REGULATORY AND POLICY DEVELOPMENTS

REGULATION OF FINANCIAL INSTITUTIONS

By: W.A. Kennett
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Federal Financial Reform

The new federal trust and loan legislation is now stalled on the desk of Minister of State for Finance, Thomas Hockin. In a period of election planning and with a crowded legislative calendar, financial institutions legislation has no priority. This is particularly the case when the ownership -commercial links policy of the government is still being actively resisted. It is now doubtful that a new bill will be tabled in the House of Commons before the summer recess. With every month's delay it becomes less likely that any more financial institutions legislation will be passed in this Parliament.

Ontario

In the meanwhile, the Province of Ontario proclaimed its *Loan and Trust Corporations Act* on April 5, 1988. New regulations came into effect at the same time. This is the first major update of this legislation since it was enacted over seventy years ago.

Québec

As noted in the last *Canadian Competition Policy Record*, the Province of Québec passed its new *Trust Companies and Savings Companies Act* on December 18, 1987. This legislation is now in force.

True to the Québec White Paper, the *Act* does not discriminate on the basis of ownership, thus sanctioning closely and widely held companies, and commercially linked companies. The *Act* also provides that not more than one-third of the board of directors may be officers or employees of the company. The board is required to have both an ethics committee and an audit committee. A "restricted party" is broadly defined and loans to such persons are prohibited with a few limited exceptions.

Extra-provincial companies must be licensed to operate in Québec and cannot exercise powers in the province that are not available to Québec companies.

Unlike the draft federal act where the powers of the Minister are numerous, the Québec act gives full powers to the Inspector General, except the power to create or force the dissolution of a company.

On March 29, 1988, the Honourable Pierre Fortier presented his first Quinquennial Report to the Québec National Assembly on the implementation of the *Securities Act*. The report finds that the *Act* is operating well but does make a few recommendations for change. The most interesting of these is that the Minister and the Chairman shall consult regularly and if a disagreement occurs the Minister may, with the approval of the government, issue written instructions and the Commission shall comply. Securities Commissions have tended to take on a life of their own at the expense of ministerial responsibility. Québec is apparently going to settle that issue in favour of ministerial responsibility.

On April 12, 1988, Minister Fortier issued a discussion paper on the deregulation of market intermediaries. The proposals would allow insurance agents and securities salespeople to market multiple but related products and would permit networking and the establishment of financial supermarkets.

Federal Provincial Relations - Securities Markets

Identical Canada-Ontario and Canada-Québec securities agreements were signed on March 25, 1988. The agreements confirm the basic division of responsibilities established by Canada and Ontario in April, 1987. They also establish sole provincial responsibility for the regulation and supervision of securities firms allowing the federal authorities access to their books and records only through the provincial authorities. The provincial authorities will be able to access the records of federally chartered parents of securities firms through the federal authorities.

With these jurisdictional problems sorted out, Minister Hockin has approved the entry of several foreign securities firms. A reciprocal arrangement has been made with the Japanese, enabling three Japanese firms to enter. Foreign banks seeking permission to establish securities firms have been discriminated against so far for reasons that are not clear.

Securities regulators from Ontario and Québec and a representative of the Office of Superintendent of Financial Institutions participated in an important first meeting of securities regulators of member countries of the Organization for Economic Cooperation and Development in May. This may be the first step in an effort to coordinate and strengthen securities regulation internationally.

Consumer Protection

Finally, credit card interest charges and financial institution service charges are continuing to attract the attention of governments. A federal-provincial working group on the cost of credit disclosure published a report in April entitled Discussion Paper on Credit Card Interest Charges. This could prove to be the first step towards the regulation of the form these interest charges may take and the requirements for their disclosure.

The House of Commons Committee on Finance and Economic Affairs has held hearings on service charges and their recommendations are awaited with great interest.

THE OWNERSHIP OF CANADIAN FINANCIAL INSTITUTIONS

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Who can own a Canadian financial institution? Unfortunately there is no simple answer to that question. In fact, the relevant rules are in a state of flux as a result of the current process of regulatory reform. This commentary is intended to summarize the new ownership regime that is emerging from that process. Some key indicators, at the federal level, of the way ahead are:

- the Blue Paper, "New Directions for the Financial Sector," released on December 18, 1986;
- Bill C-56, now passed into law, that enables federally regulated financial institutions, namely banks and certain insurance, trust and loan companies (FFI's) to invest in securities dealers;
- the draft *Loan and Trust Companies Act*, released on December 21, 1987;
- Bill C-130 to implement the *Canada-U.S. Free Trade Agreement*, given first reading on May 24, 1988.

The following is a description of the new ownership rules and is drawn principally from these sources.

Cross Ownership

Under the new federal rules already in place (Bill C-56), FFI's are now permitted to make a substantial investment in the shares of a securities dealer, subject to the approval of the Minister of Finance. That authority is to be extended to cover investments made by an FFI in the shares of any other financial institution, of whatever variety. The federal barriers to cross-ownership among different types of financial institutions are, therefore, to be eliminated. However, if an investment is made by an FFI in a provincial financial institution there are opportunities for more rather than less regulation - by the federal government through the conditions of ministerial approval and by the provincial government through its regulatory authority over the target

company. This has led to jurisdictional disputes between the federal and provincial governments in the case of investments by banks in securities dealers the only area in which there has been experience under the "open" system of cross-ownership.

Ownership by Commercial Interests

The walls between different types of financial institutions are to be replaced by a ceiling separating financial from commercial activities. Under the proposed federal rules a commercial (non-financial) entity may be denied approval either to incorporate an FFI subsidiary or to acquire more than 10% of the shares of an established FFI. Where an FFI already has a significant shareholder that is a commercial entity, no divestment will be required but that shareholder will be unable to increase its proportionate interest in the FFI. This approach may be relaxed somewhat in the case of insurance companies, which often have significant commercial associations.

Concentration of Ownership

The new credo seems to be that "big may be beautiful but the bounty must be shared." Any non-bank FFI that has a capital base of $750 million will have to have at least 35% of its shares listed for trading and widely held. For such an FFI that is commercially linked, the capital threshold is a mere $50 million. A five year grace period will be allowed to enable the big players to get on side.

Foreign Ownership

It will remain open, as at present, for a foreign-owned entity to establish a new FFI. Such action will be subject only to the rules of general application and to the requirement of giving a simple notification under the *Investment Canada Act*.

The current restrictions on the purchase of shares of an operating FFI by a foreign-controlled entity will continue to apply. These relate to all FFI's except property and casualty insurers. Generally speaking, no one foreigner may acquire more than 10% of the shares of an affected company and, collectively, foreign investors may not acquire more than 25% of such shares. But, under Bill C-130, such restrictions will not apply to U.S. residents or entities controlled by them.

These restrictions cannot normally be avoided by the foreign acquiror effecting an asset purchase or an amalgamation rather then a share purchase. The former transactions are subject to ministerial approval and such approval is likely to be withheld if control of an FFI would otherwise be transferred to foreign hands.

Absolute Limits on Ownership

The only absolute limit on the proportion of the shares of an FFI that may be held by a single shareholder, other than those thrown up by the corporate concentration and foreign ownership rules, will relate to Canadian banks that are not foreign bank subsidiaries. As is the case at present, no one person will be entitled to hold more than 10% of the shares of a domestic bank. However, the current "new bank" exception to that rule will be broadened so that a small bank that is not commercially linked may remain closely held until its capital base reaches $750 million.

Discretionary Restrictions on Ownership

An FFI other than a bank will be subject to a new ministerial approval requirement in the event that a proposed transfer of shares would result in the transferee holding 10% or more of any class of shares. In deciding whether to approve a particular transfer the Minister of Finance will be directed to apply the same sort of criteria to the transferee that he would apply to the incorporator of a new FFI - for example, whether the person in question has the necessary financial resources and business experience and is a non-commercial entity. This approval system will be retroactive to December 18, 1986, the date of the Blue Paper, in the sense that the Minister will have the power, in the public interest, to order the divestiture of shares acquired as a result of any "ten percent transaction" occurring after that date. On the other hand, it is not possible to apply for ministerial approval until the new legislation is enacted. Pending such enactment, the Minister should be advised in advance of any "ten percent transaction"

in the hope that the absence of any immediate objection can be taken as an indication that the Minister will not later make an order requiring the disposal of any shares acquired in the transaction.

Conclusion

The ownership rules for Canadian financial institutions are clearly undergoing significant adjustments. As with many other areas of regulatory change affecting such institutions, the much vented objective of de-regulation has been overshadowed by a large measure of new regulation.

THIRD PARTY REVIEW OF CANADA POST CORPORATION RATES AND SERVICES ANNOUNCED

By: John F. Blakney
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The Minister responsible for Canada Post Corporation has recently announced that he has opted for a third party review agency for Canada Post Corporation (CPC) rates and services levels which would have a statutory basis and the express authority to make recommendations to the Governor in Council on rates and service levels. The Governor in Council would, however, retain its current power to set CPC rates.

The Minister has, therefore, rejected the option of a formal independent regulatory agency modelled along the lines of the CRTC in its telecommunications regulation capacity, an option which had been favoured by the 1985 Marchment Committee report on CPC's legislative mandate, policies, practices, and future needs.

The advisory board and regulatory agency models had previously been reviewed in some detail in a government discussion paper published on March 28, 1988. The advisory board model employed in the discussion paper involved the following elements:

- statutory mandate
- members appointed by Governor in Council
- resources for a supporting professional staff
- discretionary powers to hold informal hearings and to conduct independent research;
- powers to compel evidence from CPC;
- customer complaint mediation processes;
- requirement for public reports;
- power to review both rates and service quality.

This model blends what the discussion paper describes as the better elements of the postal administration review bodies of the U.K. and Australia.

The advantages attributed to this advisory board model included:

- low cost accessibility to all users;
- low operating costs;
- ready implementation;
- ability to consider issues and make recommendations quickly and without lengthy appeal processes;
- no significant reduction in CPC management flexibility;
- preservation of the government's flexibility in decision-making;
- consistency and depth of understanding;
- public and intervenor confidence.

On the other hand, the regulatory board model was regarded as offering consistency, credibility, a prospect of reducing political involvement in CPC rate-setting, and the ability to expressly balance rates with quality of service.

The selection of the advisory board model is perhaps a recognition that costs of a regulatory board in terms of costly and formalized decision-making procedures outweighed any greater reduction in the political interference in CPC rate-setting beyond that which an advisory board might provide.

In reviewing the U.S. Postal Rate Commission, which is also restricted to an advisory role, the government's discussion paper notes that the slow and costly quasi-judicial hearing mode of evidence gathering has possibly delayed the U.S. Postal Service's financial turn around, has proven too time consuming and expensive to smaller users, and has encouraged larger users and competitors to appeal Commission decisions to the courts.

As well, in reality, the government would likely ensure that it had the power to vary or rescind an agency's rate-setting decision, particularly since a low rate award may lead to

government subsidies of CPC's operations. Such a provision, of course, inevitably opens the door to continuing caucus and Cabinet efforts to influence postal rate and service decisions.

Finally, the Minister's decision may also involve an implicit recognition that CPC's monopoly is not clearly so firmly founded as the monopoly of electricity, gas, or basic telephone service suppliers and that the establishment of a new formal price regulation body may well do more over the long run to help enshrine existing but eroding CPC monopoly powers than to protect consumers and ensure an efficient postal system.

On June 27, 1988, the Minister responsible for Canada Post announced that he planned to introduce legislation implementing the advisory board model in the near future. At the same time he announced the establishment of an interim Postal Services Review Committee to be chaired by Alan Marchment, author of the 1985 report on CPC noted above, to review rates and service issues. Separate Postal Service Customer Councils established for each CPC operating division, each having a full-time coordinator and part-time volunteers, will review and make recommendations on local and regional service matters.

CRTC TO REVIEW RESALE AND ENHANCED SERVICES RULES

On June 10, 1988, the CRTC issued a public notice announcing a review of its 1984 rules governing the classification of services as either basic or enhanced, and, by implication, the extent to which basic services may be resold as part of an enhanced services package.

The CRTC's initiative was prompted by separate applications by Call-Net Telecommunications Ltd. for a general enhanced services policy review and also specific guidance on whether certain calling features are basic or enhanced, and by Bell Canada to obtain guidance on whether Call-Net had restructured its operations in a manner consistent with the Commission's resale rules by August 19, 1988, as has been permitted by the federal Cabinet.

The Call-Net application contends that the combination of the Commission's decision that Call-Net's customized account recording and call forwarding features constituted basic service, when read with the Commission's definition of a basic service as including an "underlying" service which is capable of being used either with or without an enhancement even if they are not available to customers without the enhancement, has had the effect of ruling out the possibility of competition in enhanced voice services other than store and forward message services.

The Call-Net application also observes that, since the CRTC announced its enhanced services policy in 1984, the Commission has relaxed restrictions on resale and sharing and has significantly reduced the prices of MTS/WATS service. This reduced the potential policy concern over the loss of MTS revenue contribution to local service costs that greater resale of MTS/WATS as part of an enhanced service might entail. Call-Net, therefore, contends the Commission need no longer take as stringent an approach to the types of enhanced services which may be provided competitively using underlying long-haul leased services. In place of the current "primary function" test for enhanced services noted above, Call-Net has proposed a looser public interest test using cost-benefit analysis on a case by case basis as has been applied in CRTC system interconnect proceedings such as CNCP's 1983 application to provide public long distance service.

Call-Net also refers to the federal government's discussion paper on Telecommunication Policy published in the *Canada Gazette* in December, 1987 and to the Enhanced Telecommunication Services provisions of the *Canada-U.S. Free Trade Agreement* as evidence of a trend favouring the provision of greater opportunities for enhanced services competition.

The Commission has indicated that it intends to issue a decision prior to Call-Net's present restructuring deadline of August 19, 1988.

J.F.B.

NTA RULES ON VIA RAIL/VOYAGEUR FARE DISPUTE

By: Frank Trotter, President
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The motor coach industry in Canada has made application to both the Canadian Transport Commission (CTC), and the new National Transportation Agency (NTA), several times in the past three years to complain of VIA's low passenger fares.

On April 15, 1986, Greyhound Lines of Canada Ltd. and Eastern Canada Greyhound Lines Ltd. filed for leave to appeal VIA Rail Canada Inc.'s Special Local Passenger Tariffs CTC-X-98, CTC-X-99 and CTC-X-105 pursuant to sections 281 and 283 of the *Railway Act* and section 23 of the *National Transportation Act* on the basis that these were prejudicial to the public interest. On November 7, 1986, the CTC Railway Transport Committee concluded that the application disclosed an issue which might, upon investigation, disclose prejudice to the public interest as defined in section 3 of the *National Transportation Act* and granted leave to appeal pursuant to section 281 of the *Railway Act* and section 23 of the *National Transportation Act*. A preliminary staff report, dated May 1987, provided the results of the investigation by the staff. It stated that "in essence, the issue to be determined is whether VIA has engaged in predatory pricing practices" (p. 39). No determination of this issue, was made and at the end of August, 1987, the application was withdrawn before the hearing commenced.

On April 29, 1987, Voyageur Inc. (the operating company in Québec which is part of Les Entreprises Voyageur Ltée.) applied, pursuant to section 281 of the *Railway Act* and section 23 of the *National Transportation Act*, for leave to appeal certain VIA Rail Canada Inc. regular one-way fares on specified routes in the South Shore-Gaspé region of Québec, connecting with Québec City and Montréal. At a hearing held on July 2, 1987, the CTC Railway Transport Committee found that the public interest might be prejudiced if Voyageur's allegations were true and announced that it would investigate the matter further. A preliminary staff report of the Traffic and Tariffs Branch was released on September 13, 1987, which found little in support of Voyageur's allegations.

On September 14, 1987, Voyageur filed an application pursuant to sections 281 and 283 of the *Railway Act* in respect of VIA discount fares of 50 per cent which were filed to take effect September 8 December 17, 1987, over parts of the same routes that were subject to the original application. On December 30, 1987, the Railway Transport Committee issued its decision which denied Voyageur's application. That decision is now the subject of an application for review, dated January 29, 1988, to the new National Transportation Agency on the grounds that the Committee erred in the following ways in its decision:

(a) The Committee failed to conduct the investigation and render the decision it should have under section 281 of the *Railway Act* because it addressed issues and questions outside the scope of that section and, as a result, did not deal with the applications which were before it.
(b) The Committee erred in law when it based its decisions on irrelevant considerations.
(c) The Committee erred in law when it failed to take into account relevant considerations in conducting its investigation and rendering its decision.
(d) The Committee ignored relevant evidence.
(e) The Committee failed to apply proper legal principles in dealing with Voyageur's complaint that VIA's fares were unreasonably low.

That application is outstanding at this date.

On May 17, 1988, Voyageur Colonial Ltd. (the operating company in Ontario which is part of Les Entreprises Voyageur Ltée.) applied to the National Transportation Agency pursuant to sections 281 and 283 of the *Railway Act*, section 44(2)(b), 35(4), 40(2) and 40(3) of the *National Transportation Act*, 1987, with respect to proposed fare reductions by VIA on Ottawa-Montréal and Montréal-Toronto routes, requesting a final order disallowing the discount tariffs, or in the alternate, leave to appeal and subsequent final orders requiring VIA to remove the prejudicial features of the discount tariffs, and an interim order suspending the discount tariffs until the Agency has rendered a

final decision. The application was heard in a marathon session May 20, 1988, by a panel of the Agency: C. Dickson (Chairman), E. O'Brien and J. Mutch. The discount tariffs which were due to come into effect June 1, 1988, were suspended pending a public hearing which was subsequently scheduled to begin June 10, 1988.

By the commencement of the hearing, the case had attracted considerably more attention than had been the case in the previous several years, with the following interventions registered: Consumer's Association of Canada (the only group previously appearing in VIA/bus cases), Ontario Motor Coach Association, Greyhound Lines of Canada Ltd., Québec Bus Owner's Association, Government of Québec, Director of Investigation and Research *(Competition Act)*, CP Rail and Transport 2000. In addition, a variety of "public interest" witnesses filed written comments with the Agency, as did other industry representation (bus companies and bus manufacturers). After a number of procedural matters were addressed (Voyageur had provided responses to VIA interrogatories while VIA claimed all Voyageur interrogatories were confidential or irrelevant), the panel heard two days of evidence and cross-examination of Voyageur's marketing witnesses.

The Director of Investigation and Research intervened in the case for three purposes:

1) To clarify the general competition law principles relating to predatory pricing, with particular attention being given to the application and effectiveness of the predatory pricing provision of the *Competition Act*.
2) To make comment on the compensatory rate provision under the *Railway Act* and their interpretation in light of the compensatory rate provisions for rail freight appearing in the *National Transportation Act* and the definition of the public interest therein.
3) To make comment with respect to the commercial activities of Crown corporations and the importance that such corporations be subject to market forces free from artificial advantages unavailable to the private sector.

Voyageur claimed that the discount VIA fares on the Toronto-Montréal and Ottawa-Montréal routes are predatory, have a detrimental effect on the surface passenger transportation market, and are contrary to the public interest. Voyageur also claimed that rail and bus are competitors, that cross-subsidization between "profitable" corridor routes to support "unprofitable" rural routes is an accepted feature of the industry and that the discount VIA corridor fares thereby jeopardize the ability of the industry to support those rural services. Finally, Voyageur submitted that VIA fares below avoidable cost, when they affected the competitive alternative (bus), were contrary to the public interest, in particular, the provision of "a safe, economic, efficient and adequate network of viable transportation services making the best use of all available modes of transportation at the lowest total cost."

VIA has responded, in this and previous cases, that passenger rail transportation is a matter of public policy, that it is well-known that VIA services operate at a loss, that VIA costs are not relevant in the setting of VIA fares and that discounting practices are common in the transportation industry. According to VIA, as long as the discount program results in a net contribution to the revenues of VIA and thereby lessens the level of subsidy, then there should be no limits to VIA's discount levels.

The hearing has been adjourned until July 5, 1988.

FEDERAL REGULATORY PROCESS REFORMS TAKE ON NEW LEGAL SIGNIFICANCE

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A recent decision of the Federal Court, Trial Division, has added new, and unexpected, significance to the regulatory process reforms adopted by the Mulroney government in 1986. Mr. Justice Muldoon granted the plaintiffs in *Teal Cedar Products (1977) Ltd. v. Her Majesty the Queen et al* (unreported) an interlocutory injunction prohibiting the federal government from enforcing export control restrictions on certain cedar products which the plaintiffs manufactured. In granting the injunction, the court relied on information in a Regulatory Impact

Analysis Statement (RIAS) published with the regulations as evidence that Cabinet may have acted without jurisdiction in passing the Order in Council which added the cedar product to the Export Control List. The court concluded that information concerning the need for, and impact of, the measure provided to Cabinet through the RIAS might have been erroneous and may have misled Cabinet with the result that it might have acted without proper authority under the *Export and Import Permits Act.*

The Crown is appealing the case, but the implications of the court's reference to the RIAS must be causing officials in Ottawa to look at the process requirements with renewed attention.

In 1986, the federal government implemented wide-ranging reforms to its internal decision-making systems. The government adopted, for the first time in Canada, a comprehensive policy concerning the use of regulatory intervention. Process reforms were implemented under the *Citizen's Code of Regulatory Fairness* and the Federal Regulatory Process Action Plan. Departments and agencies were to prepare Annual Regulatory Plans, giving advance notice of the areas in which they were proposing to regulate. Draft regulations were to be pre-published in the *Canada Gazette* under a standardized notice and comment procedure. Every regulation was to be accompanied by a Regulatory Impact Analysis Statement (RIAS) which provided basic information on the need for, and impact of, the proposal. All regulatory programs were to be reviewed on a regular cycle to ensure that they were still required.

As is the norm in the federal government, these new process requirements were not given legal force through legislation. They were detailed in a Cabinet policy decision and implemented through issuance of a public policy document and through administrative instructions relayed by the newly-formed Office of Regulatory Affairs to federal departments and agencies. It was never intended that failure to comply with some aspect of the government's internal procedures would endanger the validity of a regulation. The concept of an omnibus legislated rule-making procedure, similar to that found in the U.S. federal *Administrative Procedures Act*, had been considered in Ottawa years before, and had not been adopted.

Of all the federal reforms, the requirement to prepare and publish a RIAS was, perhaps, the most significant. Prior to the new system, proposed regulations, accompanied by an often sketchy "Explanatory Notice" were given routine approval by a Cabinet committee and published in the *Canada Gazette.* It is common knowledge that these regulations were rarely scrutinized by ministers.

The RIAS requirement was implemented to serve two purposes, one internal to the government and the other external. First, the RIAS ensures that ministers are given key information about the need and impact of a proposal so that they can make an informed judgment when exercising their authority under enabling legislation. RIASs are a primary source of information for ministers who serve on the Cabinet committee which approves regulations. Second, the RIAS provides greatly improved information to the public concerning a regulation. Under the government's notice and comment procedures, RIASs are published with draft regulations in the *Canada Gazette Part I* and again with the final text of the regulations in the *Canada Gazette Part II.*

Publication of the RIAS for each regulation amounts to publication of one of the relevant internal cabinet briefing notes, a practice which is heretical in a government system devoted to the principle of Cabinet secrecy. It was this dual nature of the RIAS which made it so useful to the plaintiff in the *Teal Cedar Products* case.

Teal Cedar Products, in effect, got caught in the crossfire between Canada and the U.S. in the red cedar shakes and shingles dispute. In the summer of 1986, the U.S. imposed a 35% import tariff on shakes and shingles from Canada. This had the effect of raising the price for the manufactured product, making the unmanufactured raw materials comparatively more attractive. Canada has also long had export controls on logs. Wood products, however, are included in General Export Permit No. 2 for surveillance purposes.

As part of its defensive strategy, the federal government stopped the export of red cedar "bolts" and "blocks", which are unmanufactured sections of split cedar logs. Clearly, the government's intention was to prevent the transfer of shake and

shingle manufacturing jobs from Canada to the U.S.

The ban on exports of red cedar bolts and blocks was accomplished in June, 1986 by adding the products as item 2003 of the Export Control List, thereby requiring that an export permit be obtained. The federal government stated from the outset that such permits would normally be refused.

The authority to establish the Export Control List is found in section 3 of the *Export and Import Permits Act:*

3. The Governor in Council may establish a list of goods, to be called an Export Control List, including therein any article the export of which he deems it necessary for any of the following purposes, namely:
   - (a) (national security— not applicable in this case)
   - (a.1) to ensure that any action taken to promote the further processing in Canada of a natural resource that is produced in Canada is not rendered ineffectual by reason of the unrestricted exportation of that natural resource;
   - (a.2) to limit or keep under surveillance the export of any raw or processed material that is produced in Canada in circumstances of surplus supply and depressed prices and that is not a produce of agriculture;
   - (b) to implement an intergovernmental arrangement or commitment; or
   - (c) to ensure that there is an adequate supply and distribution of such article in Canada for defence or other needs.

Teal Cedar Products, however, was not manufacturing and exporting bolts and blocks, but "short cedar boards" which were not named in item 2003. A short cedar board is a manufactured product machine cut to length, machine cut on all four sides, and kiln-dried. Two shingles can be made by cutting a short board on a diagonal plane.

In January, 1988, the government officially advised Teal Cedar Products that permits would be required for export of short cedar boards to the U.S. After Teal responded with a suit against the government and an injunction application, the government withdrew its requirement. However, it promulgated a new regulation in February, 1988, which, in effect, added "blanks, boards, and any other material or product of red cedar suitable for use in the manufacture of shakes or shingles" to item 2003 of the Export Control List. Paragraphs 3(a.1) and (c) and section 6 of the *Export and Import Permits Act* were cited as enabling authority for the regulation.

The RIAS which was published with the new regulation stated that Canadian firms were exploiting a loophole in the original regulation by exporting red cedar blanks suitable for the manufacture of shingles and shakes. The change would simply fulfill the original intent of the June, 1986, regulation which was intended to prevent the loss of Canadian jobs in the shakes and shingles manufacturing industry. The RIAS stated that long term adverse effects on the industry would result if the change was not made. It was estimated that between 1,200 and 2,400 jobs might be lost to the U.S. if export of semi-processed cedar materials was allowed to continue. The RIAS further stated that, without the amendment, prices for shakes and shingles would be depressed, Canadian raw material prices would rise, and small firms would be forced out of business.

Teal amended its statement of claim and continued its action, seeking relief from enforcement of the new regulation. It sought an interlocutory injunction prohibiting the defendants from interfering with the export of short cedar boards until the case went to trial. Teal's problem, as found by Mr. Justice Muldoon, was that the new regulation would effectively put it out of business, with a loss of over 150 employees.

As summarized by the court, the plaintiff's case was that Cabinet had been misled about the regulation's "devastating impact" on the jobs of Teal employees, and since the object of the enabling authority in paragraph 3 (a.1) is to preserve jobs in Canada, the new regulation was *ultra vires.* The plaintiff filed affidavits asserting, among other things, that "there is no less labour involved in producing short cedar boards than there is in producing shingles." The court accepted this evidence, stating:

> In regard to those demonstrably verified assertions, it appears that the regulatory impact analysis statement takes no account of the

> plaintiff's plight or that of other similarly situated enterprises and their employees. (Reasons, pp. 10, 11)

The federal government's case, as summarized by the court, was that regardless of the information contained in the regulatory impact analysis statement, the new regulation was a "lawful expression of government policy and a legitimate act of governance in close accord with the statutory powers conferred on the Governor in Council". The defendants filed an affidavit of a government official which asserted that if exports of red cedar boards were not restricted, fewer workers would be required because the productivity of shingle machines almost doubles when short boards are being cut instead of shingles.

As noted above, the court accepted the plaintiff's assertions on the productivity question, but noted that neither side's depositions had been tested through cross-examination of the deponents.

With regard to paragraph 3 (c) of the *Export and Import Permits Act* ("maintain an adequate supply of articles in Canada for defence or other needs"), the court noted that the RIAS and the deposition of the government official were silent about any purported needs relating to national defence. Referring to the RIAS, the court stated:

> ...one wonders, then, whether the Governor in Council was misled in formulating the Order in Council, or whether reference to paragraph 3(c) was just deliberately thrown in for good measure. (Reasons, p. 13)

In granting the plaintiff an interlocutory injunction, the court reviewed jurisprudence relating to judicial review of Governor in Council decisions and to the conditions under which a court would grant a stay of proceedings or an injunction against enforcement of legislation pending litigation as to its *vires*. Citing the decision of the Supreme Court of Canada in *Attorney General of Canada* v. *Inuit Tapirisat of Canada & al*, [1980] 2 S.C.R. 735, (1980) 115 D.L.R. (3d) 1, the court held that the defendant ministers, their agents and public servants were not immune from being temporarily restrained from enforcing the new regulation if it appeared that the Governor in Council had failed to observe the provisions of paragraph 3 (a.1) of the *Export and Import Permits Act* by considering misleading information.

The court then considered the circumstances under which interlocutory injunctive relief would be granted in cases where the validity of legislation is at issue. Adopting the three-part test set out by the Supreme Court of Canada in *Att'y Gen'l of Manitoba* v. *Metropolitan Stores Ltd. & al.*, [1987] 1 S.C.R. 110, Mr. Justice Muldoon first accepted that the plaintiff's case raised "a serious question to be tried as opposed to a frivolous or vexatious claim":

> Here, the plaintiff avers that it has evidence and argument in law to show that without the demonstrable misinformation which apparently misled the Governor in Council, there was no statutory basis for promulgating...(the new regulation), which has been deadly to the plaintiff's business....
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> * * *
>
> This is an interlocutory proceeding, which does raise a serious, but narrow question for trial, although not a broad *prima facie* case. (Reasons, p. 20)

The court found that the plaintiff also had satisfied the second part of the test, "irreparable harm":

> The only imposition of irreparable harm in these circumstances lands squarely on the plaintiff which is driven out of business by enforcement of the impugned item of the export control list and lack of an appropriate export permit, with the concurrent and disastrous loss of more than 150 employees' jobs. (Reasons, p. 21)

Finally, considering the third element of the test, "balance of convenience", the court held that the Government of Canada and the general public would suffer "negligible and probably imperceptible" inconvenience from the interlocutory injunctive relief sought by the plaintiff. On the other side, the court determined that failure to grant the relief would result in irreparable harm to the plaintiff.

In concluding that the plaintiff was entitled to an interlocutory injunction, the court further commented:

> ...although there is no proof thus far of bad faith, the defendants can be seen to have pursued and snared the plaintiff by means of their regulation-making powers. In the beginning, the plaintiff was lawfully conducting its employment-generating business when its exportation of short cedar boards was

apparently unlawfully obstructed by one or more of the defendants' minions. The plaintiff then started this lawsuit and the defendants, no doubt realizing or having been advised that they were in the wrong, countermanded their orders to obstruct. Ten days later and as if in lieu of lodging a statement of defence, the defendants promulgated the item, 2003, of the export control list, whereby the plaintiff's employment-generating enterprise could be, and was, put out of business. The defendants enjoy that marvellous advantage of being able to make and amend the law precisely in order to thwart the plaintiff's enterprise and its legal recourse in response thereto. Without the interlocutory injunction, the plaintiff might not have the resources to litigate this case.

* * *

In the role of a delegated regulation maker, even the Governor in Council may perform in such a way, may appear to take such advice as well as such inordinate advantage for the government's purposes as will, until final adjudication, render the government susceptible to an interlocutory injunction. (Reasons, pp. 24, 25)

The Federal Court's order in this case enjoined the defendants, other than Her Majesty the Queen, from interfering with the plaintiff's exportation of short cedar boards and required the government to issue a valid and subsisting export permit for the duration of the injunction, notwithstanding any further amendment of the export control list.

As noted above, the federal government hasfiled notice of appeal against the injunction. In the appeal, it is likely to pursue the argument it raised in the first instance that, following *Thorne's Hardware Ltd.* v. *The Queen* [1983] 1 S.C.R. 106, courts cannot enquire into the validity of the beliefs of the Governor in Council in order to determine the validity of an Order in Council.

Regardless of the outcome of the appeal, the mere fact that a RIAS was accepted as evidence that Cabinet might have been misled concerning the impact of a regulation is a significant development. At the very least, it should cause federal department and agencies to carefully review the content of their impact analyses, and perhaps tighten up internal procedures for legal scrutiny before RIASs are submitted to Cabinet and published in the *Canada Gazette*. If the result is better and more accurate information for ministers and the private sector, the development will have been beneficial whether or not the court's decision is not upheld on appeal. If, however, the result is to "sanitize" RIASs so that they are devoid of information that might be used to support an application for judicial review, Cabinet ministers and the private sector could both end up as the losers and much of the potential of the government's regulatory process reforms in this area will have been thwarted.