APPENDIX I

EXCERPTS FROM A PAPER CIRCULATED BY THE HONOURABLE ANDRE OUELLET IN APRIL, 1981

Proposals for Amending the Combines Investigation Act

A Framework for Discussion

Adjudication of the Proposed New Law

7. There is overwhelming agreement on all sides that competition policy issues involving mergers, monopolies and other related matters should no longer be dealt with by criminal sanctions, but should be governed instead through the process of civil law. As indicated previously, however, past efforts to achieve this objective by providing for the establishment of a quasi-judicial tribunal that would exercise judgement on such matters based on complex economic factors encountered strong objection from some quarters. It was contended that such an approach would engender considerable uncertainty as to the application of the law. In addition, it would not carry with it the same appeal rights as in ordinary civil cases.

8. To meet these objections, it is proposed that the new provisions relating to mergers and monopolies (and related areas) be subject to the jurisdiction of the regular courts and thus amenable to existing rights of appeal in civil cases. In keeping with this approach, it is also intended that the matters which were referred to the Restrictive Trade Practices Commission for civil review as part of the 1975 amendments -- such as refusal to supply and tied selling -- should also come under the purview of the courts. The conspiracy provision of the present Act is a criminal offence and the revised provisions will continue to be criminal law. Because of the complexity of the issues involved, it is intended that specialization agreements between two or more companies -- as discussed at greater length later -- should be referred for review to the Restrictive Trade Practices Commission.

9. In drafting the new provisions which the courts would be called on to adjudicate, it would be the intention to establish criteria for judging merger and monopoly issues that were as simple and understandable as possible in the circumstances. If it is accepted to

utilize the courts for adjudicating the civil law matters under the amended law, the following options emerge as to what courts would be employed:

(a) Employ the Federal Court of Canada exclusively. Some Provincial Courts would have very few cases and little opportunity to acquire particular expertise (concentration of cases in the Federal Court would develop such expertise). The Federal Court is reasonably mobile, having registries in various centers, and being able to travel throughout Canada. The latter is a particular advantage because important cases involve firms and witnesses in more than one Province. All qualified lawyers can practice in the Federal Court irrespective of bar affiliations, while only members of a specific Provincial Bar can ordinarily practice in the courts of that Province. Exclusive jurisdiction in the Federal Court would promote consistency of decisions and prompter reconciliation of inconsistencies. Parliament could, if necessary, provide for additional procedures in the case of the Federal Court by way, e.g., of expert assistance to the Court.

(b) Employ the Superior Provincial Courts exclusively. In the past, most Combines cases have been tried in the provincial courts under the criminal law. Members of the Bar would, initially at least, feel more at home in Provincial Courts. Certain types of cases, like refusal to deal complaints, are usually local in nature.

(c) Confer concurrent jurisdiction on the Federal and Provincial Courts. This would be a compromise of the advantages and disadvantages of a) and b) above.

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[Mergers]

18. First, what is being proposed for the merger law is that it be removed from the criminal law area and dealt with under civil law procedures. This by itself is a significant reform which should be unanimously accepted. Rather than utilize a tribunal, it is

proposed that the issue be dealt with in the courts (see above). The basic test proposed for the new law is whether or not the merger is likely to lessen actual or potential competition "significantly". The public detriment test in the existing law is deleted to ensure that the development of the new law will not be inhibited by the past criminal law jurisprudence. Further guidance as to the application of the new law is given by specifying that any merger which would result in the new enterprise accounting for more than a given per cent of any market in Canada would lessen competition significantly. This does not mean such a merger necessarily would be prohibited, it could be subject to a remedial order by the court. The merger would still be allowed if a conditional order were feasible which would ensure that the merger did not result in a dominant position in any particular market. An order could be made conditional upon the divestiture of particular assets, a wider licensing of patents, a reduction in tariffs, a removal of import quotas, or a reduction in other restrictions which might reduce the damage to competition in particular markets which the merger would otherwise cause.

19. The principle underlying the proposed provision is that firms should be inhibited from obtaining, via acquisition of market shares, any market share in excess of the stated percentage, though of course firms are perfectly free to compete for larger shares of markets if they are efficient and competitive. The thresholds do not, of course, apply to vertical mergers since such mergers cross market boundaries. Vertical mergers would be judged with reference to the degree to which they foreclose markets, as a guide to whether or not competition is significantly lessened.

20. There are a number of advantages to the approach to the reform of merger law here proposed. The proposed civil law procedures get away from the inappropriate criminal law approach to mergers. The use of thresholds gives a high degree of certainty to firms in respect of the application of the law. The proposed law does not contain efficiency tests for judging mergers. The use of efficiency tests, though attractive in theory, are very difficult to apply in practical terms and thus create uncertainty as to the application of the law and raise the prospect of very uneven enforcement. In order to take into account the desirability of allowing

firms in some already concentrated industries to grow larger by merger in order to gain economies of scale and become internationally competitive, the merger threshold would have to be set reasonably high. If a firm grows through acquisition of competitors to account for more than that percentage of the market, it would be inhibited from further acquisitions in that market and would have to grow in the future by competing for a larger market share. It could also grow via diversification or entry into export markets. The advantage of this proposal is that it avoids the creation of uncertainty as to the application of the law in this area and leaves significant scope for firms to utilize the merger route in the process of growing and seeking to become more competitive while at the same time catching those mergers which are most destructive of competition. In addition, specialization agreements are to be allowed in spite of the conspiracy provision if they can be shown to be likely to give rise to real cost economies.

21. An additional proposal in respect of mergers is that where a merger would result in an extremely large new enterprise in terms of annual sales or assets, or where an enterprise already of that extremely large size was making additional acquisitions, the Director of Investigation and Research must be notified of the proposed mergers. The only mergers requiring pre-notification would be those acquisitions involving competitors (horizontal mergers) or acquisitions involving customers and suppliers (vertical mergers). The Director would be given a short period, say 60 days, to notify the parties to the merger that he does not propose to make an application in respect of the merger. The merger may not proceed until such notification is received from the Director or the time period has elapsed. The reporting threshold would represent a compromise between the need from a public policy viewpoint to have pre-notification and review of very large, potentially significant and complex mergers, and the desire to interfere as little as necessary with the decision-making process of firms in the market and to avoid placing additional reporting burdens on smaller firms.

22. At present, acquisitions by foreign controlled firms are reviewable under the Foreign Investment Review Act to determine if they are of significant benefit to Canada. If they are not, they are disallowed. These mergers are also subject to the Combines Investigation Act. It is proposed that a procedure be put in place along the lines set out in the former Bill C-13 to deal

more explicitly with the concurrent jurisdiction. Under the proposal, where the Director of Investigation and Research has certified to the Foreign Investment Review Agency that he will be proceeding against the merger under the Combines Investigation Act, no consideration will be given under the FIR Act to the competition issues raised by the merger which will instead be dealt with in the normal way under the competition legislation. The procedure has the advantage of allowing the review from a foreign investment viewpoint to proceed to a great extent in its normal way and has the advantage of ensuring that the application of the competition policy law is the same for both foreign and domestically controlled firms.

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[Monopoly]

29. In order to deal effectively with the single firm and joint monopoly problem it is proposed that a civil law provision be introduced which defines monopoly as a situation where one or more firms account for a dominant share of a market. For greater certainty, a firm is deemed to have a dominant share of the market if it accounts for some given percentage of a market; and where four firms or less account for some given percentage of a market they too are deemed to have a dominant share. This latter consideration brings joint monopoly situations clearly within the scope of the section.

30. The purpose of the market share thresholds set out above is to offer greater certainty as to when a dominant firm (or small group of firms) comes within the scope of the provision without introducing complex tests for attempting to determine degrees of monopoly power. The four-firm market share criterion would identify an industrial situation of quite high concentration where the prospect for the exercise of parallel anticompetitive conduct was very great.

31. As in the present Act, simply being in a monopoly or dominant position does not constitute an offence (or in

terms of the proposed civil provision, does not subject the firm to a remedial order). It is not the structure itself that is to be controlled, but rather the anticompetitive conduct employed to create, entrench or extend monopolies. Therefore, a remedial order only comes into play where the monopoly is engaging in anticompetitive conduct or where firms are found to be utilizing anticompetitive conduct to create a monopoly or extend a monopoly into other markets. In the case of joint monopoly, the small groups of firms must all be pursuing the same or very similar anticompetitive conduct. In order to give even greater certainty to the application of the proposed new law, the anticompetitive conduct, having or designed to have the effects described, will be listed in the proposed new section. Anticompetitive conduct means conduct of a restrictive, exclusionary or predatory nature and would include the folowing:

(a) selective price cutting in a market to eliminate or restrict the growth of a competitor or to prevent entry;
(b) narrowing, by a vertically integrated supplier, of the margin on which an unintegrated competitor is operating, to eliminate or restrict the growth of the competitor or to prevent entry;
(c) freight equalization by major firms on the plant of a new entrant;
(d) use of fighting brands or their equivalent to eliminate or restrict the growth of a competitor or prevent entry;
(e) pre-emptive acquisition of scarce facilities or resources;
(f) buying up products to prevent the development of competitive channels of distribution or to prevent the erosion of price levels;
(g) full-line forcing;
(h) adopting product specifications designed to be incompatible with products produced by other firms to eliminate or restrict the growth of a competitor or to prevent entry;
(i) market saturating advertising to eliminate or restrict the growth of a competitor or to prevent entry;
(j) acquisition, by vertically integrated producers, of suppliers or customers, to foreclose sources of supply to competitors or outlets through which competitors may dispose of their products;

(k) patent pooling or cross licensing arrangements which confine access to technology to a group having a dominant share of a market and restrict the growth of a competitor or prevent entry;

(l) conduct which is a criminal offence under the Act or could be the subject of an order under the civil provisions of the Act.

32. The normal remedy for such anticompetitive conduct by firms in dominant positions would be a cease and desist order. However, where the past anticompetitive conduct has caused such serious harm to the competitive environment that such an order would not restore competition to any effective extent, then the court may go further and order divestiture of assets of the monopoly to the extent necessary to remove the effect of the anticompetitive conduct.

33. The advantages of this proposal are that the issue will no longer be a criminal law matter and the proposed section, being very explicit, offers greater certainty as to its application both in respect of the definition of monopoly and the nature of the anticompetitive conduct which would subject dominant firms to remedial orders. The proposed section makes it clear that no attempt is being made to attack large size (or even dominant positions as such), but rather the object is to inhibit a firm or group of firms from employing anti-competitive conduct to create, entrench or extend dominant positions in a Canadian industry.

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[Statutory Monopoly]

37. Under present circumstances it is difficult if not impossible as a practical matter to challenge many of the restrictive kinds of clauses which are known to exist in intellectual property licences in Canada such as:

- restrictions on production or marketing that run on after the patent has expired;
- restrictions prohibiting any challenges to the validity of the patent, copyright, or industrial design;
- restrictions which prohibit the use of competing technology;
- tying arrangements which require the licensee to obtain raw materials from designated sources;

- restrictions which prohibit the licensee from exporting at all or from exporting to designated markets. (In a recent survey, out of 5,417 licences examined, 1,625 in some way constrained the freedom of the licensee to export);
- patent pooling or cross-licensing arrangements which confine access to the technology to a dominant group;
- restrictions which insist upon a grant back by the licensee of improvements to the patented invention. (In a recent survey, out of 5,417 licences examined, 788 required the licensee to assign rights in improvement inventions to the licensor.)

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39. A separate section on intellectual property abuse is proposed under civil procedures which would allow for remedial orders where use has been made of a patent, trade mark, copyright or industrial design in a manner not expressly authorized by the governing legislation where such use has adversely affected competition. The remedy would be a cease and desist type order or a compulsory licence in the case of a patent, copyright or industrial design. No order would be possible under the section which was at variance with any treaty, convention or arrangement between Canada and other countries.

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[Export and Import Restrictions
By Multinational Enterprises]

44. The section proposed here, under civil procedures, is designed to inhibit Canadian subsidiaries from implementing agreements with foreign parent or affiliated firms to restrict exports from Canada or imports into Canada where such restrictions are designed to protect price levels in Canada (import restrictions) or price levels abroad (export restrictions). Such agreements would not come within the purview of the section where the corporation in Canada does not account for at least some given percentage of the supply or production of the product in Canada, since this type of price discrimination can only be practised with any effect by major firms and thus insubstantial cases should be screened out. The

order from the court would require the Canadian subsidiary to withdraw from the agreement or to refrain from implementing or enforcing the agreement. Agreements of the above nature are clearly undesirable and unjustifiable from a Canadian public policy viewpoint.

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[Conspiracy Law]

... First, the new section would make it clear that the offence lies in the agreement and the natural effects it would have, whether or not it is subsequently implemented.

53. Second, while encompassing a conspiracy, combination or agreement, the definition of arrangement would be expanded to include a tacit arrangement or agreement where it can be shown that each of the parties adopts a course of conduct which would significantly lessen competition and intentionally arouses in each of the other parties an expectation that he will continue in that course of conduct if each of them adopts a similar course of conduct.

54. Third, for greater certainty in the application of the provision, the "undueness" test would be deleted. From a public policy viewpoint, it has always been rather anomalous to tell competitors that they could get together and agree to fix prices or otherwise lessen competition as long as it was not lessened too much. If a number of competitors get together and agree to fix their prices above the market price, for example, one assumes it is because they believe that price can be made to stick and that competition outside the agreement will follow suit. It seems paradoxical to excuse such conduct. Therefore, deeming provisions are imported into the proposed revised conspiracy section. If the agreement in question is a price fixing, or market sharing agreement, or an agreement to restrict a firm from entering or expanding a business, the agreement would be deemed to be illegal if it has any negative effect on competition. Thus where the agreement relates to one of these vitally important dimensions of competition, the burden of proof is closer to the current situation under U.S. antitrust law where the offence is per se. However, the per se approach can cause difficulties by catching in its net situations which were not intended to be caught or de minimus type situations. Therefore, even where the agreement is in respect of any one or more of these dimensions of competition, the provisions specify that the agreements must lessen or be likely to lessen competition before the deeming provision comes into operation so as to make the agreement per se

55. Of course, there are a number of other arrangements or agreements, involving other important dimensions of competition, (such as agreements on product introduction, qualities or functions of products, introducing of technological innovations, etc.), which can significantly lessen competition and are clearly contrary to the public interest. It is proposed here that these agreements be deemed to lessen competition significantly, and thus be illegal, where the parties to such agreements account for some given percentage of the market to which the agreement relates.

56. Finally, it is proposed that the exemption for agreements relating to such matters as exchange of statistics, defining of product standards, packaging, adoption of the metric system, etc., in the present Act be removed. Such agreements do not ordinarily lessen competition, in which case they need no protection. Where they are used as tools for lessening competition, they deserve no protection.

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[Specialization Agreements]

58. In conjunction with improving the existing conspiracy law, an exemption to the conspiracy offence is being proposed for certain specialization agreements which will increase the efficiency and international competitiveness of the firms participating in the agreements. It is argued that high tariffs in the past have encouraged a larger number of firms to set up operations in some Canadian markets than was justified by the size of those markets. The result has been that firms are producing too many products on short production runs, giving rise to inefficiencies. The purpose of the proposed provision is to allow firms to enter into agreements to specialize on some of their current product lines and arrange for other firms to specialize on some of their current lines, dropping others, even where such agreements significantly lessen competition, if the arrangement increases the efficiency of the participating firms. Given the complex nature of the specialization agreement and the efficiency issue which must be judged, it is proposed that the parties to the projected agreement would apply to the Restrictive Trade Practices Commission for

approval. Provision is also made for conditional approval on the condition that the firm spins off certain assets, licenses certain patents, or on the condition that the relevant tariff is reduced. The specialization agreement can be for a period of up to five years by which time it is considered the industry will have rationalized itself sufficiently so that the agreement is no longer needed and normal market forces can again be relied upon.

59. It is not proposed that specialization agreements relating to products not currently being produced by firms be exempted from the conspiracy provision. It is believed that normal market forces should govern whether or not firms enter new lines of business. The rationale for the proposed exemption is that firms are locked into the product lines they are currently producing because of past government tariff policies and the diversity of existing product lines is giving rise to inefficiencies. The section is designed to deal only with this very specific industrial problem.

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[International Cartels]

62. The present conspiracy law cannot deal effectively with situations where one or more Canadian firms agree with firms operating abroad to limit imports into Canada or exports from Canada or to otherwise limit competition in Canada. Clearly such agreements are not in the Canadian public interest. Therefore, it is proposed that such agreements with foreign firms be prohibited under the criminal law, where the Canadian firms account for a given percentage of the production or supply in Canada of the product which is the subject of the agreement. The section would not apply where the agreement is specifically authorized by an Act of Parliament.

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[Systematic Delivered Pricing]

. . . It is not the intention to prohibit delivered pricing systems or freight absorption by manufacturers. However, far short of this, it appears that it would be efficacious and

desirable to require that buyers have the option to purchase at any existing supply point and hence to treat the refusal to grant the option as a per se criminal offence. Such a provision would inhibit the abilities of tight oligopolies to coordinate their behaviour and to discriminate unduly in economic terms against different regions in Canada. The effect of the proposed section would permit a continuation of basing point and related systems but give buyers the option of choosing among the basing points in use, inserting more competitive pressures into the system. This would also reduce the abilities of large Canadian firms to engage in economic price discrimination by segmenting their markets.

66. The proposed section simply requires firms not to refuse to supply their customers at any location where the firms are supplying their product to other customers on the same terms and conditions available to customers in that location. It is a clear and specific prohibition and is likely to be self enforcing to a large extent. The current criminal law provision deals with discriminatory and predatory pricing, but not with economic price discrimination or systematic delivered pricing systems.

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[Competition Policy Applied To Banks]

68. In 1975, the Bank Act was amended to establish more stringent provisions defining anticompetitive behaviour by banks, by extending the existing ban against collusive agreements on interest paid on deposits or costs of loans to include agreements on service charges, amounts and kinds of loans, types of services provided to a customer, and classification of persons eligible or ineligible for loans.

69. It is now proposed to transfer the responsibility for competition policy that was in the Bank Act to the Combines Investigation Act, except for the two cases where the Minister of Finance has authority to over-ride competition policy on other specific public policy grounds, banking agreements requested or approved by the Minister of Finance and mergers of banks which he certifies as desirable.