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Antitrust Law and Innovation--Limits on Joint Research &(and) Development and Inter-Company Communication in Canada

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Antitrust Law and Innovation - Limits on Joint Research & Development and Inter-Company Communication in Canada

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I. INTRODUCTION

The accelerating pace of change in technology and business environments in today's economy highlights the importance of successful innovation. Technological advances and deregulation in some industries, such as telecommunications, mean that many of the assumptions used in operating a business in the past may require fundamental re-examination in both the short and long terms. Globalization of markets is requiring many Canadian firms to achieve international standards of quality, efficiency, and cost control in a relatively expeditious manner.

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Even today's dominant firms must constantly re-evaluate their products, production, and marketing.

Under these conditions, cooperation between competing firms can be essential for creating new or modified products and bringing them to market, and also for achieving efficiencies of production or distribution to enable Canadian firms to compete better at home, in the United States, or in other foreign markets. Benchmarking exercises, for example, can be powerful tools in analyzing a firm's cost structure in comparison to the best practice in the industry and identifying areas that can be improved.¹ In this regard, a member of the legal staff of General Motors in the United States has reported that "through competitive benchmarking, automobile manufacturers discovered and corrected minor differences in their procedures that cost suppliers millions of dollars and added little value. By harmonizing non-critical and non-competitive processes, automakers lowered their own and suppliers' costs."²

Communications between independent firms that do not compete with one another rarely raise issues under antitrust law; however, antitrust law and policy is generally suspicious of any collaboration between competitors, or at least collaboration between competitors who collectively possess market power.³ Nevertheless, it is important to remember that the thrust of the policy underlying this concern is a desire to preserve free markets and promote competition.⁴ The Director of the Canadian Competition Bureau has commented that the Competition Act, the Canadian antitrust legislation, "does not see competition as an end in itself. Rather, competition is a means to achieve dynamic efficiencies in the economy, and to provide competitive prices and quality products and services to Canadian industry and consumers."⁵

Although there has been considerable discussion recently by U.S. antitrust authorities in relation to the concept of "innovation markets"

¹ See, e.g., Paul S. Crampton, *Benchmarking and Other Types of Information Sharing*, Paper Delivered to Insight Conference on Emerging Issues in Competition Law, Toronto, Ontario (Mar. 10, 1994). See also Thomas Jorde & David Teece, *Rule of Reason Analysis of Horizontal Arrangements: Agreements Designed to Advance Innovation and Commercialized Technology*, 61 ANTITRUST L.J. 579 (1993) for a more detailed discussion of benchmarking from a U.S. antitrust perspective.

² William B. Slowey, *Benchmarking: Boon or Buzz Word?*, 7 ANTITRUST 30 (Sum. 1993).

³ See Michael Wiener, *Distinguishing the Legitimate from the Unlawful*, 7 ANTITRUST 22 (Sum. 1993).

⁴ At the same time, some elements of Canadian antitrust legislation, such as the price discrimination provisions, appear to have been enacted with a view to protecting small businesses. See, e.g., Calvin S. Goldman & John D. Bodrug, *The Canadian Price Discrimination Enforcement Guidelines and Their Application to Cross-Border Transactions*, 62 ANTITRUST L.J. 635, 637-38 (1994).

⁵ George N. Addy, *The Canadian Competition Act as a Model of Flexible, Forward-Looking Competition Law*, Address to the Conference on the Promotion of Competitiveness in Mexico, Monterrey, Nuevo Leon, Mexico (Oct. 5, 1993). See also Calvin S. Goldman et al, *The Role of Competition Policy in Canada's Industrial Policy*, 19 CANADA-U.S. L.J. 105 (1993).

for purposes of their analysis of mergers, this Article provides only a brief survey of this concept.⁶ In addition, this Article does not discuss in detail when the antitrust authorities in either the United States or Canada ought to engage in trying to define an innovation market in the context of evaluating mergers. To do so would entail an analysis that would go well beyond the scope of this Article.⁷ The concept of an innovation market has not yet found its way into the analysis of mergers by Canadian competition law authorities; however, given the recent developments in the United States, it is likely only a matter of time before this occurs.

Antitrust literature is increasingly recognizing that the concept of innovation, which had not been at the forefront of antitrust analysis, is now of considerable importance. In this regard, Richard Gilbert and Steven Sunshine of the U.S. Antitrust Division of the Department of Justice (DOJ) have stated:

⁶ See discussion *infra* pp. 27-30. Innovation markets are discussed in some detail by Susan S. DeSanti, Assistant Director of the Office of Policy & Evaluation, Bureau of Competition, Federal Trade Commission, in Susan S. DeSanti, *Innovation and Merger Enforcement: The View from the FTC*, Paper Delivered to the ABA Antitrust Section Spring Meeting in Washington, D.C. (Apr. 6, 1995).

In that paper she indicates that “[i]nnovation markets include intellectual property, and they may include goods where those goods are close substitutes for innovation efforts, but they also go beyond technology and goods markets, to encompass R&D spending and the process of creating new products.” *Id.* at 17. The author then states that the 1995 Antitrust Guidelines for the Licensing of Intellectual Property, released on April 6, 1995, define an innovation market as consisting of:

[T]he research and development directed to particular new or improved goods or processes, and the close substitutes for that research and development. The close substitutes are research and development efforts, technologies, and goods that significantly constrain the exercise of market power with respect to the relevant research and development, for example by limiting the ability and incentive of a hypothetical monopolist to retard the pace of research and development. The Agencies will delineate an innovation market only when the capabilities to engage in the relevant research and development can be associated with specialized assets or characteristics of specific firms. *Id.*

⁷ *Id.*; see also Richard J. Gilbert, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice, *The 1995 Antitrust Guidelines for the Licensing of Intellectual Property: New Signposts for the Intersection of Intellectual Property and The Antitrust Laws*, Paper Delivered to the ABA Antitrust Section, Spring Meeting, Washington, D.C. (Apr. 6, 1995). The author states that: “[U]sing an innovation market to analyze competitive effects is appropriate if the competitive effects of an arrangement cannot be adequately analyzed in conventional product markets.” *Id.* at 4; Richard J. Gilbert & Steven C. Sunshine, Deputy Assistant Attorney General for Economics and Deputy Assistant Attorney General for Mergers, respectively, Antitrust Division, U.S. Department of Justice, *Incorporating Dynamic Efficiency Concerns in Merger Analysis: The Use of Innovation Markets*, 63 ANTITRUST L.J. 569 (1995). The authors state that: “[I]nnovation raises competition issues in three distinct categories of product markets: markets for existing products, the R&D process itself, and markets for future products.” (citing William F. Baxter, *The Definition Measurement of Market Power in Industries Characterized by Rapidly Developing and Changing Technologies*, 53 ANTITRUST L.J. 717 (1984) *Id.* at 571. Barry A. Pupkin, *Widening Antitrust Coverage in the Era of Technology*, MERGERS & ACQUISITIONS, Nov./Dec. 1994, at 7.

[A]ntitrust analysis typically does not dwell on the nonprice aspects of competition. One reason is the difficulty of assessing consumer benefits from particular forms of nonprice competition . . . For many years, innovation shared the general neglect bestowed by antitrust authorities on other forms of nonprice competition. However, innovation's crucial role in generating economic growth and in enhancing global competitiveness warrants a more central role in antitrust analysis.⁸

Along similar lines, Susan DeSanti of the Federal Trade Commission (FTC) has recently pointed out:

[B]usiness leaders and economists alike increasingly realize that innovation is vital to efficient production and distribution. . . . Innovation is vital to the nation's economic efficiency, on both a macroeconomic and a microeconomic level. . . . Various economic studies have concluded that technological change and innovation are responsible for the major share of the nation's economic growth.⁹

The same principle is readily applicable to evaluations under Canadian competition law.¹⁰

There are, however, a number of other commentators from the private sector who, particularly in a U.S. context, recently have raised some concerns about the capability of current antitrust thinking to assess innovation considerations properly. These concerns relate not only to merger analysis, but also to the ability of firms to communicate with one another in an overall effort to become more innovative and efficient in their respective markets. It is this tension between traditional antitrust analysis, particularly in the Canadian context, and the need of firms to enhance their innovative capabilities, often by sharing information with other firms, that is the focal point of this Article.

Two of the leading U.S. commentators in this field are Thomas Jorde and David Teece, who have published a series of articles in the area of innovation and antitrust law.¹¹ The authors point out that, fifty

⁸ Gilbert & Sunshine, *supra* note 7, at 572-73.

⁹ DeSanti, *supra* note 6, at 20 (citing Solow, *Technical Change and the Aggregate Production Function*, 39 REV. ECON. & STAT. 312 (1957)); In another article by Dennis A. Yao, formerly of the FTC, and Susan S. DeSanti who was an Attorney Advisor to Commissioner Yao, the authors noted that "[e]specially as rapid technological change becomes typical of the most dynamic industries, it is increasingly important that innovation be appropriately valued under U.S. antitrust law." Dennis A. Yao & Susan DeSanti, *Innovation Issues Under the 1992 Merger Guidelines*, 61 ANTITRUST L.J. 505, 506 (1993).

¹⁰ The Director's 1991 Merger Enforcement Guidelines reflect the traditional focus when they state that "in evaluating whether the market power of the merging parties is likely to be greater than if the merger does not proceed, the focus is normally on the price dimension of competition." DIRECTOR OF INVESTIGATION AND RESEARCH, MERGER ENFORCEMENT GUIDELINES, INFORMATION BULLETIN NO. 5, § 2.1 (Hull, Quebec: Supply and Services Canada, 1991) (hereinafter "Merger Guidelines").

¹¹ See, e.g., Slowey, *supra* note 2. See also Thomas M. Jorde & David J. Teece, *Innovation*

years ago, Joseph Schumpeter recognized the central importance of innovation to competition,¹² and they go on to state that:

[T]o ensure that government does not impede innovation, courts evaluating communication and cooperation among competitors must be especially careful to take account of the requirements of innovation and the needs of firms to cooperate in order to innovate and successfully commercialize innovation. . . . Few would dispute that innovation is important to economic growth, economic development, and economic welfare. Yet antitrust analysis largely ignores it. . . . Lawyers and economists know very little about innovation, and as they do begin to understand it, there is a tendency to despair because taking it into account impairs - if not destroys - the validity of the simple model that many use to deal with antitrust policy issues. We believe that much of the accepted analytical apparatus should be modified to reflect a conceptual framework which explicitly takes innovation and its organizational requirements into account. We view innovation as the search for, and the discovery, development, improvement, and adoption of new processes, new products and new organizational structures and procedures.¹³

Jorde and Teece further state that policies which hinder innovation by focusing on short-run static efficiencies and inefficiencies, as well as welfare gains and losses, will likely have strong negative impacts on economic welfare.¹⁴ They add that behaviour which may appear to be anti-competitive in the static context may in fact be procompetitive in a dynamic sense, and that since the study of innovation is largely outside of mainstream economic research and antitrust jurisprudence, the possibility of expensive and distracting litigation followed by judicial error is significant.¹⁵ These authors advocate a structural rule of reason approach that is designed to avoid such errors, particularly in relation to information sharing designed to achieve procompetitive benchmarking objectives. For example, the authors state that:

[I]n our view . . . there is no evidence to support the notion, common in antitrust thinking, that ignorance of one's competitors' costs and/or internal quality programs is procompetitive. To the contrary, knowledge that one's competitors are ahead can be and has been a tremendous stimulus to action. Moreover, knowledge of how competitors achieved success can help guide a company committed to renovating its structures and systems, lowering costs, and achieving maximum

and Co-operation: Implications for Competition and Antitrust, in COLLABORATIONS AMONG COMPETITORS: ANTITRUST POLICY AND ECONOMICS, SECTION OF ANTITRUST LAW AMERICAN BAR ASSOCIATION 887 (Eleanor M. Fox & James T. Halverson eds., 1991).

¹² JOSEPH SCHUMPETER, CAPITALISM, SOCIALISM AND DEMOCRACY (1959).

¹³ Slowey, *supra* note 2, at 581.

¹⁴ *Id.* at 587.

¹⁵ *Id.* at 590.

efficiency.¹⁶

It should, however, be noted that the views of Jorde and Teece are currently subject to considerable debate in the United States.¹⁷ In addition, representatives of the Canadian Bureau of Competition Policy's Economics and International Affairs Directorate have suggested that the empirical evidence supporting the relationship between technological innovation and inter-firm cooperation or market concentration is mixed and that "[i]t is important that the law not be undermined through efforts to accommodate theoretical arguments that have only limited empirical application."¹⁸

The balance of this Article examines the extent to which the current competition law in Canada may permit or constrain innovative development particularly in relation to transactions or communications between competitors, and further considers whether it should do so. In other words, can antitrust law co-exist with innovative industrial policies and business practices? In our view, with the exception of the criminal conspiracy provisions, Canadian antitrust law is flexible enough to permit such co-existence. For the most part, the Canadian law and the antitrust authorities take into account the procompetitive aspects of cooperative behavior. However, concerns exist with respect to the overly broad ambit of the conspiracy provisions of the Competition Act. In this respect, we suggest that there is scope for greater recognition of potential efficiencies and innovation in assessing collaborative conduct under the Canadian law, which likely necessitates amending the conspiracy provision to accommodate a more modern balancing of competing public policy objectives.

¹⁶ *Id.* at 597. Along similar lines, Anthony Clapes, Assistant General Counsel of IBM, has recently stated that "[u]ntil antitrust enforcement officials become more familiar with dynamic models in industrial organization and, in particular, until they adopt a model describing the dynamic interdependence and long-run consumer welfare effects of innovational competition and market structure, the antitrust analysis of research and joint ventures should proceed with caution, asking rather different questions than a conventional static analysis might suggest." Anthony Clapes, *Blinded by the Light: Antitrust Analysis of Computer Industry Alliances* 61 ANTITRUST L.J. 899, 901 (1993). Similarly, William B. Slowey, Counsel, General Motors Corporation, has stated that: "[t]he antitrust laws should not be a barrier to the extension of innovation even when that goal can only be achieved by cooperation among competitors. Knowledge of state of the art efficiencies and best in class competitors need not be a clog on competition. In fact, it should provide a stimulus to improving a company's own programs." Slowey, *supra* note 2, at 31-32. Mr. Slowey also points out that subjects like price and marketing incentives or the like generally should be avoided in the benchmarking process. *Id.*

¹⁷ See, e.g., Joseph F. Brodley, *Antitrust Law and Innovation Cooperation*, in COLLABORATIONS AMONG COMPETITORS: ANTITRUST POLICY AND ECONOMICS, SECTION OF ANTITRUST LAW AMERICAN BAR ASSOCIATION 911 (Eleanor M. Fox & James T. Halverson eds., 1991).

¹⁸ Robert D. Anderson & S. Dhev Khosla, Economics and International Affairs Branch, Bureau of Competition Policy, *Competition Policy as a Dimension of Economic Policy: A Comparative Perspective*, Industry Canada Occasional Paper Number 7, 82-86 (May 1995).

II. RELEVANT ASPECTS OF CANADIAN COMPETITION LAW

A. Administration and Enforcement of the Competition Act

Before reviewing the specific provisions of the Competition Act, it may be helpful briefly to review its general scope and means of enforcement. The 1986 Competition Act is federal legislation. It applies throughout Canada to all sectors of the economy, including service, resource, and manufacturing industries. While the provinces have passed some trade practice legislation, it is generally not a factor with respect to the issues discussed in this Article.

The Act is administered by the Director of Investigation and Research who is appointed by the federal cabinet. The Director is the head of the Bureau of Competition Policy. The staff of the Bureau provides investigative and administrative support for the Director's statutory functions. The Director is an independent law enforcement officer and Ministers in the federal cabinet cannot direct him to make any particular decision or recommendation, although the Minister of Industry can require the Director to inquire into a particular matter.

The Director and the Bureau are responsible for the investigation and enforcement of both criminal offences and reviewable conduct under the Competition Act. Criminal offences are prosecuted in the regular courts while reviewable conduct is brought before the Competition Tribunal, a quasi-judicial body comprised of both judges of the Federal Court and lay members. Only the Director can commence a proceeding with respect to reviewable conduct before the Tribunal. While the Attorney General has carriage of criminal charges, he normally commences proceedings under the Competition Act only upon the recommendation of the Director. In addition, the Director's decision whether to commence an inquiry or make an application to the Tribunal is not subject to judicial review on the merits.¹⁹

Pausing on this point for a moment, the enforcement approach in Canada may be contrasted with the current situation in the United States. In the United States, competitors who propose to engage in a potential collaborative project need to consider the interpretation of the law and the enforcement policy of not only two federal agencies, but also the antitrust authorities in each of the states that may be affected. The state agencies actively enforce both the federal laws and their own state antitrust laws. To the extent that the Director's enforcement policies are clear, business decision-makers in Canada can achieve a greater degree of certainty than may exist when faced with multiple

¹⁹ Gauthier v. Director of Investigation and Research, *unreported* (Oct. 2, 1991). The Director's decisions may, however, be subject to review on general principles in the event of bias or capriciousness.

decision-makers enforcing the same law²⁰ or with the risk of political factors playing a greater role in the decision-making process, a situation which exists in the United Kingdom, for example.²¹

Fines for antitrust offences in Canada were relatively low until the maximum penalties were increased in 1986. The maximum fine for some offences is ten million dollars; other offences have no maximum and the fine is in the discretion of the court.²² Since 1986, significant fines have been imposed, including a two million dollar fine for a price fixing offence. In a current prosecution for an alleged price fixing conspiracy, the Attorney General has indicated publicly that he will be seeking fines of eight million dollars from some of the defendants. Further, the Director has stated that he intends to continue to seek higher fines and that he would like to be remembered "as the Director who got the first ten million dollar conspiracy fine."²³

The Director has also begun recommending that the Attorney General seek: (1) imprisonment for persons believed to have committed serious antitrust offences, and (2) orders prohibiting a corporation from paying fines imposed on individual officers or employees, although the Attorney General has so far been unsuccessful.²⁴ In addition, the Canadian antitrust authorities recently resorted to the extradition treaty with the United States to force an American to come to Canada to face charges under the Competition Act.²⁵

Thus, while the stakes in Canada are not yet as high as those in the United States, Competition Act offences are now widely regarded

²⁰ However, if Canadian businesses propose to engage in conduct that may have anti-competitive effects in the United States, they may face the same level of uncertainty occasioned by multiple enforcers.

²¹ See, e.g., *Screaming at the Umpire*, THE ECONOMIST, Apr. 1, 1995, at 217.

²² Section 36 of the Competition Act R.S. 1985, C.C-34, also provides that any person who has suffered loss or damage as a result of either (1) conduct contrary to any of the criminal offences under the Act, or (2) the failure of any person to comply with an order of the Tribunal or any court made under the Act, may sue for and recover from the person who engaged in such conduct an amount equal to the loss or damage suffered, together with the costs of proceeding with and investigating the matter. To date, relatively few civil actions have been brought under the Competition Act and it is difficult to assess the extent to which the risk of a civil action currently acts as a deterrent to conduct that may raise issues under the criminal provisions of the Competition Act. In any event, the risk of civil actions is likely to be less of a deterrent in Canada than it is in the United States, where a successful plaintiff may be awarded treble damages, and class actions and contingency fees have historically been more widely available.

²³ George N. Addy, *Bureau of Competition Policy Achievements of 1993; Outlook for 1994*, CANADIAN COMPETITION RECORD, Mar. 5, 1994, at 7.

²⁴ Harry Chandler, Deputy Director of Investigation and Research, Criminal Matters, *Getting Down to Business: The Strategic Direction of Criminal Competition Law Enforcement in Canada*, speech #S-11414/94-02, 14 (Mar. 10, 1994). See also *R. v. Royal LePage Real Estate Services Ltd.*, (Dec. 20, 1994), Queen's Bench of Alberta, Judicial District of Calgary (unreported) in which the Court declined to impose a term of incarceration or issue an order prohibiting a corporation from paying a fine imposed on an officer for a price maintenance offence.

²⁵ Daniel Girard, *'Sale' Brings \$130,000 Fine*, TORONTO STAR, Feb. 8, 1995, at B-1.

as serious crimes. Further, the civil provisions are more actively enforced and an investigation under either the civil or criminal side of the Act can divert significant resources and management time from more productive endeavors.

B. *Relevant Legal Issues*

The principal questions to be asked before embarking on a collaborative project with a competitor in Canada are:

- (1) Does the proposal constitute an agreement to prevent or lessen competition unduly for the purposes of the criminal conspiracy provisions of the Competition Act?
- (2) Does the proposal constitute a “merger” for the purposes of the civil merger provisions of the Competition Act and, if so, is it likely to prevent or lessen substantially some element of competition between the parties?
- (3) Do one or more parties to the proposed project possess a dominant position in any market that includes part or all of Canada for the purposes of the civil abuse of dominant position provisions of the Competition Act? If so, is the proposed conduct likely to have any significant exclusionary, disciplinary or predatory effect on a competitor that may be considered to prevent or lessen competition substantially?
- (4) Is the proposed project likely to have any anti-competitive effects on consumers, customers, exporters or other persons in the United States or other foreign jurisdictions that may raise issues under the antitrust laws of the United States or any other country?

If any of these situations apply, it is then appropriate to consider whether any exemption or defence may be available. With regard to the Canadian legislation, it may be noted that different analytical factors and defences may apply with respect to the criminal and civil provisions of the Act. For example, efficiency gains play a greater role in the analysis under the civil provisions than is permitted under the case law to date relating to the criminal conspiracy provisions.

C. *Agreements in Restraint of Trade*

The Competition Act contains, in section 45, a general prohibition on conspiracies or agreements to restrain or injure competition *unduly*. This provision has been applied most frequently in the context of price fixing or market allocation agreements and group boycotts.

Section 45 does not encompass conscious parallelism. Without an agreement, understanding or mutual consent between two or more parties, there can be no section 45 offence even if two competitors follow each other's prices or conform with respect to other aspects of competition between them. However, an agreement can be proven through a course of conduct or circumstantial evidence, and it is not necessary for

the agreement to have been carried into effect. For example, the exchange of competitively sensitive information, followed by parallel conduct, may lead a court to infer the existence of an agreement. Further, it is not necessary that the parties to an agreement specifically intend to lessen competition. An offence may be committed if the parties intended to enter into the agreement and knew its terms, and the parties, as reasonable business persons, knew or should have known that the effect of the agreement would be to prevent or lessen competition unduly.²⁶

In 1992, the Supreme Court of Canada in the *Nova Scotia Pharmaceutical Society* case (also known as “PANS”) defined “unduly” in terms of the ability of the parties to an agreement to exercise a moderate degree of market power. The Court held that, in order to constitute an offence, an agreement must have an anti-competitive effect and the parties to the agreement must possess at least a moderate degree of market power.

Mr. Justice Gonthier, writing the unanimous decision of the Court in the *PANS* case, said that “market power is the ability to behave relatively independently of the market” and that “the level of market power necessary to trigger the application of [section 45]” is not as high as substantial or complete control. He added that “what is more relevant is the capacity to behave independently of the market, in a passive way. A moderate amount of market power is required to achieve this”²⁷ Further, Mr. Justice Gonthier said that if market power exists independently of the agreement in question (as opposed to being created by the agreement), “any anti-competitive effect of the agreement will be suspicious” and that “a particularly injurious behaviour [such as price fixing or market-sharing] may also trigger liability even if market power is not so considerable.”²⁸

In contrast to the approach in the United States, the Canadian Supreme Court adopted neither a *per se* rule (which prohibits certain types of conduct, such as price fixing, regardless of the degree of lessening of competition in the market as a whole) nor a full rule of reason standard (which weighs the anti-competitive effects of an agreement against its beneficial consequences).²⁹ Mr. Justice Gonthier

²⁶ For a discussion of the *mens rea* requirements and other aspects of the criminal conspiracy provisions of the Competition Act, see Paul S. Crampton & Joel T. Kissack, *Recent Developments in Conspiracy Law and Enforcement: New Risks and Opportunities*, 38 MCGILL L.J. 569 (1993); CALVIN S. GOLDMAN, Q.C. & JOHN D. BODRUG, *COMPETITION LAW OF CANADA*, ch. 8 (1994).

²⁷ *R. v. Nova Scotia Pharmaceutical Society*, 43 C.P.R. 1, 34 (3d ed., 1992 (hereinafter “PANS”).

²⁸ *Id.* at 36-37.

²⁹ For a discussion of the U.S. law, see ABA ANTITRUST SECTION, *ANTITRUST LAW DEVELOPMENTS* 30-59 (3d ed., 1992); In particular, citing *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), the text indicates that, under the rule of reason, the fact finder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as

characterized the Canadian conspiracy provision as mandating a “partial rule of reason inquiry into the seriousness of the competitive effects of the agreement”.³⁰ Mr. Justice Gonthier stated that:

[C]onsiderations such as private gains by the parties to the agreement or counterbalancing efficiency gains by the public lie . . . outside of the inquiry under s. [45]. Competition is presumed by the Act to be in the public benefit. The only issue is whether the agreement impairs competition to the extent that it will attract liability.³¹

Since the *PANS* decision, the Canadian antitrust authorities have indicated an intention to interpret *PANS* as precluding any consideration of procompetitive aspects of an agreement. For example, even if the agreement results in the introduction of a new product, a Canadian Department of Justice lawyer has stated that “this would be no defence.”³² Nevertheless, it remains to be seen whether the courts will interpret the *PANS* decision in a similar manner.

The Competition Act may be less flexible than the U.S. law in accommodating information exchanges, such as benchmarking or col-

imposing an unreasonable restraint on competition. Subsequent cases have limited the scope of the inquiry to whether the restraint is one that promotes competition or one that suppresses competition. In this regard, the text further notes that some cases appear to equate competition with “economic efficiency,” while others interpret it, apparently more broadly, to refer to the process of rivalry among firms. *Id.* at 42-43. See also Presley Warner & Michael Trebilcock, *Rethinking Price Fixing Law*, 38 MCGILL L.J. 679, 693 (1993) (citing Bork).

³⁰ *PANS*, *supra* note 27, at 31.

³¹ *Id.* In this regard, Mr. Justice Gonthier cited and expanded upon the following passage from an earlier decision of the Supreme Court in the *Howard Smith* case: “[t]he statute proceeds upon the footing that the preventing or lessening of competition is in itself an injury to the public. It is not concerned with public injury or other public benefit from any other standpoint.” *Howard Smith Paper Mills Ltd. v. The Queen*, 29 C.P.R. 6, 13 (1957).

³² John S. Tyhurst, *Section 45 of the Competition Act: When Does Co-operation Become Conspiracy*, Paper Delivered to Insight Conference on Emerging Issues in Competition Law, Toronto, Ontario 12-14 (Mar. 10, 1994):

It would not be open to an accused to attempt to escape liability [under section 45] by arguing that an agreement which lessens competition to an undue degree nevertheless had the effect of *lowering costs* or permitting past or future gains in efficiency . . . As stated earlier, in the United States, it is possible to argue, notwithstanding the anti-competitive effects of an agreement in restraint of trade (even a so-called ‘*per se*’ offence such as price fixing), that *benefits such as new product introduction* or efficiency may be realized which justify the agreement. In Canada if an agreement lessens competition to an undue degree, *this would be no defence.* (emphasis added). *Id.*

It may, however, be noted that in a paper delivered to a Canadian Bar Association Conference in 1994, Margaret Sanderson of the Bureau of Competition Policy appeared to take a contrary view when she stated that “while the court’s review of objective intent in the *Nova Scotia Pharmaceutical Society* case suggests there is some consideration of the possible efficiency motivations of firms when engaging in various practices, it is clearly not the full ‘rule of reason’ consideration that is possible under section 79 [abuse of dominant position].” Margaret Sanderson, *It Is Better to Know Some of the Questions Than All of the Answers*, Paper Delivered to the Canadian Bar Association Conference 23 (1994).

laborative research and development which may possibly lessen some aspect of competition between the parties, but also have significant procompetitive effects that arguably outweigh any lessening of competition. For example, if the manufacturers of a product in Canada were to agree to standardize certain parts used in the manufacture of the product, there may be certain circumstances in which that could be considered to amount to a lessening in competition between them. But if the result is to lower the costs to the Canadian manufacturers significantly, the question is whether that lowering of costs ought to be weighed against the lessening in competition with respect to the components. In light of the *PANS* decision, such a balancing exercise may not be contemplated by the Canadian conspiracy law.

On the other hand, section 45 does not create a *per se* rule with respect to any particular type of agreement. Even a blatant price fixing agreement could be permissible if the parties have no market power. In other words, firms with a low market share (for example, below twenty-five percent in any market in which they compete) may engage in joint research and development or inter-company collaboration without fear of violating section 45. (At the same time, a firm with a twenty-five percent share of a market in Canada may be relatively small by international standards.)

If the markets in which the parties compete are truly international, then two or more competing Canadian firms might not possess collective market power even if they account for a high percentage of domestic production. In that case, they may be relatively free to collaborate, at least, for the purposes of Canadian law. Parties should also consider whether collaboration with regard to such international markets may lead to collusion, or be perceived to lead to collusion, with regard to any other businesses, products, or markets in which the collaborating firms compete. In addition, particularly in light of the *Hartford Insurance* and *Pilkington* cases³³ and the international guidelines released earlier this month by the DOJ and the FTC,³⁴ the parties should also consider whether a proposed co-operative project raises issues under the antitrust laws of the United States or any other country which may be affected.³⁵

³³ *Hartford Fire Insurance Co. v. California*, 113 S. Ct. 2891 (1993); *United States v. Pilkington plc*, 59 Fed. Reg. 30, 604 (June 14, 1994). For a discussion of the *Pilkington* decision, see Robert P. Taylor, *Pilkington, Microsoft, and S.C. Johnson Signal a Policy Shift at DOJ*, 9 Fall ANTITRUST 23 (Fall 1994).

³⁴ U.S. DEPARTMENT OF JUSTICE AND THE FEDERAL TRADE COMMISSION, ANTITRUST ENFORCEMENT GUIDELINES FOR INTERNATIONAL OPERATIONS (Apr. 1995).

³⁵ For a discussion of the extraterritorial application of Canadian competition laws, see Calvin S. Goldman et al, *International Mergers and the Canadian Competition Act*, FORDHAM CORP. L. INSTIT. 217 (1992); Calvin S. Goldman et al., *Canadian Competition Policy in a Competitive Global Trading Environment*, GLOBAL COMPETITION POLICY (Edward M. Graham & J. David Richardson eds., Washington: The Institute for International Economics, forthcoming).

Geographic markets are not always easy to define and the challenge for Canadian competition authorities is to adopt a dynamic analysis and recognize at an early stage that a geographic market is expanding so that Canadian firms are not left behind and permitted to collaborate only after the international market is well-established. The current Director appears to be sensitive to this issue. For example, he has commented that “geographic markets for the purposes of competition analysis seldom conform to political boundaries.”³⁶ In 1991, when the current Director was then the Senior Deputy Director responsible for the Mergers Branch, the Bureau investigated a merger in the electrical distribution equipment business. Although the Bureau concluded that the merged entity had a “significant” share of the Canadian market, the “trend toward a North American market for these products” was a factor in the Director’s decision not to challenge the acquisition.³⁷ More recently, the current Director has commented that “given the internationalization of markets, competition policy must be flexible enough both to foster competition and to enable business to make the structural adjustments necessary to respond to contemporary market demands.”³⁸

We have suggested that two firms accounting for a significant portion of Canadian production might not possess market power for the purposes of section 45 if they compete in a wider geographic market that includes other significant competitors. Conversely, there may be less antitrust risk to a Canadian firm engaging in a collaborative project with a foreign firm that carries on a similar business, either on the basis that the two firms do not compete in the same market or, if they do compete, there may be enough other foreign competitors in the international market such that the collaborating firms would not collectively possess market power. For example, Ford is reported to have significantly improved its accounts payable operations after benchmarking its procedures to those of Mazda.³⁹

Some consideration should also be given to the strategic plans of the parties and whether the collaborative activity would preclude new entry by one of the parties to the joint venture so as to *prevent* competition in Canada unduly. We are not aware of the Director having challenged any transaction on this basis in Canada to date, however an issue could arise if one of the parties was a uniquely poised entrant and had specific pre-existing plans to enter the market if the collaborative

³⁶ George N. Addy, *The Competition Act and the Telecommunication Industry*, Address to the Institute for International Research Telecommunications Conference, Toronto 11 (Mar. 29, 1994).

³⁷ *Schneider/Square D*, Backgrounder, Consumer and Corporate Affairs Canada, Sept. 17, 1991 at 3.

³⁸ Addy, *supra* note 5, at 1.

³⁹ Slowey, *supra* note 2, at 31.

project did not proceed.

In light of the low threshold of moderate market power for an undue lessening of competition established in the *PANS* decision, it can be seen that there is reason to be cautious about any type of collaborative arrangement with a competitor where there is some possibility that the parties to the arrangement could be considered to have market power and the arrangement may be viewed as resulting in some lessening of competition, even if the project is likely to bring about significant benefits to the economy as a whole.

Even after the *PANS* decision, however, it can still be argued that section 45 should not prohibit collaboration to bring a new product to market where, in the absence of the agreement in question, the product would likely not have been brought to market at all. In such a case, a court may still be entitled to find that the agreement is not likely to lessen competition unduly, even though, in isolation, one element of the arrangement could be characterized as lessening some aspect of competition. In other words, if the effect of prohibiting the agreement would be to prevent the product from coming to the market, it would seem to be an overly narrow approach for a court to focus only on one aspect of the agreement that cannot be separated from the entire arrangement. A broader perspective would be consistent with the "purpose clause" of the Competition Act, which indicates that the Act is intended to promote the efficiency and adaptability of the Canadian economy and the expansion of opportunities for Canadian participation in world markets.⁴⁰

The 1988 International Guidelines issued by the DOJ, for example, suggested that efficiencies enabling parties to provide a new service that otherwise would not be available ought to be taken into account in a rule of reason analysis.⁴¹ The difference between the U.S. and Canadian approach in this regard is illustrated by the *BMI* decision of the U.S. Supreme Court in 1979. In that case, the U.S. Supreme Court held that a rule of reason analysis should apply to blanket licence agreements issued by two associations of composers with respect to the use of copyrighted musical compositions at fees negotiated by the associations. That decision was based partly on the Court's finding that it would be virtually impossible for thousands of composers to negotiate individually over the use of each song, for each user to report the amount of use, and for each composer to police the use of his works by authorized and unauthorized users. In essence, the agreement created a

⁴⁰ COMPETITION ACT, § 1.1; However, the "purpose clause" further states that the Competition Act is also intended to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy and provide consumers with competitive prices and product choices. *Id.*

⁴¹ COMPETITION ACT, § 3.0; The 1995 U.S. Antitrust Enforcement Guidelines for International Operations released earlier this month do not contain a similar discussion.

forum for buyers and sellers that yielded improvements in the market as a whole. Similarly, in the *Nabanco* case, the U.S. Court of Appeals for the 11th Circuit upheld a uniform interchange fee payable to issuers of bank credit cards in the VISA system because individual fee negotiations were impractical, would produce instability and higher fees, and could result in the demise of the credit card system.⁴² The blanket licences in the *BMI* case could be regarded as lessening competition with respect to royalties or other terms of the agreement and the uniform interchange fee in *Nabanco* could be regarded as limiting competition in the fee charged by the card issuing banks in the VISA system; however, it is not clear whether the resulting benefits could be taken into account under a section 45 analysis.

D. Exemptions to the Conspiracy Provisions

Conspiracies or agreements relating only to the export of products from Canada are exempt from section 45. However, to be exempt they must not be likely to result in a reduction or limitation of the real value of exports, restrict any person in the export of products, or lessen competition unduly in the supply of services facilitating the export of products from Canada. No registration is required to rely on this exemption. It is also important to ensure that information exchanges among parties to an export consortium do not unnecessarily extend into other areas that may be relevant to competition in the domestic market. Further, parties to such an agreement should be cognizant of potential restrictions under the antitrust laws of the countries into which their products are exported or other countries that may be affected by their agreement.

Agreements entered into with the federal government or a provincial government, or more generally, conduct undertaken pursuant to a statutory direction or authorization may fall outside the scope of the Competition Act on the basis of the "regulated conduct defence;" however, separate consideration of whether such government involvement may constitute a defence under U.S. or other foreign antitrust laws may be required, and a number of questions remain concerning the application of the regulated conduct defense to reviewable matters under the Competition Act.

The Competition Act provides a further limited exemption for agreements relating only to cooperation in research and development, exchanging statistics, defining product standards, advertising restrictions, and measures to protect the environment. However, to benefit from the exemption, any such agreement must not be likely to lessen competition unduly in respect of prices, production, markets, customers, or channels of distribution and must not be likely to restrict any

⁴² National Bancard Corp. v. Visa USA, Inc., 479 U.S. 923 (1986).

person from entering into or expanding a business. This exemption may be helpful for a particular proposal but, in light of these limitations and the low threshold described in the *PANS* decision, it is unclear whether and to what extent this exemption either permits agreements that would otherwise be prohibited or provides a practical degree of comfort to business persons to proceed with these types of agreements where there would otherwise be some cause for concern.⁴³

E. Director's Draft Information Bulletins on Strategic Alliances

In September 1994, the Director issued a draft information bulletin on strategic alliances because he was concerned that "if there is uncertainty regarding the legality of strategic alliances, there is a risk that alliances that are beneficial for competition and the efficiency of the economy may not be pursued."⁴⁴ However, the 1994 draft bulletin reinforced the view that the Director was adopting an overly conservative approach to the enforcement of section 45. For example, the Canadian Manufacturers' Association (CMA) commented that the 1994 draft bulletin's discussion of the conspiracy provisions in section 45 of the Act was "so strong that the comforting parts of the document are overshadowed" and that "the draft bulletin tends to discourage rather than support the formation of procompetitive arrangements."⁴⁵

⁴³ DIRECTOR OF INVESTIGATION & RESEARCH, COMPETITION ACT, DRAFT INFORMATION BULLETIN ON STRATEGIC ALLIANCES UNDER THE COMPETITION ACT (Feb. 1995) (hereinafter DRAFT INFORMATION BULLETIN). This exemption may be lost if there is even an unintended lessening or prevention of competition with respect to one of the specified areas. The draft bulletin adds that:

[C]onsequently, a strategic alliance which may be directed primarily at research and development, but which is likely to have an undue effect on prices owing to an ancillary arrangement to jointly market and distribute the newly produced goods or services, may cause the Director to initiate an inquiry under the conspiracy provisions. *Id.* at 15.

⁴⁴ George N. Addy, Address to the Canadian Manufacturers' Association, Ottawa 2 (Mar. 7, 1995).

⁴⁵ *Id.* at 3. For example, the 1994 draft bulletin commented as follows on the risk of information sharing between competitors in the context of a hypothetical benchmarking exercise between clothing retailers with respect to administration, warehousing, and distribution costs:

[I]f the parties to the wider strategic alliance possess market power, and if it is found that, because of the information exchange, there is reduced uncertainty about the competitive reaction of rivals and that this is likely to lead to an undue lessening or prevention of competition, the firms risk violating the conspiracy provisions of the Act. Under these circumstances, competition concerns could arise even in cases where the information to be shared does not relate to future pricing, capacity or marketing strategies. This of course, requires a full examination into whether the parties to the benchmarking exercise collectively hold market power. Where they do, an exchange of information is more likely to raise competition concerns. . . . The difficulty with any information exchange between horizontal competitors, particularly exchanges involving commercially sensitive information such as costs, is that it is difficult to know when a benign exchange becomes potentially liable under the Competition Act. The importance of exercising extreme caution cannot be over emphasized, given the fact that potential criminal liability is involved. (emphasis added)

In February 1995, the Director issued a revised draft information bulletin on strategic alliances. The revised draft recognizes that “many firms are facing external pressures to become more innovative and efficient in order to remain competitive in domestic and foreign markets. These pressures include falling trade barriers; innovations which affect the types of products and services produced, the production process, or the organization of firms and institutions; and, consumer demands for better product and service quality, highly customized products and services, and greater product and service variety. . . . The response of some firms to these pressures is to form strategic alliances.”⁴⁶

The draft bulletin also states that:

[O]nly those elements of a strategic alliance which represent a serious restraint of competition would be targeted by the conspiracy law. This means that many of the beneficial aspects of a strategic alliance may not be challenged. For example, where competitors develop technology sharing agreements and reciprocal patent licensing there may not be a serious adverse effect on competition, but where ancillary to these arrangements the parties begin to allocate markets between themselves or agree on prices, then this may run afoul of the conspiracy provisions. Unless the benign elements of the cooperative arrangements are seen as part of a broader conspiracy they will not be challenged by the Bureau.⁴⁷

Further, the revised draft bulletin comments that strategic alliances often involve a considerable exchange of information between the parties and that “information exchange among competitors who collectively possess market power may have serious adverse effects on competition, depending upon the nature and timing of the information exchange”, particularly where the parties compete in markets with high levels of concentration, barriers to entry and relative stability, and the information exchange “may reduce uncertainty about rivals’ competitive responses and so act to further temper rivalry.”⁴⁸ The draft bulletin adds that:

[T]he risk that an inquiry may be initiated in respect of information sharing increases with several factors. First, the greater the market power collectively held by the parties to the information exchange, the more likely an information exchange in respect of any significant aspect of rivalry may adversely impact competition. Second, when particularly sensitive information important to rivalry is shared, this may be more likely to be viewed as behaviour injurious to competition. In

DIRECTOR OF INVESTIGATION AND RESEARCH, COMPETITION ACT, DRAFT INFORMATION BULLETIN, COMPETITION ACT 25 (Aug. 26, 1994). This passage was omitted from the revised draft issued in February of this year.

⁴⁶ DRAFT INFORMATION BULLETIN, *supra* note 43, at 6.

⁴⁷ *Id.* at 14.

⁴⁸ *Id.* at 16.

this regard, firms should be cautious about exchanging information in respect of current or future pricing, trading terms or marketing strategies. Firms should also be cautious in sharing the analyses or conclusions developed from the information exchange, in order to preserve their ability to act independently beyond the alliance. Direct exchanges of sensitive commercial information between competitors are riskier than those made through an independent third party, although care needs to also be taken when involving third parties. Similarly, the exchange of disaggregated data which allows for identification of an individual firm's plans is riskier than exchanges involving aggregated data. Third, any evidence of anti-competitive intent increases the likelihood that an inquiry may be initiated. Evidence of coercion on the part of one or more of the alliance partners to have another party act in a prescribed anticompetitive manner may lead to an inference of anticompetitive intent.⁴⁹

With respect to non-price aspects of competition, the draft bulletin comments that "in cases where product quality, service, promotional activity or innovation are an important determinant of competitive rivalry such that an agreement in respect of one of these is likely to have a significant adverse effect on competition between the parties, the Director may view such agreements as providing grounds for inquiry" (emphasis added).⁵⁰ Although the revised draft bulletin has a less aggressive tone and tries to be more helpful than the 1994 draft, it still leaves a great deal of room for grey areas and resulting uncertainty.

F. Specialization Agreements

The specialization agreement provisions of the Competition Act, which were added in 1986, provide a further "defense" to the conspiracy provisions that reflects the efficiency enhancing purpose of the legislation. A specialization agreement is defined as an agreement under which each party agrees to discontinue production of a particular article or service. An agreement registered under this provision is exempt

⁴⁹ *Id.* The 1995 draft bulletin also provides a helpful illustrative example with respect to information sharing. *Id.* at 28-30.

⁵⁰ *Id.* at 13. Further, the information sharing example in the 1995 draft bulletin discusses a benchmarking exercise between an appliance manufacturer and one of its competitors with respect to administration, warehousing, and distribution costs in a situation where neither firm could individually afford an information technology system, but each needs to utilize such a system in order to remain competitive with the largest firms in the industry. The 1995 draft bulletin initially comments that the two firms are unlikely to have market power given that larger firms in the industry are not participating with them, but adds that if the parties did have market power, "the benchmarking exercise could give rise to *reduced uncertainty about the competitive reaction of rivals*. Under these circumstances, a competition issue could arise even in cases where the information to be shared does not relate to future pricing, output or marketing strategies." (emphasis added). *Id.* at 28-30. This passage suggests a low threshold for the commencement of a criminal inquiry.

from challenge under either the criminal conspiracy provisions or certain reviewable provisions of the Competition Act relating to exclusive dealing. It covers only strategic alliances where each party wants longer production runs of one product.

The Tribunal may register such an agreement where it finds that the agreement has been made free of any coercion and the efficiency gains likely to result from the agreement are greater than the likely effects of any lessening of competition. If the expected efficiency gains fail to outweigh the lessening of competition likely to result from the agreement, the Tribunal could make registration conditional on the divestiture of assets or the broader licensing of patents or certain other actions. As noted above, the Supreme Court has been reluctant to consider the positive impact of efficiency gains under a "partial rule of reason" analysis in conspiracy cases. However, it is clear that the Tribunal could register some types of specialization agreements which would otherwise offend the conspiracy provisions in section 45.

In 1986, it was hoped that the specialization agreements would play a significant role in facilitating the restructuring of Canadian businesses, but so far these provisions have not been used. Representatives of the Bureau have suggested several possible explanations for their lack of use: (1) "[i]n most cases, the general standards applicable under the merger and conspiracy provisions of the Competition Act probably provide sufficient scope for efficient cooperative arrangements;" (2) the specific wording of the provisions, which may be perceived as limiting their application; (3) procedural difficulties, particularly in respect of the specialization agreement provisions which involve proceedings before the Tribunal; and (4) concerns that even if a particular arrangement is sanctioned under the Competition Act, it might raise concerns under the competition laws of other jurisdictions, such as the United States, in which the parties operate.⁵¹ Further study of this issue is required.

G. Mergers

For the purposes of the Competition Act, a "merger" is defined broadly to include any form of an acquisition of control over or a "significant interest" in the whole or a part of a business. The Director considers that the merger provisions may apply not only to acquisitions of shares or assets, but also to agreements that give a person the ability to control or influence materially another business.⁵² Asset transactions which may fall within the scope of the Act's merger provisions include purchases or leases of a brand name or intellectual property rights.⁵³ If

⁵¹ Anderson & Khosla, *supra* note 18, at 88.

⁵² See discussion *supra* at Part I.

⁵³ See discussion *supra* at Part I.

he determines that a merger is likely to prevent or lessen competition substantially, the Director may apply to the Tribunal for an order to dissolve or enjoin a merger at any time within three years of the substantial completion of the merger.⁵⁴ With respect to mergers and other reviewable matters, the Director also has the power to seek interim injunctions.⁵⁵

In defining relevant product and geographic markets, the Director's Merger Enforcement Guidelines adopt a "hypothetical monopolist" approach which is similar to that described in the 1992 U.S. Horizontal Merger Guidelines. The Competition Act specifically provides that the Tribunal may not rely solely on market shares in assessing whether a merger is likely to lessen competition.⁵⁶ However, the Merger Guidelines state that the Director is not likely to challenge a merger on the basis of concerns regarding the unilateral market power of the parties to the transaction if the post-merger market share will be less than thirty-five percent. Similarly, the Director is not likely to challenge a merger on the basis of concerns relating to the interdependent exercise of market power where the four largest firms in the market would account for less than a sixty-five percent market share or where, notwithstanding this fact, the merged entity would have less than a ten percent share.⁵⁷ These are not fixed rules. A merger below these thresholds could be challenged and many mergers with market shares above these thresholds are not challenged. In the first contested merger case, the Tribunal declined to dissolve a merger which resulted in a sixty percent market share in the rendering business in Southern Ontario.⁵⁸ Both the Director and the Tribunal will permit market share thresholds that are clearly much higher than levels which would likely be challenged in the United States.

Another distinguishing feature of Canadian merger enforcement compared to that in the United States is that the Director's focus, at least to date, has been on the likelihood of the merged entity being able to exercise unilateral market power, rather than an assessment of the

⁵⁴ COMPETITION ACT § 92. In addition, certain large mergers may be subject to pre-closing notification and waiting period requirements. *Id.* at Part IX. Part IX is similar to the Hart-Scott-Rodino Antitrust Improvements Act in the United States. Whether or not a merger exceeds the compulsory pre-closing notification criteria, all mergers of all sizes are subject to the substantive merger provisions of the Act. For a discussion of the pre-merger notification provisions of the Competition Act, see Goldman & Bodrug, *supra* note 26, at § 10.09. For a discussion of the merger provisions generally, see GOLDMAN & BODRUG, *supra* note 26, at ch. 10. See also PAUL S. CRAMPTON, *MERGERS AND THE COMPETITION ACT* (1990).

⁵⁵ COMPETITION ACT §§ 100 & 104.

⁵⁶ COMPETITION ACT § 92(2).

⁵⁷ MERGER GUIDELINES § 4.2.1.

⁵⁸ Director of Investigation and Research v. Hillsdown Holdings (Can.) Ltd., 41 C.P.R. 289 (3d. 1992).

likelihood of interdependent conduct.⁵⁹ The Canadian de-emphasis of market share and the risk of interdependent conduct reflects a recognition of the relatively concentrated markets in Canada and the need for Canadian firms to achieve internationally competitive economies of scale.

The Competition Act contains a list of factors which the Tribunal may take into account in assessing a merger, including: (1) the impact of foreign competitors; (2) barriers to entry (including tariffs and regulatory control over entry); (3) the degree of effective competition remaining; (4) whether the merger will result in the removal of a vigorous and effective competitor; and (5) the nature and extent of change and innovation in a relevant market.⁶⁰ There is, therefore, specific statutory recognition of innovation as a factor in assessing a merger. Of these factors, foreign competition and the level of barriers to entry appear to have the greatest influence on the Director's decision whether to challenge a merger.⁶¹

In the context of strategic alliances, joint research and collaboration between competitors, the express requirement that the Tribunal consider the nature and extent of change and innovation in the relevant market can be particularly important. For example, the Director has commented that:

[T]echnological change can drastically alter the definition of relevant antitrust markets. There is perhaps no better example of this than the potential effect on competition of the convergence of telephone, cable, broadcast, wireless, and computer technologies. Technological change and innovation can broaden the definition of relevant markets, increase the opportunities for competitive entry, and constrain the exercise of market power by incumbent firms.⁶²

Similarly, the Director's Merger Enforcement Guidelines state that:

[T]he pressures imposed on remaining competitors in a market by the

⁵⁹ MERGER GUIDELINES § 2.2. However, the Tribunal has identified "enhanced ability for tacit collusion" as one of the issues which should be the focus of attention in any merger case. *Director of Investigation and Research v. Imperial Oil Ltd.* CT/89-3, #390 (Comp. Trib.) 54 (Jan. 26, 1990).

⁶⁰ COMPETITION ACT § 93.

⁶¹ See R.S. Khemani & D.M. Shapiro, *An Empirical Analysis of Canadian Merger Policy*, 41 J. INDUSTR. ECON. 161, Table II (June 1993). In addition, the Merger Guidelines indicate that "the assessment of information relating to future entry [§ 93(d)], business failure, and exit [§ 93(b)], or effective remaining competition [§ 93(e)] may, in certain circumstances, provide a sufficient basis, in and of itself, for concluding that a merger is not likely to prevent or lessen competition substantially. That is to say, this conclusion may be arrived at notwithstanding the existence of information that is, on balance, unfavourable to the merger in terms of each of the other factors that may be relevant under section 93." MERGER GUIDELINES § 4.1.

⁶² Addy, *supra* note 5, at 11-12.

nature and extent of dynamic developments in any of these areas [i.e., distribution, service, sales, marketing, packaging, buyer tastes, purchase patterns, firm's structure, the regulatory environment, and the economy as a whole] may be such as to ensure that a material price increase is unlikely to occur or will not be sustainable. This may be especially the case where a merger stimulates or accelerates the change or innovation in question.⁶³

At the same time, consideration of innovation and future changes in the market can give rise to other possible issues. For example, the Director has commented that:

[I]n rapidly changing industries such as telecommunications, it may be less important to focus on the potential effects of a particular transaction on existing levels of competition. Instead, it could perhaps be more helpful to look forward and consider if the transaction would likely 'prevent' future competition that might otherwise come about as a result of technological expansion.⁶⁴

Thus, for example, if in the absence of a proposed joint venture one of the parties would likely have entered the market as an independent competitor, the joint venture may be considered to have prevented competition. We are not, however, aware of the Director having challenged any joint venture or other transaction on that basis to date.

H. The Efficiency Exception for Mergers

The Competition Act expressly provides that the Tribunal may not make an order under the merger provisions if it finds that (1) the gains in efficiency likely to be brought about by the merger will be greater than, and will offset, the effects of any prevention or lessening of competition that is likely to result from the merger, (2) the claimed efficiency gains would not likely be attained if the order enjoining the merger were made, and (3) the alleged efficiency gains would not be brought about by reason only of a redistribution of income. As noted above, efficiencies may not be balanced against anti-competitive consequences of an agreement in the context of the criminal conspiracy provisions. Combined with the fact that affiliated entities cannot conspire with one another,⁶⁵ this can result in the paradoxical situation in which two competitors can fully merge their businesses, without violating the conspiracy provisions or providing grounds for a remedial order under the civil provisions of the Competition Act, in circumstances where less extensive co-operation between them could possibly violate the criminal conspiracy provisions in section 45 of the Act. Thus, the current state

⁶³ MERGER GUIDELINES § 4.9.

⁶⁴ Addy, *supra* note 5, at 9.

⁶⁵ COMPETITION ACT § 45(8).

of the law could encourage parties to merge to avoid criminal liability with respect to collaboration between them and thereby tolerate relatively more anti-competitive action while relatively less anti-competitive conduct is prohibited.⁶⁶

In addition, the Competition Act directs the Tribunal to consider whether such efficiency gains will result in a significant increase in the real value of exports or a significant substitution of domestic products for imported products. Conflicting views have been expressed about how any such an increase in exports or substitution of imports is to be taken into account.⁶⁷ A full panel of the Tribunal is yet to rule on this issue.

In the *Hillsdown* case, the first contested merger proceeding before the Tribunal, both the Director and the acquiror took the position that section 96 directs the Tribunal to balance the gains in efficiency likely to arise from a merger against the misallocation of resources or the “deadweight loss” to society as a whole resulting from any increased prices which the merged firm is able to impose as a result of the merger. This has been characterized as a “total welfare” approach. In the Director’s view, it is not necessary to establish that the efficiency gains will be passed on to the consumer. The Tribunal suggested, however, that section 96 could be read to permit it to take into account a much broader range of effects, including wealth transfers.⁶⁸

After referring to the above-noted purpose clause of the Competition Act, the Tribunal also generally reviewed “the various purposes served by competition law in relation to efficiency gains” and commented that:

[O]ne traditional purpose has been to protect the consumer from being charged supra-competitive prices. While one can argue that this is insignificant from the point of view of loss to the economy as a whole, . . . there is a powerful political argument for preventing such accretions of wealth at the consumer’s expense. Another purpose which has traditionally been seen as served by competition law is to encourage the dispersal of power and the distribution of wealth A third objective of competition law is seen as that of protecting the small firm against more powerful rivals These objectives can run counter to the fourth objective which is that of furthering the efficiency of the economy as a whole.⁶⁹

Against this background, the Tribunal questioned whether it was appropriate to give precedence to the efficiency objective in the purpose

⁶⁶ See Thomas W. Ross, *Proposals for a New Canadian Competition Law on Conspiracy*, 36 ANTITRUST BULL. 851, 852 (1991). It is, however, theoretically possible that the merger itself could be subject to a criminal inquiry.

⁶⁷ See GOLDMAN & BODRUG, *supra* note 26, at § 10.05. See also CRAMPTON, *supra* note 54.

⁶⁸ *Hillsdown Holdings*, *supra* note 58, at 343.

⁶⁹ *Id.* at 338-39.

clause over the goals of providing “competitive prices” and “equitable opportunities for small and medium-sized enterprises,” which are also included in the purpose clause.⁷⁰

Finally, the Tribunal raised “as a question” whether wealth transfers are always neutral and posed the following two examples: (1) a merger of two drug companies where the relevant product is a life-saving drug, and (2) a merger resulting in a dominant firm which charges supra-competitive prices and transferring wealth from Canada. These examples suggest that the Tribunal may be willing to consider a very broad range of possible negative effects of a merger which must be demonstrated to be offset by efficiency gains in order for section 96 to apply.

It has been suggested that the combined effect of the deadweight loss and the neutral wealth transfer resulting from a price increase typically far exceeds any efficiencies which may be brought about by a merger.⁷¹ Thus, the approach of the Tribunal in the *Hillsdown* case could leave the efficiency exception as a largely academic possibility.⁷² Nevertheless, a former Director indicated that the Bureau would continue to apply the approach set forth in the Merger Guidelines⁷³ and the current Director has identified the efficiency exception in the Canadian legislation as one of the factors that contributed to different decisions by the Canadian Bureau and the European Commission in the *deHavilland* case.⁷⁴

I. Joint Ventures

The Competition Act expressly prohibits the Tribunal from making a prohibition or other remedial order under the merger provisions of the Act against certain joint ventures with respect to projects that do not involve the formation of a separate corporation. In order to qualify for this exception, the joint venture must satisfy the following criteria: (1) the project would not take place without the joint venture; (2) the joint venture results in no change in control of any of the parent corporations; (3) the parties agree in writing to the terms of their relation-

⁷⁰ *Id.* at 343.

⁷¹ Alan A. Fisher & Robert H. Lande, *Efficiency Considerations in Merger Enforcement*, CAL. L. REV. 1580, 1644-45 (1983).

⁷² See Paul S. Crampton, *The Efficiency Exception for Mergers: An Assessment of Early Signals from the Competition Tribunal*, 21 CANADIAN BUS. L.J. 371 (1993).

⁷³ Howard I. Wetston, Q.C., Director of Investigation and Research, *Decisions and Developments: Competition Law and Policy, Remarks*, Speech #S-10728/92-07, 5 (June 8, 1992).

⁷⁴ The Director decided not to challenge the proposed acquisition of deHavilland by Aérospatiale/Alenia on the basis that it was not likely to lessen competition substantially in Canada, while the EC blocked the transaction on the basis that it would create a dominant position in the world market for commuter aircraft. See George N. Addy, *International Coordination of Competition Policies*, Paper Delivered to the HWWA-Institut für Wirtschaftsforschung - Hamburg (Oct. 9-11, 1991).

ship, including the contribution of assets; (4) the agreement restricts the range of activities to be carried on by the joint venture and provides for its termination; and (5) the joint venture does not prevent or lessen competition except to the extent reasonably required to complete the joint venture. A former Director has stated that (1) covenants barring the parent firms from engaging in independent research, (2) requirements for the sharing of information about production costs, or (3) restrictions on the licensing of technology not developed through the joint venture could deprive the parties of the benefit of this exception.⁷⁶ In such instances, or others where the joint venture exception does not apply, the merger review provisions of the Competition Act are fully applicable.

The Director's Merger Guidelines do not specifically discuss joint ventures. However, a former Director has elsewhere provided some general guidance on R&D joint ventures by indicating that a pure joint venture with no ancillary restraints limiting independent research, production, marketing of products, or licensing of technology developed by the parents would not generally be considered anti-competitive.⁷⁶ On the other hand, the former Director also expressed the view that a joint venture extending beyond research to encompass joint production and marketing of a new product in an industry characterized by high concentration, barriers to entry, and no foreign competition "might well be considered anti-competitive," although this position could still be tempered by the availability of effective substitutes and the expected market share of the parent firms. However, the former Director added that "any covenants barring independent competition by the parent firms would most likely render the venture unacceptable, unless the venture could be shown to generate very substantial efficiency gains."⁷⁷

There are no publicly reported cases with respect to this joint venture exception and the Bureau has indicated that it is not aware of any use of the joint venture defense.⁷⁸ However, these provisions do not require registration and a similar provision exempts certain joint ventures from the pre-notification requirements of the Competition Act.⁷⁹ Thus, it is possible that private parties may have relied on this exemption without making either a public announcement or a notification to the Bureau. It may also be noted that these provisions do not exempt a joint venture from a challenge under the criminal conspiracy provisions in section 45 of the Competition Act.

⁷⁶ Howard I. Wetston, *The Treatment of Cooperative R&D Activities under the Competition Act*, CONSUMER AND CORPORATE AFFAIRS CANADA, Mar. 4, 1988, at 3-4.

⁷⁶ *Id.* at 8.

⁷⁷ *Id.* at 8-9.

⁷⁸ See Anderson & Khosla, *supra* note 18, at 88.

⁷⁹ COMPETITION ACT § 112.

J. Abuse of Dominant Position

Another type of reviewable conduct described in the abuse of dominant position provisions of the Competition Act could potentially apply to intercompany collaboration in Canada if one or more of the companies involved could be considered to substantially or completely control a type of business in Canada, either on its own or jointly with other parties to the arrangement, and their conduct has a predatory, exclusionary, or disciplinary effect on a competitor. Such an effect might be felt by a competitor that is excluded from the collaborative project. Before the Tribunal can issue an order under this provision, it must also find that such persons have engaged in a practice of anti-competitive acts that have had, or are likely to have, the effect of preventing or lessening competition substantially. This is similar to the test under the merger provisions. Conduct that might qualify as an anti-competitive act includes the adoption of product specifications that are incompatible with products produced by other persons and which are designed to prevent entry by others into, or eliminate others from, a market.

These provisions also recognize the efficiency enhancing objectives of the Act by expressly requiring the Tribunal to consider whether the practice in question is a result of superior competitive performance. The Competition Act also provides that an act engaged in pursuant only to the exercise of any patent or other intellectual or industrial property right is not anti-competitive for these purposes.

The abuse of dominant position provisions should not prevent a group of competitors from collaborating; they may, however, prevent them from adopting practices or terms of participation that, for example, exclude competitors with the result of substantially lessening competition in a market in Canada.

It is also possible that abuse of dominant position issues could arise even in the context of a joint venture between two firms that do not compete with one another if one of the participating firms has a dominant position in a market. For example, one situation that a representative of the DOJ has indicated could raise issues is a requirement that the suppliers of materials to a joint venture refrain from supplying similar materials to manufacturers that compete with the joint venture.⁸⁰

K. Obtaining Certainty with Respect to Specific Proposed Conduct

Particularly outside the context of conspiracy or bid rigging, since the current legislation was passed in 1986, the Director has adopted an overall pro-active approach to compliance in enforcing the Competition Act. Generally, the three individuals who have held the position since

⁸⁰ Gilbert, *supra* note 7, at 8.

May 1986⁸¹ have favoured consultation and co-operation in investigating and resolving issues. Pursuant to the Director's Program of Compliance, private persons may seek advisory opinions on whether the Director believes that certain proposed conduct would provide grounds for him to commence an inquiry.⁸² Such opinions can be obtained on a confidential basis. The precise scope of that confidentiality is, however, subject to some debate.⁸³ Unlike the business review program in the United States, they are not made public by the Bureau. With respect to mergers, the Director generally adopts an "open door" policy and a "fix it first" approach by, for example, being receptive to reasonable proposals to negotiate a solution (such as a partial divestiture) to any concerns about possible anti-competitive effects of a merger. Thus, there may be certain types of proposed collaboration that raise some issues under the Competition Act, but in respect of which the parties can obtain sufficient comfort with respect to the Director's enforcement position to permit them to proceed.

III. INNOVATION AND ANTITRUST POLICY

A. Innovation Markets

A relatively new and potentially significant factor with respect to the application of antitrust law to innovation is the development of the concept of an "innovation market" by the U.S. antitrust authorities.⁸⁴ The concept is discussed in the new Intellectual Property Guidelines issued earlier this month by the DOJ and the FTC.⁸⁵ The U.S. guidelines indicate that the DOJ and the FTC may be prepared to examine the effect of a proposed arrangement on "the development of goods that do not yet exist" or, alternatively, "the development of new or improved goods or processes in geographic markets where there is no actual or likely potential competition in the relevant goods."⁸⁶ The U.S.

⁸¹ Calvin S. Goldman, Q.C., one of the authors of this Article, was the Director from May 1986 until October 1989. His successor, Howard I. Wetston (who is now a Federal Court judge), was the Director until June 1993. The current Director, Mr. George N. Addy, was the Senior Deputy Director of Investigation and Research during Mr. Wetston's tenure and counsel to the Director for the latter part of Mr. Goldman's tenure.

⁸² DIRECTOR OF INVESTIGATION AND RESEARCH, PROGRAM OF COMPLIANCE, INFORMATION BULLETIN No. 3 (Hull, Quebec: Supply and Services Canada, 1993).

⁸³ See DIRECTOR OF INVESTIGATION AND RESEARCH, COMPETITION ACT, THE DRAFT INFORMATION BULLETIN ON CONFIDENTIALITY OF INFORMATION UNDER THE COMPETITION ACT (July 22, 1994); Calvin S. Goldman, Q.C. & Joel T. Kissack, *Joint Sovereign Criminal Investigations: U.S. and Foreign Governments - Can They Really Do That? A Canadian Perspective*, Paper Prepared for the Criminal Antitrust Law and Procedure Workshop, American Bar Association Section of Antitrust Law, Dallas, Texas (Feb. 23-24, 1995).

⁸⁴ See discussion *supra* notes 6-7.

⁸⁵ DEPT. OF JUSTICE AND FEDERAL TRADE COMMISSION, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY § 3.2.3 (Apr. 6, 1995).

⁸⁶ *Id.*

authorities have, in essence, indicated a willingness to consider that relevant antitrust markets may exist for research and development, and that mergers of firms with specialized assets or characteristics could lessen competition in a market for research and development.

The U.S. guidelines suggest that a firm may be considered to have market power with respect to the relevant research and development comprising an innovation market if it has the ability to retard the pace of research and development. However, the U.S. guidelines also establish an antitrust "safety zone" and state that if the arrangements do not involve a *per se* offense and, in addition to the parties to the joint venture (taken collectively), at least four other independently controlled entities possess comparable capabilities and incentives to undertake R&D of the relevant product or other products that would be close substitutes, the U.S. agencies would not likely challenge the joint venture.⁸⁷

One of the bases for the DOJ's challenge to a proposed acquisition of the Allison Division of General Motors by ZF Friedrichshafen (ZF) was the alleged likely adverse effects on competition in a worldwide innovation market for the design and development of new and improved heavy-duty transmissions for trucks and buses.⁸⁸ The DOJ apparently had concerns in this regard even if General Motors and ZF were neither actual nor likely potential competitors for automatic transmissions for large trucks and buses in the United States. The elimination of ZF's separate research and development activities was considered anti-competitive even if ZF were not itself likely to enter the U.S. market with any product it developed.⁸⁹

The FTC has also recently challenged mergers relating to research or innovation markets where (1) two out of only three pharmaceutical companies working on a particular type of vaccine proposed to merge⁹⁰ and (2) a dominant supplier of a particular type of medical implant product acquired a firm that had an exclusive licensing contract with the Mayo Clinic to develop and sell next-generation implant products that were at the clinical trial phase, even though the acquired entity did not currently have any such product.⁹¹ Finally, in *Shell-Montedison*, the FTC entered into a proposed consent order regarding a joint venture that merged the worldwide polypropylene businesses of the two parties, including their production, R&D, and licensing technology operations. The U.S. subsidiary of one of the parties was excluded from the joint venture, but the FTC complaint alleged that because of its parent's participation in the joint venture, the subsidiary

⁸⁷ *Id.* at ex. 4 & § 4.3.

⁸⁸ Gilbert, *supra* note 7, at 5-6.

⁸⁹ *Id.*

⁹⁰ American Home Products Corp., C-3557 (Feb. 14, 1994).

⁹¹ Wright Medical Technology, Inc., C-3564 (Mar. 23, 1995).

would no longer have sufficient incentive to compete with respect to R&D and licensing of polypropylene technology. Even the parties' proposal to exclude the parent's innovation and technology licensing businesses from the joint venture was not sufficient to satisfy the FTC and the proposed consent order requires divestiture by the parent company of an integrated polypropylene company sufficient to support continued research and development in polypropylene technology and to be a credible licensor of technology.⁹²

An innovation market is a novel concept that can be expected to generate significant discussion in legal and academic circles. In the meantime, while the Canadian antitrust authorities have not yet expressed any views on the U.S. intellectual property guidelines or the issues they raise in this regard, the Canadian authorities closely watch developments in the United States and undoubtedly have had and will continue to have discussions with their U.S. counterparts concerning their approach to this concept. It also may be noted that while the concept of innovation markets has been developed in the context of mergers, in theory, there would appear to be no basis to preclude its possible application in the context of the conspiracy provisions of the Act.

The Canadian Merger Guidelines may go some way to anticipating innovation markets when they state that:

[I]t is . . . important to assess the extent to which a merger is likely to facilitate the exercise of market power by impeding the process of change and innovation. This can occur, for example, where the introduction of new products, processes, marketing approaches, aggressive R&D initiatives or business methods, etc., is hindered or delayed by a merger which eliminates a new and innovative firm that presents a serious threat to incumbent firms.⁹³

Consideration of innovation markets may require a shift in the Bureau's focus on the price effects of an agreement or a merger, both in assessing the effects of certain conduct⁹⁴ and in its approach to market definition.⁹⁵

However, issues arise with respect to whether the assertion of possible innovation markets may be characterized as dealing with speculative possible outcomes concerning products that do not even currently exist. As suggested by the Merger Guidelines' above-noted reference to innovative firms that represent a "serious threat" and the suggestion

⁹² Shell-Montedison, File no. 941 0043 (Jan. 11, 1995). See also the discussion of this case in DeSanti, *supra* note 6, at 10-11.

⁹³ MERGER GUIDELINES § 4.9.

⁹⁴ See, e.g., MERGER GUIDELINES § 2.1 which state that "[i]n evaluating whether the market power of the merging parties is likely to be greater than if the merger does not proceed, the focus is normally on the price dimension of competition."

⁹⁵ See, e.g., MERGER GUIDELINES § 3.1 adoption of the "hypothetical monopolist" test.

elsewhere in the Guidelines that strong evidence of a prior intent to enter *de novo* would be required before the Director would challenge a conglomerate merger on the basis of concerns about prevention of competition,⁹⁶ it may be difficult for the Bureau to raise concerns about the effects of a merger or other conduct on an "innovation market" to a level that could satisfy either the civil standard of proof with respect to a likely prevention or lessening of competition or a criminal standard of proof with regard to an undue lessening of competition.

B. Policy Considerations and Recommendations

In the 1995 draft information bulletin on strategic alliances, the Director has tried to provide additional guidance to business people regarding the criteria under which information sharing and other cooperative arrangements may or may not give rise to inquiries under the Competition Act. The changes made from the first draft of the bulletin provide more helpful guidance of the types of arrangements which business people can consider without risk of offending the conspiracy provisions of the Act. However, even though the Director should be applauded for his efforts to provide this guidance, concerns remain that exchanges of information which may enhance innovation and efficiency may still be constrained because of the serious risks to individuals and corporations in the event that any such exchanges do cause the Director to commence an inquiry under the Act and possibly lead to criminal prosecution. The fact is that there are still many grey areas in section 45 of the Act and the enforcement policy of the Director in any given instance. In other words, leaving aside exchanges of present or future pricing information or other clearly sensitive competitive information pertaining to customers, bidding programs, or the like, numerous situations can arise where, in the absence of jurisprudence or specific policy guidance from the Director, some risk of an inquiry under the criminal provisions of the Competition Act remains. For example, exchanges of past cost data from which pricing patterns may be inferred, can, in certain circumstances, particularly as between significant competitors in Canada, give rise to a number of questions as to both the application of section 45 and the Director's enforcement policy, even though it is not in the same category as exchanging proposed price lists.

To date, there have been no convictions under the Competition Act involving conduct amounting to nothing more than an agreement

⁹⁶ *Id.* at § 4.12. "In general, conglomerate mergers can only give rise to concerns under the Act where it can be demonstrated that, in absence of the merger, one of the merging parties would likely have entered the market *de novo* . . . Before concluding that *de novo* entry would likely have occurred in absence of the merger, the Director generally requires objectively verifiable information that clearly supports this proposition, e.g., internal documents that pre-date the merger, recent initiatives by the firm to contest the market, an application for regulatory approval, or the registration of a patent." *Id.*

to exchange information;⁹⁷ whenever a conviction has been entered, the court also found that the accused had engaged in other behaviour, such as agreeing to fix prices.⁹⁸ The Deputy Director of the Criminal Matters Branch of the Bureau has provided some additional guidance on when information exchanges among industry participants may breach the conspiracy provisions of the Competition Act. He stated that the Bureau will consider the structure of the market, whether the parties to the agreement have engaged in additional conduct that might suggest the existence of an anti-competitive goal, and the nature of the information exchanged.⁹⁹ Once again, although the Bureau has made efforts to provide specific guidance, the examples given offer relatively narrow latitude for procompetitive information exchanges designed to achieve greater efficiency and innovation by entities in a market. Similarly, the 1995 draft information bulletin on strategic alliances states that:

[G]enerally, the Bureau will examine alliances that involve the future acquisition of control as mergers, unless the acquisition of control is revealed to be a sham. Where there is evidence of a possible agreement in violation of the conspiracy provisions arising from an alliance or discussion related to a prospective strategic alliance, the Director will launch a criminal investigation. Factors which bear on this decision include evidence of an anti-competitive objective or intent, covert or fraudulent behaviour, the nature of the evidence and whether there is a need for deterrence through criminal remedies.¹⁰⁰

The qualifications with regard to a possible agreement in violation of the conspiracy provisions, any anti-competitive “objective or intent,” and the need for deterrence may diminish the comfort that a business person may take from this passage. Indeed, in a recent interview given by the Director, he expressed an unwillingness to define any numerical market share safe harbor for avoiding issues of undue influence under the Canadian conspiracy provisions.¹⁰¹ In contrast, the U.S. antitrust authorities have been prepared to make a more definitive public statement of their policy with respect to electing to proceed on either a civil or

⁹⁷ See Crampton, *supra* note 1.

⁹⁸ *Id.* at 11.

⁹⁹ See Harry Chandler, *Competition Law Issues in the Upstream Oil and Gas Industry*, 31 ALTA. L.R. 72, 81 (1993). In that paper, the Deputy Director offered the following suggestions to avoid coming into conflict with the Competition Act: (1) the parties should ensure that information exchanges are of a generalized nature and non-company specific; (2) individual firms should be free to determine which policies to follow on their own; (3) information should be based on historical data with no indication of future prices or trading terms; (4) parties should avoid any policing to coerce members to follow association guidelines; and (5) where there is a collection of data from industry participants, they should be collected by an independent firm, and the collection of the data should ensure that the anonymity of members is preserved. *Id.*

¹⁰⁰ DRAFT INFORMATION BULLETIN, *supra* note 43, at 11.

¹⁰¹ Interview with George N. Addy, Director of Investigation and Research, Canadian Bureau of Competition Policy 9 ANTITRUST 6, 7-8 (Spr. 1995).

criminal basis:

[V]iolations of the Sherman Act may be prosecuted as civil or criminal offenses. Conduct that the Department prosecutes criminally is limited to traditional *per se* offences of the law, which typically involve price-fixing, customer allocation, bid-rigging or their cartel activities that would also violations of the law in many countries.¹⁰²

Because of the historical criminal law limitations of Canadian competition law, the provision which governs information exchanges between or among competitors has remained in the criminal law arena for over 100 years. However, since a 1988 decision of the Supreme Court of Canada that affirmed the ability of the federal government to enact competition legislation for non-criminal trade and commerce purposes,¹⁰³ the federal Parliament has latitude to amend the conspiracy provisions to allow for broader types of information exchanges which ought not to raise criminal issues but may be subject to civil reviewable provisions under the Competition Act. In fact, Canada is now virtually alone in its use of a criminal law provision without offsetting efficiency considerations as the governing law in regard to communications between competitors. Even in the United States, there is greater latitude in this area given the ability of the courts to evaluate certain kinds of non-*per se* exchanges under the rule of reason. While small Canadian firms may have greater latitude under the Canadian law as long as they do not possess market power, if they compete in markets that include the United States, they may nevertheless be subject to the same *per se* restrictions under U.S. law. On the other hand, Canadian firms that may collectively possess market power in one or more markets can find themselves at a competitive disadvantage to U.S. firms in relation to possible exchanges between domestic competitors of information of a non-*per se* nature.

One of the most comprehensive analyses of this Canadian issue is contained in a paper published by Presley Warner and Michael Trebilcock.¹⁰⁴ In that paper, the authors state that:

[T]he current prohibition [in section 45] is underinclusive because it can allow manifestly anti-competitive arrangements to escape condemnation. We believe that some horizontal arrangements, such as naked price-fixing and market sharing arrangements must be deterred with criminal sanctions. But the current prohibition, which requires the Crown to prove on a criminal burden of proof that an arrangement has lessened competition 'unduly', can allow price-fixers to escape conviction. . . . At the same time, the current prohibition is

¹⁰² UNITED STATES DEPT. OF JUSTICE AND FEDERAL TRADE COMMISSION, ANTITRUST ENFORCEMENT GUIDELINES FOR INTERNATIONAL OPERATIONS § 2.1 (Apr. 1995).

¹⁰³ City National Leasing Ltd. v. General Motors of Canada Ltd., 1 S.C.R. 641 (1989).

¹⁰⁴ Warner & Trebilcock, *supra* note 29.

overinclusive because it subjects all horizontal arrangements to criminal prohibitions and casts a shadow over many arrangements that may potentially increase welfare. Apart from the obvious price-fixing case, the welfare effects of many horizontal arrangements are ambiguous, and arrangements with ambiguous welfare effects should not be deterred and do not require criminal sanctions.¹⁰⁵

The authors advocate that the Tribunal is better equipped to analyze the welfare effects of ambiguous arrangements in comparison to the criminal courts in Canada. They propose a new criminal prohibition against covert horizontal arrangements, as opposed to targeting “naked” price-fixing arrangements, which have or are likely to have an effect on fixing the price of goods or services supplied by the parties to the arrangement, and which is not the subject of a notification to the Bureau prior to the time at which the arrangement takes effect or within a specified time thereafter. The authors advocate that the criminal prohibition be complemented with a civil review provision which would involve the Tribunal assessing whether notified arrangements are likely to lessen competition substantially in the same manner that currently applies to mergers.

In another paper delivered last year by Timothy Kennish and Thomas Ross, the authors state that there are many kinds of agreements which have been recognized for some time as not being anti-competitive even if entered into by actual or potential competitors.¹⁰⁶ Examples include agreements not to compete for a specific period of time which are ancillary to the sale of a business, and agreements on product standards. Kennish and Ross note that there has been a rapid increase in various kinds of strategic alliances in recent years, including arrangements between firms pertaining to R&D, production and distribution joint ventures, sharing of facilities, specialization agreements and licensing of production or distribution. The authors point out that even in the United States, in recent years, agreements between competitors are being re-examined in terms of whether they give rise to *per se* illegality, apart from agreements that pertain to specific price fixing or market allocation.¹⁰⁷

¹⁰⁵ *Id.* at 690.

¹⁰⁶ Timothy Kennish & Thomas Ross, *Toward a New Canadian Approach to Agreements Between Competitors* prepared for the University of Toronto Law and Economics Programme, Selected Issues in the Economics of Policy, (June 20, 1994). The authors also state that: “[t]here is widespread agreement that garden-variety price fixing, bid-rigging and market allocation schemes impose significant social costs and should be prohibited. Indeed, the aggressive approach toward such agreements taken under U.S. antitrust law is applauded even by those associated with the Chicago school.” *Id.* at 5 (citing ROBERT BORK, *THE ANTITRUST PARADOX* 273 (1976) & RICHARD POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 39 (1976)).

¹⁰⁷ See *Broadcast Music Inc. v. Columbia Broadcasting System*, 441 U.S. 1 (1979), and *National Collegiate Athletic Association v. Board of Regents of The University of Oklahoma*, 468 U.S. 85 (1984).

In light of the foregoing, Kennish and Ross advocate two types of reform that would enable the Canadian law to adopt a more realistic approach to the evaluation of horizontal agreements, including information exchanges and strategic alliances. One approach would involve interpreting the word "unduly" in section 45 as permitting consideration of the benefits of the agreement; however, any such interpretation would run directly contrary to the *PANS* case (discussed above) and would therefore require legislative amendment. A second approach would involve legislative reform of section 45 to create a civil review provision governing all types of agreements apart from naked restraints which would be *per se* illegal (i.e., the word "unduly" would be deleted from section 45 with respect to these types of agreements). The authors propose that all other kinds of agreements which have at least some beneficial features be made subject to review by the Tribunal in a manner similar to that currently available for mergers, including consideration of efficiencies.¹⁰⁸

The options proposed in the papers discussed above are worth serious consideration given the potential overbreadth of Canada's current criminal conspiracy law. Even with the specific guidance offered in the draft information bulletin on strategic alliances, it is doubtful that business persons will find sufficient comfort to allow the kinds of procompetitive information exchanges to occur in a manner that could be achieved without facing the concurrent risk of serious criminal proceedings. The fact will remain that, in the absence of legislative reform or at least clearer statements of enforcement policy with respect to the exercise of prosecutorial discretion to proceed under the criminal or civil provisions of the Competition Act, a broad array of strategic alliances and information exchanges may still be subject to the risk of an inquiry under the criminal provisions of the Canadian legislation. This situation fails to ensure that Canada is obtaining the maximum innovative development and growth from its firms while still protecting against anti-competitive economic costs. In the result, Canadian firms may be placed at a competitive disadvantage. Businesses in Canada do not have the flexibility that exists under the rule of reason in U.S. law, nor do they have the latitude to proceed with alternative notification or clearance processes which exist in other jurisdictions.¹⁰⁹ In this respect, the compatibility of a country's competition laws becomes increasingly important in a free trade environment. While free trade should not dictate that competition or other laws be identical, as markets are inte-

¹⁰⁸ Kennish and Ross also advocate a statutory amendment to provide that where an arrangement constitutes a "merger" for the purposes of section 91 (i.e., it involves an acquisition of control of a business or a significant interest by one party in the business of another), it should be exempt from challenge under § 45. Kennish & Ross, *supra* note 106, at 41.

¹⁰⁹ See Warner & Trebilcock, *supra* note 29, at 700-07, where the authors discuss the E.C. and U.K. regimes.

grated, differences in competition laws can create competitive disadvantages.

The Canadian government should consider the experience of the United States and other jurisdictions which take efficiency and other procompetitive aspects of inter-firm collaboration into account in this context. This is especially so given the fact that the United States has the most vigorously enforced antitrust laws among OECD member countries. As the Canadian government begins to consider over the next year possible amendments to the Competition Act,¹¹⁰ it makes sense to re-examine whether it is now time to provide for a balancing process for various kinds of strategic alliances and information exchanges which are not likely to bring about clear costs to consumers and industries in Canada.¹¹¹

Our specific proposal is that a strict standard ought to apply in regard to covert agreements between competitors with respect to present or future prices, customer allocations, market allocations, bidding terms or possibly other analogous matters. Legislative reform in this area might call for elimination of the "unduly" test in section 45. The exact scope of this strict standard should be examined carefully by representatives of the Bureau and the private sector in an effective consultation process. At the same time, in our view, an agreement should not be prohibited solely because it is covert unless it relates to one of the seriously anti-competitive categories. Two competitors may not want to announce publicly that they are exchanging past quality control procedures, for example, and this should not be problematic. In our view,

¹¹⁰ Addy, *supra* note 44.

¹¹¹ In a paper delivered to the Canada-U.S. Law Institute in 1993 by Goldman & Kissack, *supra* note 5, at 123-26, the authors advocated reforming the conspiracy provisions to more clearly address information exchanges among competitors, especially for benchmarking purposes. The authors pointed to the legislation's willingness to engage in a balancing process in assessing mergers, joint ventures and in specialization agreements while not allowing for the same balancing process in respect of other kinds of horizontal arrangements which are governed by the conspiracy provision. The question continues to exist whether this distinction is still justified. It may also be noted that, in December 1993, one of the authors of this paper, C.S. Goldman, raised certain analogous issues on behalf of the Business & Advisory Industry Committee of the OECD at an OECD Competition Law and Policy Committee roundtable discussion on horizontal arrangements. On behalf of BIAC, he indicated that it is important to try to ensure that criminal or other administrative law restraints on horizontal agreements in OECD countries do not go so far as to preclude certain kinds of procompetitive industry co-operation designed to attain cost and quality control by means of processes such as benchmarking. He indicated that these kinds of exchanges as well as sharing of technological advances and innovation can lead industries to become more efficient and ultimately more competitive, provided that these exchanges do not involve certain types of information which will lead to anti-competitive results. He suggested that it would be useful if the Competition Law and Policy Committee of the OECD were to study this issue and perhaps develop a recommendation to assist in articulating a set of standards that would allow greater exchanges of certain kinds of information among competitors where the efficiency enhancing potential is high and the risk of competitive injury is correspondingly low. Thus far, the OECD has not commenced a study of this issue, but it remains to be seen whether it will do so in the future.

other types of agreements between competitors which do not relate to one of these categories ought to be subject to review by the Tribunal, on application by the Director, in a manner analogous to the test for mergers. This would incorporate a determination of whether efficiency gains may offset any substantial lessening or prevention of competition. In the event of an overt agreement which relates to one of the serious categories and raises significant competition issues, the Director could seek an injunction from the Tribunal, as he is currently empowered to do in respect of the civil provisions of the Competition Act. Further, the consultative assessment process should also consider not only the availability of interim injunctions but also whether private parties, in addition to the Director, should have standing to seek injunctions or damages in respect of both the criminal and civil provisions of the Act.

The Director recently announced the establishment of an Amendments Unit within the Bureau to consider recommending amendments to the Competition Act.¹¹² Although he did not identify any of the matters discussed in this Article as areas for amendment that the Bureau is assessing at this time, the formation of the Amendments Unit may present an opportunity for interested parties to advocate amendments to the conspiracy provisions of the Competition Act in order to allow it to operate in a manner which will more effectively protect both competition and efficiency enhancing activities of firms in Canada. While certain types of amendments to other provisions of the Competition Act may be accomplished in a shorter period, significant changes to section 45 are likely to take more time; however, the consultative process can be commenced in the near future.

IV. CONCLUSION

The Competition Act incorporates principles that suggest there is room for the co-existence of antitrust law and innovation. These principles are reflected in (1) the R&D "exception" to the conspiracy provisions, (2) the specialization agreement provisions, (3) the joint venture provisions, (4) the efficiency exception to the merger provisions, and (5) the purpose clause of the Act. Further, the concepts of market definition and "undue" or "substantial" lessening of competition, and the possibility of adopting a dynamic rather than a static competitive market analysis, permit a significant degree of flexibility in applying the Competition Act in an efficiency enhancing manner. The Director also can encourage efficiency enhancing collaboration by examining certain types of strategic alliances under the civil merger or abuse of dominance provisions, rather than the criminal conspiracy provisions of the Competition Act. Also, by continuing to make available to business persons an effective program of compliance and advisory opinions, the

¹¹² Addy, *supra* note 44, at 10.

Director can assist Canadian firms in pursuing efficiency enhancing strategic alliances.

However, real constraints on potential innovation, the achievement of efficiencies and other pro-competitive aspects of cooperation with competitors continue to exist under the conspiracy provisions of the Competition Act. As reflected in the draft information bulletins on strategic alliances, the Director's approach to the conspiracy provisions does not give a great deal of latitude to efficiency and innovation justifications. The analysis of the Supreme Court in the *PANS* case and the discussion in the draft strategic alliance bulletin may inhibit certain types of efficiency enhancing collaborations and place Canadian firms at a competitive disadvantage. At the same time, in the context of merger reviews, the Director has recognized the importance of assessing the dynamics of changing markets, particularly in the telecommunications area. In this respect, antitrust policy in Canada ought not to be saddled with a static approach in any area, including information exchanges and other kinds of potentially pro-competitive understandings between competitors. It is now time to undertake serious reconsideration of the scope of Canada's criminal prohibition in this area of the law.

