Price Maintenance: The View from Canada

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In 2009, Canada’s price maintenance rule underwent a major change. The previous longstanding criminal provision prohibiting price maintenance was replaced by a civil regime having the effect of allowing suppliers to set resale prices for their products, provided their conduct does not lead to an adverse effect on competition. This legislative change followed in the footsteps of the 2007 decision of the United States Supreme Court in *Leegin Creative Leather Products* and brought Canada’s treatment of vertical price restraints into line with modern economic thinking, which recognizes that resale price maintenance has the potential to create both pro- and anti-competitive effects.

Resale Price Maintenance

Resale price maintenance, or RPM, is a practice whereby a manufacturer or other supplier controls the price at which a downstream firm (typically a distributor or retailer) sells the manufacturer’s product. Prices are influenced by imposing either a price floor (minimum resale price maintenance) or a price ceiling (maximum resale price maintenance). The supplier ensures compliance by penalizing the downstream party for any deviance from the supplier’s pricing policy. For instance, if a reseller refuses to maintain prices, the supplier would stop doing business with it.

Maximum resale price maintenance usually raises less competition concerns. Indeed, under Canadian competition law, maximum prices have always been lawful.

Economists have long recognized that there are circumstances in which RPM offers efficiency benefits and may therefore be pro-competitive. One such benefit is when a retailer provides services that enhance the value of the manufacturer’s products. Without RPM, there is a risk that consumers will “free ride” on the services provided by one retailer, while making their actual purchases from a third-party “deep discount” retailer. This possibility discourages the full-service retailer from investing in services to consumers in connection with the product, thereby leading to an overall lessening of service levels associated with the product.

Similarly, when one retailer invests heavily to “open up” a new market, it does not want a second retailer to come along and undercut its prices, while benefiting from the first retailer’s initial investment. For high-end brands, the establishment of a minimum retail price counters the threat of discounting, which can cheapen the image of the brand in the eyes of consumers. Consumers expect luxury goods to come with a certain level of service. The economics of their business model dictate that discount retailers may not be capable of providing that level of service.

On the other hand, RPM can also facilitate collusion between retailers. Pressure for price maintenance often comes not only from suppliers, but also from competitors of a discounting retailer who apply pressure on their supplier to discourage competing retailers from dropping the prices at which they sell the supplier’s products. If the pressure has its desired effect, the retailers who refuse to discount are protected from competition and ultimately consumers pay higher prices.

In light of the conflicting results of this analysis, many commentators have concluded that RPM cannot be deemed either purely pro-competitive or purely anti-competitive. They therefore oppose treating
RPM as a *per se* violation and prefer to instead examine instances of resale price maintenance on a case-by-case basis.

**Price Maintenance in the United States**

In *Leegin*, the United States Supreme Court overturned a nearly century-old ban on setting minimum resale prices. *Leegin* was allowed to require retailers to sell its leather products at a certain price, or risk losing distribution rights. The Court stated that a manufacturer’s agreement with a retailer to sell products of the manufacturer at, or above, a specified minimum price is no longer *per se* illegal. Instead, minimum resale price agreements are to be evaluated on a case-by-case basis under the “rule of reason”, which allows potential benefits to competition to be weighed against potential anti-competitive effects. *Leegin* overturned a 1911 decision on vertical price arrangements known as *Dr. Miles Medical Co. v. John D. Park & Sons Co.*[^2], which had set out that minimum price agreements were automatically illegal - or illegal *per se* - regardless of the circumstances.

During much of the period between *Dr. Miles* and *Leegin*, U.S. manufacturers had been able to apply the principle in the 1919 United States Supreme Court decision in *United States v. Colgate & Co.*[^3], which carved out a permissible arrangement for influencing resale prices. The “Colgate Exception” allowed a supplier to announce that it would deal only with resellers that observe the supplier’s unilaterally-set minimum resale prices. While resellers remained free to set their own resale prices, a supplier could refuse to deal with a reseller that did not observe the supplier’s unilaterally-set minimum resale prices. *Colgate* required a company to act unilaterally, thereby avoiding issues under the *Sherman Act*[^4] because there was no specific agreement.

**Europe**

In Europe, RPM is generally considered to be a “hard core restriction”, which is presumed to be anti-competitive. However, most European countries allow this presumption to be rebutted with proof of offsetting efficiency benefits.

**Canada’s Modernized Price Maintenance Rule**

Following the recommendation of the 2008 Competition Policy Review Panel, which was established by the Ministers of Industry and Finance, the Canadian Government eliminated the criminal offence of price maintenance as part of its 2009 Budget Implementation Act that also included a radical overhaul of the *Competition Act*.[^5] In its place, a new, non-criminal reviewable practice of price maintenance was introduced under which the Competition Tribunal can review and prohibit such a practice. If the Tribunal determines that the respondent has engaged in price maintenance, it may order the respondent to stop engaging in the practice or accept the other person as a customer on usual trade terms. However, the Tribunal has no authority to fine or make other monetary awards.

Previously, price maintenance had been a *per se* offence under the *Competition Act*, which explicitly prohibited attempts to influence prices upwards, whether by way of agreement, promise, threat, refusal to supply or other similar means. A person who contravened this prohibition was subject to a fine at the discretion of the Court (no maximum) and/or five years’ imprisonment.

Canada’s earlier price maintenance rule originated in the report of the McQuarrie Committee in 1951, which had been concerned with the high rate of inflation. At the time, the control of retail prices by suppliers was widespread in the economy. Over the years, the question of whether resale price maintenance should be decriminalized was increasingly debated. Also, prosecutions under the RPM rule were also relatively rare.
More importantly, price maintenance may now only be the subject of an order of the Competition Tribunal if it has had, is having or is likely to have an "adverse effect on competition" in a market. The concept of an adverse effect on competition already exists under the refusal to deal provision of the Act. The adverse effect requirement is easier to prove than the existence of a "substantial lessening or prevention of competition", as must be proven in relation to the other civil reviewable practices in the Competition Act.

In its 2006 decision in *B-Filer Inc. et al. v. The Bank of Nova Scotia,* the Tribunal stated that any refusal to deal removes one potential supplier from the marketplace and, therefore, at least *prima facie,* is likely to have some “adverse” effect on competition. Thus, at first glance, as a result of the practice, the remaining market participants are placed in a position of enhanced market power. However, in a competitive market, although a refusal to deal removes one potential supplier from the marketplace, the effects may be negligible, since one less firm selling a product may go unnoticed or may allow for a profitable opportunity for entry by a new firm. On the other hand, if remaining market participants are placed in a position of created, enhanced or preserved market power, then the effect may be considered “adverse”, even if not “substantial”.

As under the previous criminal regime, Canada’s new civil regime in respect of RPM continues to make available a defence relating to suggested resale prices, whereby the producer or supplier of a product that suggests a resale price or minimum resale price for the product is absolved of allegations of price maintenance if the supplier makes it clear to the reseller that they are under no obligation to accept the suggestion and would in no way suffer in their business relations with the producer or supplier or with any other person if they failed to accept the suggestion.

The amendments make two other changes which also reduce the situations in which the price maintenance provision will apply. The *Competition Act* now provides that the person must actually have engaged in the conduct. Mere attempts to influence prices upward are no longer problematic. In addition, the new provision only applies to supplier-customer situations (i.e. “resale price maintenance”), whereas the prior criminal offence also covered horizontal interactions (e.g. one competitor pressuring another to raise its prices).

As in the previous rule, the new RPM provision contains a number of statutory defences that prohibit the Tribunal from making an order against a supplier in respect of its refusal to supply. Included in these defences are cases where the product was being used as a loss leader or for “bait-and-switch” selling, or cases where the reseller failed to provide a reasonable level of service that purchasers of the products might reasonably expect. These defences respond to some of the pro-competitive rationales for price maintenance that had been put forward in recent years.

Canada’s new price maintenance rule has been added to the list of provisions where a private right of action is available. Thus, both the Commissioner of Competition and private parties may now initiate Competition Tribunal proceedings in respect of price maintenance (although a private party first must obtain leave of the Tribunal).

**Implications for Business**

Even before *Leegin,* US rules relating to RPM were more relaxed than Canadian rules. As a result of *Leegin,* the power of suppliers to set resale prices was significantly increased in the United States, resulting in a different standard between Canada and the US that required careful management of continental distribution chains by firms selling into Canada and their Canadian subsidiaries as a result of the stricter law that remained in force in Canada.
However, the 2009 change to Canada’s price maintenance provision more closely aligns the US and Canadian standards by removing practices that do not really constitute criminal activity from the criminal law and placing them in a context where such practices are dealt with by the Competition Tribunal only when anti-competitive effects result.

The amendment to Canada’s price maintenance rules gives suppliers more flexibility in their pricing decisions. When combined with the recent removal of the burdens of complying with rigid price discrimination/promotional allowance rules, now that outright prohibitions against mandated minimum resale prices have been removed, only firms whose pricing might have negative effects on competition need to be concerned, as they would risk coming up against the adverse effects test found in the new provision.

That said, firms having a material share of a market should not lose sight of the fact that there are large fines for those found to have violated the abuse of dominance provision of the Competition Act, including as a result of their pricing policies.

Firms must also ensure that they do not contravene the new criminal prohibitions against agreements between competitors to control prices. In Canada, such agreements are now per se illegal (i.e. they are illegal, regardless of their economic effects). Under this new “dual-track” regime that came into effect on March 12, 2010, there is a per se criminal offence intended to apply to hard-core cartels and a civil review provision intended to apply to other agreements between competitors.

The new rules permit more flexibility in crafting pricing programs on a North American (or wider) basis. For example, unilateral minimum advertised pricing policies (MAPPs) are now permitted in Canada. These have long been used in the United States, but were problematic under the previous Canadian price maintenance rules. In light of Leegin and the new Canadian RPM rules, we expect that manufacturers will seek greater control of pricing down the North American supply chains for their products. While resale price maintenance is presumed to be lawful, provided it does not have an adverse effect on competition, firms doing business in Canada should still be cautious, especially if they enjoy market power.

There have not yet been any cases under Canada’s new RPM provision. On another note, it also remains to be seen whether European jurisdictions will follow the North American trend towards dealing with RPM based on the “rule of reason”, rather than the per se standard. Much remains to be determined.

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2 220 US 373 (1911).  
3 250 U.S. 300 (1919).  
5 Competition Act, RSC 1985, c. C-34.  
6 2006 Comp. Trib. 42.  
7 Other provisions of the Competition Act where a private right of action is available include those pertaining to refusal to deal, exclusive dealing, tied selling and market restriction.  
8 In Canada, market shares of less than 35% (or 65% in a joint dominance case) will generally be considered by the Competition Bureau as indicating an absence of market power or dominance, while market shares above this level will normally prompt further examination.