

## Canada's Abuse of Dominance Law Protects Competition – And Competitors

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The Federal Court of Appeal's recent decision in *Commissioner of Competition v. Canada Pipe Company Ltd.*<sup>1</sup> is the first interpretation of the *Competition Act's* abuse of dominance provisions by a Canadian court. The FCA set aside a Competition Tribunal decision which had concluded that a loyalty rebate program employed by a dominant firm did not have anti-competitive effects. In doing so, the Court clarified the legal tests for determining what constitutes a "practice of anti-competitive acts" and a "substantial lessening or prevention of competition".

### Legal Framework

Under Section 79 of the *Competition Act*, abuse of dominant position occurs where the following three elements exist:

- one or more persons must be dominant in that they substantially control of a class of business throughout Canada or in any area therein;
- the dominant firm(s) must be engaging in a practice of anti-competitive acts; and
- the anti-competitive acts must have had, be having or be likely to have the effect of preventing or lessening competition substantially in a market.

### The Proceedings

In 2002, the Commissioner brought an application which alleged that a loyalty rebate program operated by Canada Pipe (the Stocking Distributor Program, or "SDP") constituted an abuse of dominance as well as exclusive dealing. The SDP offered a variety of rebates and discounts — representing a savings of up to 40% — to distributors who purchased all of their cast iron drain, waste and vent ("DWV") products from Canada Pipe.

On February 3, 2005, the Competition Tribunal dismissed the Commissioner's application. The Tribunal found that

<sup>1</sup> Available online at: <http://decisions.fca-caf.gc.ca/fca/2006/2006fca233.shtml>.

Canada Pipe was dominant and had engaged in exclusive dealing, but that the SDP did not amount to a practice of anti-competitive acts and there was no existing or likely substantial lessening of competition.<sup>2</sup> The Commissioner appealed the Tribunal's decision to the FCA and Canada Pipe cross-appealed the dominance finding.

It is well settled that the "substantial control of a class of business" element requires a demonstration that the dominant firm has market power in a properly defined relevant product and geographic market. The FCA confirmed this in the course of a 2:1 decision dismissing the cross appeal and upholding the Tribunal's findings that Canada Pipe had market power in six regional cast iron DWV markets.<sup>3</sup> However, on the main appeal the FCA found legal errors in the treatment of anti-competitive acts and the substantial lessening of competition analysis. The case was therefore remanded for reconsideration by the Tribunal in accordance with the FCA's reasons. This step has been stayed while Canada Pipe seeks leave to appeal the FCA's decision to the Supreme Court of Canada.

Unless the FCA is subsequently reversed, we believe that its decision makes three important contributions to the way in which loyalty rebates and other potentially monopolistic practices will be dealt with under Canada's abuse of dominance regime:

- anti-competitive acts require targeting of competitors;
- substantial prevention or lessening of competition must be assessed using a relativistic ("but for") methodology; and
- these determinations must be considered in three separate time periods — past, present and future.

<sup>2</sup> A summary of the decision is available online at: <http://www.ct-cc.gc.ca/CMFiles/InfoNoteCanadaPipe53LCR-6152005-6676.e53LCR-6152005-6676.pdf>.

<sup>3</sup> Available online at: <http://decisions.fca-caf.gc.ca/fca/2006/2006fca236.shtml>.

## Anti-Competitive Acts — Competitors Must Be Targeted

The Tribunal found that the SDP did not constitute a practice of anti-competitive acts on the basis that a practice must have a negative effect on *competition* to be anti-competitive. This was a departure from previous cases where the Tribunal had determined that the effect of a practice was simply one factor to consider along with an assessment of whether there was a predatory, exclusionary or disciplinary purpose.

The FCA held as a matter of statutory interpretation that there is no requirement that a practice has negative impacts on competition *when assessing whether conduct amounts to an anti-competitive act*. The focus of the analysis should be on the purpose of the act and the intended impact on *competitors*. The FCA rejected the position that actual consumer harm is relevant in respect of this element of abuse of dominance.

The FCA's holding that a practice of anti-competitive acts must involve an exclusionary, predatory, disciplinary or other negative purpose directed at a competitor is controversial. It is based on the observation that all but one of the illustrative anti-competitive acts in Section 78 of the *Competition Act* contain such phrasing. However, this may be too narrow an approach given that one of the general statutory examples ("buying up products to prevent the erosion of existing price levels") as well as two of the airline-specific examples added by regulation in 2000 do not contain such competitor / purpose phrasings. It also ignores the plain language in the opening of Section 78 which states that the list of illustrated anti-competitive acts is provided "without restricting the generality of the term."

This holding will require the Bureau to ensure it has evidence of an anti-competitive purpose in respect of all conduct that it complains about in an abuse case — and that this purpose must target competitors rather than just higher prices or the reduction of competition. This may make the Bureau's task easier in some cases, but more difficult in others. For example, if this approach is applied to the "joint dominance" branch of the abuse provisions, the use of "facilitating practices" that allow competitors to engage in coordinated behaviour may not be reachable because such practices generally do not target other competitors.

## Substantial Lessening or Prevention of Competition — "But For" Analysis

The Tribunal had decided that the SDP was not responsible for any substantial lessening or prevention of competition and was not a barrier to entry or expansion. In support of this finding, it had pointed to the availability of imports, new entrants, distributors' ability to switch suppliers and the existence of some competitive pricing in the market.

The FCA found that the Tribunal had improperly focussed on whether the *absolute* level of competition remaining in the market was substantial, rather than on the *relative* difference in the level of competition that would have existed with versus without the SDP. It endorsed the "but for" methodology and stated that, while this is not the only correct approach, the Tribunal must in every instance at least consider the following question: "Would the relevant markets — in the past, present or future — be substantially more competitive but for the impugned practice of anti-competitive acts?" The FCA suggested that this question could be answered by considering more discrete components, such as whether entry or expansion might be substantially faster, more frequent or more significant without the SDP; whether switching between products and suppliers might be substantially more frequent; whether prices might be substantially lower; and whether the quality of products might be substantially greater.

The FCA's insistence that the "substantial lessening or prevention of competition" element requires a comparative assessment is not surprising. Antitrust lawyers and economists routinely talk about the "but-for world" and the decision is a salutary reminder that the status quo is not necessarily the appropriate benchmark for analyzing competitive effects. While rigorous comparative analysis may cut either way in any particular case, in general it will likely be easier for the Competition Bureau to meet the substantiality test using a relative rather than an absolute benchmark.

## Time Matters

A less prominent but potentially important aspect of the FCA's somewhat formalistic analysis of the statutory provisions is its holding that there are six possible permutations of abuse: past, present and/or likely future occurrences of either a substantial lessening or prevention of competition. This could be significant in cases where abusive conduct has stopped but may have resulted in market conditions that the Bureau would like to address

with a remedial order to restore competition (which theoretically can include divestiture). It may also prove important where a particular business practice would not have been regarded as abusive when originally initiated, but becomes so through subsequent developments that change the relationship between the parties or the market structure. This too will add flexibility that may assist the Bureau in bringing future abuse cases.

## Conclusion

Overall, we do not expect that this decision will dramatically strengthen or weaken Canada's balanced and effective dominance regime. And the outcome — a remand to the Competition Tribunal — should not be

misinterpreted as a signal that loyalty programs are now inherently risky in Canada. Nor does the decision provide any sophisticated guidance on the economic principles to be used to assess this or other potentially exclusionary types of conduct such as bundling or predatory pricing.

Some observers have expressed concern that this ruling will result in abuse findings where there is anti-competitive activity that harms competitors but does not harm economic welfare. We do not agree: the decision appears to be quite clear that negative impact on both competitors and competition are now required elements in Canada.