COMMENT AND ANALYSIS

IMPLEMENTING FOREIGN CONSPIRACIES: GUILTY NOTWITHSTANDING?

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The recent conviction, following a guilty plea, of a Canadian corporation for implementing a foreign conspiracy pursuant to s. 46 of the *Competition Act* raises the issue of the constitutional validity of that provision.[1]

In order to ensure that the prohibition on trade conspiracies in Canada remains an effective one in an international business community, few would dispute the need to deter foreign conspiracies in this country. Section 46 of the *Competition Act* purports to do just that. This provision provides that a corporation in Canada is deemed guilty of an offence when the corporation implements a "foreign directive", that directive being for the purpose of giving effect to a conspiracy in contravention of s. 45. The corporation is guilty of the offence "whether or not any director or officer of the corporation in Canada has knowledge of the conspiracy." In other words, the section penalizes participation in a conspiracy absent intent or knowledge of the illegal activity.

It is submitted that s. 46, while a strong measure obviously designed to counter the implementation of foreign conspiracies in this country, may violate the *Canadian Charter of Rights and Freedoms* as it fails to provide for a minimal *mens rea* component and constitutes an absolute liability offence for which there is no defence of due diligence.

A brief review of the elements of the offence of conspiracy and the classification of offences is necessary for a full understanding of the potential constitutional deficiencies of s. 46 of the Act.

The Offence of Conspiracy

There are two material elements to the offence of conspiracy in s. 45 of the *Competition Act*: an agreement entered into by the accused; and an undue prevention or lessening of competition flowing from that agreement.[2] The mental element of the offence requires proof of both subjective and objective fault.[3] To satisfy the subjective element, the Crown is required to prove that the accused had the intention to enter into the agreement and had knowledge of the terms of the agreement. The objective component requires the Crown to establish that on an objective view of the evidence, the accused intended to lessen competition unduly.

With respect to the first element, that of "agreement", the statutory offence is much like criminal conspiracy under the *Criminal Code* and our courts have required more than knowledge of a plan or passive acquiesence to convict under this legislation. Thus, a conviction for criminal conspiracy will result where there has been some meeting of the minds.[4]

The requirement of active participation appears to be preserved in s. 45 of the *Competition Act* given that the Supreme Court has stated that it must be proved that the accused intended to enter into an agreement and have some knowledge of its terms. Thus, the offence differs from its *Criminal Code* counterpart as a consequence of the addition of the objective component, with the result that the Crown need not prove that the accused actually intended to lessen competition unduly.

Classification of Offences

Most regulatory offences are considered as *prima facie* "strict liability" offences. These terms were defined by the Supreme Court of Canada in the seminal case of *R.* v. *City of Sault Ste. Marie*.[5] The *Sault Ste. Marie* decision established that three types of offences exist which Dickson J. (as he then was) described as follows:

> 1. Offences in which *mens rea*, consisting of some positive state of mind such as intent, knowledge, or recklessness, must be proved by the prosecution either as an inference from the nature of the act committed, or by additional evidence.
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> 2. Offences in which there is no necessity for the prosecution to prove the existence of *mens rea*; the doing of the prohibited act *prima facie* imports the offence, leaving it open to the accused to avoid liability of proving [on a balance of probabilities] that he took all reasonable care. This involves consideration of what a reasonable man would have done in the circumstances. The defence will be available if the accused reasonably believed in a mistaken set of facts which, if true, would render the act or omission innocent, or if he took all reasonable steps to avoid the particular event. These offences may properly be called offences of strict liability...
>
> 3. Offences of absolute liability where it is not open to the accused to exculpate himself by showing that he was free of fault.[6]

Subsequently, the Supreme Court of Canada in *R.* v. *Wholesale Travel Group Inc.*[7] concluded that the *Competition Act* is essentially regulatory in nature and therefore characterized the offence of misleading advertising as falling into the second category, the offence being one of strict liability for which a defence of due diligence is required and proof of a mental element is not required. Conversely, in *R.* v. *Nova Scotia Pharmaceutical Society*,[8] the Supreme Court held that the offence of conspiracy in s. 45 requires proof of some mental element.

The offence created by s. 46 is more closely akin to the statutory offence of conspiracy. Indeed, it penalizes an accused for commiting an act which, if the accused had been charged pursuant to s. 45, could constitute

the *actus reus* of the offence of conspiracy. Instead, the Crown may elect to charge the accused with implementing, thus avoiding difficult questions of proof of intent. In defending charges under s. 46, a corporate accused may face the prospect of a conviction for its role in a foreign conspiracy in the absence of any guilty intent or active participation in the sense required to otherwise support a conviction under s. 45. Section 46 requires the Crown only to prove the implementation of a foreign directive and upon proof of implementation, the corporation is deemed guilty of an offence. Although the section does not specifically provide that the offence is one of absolute liability, that is its effect.

The "Guilty Mind" and the *Charter*

By not requiring the mental element of knowledge, s. 46 of the *Competition Act* could be challenged as an infringment of s. 7 of the *Charter*, which protects the right to life, liberty and security of the person, and section 11(d) of the *Charter*, which protects the right to be presumed innocent until proven guilty. In this respect, three principles can be gleaned from recent Supreme Court jurisprudence which are relevant to the discussion of *mens rea* and the *Charter*.

First, legislation which creates an absolute liability offence coupled with imprisonment is unconstitutional. However, whether or not the same rationale applies where a corporation commits an absolute liability offence for which only a fine can be imposed is unclear.

Second, the same constitutional standards do not necessarily apply to regulatory offences as those that apply to true criminal offences. As already noted, the Supreme Court has characterized the *Competition Act* as essentially regulatory in nature, despite the fact that the Act carries serious penal consequences for a breach thereof.

Third, a minimum level of *mens rea* must be proved for some offences, whether criminal or regulatory in nature. What level of *mens rea* is constitutionally required depends on the stigma resulting from a conviction and the severity of the penalties imposed.

Absolute Liability Offences

The Supreme Court of Canada, in *Reference re Section 94(2) of the Motor Vehicle Act*,[9] struck down as unconstitutional a British Columbia statute which created an absolute liability offence applicable to driving with a suspended license. The statute provided that a person who drove a motor vehicle while prohibited from driving or whose licence had been suspended, committed an absolute liability offence whether or not the accused knew of the prohibition or suspension. The accused was subject to a mandatory jail term of 7 days.

Lamer J. (as he then was), commented that "it has from time immemorial been part of our system of laws that the innocent not be punished."[10] However, he was also of the view that absolute liability offences do not *per se* offend s. 7 of the *Charter*. In this respect, he stated:

> A law enacting an absolute liability offence will violate s. 7 of the *Charter* only if and to the extent that it has the potential of depriving life, liberty or security of the person.
>
> Obviously, imprisonment (including probation orders) deprives persons of their liberty. An offence has that potential as of the moment it is open to the judge to impose imprisonment. There is no need that imprisonment, as in s. 94(2), be made mandatory.
>
> I am therefore of the view that the combination of imprisonment and of absolute liability violates s. 7 of the *Charter* and can only be salvaged if the authorities demonstrate under s. 1 that such a deprivation of liberty in breach of those principles of fundamental justice is, in a free and democratic society, under the circumstances, a justified reasonable limit to one's rights under s. 7.[11]

Lamer J. did not address the question of whether imprisonment as an alternative to the non-payment of a fine for an absolute liability offence, or a term of minimum imprisonment in such circumstances would similarly offend s. 7. However, he did comment that he would not want to be taken as having inferentially decided that absolute liability may not offend s. 7 so long as imprisonment or probation orders were not available as a sentence. In this case, the argument had only been directed at the "liberty" component of s. 7 and not at "security of the person." Thus, it remains an open question whether punishment other than imprisonment for an absolute liability offence may in some circumstances similarly offend the *Charter*.

Such a result is less clear however, in the case of a corporation. In this respect, Lamer J. commented that:

> Even if it be decided that s. 7 does extend to corporations, I think the balancing under s. 1 of the public interest against the financial interests of a corporation would give very different results from that of balancing public interest and the liberty or security of the person of a human being.[12]

The Ontario Court of Appeal, in *R.* v. *Metro News Ltd.*,[13] applied the reasoning in the *Reference re section 94(2)* case in striking down the former s. 159(6) of the *Criminal Code* which, in the Court's view, created an absolute liability offence in violation of s. 7 of the *Charter*. Section 159 of the *Code* provided that any one who distributed obscene written matter committed an offence while s. 159(6) provided that the fact that the accused was ignorant of the nature or presence of the obscene matter was no defence. Martin J.A. characterized s. 159(6) as creating an unconstitutional absolute liability offence for which a penalty of imprisonment was possible.[14]

It was contended, however, that s. 7 offered no protection to the corporate accused because imprisonment as a penalty could not apply to a corporation. Martin J.A noted that s. 159(6) was not limited in its application to a corporate accused and that any human person so charged would be liable to imprisonment. Therefore, a corporation could defend a criminal charge on constitutional grounds even though it would not be liable to the same penalty.

Given that the wording of s. 46 of the *Competition Act* is somewhat similar to that considered in both the *Reference re Section 94(2)* and the *Metro News* cases, one might at first blush conclude that the provision creates an unconstitutional absolute liability offence. However, any constitutional prohibition on absolute liability offences must be balanced against the principle that regulatory and *Criminal Code* offences might require different constitutional treatment.

Regulatory Offences and "True" Crimes

The fact that the *Competition Act* is regulatory in nature and the offences contained therein involve a lesser degree of moral culpability obviously had some influence on the Supreme Court in rendering such decisions as *Thomson Newspapers Ltd.* v. *Canada (Director of Investigation and Research, Restrictive Trade Practices Commission)*,[15] and the *Wholesale Travel Group* case.

In *Thomson Newspapers*, the issue was whether s. 17 of the *Combines Investigation Act,* which permitted the examination of witnesses and production of records, violated either of s. 7 or s. 8 of the *Charter.* In coming to his conclusion that neither s. 7 nor s. 8 had been infringed, LaForest J. noted that the Act was not truly criminal in nature and therefore a lesser degree of privacy should be granted to witnesses. In this respect, he commented that:

> ...the Act is really aimed at the regulation of the economy and business, with a view to the preservation of the competitive conditions which are crucial to the operation of a free market economy...
>
> The conduct regulated or prohibited by the Act is not conduct which is by its very nature morally or socially reprehensible. It is instead conduct we wish to discourage because of our desire to maintain an economic system which is at once productive and consistent with our values of individual liberty. It is, in short, not conduct which would be generally regarded as by its very nature criminal and worthy of criminal sanction. It is conduct which is only criminal in the sense that it is in fact prohibited by law...
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> The Act is thus not concerned with "real crimes" but with what has been called "regulatory" or "public welfare" offences.[16]

In the *Wholesale Travel Group* case, the Court considered whether the offence of misleading advertising in the *Competition Act*, which is constituted as a strict liability offence, violated s. 7 of the *Charter.* In drawing the conclusion that the misleading advertising provisions met the constitutional hurdle, three of seven judges commented that regulatory and criminal offences must be accorded different constitutional treatment. Cory J. pointed out that regulatory offences and crimes embody different concepts of fault and the former import a lesser degree of culpability.[17] Applying the comments of LaForest J. in *Thomson Newspapers*, Cory J. concluded that the *Competition Act* in all its aspects is regulatory in character and that the offence of false advertising, because it is not one involving moral turpitude, should be considered regulatory and not truly criminal in nature.

A Minimum Level of *Mens Rea*

The Supreme Court of Canada has suggested that for some offences the *Charter* mandates a minimum level of *mens rea*, whether that be proof of subjective or objective intent or of negligent conduct.

As discussed above, the Supreme Court decided in the *Reference re Section 94(2)* case that absolute liability offences will offend the *Charter* when combined with mandatory imprisonment. However, the Court was careful to note that not all absolute liability offences will *per se* offend the *Charter*. The Court's comments on *mens rea* in that case were further explained in a series of cases dealing with the constructive murder provisions of the *Criminal Code*, those cases being: *R.* v. *Vaillancourt*, [18] *R.* v. *Martineau*,[19] *R.* v. *Logan*,[20] and R. v. *Rodney* [21] and with statutory rape: *R.* v. *Nguyen*; R. v. *Hess*.[22]

In *Vaillancourt,* Lamer J.(as he then was) discussed the relationship between sections 7 and 11(d) of the *Charter* in respect of the *mens rea* component of an offence. He concluded that before an accused can be convicted of an offence, the trier of fact must be satisfied beyond a reasonable doubt of the existence of all of the essential elements of the offence. Any provision which permits conviction notwithstanding the existence of a reasonable doubt on any essential element offends both sections 7 and 11(d). Both provisions will also be infringed where the statutory definition of the offence does not include an element which is required by s. 7.

Lamer J. was also of the view that one of the principles of fundamental justice enshrined in s. 7 is that a minimum mental state is a constitutionally required element of certain offences. For the purposes of this appeal, the Supreme Court assumed that a conviction should not be obtained for murder in the absence of proof beyond a reasonable doubt of at least objective foreseeability, leaving for another time the question of whether proof of subjective intent might actually be required in respect of constructive murder offences. However, in his view, the constructive murder provisions at issue on the appeal permitted a conviction even in the absence of a reasonable doubt of objective foreseeability. Because the provisions so permitted, they also infringed s. 11(d) of the *Charter*.

In the *Martineau*, *Logan* and *Rodney* cases, all of which were heard together, the Court struck down the remaining constructive murder provisions of the *Criminal Code* and read down s. 21(2) of the *Code* which provides that persons with an intention in common to carry out an unlawful purpose with another person who commits an offence, when each of them knew or ought to have known that the commission of the offence would be a probable consequence, is a party to that offence.

Lamer C.J.C., writing the majority judgments in all three cases, makes it clear that subjective intent is the minimum fault requirement for murder, given the special stigma which attaches to murder and the

seriousness of the penalties provided for. With respect to s. 21 of the *Criminal Code*, Lamer C.J.C. held that if the principles of fundamental justice require a minimum *mens rea* in respect of the principle offence, the same minimum level of *mens rea* is required to convict a party to that offence pursuant to s. 21.

In the *Regina* v. *Nguyen*; *Regina* v. *Hess* case, the Supreme Court considered the constitutionality of the offence of statutory rape. Former s. 146 of the *Criminal Code* provided that every man who had sexual intercourse with a female under the age of 14 years, whether or not he believed her to be 14 years of age or more, was guilty of an indictable offence for which the penalty was imprisonment for life.

Wilson J., writing for the majority of the Court, concluded that s. 146 of the *Code* removed the defence that the accused *bona fide* believed the female to be more than 14 years of age. In her view, offences which are punishable by imprisonment and which do not allow the accused at a minimum, a due diligence defence, offend s. 7 of the *Charter*.

Subsequently, in the *Wholesale Travel Group* case, it was argued that given the stigma arising from a conviction and the penalties imposed in respect of the *Competition Act* offence of misleading advertising, the minimum acceptable level of *mens rea* required proof of subjective intent. The accused contended that the section violated the *Charter* because proof of subjective *mens rea* was not a requirement of the offence for which imprisonment was available as punishment. A majority of the Court upheld the misleading advertising provisions of the *Competition Act* but struck down a portion of the statutory due diligence defence.

There is no clear rationale for the Court's decision to uphold the offence. Cory J., L'Heureux-Dubé J. concurring, concluded that s. 7 of the *Charter* requires proof of some degree of fault.[23] That fault may be demonstrated by proof of subjective or objective intent, or by proof of negligent conduct depending on the nature of the offence. With respect to regulatory offences, Cory J. held that proof of negligence satisfies s. 7 of the *Charter*. Regulatory offences do not involve moral blameworthiness in the same manner as criminal fault and should be treated differently from criminal offences given the "licensing" rationale which underlies regulatory legislation. In Cory J.'s opinion, those who choose to participate in regulated activities place themselves in a responsible relationship to the public and must accept the consequences of such responsibility.

Lamer C.J.C. concluded that because the offence of misleading advertising is punishable by up to five years imprisonment, it cannot be an offence of absolute liability and mandates a minimum fault requirement of negligence for which the defence of due diligence must be available. Hence, the offence is one of strict liability. However, neither was subjective *mens rea* required by the *Charter* for all offences. The offence of misleading advertising did not carry the same type of stigma as *Criminal Code* offences.

Conversely, the Supreme Court has also recently determined that the conspiracy provision in the *Competition Act* does require some proof of subjective *mens rea* in respect of one element of the offence. In the *Pharmaceutical* case, the accused were charged with offences pursuant to s. 45(1)(c) and sought a declaration that s. 45 was in violation of s. 7 of the *Charter* on the basis that the provision did not require subjective *mens rea* to be established and that the word "unduly" rendered the section impermissibly vague.

Gonthier J., writing for the Court, applied the Court's previous decision in *Wholesale Travel Group* and held that the requirement of a mental element of fault is constitutionally guaranteed by the *Charter*. He noted that fault may be established by proof of intent whether subjective or objective or by proof of negligent conduct, depending on the nature of the offence. Gonthier J. concluded that s. 45 is composed of both subjective and objective elements. To satisfy the subjective element, the Crown must prove that the accused had the intention to enter into the agreement and had knowledge of the agreement.[24] To satisfy the objective element, the Crown is required to prove that on an objective view of the evidence, the accused intended to lessen competition unduly. In Gonthier J.'s view, this was sufficient to withstand the constitutional test with the result that s. 45 did not violate s. 7 of the *Charter*.

To summarize, the Supreme Court of Canada has interpreted the constitutional requirement of *mens rea* in the following manner:

1) where the penalty of imprisonment will follow on conviction, the acceptable constitutional minimum *mens rea* must be at least negligence;

2) where the offence is one for which there is a stigma on conviction and which carries severe penalties, subjective *mens rea* may be required;

3) the *Competition Act* offence of misleading advertising is an offence of strict liability for which the minimum *mens rea* is negligence;

4) the *Competition Act* offence of conspiracy to lessen competition requires proof of both subjective and objective *mens rea*. With respect to subjective *mens rea*, the Crown must prove that the accused had the intention to enter into the agreement and had knowledge of the agreement.

Implementation of Foreign Directives as Absolute Liability Offences

The above principles may not necessarily be applicable to the foreign directive provision in the *Competition Act*. First, it is clear from the Court's reasons in the *Reference re Section 94(2)* case that some absolute liability offences may meet the constitutional hurdle. Because a corporation is not subject to a term of imprisonment, absolute liability in this context may be unobjectionable. Unlike the provision considered in the *Metro News* case, the foreign directive provision clearly applies only to a corporate accused and not to human persons.

Second, Cory J.'s approach in the *Wholesale Travel Group* case indicates that a somewhat lesser constitutional standard applies to *Competition Act* offences, given the Act's regulatory character. However, given that the Court has already determined negligence to be the appropriate standard in respect of the offence of misleading advertising, and that the offence of conspiracy pursuant to s. 45 requires proof of subjective *mens rea*, it is doubtful that the constitutional *mens rea* standard for implementing could justifiably approach absolute liability.

On the other hand, if one were to adopt the approach of Lamer C.J.C. in the *Wholesale Travel Group* case, it is less clear that negligence is necessarily the minimum basis upon which to convict a corporation for regulatory offences. Lamer C.J.C. based his decision on the fact that the penalty imposed was 5 years imprisonment and therefore, following his reasons in *Reference re Section 94(2)*, an offence of absolute liability was prohibited. A corporation, if convicted of conspiracy pursuant to s. 45 or implementing pursuant to s. 46, is not similarly subject to imprisonment. On this basis, a court may conclude that negligence is not the appropriate minimum standard in respect of implementing and that s. 46 does not therefore create an unconstitutional absolute liability offence.

In the above discussion, it has been assumed that at a constitutional minimum, negligence is the appropriate *mens rea* standard in respect of s. 46. However, given that the offence of implementing has the effect of deeming an accused to be guilty of participation in a conspiracy, there is some basis to suggest that s. 46 requires the same minimum *mens rea* as is constitutionally required for the s. 45 offence of conspiracy. Section 46, in abrogating the mental element, is in direct conflict with the *Pharmaceutical* case which holds that some subjective intent must be proved in order to support a conviction for conspiracy pursuant to s. 45.

As s. 46 is currently worded, a conviction may result where the accused has committed an overt act which furthers the foreign conspiracy in the absence of the requisite mental element which would otherwise be constitutionally required under s. 45. For example, a Canadian corporation may be directed by its foreign parent to bid a certain price for a particular tender. The Canadian corporation may have no knowledge that the foreign parent is involved in a foreign conspiracy and that the Canadian corporation's actions in bidding that price will constitute an act in furtherance of the foreign conspiracy. Clearly, such an act under s. 45, absent any mental intent to enter into the agreement, would not constitute an offence. Conversely, under s. 46, such an action is an offence. It may be difficult for the Crown to put forward any substantial policy rationale which would justify different *mens rea* standards for implementing a foreign conspiracy and taking part in a domestic conspiracy.

Should s. 46 be successfully challenged, the proper remedy would undoubtedly be reading down and not a wholesale striking out of the entire provision. In *R.* v. *Schachter*,[25] the Supreme Court defined the ambit of s. 52 of the *Charter* in respect of a court's ability to grant remedial relief by striking down or reading in legislative provisions.

The Court held that in choosing a remedial course under s. 52, the extent of the inconsistency which must be struck down must be defined. In some circumstances, the inconsistent portion must be struck down broadly. This will almost always be the case where the purpose of the legislation is not sufficiently pressing or substantial to warrant overriding a *Charter* right. Where the purpose of the legislation is pressing and substantial, but the means to achieve that objective are not rationally connected to it, the inconsistency to be struck down will generally be the particular portion of the legislation which fails the rational connection test. Where the measures do not impair as little as possible the right in question or are not proportional to the objective, severance, reading in or striking down may be appropriate.

Section 46 of the *Competition Act* is composed of two aspects. One aspect is the purported extension of Canadian jurisdiction to foreign conspiracies. In this respect, s. 46 is somewhat similar to s. 465 of the *Criminal Code*. The second aspect is the deeming provision of the section which removes the mental element of the offence and any due diligence defence. Thus, any constitutional challenge arises as a result of the words "deemed" and "whether or not the directors of officers had knowledge."

It is unlikely that a court would strike the section down in its entirety given that the purpose of the legislation is undoubtedly sufficiently pressing and substantial (see for example the Court's decision in *Wholesale Travel Group* where the purpose of the misleading advertising provisions was held to be sufficiently important). If the Crown failed to prove rational connection and proportionality as required by s. 1 of the *Charter*, a court could simply strike out the offending words with the result that a conviction could be obtained where the Canadian corporation implemented a foreign directive either knowing it to be in furtherance of a foreign agreement to lessen competition or having turned a blind eye to the foreign conspiracy. Permitting a conviction where the corporation cannot establish a due diligence defence would seem to be more consistent with the Supreme Court's approach to other regulatory offences.

Notes

1 See D. Gilkes, "Chemagro fined under s. 46 of *Competition Act*", *supra* this issue at 3.
2 *R.* v. *Nova Scotia Pharmaceutical Society* (1992), 93 D.L.R. (4th) 36 (S.C.C.).
3 *Ibid.* at 72.
4 D. Stewart, *Canadian Criminal Law*, 2nd edition (Toronto: Carswell, 1987) at 571. See also *R.* v. *McNamara et al.* (1981), 56 C.C.C. (2d) 193 at 452 (Ont. C.A.) affd. *sub nom Canadian Dock and Dredge* v. *The Queen*.
5 [1978] 2 S.C.R. 1299.

6 *Ibid.* at 1325-26.
7 (1991), 67 C.C.C. (3d) 193 (S.C.C.).
8 *Supra*, note 2.
9 [1985] 2 S.C.R. 486.
10 *Ibid.* at 513.
11 *Ibid.* at 515.
12 *Ibid.* at 518.
13 (1986), 16 O.A.C. 319 (C.A.).
14 See also *R.* v. *St. John News Co. Ltd.* (1984), 17 C.C.C. (3d) 234 (N.B.Q.B.).
15 [1990] 1 S.C.R. 425.
16 *Ibid.* at 510.
17 *Supra*, note 7 at 238.
18 [1987] 2 S.C.R. 636.
19 (1990), 58 C.C.C. (3d) 353 (S.C.C.).
20 (1990), 58 C.C.C. (3d) 391 (S.C.C.).
21 (1990), 58 C.C.C. (3d) 408 (S.C.C.).
22 (1990), 59 C.C.C. (3d) 161 (S.C.C.).
23 *Supra*, note 7 at 251-52.
24 *Supra*, note 2 at 72.
25 (1992), 93 D.L.R. (4th) 1 (S.C.C.).

NEW FEDERAL TELECOMMUNICATIONS LEGISLATION PASSED

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The new federal *Telecommunications Act* was passed by Parliament in June of this year and will come into force on October 25.[1] The enacted legislation is substantially different from the Bill introduced in the House in February 1992. The principal differences are as follows:

1. The Act no longer includes a regime for requiring ministerial licences to operate a telecommunications service supplier subject to federal jurisdiction. However, the foreign investment limits that were a major reason behind the original licensing proposal have been retained (see discussion below);

2. There is a serious attempt to exempt from the legislation businesses which act purely as resellers of communications services provided to them by carriers that own transmission and switching facilities;

3. The elaborate and internally contradictory purposes clause, while continuing to position telecommunications as a politically strategic industry (i.e. one having an important role in maintaining Canadian identity and sovereignty) places somewhat greater emphasis on the promotion of competition, the protection of individual privacy, and attention to regional interests;

4. The proposed capacity of the Governor in Council to issue directives on matters of national security has been deleted;

5. The provinces have been given the capacity to initiate consultations with the Federal Minister responsible for communications in relation to the possible exercise by the Governor in Council of its power to issue directions on broad policy matters to the CRTC;

6. The CRTC's power to forebear from regulating carriers subject to its jurisdiction has been tightened up somewhat by establishing that the CRTC is required to forebear (to the extent and subject to such conditions as the CRTC considers to be appropriate) from regulating a service or a carrier where it determines that services or the carrier itself will be subject to sufficient competition to protect the interests of the users;

7. The legislation retains the power to exempt a class of carrier from the legislation, but has shifted the administration of this power from the Minister of Communications to the CRTC;

8. The CRTC has been given a 45 day time limit to make a decision on how to proceed with individual carrier tariff filings if it does not approve or disapprove the filing before that date.

The foreign ownership limits and the structure for defining businesses subject to the *Telecommunications Act* are likely to prove contentious and difficult to implement.

Although the licensing regime has been removed, the way in which the Act would enforce foreign ownership limits may prove to be even more draconian than the Government's initial proposals. In effect, a business which finds that for whatever reason its voting share structure violates the limits on non-Canadian ownership established by the Act (and implementation regulations discussed below) is faced with an immediate statutory prohibition against continuing to operate as a telecommunications common carrier.

The statutory foreign ownership limit is 20% of a telecommunication common carrier's voting shares. However, proposed implementation and enforcement regulations published in July, and expected to be made on or before the date the Act comes into force, would permit a Canadian carrier to be owned by one or more corporations, each of which has no more than one third of its voting shares owned by non-Canadians. It can be expected that many carriers will eventually elect to obtain this holding company top-up opportunity in order to maximize access to capital markets and to improve their ability to enter into equity-technology swaps with more advanced non-Canadian telecommunication businesses.

In order to soften the blow of the statute's blunt prohibition against operating as a carrier if the ownership limits are violated to any detectable degree, the proposed regulations would provide a number of monitoring duties and intermediate obligations on the carrier and its Board and shareholders aimed at providing a breathing space to permit the carrier to wind down an excessive non-Canadian voting share position to a level that complies with the Act or Regulations before having to cease operating as a telecommunications common carrier. In the event that the carrier's Board or shareholders failed to bring the ownership position under the limit, the Regulations authorize the CRTC to step into the management of the corporation to achieve that outcome.

The application of the foreign ownership limits is likely to raise a number of ongoing issues. First, will be the unease over the blanket application of foreign ownership limits to all Canadian carriers regardless of their size or actual strategic importance either in terms of the elaborate telecommunications policy statement of the Act or more generally in terms of the efficiency of the basic infrastructure of the Canadian economy. Presently, to get out of the foreign ownership controls, a Canadian telecommunications service business must either structure its affairs in order not to be caught by the jurisdiction of the *Telecommunications Act* (a virtual impossibility for ambitious network services businesses), or the class of business in which the carrier is found (with "class" yet to be defined by the CRTC) must be exempted from the Act as a whole or from elements of the legislation (such as foreign ownership controls) by a CRTC order issued after a proceeding.

Second, the administration of the regulations with special duties being imposed on shareholders, boards, and corporations is likely to raise a number of ongoing corporate governance problems, particularly in relation to the discharge of directors' fiduciary obligations towards the corporation in the face of supervening regulatory duties and the extent to which shareholders who are not subject to federal regulatory jurisdiction may be compelled by this scheme to take certain action contemplated under the Regulations to permit enforcement of the limits.

Third, there will be substantial compliance costs incurred by carriers subject to the Act, both large and small, in order to comply with the new duties imposed by the implementation Regulations, especially if their stock is publicly traded.

Fourth, the limits and the way in which they are enforced may in practice make it very difficult for Canadian carriers not already listed on foreign stock exchanges (Bell through BCE may currently be the only one so listed) to obtain a listing on foreign exchanges in order to increase access to capital markets.

The legislation also retains much of the original elaborate sequence of definitions of the attributes of a telecommunications service business that would bring it under the jurisdiction of the *Telecommunications Act* while adding even more difficult to interpret definitions. Under the revised set of definitions, although the government has announced that the resale sector is to be excluded from the legislation, a telecommunications common carrier continues to be a business which "owns or operates a transmission facility" used by the business to provide telecommunication services. This concept of owning or operating a transmission facility is the same as the key aspect of the definition of a company subject to CRTC regulation under the predecessor *Railway Act*. The CRTC has already interpreted this concept as entailing network management activities by a reseller such as the capacity to select alternative routes for a particular point to point transmission involving one or more services of other carriers.[2] Thus, the Act does not reflect accurately the statements of the government to the effect that only businesses which owned a substantial portion of their transmission facilities would be caught by the legislation.

The Act provides a definition of "exempt transmission facilities" that provides an opportunity to narrow by regulation the types of transmission facilities which if operated by a reseller would make that firm subject to the Act. However, using this opportunity to exempt a well-defined set of competitive businesses having no strategic importance from the Act while ensuring that strategically important carriers having significant market power are still caught, may prove to be a daunting task.

As a practical matter, all telecommunications carriers provide services through a mixture of owned facilities and resold services involving a variety of point-to-point stage lengths. Stentor members, through inter-member interconnection arrangements, effectively resell the services provided by their counterparts in other provinces in order to provide Canada-Canada services. Teleglobe Canada, apart from earth stations and

switching facilities, obtains the other elements of its telecommunications network from other third party suppliers such as undersea cable owners, Intelsat, and Stentor.

Thus, it would appear that only rudimentary resale operations that add billing features to products directly resold without modification from telephone companies (firms now known as rebillers) might confidently assume that they would not be subject to the *Telecommunications Act* once it comes into force and that other resellers or hybrid carriers may be unable to rely on the definition of telecommunications common carrier to avoid being caught by the Act.

This jurisdictional uncertainty coupled with the blunt foreign ownership controls of the legislation may create some difficulties for new entrants, particularly into the long distance and enhanced services businesses. That is, new entrants may not have sufficient capital market access to allow them to begin competing effectively and in a timely fashion with the established telephone companies which have had their foreign ownership positions (to the extent that they do not comply with the legislation's limits) specially grandfathered by the legislation.

Finally, the enacted legislation retains the fundamental dilemmas of: (1) a government contemplating ever more elaborate policy roles for an industry which is increasingly competitive and capable of supporting a large number of diverse firms, and of (2) first establishing more extensive industry regulation before discretionary and process-laden deregulation powers may be implemented.

The policy statement of the Act does not decrease regulatory burdens; rather it creates an expectation that through greater regulation this industry can be tied more tightly to political decisions respecting maintenance of and promotion of Canadian identity and sovereignty. Accordingly, it can be reasonably expected that the various CRTC powers to reduce the regulatory burdens imposed on Canadian telecommunication carriers subject to the Act as well as the power to exempt businesses from the ambit of the legislation will be actively tested by many participants in the market over the next few years.

It can only be hoped that incremental regulatory actions to confine the sweeping ambit of the new legislation reasonably keep pace with changing industry conditions and public expectations.

Notes

[1] For an analysis of the proposed legislation tabled as Bill C-62 in Parliament on February 27, 1992, see J.F. Blakney, "New Federal Telecommunications Legislation - A Commentary" (1992) 13:1 Can. Comp. Rec. 64.

[2] See J.F. Blakney, "CRTC Decides to Regulate Resellers and Rogers Network Services" (1992) 13:2 Can. Comp. Rec. 13.

CANADIAN COMPETITION RECORD

COMPETITION LAW AND TRADE POLICY: HONK IF YOU LOVE COMPETITION POLICY

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Finding Religion

Proposing competition law "solutions" for trade policy "problems" has become fashionable in legal and economic circles. For the most part, this has been positive. In fact, the research and analysis has been insightful and sometimes ground breaking, particularly with respect to anti-dumping. However, some proponents of competition policy solutions are starting to sound almost religious - the temptation likely stems from the attractive simplicity of the underlying consumer welfare economics story. Still, it must be remembered that legal and economic theories only go so far, and for the competition policy solution to move forward, it will be necessary to get the politics right. When seen from a political perspective, the linkages and frictions between competition policy and trade policy are anything but simple. They are in fact subtle, complex and not yet very well understood.

More work has to be done on understanding and dealing with the political dimensions of the competition/ trade policy interrelationship. It is too early to be religious, let alone politically convincing, with respect to pursuing competition policy solutions for trade policy problems. The recent reluctance of the Canadian business community to support the position of the Joint Chambers of Commerce regarding the replacement of anti-dumping laws by competition laws, perhaps the easiest context for substitution, is just one example of the political hurdles that will stand in the way.

The Reach and Implications of Trade Policy

Trade policy issues are complex because they invariably implicate broader economic and social issues. To understand these implications, it is necessary to take into account the following aspects of the reach of trade policy:

- Trade policy essentially involves government measures that directly or indirectly encourage or restrain imports and exports. As such, it encompasses issues of foreign policy and international relations. Further, it involves the accommodation and balancing of a broad range of interests within Canada and of an equally broad but different mix of interests within the countries with which we trade. Trade policy also involves accommodations between Canada and these countries while trade negotiation is a polite term for the confrontation of these interests.

- Many measures which appear to be purely domestic and unrelated to international trade (eg. local building codes) have trade policy implications (eg. on imports of building products). Equally, measures which appear to be expressions of foreign policy (eg. Iraq oil embargo) can have significant effects in domestic markets (eg. on the price of gasoline) and in world trade (eg. diversion of oil exports).

- Trade measures in one country have effects in other countries. For example, actions by an export marketing agency for Canadian wheat or potash can affect competition in foreign markets. Similarly, a U.S. section 301[1] market opening initiative on Canadian beer can work to the advantage of Canadian consumers.

- While trade measures most clearly relate to the movement of goods, such measures invariably impact on and are intricately linked to the location and movement of ideas, capital (investment) and people (labour).

- Trade issues are strongly affected by shifting social and cultural attitudes and the expression of basic instincts such as the distrust of foreigners (eg. "Japan bashing" in the U.S.), and the preservation of jobs, communities, culture, etc.

Linkage or Friction?

The economic rationale for trade liberalization, whether effected unilaterally or negotiated on a bilateral or multilateral basis, is the realization of comparative advantage and economic efficiency through open markets and free trade. The underlying consumer welfare rationale for most expressions of competition policy is similar to the economic efficiency rationale for trade liberalization. Measures which encourage imports (eg. tariff reductions) are therefore generally compatible with competition policy (ie. increased opportunity for foreign entry) and provide an opportunity for linkages. Measures which encourage exports to foreign markets (eg. U.S. section 301) can also be compatible with competition policy objectives in the foreign market. A good example is Canadian beer. While the Canadian competition authorities anticipated increased U.S. penetration when they allowed the Molson/Carling O'Keefe merger, it was the aggressive use of trade law by the U.S. that reduced entry barriers.

The main trade measures that give rise to possible frictions are those that restrain imports (eg. tariffs, safeguards, anti-dumping); or restrain exports (eg. VERs); and, to a lesser extent, those that encourage exports (i.e. export cartels vs. anti-conspiracy laws). The most direct instances of friction occur where trade measures restrict imports, as in the anti-dumping area. Such measures, which are efficiency restricting, can most often be attributed to the balancing of social or political interests, either real or perceived.

It is curious that the more religious competition policy theorists take a broad brush libertarian approach to eliminating such impediments to international trade such as anti-dumping, yet do not as strongly resist other domestic measures driven by social and political concerns which clearly interfere with economic efficiency and open competition. The very long list of such measures would include Sunday shopping laws, minimum wage laws, government procurement preferences, investment screening measures, licensing statutes, environmental standards, health and safety laws, and municipal zoning laws. The message for the religious is that tradeoffs and balancing real or perceived social and economic interests are the political reality, both domestically and internationally.

Why Protection?

It is obvious that trade measures can insulate some industries and companies from the effects of free and open competition. In a time of rapid change, trade protection can retard the full impact of opening markets and allow time (decades?) for business and labour to adjust.

For the first time in its history, the U.S. finds itself in an economic world that it can neither dominate nor withdraw from. Without precedent to rely on, and facing rapid global change, it should not be terribly surprising that the "America First" supporters and the U.S. congressmen whose careers depend on gauging public sentiment feel a need to go slow on trade liberalization or to protect vulnerable industries. They may be wrong in economic terms or may underestimate the competitive strength of U.S. industry but economic theory is not going to dissolve the political hurdles facing those who want to break down barriers facing Canadian exporters to the U.S. market.

There are similar suspicions and sentiments resisting trade promoting measures in this country. Indeed, many Canadians, perhaps a majority, continue to oppose the Free Trade Agreement (FTA). They believe that such trade liberalization has cost Canadians jobs and industries, and that we will continue to be hurt in our largest manufacturing industry - autos and parts. The gut questions they ask are: what Canadian industries are expendable and how much in unemployment costs, foregone tax revenue, welfare payments and/or social costs are we supposed to pay to have an efficiently functioning consumer market, if consumers cannot find jobs to give them enough money to spend on the fruits of efficiency? They may be wrong in the long term and in theory, but they are entitled to answers.

Raising political concerns is not some indirect argument for protectionism. Simply put, there are public attitudes that need to be understood and fairly addressed before theoretical solutions can find real world acceptance.

A Political Perspective on the Anti-dumping Issue

Perhaps the strongest legal and economic case for a competition law solution to a trade law problem or at least the case that has received the most attention - arises in the anti-dumping context. Many have argued that current U.S. and Canadian anti-dumping laws impede the efficient allocation of resources in an integrating market and, as applied by Canadian and U.S. administrators, constitute an irritating and distorting intervention in cross-border trade. They propose to solve the problem by eliminating anti-dumping and offering up a cross-border price discrimination and/or predatory pricing regime in its place.

The real objective of Canadian exporters is to eliminate, or secure exemption from, the application of U.S. anti-dumping protection. The antitrust element is a tradeoff. But as discussed in more detail below, it is certainly arguable that the case for doing away with anti-dumping gains little, and in fact becomes more politically complicated and confused, by being linked to antitrust substitution. Indeed, the effort spent on an antitrust solution may have drawn attention and energy away from development and support for more achievable trade policy remedies that could minimize the negative impact of the U.S. anti-dumping laws on Canadian exports (eg. agreed methodologies for dumping margin calculations, etc.).

There are sound political reasons why the elimination of U.S. anti-dumping, with or without antitrust substitution, should not be pursued at this time. The most fundamental reason is that U.S. political attitudes are too strongly opposed. In fact, Americans have shown that they place a great deal of importance on the preservation of anti-dumping protection. They refused, from the outset of the FTA negotiations, to grant Canada an anti-dumping exemption and never wavered. If anything, U.S. political attitudes for preserving trade remedy protection have hardened since 1988. The surrender of anti-dumping protection is simply a non-starter from a U.S. political perspective.

Even if the conclusion that U.S. anti-dumping laws are sacrosanct is wrong, it is close enough to being right that any such concession would only come at a very high price for Canada. Offering up antitrust remedies as they now stand in substitution for anti-dumping protection will not be enough. Although Canadians are now somewhat insulated from the full discovery and investigative procedures, injunctions, fines and private treble damage actions of the U.S. antitrust laws, we cannot expect this to remain the case if the antitrust carrot is to be sufficiently meaningful to get the Americans to relieve us from their anti-dumping laws. Could the U.S. politically accept antitrust as the only remedy without being assured that U.S. plaintiffs and investigative agencies would have essentially the same procedural and remedial rights with respect to Canadians as they enjoy in proceedings involving Americans?

Someone will also have to have a fairly good explanation for the Canadian business community as to why, after spending 50 years passing laws designed to impede the extraterritorial application of U.S. antitrust laws, Canada should suddenly change its mind. It is also hard to imagine why the Canadian business

community would be willing to expose itself to U.S. procedures and remedies, when a few years earlier it strenuously resisted the inclusion of similar provisions in Canada's domestic competition laws. Indeed, if the Canadian business community were willing to live with treble damages in the cross border context, what possible justification would it have for not agreeing that Canadian plaintiffs be put on a similar footing in any future reform of the domestic competition laws? As these questions indicate, introducing the antitrust substitution argument may do more to create antitrust problems for Canadian companies than it does to solve their trade problems.

Moreover, while the position of those who support the substitution of anti-dumping law by competition law is consistent with where Canada started in the FTA negotiations, it is not consistent with where we ended up. The review of domestic anti-dumping decisions by bi-national panels is a ground-breaking system which has worked well. A more sensible approach might see us trying to build on that success to regularize and limit the more arbitrary elements in the anti-dumping laws of both countries. It is ironic that many of those who regarded the negotiation of Chapter 19 as a coup because it put the review of anti-dumping decisions beyond the reach of the U.S. courts, now want to abandon the panel process and subject Canadian exporters to the very institutions they sought to avoid. This change would apply not only at the review or appellate level, but in the first instance as well.

The proponents of substitution may also be underestimating the creativity of U.S. antitrust and trade lawyers and the protective instincts of U.S. producers. Taking the anti-dumping weapon out of U.S. hands would still leave Canadian exporters exposed to possible countervail, safeguard, section 337, and a host of other proceedings. Indeed, doing away with anti-dumping may do little more than divert U.S. protectionist energies to these other remedies which can have substantially the same impact on Canada. For example, the Honda matter, which could discourage foreign investment in Canada, was not an anti-dumping case, but a customs audit dealing with rules of origin.

As well, we may be looking at an experimental solution for something that may not really be that big a problem. Canadians have been told so often and for so long that they need relief from U.S. contingent protection laws that the dimensions of the anti-dumping problem may have become more imagined than real. In each of the ten years to 1991 there has been an average of only three U.S. anti-dumping cases brought against Canada and only about half of them have been successful. In fact, the average annual value of export trade affected was less than $500 million, which is a small percentage of the value of Canadian exports affected by just one U.S. countervailing duty case, softwood lumber. Admittedly these kinds of figures understate the full chilling impact of U.S. anti-dumping, not only on exports but on future foreign investment in Canada. However, one would expect that those advocating a solution to a "problem" should at least attempt to quantify it. For example, even if one were to multiply the actual value of directly affected exports by a factor of 10 to quantify the chilling or "deterrent" effects of U.S. anti-dumping laws, it would still mean that U.S. anti-dumping was a factor in less than 2% of Canadian exports to the U.S.

Conclusion

Honking the horn in support of competition policy as the answer to complex trade policy questions, particularly in the anti-dumping area, has become fashionable and has attracted highly credible support in legal and economic circles. While the intellectual effort and energy spent on the issue has been insightful, it must be remembered that trade policy issues are entwined in complicated domestic and foreign politics that will have to be factored into the debate. Therefore, no amount of honking will avoid the reality that neither the U.S. nor the Canadian publics are ready to accept the competition policy solution.

Notes

[1] *Trade Act of 1974*, Pub. L. No. 93-618, s. 301, 88 Stat. 1978, as amended by *Trade Agreements Act of 1979*, Pub. L. No. 96-39, s. 901, 93 Stat. 144, and as amended by *Trade and Tariff Act of 1984*, Pub. L. No. 98-573, s. 304, 98 Stat. 3002, 19 U.S.C. s. 2411.

CANADIAN COMPETITION RECORD

GEMINI II: THE SAGA CONTINUES

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Introduction

On July 30, 1993, the Federal Court of Appeal (FCA) overturned the decision of the Competition Tribunal in *Gemini II*[1] respecting the Tribunal's jurisdiction to vary or rescind its consent order (the Consent Order) dated July 7, 1989, which contemplated the merger of the computer reservation systems (CRS) of Air Canada and Canadian Airlines International Ltd. (Canadian). The merged entity is called The Gemini Group Limited Partnership (Gemini) and is currently owned by three partners: Air Canada, PWA Corporation (PWA) (Canadian's parent), and Covia Canada Partnership Corp. (Covia). The Competition Tribunal had held that it did not have the jurisdiction to grant the Director's application to vary the Consent Order.[2]

Application of Director

The basis for the Director's application for a variation of the Consent Order was that circumstances had changed since it was issued and that competition in the Canadian airline industry is now threatened by Canadian's inability to withdraw from a hosting contract (the Gemini Hosting Contract) entered into among Gemini, Air Canada and Canadian on June 30, 1989. In his application, the Director asked the Tribunal to order the early termination of the Gemini Hosting Contract and any other hosting contracts among the parties.

In the absence of such an order, Canadian would not be able to unilaterally withdraw from the Gemini Hosting Contract prior to July 1, 1999, if Gemini remains solvent. Canadian desires to withdraw from the Gemini Hosting Contract because PWA has been incurring substantial losses and the only entity that has expressed an interest in investing in PWA is AMR Corporation (the parent of American Airlines Inc.), which has made an investment proposal to PWA that is conditional upon Canadian being hosted on American Airlines' Sabre CRS. Air Canada has offered to merge with PWA, but PWA has rejected Air Canada's offers.

Decision of the Tribunal

Section 92 of the *Competition Act*[3] (the Act) authorizes the Tribunal to make an order on the application of the Director where the Director and the person in respect of whom the order is sought agree on the terms of the order. Pursuant to section 106 of the Act, consent orders may be varied or rescinded only in the following circumstances:

(a) the circumstances that led to the making of the order have changed and, in the circumstances existing at the time of the application, the order would not have been made or would have been ineffective to achieve its intended purpose, or

(b) the Director and the person against whom the order was made have consented to an alternative order.

Section 106 of the Act also provides that the application to vary a consent order may be made by either the Director or the person against whom the order was made.

The Tribunal refused to grant the order sought by the Director on the grounds that the circumstances that led to the making of the Consent Order had not changed and "it is not possible to say that in the circumstances that exist at present the order would not have been made or would have been ineffective to achieve its intended purpose."[4]

The Tribunal enunciated the following test for varying consent orders:

(i) the change in circumstances which would permit adding terms to an earlier order must be those that "demonstrably were taken into account by the Tribunal at the time of, and directly caused, the making of the order"; and

(ii) the order should only be varied if "it has become useless or inadequate for its intended purpose of solving the problem" that led to the making of the order.[5]

Change in Circumstances

With respect to the first part of the test, the majority of the Tribunal concluded that by using the words "that led to" in subsection 106(a), Parliament must have intended there to be a direct causal link between the existence of certain circumstances and the decision of the Tribunal. The logical relevance of some background condition existing at the time the original order was made would not be sufficient.[6]

The Director argued that the business relationships associated with the Gemini merger were part of the circumstances leading to the Consent Order. Accordingly, the Tribunal would have jurisdiction to vary the Consent Order if it were satisfied that at the time of the making of the Consent Order, it contemplated an "on-going competitive duopoly in the Airline industry in Canada" and that such situation no longer exists. The opponents of the application argued that the existence of an airline duopoly and the hosting arrangements with Gemini were part of the background facts to, but not the cause of, the Consent Order. Rather, the direct cause of the Consent Order was the need to ensure that the merger would not allow Gemini's CRS to be used in an anti-competitive fashion.

After reviewing the circumstances taken into account which led to the Consent Order, the majority of the Tribunal found that the "whole concern expressed was as to this merger preventing or lessening competition substantially in the provision of computer reservation systems services to airlines, travel agents and consumers."[7] The majority found that while the duopoly in the Canadian airline market and the hosting of the two major airlines in Gemini were identified in the documents forming the basis of the Consent Order, they were not noted as causes for the Consent Order. In addition, the majority decision noted that the concern about vertical integration expressed at the time of making the Consent Order did not appear to have changed, nor had any obvious change in the need to control vertical integration been demonstrated. The majority decision accordingly found that the circumstances that led to the making of the Consent Order had not changed. It also observed:

> The fact that one remedial term of the Consent Order, prohibiting collusive use of Gemini, might no longer be necessary if the airline duopoly becomes a monopoly, does not make the order subject to expansion in order to ensure the preservation of that duopoly.[8]

It would appear from the majority's decision that Mr. Justice Strayer and Lay Member Smith believed that the Gemini Hosting Contract was something that had been entered into independently of the Consent Order by parties who had accepted the usual risks associated with entering into a contract of that nature, and who should not now be permitted to "resile from a settlement of litigation because that settlement has turned out, for reasons unforeseen at the time, to be less advantageous than expected to the interests of a party or the public."[9]

Whether the Order Would Have Been Made in the Circumstances

For the same reasons, the majority of the Tribunal found that in the circumstances existing at present, the Consent Order would not have been made or would have been ineffective to achieve its intended purpose. In reaching this conclusion, it noted that it was "of fundamental importance ... that the Director does not object to the continuation of any provision in the Consent Order."[10] In particular, the majority noted that there had been no complaints made by third parties with respect to the way they had been treated by Gemini, and that the Consent Order does not either require or endorse the Gemini Hosting Contract. The majority further noted that if the Consent Order were rescinded, this would in no way assist Canadian, which would still be bound by the contract. The majority therefore concluded that the Director was really seeking a variation to make the Consent Order serve another purpose: the preservation of a duopoly in the Canadian airline industry.

In this respect, the Tribunal stated:

> [W]e cannot add to the original order a release from a contract that was not required by that original order but which was freely entered into at that time by Canadian for no doubt good commercial reasons, simply because Canadian has since entered into another contract inconsistent with the first, for other good commercial reasons. The first contract was not and is not anti-competitive *per se*. It has become so only because it is an obstacle to restoring Canadian's financial viability - a viability whose protection was not the object of the Consent Order.[11]

Power to Vary Without Consent

The Tribunal did not accept the arguments that its authority to vary the Consent Order was dependent upon the consent of both parties and noted that it had already expressed the view in its original reasons for the Consent Order[12] that it could include terms and conditions under section 106 of the Act without the consent of all parties. The Tribunal asserted that section 106 permits the rescission or variation of any orders made under Part VIII of the Act, many of which would not be consent orders, and that the section clearly authorizes changes in those orders. In the Tribunal's view, "Parliament would certainly have been more specific if it intended the variation or rescission of consent orders to be treated in a different way."[13]

Substantial Lessening of Competition

In anticipation of appeals, the Tribunal proceeded to address the competition issues in the case. In short, it unanimously agreed with the Director that: (i) "the AMR deal is currently the only transaction available to save PWA and Canadian";[14] (ii) "the end result of [the failure of PWA] would undoubtedly be a substantial lessening of competition in most if not all airline passenger markets on southern routes in Canada";[15] and (iii) "Gemini is unlikely to fail financially in the foreseeable future, even if Canadian transfers its hosting to Sabre."[16]

Remedial Jurisdiction

With respect to remedies, the Tribunal indicated that its starting premise is that "our role is to protect the public interest in competition, and not to provide contractual remedies for private parties."[17] Further, the Tribunal indicated its role was not to provide for compensation when, acting in the public interest, it deliberately interferes with private contracts. Accordingly, the Tribunal found that it did not have authority to award compensation for the loss by Gemini or others of future benefits that would have arisen under the Gemini Hosting Contract had it not been terminated. However, the Tribunal found that it could impose conditions to facilitate the termination of the Gemini Hosting Contract and make that termination less harmful to the other parties. Such an approach would be within its implicit powers and represent a fair

balance between public and private interests. Therefore, the Tribunal found that it could order Canadian to pay certain of Gemini's costs arising from the termination and dehosting. Further, it could require Gemini to take necessary steps to facilitate the dehosting of Canadian.

The Tribunal indicated that had it found that it had jurisdiction to vary the Consent Order, it would have granted the Director's request to amend the Gemini Hosting Contract to permit Canadian to de-host from Gemini on at least twelve months' notice and upon reimbursement by Canadian to Gemini of specified costs associated with de-hosting.

Federal Court of Appeal Decision

The Director appealed the Tribunal's ruling regarding its jurisdiction to make the requested order, while Canadian appealed the decision on both jurisdictional and certain factual findings. Air Canada, Gemini and Covia appealed the Tribunal's factual findings.

The FCA unanimously reversed the Tribunal's decision with respect to its jurisdiction to vary the Consent Order. However, only one of the three judges, Mr. Justice MacGuigan, agreed with the Tribunal's view that the Consent Order could be varied without the consent of both the Director and the respondents. Mr. Justice Hugessen and Mr. Justice Heald ruled that the Consent Order could only be varied with the consent of the Director and the respondents, and that failing such consent "the Tribunal is limited to ordering the dissolution of the merger ... or the divestiture of assets or shares... ."[18]

Change in Circumstances

The FCA unanimously concluded that the Tribunal erred in law in its interpretation of the conditions precedent imposed by subsection 106(a) of the Act with respect to its power to vary a previous order.

As discussed above, the Tribunal concluded that section 106 permitted variance or rescission of a consent order only under circumstances that were directly and demonstrably different from those that caused the order to be issued in the first place. However, the FCA found that all that is required is the establishment of a "simple causal relationship between the [changed] circumstances and the order."[19] Further, it is not necessary to relate the changed circumstances to the purposes sought to be achieved by the order.[20]

The FCA found that "the existence of a strong duopoly in the airline business was an important feature of the landscape in which the previous order had been made" and that the "drastic change" in the financial position of Canadian and its "imminent failure" were changes in the circumstances that had led to the making of the Consent Order.[21] The FCA also determined that under the changed circumstances, the Consent Order would not have been made.

Power to Vary

The FCA majority then ruled that where "the order sought to be varied is one which was given under paragraph 92(1)(e) and resulted from a consent, the Tribunal has no powers beyond those with which it was originally vested at the time of the Director's first application."[22] In other words, in the absence of consent, the Tribunal is limited to the "drastic powers" of dissolution or divestiture.[23] Mr. Justice Hugessen observed that it is "the all-or-nothing nature" of the dissolution and divestiture provisions in paragraph 92(1)(e) which give the consent provision in paragraph 92(1)(e) "its vitality and increase its utility."[24]

Mr. Justice Hugessen further suggested that the policy of the Act favours and encourages "... solutions which the parties and the Director, with the guidance and consent of the Tribunal, fashion for themselves ... ."[25] Indeed, his decision seems to have been motivated, at least in part, by a desire to promote and facilitate negotiated solutions, and cloak such solutions with greater certainty.[26] This latter laudable objective was also highlighted by Mr. Justice Heald, who stated: "The high threshold for intervention imposed by the scheme of the statute is necessary in order to clothe existing orders with an acceptable degree of stability and certainty."[27]

Mr. Justice Hugessen then made the following observation:

> On the application to vary, just as was the case on the original application, the parties are given the same incentives to negotiate a consent order which will respond sensitively to both public and commercial interests in the light of the changed circumstances; they are likewise subject to the same dangers of an all-or-nothing order should they fail to do so.[28]

The fact that there are typically far more costs associated with abandoning a consummated merger than abandoning a proposed merger is not noted.

Mr. Justice Hugessen also stated that the rationale for the dissolution and divestiture provisions in subparagraphs 92(1)(e)(i) and (ii) is to "lead to the sophisticated [consent] solutions of subparagraph 92(1)(e)(iii)."[29] It is important to note that there are situations where nothing short of a structural solution such as dissolution or divestiture would adequately address the substantial prevention or lessening of competition likely to result from a merger challenged by the Director.

In addition to the foregoing, Mr. Justice Hugessen suggested in the course of his reasons for judgment that it "is entirely right" that the Tribunal should play "an activist and interventionist role in the making of consent orders."[30] Some may argue that an activist or interventionist Tribunal, or the perception that it is so, would contribute to the uncertainty associated with participating in the consent order process and, possibly, the reluctance that merging parties have to participate in such proceedings.

After agreeing with the two principal findings of Mr. Justice Hugessen, Mr. Justice Heald emphasized that "the merger must be the cause of the anti-competitive effects in issue since the Tribunal's powers under Part VIII of the Act are restricted to redressing the effects of specific types of behaviour, one of which is mergers."[31] This case provides a good reason why that may not be the best test, because there will be situations where the merger is not the cause of the anti-competitive effects that need to be addressed through variation of the order.

Disposition

In light of the foregoing, the majority of the FCA set aside the decision of the Tribunal and returned the matter to the Tribunal for reconsideration on the basis that the condition precedent to the exercise of the power to rescind or vary had been met, but that the power to rescind or vary may only be exercised in accordance with the provisions of section 92 of the Act. The cross-appeals of Gemini, Air Canada and Covia regarding the factual findings of the Tribunal were dismissed. Both Mr. Justice Hugessen and Mr. Justice MacGuigan agreed with the Tribunal that it did not have the jurisdiction to make compensatory awards, and Mr. Justice MacGuigan agreed with the Tribunal that it had the power to impose terms to facilitate the termination of the Gemini contract, e.g., requiring Canadian to pay certain of Gemini's costs arising from the termination and dehosting of Canadian.[32] Mr. Justice Hugessen and Mr. Justice Heald did not address this latter issue, nor did Mr. Justice Heald address the issue of compensation.

Gemini has filed an application for leave to appeal to the Supreme Court of Canada. It is expected that Air Canada and Covia will soon follow suit. The Tribunal has scheduled a pre-hearing conference for September 28, 1993, to address issues such as timing and the scope of the hearing.

Implications of Federal Court Decision

Consent orders are an alternative resolution to contested merger proceedings and have the potential to be attractive to the Director for several reasons. First, they avoid the greater time, resources and possible adverse publicity associated with contested proceedings. In addition, consent orders provide greater flexibility to fine tune the terms of the order than do orders made in the context of contested proceedings. Consent orders should also offer greater certainty than contested proceedings.

The FCA's decision has several implications for the consent order process. First and foremost, it provides a welcome endorsement of, and encouragement for, the negotiated settlement approach to mergers. This is consistent with the approach that the Bureau has adopted since the 1986 amendments to the Act. At the same time, some aspects of the FCA's decision raise significant practical issues for merging parties to consider. First, the FCA's decision gives the Tribunal the ability to rescind or vary consent orders on very broad grounds. All that must be established is a "simple causal relationship between the [changed]

circumstances and the order" and that as a result of those changed circumstances, the order would not have been made or would have been ineffective to achieve its intended purpose. This low intervention threshold creates greater scope for varying consent orders and raises issues regarding the certainty associated with becoming a party to a consent order.

In addition, by underscoring the fact that the only alternatives to a failure to reach a consensus regarding a variation are dissolution and divestiture, the FCA majority decision may result in increased pressure on respondents to give that consent. If the threat of the "drastic" alternatives of dissolution or divestiture forces parties to agree to the variation sought by the Director, the disagreement between Mr. Justice Hugessen and Mr. Justice Heald, on one hand, and Mr. Justice MacGuigan and the Tribunal on the other hand, may have little practical significance. In both situations, parties to a consent order would have that order subsequently varied in circumstances where they may have preferred no variation.

As a result of the FCA's decision, parties to a merger should carefully consider the possibility that circumstances which exist at the time a consent order is being considered may change. If it is reasonable to expect that circumstances may change, the parties may want to consider either making it attractive for the Director to accept informal undertakings or restructuring their transactions to achieve a "fix-it-first" remedy, rather than negotiating a consent order that might subsequently be varied as a result of unforseen developments.

If the consent order route is pursued, it may also be prudent to identify in the order, to the extent possible, the circumstances giving rise to the order. This should increase certainty as to the circumstances in which the order may be varied or the merger dissolved. Clearly, not all of the circumstances may be identifiable, but, arguably, this approach may make it more difficult to subsequently establish that unidentified circumstances are related to the circumstances that led to the making of the consent order. What one usually wants to avoid is a situation where any deviation from the status quo may provide grounds for rescinding the order. Of course, if the strategy is to make the circumstances under which the order can be varied or the merger dissolved as broad as possible, the above described approach may not be advisable.

Notes

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1 *Director of Investigation and Research* v. *Air Canada*, (unreported), CT-88/1, April 22, 1993.
2 See D. A. Campbell and R. T. Hughes, "Competition Tribunal Issues Decision in Airlines Case" (1993) 14:2 Can. Comp. Rec. 1.
3 *Competition Act*, R.S., 1985, c. C-34.
4 *Supra*, note 1 at 35.
5 *Ibid.* at 25.
6 *Ibid.* at 24.
7 *Ibid.* at 32.
8 *Ibid.* at 35.
9 *Ibid.* at 31.

[10] *Ibid.* at 36.
[11] *Ibid.* at 39.
[12] *Reasons for Consent Order* dated July 7, 1989, at 64.
[13] *Supra*, note 1 at 27.
[14] *Ibid.* at 61.
[15] *Ibid.* at 81.
[16] *Ibid.* at 108.
[17] *Ibid.* at 110.
[18] *The Director of Investigation and Research et al.* v. *Air Canada et al.*, (Unreported, July 30, 1993, A-302-93, at p. 9 of Hugessen J.A.'s decision; see also p. 4 of Heald J.A.'s decision).
[19] *Ibid.* at p. 4 of Hugessen J.A.'s decision; see also p. 2 of Heald J.A.'s decision.
[20] *Ibid.*
[21] *Ibid.* at p. 4 of Hugessen J.A.'s decision; see also pp. 18-19 of MacGuigan J.A.'s decision, and p. 2 of the decision of Heald J.A., who observed: "The financial viability of the initial parties to the Gemini merger on June 1, 1987, namely Air Canada and Canadian, was clearly an important component of the rationale for the 1989 consent order. In its current financial position, Canadian would not have agreed to the Gemini merger."
[22] *Ibid.* at p. 10 of Hugessen J.A.'s decision and p. 3 of Heald J.A.'s decision.
[23] *Ibid.* at p. 9 of Hugessen J.A.'s decision.
[24] *Ibid.*
[25] *Ibid.* at 13.
[26] *Ibid.* at 10 and 12.
[27] *Ibid* at p. 5 of Heald J.A.'s decision.
[28] *Ibid.* at 10.
[29] *Ibid.* at 13.
[30] *Ibid.*
[31] *Ibid.* at p. 5 of Heald J.A.'s decision.
[32] *Ibid.* at p. 14 of Hugessen J.A.'s decision and p. 29 of MacGuigan J.A.'s decision.

CANADIAN COMPETITION RECORD

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