

**PROPOSED AMENDMENTS TO  
SECTION 45 OF THE COMPETITION ACT**

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## INTRODUCTION

We have been asked by the Commissioner of Competition for our views on possible amendments to section 45 of the *Competition Act*<sup>1</sup> (the "Act"). More specifically the Commissioner, in the terms of reference setting out our mandate, has requested that we consider the feasibility of a "two-track" approach which would have the following general characteristics:

1. a criminal provision would prohibit as *per se* offences agreements to fix prices, share markets, restrict output and engage in primary or secondary boycotts directed at a competitor; subjective *mens rea* would be required as to the formation of the agreement, but only objective *mens rea* would be necessary in relation to the effects of the agreement on competition;
2. there would be an appropriate exception or defence to this criminal prohibition based on the "ancillary restraint doctrine"; and
3. a civil provision would apply to "complex competitor agreements"<sup>2</sup> incorporating an appropriate rule of reason analysis to evaluate both the impact on competition and the reasonableness of the agreements from a public interest perspective".

The appropriateness of the current section 45 of the Act and its possible amendment probably constitute the most significant and complex challenge faced today in Canadian competition law. How to deal with competitor agreements has been at the heart of antitrust debate in Canada for more than thirty years. In the United States, commentators and the courts have for years struggled with where to draw the line between *per se* and rule of reason situations. The European Commission is in the midst of making fundamental changes to its approach to the enforcement of Article 81 of the EC Treaty dealing with anti-competitive agreements<sup>3</sup>.

We have had only a short period of time to consider this complex question. We point this out because the nature and extent of our contribution are a function of the limited time we were granted to consider the extremely complex issues raised by our

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<sup>1</sup> R.S.C. 1985, c. C-34 as amended.

<sup>2</sup> We assume that this new civil provision would apply only to agreements that otherwise have a significant adverse impact on competition.

<sup>3</sup> EC, *White Paper on Modernisation of the Rules Implementing Articles 85 and 86 of the E.C. Treaty* [1999] O.J.C. 132/1.

terms of reference. For example, we have not been able to fully analyze the scope of foreign law on the issues discussed in this paper or obtain expert input on economic issues.

We have agreed to consider this issue because we believe strongly that the current section 45 is flawed and must be amended. We are not the first to consider whether changes to the law are necessary to deal with horizontal agreements. The concept of a *per se* prohibition was first proposed as far back as 1969 by the Economic Council<sup>4</sup> and soon found its way, albeit in a rather complex form, in a Government Bill<sup>5</sup> which generated a lengthy debate and was subsequently abandoned. The issue was again in the limelight in the 90's, when the Supreme Court of Canada handed down its decision on the constitutional validity of section 45 in *Nova Scotia Pharmaceutical Society*<sup>6</sup>. This significant judicial development, coupled with the growing incidence of strategic alliances, led some highly respected commentators to suggest revamping section 45 to provide for a two-track approach whereby certain so-called "hard core cartels" would be prohibited irrespective of their effect on competition ("*per se*"), while other types of agreements between competitors would be subject to civil review and to a "rule of reason" analysis<sup>7</sup>. A private member bill containing provisions to this effect, Bill C-472, was tabled in the House of Commons<sup>8</sup> and a public consultation on this and other private

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<sup>4</sup> Economic Council of Canada, *Interim Report on Competition Policy*, (Ottawa, 1969), at 102.

<sup>5</sup> Bill C-256, *An Act to Promote Competition, to provide for the general regulation of trade and commerce, to promote honest and fair dealing, to establish a Competitive Practices Tribunal and the office of the Commissioner, to repeal the Combines Investigation Act and to make consequential amendments to the Bank Act*, 3d Sess., 28th Parl., 1970-1971, s. 16 [hereinafter Bill C-256].

<sup>6</sup> *R. v. Nova Scotia Pharmaceuticals Society*, [1992] 2 S.C.R. 606, sometimes referred to as the "PANS case".

<sup>7</sup> See *inter alia* W.T. Stanbury, "Legislation to Control Agreements in Restraint of Trade in Canada: Review of the Historical Record and Proposals for Reform" (National Conference on the Centenary of Competition Law and Policy in Canada, Toronto, 24-25 October 1989) [unpublished] [hereinafter Stanbury]; T. Ross, "Proposals for a New Canadian Competition Law on Conspiracy" (1991) 36 *Antitrust Bull.* 851; P.L. Warner and M.J. Trebilcock, "Rethinking Price-Fixing Law" (1993) 38 *McGill L.J.* 679 [hereinafter Warner and Trebilcock]; J.T. Kennish and T.W. Ross, "Towards a New Approach to Agreements between Competitors" (1997) 28 *Can. Bus. L.J.* 22 [hereinafter Kennish and Ross].

<sup>8</sup> Bill C-472, *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 Sess., 36th Parl., 1999-2000, ss. 1 and 7; Bill C-472 died on the Order Paper with the dissolution of Parliament on October 22, 2000.

bills was undertaken by the Public Policy Forum, which issued its report on December 20, 2000<sup>9</sup>.

We propose to first discuss section 45 as it presently stands. We need to fully understand the scope of current law and be satisfied that it does raise serious problems<sup>10</sup> before considering these problems and evaluating possible solutions. This will allow us to make suggestions as to how, in our view, section 45 should be redrafted.

## THE CASE FOR AMENDING SECTION 45

### 1. Current Law

Section 45 prohibits all agreements which unduly restrict competition, not just hard core cartels such as price-fixing or market-sharing agreements. It can apply to any agreement which is likely to lessen competition, such as joint ventures, mergers and strategic alliances, including specialization agreements<sup>11</sup>. It applies not only to agreements between competing sellers, but also between competing buyers and could therefore, for example, apply to a buying group. Finally, although it has largely been used against horizontal agreements, nothing prevents section 45 from being applied to vertical agreements.

Section 45 creates an indictable offence of the most serious kind, punishable by heavy fines and jail terms of up to five years. Mr. Justice Gonthier, speaking for a unanimous Supreme Court of Canada in *Nova Scotia Pharmaceutical*, stated that section

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<sup>9</sup> Public Policy Forum, *Amendments to the Competition Act and the Competition Tribunal Act: A report on Consultations, Final Report Submitted to the Commissioner of Competition*, (Ottawa, December 20, 2000) [unpublished].

<sup>10</sup> Some commentators have suggested that the case for change may not have been convincingly made: McMillan Binch, "Submission to the Public Policy Forum Regarding Proposals to Amend the Competition Act Contained in Bills C-471 and C-472" (30 June 2000) [unpublished]; Lang Michener, "Report to the Public Policy Forum" (2000) [unpublished]; Canadian Bar Association, National Competition Law Section, "Submission on the Public Policy Forum Consultation Concerning Amendments to the *Competition Act* and the *Competition Tribunal Act*" (March 2001) [unpublished].

<sup>11</sup> In fact, sections 45.1, 79(7), 90 and 98 of the Act confirm that section 45 could apply to a merger, a joint venture, a specialization agreement and joint dominance resulting from an agreement; the *Information Bulletin on Strategic Alliances* also confirms that section 45 applies to strategic alliances. (Industry Canada, Director of Investigation and Research, *Information Bulletin on Strategic Alliances* (Ottawa: Supply and Services Canada, 1995) at section 3.2.

45 remains at the core of the criminal part of the Act and is not just "another regulatory provision"<sup>12</sup>.

Parliament chose to prohibit only those agreements which "unduly" lessen competition. The effects or likely effects of the agreement on competition must therefore be measured, which means that the relevant market must be defined, a difficult and contentious endeavour in many cases. While section 45 is a true criminal prohibition, it does not specify at which point the lessening of competition is significant enough to become "undue" and therefore attract criminal sanction. This makes it virtually impossible in many cases to assess whether a particular agreement constitutes a criminal offence. There are of course situations where it is readily apparent that competition will be lessened to a very significant degree as a result of an agreement: if all, or almost all, members of an industry agree to fix the price at which their product is sold and if the market can readily be defined, the agreement would unduly lessen competition. It is, in fact, in such situations that the Attorney General has succeeded in obtaining guilty pleas and very considerable fines from both corporations and individuals. The problem is not with such agreements, but rather with other competitor agreements where the market is difficult to define or, even if it is readily definable, where only some competitors participate in the agreement.

The critical question under section 45 as drafted is the meaning of the term "unduly". Prior to *Nova Scotia Pharmaceutical*, the courts had interpreted "unduly" first by stating what was not relevant to determine whether an agreement offends section 45: unduly was not to be determined by reference to whether the prices agreed upon were reasonable, or the profits realized not excessive, or to whether the agreement was necessary to stabilize the industry or preserve jobs<sup>13</sup>. The courts then stated that a lessening of competition was undue if it was "improper, inordinate, excessive or oppressive"<sup>14</sup>, a list of synonyms which did not really clarify the matter. Despite numerous decisions interpreting "unduly", businesses were still left without meaningful

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<sup>12</sup> *Supra* note 6 at 649.

<sup>13</sup> *Weidman v. Shragge* (1912), 20 C.C.C. 117 at 147, 152 (S.C.C.); *Stinson-Reeb Builders Supply Co. v. R.* (1929), 52 C.C.C. 66 at 70 (S.C.C.); *Container Materials Ltd. v. R.*, [1942] S.C.R. 147 at 152.

<sup>14</sup> *Weidman v. Shragge*, *ibid.* at 151-152; *R. v. Elliott* (1905), 9 C.C.C. 505 (Ont. C.A.).

guidance as to what agreements were prohibited. In fact, some decisions actually recognized that section 45 was vague and difficult to interpret<sup>15</sup>.

This state of uncertainty paved the way for the constitutional challenges<sup>16</sup> of the late 80's, which would culminate in the Supreme Court of Canada's decision in *Nova Scotia Pharmaceutical*<sup>17</sup>.

It is not necessary to discuss at length the Charter issues decided in *Nova Scotia Pharmaceutical*. Suffice it to say that the Court concluded that, notwithstanding the obvious lack of precision of the word "unduly", section 45 was not sufficiently vague to offend section 7 of the Charter. The Court also rejected a Charter argument based on section 45(2.2), which provides that the Crown is not required to establish the accused's criminal intent with respect to the undue lessening of competition. The Court held that the Crown only had to prove an objective *mens rea* with respect to the effect of the agreement, but that this complied with the Charter.

The significance of *Nova Scotia Pharmaceutical*, for our purposes, is that, in disposing of the Charter arguments, the Court considered section 45 extensively and it specifically addressed the issue of what constitutes an undue lessening of competition.

Notwithstanding the Court's conclusion that section 45 is not void for vagueness under the Charter, the decision in *Nova Scotia Pharmaceutical*, as we shall see, contributed to the existing uncertainty. The Court did however clarify what factors should not be considered in determining whether an agreement offends section 45. The only relevant issue is the effect of the impugned agreement on competition: factors such as the benefits to the parties and, more importantly for our purposes, "counterbalancing efficiency gains ... lie ... outside of the inquiry"<sup>18</sup>. As a result, the parties commit a criminal offence notwithstanding that the agreement, which unduly lessens competition, results in significant and potentially off-setting efficiencies. Under section 45 as it stands today, there is therefore no room for a consideration of efficiencies as part of a "rule of reason" analysis, as is the case in the United States.

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<sup>15</sup> *Weidman v. Shragge*, *ibid.* at 130; *Howard Smith Paper Mills Ltd v. R.*, [1957] S.C.R. 403 at 425; *R. v. Electrical Contractors Ass'n*, (1961), 131 C.C.C. 145 at 152-156 (Ont. C.A.); *R. v. J.J. Beamish Construction Co. Ltd.* (1967), 65 D.L.R. (2d) 260 at 273 (Ont. C.A.); *Canada (A.G.) v. Canadian National Transportation, Ltd.*, [1983] 2 S.C.R. 206 at 273.

<sup>16</sup> *Association québécoise des pharmaciens propriétaires v. Canada (P.G.)*, [1991] R.J.Q. 205; *R. v. Nova Scotia Pharmaceutical Society* (1990), 32 C.P.R. (3d) 259 (N.S.S.C. (T.D.)); *R. v. Nova Scotia Pharmaceutical Society* (1991), 36 C.P.R. (3d) 173 (N.S.S.C. (A.D.)).

<sup>17</sup> *Supra* note 6.

<sup>18</sup> *Ibid.* at 647.

The Court then indicated what factors should be considered to determine if a lessening of competition is undue. The Court stated that "... there are two major elements to this inquiry, that is (1) the structure of the market and (2) the behaviour of the parties to the agreement"<sup>19</sup>.

Undueness is first a function of the market power of the parties to the agreement. This requires defining the relevant product and geographic markets, a task fraught with complexity; indeed economists often disagree on the definition of a particular market even though they all rely on sound economic reasoning<sup>20</sup>. The Court actually referred to the "intricacies of outlining the relevant market" and recognized that this may "... require considerable inquiry"<sup>21</sup>. Once the market is defined, one then looks at the combined market share of the parties to the agreement, although the Court did not specify what market share is sufficient to trigger the application of section 45.

The Court however added that "market share alone is not determinative ..."<sup>22</sup>. Many other factors must be taken into account to determine whether the parties have market power, including the following:

- (a) the number of competitors and the degree of concentration;
- (b) the barriers to entry;
- (c) the geographic distribution of buyers and sellers;
- (d) the differences in the degree of integration among competitors;
- (e) product differentiation;
- (f) countervailing power; and
- (g) cross-elasticity of demand.

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<sup>19</sup> *Ibid.* at 651.

<sup>20</sup> One need only consider examples such as potato chips (salted snacks? snacks? food?) and carbonated soft drinks (branded and/or unbranded? all non-alcoholic beverages? all beverages?) to be convinced of the difficulty of defining the relevant product market, not to mention the relevant geographic market.

<sup>21</sup> *Ibid.* at 652.

<sup>22</sup> *Ibid.* at 653.

A business person is therefore required to consider all of these factors (a list which the Court indicated is not exhaustive) to determine if the parties to a contemplated agreement might have enough market power to commit a criminal offence<sup>23</sup>.

According to *Nova Scotia Pharmaceutical*, however, market power is not determinative of the question; another factor which needs to be considered is the "behaviour" of the parties. According to the Court, this refers to the facet of competition affected by the agreement and how important it is to the customers. Consideration must also be given to the object of the agreement and "... the manner in which the agreement has been or will be carried out and, in general, any behaviour that tends to reduce competition or limit entry"<sup>24</sup>. The Court's reasons for judgment are not explicit as to what is meant by the "manner" in which the agreement is carried out, or what types of "behaviour" are relevant to this analysis. Our hypothetical business person has an even more daunting task with respect to behaviour than with respect to determining whether the parties have market power. This problem is heightened by the fact that the Court does not mention whether "good" behaviour should also be considered in the analysis.

After determining what factors need to be considered, the Court further stated that "unduly" is a function of the interrelationship between the parties' market power and their behaviour. If the conduct is highly injurious to competition, such as price fixing and market sharing, the parties do not need to have a high degree of market power to lessen competition unduly. Conversely, if their market power is considerable, any agreement affecting competition may be contrary to section 45, even if the behaviour is not so prejudicial.

Having thus summarized the inquiry mandated by section 45, the Court held that it did not violate the Charter on grounds of vagueness. The constitutional challenge may have been solved but, as professor Trebilcock wrote in a recent article, the Court may not have "been especially successful in clarifying the content and scope of section 45(1)(c)".<sup>25</sup> In our view, determining whether an agreement lessens competition unduly is now even more complex and, as a result, more uncertain than it was before. In the

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<sup>23</sup> The Court added that it is not necessary for the parties to dominate or control a market completely (which is provided in section 45(2)) and stated that a "moderate" level of market power will suffice ( *Ibid.* at 654); the Court in this regard referred to *R. v. Abitibi Power & Paper Co.* (1960), 131 C.C.C. 201 (Qc. Q.B.), which, interestingly, dealt with an agreement between buyers where the combined market shares of the parties was found to be between 56 and 74 %.

<sup>24</sup> *R. v. Nova Scotia Pharmaceutical Society*, *supra* note 6 at 355 (emphasis added).

<sup>25</sup> M.J. Trebilcock, "The Supreme Court and Strengthening the Conditions for Effective Competition in the Canadian Economy" (2000) 80 Can. B.R. 542, at 603.

current environment, the parties have to carry out a full competitive analysis to determine whether they have market power, deal with the ill-defined concept of behaviour and somehow measure if the combination of these two factors exceeds a threshold of "seriousness", a concept which cannot be objectively ascertained.

## 2. Problems Raised by Section 45

### (a) Inappropriate Use of Criminal Law

Because of the uncertainty relating to its interpretation, section 45 does not meet the basic standards of clarity and predictability which should characterize criminal offences. In addition, while the economic analysis mandated by *Nova Scotia Pharmaceutical* is not unusual in competition law, such analysis is ill-suited in the context of the enforcement of a criminal provision. The following excerpt on the limitations of criminal law from Skeoch and McDonald, two of the most respected commentators on Canadian competition law, is of particular relevance to the issues discussed here:

"One of the central difficulties with using the criminal law in this field is that the function of criminal law and the purpose and capacity of the criminal sanction depend upon a substantive prohibition that is defined sufficiently precisely in advance that a person has fair notice, before engaging in the conduct, that it is against the law and the public interest for him to do so. Ideally a widely accepted moral disapproval of the conduct exists in addition to the specific prohibition. Competition law, however, cannot realistically define many undesirable events except in terms of their economic effect or likely economic effect. Mergers, uses of market power, and price differentials, for example, are desirable, inconsequential, or harmful only according to the market context in which they occur.

The growing complexity of the economy, and of economic analysis, has no doubt contributed significantly to the inability to frame many effective specific laws in this field. It has also contributed to the disappearance of much of the moral force underlying the original enactment of combines laws. The point is that there are situations where businessmen do things that, while they should be prohibited, nevertheless do not warrant the ignominy of criminal charge and conviction.

Not only is the exclusive use of criminal law in this field negative and confrontationist in approach and effect, but criminal procedures are slow, costly and procedurally cumbersome. The publicly imposed sanctions for breach of criminal laws are severe and the procedural safeguards to prevent unwarranted conviction are accordingly more stringent than the comparable safeguards in civil actions. [...]

Criminal law does have a vital role to play in the total enforcement scheme but only in the limited sphere where it can be effective, namely, with respect to conduct that can be defined with a reasonably high degree of precision and that is generally agreed to be contrary to the public interest regardless of its more specific factual context. In those areas of deliberate deviance criminal penalties should be as severe as might be required to stamp out the practice. This may require jail sentences in appropriate cases.

The need to restrict criminal law to matters that can be reasonably precisely defined is underscored by the recent provision for civil damage actions in cases where criminal activity causes private injury, regardless of whether or not a criminal conviction has resulted."<sup>26</sup>

(b) Overbreadth of Section 45 Creates a Chilling Effect

Section 45 is an overbroad criminal provision, its proper interpretation is far from being clear, and it does not allow for consideration of efficiencies. Because many business people understandably refuse to take any risk of committing a criminal offence, section 45 often prevents the implementation of pro-competitive agreements, such as strategic alliances which make more efficient use of resources.

It is widely recognized that cooperation among competitors can lead to substantial economic benefits:

"...horizontal cooperation can lead to substantial economic benefits. Companies need to respond to increasing competitive pressure and a changing market place driven by globalisation, 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."<sup>27</sup>

It is difficult to demonstrate the chilling effect of section 45 in respect of strategic alliances, because the decision not to proceed with a business arrangement is rarely made public. The chilling effect is however real. Kennish comments as follows:

<sup>26</sup> L.A. Skeoch and B.C. McDonald, *Dynamic Change and Accountability in a Canadian Market Economy: Proposals for the Further Revision of Canadian Competition Policy by an Independent Committee Appointed by the Minister of Consumer and Corporate Affairs*, (Ottawa: Supply and Services Canada, 1976) at 39-41 (emphasis added).

<sup>27</sup> EC, *Guidelines on the Applicability of Article 81 of the E.C. Treaty to Horizontal Cooperation Agreements*, [2001] O.J.C. 3/2 [hereinafter *EC Guidelines*] para. 18 and 25. See also Federal Trade Commission and U.S. Department of Justice, *Antitrust Guidelines for Collaboration Among Competitors* (April 2000) [hereinafter *US Antitrust Guidelines*] at p. 1 and following.

"The principal conclusion which may be drawn from the PANS case, insofar as is relevant to strategic alliances between competitor firms, is that, while it is useful to have greater clarification on these issues, it is now more apparent than ever that it is inappropriate that section 45, which adopts a relatively inflexible and essentially structural approach to the determination of the legality of horizontal agreements among competitor firms and is largely insensitive to consideration of efficiencies or pro-competitive effects, should be governing as to the legality of such arrangements. Be that as it may, section 45 continues to have potential application to these situations and the risk remains that the full development of strategic alliances may be impeded by the chilling prospect of potential criminal enforcement of section 45."<sup>28</sup>

Others have also referred to the chilling effect of section 45<sup>29</sup>. On the basis of our experience, we are convinced that a large number of pro-competitive arrangements, which otherwise present some antitrust risk, do not proceed because counsel cannot give an unqualified opinion that there is no risk of criminal prosecution. Consider the following types of competitor agreements where the parties would have a not insignificant market share:

- setting up a joint production system;
- setting up a joint distribution system;
- joint purchasing of a given product;
- joint licensing of intellectual property rights<sup>30</sup>;
- an agreement to jointly develop, manufacture and market a new product;
- a specialization agreement<sup>31</sup>;
- any agreement whereby businesses are attempting to enhance network effects<sup>32</sup>.

Even though all of these agreements could generate efficiencies, such efficiencies are not relevant to determine criminal liability under section 45. Because the risk of

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<sup>28</sup> J.T. Kennish, "The Treatment of Strategic Alliances Under the Competition Act", (Annual Conference of the Canadian Bar Association, Montreal, 30 September 1994) [unpublished] at 19.

<sup>29</sup> See e.g. Kennish and Ross, *supra* note 7, at 51-53.

<sup>30</sup> *Broadcast Music Inc. v. Columbia Broadcasting Systems Inc.* 441 U.S. 1 (1979) [hereinafter *Broadcast Music*].

<sup>31</sup> Although sections 85 and following of the Act provide for an exemption from section 45, the pre-conditions are so daunting and the proceedings so cumbersome that the exemption has never been used and the chilling effect of section 45 remains.

<sup>32</sup> Such as credit cards, payment systems, etc. which require extensive agreements on types of infrastructures, prices, etc. but which are usually pro-competitive.

criminal sanctions cannot be eliminated with certainty, many business persons will be reluctant to conclude such arrangements if they have anti-competitive effects.

It is sometimes argued that businesses should find comfort in the fact that the Attorney General would properly exercise her prosecutorial discretion and would not prosecute beneficial strategic alliances even if they did have anti-competitive effects; in support of this proposition, reference is made to the fact that prosecutions under section 45 have generally been against price-fixing, market-sharing and other similar cartels that did not generate pro-competitive effects<sup>33</sup>.

We strongly believe that if section 45 is only meant to apply to certain types of agreements, we should change the law, not rely on prosecutorial discretion which can be exercised differently depending on the individuals. Further, prosecutorial discretion has no effect on the application of section 36 which provides for private actions for damages in cases of violation of the criminal provisions of the Act.

While it is possible to submit agreements to the Bureau for an advisory opinion, which could theoretically alleviate the chilling effect to some extent, the Bureau cannot change the law, consider efficiencies which have been held to be irrelevant, or eliminate the risk of civil liability.

(c) Enforcement Problems

In our view, section 45 has only worked reasonably well with respect to hard core cartels, at least where the relevant market is readily definable<sup>34</sup> and where all or almost all of the industry participants are parties to the agreement, as is demonstrated by the recent findings of guilt and significant fines imposed in cartel cases<sup>35</sup>. If the accused are acquitted in such cases, it is not because the Crown cannot establish an undue lessening of competition, but because it cannot establish the existence of an agreement. However, in many cases, the market is not readily definable – and experts can have legitimate disagreement on the issue – with the result that establishing guilt beyond reasonable doubt is a very difficult, if not impossible task.

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<sup>33</sup> H. Chandler and R. Jackson "Beyond Merriment and Diversion: the Treatment of Conspiracies Under Canada's Competition Act" (Round Table on Competition Act Amendments, Toronto, May 25, 2000) Insight.

<sup>34</sup> Snow removal, driving lessons, vitamins or other food additives for which there is no substitute.

<sup>35</sup> See for example, "Fines in Order of Magnitude - Competition Act" (<http://strategis.ic.gc.ca/SSG/ct01709e.html>)

Because of the uncertainty surrounding the interpretation of unduly and of the heavy burden of proof on the Crown, section 45 is much less effective to challenge other types of horizontal agreements which significantly lessen competition, for example hard core cartels where the market is not readily definable<sup>36</sup> or other agreements which may not constitute cartels but where the competitive harm is greater than the benefits resulting therefrom. From a public policy perspective, these agreements should be prevented, although not all should attract criminal sanction.

### **3. The Need for Change**

We are convinced that the treatment of horizontal agreements under the Act needs to be significantly changed. As it now stands, section 45 creates a most serious indictable offence, but does not give fair warning of what is prohibited. In addition, because no consideration can be given to efficiencies, section 45 is overinclusive and condemns practices which are not the object of "widely accepted moral disapproval", to use the words of Skeoch and McDonald<sup>37</sup>. We do not think it is appropriate for criminal liability, which entails heavy fines and possible incarceration, to depend on an analysis of complex economic factors by the court. A person's guilt should not hinge upon the court's views on cross-elasticity of demand, the height of barriers to entry or the strength of countervailing buying power, to give a few examples.

That alone, in our view, justifies amending section 45 to ensure that the criminal prohibition meets with widely accepted moral disapproval, and that guilt or innocence does not depend on the application of complex economic principles.

However, other anti-competitive horizontal agreements need to be prevented or discontinued if their prejudicial impact on competition is not offset by the benefits they generate. The law needs to be decriminalized in regard to such agreements, to alleviate the prosecution's burden of proof and to allow consideration of such agreements in a more dynamic, forward-looking context. There is no reason why horizontal agreements

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<sup>36</sup> *R. v. Clarke Transport Canada Inc.* (1995), 64 C.P.R. (3d) 289 (Ont. Ct. Gen. Div.).

<sup>37</sup> Skeoch and McDonald, *supra* note 26.

which are likely to generate benefits should be treated differently and more severely than mergers, which are simply another form of economic integration<sup>38</sup>.

These changes should result in better criminal law and help solve enforcement problems. We should have criminal prohibitions which are fair and that business people can understand. This should alleviate the chilling effect which results from existing law, which will in turn encourage beneficial agreements that now may never be implemented and contribute to economic improvement. Finally, revamping section 45 is an opportunity to harmonize our treatment of competitor agreements with the way they are dealt with by our key trading partners, and thus minimize the risk that an agreement with effects in more than one jurisdiction will be treated differently from an antitrust perspective.

For the reasons mentioned above, we believe that the *status quo* is unacceptable. There is no "quick-fix" to the problems resulting from section 45. For example, amending section 45 to allow the court to balance benefits against anti-competitive harm would increase the degree of economic analysis upon which guilt or innocence would depend. Even though consideration of pro-competitive effects is certainly desirable, the criminal courts are not the proper forum for measuring the economic consequences of an agreement. Another solution, which is not desirable, would be to delete the word "unduly" from section 45. This would extend the prohibition to any anti-competitive agreement, even *de minimis* situations, while not allowing for consideration of any benefits. Section 45 would be even more over-inclusive and have an even greater chilling effect. What is needed, in our view, is a complete redrafting of the law on horizontal agreements.

#### **4. The objectives of change**

In amending the law, we should attempt to reconcile as best as we can the following objectives:

- (a) making any criminal prohibition as clear and certain as possible so as to minimize the chilling effect on beneficial agreements;

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<sup>38</sup> Other commentators agree that horizontal integration by contract and by ownership should be treated on a similar legal footing; see, for example, P. Hughes, M. Sanderson and M.J. Trebilcock, Legislative Comment on *An Act to Promote Competition, to provide for the general regulation of trade and commerce, to promote honest and fair dealing, to establish a Competitive Practices Tribunal and the office of the Commissioner, to repeal the Combines Investigation Act and to make consequential amendments to the Bank Act*, Bill C-472 [unpublished]

- (b) maintaining criminal condemnation of hard core cartels, all of which should be severely punished;
- (c) minimizing the application of economic concepts such as markets, market power and efficiencies in the enforcement of any criminal prohibition;
- (d) avoiding criminal liability for competitor agreements which can reasonably be expected to generate efficiencies;
- (e) providing a means to prevent or terminate non-hard core horizontal agreements that significantly lessen competition if the lessening of competition is not offset by efficiencies.

There is no magic solution that reconciles all of these objectives. A vague criminal prohibition creates much flexibility but less certainty. A provision that actually lists every kind of agreement that is criminally prohibited is more certain but less flexible. Attempting to avoid criminal liability for *de minimis* situations by resorting to a bright line minimum market share criterion – as did Bill C-472 – might avoid condemnation of cartels with very little anti-competitive effect, but will quickly bring us back to asking the criminal courts to determine the relevant market and engage in complex competitive analysis. While there is no perfect solution, we think that the proposal described below would constitute a significant improvement over existing law and fairly balances the objectives listed above.

## **A PROPOSAL FOR CHANGE**

We believe section 45 should be replaced by two provisions, one criminal and one civil. The criminal provision would create a *per se* offence for hard core cartels. The civil provision, with a lower standard of proof, would allow the Commissioner to challenge before the Competition Tribunal (the "Tribunal") other horizontal agreements that substantially lessen competition.

Our proposal requires consideration of three different issues: the types of conduct which should be prohibited *per se*, the exceptions to the criminal prohibition and the scope of a new civil provision<sup>39</sup>.

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<sup>39</sup> In this regard, we are indebted to a short but thought-provoking article by Muris, T.J. "The New Rule of Reason", (1989) 57 Antitrust L.J. 859.

While we agree with the general structure of the model suggested by the Commissioner in our terms of reference, our proposal will make it clear that we have reservations with respect to some important aspects of this model.

## 1. The per se prohibition

There is relatively general agreement that hard core cartels should be criminally prohibited. As pointed out by Warner and Trebilcock, cartels charge monopoly prices but, unlike some monopolies and horizontal mergers, almost never generate offsetting efficiencies from economies of scale because the scale of production does not change.<sup>40</sup> Hard core cartels, aimed at increasing or preventing the reduction of prices or restricting output, virtually always lack any redeeming value.

Criminal prohibitions need to be certain and conviction should not depend on complex economic analysis. The word "unduly" should therefore be deleted and *per se* offences established in regard to hard core cartels. The challenge is to define the prohibition while avoiding condemning beneficial agreements or agreements that do not meet with general moral disapproval.

Most observers are of the view that agreements to fix prices, allocate markets or customers and restrict output should be condemned *per se*<sup>41</sup> as they are rarely, if ever, beneficial and their only effect is to reduce output and increase prices. Other proposals would also prohibit *per se* agreements to boycott competitors or suppliers or customers of a competitor<sup>42</sup>.

### (a) General Comments

We propose to review separately each of these categories of agreements. Before doing so, however, we wish to make some comments applicable to all *per se* prohibitions.

- (i) Any criminal prohibition must continue to apply to agreements only, not to unilateral conduct. Our courts have interpreted the words in the present section 45 ("... conspires, combines, agrees or arranges...") as requiring an agreement i.e.

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<sup>40</sup> Warner and Trebilcock, *supra* note 7 at 681-684.

<sup>41</sup> U.S. *Antitrust Guidelines for Collaboration Among Competitors* (April 2000) [hereinafter *US Antitrust Guidelines*]; *EC Guidelines*, *supra*, note 27 para. 18 and 25; OECD, *Hard Core Cartels*, (2000) [hereinafter *OECD*]; Public Policy Forum, *supra* note 9 at 28-29.

<sup>42</sup> See *inter alia* Bill C-472, *supra* note 8 and the model proposed in our terms of reference.

- a true meeting of the minds ("*actus contra actus*")<sup>43</sup>. We would recommend prohibiting simply "agreements". To use the words "agreement or arrangement", as in section 45(1) of Bill C-472, could lead to the conclusion that something less than a true agreement is prohibited.
- (ii) The new *per se* prohibitions should only be aimed at agreements among competitors, not at vertical agreements. This would differ from U.S. law which does not contain extensive provisions, as exist in Canada, dealing expressly with vertical practices such as price maintenance, tied selling, exclusive dealing and market restriction. Existing provisions of the Act are capable of dealing with harmful vertical agreements. Further, in condemning agreements among competitors, we do not think the courts would apply the prohibition to vertical agreements between parties who are otherwise competitors<sup>44</sup>. If there were any doubt about this, language could be added to make it clear that what is proscribed are agreements among competitors acting as such.
- (iii) The prohibition should extend to agreements among competitors and potential competitors; as pointed out by the Canadian Bar Association<sup>45</sup>, market allocation agreements are often made between parties that do not, but could compete with each other. The downside of extending the prohibition to potential competitors is the risk that the courts could be overbroad in their definition of this concept, which would undermine the objective of certainty. However, the prosecution's burden of proof beyond a reasonable doubt should limit the concept of potential competitors to firms that would probably become competitors in the absence of the agreement or that affect the conduct of existing competitors<sup>46</sup>.

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<sup>43</sup> *R. v. Gage* No. 2 (1908), 13 C.C.C. 428 at 450 (Man. C.A.); *Howard Smith Paper Mills v. R.*, *supra* note 15 at 413; *R. v. Atlantic Sugar Refineries Co. Ltd.* (1976), 26 C.P.R. (2d) 14 at 23 (Queb. Sup. Ct.); *Régie des marchés agricoles et alimentaires du Québec v. Fédération des producteurs de porcs du Québec* (9 June 1997), Montreal 500-09-002081-966 J.E. 97-1356 at 39 (C.A.); *R. v. Armco Canada Ltd.* (1976), C.P.R. (2d) 145 at 152-155 (Ont. C.A.).

<sup>44</sup> As suggested by McMillan Binch, *supra* note 10 at 24.

<sup>45</sup> *Supra* note 10, at p.46

<sup>46</sup> See *U.S. Antitrust Guidelines*, *supra* note 27 p. 2 note 6, which states that: "a firm is treated as a potential competitor if there is evidence that entry by that firm is reasonably probable in the absence of the relevant agreement, or that competitively significant decisions by actual competitors are constrained by concerns that anti-competitive conduct likely would induce the firm to enter".

- (iv) We would recommend not applying the *per se* prohibition to agreements among buyers for two principal reasons. First, we believe that agreements among buyers are generally far more likely to have pro-competitive effects such as lower prices and greater output for consumers than agreements among sellers:

"Our analysis suggests that buyer agreements are rarely likely to have significant anti-competitive effect and, therefore, that the antitrust treatment of joint buyer activity should not be symmetric to the treatment of joint seller activity. When sellers exercise monopoly power, the almost universal result is higher prices, lower output and misallocated resources; noneconomic values that many believe the antitrust laws are design to protect are impaired as well. In contrast, joint purchasing arrangements often produce lower prices and greater output for consumers without any serious threat of resource misallocation or any other impairment of the public interest as protected by the antitrust laws. The antitrust treatment of purchaser conduct should be correspondingly lenient."<sup>47</sup>

Second, our observation is that generally there is less concentration of buyers than sellers in Canadian markets and, therefore, groups of buyers are less likely to have market power than groups of sellers. There have been, in fact, very few cases brought in either Canada or the U.S. alleging illegal agreements among buyers, which suggests that the problem of anti-competitive agreements among buyers is considered by the enforcement authorities to be less problematic than anti-competitive agreements among sellers.

- (v) *Per se* prohibitions should not apply to agreements between affiliates, and this should include not only "companies" (as in the present section 45 and in Bill C-472) but also other entities such as controlled partnerships (see section 2(2) of the Act).
- (vi) There remains the question of whether the prohibition should be drafted by reference to the effects of the agreement ("... would or would be likely to have the effect of ... fixing, establishing, controlling or maintaining prices ..." as in Bill C-472), or by reference to the object of the agreement. We believe that referring to the "effect" of an agreement bears the serious risk of being overinclusive, because

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<sup>47</sup> Jacobson J.M. and Dorman G., "Joint Purchasing, Monopsony and Antitrust", (1991) The Antitrust Bulletin, Spring 1991, 1, at p. 2, an excellent article which discusses this and other aspects of the appropriate competition law treatment of conspiracies among buyers

it would cover agreements which have the indirect effect of, for instance, maintaining prices. The *per se* criminal prohibition should only apply to cartels which are aimed specifically at fixing prices, allocating markets and restricting output, not to agreements which might indirectly influence prices, markets and production. An alternative is to cast the prohibition in terms of the object of the agreement. This however would require the court to determine what is the true object of an agreement, which may in some cases prove to be a very difficult task<sup>48</sup>.

We think the best way to define the prohibited conduct is by referring to the nature of the agreement, rather than to its effect or object. A *per se* offence should be as simple as possible. We should adopt the section 47 model which creates a *per se* offence for bid-rigging by referring to the nature of the agreement. The new section should be drafted by reference to the nature of the agreement, for example by condemning agreements between one or more competitors or potential competitors by which the parties fix prices, allocate markets or restrict output. This approach would have the added advantage of simplifying the *mens rea* requirement. The Crown would have to show a subjective intent by the accused to enter into an agreement of the type described. There would be no need to discuss whether a distinct or different type of *mens rea* is required with respect to "likely effects" of the agreement.

(b) The *Per Se* Prohibition

(i) Price Fixing

No one would contest that, if there is to be some sort of *per se* prohibition, it must be aimed at price fixing agreements. The difficulty is to define the conduct we want to capture by the prohibition. In our view, the prohibition should be aimed at agreements by which the parties set the price at which they sell or offer to sell a product, agree to increase such price or agree not to reduce it. This would condemn an agreement on a floor price, which is in fact an agreement not to reduce the price. It would not however apply to an agreement on a genuine

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<sup>48</sup> For instance, in Bork's example of small retailers who fix the price of a product for purposes of joint advertising (referred to in Ross, *supra* note 7, at 862), liability would depend on whether the Court determined that their object was to fix prices or to jointly advertise.

ceiling price, because such agreement does not set, increase or prevent the reduction of the price of a product. We think the prohibition suggested is broad enough to apply to agreements on price components, i.e. factors which directly affect the price, like a discount, rebate, allowance or terms of payment. We are confident that the courts will consider agreements on discounts, rebates and allowances as tantamount to agreements to set, increase or not to decrease prices.

(ii) Market and Customer Allocations

As far back as 1969, the Economic Council had concluded that "collusive arrangements between competitors to allocate markets" should constitute *per se* offences<sup>49</sup>. There does not appear to have been much disagreement since then on this issue<sup>50</sup>. A *per se* prohibition of horizontal agreements, must therefore include market and customer allocation agreements, by which competitors agree not to compete with each other in certain territories or markets, or with respect to certain customers.

There remains the problem that the prohibition of agreements to allocate markets or categories of customers could apply to many commercial agreements which are generally viewed as beneficial, such as non-compete clauses in merger agreements, commercial leases and franchise agreements. And yet, no one would suggest the *per se* prohibition of such agreements. This confirms the need for an exception to any *per se* prohibition, no matter how tightly it is drafted. We discuss such an exception in the next section of this document.

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<sup>49</sup> *Supra*, note 4 at 101-102; the Council recognized the difficulty of *per se* bans and the requirement for some exceptions in favour of franchise agreements and "to allow the continuance of such practices whereby a group of drugstores in an area arrange that one or more of them will stay open on Sundays."

<sup>50</sup> Kennish and Ross, *supra* note 7 at 64, would prohibit as a *per se* offence "allocating, as between the parties or any of them, any markets, territories or customers ...". Bill C-256, *supra* note 5, would have banned agreements to divide or allocate markets. U.S. law has always prohibited market-sharing agreements as *per se* offences (ABA Section of Antitrust Law, *Antitrust Law Developments*, 4th ed. (Chicago: American Bar Association, 1997) at 97-100 [hereinafter *ABA Antitrust Law Developments*]). The EU considers such agreements to be among the most egregious cartels which almost always contravene section 81(1) of the EC Treaty (*EC Guidelines, supra* note 27 at para. 25) And, finally, the OECD discussion of hard core cartels refers to agreements to "divide or share markets as the most egregious violations of competition law ..." (*supra* note 41 at 6, referring to OECD, *Recommendations of the Council Concerning Effective Action Against Hard Core Cartels*, Doc. No. OECD C/M(98)7/PROV (25 February 1998).

We would therefore propose, subject to such an exception, the *per se* prohibition of agreements among competitors to allocate markets, territories, customers or sales.

(iii) Output Restriction

There is no doubt that a "bare" agreement to maintain or reduce output, is inherently anti-competitive. It could be argued that if price-fixing agreements are prohibited, there is no need for prohibition of output restriction agreements since they necessarily have an effect on prices. In fact, this is the reason why such agreements constitute *per se* offences in the United States:

"Because the law of supply and demand indicates that an agreement to limit output is tantamount to an agreement to fix price, courts have also applied the *per se* rule to agreements to limit production or set quotas, to discontinue a product ..."<sup>51</sup>

However, because we recommend that price-fixing should not be defined by reference to the effect of the agreement on prices, we think a separate prohibition for output restriction agreements is necessary. The wording should make it clear that the prohibition is aimed not only at agreements to reduce output, but also at agreements to maintain or not to increase production or supply of a product. The prohibition should also extend to agreements which prevent output, such as agreements to refrain from producing a product.

The problem here, as with any *per se* prohibition, is that it will also extend to agreements which can be beneficial, such as some forms of joint ventures or strategic alliances. This again confirms the need for an exception to the *per se* prohibition which we consider below.

We would therefore recommend a *per se* prohibition of agreements between competitors to prevent, reduce or maintain the production of a product. This would catch not only agreements to prevent, reduce or not to increase production, but also agreements on quotas, to discontinue a product, or to fix volumes or maximum volumes of products sold<sup>52</sup>.

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<sup>51</sup> ABA Antitrust Law Developments, *supra* note 50 at 82.

<sup>52</sup> See cases referred to in ABA Antitrust Law Developments, *supra* note 50 at 82 – 83

## (iv) Boycotts

An agreement to boycott is an agreement not to deal with one or more persons. It is easy to imagine concerted boycotts having anti-competitive effects, as where all competitors agree to pressure suppliers not to sell to a potential new entrant<sup>53</sup>. However, the anti-competitive harm is not always so evident and, in many cases, where it does exist, the concerted boycott might be part of an arrangement that generates some benefits. For example, buying groups might exclude some would-be members on perfectly legitimate grounds; ATM networks might exclude financial institutions because they do not meet certain technical requirements.

In the United States, concerted boycotts, sometimes referred to as agreements to refuse to deal, have been held to constitute *per se* offences in violation of section 1 of the *Sherman Act*. However, there is some confusion in U.S. law on this subject<sup>54</sup>. As stated by the ABA Section of Antitrust Law:

"In earlier cases, the Supreme Court routinely held horizontal refusals to deal to be *per se* violations of section 1. More recently, the Supreme Court and other courts have recognized that some horizontal refusals to deal should be examined under the rule of reason. As a result, the circumstances in which a concerted refusal to deal constitutes a *per se* unlawful group boycott have not always been clearly defined. As the Supreme Court has observed, 'there is more confusion about the scope and operation of the *per se* rule against group boycotts than in reference to any other aspect of the *per se* doctrine'."<sup>55</sup>

We have serious concerns about the *per se* prohibition of "primary or secondary boycotts directed at a competitor"<sup>56</sup>. It is noteworthy that, in its definition of hard core cartels, the OECD does not include boycotts<sup>57</sup>. Likewise, the European Guidelines do not include boycotts in the most egregious agreements "... that almost always fall under article 81(1)"<sup>58</sup>. The least that can be said is that there is no consensus that concerted boycotts are inherently anti-competitive and meet

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<sup>53</sup> This was one of the allegations, eventually dismissed by the Court, in *R. v. Atlantic Sugar Refineries Co. Ltd.*, *supra* note 43 at 61.

<sup>54</sup> See, for example, McQuinn, R. "Boycott Law After *Northwest Wholesale Stationer*" [1989] 57 *Antitrust L.J.* 839.

<sup>55</sup> *ABA Antitrust Law Developments*, *supra* note 50 at 101-102.

<sup>56</sup> Bill C-472, *supra* note 8, would have condemned as a *per se* offence agreements "boycotting a competitor or a competitor's suppliers or customers".

<sup>57</sup> OECD, *supra* note 41 at 6.

<sup>58</sup> *EC Guidelines*, *supra* note 27 at para. 25.

with "general moral disapproval". We would note that, unlike price-fixing, a boycott by its very nature becomes quickly known to the victim, and probably the Bureau to the extent that a complaint is lodged. In appropriate circumstances therefore, a civil proceeding (which might include readily obtainable injunctive relief) would likely follow and be a far more effective and expeditious remedy than a criminal prosecution.

We would therefore propose not to ban concerted boycotts as a *per se* offence, but such conduct would however remain subject to the civil provision discussed below.

## 2. The exception

The *per se* prohibition is aimed at banning as criminal offences agreements which have no other function than to increase prices or restrict output<sup>59</sup>: this is why they can be described as "hard core" cartels. Because such agreements usually have no other effect than to lessen competition, they meet with "widely accepted moral disapproval"<sup>60</sup> and should properly be prohibited as criminal offences.

No matter how carefully the *per se* prohibition is drafted, however, it will inevitably apply to agreements that are not hard core cartels and do not meet the test of moral disapproval. We have given examples of agreements that fix prices, allocate markets or restrict output, and yet which are not hard core anti-competitive restraints<sup>61</sup>. We believe that fairness dictates that there be an exception to the criminal *per se* ban for such agreements. We are not suggesting that these arrangements should escape antitrust scrutiny, merely that they should be excluded from the *per se* criminal prohibition and be subject to civil review, as discussed below.

The idea is to exempt from criminal condemnation agreements that in fact do fix prices, allocate markets or restrict output, but are not hard core cartels. Since what is contemplated is an exception to a criminal offence, it will have to be established before a criminal court. In order to attain the objectives set out above, the exception, if at all possible, should not require the court to define the relevant market, measure the lessening

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<sup>59</sup> In *Broadcast Music*, *supra* note 30 at para. 44, the U.S. Supreme Court refers to agreements which have "no purpose except stifling of competition".

<sup>60</sup> Skeoch and McDonald, *supra* note 26.

<sup>61</sup> The CBA Submission to the Public Policy Forum, *supra* note 10 at 45-46, lists a number of examples of such agreements; see also McMillan Binch, *supra* note 10 at 25-26.

of competition or the efficiencies, as the case may be, or determine if the efficiencies outweigh the competitive harm.

Ideally, the exception should be simple and have the following components:

- the anti-competitive restraint is part of a broader arrangement;
- this arrangement is likely to generate efficiencies; and
- the restraint is reasonably necessary to achieve the efficiencies.

Finally, we believe that the burden of proving the applicability of this exception should lie with the accused, on a balance of probabilities.

(a) Part of a Broader Arrangement

Our objective is to exempt price-fixing, market-sharing and output-restricting agreements that do more than just lessen competition, i.e. that are not hard core cartels. This necessarily means that they are part of a broader arrangement which includes features other than the anti-competitive restraint. Because the features other than this restraint may be embodied in a single agreement or in more than one agreement, we suggest defining the exception by reference to the words "broader arrangement" to capture both situations.

We are asked to consider the appropriateness of providing an exception to the *per se* prohibition based on the "ancillary restraint" doctrine. We are concerned that the use of the word "ancillary", as in Bill C-472, could imply that the restraint is an "accessory" to something else, and would require the court to determine if the anti-competitive restraint or the "something else" is the main purpose of the agreement between the parties. To refer to the example used above, if a number of small retailers fixed the price of a product which they jointly advertised, the "ancillary restraint" exception as worded in Bill C-472 could only be available if the court determined that the main purpose of the parties was joint advertising and not price-fixing. We think the exception should be available if the broader arrangement is likely to generate competitive benefits, irrespective of whether the benefits are ancillary to the restraint or the restraint is ancillary to the benefits, because criminal liability should not depend on what may amount to a subjective determination.

(b) Likely to Generate Efficiencies

The next step is to determine what kind of broader arrangement should be exempted from criminal liability even if it contains an anti-competitive restraint. The first possibility is that the nature of this arrangement is immaterial, as long as it contains features other than the competitive restraint. This is the approach used in Bill C-472, which would exempt collusion which is ancillary to "another agreement". There is no requirement as to what this agreement must be; it can, literally, be anything, as long as it is more than the anti-competitive restraint. The second possibility is to qualify the nature of the broader arrangement, which includes the anti-competitive restraint. Given the context of competition law, we are of the view that the broader arrangement must, at least, have some pro-competitive features.

We think the second option is preferable: an inherently anti-competitive restraint should not be exempted merely because it is part of a broader arrangement of any nature. There has to be some evidence that this arrangement generates or is likely to generate some pro-competitive benefits. An anti-competitive agreement should not escape criminal liability unless it has some competitive benefits, not merely because it is related to some other goal or likely to generate private benefits to the parties<sup>62</sup>. There must be some advantage to the competitive process.

This objective could be achieved by reference in the exception to "efficiencies" or to "competitive benefits"<sup>63</sup>. While the term competitive benefits might be broader than the concept of efficiencies, we think the exception should refer to efficiencies because, as this term is already well-known in competition law, this will create more certainty in the context of a criminal provision. Further, if the parties are of the view that their agreement will generate benefits to the competitive process, but are unsure as to whether such benefits constitute efficiencies, they could, by notifying their agreement as described below, avoid all risk of criminal liability. We would want all competitive benefits to be considered in the analysis, such as quality improvement, increased research and development, increased incentive to innovation, creation of new products and similar

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<sup>62</sup> Under current law, such factors are not relevant to the application of section 45: *Weidman v. Shragge*, *supra* note 13 at 147, 152; *Stinson-Reeb Builders Supply Co. v. R.* (1929), *supra* note 13 at 70; *Container Materials Ltd. v. R.*, *supra* note 13 at 152.

<sup>63</sup> Commentators are not always clear in this regard: some seem to consider the terms competitive benefits and efficiencies as interchangeable, while others distinguish the concepts; see for instance *US Antitrust Guidelines*, *supra* note 41, section 2.1; McQuinn, *supra* note 54, 840; Muris, *supra* note 39, 861-62.

benefits. We think however that such benefits can be considered to constitute dynamic efficiencies<sup>64</sup>.

In our view, the exception should not require showing that the arrangement would result in actual efficiencies. All that should be required is to show that the arrangement is likely to generate efficiencies. This would cover cases where the parties thought that their agreement would generate efficiencies which did not materialize, as long as the accused can show that the efficiencies claimed are plausible in the context of the broader arrangement. We are not suggesting that the exception should be available merely because the accused claim they believe their arrangement likely to generate efficiencies. The court will have to consider the nature of the arrangement and all surrounding circumstances, to determine whether it is plausible that efficiencies are likely to result from the alleged arrangement.

It may well be that efficiencies can only result from some form of economic integration<sup>65</sup>. However, we do not think it is necessary to specify in the exception that the broader arrangement should amount to economic integration. Once it is clear that what is required is a broader arrangement likely to generate efficiencies, its actual structure is not significant for the purpose of the exception.

(c) Reasonably Necessary to Achieve Efficiencies

It is not sufficient in our view to merely establish that the restraint is part of a broader arrangement likely to generate efficiencies. The parties should also have to show that the restraint is "reasonably necessary" to achieve the efficiencies generated by their broader arrangement. It is not sufficient that the parties have accompanied their cartel by legitimate beneficial joint activities: there must be a reasonable relationship between the restraint and the efficiencies, otherwise the parties to a hard core cartel could avoid criminal liability by merely adding unrelated features to their anti-competitive restraints.

The exception should be designed to exempt from criminal liability all arrangements that are not hard core cartels. The burden should therefore be to establish more than a mere contemporaneity between the restraint and the efficiencies, but less than showing that the restraint is essential to achieving the efficiencies or that no less restrictive alternative exists to achieve them.

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<sup>64</sup> As contemplated in the *Merger Enforcement Guidelines*, at Appendix 2 (Industry Canada, Director of Investigation and Research, Ottawa: Supply and Services Canada, 1991).

<sup>65</sup> *US Antitrust Guidelines*, *supra* note 41, section 3.2.

Finally, as indicated above, criminal courts are not the appropriate forum for economic debate. As a result, there should be no requirement to establish that the efficiencies are significant, or that they are sufficient to offset the competitive harm. The purpose of the inquiry is merely to determine whether the anti-competitive restraint is a hard core cartel or is reasonably related to an efficiency-enhancing arrangement, in order to escape criminal liability. This should not require the court to measure the harm against the benefits, an analysis which should be carried out in the civil context described below.

(d) Burden of Proof

Absent specific wording in a statutory provision<sup>66</sup>, the normal standard of proof for an exception or a defence to a criminal offence is that the accused must raise a reasonable doubt:

"The accused raises the defence by pointing to facts capable of supporting it, at which point the Crown must disprove the defence beyond a reasonable doubt."<sup>67</sup>

In other words, unless specific wording on the onus of proof is inserted in the exception, the accused would be able to escape criminal liability by merely raising a reasonable doubt as to the existence of an arrangement likely to result in efficiencies, and as to whether the anti-competitive restraint is reasonably necessary to achieve such efficiencies. Once the accused has raised a reasonable doubt, the Crown, to obtain a conviction, would have to establish beyond a reasonable doubt that the competitive restraint is not part of an arrangement, that it is not reasonably necessary to that arrangement, and that the arrangement is not likely to result in any efficiencies.

If this approach is used, we are concerned that the accused's burden of proof might be insufficient and result in unjustified acquittals in cases of true hard core cartels. As indicated above, the exception we contemplate would not require showing that the arrangement would generate actual or significant efficiencies, that such efficiencies constitute the main objective of the parties, or that the efficiencies outweigh the competitive harm resulting from the restraint. If the accused is only required to raise a reasonable doubt with respect to the elements of the exception, it may be too easy for parties to a hard core cartel to devise "arrangements" surrounding their collusive

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<sup>66</sup> See for example s. 45(7)(d) of Bill C-472, *supra* note 8, which does not refer to the burden of proof.

<sup>67</sup> *R. v. Sharpe*, [2001] 1 S.C.R. 45 at para 66.

activities, and thereby raise a reasonable doubt that such arrangements will result in some sort of efficiency. As any doubt in the trier of facts' mind must be resolved in favour of the accused, courts might acquit even on the basis of questionable evidence of efficiencies, if the accused's burden of proof is to merely raise a reasonable doubt. This would impair the Crown's ability to obtain convictions in the case of hard core cartels.

An alternative approach would be to impose a legal burden on the accused, i.e. to require that the accused establish the exception on a balance of probabilities. This however raises constitutional issues, because provisions requiring the accused to prove any facts on a balance of probabilities to avoid conviction violate the presumption of innocence guaranteed by sections 7 and 11(d) of the *Canadian Charter of Rights and Freedoms*<sup>68</sup>:

"The real concern is not whether the accused must disprove an element or prove an excuse, but that an accused may be convicted while a reasonable doubt exists. When that possibility exists, there is a breach of the presumption of innocence.

The exact characterization of a factor as an essential element, a collateral factor, and excuse, or a defence should not affect the analysis of the presumption of innocence. It is the final effect of a provision on the verdict that is decisive. If an accused is required to prove some fact on a balance of probabilities to avoid conviction, the provision violates the presumption of innocence because it permits a conviction in spite of a reasonable doubt in the mind of the trier of fact as to the guilt of the accused."<sup>69</sup>

This violation would have to be justified under section 1 of the Charter. While the scope of this paper does not allow us to embark upon a full-blown section 1 analysis<sup>70</sup>, our preliminary view is that the reverse onus provision may well be justifiable under section 1 of the Charter, *inter alia* on the following grounds:

- the accused is in a better position than the Crown to establish that the anti-competitive restraint is reasonably necessary to a broader arrangement and that there are efficiencies which are likely to flow from such arrangement;<sup>71</sup>

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<sup>68</sup> Schedule B to the *Canada Act 1982* (U.K.) 1982, c. 11.

<sup>69</sup> *R. v. Whyte*, [1988] 2 S.C.R. 3, para 31, 32 (emphasis added); see also *R. v. Keegstra*, [1990] 3 S.C.R. 697; *R. v. Laba*, [1994] 3 S.C.R. 965.

<sup>70</sup> As described *inter alia* in *R. v. Chaulk*, [1990] 3 S.C.R. 1303.

<sup>71</sup> See *R. v. Daviault*, [1994] 3 S.C.R. 63; *R. v. Stone*, [1999] 2 S.C.R. 290; *R. v. Curtis*, (1998) 38 O.R. 3d. 135 (C.A.). See also T.C. Arthur, "A Workable Rule of Reason: a Less Ambitious Antitrust Role for the Federal Courts" (2000) 68 *Antitrust L.J.* 337 at 380

- the Crown would have an extremely onerous burden if it were required to prove beyond a reasonable doubt that the anti-competitive restraint is not reasonably necessary for the alleged arrangement, or that the alleged arrangement would not generate any efficiencies<sup>72</sup>;
- the exemption actually creates a defence that would not otherwise be available to the accused<sup>73</sup>; as the Court stated in *R. v. Peck*<sup>74</sup>, an offence which would not be open to challenge if the defence was not offered at all, should not be struck down because Parliament created a defence additional to those available at common law.

A full section 1 analysis would consider if alternative, less restrictive approaches would achieve the desired objective of lowering the Crown's burden of proof. An alternative would be to draft a more demanding exception which could, for example, require showing the existence of significant efficiencies, or that the efficiencies outweigh the competitive harm, or that there are no less restrictive means to achieve the efficiencies, while keeping the lighter burden of proof based on reasonable doubt. However, as explained above, this alternative approach is not desirable, as it would involve criminal courts in economic analysis, a task which should properly be carried out in the civil context discussed hereafter.

(e) Notification

We have suggested a *per se* offence described with sufficient precision to limit its applicability to the most injurious types of anti-competitive restraints. We have also proposed an exception to this *per se* prohibition to further limit possible criminal liability in order to avoid the chilling effect on agreements likely to generate efficiency gains and which therefore should not be subject to a criminal procedure. However, because it may not always be easy to determine with certainty whether the exception applies, more particularly whether the anti-competitive restraint is reasonably necessary for the achievement of the efficiencies, and because the mere possibility of criminal liability will often prevent the implementation of beneficial arrangements, we have also considered whether a notification process should be adopted as a further exception to increase legal certainty.

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<sup>72</sup> *R. v. Whyte*, *supra* note 69; *R. v. Curtis*, *ibid.*.

<sup>73</sup> *R. v. Whyte*, *ibid.*; *R. v. Keegstra*, *supra* note 68; *R. v. Peck* (1994), 128 N.S.R.(2d) 206 (N.S.C.A.)

<sup>74</sup> *Ibid.* at 213.

Warner and Trebilcock<sup>75</sup> propose a *per se* prohibition for all secret or covert price fixing agreements. The only exception to this criminal prohibition would be for agreements notified to the Competition Bureau prior to taking effect. Notification would be optional, but would remove any threat of criminal sanction, as it would afford a complete defence to a criminal charge. Warner and Trebilcock propose a mere notification process, not a registration or authorization procedure, although they contemplate that the Commissioner could request further information in order to determine whether the agreement should be enjoined under a new civil provision relating to horizontal agreements which they also propose<sup>76</sup>.

This proposal has been commented upon by Kennish and Ross<sup>77</sup>, who are of the view that the proposed notification process is faulty because the Bureau could be buried in notifications and some hard core cartels may go largely unnoticed, particularly if they are dressed up to hide their true intent. Kennish and Ross are also of the view that because secrecy is frequently an important strategic weapon for firms undertaking significant initiatives, the parties may well choose not to notify to protect the confidentiality of their project and, under the Warner and Trebilcock proposal, thereby expose themselves to criminal prosecution.

Bill C-472 proposes a clearance certificate similar to the advance ruling certificate for mergers pursuant to section 102 of the Act, something very different from notification. Under section 79.2 of Bill C-472, the Commissioner would be authorized to issue a clearance certificate if he is satisfied that no substantial lessening of competition would result from the agreement. If the clearance certificate is issued, the parties would be immune from prosecution for three years under both the *per se* criminal prohibition and a new civil provision dealing with horizontal agreements. The Commissioner would be required to consider the requests for clearance certificates "as expeditiously as possible", but no time frame is given for the Commissioner's response. In addition, section 45(7)(c) would exempt from criminal liability agreements of which "notice was given to the Commissioner pursuant to section 79.2(1)"; however, no such "notification" is provided for in section 79.2, but only an "application" or a "request" for a clearance certificate.

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<sup>75</sup> Warner and Trebilcock, *supra* note 7.

<sup>76</sup> This proposal was recently reiterated, albeit with some interesting changes in P. Hughes *et al.*, *supra* note 38

<sup>77</sup> Kennish and Ross, *supra*, note 7.

An additional exception to the *per se* prohibitions proposed above, based on a notification process along the lines suggested by Warner and Trebilcock is, in our view, the best approach. This notification process would have the following characteristics:

- it would be a simple notification, not a request for exemption or a process which imposes a waiting period to the parties before implementation;
- agreements notified to the Competition Bureau would be immune from criminal prosecution, and as a consequence from section 36 actions for damages, for conduct subsequent to the date of filing of the notification; the agreements would however remain subject to the civil provision discussed below;
- immunity from prosecution would be maintained for conduct that is carried out in accordance with the terms of the agreement, and so long as no significant change is made to the agreement, in which case further notification would be required;
- notification would not be mandatory but would simply be an option offered to businesses wishing to avoid all risk of criminal liability, for example in cases where uncertainty remains as to the applicability of the exception described above;
- notification would only require information about the agreement and the parties thereto, and the filing of the relevant documents; it would then be open to the Commissioner to request more information if he felt that further investigation is called for to determine whether the agreement should be challenged under the civil provision;
- a modest fee would cover the costs of operation to the notification system;
- the notification would be confidential, as in the case of pre-merger notification filings, and section 29 of the Act would have to be amended accordingly; if notification were public<sup>78</sup>, we believe the system would not be effective, as business people would refrain from notifying rather than have their business agreements become public. In respect of confidentiality, as with other aspects of our proposal, the treatment of horizontal agreements should parallel that of mergers.

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<sup>78</sup> As suggested in P. Hughes *et al.*, *supra* note 38.

As Warner and Trebilcock point out<sup>79</sup>, because of the inherent imperfections of drafting, a *per se* prohibition will almost always be overinclusive and target potentially pro-competitive arrangements. Even though we have tried to restrain the scope of the *per se* prohibition by recommending an exception for agreements which generate efficiencies, there will always be room for uncertainty with the consequential chilling effect described above.

The notification process we propose provides the parties to an agreement with the option to eliminate all risk of criminal liability by simply notifying their arrangement to the Competition Bureau. Despite the fact that the proposed notification is not an authorization process, we are fully aware that the filing of a notification will, in some cases, properly trigger further inquiry by the Bureau, a consequence which may discourage some parties from notifying their arrangement. However, those who do not wish to proceed if there is the slightest risk of criminal sanction, will have the option to notify and therefore eliminate the risk of criminal liability. We think this is an alternative which should be given to Canadian businesses in order to encourage pro-competitive arrangements. It also provides for a means of avoiding criminal liability in the case of agreements which technically fall within the *per se* prohibition but have obviously only a *de minimis* effect on competition.

Our proposal should not overly burden the Bureau with notifications. For one thing, only arrangements which include an anti-competitive restraint, as defined in the *per se* prohibition, would have to be notified. Second, as the *per se* prohibition we propose would provide for an exception for restraints that are part of a broader efficiency-enhancing arrangement, there would not be the need to notify all arrangements which contain an anti-competitive restraint, as would have been the case under the Warner and Trebilcock proposal, which would criminalize all secret agreements which have a price-fixing effect. As a result, to respond to Kennish and Ross' criticism, those who prefer to maintain total secrecy will not necessarily have to notify their arrangement if they are satisfied that the agreement falls within the "broader arrangement" exception.

Third, it will not be necessary for the Bureau to carry out more than a cursory review of the information filed; in most cases, we believe that this information can be reviewed very quickly and will enable the Bureau to easily identify those arrangements

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<sup>79</sup> Warner and Trebilcock, *supra*, note 7 at 715-716.

where further inquiry or intervention is required under the civil provision discussed below.

Finally, because of the inherent secrecy of hard core cartels, there is very little risk in our view that parties to such agreements will notify to escape criminal sanctions; even if they did notify, their agreement would be subject to civil review and could still be prohibited and discontinued following notification, thereby protecting the public interest.

## **A NEW REVIEWABLE PRACTICE**

We believe that the Act should contain a new reviewable practice to deal with anti-competitive agreements among competitors which substantially lessen competition, and that there should be an efficiency exception to this provision.<sup>80</sup>

In light of our proposed amendments to section 45 to restrict the scope of criminal liability to hard core cartels, there is obviously a need for a further provision to deal with all other horizontal agreements which are covered by the current section 45. While these other competitor agreements do not in our view warrant criminal sanction, they may however have a prejudicial effect on competition which the law should prevent or curtail.

Some commentators suggest that there is no need for a new civil provision on competitor agreements because the current civil provision dealing with mergers and abuse of dominant position provide coverage for non hard-core horizontal agreements<sup>81</sup>. We do not agree with this proposition. First, there are numerous competitor agreements which do not qualify as a "merger" within the meaning of section 91 of the Act and therefore are not reviewable under the provisions applicable to mergers. Second, abuse of dominance requires establishing a practice of anti-competitive acts, i.e. acts which are aimed at excluding competitors. One of the fundamental characteristics of an anti-competitive act is that the competitor of the dominant firm(s) is a victim, not an ally<sup>82</sup>. Most agreements among competitors are not aimed at competitors. A new provision is required to deal with horizontal agreements which prevent or lessen competition but are not aimed at excluding or otherwise injuring competitors.

### **1. Scope of Reviewable Practice**

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<sup>80</sup> This is also the approach proposed by other commentators; see Warner and Trebilcock, *supra* note 7 at 972; Kennish and Ross, *supra* note 7; and Stanbury, *supra* note 7.

<sup>81</sup> McMillan Binch, *supra* note 10.

<sup>82</sup> *Canada (D.I.R.) v. NutraSweet Co* (1990), 32 C.P.R. (3d) 1 at 37 (Comp. Trib.).

In our view, the new civil provision, similar in nature to the other provisions of Part VIII of the Act, would have the following characteristics:

- It would authorize the Commissioner to apply to the Tribunal with respect to agreements between competitors which have or are likely to have the effect of preventing or lessening competition substantially in a market. It would apply to any horizontal agreement which has a substantial adverse effect on competition, not just those arrangements which contain an anti-competitive restraint and are exempted from the *per se* prohibition pursuant to the exceptions described above.
- It would apply to agreements between actual or potential competitors, but would not extend to vertical agreements. The Act already includes specific provisions dealing with some types of vertical agreements (such as sections 61 and 77). The new provision should not serve as a catch-all for agreements which Parliament has chosen not to include in the existing provisions dealing with vertical practices.
- The new provision would extend to agreements between competing buyers. Although there is no consensus that such agreements are inherently anti-competitive, which is why we recommend not including them in the proposed *per se* prohibition, buyer agreements can in some cases have anti-competitive effects and should therefore be reviewable.

As indicated above, the test under the new provision should be whether the agreement prevents or lessens competition substantially, the standard test used in the Act and in respect of which there is case law available for guidance. This would provide for an appropriate "rule of reason" analysis to evaluate the impact of the agreement on competition. However, we do not believe that the test should evaluate the "reasonableness of the agreements from a public interest perspective", as mentioned in the model described in our terms of reference. Re-introducing the concept of public interest in this provision would bring us back to section 33 of the *Combines Investigation Act*<sup>83</sup> dealing with mergers and monopolies which, as can be seen from the Supreme Court of Canada's decision in *Irving*<sup>84</sup>, is not the type of criteria which the courts can properly consider.

## 2. Exceptions

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<sup>83</sup> S.C. 1960, c. 45

<sup>84</sup> *R. v. K.C. Irving Ltd.*, [1978] 1 S.C.R. 408

An efficiency exception is absolutely essential in the context of this new provision, and the absence of such an exception in Bill C-472 is surprising. One of the objectives of the proposed overhaul of section 45 is precisely to allow for consideration of efficiencies in order to encourage efficiency-enhancing agreements. In fact, as mentioned above, one of the major problems with section 45 today is that efficiencies have been held to be irrelevant to the analysis. Additionally, most if not all efficiency-enhancing horizontal agreements will result in some form of economic integration. Because the merger provisions allow for an efficiency exception, a similar exception should apply to the new provision to avoid favouring mergers over other forms of economic integration. For this reason, we believe the efficiency exception contemplated here should, *mutatis mutandis*, mirror section 96 applicable to mergers. The object of this paper is not to discuss the scope of what would constitute an appropriate efficiency defence, an issue on which the expected decision of the Supreme Court of Canada in *Superior Propane*<sup>85</sup> will probably have significant bearing. The fact is however that the efficiency exception should be similar in nature, whether it applies to mergers or to other horizontal agreements.

There should also be an exception to the civil provision for agreements made exclusively between or among affiliates. The exception should extend to corporations and partnerships, to conform with section 2(2) of the Act.

### **3. Order of the Tribunal**

In order to make the treatment of other forms of economic integration consistent with the treatment of mergers, the Tribunal's powers should be limited to issuing orders similar to those listed in section 92 of the Act. In other words, the Tribunal should be empowered to prohibit the parties from implementing their agreement, in whole or in part, to order them to terminate an existing agreement, in whole or in part or, with the parties' consent, to take any other action. We believe the issue of whether the Tribunal should be authorized to order the parties, without their consent, to take action to overcome the anti-competitive effects of their agreement or to restore competition in the market, as contemplated in section 79.1(1)(d) of Bill C-472, could be problematic and should be given extensive consideration. We are concerned about incorporating in a provision dealing with horizontal agreements the extensive powers given to the Tribunal

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<sup>85</sup> *Canada (Commissioner of Competition) v. Superior Propane Inc.* (2001), 11 C.P.R. (4th) 289 (F.C.A.), leave to appeal to S.C.C. pending (Court file # 28593)

with respect to abuse of dominant position, exclusive dealing, tied selling and market restriction. These powers may be justified in cases where the exclusionary practices may have weakened competition to such a degree that an order prohibiting the continuation of the practice would be insufficient. In the case of horizontal agreements, however, if the parties are ordered to terminate their agreement, they remain competitors and can, without further intervention, restore competition to the market. As mentioned above, we believe the Tribunal should not have more extensive powers with respect to horizontal agreements than with respect to mergers.

Finally, it goes without saying that the consent order process contemplated in section 105 of the Act should apply to the new provision on horizontal agreements.

#### **4. Private Access**

Private access to the Tribunal has been discussed for some time and continues to be on the agenda. If a new civil provision on horizontal agreements is added to the Act, the issue of private access in this regard would require extensive consideration. Without expressing an opinion on the advisability of private access with respect to any of the other reviewable practices, we believe that there is little basis for permitting private access for mergers. Because, for the reasons outlined above, horizontal agreements should be dealt with in a manner which closely mirrors the treatment of mergers, we cannot see good reasons to permit private access with respect to horizontal agreements to which the new civil provision would apply.

### **CONCLUSION**

There is no perfect solution to the problems raised by section 45 because the objectives listed above cannot be entirely reconciled. We do not think however that this should prevent a much-needed improvement to our law. We reiterate our conviction that section 45, as it stands now, is not appropriate criminal law because it does not give fair warning of what is prohibited, not to mention the resulting significant chilling effect.

We think that our proposal is a solid basis for change and a significant improvement over present law.

Due to the limited time available to us, we have not been able to consider the many other necessary consequential changes to the Act which would be required if our proposal is implemented. For instance, we would need to consider repealing or amending subsections 45(2) to 45(8) and sections 45.1, 46, 48, 49, 85 to 90 and 61 of the Act. It is

quite clear that some of these provisions will become redundant e.g. subsection 45(2) and 45(2.2) relating to the meaning of unduly lessening of competition and to the *mens rea* requirement.