock-Warner model, immunity from criminal prosecution would not depend on the Commissioner’s acceptance of a notified arrangement, rather immunity would flow from notification itself. The authors reason that by making criminal immunity automatic upon notification, the delays and administrative burden that have been experienced in the EC Treaty system will be avoided.²²⁰ While notification forecloses criminal prosecution, under the Trebilcock-Warner Model the Commissioner would retain the right to pursue a civil remedy as against any notified arrangement it considered to be anti-competitive. Warner et al. propose that the merger review process be

²¹⁷ Ross, *supra* note 7 at 869-70.

²¹⁸ Warner et al., *supra* note 70 at 718.

²¹⁹ Warner et al., *supra* note 70 at 717.

²²⁰ Warner et al., *supra* note 70 at 719.

adopted for civil review of notified arrangements. For example, under the Trebilcock-Warner Model, notified arrangements would constitute reviewable practices, within the meaning of Part VIII of the Act, and the Tribunal would apply the standard of “substantial lessening or prevention of competition” found in s. 92 of the Act when reviewing an impugned, notified arrangement.²²¹ Relatedly, the efficiency defence in s. 96 of the Act would be available to parties defending a notified arrangement.²²² Finally, Warner et al. proposed that s. 36 of the Act be amended to declare all arrangements in violation of the criminal prohibition unenforceable and to proscribe private actions in respect of notified arrangements.

The model proposed under Bill C-472 is very similar to the Trebilcock-Warner Model. This Bill would have amended section 45 to include a criminal prohibition against collusive arrangements between one or more competitors that

... if implemented would or would likely have had the effect of

- (a) fixing, establishing, controlling or maintaining the minimum price of a product;
- (b) allocating any markets, territories, customers or sales for the product as between the person and the competitor;
- (c) boycotting a competitor or competitor’s suppliers or customers; or
- (d) preventing, eliminating, lessening or otherwise limiting the production or supply of a product.

All other arrangements would have been subject to review under a companion civil provision,²²³ pursuant to which the Commissioner would have been entitled to seek remedial orders from the Tribunal in relation to those arrangements which were shown to substantially prevent or lessen competition.²²⁴ Bill C-472 would also have created express exceptions to the prohibition for ancillary restraints and arrangements among participants who collectively did not hold more than 25% of the relevant market.²²⁵

²²¹ Warner et al., *supra* note 70 at 720.

²²² Warner et al., *supra* note 70 at 721.

²²³ *See* s. 79.1.

²²⁴ *See* s. 791.

²²⁵ *See* ss. 45(7)(d) and (e).

Like the Trebilcock-Warner Model, Bill C-472 provided for notification. However, the Bill C-472 notification regime differed from Warner et al.'s model in two ways. First, while it too provided for the notification of potentially criminal arrangements, the effect of which would have been automatic immunization from criminal prosecution, Bill C-472 did not require notification prior to entering into an arrangement.²²⁶ Instead, parties would have been entitled to notify and insulate themselves from criminal prosecution at any time. Second, the Bill provided for the issuance of clearance certificates, available only prior to entering into an arrangement and valid for three years, that would have had the effect of immunizing the notified arrangement from both civil review and criminal prosecution.²²⁷ In contrast, under the Trebilcock-Warner Model, notified arrangements, while immunized from criminal review, would have remained subject to civil scrutiny by the Tribunal, at the Commissioner's discretion.

(c) Concerns Raised by Previous Proposals

(i) “Between Competitors”

The criminal prohibition proposed by Bill C-472 offers a useful precedent. In fact, the criminal prohibition recommended below shares many of its features. We note, however, that, similar to the prohibition formulated by Warner et al., Bill C-472 proscribed only arrangements between competitors.²²⁸ In our view, this limitation is problematic for a number of reasons: First, the question of whether the parties to an arrangement are actual, or even potential, competitors imports a complex market definition exercise into what is meant to be a summary review process. In addition, the criminal prohibition under Bill C-472 would have been inapplicable to arrangements between potential competitors or parties in a vertical relationship. At the same time, we recognize that the economic presumption which supports the application of *per se* prohibitions to hard-core, cartel behaviour among competitors, namely, certainty concerning its anti-competitive effects, may not hold for arrangements between parties who are not competitors, with the result that there is a greater need to consider the net competitive effects of such arrangements in particular instances.

Limiting the prohibition to agreements between competitors is also inconsistent with each of the jurisdictions which are reviewed above. Specifically, Article 81(1) applies broadly to “agreements between undertakings [and] decisions by associations of undertakings”. Similarly, the Joint Guidelines defines the term “competitor” as “encompassing both actual and potential competitors”. Generally, Section 45 of the Australian *Trade Practices Act* applies to both actual and likely competitors. The New Zealand statute applies to “persons” generally, and specifically, to actual, likely or potential competitions in respect of price-fixing agreements. The *per se* prohibitions in the

²²⁶ See s. 45(7)(c).

²²⁷ See s. 79.2(2).

²²⁸ See s. 45(1); Warner et al., *supra* note 70 at 717.

South African statute apply to “parties in a legal relationship” and to “firms or associations of firms”.

(ii) Market Share Exception

The 25% market share exception found in section 45(7)(e) of Bill C-472 is unusual and merits comment. Section 45(7)(e) permits parties who are or have been engaged in hard-core cartel behaviour to avoid its application solely on the basis of their market presence, or lack thereof, irrespective of the effect of the conduct and of the level of concentration within the relevant market. To illustrate the pitfalls in focusing exclusively upon market share, reference may be made to an example reviewed in Ross’s paper. Ross states:

An example offered by Bork involves a cooperative advertising arrangement among a small number of retail pharmacists in a large city. To realize economies of scale in advertising, they agree to prepare a common advertisement and honour the prices listed. While this is no doubt (in part) an agreement to fix price, the arrangement can have no negative effect on competition (since the retailers together represent a tiny fraction of scales in the city) and will in fact be beneficial to the extent that it improves information in the market and lowers the cost of advertising.

In considering the application of the exemption that was proposed in Bill C-472 to the above example, if we assume that the pharmacists referred to in the above example collectively represent 25% of the market and the market is not heavily concentrated, with a significant number of similarly sized or larger competitors, then the proposed advertising arrangement will not have a significant impact upon competition and should not be subject to the *per se* prohibitions proposed in Bill C-472. However, if we assume that the proposed arrangement involves two pharmacies which collectively hold 25% of the market, with the remaining market share being held by a chain controlled by a single entity, the proposed arrangement would likely result in a substantial lessening of competition and further increase the risk of interdependent behaviour among these market participants.

Further, by way of comparison, the *de minimus* doctrine under EC law is inapplicable in the context of hard-core cartel behaviour. According to the *Commission Notice on Agreements of Minor Importance* (97/C 372/04),²²⁹ horizontal or vertical agreements which have the effect of fixing prices, limiting production or sales, sharing markets or sources of supply or, in the case of vertical agreements, conferring territorial protection on the participants or third parties cannot benefit from this exclusion regardless of the participants’ aggregate market share. The *de minimus* doctrine also has no application where the market is heavily concentrated, even if the participants’ respective market shares are small. Similarly, in *FTC v. Superior Court Trial Lawyers Association*,²³⁰ the United States Supreme Court confirmed that the absence of market power is no defence to *per se* illegality.

²²⁹ *Supra* note 41.

²³⁰ 493 U.S. 411 (1990).

In fact, none of the regimes discussed above contains any exception based exclusively upon market share. From a practical perspective, we also note that the application of this exception will likely require a full determination of the relevant market, thereby reducing the efficacy of the section 45 prohibitions.

For these reasons, we do not support a statutory market share exception. As an alternative, we recommend that a market share exception, if any, should be published as a guideline. The guideline-approach offers superior and important flexibility from a policy-making perspective.

(iii) Dual Track Model

The amendments proposed in Bill C-472 also would have gone a long way towards creating an effective, dual track model, while preserving criminal sanctions for hard-core cartel behaviour. However, we believe that two elements of the model require further review: (a) notification and the immunization of hard-core cartel behaviour; and, (b) the availability of rule of reason review for arrangements about to be entered into or given effect. These elements are considered below.

(1) Criminal Immunity

As noted above, the amendments proposed in Bill C-472 would have permitted parties to immunize covert, hard-core cartel behaviour from criminal prosecution by notifying. Specifically, section 45(7)(c) provides that an arrangement shall not be considered “collusion”, within the meaning of s. 45(1), if “notice of it is given to the Commissioner pursuant to subsection 79.2(1)”. The unilateral, and non-discretionary entitlement to criminal immunity found in section 45(7)(c) would have created the risk that parties would enter into arrangements that they knew violated section 45 and then notify the arrangement solely for the purpose of avoiding criminal penalties and depriving private plaintiffs of a remedy under section 36 of the Act. Likewise, the Trebilcock-Warner Model also raises the spectre of strategic behaviour. In this case, however, the risk is that parties to an agreement that has not yet been entered into or given effect will notify and then proceed after the 30 day waiting period knowing that: (a) the Commissioner may have difficulty securing an interim injunction to prevent them from proceeding with the arrangement; and, (b) that although it is likely that the arrangement will ultimately be condemned in the end, they have successfully insulated themselves from criminal sanctions as well as civil damages.

Further, although, section 79.2 of Bill C-472 provides that clearance certificates are available only for agreements “about to be entered into”, section 45(7)(c) does not impose a similar limit on the right to notify. As we have already indicated, this suggests that under the system proposed by Bill C-472, parties would have been entitled to notify and immunize themselves from criminal prosecution even where they had already implemented the agreement. Parties should not have an unqualified, unilateral entitlement to avoid criminal liability. However, the idea of granting immunity or leniency, based on post-agreement notification may have some benefits. Like pre-agreement notifications, post-agreement notifications would ease the Commissioner’s detection and evidence gathering tasks. Also, post-agreement notification would permit parties that had

unwittingly entered into a potentially criminal arrangement as well as parties to an arrangement which, as a result of a material change in market circumstances, had become potentially criminal, to notify. To encourage parties to notify agreements which have already been implemented, the Bureau may wish to extend some form of immunity, similar to that granted under the existing Immunity Program, to the party which submits a post-agreement notification under an amended section 45.²³¹

(2) Unavailability of a Rule of Reason Analysis

Bill C-472 contemplates a full-blown rule of reason analysis only in relation to arrangements that have already taken effect or been entered into. The Bill does not empower the Commissioner to seek a full rule of reason review by the Tribunal prior to the parties having entered into an arrangement. This raises two points. First, under Bill C-472, where the Commissioner refuses to grant a clearance certificate, the parties are forced either to abandon their arrangement or to proceed without knowing whether the arrangement will subsequently be unravelled, in whole or in part, pursuant to an order by the Tribunal under ss. 79.1(1)(c) or (d). Second, Bill C-472 is, in this respect, inconsistent with the merger review process under s. 92 of the Act. Under that section, the Commissioner is empowered to seek a remedy from the Tribunal in respect of “proposed mergers”. In our view, the objectives of certainty, predictability, and harmonization dictate, at a minimum, that the Commissioner should be similarly empowered to seek a review of competitor collaborations prior to their implementation.

(iv) Civil Remedies

The Trebilcock-Warner Model is not explicit concerning the powers that the Tribunal would enjoy under their proposed civil review procedure. It appears, however, that they would vest the Tribunal with powers similar, if not identical, to those available to it under the merger review process.²³² Under the amendments proposed by Bill C-472, the Tribunal would have had the power (a) to prohibit a person from carrying into effect or continuing an arrangement²³³ and, additionally, (b) to “order the person to take such actions as the Tribunal considers reasonable and necessary to overcome any of the effects of the agreement or arrangement or to restore competition in the market including, without limitation, directing modifications to the agreement or arrangement”.²³⁴

Arrangements that are not *per se* illegal may still warrant deterrence and censure if, pursuant to a rule of reason analysis, they are found to cause significant anti-competitive harm which is not compensated for by pro-competitive benefits. In this light, there is a strong argument that the

²³¹ See at <http://strategis.ic.gc.ca/SSG/ct01990e.html>.

²³² See Warner et al. *supra* note 70 at 720-21; see s. 92 of the Act.

²³³ See s. 79.1(1)(c).

²³⁴ Section 79.1(2)(d).

Tribunal should have the power to impose administrative monetary penalties in appropriate circumstances. As part of the amendments introduced in 1999, the Tribunal was given remedial powers of this kind under Part VII.1 of the Act.²³⁵

It should be noted, however, that the power to impose monetary penalties may attract a criminal due process argument to the effect that the Tribunal must, if it is to impose what amounts to fines, review any matters coming before it to a higher standard than the civil burden of proof. This would, of course, detract from a key advantage of civil review, namely, avoidance (or minimization) of the high cost and delay associated with a more stringent burden of proof (*e.g.*, beyond a reasonable doubt).

(d) New Proposal for Amendment

We believe that a “dual track” regime represents the most advantageous approach to balancing the need, on the one hand, for effective deterrence and punishment of hard-core cartel behaviour and, on the other hand, for a forum in which pro-competitive, welfare enhancing collaborations can be effectively differentiated from those which are not.

(i) Criminal Prohibition

The statutory language used in a criminal prohibition should be similar or identical to the language employed in s. 45(1) of Bill C-472. Based on our comparative review (*see* Australia and New Zealand), we believe that drafting precision and specificity will minimize the characterization problem that, as was noted above, has proved highly problematic under the American regime. We also endorse the adoption of *per se* prohibitions against hard-core cartel behaviour, such as price fixing and market allocation, based on the view that, relative to a rule of reason standard, these will result in more efficient and effective enforcement as well as increased certainty and predictability for those whose conduct may be subject to scrutiny.

(ii) Civil Provision

Under the model we propose, all other arrangements would be subject to review pursuant to a civil provision.

As noted above, the establishment of a civil regime has a number of advantages, including harmonization between the treatment of mergers and strategic alliances. The potential anti-competitive effects flowing from a merger are generally more significant than those resulting from collaborations or strategic alliances between competitors. While most mergers completely end competition between the merging parties, collaborations normally preserve some form of

²³⁵

See s. 74.10(1)(c).

competition between the parties.²³⁶ On this basis, it is difficult to justify subjecting mergers to non-criminal review before an administrative tribunal, while potentially less anti-competitive arrangements are reviewed exclusively under a criminal prohibition. Further, as Ross notes, “decisions firms make about how to structure their activities should be driven by considerations of economic efficiency, not by their desire to find the path of least antitrust resistance”.²³⁷

The availability of a civil review process will also permit the Commissioner, in appropriate cases, to prove his case to the lower “balance of probabilities” standard and to gather evidence through the discovery mechanisms available in proceedings before the Tribunal. Further, a number of commentators believe that the Competition Tribunal is better equipped, relative to the courts, to engage in the detailed economic analysis required by rule of reason analysis. Also, matters such as potential anti-competitive effects and corresponding benefits, are predictive and speculative matters for which the specialized Tribunal and the lower standard of proof in Tribunal proceedings may be more appropriate.

Nevertheless, despite the advantages of a civil regime, given the importance of the conspiracy provision and the significant distortions and losses to consumers which may arise from hard-core cartel behaviour, it is also desirable to retain a criminal prohibition. The most efficient means of enforcing the prohibitions against hard-core cartel behaviour is through deterrence. It is unlikely that the prohibitions available through reviewable matters would result in a sufficient level of deterrence.

The level of deterrence may be increased, to some degree, by amending section 36 of the *Act* to permit private parties to recover damages suffered as a result of arrangements that are the subject of a remedy under the civil provision. We question whether the Commissioner’s decision to pursue a remedy under a civil provision, as opposed to a criminal route, is a sufficient basis to deny recovery to a private party that has suffered losses as a result of anti-competitive conduct. Further, the risk of such civil liability would encourage parties to delay implementation of the arrangement pending the disposition of any Tribunal proceedings relating to that arrangement.

It should be open to “respondents” under the civil review process to rely on the efficiency exception found in section 96 of the *Competition Act*. This defence would provide the mechanism through which the Tribunal would have occasion to consider the net pro-competitive effects of an impugned competitor collaboration. We propose to allow parties to defend a proceeding on the basis that the efficiency gains resulting from their collaboration outweigh its harm to competition. In this way, the Tribunal may apply a full rule of reason analysis to collaborations among competitors.

As noted above, permitting the consideration of social objectives, apart from narrow economic efficiencies, under the civil review process would mark a significant, and unadvised, alteration of Canada’s current competition regime. In our view, the Commissioner should resist weighing non-

²³⁶ See Joint Guidelines, *supra* note 2.

²³⁷ Ross, *supra* note 7 at 870.

economic factors. The absence of a principled basis for courts to accept or reject non-economic considerations will lead to inconsistency and unpredictability in the law. Also, multiple objectives and, in particular, the combination of economic and non-objectives in a single policy tool is a recipe for policy failure. As the New Zealand Commission has observed: “It is not easy to make a judgment between two public policies”.²³⁸ This is particularly so where the public policies being compared and weighed against one another are different in kind.

(iii) Notification

We recommend the adoption of a notification system, the principal purposes of which, from a functional standpoint, would be to:

- (a) reduce the inflexibility and overbreadth of the *per se* prohibitions; and
- (b) diminish the burden on the Commissioner’s enforcement resources by reducing its detection and evidence gathering costs.

Such a notification system has a number of advantages, certain of which have been demonstrated through the experience under Article 81(3) of the EC Treaty; specifically: the EC Treaty notification system has permitted the Commission to build a coherent body of precedent decisions; parties benefit from submitting a notification as it has the effect of “stopping the clock” for the purposes of the imposition of a fine for any infringement; a determination by the Commission provides legal certainty for the parties; and, the notification regime has proved to be extremely flexible in permitting pro-competitive collaborations.

As with the EC Treaty system, the Canadian Commissioner may encourage notification by not imposing a fine for the period between the date of notification and any decision concerning the arrangement. However, a system which requires notification of all forms of agreements which could potentially violate the criminal or civil provision may be unmanageable. As indicated in the EC Commission’s *White Paper on Modernisation* which are discussed above, the EC Treaty notification system also results in significant delays which may have discouraged parties from pursuing potentially pro-competitive alliances. Also, critics of the EC regime note that the broad interpretation of Article 81(1) requires notifications to be submitted for arrangements which do not raise any significant competition concerns. The universal dissatisfaction with the EC notification regime supports a consideration of a different model of notification.

Including a notification and exemption regime will result in further harmonization with the merger provisions. Similar to the issuance of advance ruling certificates under section 102 of the Canadian *Competition Act*, under the proposed notification system, the Commissioner would be empowered

²³⁸ *Amcor*, *supra* note 190 at para. 75 (quoted in Adhar, *supra* note 159 at 146). In that case, the Commission was asked to weigh the benefit of “utilization of resources and the flow-on effects” against the detriment to competition.

to grant exemptions or “clearance certificates” for specific arrangements. The intent is that the issuance of a clearance certificate will insulate the collaboration from both criminal and civil review. Although we note that the *Competition Act* does not expressly provide that the issuance of an advance ruling certificate insulates a proposed merger from review under either section 45 or 79, it is recognized that it would not be appropriate or consistent with the established practice under the *Act* to commence proceedings under either of these sections in respect of an arrangement that has been approved by the Commissioner through the issuance of an advance ruling certificate. Similarly, where the Commissioner has approved a collaboration through the proposed notification process, it would not be appropriate to commence proceedings under section 45 in respect of that collaboration. Legislative amendments dealing with the effect of advance ruling certificates and the proposed clearance certificates may be required to ensure that this intent is achieved.

In our view, the notification system adopted should strike a balance between a model based purely on the exercise of administrative discretion and one in which civil review is automatic upon notification. This will preserve administrative discretion regarding the applicable review process while resulting in greater symmetry with merger review. We propose two alternative models – the Discretionary Track Model and the Civil Track Model.

(1) Discretionary Track Model (the “DTM”)

The DTM applies both to arrangements that have and have not been entered into or given effect. Under this model, parties whose actual or proposed arrangement would appear to be contrary to a *per se* prohibition found in the amended section would be entitled to submit an application to the Commissioner requesting an exemption. The Commissioner would have the discretion to respond in one of three ways:

- (a) grant an exemption to the parties by issuing a Clearance Certificate;
- (b) refer the matter to the Competition Tribunal pursuant to the civil provision. The civil provision would provide for both a consent or approval procedure, as well as for review of agreements that have already been entered into; or
- (c) advise the parties that a Clearance Certificate will not be granted and that the Commissioner will refer the matter to the Attorney General for criminal prosecution. In the case of an arrangement that has already been entered into or given effect, the Immunity Program may apply in the manner described above.

As is plain from the foregoing, the DTM empowers the Commissioner, in a manner similar to merger review, with a discretion to elect, on a case-by-case basis, between pursuing a civil or criminal remedy. In addition to being consistent with the elections found throughout the Act (*see also* the Act’s dual track, misleading advertising regime), this aspect of the DTM offers the important advantage of negating the potential for strategic behaviour which flows from a notification system that provides parties with a unilateral, non-discretionary entitlement to criminal immunity.

Empowering the Commissioner to elect between criminal and civil provisions is also consistent with the American approach. As noted above, the Department of Justice has concluded that criminal sanctions are unquestionably appropriate for hard-core cartel behaviour that is, by definition, harmful to consumers. On the other hand, the DOJ also recognizes that where a legitimate disagreement exists as to whether the pro-competitive benefits of an arrangement outweigh its anti-competitive effects criminal prosecution is inappropriate. Section 1 of the *Sherman Act* gives the DOJ the discretion to determine whether the civil or criminal route is appropriate, taking into account the particular facts of each case.

Also, providing the Commissioner with the discretion to determine which types of collaborations will be subject to criminal prosecution, as opposed to an administrative review, assists the Commissioner in steering the development of competition policy in respect of competitor collaborations. The considerations informing the Commissioner's decision whether to pursue a civil remedy or refer the matter for criminal prosecution may be set out in guidelines similar to those applicable to the misleading advertising regime.²³⁹ For example, one factor which may be considered in determining the appropriate route may be whether the arrangement has as its object the restriction of competition, or whether that is merely the effect of the arrangement. The Commissioner may be more inclined to recommend criminal prosecution in respect of an intentional contravention of the provision.

(2) Civil Track Model (the "CTM")

In contrast to the DTM, this model applies only to arrangements that have not been entered into or given effect. Parties whose proposed arrangement would appear to be contrary to a *per se* prohibition found in the amended section would be entitled to notify the Commissioner and request an exemption prior to implementing the arrangement. However, unlike the DTM, the Commissioner's discretion would be limited to responding in one of two ways:

- (a) grant a Clearance Certificate to the parties; or
- (b) advise the parties that a Clearance Certificate will not be granted and that if the agreement is carried out, the Commissioner will seek a remedy on application to the Competition Tribunal pursuant to the civil provision.

Upon receipt of notification, criminal prosecution would cease to be an option under this model. Instead, under the CTM, all arrangements that are notified would be reviewed on the basis of a full rule of reason analysis pursuant to the civil provision. This approach is somewhat problematic because naked, hard-core cartel behaviour that is more effectively and more appropriately addressed and deterred through the application of a *per se* criminal prohibition, would be subject to a full-blown competitive effects analysis under the civil provision. Also, the time- and cost-effectiveness

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See "Misleading Representations and Deceptive Marketing Practices: Choice of Criminal or Civil Track under the *Competition Act*" available at <http://strategis.ic.gc.ca/SSG/ct01881e.html>.

of a *per se* approach is lost because a competitive effects analysis would be required even for an arrangement that is clearly contrary to a *per se* prohibition and that has no chance of avoiding condemnation by the Tribunal. For all these reasons, the CTM may reduce the efficiency and effectiveness with which the Commissioner is able to “prosecute” naked, hard-core cartel behaviour. On the other hand, the use of administrative remedies, rather than criminal sanctions, to “punish” an arrangement that is plainly contrary to a *per se* prohibition could arguably be justified on the basis that prior to the time that the arrangement is entered into or takes effect there has been no actual harm that would warrant criminal sanction.

It should be noted that the CTM would require the institution of measures aimed at minimizing abuse of the notification system. As explained above, the availability of unilateral criminal immunity increases the risk of strategic behaviour. To protect against the possibility of abuse, we recommend that a provision be included which would render immunity contingent on non-implementation of the collaboration, pending the initiation of proceedings by the Commissioner before the Competition Tribunal or the expiry of a fixed statutory time limit, similar to the waiting period applicable under the merger review process.

Warner et al. have criticized models based on administrative discretion in the following terms:

We cannot emphasize too strongly that the notification regime we propose is *not* a registration or authorization procedure. To empower the Director to review notifications and to decide whether to accept, reject or propose modifications to the underlying agreement as a precondition of the parties’ immunity from criminal prosecution would impose heavy burdens on both the parties and the Bureau. Conferring such powers on the Director risks creating the same paper nightmare that has bedevilled both the European Commission, with negative clearance and exemption applications under article 85 of the *Treaty of Rome*, and the Office of Fair Trading in the United Kingdom under the *Restrictive Trade Practices Act*. Under both regimes, parties are subjected to enormous delays and great uncertainty pending the administrative review of often trivial or benign arrangements by official agencies.

To avoid the issue of large number of notifications referred to by the learned authors above, the Commission may issue administrative guidelines, providing guidance on the interpretation of the criminal prohibitions. Further, in contrast to the single track model under Article 81 of the EC Treaty which invites notification of any arrangement that may substantially lessen competition, under the CTM, notifications would be required only in respect of the small subset of arrangements otherwise prohibited by the *per se* criminal prohibitions. In addition, we believe that the above view is also often motivated by the belief by some commentators that the Commissioner’s role should be limited to the role of a prosecutor or litigant with as little administrative discretion as possible. We believe that the competition policy model in Canada expressed, as embodied in the *Act*, clearly provides the Commissioner with a policy-making role, through the exercise of administrative discretion, similar to the European Community model. Canadian regulatory policy has, in general, favoured the efficiencies that administrative discretion provides, relative to the more litigious models

of regulation in the United States. In essence this approach provides for administrative discretion in granting exemptions (similar to Europe) and determining the type of proceeding that may be commenced (as in the US).

Further, the number of notifications could also be reduced by carefully limiting the scope of the criminal prohibitions, through exemptions for agreements that rarely or never require a remedy. For example, an “ancillary restraints” exemption could be adopted. In fact, the Terms of Reference and Bill C-472 both proposed an exception for “ancillary restraints”. As noted above, the ancillary restraints doctrine has been applied under both Article 81(1) of the EC Treaty and section 1 of the *Sherman Act*. An ancillary restraints exemption would permit the courts to exempt arrangements that are objectively necessary for the performance of a specific type of pro-competitive agreement or are essential to induce a party to the contract to take on the commercial risk inherent in the arrangement. For example, section 45(7)(d) states, in pertinent part:

(7) An agreement or arrangement shall not be considered to be collusion if

...

(d) it is ancillary to, and reasonably necessary for, another agreement or arrangement among the same participants and the other agreement or arrangement would not itself constitute collusion, when considered on a separate basis.

The advantage of the DTM and CTM is that they provide the Commissioner with a broad and flexible discretion to exempt arrangements based on the particular circumstances of each case. The Commissioner would be entitled to consider a wide range of circumstances in exercising its discretion, including any undertakings given by the parties. The concern raised in the Public Policy Review forum, namely, that static characterization of competitor arrangements will prove to be insufficiently flexible, relative to the fast-evolving technology world, could be addressed by policy guidelines that outline the factors governing the Commissioner’s discretionary decision-making. Further, through such guidelines, the Commissioner would be able to manage and oversee the development of competition policy in relation to permissible competitor collaborations, without having to rely on the unpredictable direction of case law. At the same time, the ability to refer certain arrangements to the Tribunal for review would allow competition policy to develop outside of a purely administrative model. Finally, in circumstances where the net pro-competitive benefits are clear cut, Clearance Certificates would provide the legal certainty required by business planners.

Schedule II - Article 81 of the EC Treaty

Article 81

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:
 - (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
 - (b) limit or control production, markets, technical development, or investment;
 - (c) share markets or sources of supply;
 - (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
 - (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.
2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.
3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:
 - any agreement or category of agreements between undertakings;
 - any decision or category of decisions by associations of undertakings;
 - any concerted practice or category of concerted practices;which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
 - (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;

- (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in questions.