CANADIAN COMPETITION LAW AND POLICY DEVELOPMENTS

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THE "UNDUENESS" THRESHOLD AND SECTION 45: A COMMENTARY ON *CLARKE TRANSPORT*

Introduction

On November 9, 1995, the Ontario Court of Justice (General Division) rendered its decision in *R.* v. *Clarke Transport Canada Inc. et al.* ("*Clarke Transport*").[1] The Court held that the corporate accused were not guilty of contravening section 45 of the *Competition Act,* despite overwhelming evidence the accused had entered into an agreement in respect of market prices. Mr. Justice Moldaver relied extensively on the judgments in *Nova Scotia Pharmaceutical Society* v. *The Queen*[2] ("*PANS*") and *Canada (Director of Investigation and Research)* v. *Southam Inc.*[3] ("*Southam*") in concluding that the Crown was unable to prove, beyond a reasonable doubt, that the likely effect of the agreement would be an undue prevention or lessening of competition.

Section 45

The corporate accused, Clarke Transport Canada Inc., Consolidated Fastfrate Transport Inc., Cottrell Transport Inc., Northern Pool Express Ltd. and TNT Canada Inc. (collectively, the "Accused"), were charged with conspiring, combining, agreeing or arranging to prevent, or lessen, unduly, competition in the pool car freight forwarding market for shipments of freight, in mixed carloads, from Toronto to points west.

Subsections 45(1) and (2) of the Act state as follows:

> (1) Every one who conspires, combines, agrees or arranges with another person
>
> (a) to limit unduly the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any product,
>
> (b) to prevent, limit or lessen, unduly, the manufacture or production of a product or to enhance unreasonably the price thereof,
>
> (c) to prevent or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, storage, rental, transportation or supply of a product, or in the price of insurance on persons or property, or
>
> (d) to otherwise restrain or injure competition unduly,
>
> is guilty of an indictable offence and liable to imprisonment for a term not exceeding five years or to a fine not exceeding ten million dollars or both.
>
> (2) For greater certainty, in establishing that a conspiracy, combination, agreement or arrangement is in contravention of subsection (1), it shall not

> be necessary to prove that the conspiracy, combination, agreement or arrangement, if carried into effect, would or would be likely to eliminate, completely or virtually, competition in the market to which it relates or that it was the object of any or all of the parties thereto to eliminate, completely or virtually, competition in that market.

Furthermore, subsection (2.2) states as follows:

> For greater certainty, in establishing that a conspiracy, combination, agreement or arrangement is in contravention of subsection (1), it is necessary to prove that the parties thereto intended to and did enter into the conspiracy, combination, agreement or arrangement, but it is not necessary to prove that the parties intended that the conspiracy, combination, agreement or arrangement have an effect set out in subsection (1).

Pursuant to these provisions and the judgment of Justice Gonthier in *PANS*, Justice Moldaver held that the *actus reus* components of the offence may be summarized as follows:

(i) the existence of a conspiracy, combination, agreement or arrangement entered into by the accused; and

(ii) an undue prevention or lessening of competition flowing from this agreement.[4]

Furthermore, in order to satisfy the undueness requirement in (ii) immediately above, Justice Moldaver held that there could be no violation of paragraph 45(1)(c) without first showing that the accused possessed market power, which he defined as having the ability to "behave relatively independently of the market, in a passive way."[5] Justice Moldaver further stated that market power had to be accompanied by some degree of anti-competitive behaviour.

Turning to the *mens rea* components of the offence, Justice Moldaver held that these components had been modified as a result of *PANS*, wherein Justice Gonthier held as follows:

> The sections of the Act set out above [subsections 32(1), 32(1.1) and 32(1.3) — now subsections 45(1), 45(2) and 45(2.2)] require the proof of two fault elements: one subjective, the other objective.
>
> 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 terms of that agreement. Once that is established, it would ordinarily be reasonable to draw the inference that the accused intended to carry out the terms in the agreement, unless there was evidence that the accused did not intend to carry out the terms of the agreement.
>
> In order to satisfy the objective element of the offence, the Crown must establish that on an objective view of the evidence adduced the accused intended to lessen competition unduly. This surely does not impose too high a burden on the Crown. Section 32(1)(c) requires that the Crown demonstrate that the effect of the agreement will be to prevent competition or to lessen it unduly. Once again, it would be a logical inference to draw that a reasonable business person who can be presumed to be familiar with the business in which he or she engages would or should have known that the likely effect of such an agreement would be to unduly lessen competition.[6]

Therefore, to summarize, Justice Moldaver concluded that the Crown must prove the following to establish a violation of section 45:

(i) the *actus reus* components of the offence:

(a) the existence of a conspiracy, combination, agreement or arrangement entered into by the accused; and

(b) an undue prevention or lessening of competition, which requires, as a

prerequisite, some degree of market power and some degree of anti-competitive behaviour; and

(ii) the *mens rea* components of the offence:

(a) a *subjective* element consisting of an intent to enter into the agreement and knowledge of its terms; and

(b) an *objective* element that the accused intended to lessen competition unduly.

Based on these requirements and the facts in *Clarke Transport*, the central issue before the Court was whether the parties to the agreement possessed the requisite market power.

Industry Overview and Facts

As noted above, *Clarke Transport* dealt with competition affecting the freight forwarding industry and, in particular, the business of pool car operators. The "modern era" of the pool car industry began in 1969 with the issuance of Tariff 505 (the "Tariff"), which relaxed the commodity mixing restrictions previously imposed by railway operators. The Tariff enabled pool car operators to be more competitive with long distance trucking and provided incentives for heavier loading by allowing greater flexibility in terms of the mixing of commodities. In essence, the Tariff created an opportunity for the development of a niche player in the freight forwarding business, i.e. the pool car operator. A critical issue in *Clarke Transport* was whether this niche business constituted a market, in and of itself.

The Tariff did, however, contain several restrictions. Only companies which met the definition of a "Commercial Pool Car Operator" had access to the Tariff rates. Another restriction was the "50 percent rule", which stated that, in applying the provisions of the Tariff, the weight of any commodity as described in the Canadian Classification and loaded in a car for movement from consignor to consignee must not exceed 50 percent of the weight of all commodities in the car. The rule was intended to keep pool car operators in the "mixed carload" rather than "carload" business, but it was not rigidly enforced.

Turning to the facts in *Clarke Transport*, the Accused were engaged in the pool car freight forwarding business to Western Canada over long haul routes — generally distances of over 500 miles. Essentially, the business was comprised of assembling and consolidating less-than-carload shipments of freight into carload shipments, which were then transported by rail in box cars. The pool car operators paid the railways for their services in accordance with tariffs fixed by the railways. The growth of the pool car operator business provided the railways with a critical backhaul business to complement their resource based (e.g. forest products) headhaul business from Western to Eastern Canada.

The Accused were charged with having conspired to unduly lessen competition in the transportation of carloads of mixed commodities by rail from Toronto to various destinations in Western Canada over the eleven year period between 1976 and 1987. The key component of their alleged conspiracy was a "customer protection scheme" (the "CPS"), which operated in a manner that ensured parties to the agreement were protected from having their rates undercut by other parties to the agreement. Several means were employed to ensure this result, the most significant of which was the exchange of "Special

Rate Notices" ("SRNs"). The SRNs contained information from an individual member-operator regarding existing customers, the rates being charged and the product to be shipped. It was understood that other members would not undercut those rates when quoting to such customers.

With respect to alternative modes of freight forwarding, apparently very little evidence was led concerning the nature, scope, structure or working operations of either the trucking or intermodal rail industries. However, it was established that the trucking industry had many operators and carried essentially the same freight as pool car operators through both its truckload and less-than-truckload service. With respect to intermodal services, three categories were identified, but common to each was the fact that intermodal services shipped identical kinds of freight as pool car operators to identical locations.

The Analysis of the Court

Existence of an Agreement

Typically, the most difficult issue to assess in the analysis of an alleged violation of section 45 is establishing the *existence* of a conspiracy, combination, agreement or arrangement among the accused. This was not the case in *Clarke Transport*, because Justice Moldaver found the evidence of an agreement to be "overwhelming". Justice Moldaver further concluded that the Accused had entered into the agreement fully aware of its terms and with full knowledge that its effects, if implemented, would be to lessen competition.

Moreover, the agreement was found to have been implemented and maintained from 1976 to 1987, thereby engaging the Accused in the elimination of price competition for existing customers through the use of SRNs as well as other forms of anti-competitive behaviour (e.g. the establishment of a common tariff, the coordination of general rate increases, attempts to discourage new entrants into the railway tariff, collective action to confront the competitive threat posed by new entrants and pressure tactics brought to bear on new entrants to join or at least to respect the agreement.)[7] A "mutual understanding" with truckers, although alleged by the Crown, was not proved.[8]

The "Undueness" Requirement

Having confirmed the existence of an agreement, Justice Moldaver addressed the "undueness" components of section 45 as noted above, i.e. an inquiry into whether there was (i) some degree of market power and (ii) some behaviour likely to injure competition.[9] Justice Moldaver concluded that the absence of one of these features would be fatal to a section 45 prosecution,[10] but he also cited the *dicta* in *PANS* that "[a] particularly injurious behaviour may also trigger liability even if market power is not so considerable."[11] This latter statement did not, however, encompass situations where market power was non-existent or negligible.

By contrast, the Crown relied for its interpretation of the "undueness" requirement on *R.* v. *Anthes Business Forms Ltd.*,[12] where Justice Houlden stated:

> If the Court could find on the evidence that the purpose or intention of the parties was to prevent or lessen competition unduly, undoubtedly this would be sufficient for a conviction. But the Crown was not required to prove such a purpose or intention. On the basis of the Container Materials judgment, it was only necessary for the Crown to prove that the effect of the agreement, if it was

> put into operation, would be to prevent or lessen competition unduly.[13]

Justice Moldaver distinguished *Anthes* on the grounds that it was an appeal case involving allegations that the trial judge had erred in imposing a burden on the Crown to prove an intention on the part of the accused to unduly lessen competition. Justice Moldaver concluded that Justice Houlden was referring to the *mens rea* and not the *actus reus* components of the predecessor provision under the *Combines Investigation Act*. Moreover, Justice Moldaver concluded that, while the *actus reus* requirements had not changed since *Anthes*, the *mens rea* components had been modified to require both a subjective and objective fault component.

(i) Market Power and the Relevant Market

In relying on the wording of section 45(2) and the approach for determining undueness in the dissenting opinion of Justice Laskin in *R.* v. *J.J. Beamish Construction Co. Ltd.*,[14] Justice Moldaver held that defining the relevant market is a prerequisite for determining market power and hence "undueness". Specifically, he described the relevant market as "the yardstick against which the component elements of undueness may be measured."[15]

The Crown argued that the relevant market was the market for pool car services and that switching between service options (e.g. truckers and intermodal services) occurred only at the fringe of these markets. To advance this position, the Crown relied on shipper witnesses, expert testimony and the Clarke Rate Quote Analysis.

By contrast, the defence argued that the relevant market also included transportation services to Western Canada provided by long-haul truckers and intermodal rail operators, because these parties engaged in the movement of the same kinds of freight from Toronto to points west. Therefore, it was argued that significant inter-industry competition existed and that such competition was pervasive, rather than just marginal in nature.

In his examination of the relevant market, Justice Moldaver relied on the factors set out by the Federal Court of Appeal in *Southam*. The principal factor was the substitutability of the product, which could be demonstrated through statistical evidence, anecdotal evidence and practical indicia. Thus, factors such as functional interchangeability and industry views/behaviour are now explicitly required considerations when undertaking the exercise of defining a market.

However, even where functional interchangeability was found to exist, Justice Moldaver appropriately cautioned that the "superior product" argument may lead to a finding of two products not being in the same market. To illustrate this point, Justice Moldaver referred to the *Southam* decision and the example that a Rolls Royce would not be in the same relevant market as a Lada. In *Southam*, Justice Robertson had suggested examining evidence of inter-industry competition to address the superior-product concern.[16]

Following his consideration of the evidence presented to the Court, Justice Moldaver found that the Crown had failed to establish that the relevant product market was the product of pool car services.[17] Instead, he found that pool car operators, the trucking industry and intermodal operators were equally capable of moving, and indeed did move, identical kinds of freight on behalf of shippers from

Ontario to points west. The Court found that substantial rivalry existed among the three types of transportation services "as they constantly vied with each other for the patronage of shippers requiring freight forwarding services."[18] The differences in rates and services between the three industries were not found to be sufficient to warrant a finding that a separate market could be delineated for the services provided by pool car operators.

Certain businesses were, however, excluded from the definition of the relevant market. For example, in addressing functional interchangeability, Justice Moldaver relied on the "superior product" concept to eliminate freight forwarding services provided by airlines from the relevant market. Furthermore, services provided by Purolator and other similar businesses were excluded from the relevant market due to the type of freight being moved. Also, full carload services were removed from the relevant market due to the "50 per cent rule". However, Justice Moldaver rejected the suggestion that competition only existed at the fringes of the various industries and the contention that such competition arose as a result of the collective market power of the Accused, which allegedly enabled them to maximize profits by pricing up to the elastic portion of the market demand curve.[19] Finally, the geographic market was defined, without dispute, as "the western markets".

(ii) Market Power

Following his inclusion of standard, over-the-road trucking and intermodal rail services in the relevant market, Justice Moldaver turned to an examination of whether the Crown had met its burden of proof regarding the requisite degree of market power. Relying on *PANS* and his conclusion that both (i) a degree of market power sufficient to enable the accused to behave relatively independently of the market, in a passive way and (ii) some anti-competitive behaviour must be found,[20] Justice Moldaver held that the Crown had failed to prove that the Accused possessed the requisite level of market power.

In so finding, Justice Moldaver rejected the argument by the Crown that market power could be inferred from the fact the Accused had succeeded in maintaining their agreement for a period of eleven years. The Crown also suggested that market power was evidenced by low demand elasticity and high barriers to entry into the pool car operator business. However, the Court found that evidence of functional interchangeability and inter-industry competition far outweighed the low demand elasticity argument. The fact that the agreement had been maintained for eleven years was not accepted as proof of shippers/ customers being captive to pool car operators; it merely showed that customers were not willing to "switch for pennies".

The Court also found no evidence to support the claim that the Accused, through their collective market power, priced up to the elastic portion of the market demand curve, i.e. to the next best alternative mode. Also, with respect to the barriers to entry argument, the Court found that, although barriers into the pool car service market may be high, entry into the trucking industry, which was part of the relevant market, was relatively easy.

The Implications of *Clarke Transport*

Turning first to the application of the law, it is submitted that Justice Moldaver correctly interpreted the application of section 45, based on both the

statutory provisions and jurisprudence to date. Having said that, Justice Moldaver issued a *caveat* that, even if he had misconstrued the law, the result would not change as he remained unconvinced that the agreement had an anti-competitive object. Justice Moldaver concluded that the agreement was aimed at preserving the industry by stabilizing rates. Presumably, Justice Moldaver's definition of the market limited the potential anti-competitive impact of the conduct set out in the agreement to a level that would not offend section 45, i.e. something less than "undueness".

That being said, the decision in *Clarke Transport* does raise a number of issues regarding the efficacy of our conspiracy provisions. For example, on the one hand, while there are clear advantages to maintaining a criminal law regime for conspiratorial behaviour, the Crown has the formidable task of ensuring its analysis of the relevant market and conclusions regarding market power, among other factors, to satisfy the criminal burden of proof, i.e. "beyond a reasonable doubt". This is further complicated in the case of section 45 as a result of its requiring the showing of an undue prevention or lessening of competition. By contrast, in the case of a *per se* offence such as bid-rigging, the impact on competition is not an issue, as the Crown need only prove the commission of the act. In the context of a *rule of reason* analysis, as required under section 45, the burden on the Crown is far more substantial. Therefore, one may question whether the high evidentiary threshold required of the Crown is sufficient to justify a *per se* approach to conspiratorial behaviour as is currently done in the United States.

However, assuming the current approach toward conspiratorial behaviour is more appropriate and that Justice Moldaver was correct in his assessment of the competitive dynamics of the freight forwarding industry, the above presumptions do not address the inefficiencies that may still arise under such circumstances. One such example is the declining industry scenario discussed by Dunlop *et al.* in their review of cartels:

> Industries facing a long-term decline in demand for their output ... may suffer from problems of chronic excess capacity. Substantial excess capacity overhanging a market is likely to encourage especially vigorous competition and to render many firms' operations unprofitable. A cartel that fixes prices and allocates market shares amongst firms in the industry may promote a measure of stability in the industry by enabling a normal return to be made on capital, by enabling better wages to be paid to employees, and by avoiding the disruptive impacts of firm failures or exits on dependent communities .... However, why these circumstances justify private or state-sanctioned cartelization of the industry is not at all clear. Without intervention, the long-term effects of "cut-throat" competition in such an industry will be that insufficient revenues will be generated to replace or maintain fixed assets. As they wear out, industry capacity will be gradually reduced and a relatively orderly exit from the industry will occur over time as resources, including manpower, are deployed in other more highly valued economic activities. This is an efficient outcome. Cartelization is only likely to retard efficient adjustment processes.[21]

Therefore, the *rule of reason* approach, even where correctly applied, may still lead to inefficiencies depending on the specific market circumstances.

Conclusion

The decision in *Clarke Transport* is a major development in the evolution of section 45 of the Act. It has shown that, despite irrefutable proof that competitors had entered into an agreement in respect of market prices, such an agreement would not contravene the Act, unless the parties thereto possessed sufficient market power. It is submitted

that the *Clarke Transport* decision may result in more cooperative behaviour between competitors in reliance on the assumption that such competitors do not collectively possess market power. Considered along with the arguably more expansive approach to market definition established by *Southam*, *Clarke Transport* may result in the scope of conduct permissible under section 45 being pushed to new limits.

P.C. and N.N.

Notes

1 [1995] O.J. No. 3395, Court File No. TO-209220.
2 (1992), 74 C.C.C. (3d) 289 (S.C.C.).
3 (1995), 127 D.L.R. (4th) 263 (Fed. C.A.).
4 *Supra*, note 1 at 14.
5 *Supra*, note 2 at 321.
6 *Ibid.* at 326.
7 *Supra*, note 1, paragraph 53.
8 Justice Moldaver found that the one witness who had claimed to have engaged in rate-checking with truckers "stood out like a sore thumb," *ibid.* at paragraph 59.
9 *Ibid.* at paragraph 70.
10 *Ibid.* at paragraph 73.
11 *Ibid.* at paragraph 78.
12 (1976), 26 C.C.C. (2d) 349 (Ont. C.A.).
13 *Ibid.* at 373-4.
14 (1968), 2 C.C.C. 5 (Ont. C.A.).
15 *Supra*, note 1, paragraph 102.
16 *Ibid.* citing Robertson J.A. in *Southam*, *supra*, note 3 at 87.
17 In so finding, Justice Moldaver cited one Crown witness, Dr. Chow, in particular. Dr. Chow's conclusions were found to be "at best suspect and at worst wrong" and often founded upon "faulty assumptions, misperceptions, errors, miscalculations and a failure to take into account pertinent facts".
18 *Supra*, note 1, paragraph 133.
19 *Ibid.* at paragraph 155.
20 *Ibid.* at paragraphs 159-161, citing.
21 B. Dunlop, D. McQueen and M. Trebilcock, *Canadian Competition Policy A Legal and Economic Analysis* (Toronto: Canada Law Book, 1987) at 115-116.

DIRECTOR'S POLICY ON STRATEGIC ALLIANCES OUTLINED IN NEW *INFORMATION BULLETIN*

On November 23, 1995, George Addy, Director of Investigation and Research under the *Competition Act*, published an *Information Bulletin* (the "*Bulletin*") entitled *Strategic Alliances Under the Competition Act.*[1] In the Preface, the Director observes that some strategic alliances beneficial to the economy may be abandoned due to uncertainty on the part of some business people regarding their legality. The *Bulletin* was published as a policy statement to clarify the Director's enforcement approach to strategic alliances under the Act. It includes an Appendix containing nine "illustrative scenarios" which highlight the likely analytical framework to be taken by the Bureau in various situations. The *Bulletin* does not represent a substantive change in enforcement policy or a restatement of the law, nor is it to be interpreted as a binding statement of how the Bureau will exercise discretion in a particular situation.

The *Bulletin* does not offer a definition of the term "strategic alliances", but instead relies upon several of the more common features of alliances. The *Bulletin* states that these features appear to be:

- the relative continuing independence of the parties in respect of those matters not covered by the alliance;
- a set (albeit longer-term) time frame;
- limited scope of the arrangement and greater flexibility of the parties compared to takeovers or acquisitions; and

- reciprocity between the parties, as seen in the sharing of objectives, information and key assets.

As there are no specific provisions within the Act dealing exclusively with strategic alliances, the Bureau's analysis of these arrangements will follow the analytical framework dictated by the applicable section of the Act. The fact that a relationship between two or more firms is called a strategic alliance does not affect its legal status under the Act in any material manner.

Provisions Most Relevant to Strategic Alliances

The *Bulletin* focuses on sections of the Act most applicable to horizontal alliances, as it has been the Bureau's experience that such arrangements involving competitors are more likely to raise competition issues than either vertical or conglomerate alliances. While inquiries pursuant to either the abuse, conspiracy or merger provisions may be commenced concurrently, the Act limits prosecutions or applications to the Competition Tribunal to a single section on the basis of the same or substantially the same facts. An analytical framework is implicitly determined in deciding which provision is the most appropriate. For example, the Bureau will generally examine alliances that involve the future acquisition of control as mergers (unless that acquisition is believed to be a sham), and the applicable analytical framework would be a substantial lessening or prevention of competition test with an efficiency trade-off.

Conspiracy Provisions

The *Bulletin* reviews the three elements of the section 45 conspiracy offence, as well as the Supreme Court's two-step approach to undueness outlined in the *R.* v. *Nova Scotia Pharmaceutical Society*[2] decision. It notes that the defences and exceptions, under subsections 45(3) and 45(4) respectively, have not been argued in a conspiracy case to date, as most section 45 cases have been brought for price-fixing or market sharing agreements. The *Bulletin* states that, because the scope of the subsection 45(4) exceptions is relatively wide, firms possessing market power who wish to avail themselves of a subsection 45(3) defence may wish to strictly confine the agreement to the elements of the specific defence in that subsection in order to avoid straying into the subsection 45(4) exceptions.

However, it is important to note that the defences are not without limits. A defence may be lost if the alliance is likely to lead to an undue lessening or prevention of competition in respect of prices, quantity or quality of production, markets or customers, or channels or methods of distribution, or if the alliance restricts anyone from entering into or expanding a business. The agreement need not be explicitly directed at any of these dimensions of competition in order for a defence to be lost, only that one of these dimensions of competition is likely to be lessened or prevented unduly as a result of the alliance.

Strategic alliances often involve a considerable exchange of information between the parties and such information sharing among competitors may trigger a section 45 conspiracy inquiry. The *Bulletin* acknowledges that competitive markets function more efficiently when information is relatively free and openly available to market participants, but recognizes that information exchanged among competitors who collectively possess market power may have serious adverse effects on competition. In

light of the Supreme Court's test for undueness, the *Bulletin* notes that section 45 will not apply to an information exchange unless the parties to the exchange collectively possess market power and are engaged in the type of information sharing which may adversely impact competitive rivalry in a serious or significant way.

Risk of a formal inquiry under section 45 can be reduced if alliance members design the sharing of information in a manner which preserves the ability of the individual parties to determine "independently" what market strategy they will follow outside the alliance. It is also advisable not to use the alliance as a means of "signaling" to competitors what action the members wish outside rivals to take or what action members desire of each other in an area outside the scope of the agreement.

On the other hand, the risk of an inquiry increases if there is greater collective market power, sharing of sensitive information or evidence of anti-competitive intent. Direct exchanges of sensitive information are riskier than those made through independent third parties. Firms should also be cautious about sharing analyses and conclusions, or disaggregated data which allows for identification of individual firms' plans.

The specific defences to the general conspiracy provisions involving export consortia and specialization agreements are also discussed. The subsection 45(5) export defence applies where the agreement relates only to the export of products from Canada. The defence can be lost under certain circumstances. First, it only applies to the kinds of agreements referred to above. Second, the defence is lost if the alliance is likely to reduce or limit the real value of the exported product. Third, the defence is negated in cases where the export alliance restricts other firms from entering or expanding their business of exporting products from Canada. Finally, the defence will be lost if competition in the supply of services facilitating the export is unduly prevented or lessened. It is important to recognize that the export defence provides no defence or exemption under the competition laws of foreign countries where the consortia hope to sell their products.

The exemption from the conspiracy provisions for specialization agreements will only apply where firms decide to discontinue existing production of a particular article or service in exchange for the same from another firm. If the alliance contemplates more than an exchange of existing production, the exemption will not apply. It will also be unavailable if the parties do not wish to subject their agreement to the mandatory civil review before the Competition Tribunal that is required in order to have the agreement registered.

Merger Provisions

Given the frequency of equity investments in strategic alliances and the broad definition given to mergers in section 91, these agreements may be subject to review under the civil merger provisions. It is the Director's position that the "significant interest" aspect of the section 91 merger definition arises when one or more persons directly or indirectly acquire or establish the ability to materially influence the economic behavior of the business, or part thereof. Given the wide range of ownership structures and arrangements which may be implemented, the determination of whether a "significant interest" exists can only be made on a case-by-case basis. If the definition of a merger is satisfied, then the strategic alliance will be reviewed following the

analytical framework set out in the *Merger Enforcement Guidelines*.

A strategic alliance may be exempt from the merger provisions if it falls within the section 95 joint venture provisions. However, because section 95 only covers agreements related to a specific project or program of research and development, it may have limited application to strategic alliances where broader collaborations are often present.

Other Matters

The *Bulletin* also points out that strategic alliances may be reviewable under the abuse of dominant position provisions. In discussing the conditions that will need to apply for a case to be made, the *Bulletin* notes that in its decisions to date the Tribunal has taken a broad view of what constitutes a practice of anti-competitive acts. The *Bulletin* then discusses the Director's general education and communications program and the Program of Advisory Opinions available from the Bureau.

Conclusions and Appendix

The *Bulletin* concludes that since black and white issues are infrequent when applying the Act to strategic alliances which maintain, create or enhance market power, parties may wish to request an advisory opinion if they believe their alliance is likely to have this effect. The *Bulletin* also notes that it is important to focus on the actual and likely competitive effects of strategic alliances. Most of these agreements will not be an issue under the Act, since in most cases they are unlikely to have as their purpose or effect the maintenance, creation or enhancement of market power.

The nine illustrative scenarios discussed in Appendix 1 are meant to assist by highlighting the likely analytical approach taken by the Bureau in the examples given which involve a conspiracy, information sharing, cooperative measures to meet environmental regulations, an export consortium, a specialization agreement, a merger, an international alliance, abuse of dominance and an industry-wide agreement.

J.S.T. and J.D.J.

Notes

1 See Bureau of Competition Policy, *Strategic Alliances Under the Competition Act* (Ottawa: Industry Canada, 1995). For a copy of the related News Release issued by the Bureau of Competition Policy, see "Director Releases Bulletin on Strategic Alliances", *infra*, at 12.

2 [1992] 2 S.C.R. 606, 43 C.P.R. (3d) 1.

UPDATE ON STATUS OF YELLOW PAGES PUBLISHERS CASE

As reported in a previous issue of the *Record*,[1] on December 22, 1994, the Director of Investigation and Research commenced an Application pursuant to sections 75, 77 and 79 of the *Competition Act* against Tele-Direct (Publications) Inc. and Tele-Direct (Services) Inc. alleging that the Respondents had engaged in anti-competitive restrictive trade practices which substantially lessen competition in the telephone directory advertising services market and the telephone directory advertising space market in the geographic areas in which the Respondents operate.

The hearing before the Competition Tribunal commenced on September 14, 1995 and continued throughout the months of October and November, adjourning on December 8, 1995.

As of December 8, the Respondent had not yet completed its case. The Respondent was expected to complete its case at the hearing to be continued on January 22, 1996 and was anticipated to lead expert evidence with respect to the issue, among other things, of the proper product market definition which they say is "telephone directories". Closing arguments should be completed in mid-February 1996.

K.B.G.

Notes

1 Debbie A. Campbell, "Director Brings Application Before Competition Tribunal Regarding Yellow Pages Publishers" (1994-1995) 15:4 Can. Comp. Rec. 8.

DIRECTOR RELEASES BULLETIN ON STRATEGIC ALLIANCES

The following is a News Release issued by the Competition Bureau on November 23, 1995, and is reproduced with permission.

OTTAWA, November 23, 1995 — George N. Addy, Director of Investigation and Research under the *Competition Act*, released today an enforcement *Information Bulletin* entitled STRATEGIC ALLIANCES UNDER THE *COMPETITION ACT*. The document is being released after an extensive consultation process with industry, legal counsel, economists and government.

The principal objective in issuing the *Bulletin* is to provide guidance regarding the Director's enforcement policy with respect to strategic alliances under the *Competition Act*, and especially under the merger review provisions and the criminal conspiracy provision.

"Uncertainty regarding the legality of strategic alliances may increase the risk that opportunities to create alliances which are pro-competitive may not be pursued. To reduce this uncertainty, I am issuing this policy statement to provide general guidance on my enforcement approach to strategic alliances under the *Competition Act*," Mr. Addy said.

The *Bulletin* reflects the Director's overall compliance policy of informing the legal and business communities, both Canadian and international, about the Director's policies and practices regarding the enforcement and administration of the Act. The Bureau has issued a series of enforcement guidelines on such subjects as mergers, price discrimination, predatory pricing, misleading advertising and compliance.

A copy of the document may be obtained by contacting the Complaints and Public Enquiries Centre of the Bureau at this toll free number: 1-800-348-5358. The document is also available on the internet: http://www.ic.gc.ca/ic-data/marketplace/competition/.

DIRECTOR SEEKS CONSENT ORDER FROM COMPETITION TRIBUNAL IN INTERAC

The following is a News Release issued by the Competition Bureau on December 14, 1995, and is reproduced with permission.

OTTAWA, December 14, 1995 — George N. Addy, Director of Investigation and Research under the *Competition Act*, filed an Application for a Consent Order today with the Competition Tribunal against

Interac Inc. and Canada's major financial institutions, which are the Charter members of the Interac Association ("Interac"). This application is made under sections 79 and 105 of the Act and alleges abuses of a "joint dominant position".

This Application is the result of a lengthy investigation by the Director and extensive discussions between the Director and Interac. "Electronic networks used for financial service transactions are a vital part of the Canadian economy. The Consent Order will ensure that shared electronic networks are, to the fullest extent possible, competitive. Consumers want the benefits of a competitive environment to ensure the widest variety of services and lowest prices possible," Mr. Addy said. "Consumers and other users of these systems also want to make sure that the high level of network security and integrity that exists today will be preserved. I believe the Consent Order meets both these objectives."

The Application alleges that Interac's Charter members created the dominant shared electronic services network in Canada and abused their market power in several ways:

- they put in place a structure and membership criteria that discriminate against non-financial institutions, including third party processors and retailers, and against non-Charter members;

- they have imposed excessively high fees for new members wanting to join Interac;

- they have unnecessarily limited the services that can be provided over the Interac network thereby depriving consumers of the benefits of innovation.

As a result, competition has been lessened substantially in the Canadian market.

The Charter members of Interac are consenting to the Director's request for an Order which will require that membership in Interac be opened on a non-discriminatory basis and that members are prohibited from engaging in specified anti-competitive acts. Interac currently provides a shared cash dispensing service whereby cards issued by one member of Interac can be used to obtain cash from an automated banking machine (ABM) owned by another Interac member. Interac also provides an electronic funds transfer at the point-of-sale service (Interac Direct Payment) which allows consumers to make purchases at participating retail outlets using Interac trademarked debit cards.

The financial institutions and parties that are subject to the Application and have consented to the Order filed are:

- Bank of Montreal,
- The Bank of Nova Scotia,
- Canada Trustco Mortgage Company,
- Canadian Imperial Bank of Commerce,
- La Confédération des Caisses Populaires et d'Économie Desjardins du Québec,
- Credit Union Central of Canada,
- National Bank of Canada,
- Royal Bank of Canada,
- The Toronto-Dominion Bank,
- Interac Inc.

The Application and draft Consent Order are on the public record and available from the Competition Tribunal.

INTERAC CASE

The following is an Information Backgrounder prepared by the Competition Bureau and is reproduced with permission.

Summary

On December 14, 1995, following a lengthy investigation into the activities of the Interac Association ("Interac") the Director of Investigation and Research (the "Director"), George N. Addy, filed an Application with the Competition Tribunal for the issuance of a Consent Order involving the nine Charter Members of Interac (i.e. Bank of Montreal, The Bank of Nova Scotia, Canada Trust, Canadian Imperial Bank of Commerce, La Confédération des Caisses Populaires et D'Économie Desjardins du Québec, Credit Union Central of Canada, National Bank of Canada, Royal Bank of Canada and The Toronto-Dominion Bank) and Interac Inc.

The filing of this Application follows more than a year of in-depth discussions with Interac. The result of these extensive discussions is the successful resolution of all the key competition issues identified by the Director in this matter. The changes contemplated in the Consent Order will restore competition in this rapidly growing and important industry. The changes will allow a wider array of participants to utilize the Interac network and contribute to creating an environment that is conducive to the introduction of new services. At the same time, care has been taken to ensure that the degree of consumer convenience currently offered by Interac will not be diminished and that the high level of network security currently in existence will not be jeopardized.

If approved by the Competition Tribunal, the Consent Order, which would be issued pursuant to sections 79 and 105 of the *Competition Act*, will restore competition in the industry while avoiding the delays and costs that would be associated with bringing this matter before the Competition Tribunal on a contested basis.

This matter was pursued by the Director as a case of "joint dominance" under the abuse of dominant position provisions (sections 78 and 79) of the *Competition Act*. The Application filed by the Director alleges that the Charter Members of Interac substantially or completely control the market for the supply of shared electronic network services in Canada by leveraging their control of demand deposits and automated banking machines ("ABMs") in Canada. They are alleged to have engaged in a practice of anti-competitive acts which has had, and is continuing to have, the effect of preventing or substantially lessening competition in Canada in two markets; namely, in the "intermediate" market for the supply of shared service providers; and in the "retail" market for the supply of shared electronic financial services to consumers or cardholders.

Director's Investigation

The Director's investigation into this highly complex matter has been ongoing since May of 1990. The Director formally commenced the inquiry in July of 1992 when he believed that reasonable grounds existed for the making of a Remedial Order by the Competition Tribunal. Contact with Interac representatives has been ongoing throughout this lengthy period and has culminated in a draft Consent Order that, in keeping with the purpose of the *Competition Act*, is designed to stimulate and ensure competition in Canada.

During the investigation, the Director's staff in the Bureau of Competition Policy interviewed more than 100 persons and obtained information from a variety of sources, including: the parties in this matter; sponsored members of Interac; network operators; government departments and agencies; trade and consumer associations; as well as potential network participants such as retailers, third party processors, brokerage and investment dealers and insurance firms. In addition, the advisory services of network industry, banking, economic and legal experts were contracted by the Director.

Relevant Market

The Director determined that the relevant market in which Interac operates is the supply of shared electronic network services in Canada. These services ultimately enable Interac members to offer consumers widespread ability to obtain electronic on-line access to demand accounts, including lines of credit, attached to a deposit account or a credit or charge card. This is achieved by cardholders of one Interac member being able, by virtue of the Interac network, to utilize ABMs and Interac Direct payment ("IDP") terminals of other Interac members.

Individual financial institutions' proprietary and small or regional shared electronic networks are, by comparison to Interac, inadequate substitutes. Therefore, it has become essential for financial institutions, and increasingly essential for non-financial institutions, to connect to the Interac network in order to effectively compete in Canada in markets such as retail banking and credit/charge cards.

Anti-Competitive Acts

The Charter members of Interac are alleged in the Director's Application to have enacted and enforced By-laws which, among other things, have:

i) restricted membership in Interac to Canadian deposit-taking financial institutions that are members of the Canadian Payments Association, thereby precluding retailers, third party processors and others from participating as members;

ii) restricted certain network privileges to the Charter Members of Interac and effectively closed this class of membership to new members;

iii) established excessively high new member or initiation fees for both its ABM and IDP services and thereby discouraged participation in these services;

iv) prohibited members from charging cardholders of other members for ABM use, thereby depriving consumers of ABM deployment determined by market forces; and

v) imposed strict account eligibility criteria and limitations on the use of the network software and thereby precluded or impeded the introduction of new services or innovative products on the network.

Substantial Lessening of Competition

The practice of anti-competitive acts engaged in by the Charter Members of Interac has had, and is continuing to have, the effect of preventing or lessening competition substantially in the supply of shared electronic network services to intermediate suppliers including third party processors, financial institutions and retailers. The practice of anti-competitive acts is also alleged in the Director's Application to be having the effect of lessening competition substantially in the supply of shared electronic financial services to consumers.

Relief Sought

The Director is seeking a Consent Order that will not only bring about an end to the practice of anti-competitive acts but also put in place changes necessary to restore competition to this market. The relief being sought can be categorized into three major areas: Access, Fees and Innovation.

Access

The Consent Order would require Interac to open its network to potential participants on a non-discriminatory basis, except that Interac will be allowed to stipulate that only regulated financial institutions will be entitled to issue cards which access the network. Accordingly, participation will not be limited to members of the Canadian Payments Association and others will be able to take advantage of certain privileges currently restricted to Charter Members; most notably the right to directly connect to the network.

Fees

The Consent Order will prohibit Interac from continuing its current practice of levying new member entry fees based on card issuance. Rather, fees will be collected on a user or transaction basis payable by all members.

The Consent Order also requires Interac to discontinue its prohibition of surcharging. Accordingly, ABM deployers will be able to determine and charge a competitive price for ABM services. The current inability of ABM deployers to levy a charge to a cardholder of another Interac member precludes the deployment of ABMs in accordance with market forces.

Innovation

The Consent Order would alter the composition of the Interac Board of Directors, remove Interac's prohibition of pass-through accounts, and make available the Interac network software for new services that require on-line access to demand accounts.

Conclusions

Following a thorough examination of all of the competition issues related to the supply of shared electronic network services in Canada by the Charter Members of the Interac Association, and following extensive discussions with Interac, the Director concluded that the remedial measures contained in the Draft Consent Order will restore competition to this vital and ever-growing market.

ANOTHER FINE LEVIED UNDER THE *COMPETITION ACT* IN JOINT CANADA - U.S. INVESTIGATION

The following is a News Release issued by the Competition Bureau on December 18, 1995, and is reproduced with permission.

OTTAWA, December 18, 1995 — George N. Addy, Director of Investigation and Research under the *Competition Act*, announced today that Rittenhouse Ribbons & Rolls Ltd. was convicted and fined $98,000 in the Federal Court, Trial Division, in Toronto, Ontario, for attempting to induce a supplier of thermal facsimile paper to cut off supplies to a Vancouver distributor, because of the latter's low pricing policy.

The company pleaded guilty today to one charge under section 61(6) of the Act. The illegal conduct involved pressure placed on a supplier by Rittenhouse Inc., a large American converter of fax paper which is also the parent company of Rittenhouse Ribbons & Rolls Ltd. The offence involved firms in Canada, the United States, Japan and Hong Kong.

"The fine recognizes the serious nature of price maintenance. The resolution of this case demonstrates yet again the benefits of cooperative arrangements among competition law agencies," Mr. Addy said. "In the global economy, cooperation among competition law agencies is essential to ensure strong enforcement of competition and antitrust legislation. This is particularly true in the evolving North American economy. Firms that operate internationally need to understand the need to respect our country's competition laws."

This is the third significant fine obtained in the thermal fax paper inquiry, which is part of an ongoing joint investigative effort undertaken by the Bureau of Competition Policy and the U.S. Department of Justice (Antitrust Division). In Canada, there have been previous fines of $950,000 against Kanzaki Speciality Papers Inc. of Ware, Massachusetts, and $950,000 against Mitsubishi Corporation of Tokyo, Japan, for their role in a North American price-fixing conspiracy.