JOINT VENTURE DECISION CRIMINAL, ALBERTA COURT SAYS

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An Alberta court has held that a decision by joint operators of an oil field to sole source a contract constituted a conspiracy contrary to section 45 of the *Competition Act*, a criminal offence, and awarded damages to the company that lost out on the business.[1]

The Rainbow Lake Oilfield

Husky Oil Operations Ltd. and Mobil Oil Canada (now ExxonMobil Canada Ltd.) each owned 50% of the Rainbow Lake oilfield and operated it jointly. They embarked on a joint synergy initiative called "Mosky", whose object was to reduce costs on jointly-owned properties in the Rainbow Lake area. In 1996, as part of this initiative, they decided to sole source fluid hauling for the Rainbow Lake oilfield. Fluid hauling was the second biggest cost of the oilfield. Before 1996, they had contracted with two fluid haulers. Husky and Mobil interviewed both incumbent fluid haulers, and decided on one of them. The loser, Kolt Oilfield, ultimately went out of business and sued.

Kolt claimed that the decision by the joint operators to sole source fluid hauling eliminated competition to supply fluid hauling to the oilfield and therefore offended section 45 of the *Competition Act*. At the time, this provision made it a criminal offence to enter into an agreement to lessen competition unduly.[2]

Not a "single entity"

Mobil objected at trial that Mobil and Husky should be considered to be a single entity for competition law purposes, and thus incapable of conspiring with one another. The trial judge rejected this assertion based on a boilerplate clause in the agreement under which they operated the oilfield that said that the parties were not partners or joint venturers, but were tenants in common of the oilfield.

Breach of section 45

The trial judge then conducted the two stage analysis mandated by the Supreme Court in *PANS* for determining if there had been an "undue lessening" of competition:[3] the structure of the market and the behaviour of the parties to the agreement.

Beginning with market structure, Belzil J. concluded that fluid hauling constituted the product market, and that the geographic market was limited to Rainbow Lake. Husky was the dominant oil and gas producer in the Rainbow Lake area.[4] Husky also operated a large processing plant, which enhanced its market power. Husky and Mobil were high volume customers generating over $1 million annually in revenue for Kolt. The judge noted that Kolt lost a major customer in 1997, when Canadian National Resources Ltd. linked its well to a pipeline, thus doing away with the need for fluid hauling.

Belzil J. also considered barriers to entry. He accepted that start-up costs would not be prohibitive, but that they would be significant and operate as a barrier to entry. He refused to accept the defendants' contention that other more efficient fluid haulers could enter the market, noting that there was no evidence of any potential competitor poised to enter the market at the relevant time.

Turning to the behaviour of the parties, Belzil J. noted that Husky and Mobil admitted to entering into an agreement to sole source fluid hauling. He rejected as irrelevant their contention that the purpose of the agreement was to enhance efficiency, noting that in *PANS* the Supreme Court had rejected the availability of an efficiency defence. Belzil J. seems to have been particularly struck by the admission on cross-examination by a Mobil representative that Husky and Mobil considered that competition between the two haulers had got the prices to where they were, and the competition had to be taken out of the process in order to get the prices to where they wanted them.

Finally, Belzil J. held that Husky and Mobil breached section 45 by entering into an agreement that prevented Kolt from competing for their business:

> 173 The Plaintiff had no contractual entitlement to revenue from the Defendants for fluid hauling, but did have the legal protection, afforded to it by s. 45, to have the opportunity to compete in the marketplace for this revenue. The decision by the Defendants to use Cardusty exclusively for their fluid hauling requirements prevented the Plaintiff from competing for this business.

This led Belzil J. to conclude that Husky and Mobil were also liable for the torts of civil conspiracy and unlawful interference with economic relations.

Damages awarded "at large"

Turning to the assessment of damages, Belzil J. determined that because of the various contingencies, both positive and negative, he would assess damages from November 13, 1996 (the date that Kolt was advised it had lost the fluid hauling business) until the date of trial, which was over 14 years. He applied no contingency adjustment during this period. Since the business failed entirely in May 1997, Belzil J. held that he should assess damages based on the entire revenue of Kolt, not just the revenue from Husky and Mobil. He also held that he should assess damages based on Kolt maintaining the same fleet size as it had before the breach.

Despite having made these findings, Belzil J. did not draw any conclusions as to the amount of damages that a calculation based on his findings would yield. Instead, he noted that damages can be awarded "at large" for the torts of civil conspiracy and unlawful interference with economic relations.[5] He awarded $5 million. He then stated that "This award, which is exclusive of pre-judgment interest, is compensatory only". However, there is nothing in Belzil J.'s reasons indicating how he derived this figure.

Belzil J. also awarded $500,000 in punitive damages.

Why this decision is wrong

Belzil J.'s decision is clearly wrong, in the sense that Husky and Mobil's conduct was not the sort of conduct that section 45 was intended to address. A competition lawyer would have advised Husky and Mobil that the chances of an investigation and referral for prosecution by the Competition Bureau were remote.

To be sure, on its face, Husky and Mobil's conduct appears to fit within the parameters of section 45. It might be argued that Belzil J. was correct in his conclusion that Husky and Mobil breached section 45, and that to the extent that this is a perverse result, it is indicative of the overreach of the old section 45. Indeed, one of the reasons for amending section 45 in 2010 was the potential of the old provision to criminalize economically innocuous conduct by joint venturers. Belzil J.'s decision would appear to validate that argument.

In my view, however, Belzil J. was wrong to conclude that Husky and Mobil had violated section 45.

First, Belzil J. should not have dismissed the single entity doctrine so quickly.[6] Belzil J. dismissed the argument because the contract originally entered into in 1964 between predecessors to both Husky and Mobil expressly precluded virtually every kind of relationship between them, including partnership and joint venture.

The single entity doctrine was developed in the United States. It exempts from scrutiny under *Sherman Act* §1 (the US' conspiracy provision) arrangements where two or more legally distinct enterprises in fact form one economic actor. The doctrine looks at the substance of the relationship, not its formalities. Thus whether the companies involved are legally distinct is not determinative; the question is whether they constitute independent centres of decision-making. If they do not, then the arrangement is exempt. The US Supreme Court summarized this doctrine in the recent *American Needle* case:

> Because the inquiry is one of competitive reality, it is not determinative that two parties to an alleged §1 violation are legally distinct entities. Nor, however, is it determinative that two legally distinct entities have organized themselves under a single umbrella or into a structured joint venture. The question is whether the agreement joins together "independent centers of decision making." Id., at 769. If it does, the entities are capable of conspiring under §1, and the court must decide whether the restraint of trade is an unreasonable and therefore illegal one.

The Husky-Mobil arrangement would likely satisfy the test under the US single entity doctrine. The Husky-Mobil arrangement in substance created one economic actor, the Rainbow Lake oilfield business, and one centre of decision-making. In my view, Belzil J. was wrong to ignore current operational realities in favour of a 56-year-old contract when assessing the arrangement for competition law purposes.

The question remains whether the single entity doctrine could be asserted as a defence under the old section 45. Section 45 exempted agreements between companies that are subsidiaries or parents of one another, or subsidiaries of the same parent. Because this exemption was based on corporate structure rather than economic substance, it did not insulate joint ventures from scrutiny. But section 45 applied to agreements "with another person". Arguably, where there is one centre of decision-making, there is one "person" from the standpoint of a competition lawyer, even though there may be two or more legal persons. This would be consistent with the mischief that section 45 addresses, which is agreements between entities that constitute (or should constitute) separate centres of decision-making, and not actions of two entities that form one centre of decision-making (unless the combination is itself criminal).

Second, Belzil J. erred in finding that Husky and Mobil had excluded Kolt from the opportunity to compete. The evidence related by Belzil J. shows very clearly the opposite: the Husky and Mobil team charged with lowering fluid hauling costs held a bid process with both Kolt and its competitor Cardusty as bidders. Kolt competed, and lost.

Belzil J.'s decision really amounts to imposing a requirement on Husky and Mobil to send sufficient volumes of work to both Kolt and Cardusty to keep them alive as viable fluid hauling providers, so that they could compete on what amounted to a spot hauling market. Belzil J. expressed this in the negative:

> The decision by the Defendants to use Cardusty exclusively for their fluid hauling requirements prevented the Plaintiff from competing for this business.

Belzil J.'s assertion that his "conclusion is entirely consistent with interpreting the *Competition Act* in a manner which protects competition, not the individual competitor" could not be more wrong: he interpreted the *Competition Act* as requiring the preservation of a particular, static, market structure. Indeed, on Belzil J.'s reasoning, it would have been unlawful for Husky and Mobil to replace fluid hauling entirely with a pipeline.

The Husky-Mobil case is a nearly perfect illustration of the potential that the old section 45 had to criminalize efficiency-enhancing behaviour by joint venturers. Happily, it is not only the first case to realize these fears, but almost certainly also the last. The reform of section 45 in 2010 made it inapplicable to buying-side (monopsony) agreements. It also introduced an ancillary restraints defence designed to protect legitimate joint ventures. As a result, joint venturers seeking to improve purchasing efficiencies are no longer subject to potential criminal sanctions and damages should a judge disagree with their goals.

Endnotes

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[1] *321665 Alberta Ltd. v. ExxonMobil Canada Ltd.*, 2011 ABQB 292.

[2] Effective March 12, 2010, section 45 was amended to prohibit agreements between competitors to fix selling prices, to allocate customers, sales or markets, or to fix or limit production or supply. There is no longer a requirement to prove an anti-competitive effect – such agreements are simply illegal unless the defence can prove that they are "ancillary and necessary" to another or larger agreement that does not itself violate the section. Significantly, the amendments rendered section 45 inapplicable to buying-side agreements such as that in issue in this case. Buying-side (monopsony) agreements are now civilly reviewable by the Competition Tribunal, but can no longer be the subject of fines or civil suits for damages in provincial court.

[3] *R. v. Nova Scotia Pharmaceutical Society (No. 2)*, [1992] 2 S.C.R. 606.

[4] This conclusion would appear to be inconsistent with the evidence, summarized by Belzil J., that Mobil had some 100% properties in the Rainbow Lake area in addition to properties 50% owned with Husky. The bulk of Husky's interests were in the properties 50% owned with Mobil. Presumably Belzil J. meant to conclude that Husky and Mobil together were dominant.

[5] Damages at large are damages awarded to compensate a plaintiff for a loss, but without requiring the plaintiff to prove the loss with particularity.

[6] To be fair, it is not clear how much of an argument was made. The judge noted that no authority was cited for this proposition. In fact, the single entity doctrine is well established in the United States. The leading case in the US is *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984). The doctrine was most recently discussed by the Supreme Court in *American Needle Inc. v. National Football League*, 560 U.S. ___, 130 S. Ct. 2201 (2010).