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DYNAMIC CHANGE AND ACCOUNTABILITY IN A CANADIAN MARKET ECONOMY: SUMMARY AND CRITIQUE

By W. T. STANBURY*

A. INTRODUCTION

The purpose of this paper is to provide both a useful summary and a critique of the recent report by Messrs. Skeoch and McDonald to the Department of Consumer and Corporate Affairs.¹

Their report provided a series of policy proposals for the Stage II amendments to the *Combines Investigation Act*² which were introduced into Parliament in March 1977. Dr. Skeoch, Mr. McDonald and a committee of three, two senior business executives and a lawyer associated with small business, were asked to deal with mergers, monopolization, price discrimination, loss-leader selling, rationalization and export agreements and interlocking directorates. They have reported on these and other matters, including basing-point pricing, intellectual and industrial property and, in much more detail, on the

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¹ Lawrence A. Skeoch with Bruce C. McDonald (in consultation with Michel Belanger, Reuben M. Bromstein, and William O. Twaits), *Dynamic Change and Accountability in a Canadian Market Economy* (Ottawa: Minister of Supply and Services, Canada, 1976) 361 pp.

² R.S.C. 1970, c. C-23, as amended by c. 10 (1st Supp.); c. 10 (2nd Supp.); 1974-75-76, c. 76. See, *Proposals for a New Competition Policy for Canada* (Ottawa: Consumer and Corporate Affairs, 1977).

administrative and adjudicative details relating to their proposed amendments to the *Combines Investigation Act*.

1. *Some Historical Perspective*

Dynamic Change and Accountability in a Canadian Market Economy represents a major policy input into the process of reforming Canada's competition policy. This process began in July of 1966 when the Government of Canada requested the Economic Council of Canada to prepare a report on, among other things, "combines, mergers, monopolies and restraint of trade."³ Two years later, the Council published its *Interim Report on Competition Policy*,⁴ in which it proposed major revisions to the *Combines Investigation Act*. On June 29, 1971 the Government introduced Bill C-256, the *Competition Act*, in the House of Commons and it was given first reading. It was a large and complex bill, containing some 103 sections and was 106 pages long.⁵

Compared to the existing laws on restraint of trade, the *Competition Act* represented a large discontinuous change in the environment of Canadian businessmen. Their reaction was predominantly negative. Five months after the Act was introduced, the *Financial Post* observed, "[n]ot since the early days of the great tax debate has a single government proposal aroused the ire of the business community to the extent the Competition Act has."⁶ Early in 1972, it was announced that a revised bill would be re-introduced and that it would incorporate substantial changes in light of business' representations. In the House of Commons on July 18, 1973 Herb Gray, the fourth Minister of Consumer and Corporate Affairs in five and one-half years, announced that Canada's new competition policy would be implemented in stages. On November 7, 1973 a series of amendments to the *Combines Investigation Act* was given first reading in the House of Commons. This bill (C-227, later C-7 and C-2) was described as Stage I⁷ and became law effective January 1, 1976.⁸

The Stage I amendments include a number of important changes to the Act.⁹ For the first time since 1935, services are to come within the purview

³ Press Release, Privy Council Office, July 22, 1966.

⁴ Economic Council of Canada, *Interim Report on Competition Policy* (Ottawa: Queen's Printer, 1969) 244 pp.

⁵ The bill was accompanied by a 137 page volume entitled, *The Competition Act: Explanatory Notes* (Ottawa: Department of Consumer and Corporate Affairs, 1971) (mimeo).

⁶ *The Financial Post*, December 11, 1971 at 1.

⁷ The original bill is contained in, *Proposals for a New Competition Policy for Canada, First Stage* (Ottawa: Department of Consumer and Corporate Affairs, 1973).

⁸ Section 32 of the new *Combines Investigation Act* became applicable to services on July 1, 1976.

⁹ The 1975 amendments are discussed in some detail in: W.T. Stanbury, ed., *Papers on the 1975 Amendments to the Combines Investigation Act* (Vancouver: Faculty of Commerce and Business Administration, University of British Columbia, 1976); Gordon Kaiser, *The New Competition Law: Stage One* (1976), 1 *Canadian Business Law Journal* 147; *Background Papers: Stage 1, Competition Policy*, Bureau of Competition Policy (Ottawa: Department of Consumer and Corporate Affairs, 1976) (mimeo). A short but useful description is contained in *Report of the Director of Investigation and Research, Combines Investigation Act for the year ended March 31, 1976* (Ottawa: Minister of Supply and Services, Canada, 1976) at 9-14.

of the Act.¹⁰ The amendments grant a civil jurisdiction to the Restrictive Trade Practices Commission (RTPC) to review certain trade practices which may be desirable or undesirable depending on the facts in specific cases. The RTPC is given the power to make remedial orders with respect to consignment selling, exclusive dealing, tied selling, refusal to deal and market restrictions. The RTPC has also been given jurisdiction, where Canadian firms are adversely affected, to review the implementation of foreign judgments or orders, the refusal to supply by foreign suppliers, and the implementation of foreign laws considered binding on a Canadian subsidiary by its foreign parent.

The amendments provide for the institution of private civil suits for single damages in respect of the Act's criminal offences and in respect of violations of the RTPC's orders or a court's order. While the term "unduly" remains in the conspiracy section, a new section prevents the application of the "virtual monopoly doctrine." Bid-rigging is made illegal *per se*, unless the arrangement is made known to the person requesting the bids or tenders.

The most extensive set of amendments in Stage I relates to misleading advertising and deceptive trade practices. All representations, in any form whatsoever, that are false or misleading in a material respect are prohibited, substantially broadening the section. Tests and testimonials must be accurate and the permission to use them must be obtained. Where double-ticketing occurs, the product must be offered for sale at the lower price. Inducements to participate in a pyramid or referral selling scheme are prohibited, except for those that are registered in a province in which the inducements are made. Bait and switch selling is prohibited and any product advertised at a bargain price must be available for sale in reasonable quantities. A seller is not liable where he can establish that the non-availability of the product was due to circumstances beyond his control or that a reasonable substitute was offered. Sales of a product by a seller at a price higher than his currently advertised price is prohibited, unless the advertised price is an error and is immediately corrected. Promotional contests must now disclose information on the number and value of prizes and any information relating to the chances of winning a contest that does not select participants or distribute prizes on the basis of skill or on a random basis.

The section on resale price maintenance is also strengthened. It now prohibits any attempt to influence upward or discourage the reduction of the selling or advertised price of an article. A supplier must now make it clear to his customers that any price suggested by him is just that and the customer has no obligations to sell at that price. The refusal to supply provision is broadened to include other forms of discrimination that might be used to induce a supplier's customers to maintain prices. It is also an offence for a customer of a supplier to induce the supplier to refuse to sell to other customers because of their low pricing policy.

B. OVERVIEW OF THE *DYNAMIC CHANGE* REPORT

The main thesis (described modestly as an hypothesis) of the Committee's report is stated as follows:

¹⁰ Since s. 34(1)(a), dealing with price discrimination, retains the word "articles" (rather than "product" which includes services) it does not apply to services.

the role of government policy should be not to direct and manage the economy in detail but to facilitate change and thus release and reinvigorate the dynamic forces that have been responsible for the prodigious economic growth that the market-directed, private enterprise system has demonstrated it is capable of achieving.¹¹

The authors see their policy proposals as those which "will most effectively facilitate long-run dynamic change within the Canadian economy, that will encourage the adoption of real-cost economies, and that will discourage restraints which will result from mere market power rather than superior economic performance."¹²

The report can be properly characterized in terms of the following themes:

1) A Systems View of the Economy

At the outset, Skeoch and McDonald argue that "the market economy involves an organic and historical process that conditions developments over the entire economy";¹³ they repeatedly emphasize "the interconnection of the various elements in the total economy."¹⁴ The authors criticize the element of "hypochondria" and "over-simplification" in recent Canadian economic policy. They assert that, "there is no fundamental analysis of how the problems are inter-related and how the proposed remedies would interact and affect the economic system as a whole."¹⁵ Throughout the report, in assessing the alternatives, they request the policy-maker to "take into account the larger social and economic perspective."¹⁶

2) Emphasis on Facilitating the Process of Change

Skeoch and McDonald wish to "release and reinvigorate the dynamic forces" which they see as the key to economic growth in the context of a private enterprise economy. Beginning with the title of the report, they stress that the objective of competition policy should be to facilitate the process of economic change. However, "[t]he benefits from dynamic change¹⁷ will . . . only materialize in the long run as industry gradually exploits opportunities for economies of scale, for organizational innovations, and for improvements in management efficiency."¹⁸ They believe that the job of the policy-maker is to "encourage the private sector to adopt patterns of conduct that will promote dynamic change and avoid artificial restraints."¹⁹ In particular, "[t]he problem

¹¹ *Supra*, note 1 at 202.

¹² *Id.* at ii.

¹³ *Id.* at 9.

¹⁴ *Id.*

¹⁵ *Id.* at 29.

¹⁶ *Id.* at 324.

¹⁷ Perhaps the linking of the words "dynamic change" has been done for emphasis, but the modifier "dynamic" appears to be redundant. "Dynamic," according to a dictionary, is defined to be "of or pertaining to forces not in equilibrium, or in motion as the result of force" and as "producing or involving change or action."

¹⁸ *Supra*, note 1 at 36.

¹⁹ *Id.* at 23.

is how to facilitate the process of change by policies of general application and at the same time to assist the individual to adjust to the changes that do occur."²⁰

Four years earlier, with respect to the *Competition Act*, Professor Skeoch expressed the same view as that adopted in the report:

[T]he central focus of policy relating to industrial organization should be to promote dynamic change and growth through encouraging flexibility and adaptability in the economy. Such a policy must emphasize not the efficient allocation of existing resources among alternative uses in terms of keeping down costs and profits, but the encouragement of new methods of production and distribution, the development of new institutions for liberating and expanding the growth opportunities in the economy.²¹

The clarion cry seems to be: "Let the market work." As Skeoch and McDonald reiterate in the report, they have "a longer-run outlook based on the encouragement of adaptability and flexibility directed to the achievement of real-cost economies through a market system, and the curbing of artificial restraints, that is, those not based on superior economic performance."²²

3) Minimal Interventionism

The authors may be described as small "c" conservatives with respect to government intervention in the economy. They are reluctant to see the government intervene at all. Alternatively, one can view them as nineteenth century liberals holding that "the government which governs best, governs least." They assert the present validity of Adam Smith's strictures on government that, "governments are inherently inefficient in administration because their agents are paid out of state funds and not out of the proceeds of successful administration."²³ With respect to government intervention, Skeoch and McDonald again use Smith to set the tone of their approach by saying "that state intervention tends to result in large and enduring errors, whereas the errors of free economic enterprise in addition to being more transient . . . and of smaller scale, are likely to neutralize one another."²⁴

The authors provide the counsel of age and experience; such counsel shows a cynical appreciation of the imperfections of men and the institutions through which they wield power. They espouse a "system in which there are checks and balances which limit the opportunities for any individual to make decisions which affect the whole system."²⁵ In particular, "[t]he system should be devised in such a way that extreme views and incompetent individuals have the least possible chance of doing harm."²⁶ Thus, we are

²⁰ *Id.* at 10.

²¹ L. A. Skeoch, "Basic Economic and Policy Considerations," in L. A. Skeoch, ed., *Canadian Competition Policy* (Kingston: Industrial Relations Centre, Queen's University, 1972) at 8.

²² *Supra*, note 1 at 224.

²³ *Id.* at 14.

²⁴ *Id.*

²⁵ *Id.* at 15-16.

²⁶ *Id.* at 17.

offered the dynamic possibilities of the market as a means to achieve both our economic and political goals.

When the government must intervene, Skeoch and McDonald want it to keep a "low profile." Perhaps because they also advocate respect for the systemic view, they see the "need for caution in tinkering with the institutional and organizational structure of the economy."²⁷ The report advocates "a general presumption against government interference in the normal operations of the economy, which extends to mergers and other aspects of competition policy."²⁸ They assert, "[m]arket economies cannot be fine-tuned."²⁹ Consequently, their approach to policy is to "grope forward by means of methods which are as general as possible."³⁰

Skeoch and McDonald see changes in competition policy laws as essentially a burden on business firms. "We should be very clear about the justification before we impose additional burdens on the business community, especially at a time when it is being urged to become more enterprising and productive."³¹ The authors remind us "that improvement is at best slow" and that "we all live under the cold star of scarcity."³² They urge a "balanced" and long-term view of competition policy problems.

The logical extension of both the systemic and intervention-minimizing views is that the policy-maker's role be constrained and that the power to effect public policy be decentralized. This is evident in a number of the report's recommendations. For example, it is recommended that the Director of Investigation and Research *not* be given the power to prosecute criminal cases independently of the Department of Justice. "[C]riminal prosecution itself is so serious that an independent check on the single-minded enthusiasm of the investigators and policy makers might on rare occasion be a useful safeguard."³³ Similarly, the authors propose that the orders of their quasi-judicial tribunal (the National Markets Board) be appealable to the Cabinet. This is advocated in terms of the "need for a safety valve," the necessity for "over-riding coordination of national policies" and the requirement that "raw political questions"³⁴ be ultimately in the hands of elected officials.

C. SUMMARY OF THE REPORT

1. *Merger Policy*

The report endorses what might be called a real-economies theory of mergers rather than one based primarily on capital market opportunities (imperfections), tax considerations and stock market enthusiasm. Skeoch and

²⁷ *Id.* at 8.

²⁸ *Id.* at 307.

²⁹ *Id.* at 300.

³⁰ *Id.* at 17.

³¹ *Id.* at 326.

³² *Id.* at 29.

³³ *Id.* at 319.

³⁴ *Id.* at 314.

McDonald are concerned to understand the relationship between the number and type of mergers and technological variables, marketing policy, the rate of market growth, effects of barriers to entry and changes in costs. While endorsing this most useful analytical approach, they offer no new analysis of their own, and appear to base their policy proposals, at least in part, upon the work of Reuber and Roseman,³⁵ whose analysis concentrated on the period 1945 to 1961.

The authors conclude that "it would appear that the *general* merger movement in Canada has not given rise to any important consequences for the economy."³⁶ This statement is accompanied by a footnote, which cites the following words from the Book of Job: "Who is this that darkeneth counsel by words without knowledge?" Having drawn the conclusion that mergers have not had important consequences for the Canadian economy, they endorse "a more sophisticated analysis" of mergers. They recognize that Canadian data is "seriously inadequate" for determining "the degree to which mergers were affecting the 'structure' of similar industry sub-divisions . . . [or] whether the different countries involved in the comparisons were undergoing a similar cross-sectional merger experience."³⁷ Despite these admissions, Skeoch and McDonald draw a fairly strong conclusion that "a significant proportion of domestic mergers constitute [*sic*] a response to specific functional influences of international reach."³⁸

The report states that the preferred approach to merger policy is "to alter the reaction pattern of the economy so as to promote economic development and dynamic change rather than to attempt to 'fine tune' merger policy in such a way as to sort out comprehensively and with precision the mergers that are undertaken."³⁹ Skeoch and McDonald argue that the jurisprudence derived from the only two contested prosecutions, *R. v. Canadian Breweries Ltd.*⁴⁰ and *R. v. British Columbia Sugar Refining Company Ltd.*,⁴¹ "provides little assistance in formulating merger policy"⁴² because of the "distressing irrelevance"⁴³ of the criteria used by the judges to determine the legality of the mergers.

As the basis for their policy proposals, they state that the thrust of merger policy should be

- (1) to permit the growth of firms (even involving the reduction of the number of firms) based on real-cost economies, including static economies of scale,

³⁵ Grant L. Reuber and Frank Roseman, *The Take-Over of Canadian Firms, 1945-61*, Special Study No. 10, Economic Council of Canada (Ottawa: Queen's Printer, 1969).

³⁶ *Supra*, note 1 at 56.

³⁷ *Id.* at 58.

³⁸ *Id.* at 68.

³⁹ *Id.* at 70.

⁴⁰ *R. v. Canadian Breweries Ltd.*, [1960] O.R. 601; 33 C.R. 1; 126 C.C.C. 133; 34 C.P.R. 179.

⁴¹ *R. v. British Columbia Sugar Refining Co. Ltd.* (1960), 32 W.W.R. 577; 129 C.C.C. 7; (1962), 38 C.P.R. 177; 36 C.R. 32.

⁴² *Supra*, note 1 at 70.

⁴³ *Id.* at 71.

- but emphasizing those advantages relating to technological progress, product variation and organizational change; and
- (2) to discourage expansion of firm size (or the maintenance of firm size against new entrants) which results from the exploitation of artificial restraints.⁴⁴

Implementation of their policy involves a four-stage process of evaluation. The first stage is the identification of "significant" mergers. The central element in analyzing the impact of a merger, the report asserts, "is the identification of the pertinent market within which it occurs."⁴⁵ This can only be done in the context of the specific problem under consideration. However, "[t]he basic principle is to take full account of competition among products and of the position of buyers as well as sellers."⁴⁶

The second main element in the identification of significant mergers is the analysis of the structure of the market for the purpose of assessing the degree of market power possessed by the merging firms.⁴⁷ Skeoch and McDonald emphasize that in addition to the usual elements of market structure (concentration, product differentiation, barriers to entry, the rate of growth of demand, the price elasticity of demand and the ratio of fixed to variable costs) it is important to assess the "extent to which dynamic change is occurring in the market."⁴⁸ As a "first approximation" in determining the significance of a merger, consideration should be given to barriers to entry, the rate of growth of demand and the nature and extent of dynamic change.

The authors recognize the possibility of a "failing firm" exemption, but also note the prophylactic effect of business failures on the adjustment process. With respect to share of market as a criterion, they assert it is of limited relevance in the small Canadian economy. They do, however, recognize its value in defining minimum levels of significance.

The second stage in the public policy analysis of mergers (assuming that they are economically significant) is the assessment of the primary consequences of the merger. These refer to the "probable impact of the merger in strengthening or creating artificial restraints."⁴⁹ Such restraints include the possession of scarce natural resources, patents or licences or contracts relating to some specific technology, discriminatory vertical reciprocal buying/selling arrangements and discriminatory arrangements with labour unions. Skeoch and McDonald emphasize that this list or any other cannot be made exhaustive. They also point out that it may be the combination of restraints which results in the adverse impact. In line with their emphasis on competition as a dynamic process, they stress that a proposed merger must not strengthen barriers to entry to the industry or industries involved.

If the analysis of the primary merger consequences is unfavourable to the proposed merger it becomes necessary to assess the secondary consequences

⁴⁴ *Id.* at 72.

⁴⁵ *Id.* at 84.

⁴⁶ *Id.* at 85.

⁴⁷ *Id.* at 86.

⁴⁸ *Id.*

⁴⁹ *Id.* at 88.

of the merger. In this, the third stage of the evaluation process, the analysis is concerned with longer-run considerations. These include barriers to entry, real-cost economies (both in production and in selling and distribution) and factors promoting dynamic change both within and among firms. The report emphasizes that "the analysis would not attempt to establish 'specific actualities' but to forecast and appraise reasonable probabilities."⁵⁰ Where the secondary consequences of the merger offset the disadvantages of the primary consequences, the merger would be approved. If not, the fourth stage in the evaluation process becomes operative.

Stage four involves "examining the possibility of altering the reaction pattern of the industry by changes in the economic environment."⁵¹ Such changes might involve reductions in tariffs, the divestiture of part of the merger firm, the substitution of a joint venture for all or part of the merger, and the licencing of patents. The Director of Investigation and Research would be responsible for negotiating such changes, and any agreement would have to be approved by the proposed National Markets Board.⁵²

The authors defend their four-stage, case-by-case evaluation process by arguing that a non-discretionary approach, incorporating concentration or profit rate criteria, would obscure rather than illuminate the essential issues. For example, they point out that a low profit rate may conceal market power expressed in the form of inefficiency in production and distribution. They also note that reliance on one or two measures of market effectiveness could result in overlooking a combination of secondary factors. In short, they argue, there is no real substitute for informed judgment.

Skeoch and McDonald see the Canadian economy as increasingly integrated in the global economic system. Multinational enterprises "possess either special skills or strong public reputations which can give them an important edge when they attempt to enter a foreign market."⁵³ As a result, they may be able to pay more for local firms than domestic investors. Given their emphasis on "dynamic change," they are obviously concerned with the impact of foreign investment in Canada on research and development and the process of innovation. They assert:

The Canadian view apparently holds that foreign-owned subsidiaries do little research in Canada and, as a result, discourage the development of a research and development "industry" in Canada, and, in consequence, make more difficult the growth of a sophisticated manufacturing sector here.⁵⁴

They argue that there is not much evidence to support such a view and that government efforts to encourage R & D have been both expensive and ineffective. Skeoch and McDonald argue at some length that the conclusion of a U.K. study, to the effect that the alternative to developing an independent

⁵⁰ *Id.* at 89.

⁵¹ *Id.*

⁵² The nature and functions of the National Markets Board are discussed below. See text, *infra*, following note 124.

⁵³ *Supra*, note 1 at 97.

⁵⁴ *Id.* at 100.

European technological community is economic decline and domination by the U.S., "is wrong, and misleadingly over-simplified."⁵⁵ They strongly imply that the same is true for Canada. The public policy issue, as they see it, is "that in manufacturing and high-technology production the new-product oligopoly will continue to be the most important market form in the foreseeable future."⁵⁶ The developments which will influence the manufacturing and high technology industries will be international — unless inhibited by government intervention. What is a good merger policy in this context? It "involves the relevant agency in predicting the longer-run effects of certain limitations on (or extensions of) the firm's planned production and marketing designs within a non-static framework."⁵⁷

The essence of the correct policy, say the authors, is to "avoid detailed tinkering with elements of structure and behaviour and should rely *primarily* on eliminating artificial restraints and on maintaining pressure for adjustment from as many directions as is feasible. . . ."⁵⁸

The report is sharply critical of the evaluation of mergers by the Foreign Investment Review Agency. As the authors see it, FIRA has "no well-developed theory . . . of industrial and market behaviour and performance in the domestic-international context to guide and illuminate decisions for the private sector and to test the validity of decisions made by the enforcement agency."⁵⁹ They see FIRA's stated criteria as "unduly concerned with short-run considerations" and as taking the form of *ad hoc* intervention in matters of detail.⁶⁰ In addition, they note, the ten criteria are "riddled with ambiguity," especially those specifying "improved productivity and industrial efficiency," "innovation" and "enhance[d] technological development."⁶¹ Skeoch and McDonald can see no merit in handling inward foreign mergers any differently than domestic mergers. They strongly recommend that if their proposals with respect to domestic mergers are adopted, "the same method should apply to all forms of inward foreign mergers, partial mergers and quasi-mergers."⁶²

2. *Monopoly and the Abuse of Monopoly Power*

Skeoch and McDonald begin by pointing out that the existence of monopoly and the exercise of monopoly power are not recent phenomena; nor are they associated with bigness in absolute terms. They find much to agree with in the statement that all levels of government have been the creators and protectors of monopoly: "it would . . . have to be conceded that government-sponsored restraints have accounted for many of the worst examples

⁵⁵ *Id.* at 102.

⁵⁶ *Id.* at 105.

⁵⁷ *Id.*

⁵⁸ *Id.* at 105-06.

⁵⁹ *Id.* at 106.

⁶⁰ *Id.* at 108.

⁶¹ *Id.* at 111.

⁶² *Id.* at 112.

in the rogues' gallery of restrictive practices."⁶³ The report states that monopoly elements in the private sector can be kept within reasonable limits by "appropriate policies with respect to new mergers, effective enforcement of policies to discourage abuse of monopoly power, and the development of policies to promote change based on real-cost economics."⁶⁴ Skeoch and McDonald go on to imply that the greatest problems lie where government has lent its hand in the creation and protection of monopoly positions.

How is monopoly power to be identified? They assert:

it is the size of the seller relative to the market and to its ability to use power to restrain, block, obstruct or exclude entry or the offering of alternatives in the medium-term or in the longer-run, that is important.⁶⁵

They point out that such monopoly power may not be associated exclusively with a single entity, but may occur as the result of concerted action by a large number of smaller producers. Despite the legislation against resale price maintenance since 1952, "it would appear safe to conclude that the cost to consumers [of *voluntary* resale price maintenance] alone [has] been in the range of several hundreds of millions of dollars per year."⁶⁶ They point out that "it is, however, the large firm or group of large firms in a highly concentrated market, that is generally considered to exemplify 'monopoly' and to pose the most serious threat of misuse of monopoly power."⁶⁷ Yet, in identifying monopoly power, they reject the structuralist approach, and in particular, argue that the empirical (econometric) studies seeking to relate market structure variables to aspects of performance "have been so inconclusive that it would be hazardous to conclude that firms below a given size (or a given market share) consistently presented no monopoly problems, or that firms above a given size (or market share) could be reliably presumed to present such problems."⁶⁸ But when they then look at performance criteria to identify areas of monopoly power they also see significant defects. They point out that the concept of "fair prices" is usually a cost-plus-profit concept, and as such is "inconsistent with the role assigned to prices in a dynamic market economy."⁶⁹ Excess profits, in the sense of the return to monopoly, are hard to identify and differentiate from the returns to superior entrepreneurial performance and the return for risk bearing. More importantly, low rates of return may be the result of holding "an umbrella over the rest of the industry and applying a rule of 'live and let live' "⁷⁰ in order to forestall entry and the disturbing consequences of "dynamic change." The result of such constrained behaviour by firms is that "it tends to slow down the rate of dynamic change and reduces the flexibility and adaptability of the economy."⁷¹

⁶³ *Id.* at 129.

⁶⁴ *Id.* at 132.

⁶⁵ *Id.* at 133.

⁶⁶ *Id.* at 137.

⁶⁷ *Id.*

⁶⁸ *Id.* at 138.

⁶⁹ *Id.* at 139.

⁷⁰ *Id.* at 141.

⁷¹ *Id.* at 143.

In the short run, firms may dissipate their monopoly profits in the form of increases in costs. Therefore, Skeoch and McDonald argue that, "[t]he role of public policy . . . [is] to prevent such firms from entrenching or exploiting their market power by artificial restraints or abuse of their dominant positions."⁷² They see little role for economies of scale in establishing "some minimum justifiable absolute firm size."⁷³ They reject engineering estimates as inappropriate when the longer-run perspective is to be applied. Because the large corporation is a multi-market enterprise, "the search for an optimal scale of operations for each industry runs the danger of becoming merely a formal, academic exercise."⁷⁴ The approach advocated by the report "would be to define 'dominant firms' and then to examine how that dominance was maintained or extended (and perhaps how it had been achieved)."⁷⁵

In considering public policy toward the existing centres of monopoly power, Skeoch and McDonald see no merit in attempting to eliminate the base(s) of such power. They present their argument in terms of "why not," i.e., the difficulties of adopting such a policy: (i) it should be non-discriminatory, but in practice it will be difficult to apply to labour, the professions and agriculture; (ii) the policy will be constrained by the existence of economies of scale at the level of the plant; (iii) breaking up larger, successful firms may have both "internal" effects and adverse demonstration effects; (iv) the international aspects are difficult to assess — large firms appear to be necessary to operate successfully internationally; (v) the prohibition of the abuse of monopoly power will go a long way to eliminate the undesirable aspects of monopoly power; and (vi) the "structural foundations of the future" ought not to be shaped by the values of a few government officials inadequately aware of "unforeseen developments in technology, economic organization and in social institutions."⁷⁶ The benefits of undermining the base(s) of existing positions of monopoly power are not set out.

Their policy proposal in respect of monopoly is that dominant firms be prohibited from engaging in forms of conduct which are judged to be abuses of monopoly power. They define a "dominant firm" as

one that is capable within broad limits of choosing its rate of profits (or its share of the market) undeterred by the consideration that rivals may compete away these profits by offering better terms to customers.⁷⁷

In general terms, "abuse of market power" includes "all forms of competitive action not based on superior economic performance."⁷⁸ The following kinds of behaviour are included in the definition: "preclusive acquiring [*sic*] or ownership of resources and facilities; deliberated [*sic*] exclusion; reinforcing a dominant position by exclusive dealing and tying arrangements or by refusal to deal; predatory discrimination; a design to forestall competition and to hold

⁷² *Id.* at 143-44.

⁷³ *Id.* at 144.

⁷⁴ *Id.* at 145.

⁷⁵ *Id.*

⁷⁶ *Id.* at 148-50.

⁷⁷ *Id.* at 150.

⁷⁸ *Id.* at 151.

its monopoly position by other than the achievement of real-cost economies; the use of reciprocal dealing advantages. . . ."⁷⁹

In their draft statute, the authors put the matter somewhat differently, defining misuse of dominant position to be

any form of competitive conduct that constitutes, or has the effect of creating or enhancing, a significant artificial restraint in a market, and which is not justified or offset by real-cost economies resulting from that conduct.⁸⁰

Where misuse of monopoly power was established by the Director of Investigation and Research before the National Markets Board, the Board would issue a remedial order. In serious cases, the Board could recommend changes in tariffs or other measures "to neutralize the firm's dominant position."⁸¹ Only persistent abuse of monopoly power would justify dissolution or divestiture.

In addition, they recommend that "regulated industries should be deemed to be generally subject to combines legislation."⁸² They should be exempted only when the restrictive conduct is specifically imposed by legislation, when it is actively supervised by regulatory officials, and when the restraint imposed by legislation is the least restrictive means available to achieve the legislative objective.⁸³ Skeoch and McDonald would also like to see their approach applied to agricultural marketing boards, which they view as simply government-mandated cartels. In the general area of government authorized and supervised monopolies beyond the reach of legislation, they recommend that the Director of Investigation and Research "institute appropriate research studies to clarify their significance for the government and the public."⁸⁴

3. *Structural Rationalization, Export Agreements and Specialization Agreements*

Skeoch and McDonald, following the Swedish approach, take structural rationalization to mean measures designed to increase effective industry performance through changes in the structure of an industry taken either collectively by industry enterprises or, in special circumstances, by public authorities.⁸⁵ Industry structure in this context refers to the number, size, location, and range of products of the firms in the trade.

They point out that the Swedish approach specifies three general conditions to be met through the cooperative efforts of the firms: (1) "The unit to be created by the restriction of competition must remain exposed to effective competition from without the unit"; (2) given the first condition, it must be highly probable that the firms party to the agreement will operate more efficiently; and (3) firms must not be forced into nor excluded from the agree-

⁷⁹ *Id.*

⁸⁰ *Id.* at 156.

⁸¹ *Id.* at 151.

⁸² *Id.* at 152.

⁸³ *Id.*

⁸⁴ *Id.* at 155.

⁸⁵ *Id.* at 170.

ment.⁸⁶ While structural rationalization is promoted by the provision of information concerning supply and demand, cooperation in R & D, cooperation in technical and other forms of training and by changes in labour agreements and in legislation, the main measures involve: "mergers and discontinuations, joint sales organizations and cooperation in production."⁸⁷

The authors emphasize that in the Swedish approach rationalization activities are undertaken by private groups on their own initiative, subject to the constraints indicated. They note that, in Canada, both big and small business have "a long tradition of reliance on government for help in solving [their] problems."⁸⁸ They argue that if structural rationalization is sponsored directly by government, and it is unsuccessful, the firms involved "would feel justified in demanding a measure of state protection, subsidization, or freedom to engage in restrictive practices."⁸⁹ There are other difficulties in the Canadian case; obtaining the necessary cooperation of labour and the efforts of provincial governments to build their own industrial base may frustrate rationalization.

Public policies aimed at structural rationalization, export and specialization agreements are based on the idea that positive intervention is required to speed up the economic transformation processes and so improve the economy's performance. They assert that demands for rationalization in the U.K. and Germany occurred in the context of the spread of rigidities, the erosion of market influences and the intervention of the state in the interest of "national solidarity."⁹⁰ As they point out:

The supporters of rationalization had no confidence in the "haphazard and ruthless" forces of competition to achieve the reorganization of industry into units of greater efficiency. . . .⁹¹

However, Skeoch and McDonald conclude that where the transformation process is too slow or ineffective "it is impossible to restore vigorous market-oriented performance by tinkering with structural elements in given industries."⁹²

The factors supporting the case for structural rationalization, the authors argue, are of two groups: those which originate in the area of international business, i.e., are universalist in impact, and those which are internal to the individual country. Such factors as changes in technological and organizational methods, the increased volatility of demand and the increased minimum economic size of firms are included in the first category. Internal factors include preventing the erosion of profitability, increased labour costs, and technically more complex methods of production.

⁸⁶ *Id.* at 172.

⁸⁷ *Id.* at 173.

⁸⁸ *Id.*

⁸⁹ *Id.* at 174.

⁹⁰ *Id.* at 161.

⁹¹ *Id.* at 163.

⁹² *Id.* at 164.

What are Skeoch and McDonald's policy proposals? First, the initiative for structural rationalization must come from the private sector. The role of government should be to ameliorate the impact of the changes on labour and in allocating the costs of adjustment between the firms and the state. Second, where the diversity of products is to be reduced, the users will have a voice in deciding what products are to be eliminated. For practical purposes, this would apply to industrial or commercial buyers. Third, the three basic conditions specified in the Swedish approach will be necessary for the protection of the public. They suggest a fourth condition — that export sales agreements not be associated with international cartels. Fourth, a full record of all rationalization agreements should be filed with the Director of Investigation and Research. However, Skeoch and McDonald do *not* recommend a programme of advance clearance (although that would be available on request) or compulsory prior examination of rationalization arrangements.⁹³ But, like mergers, such arrangements could be challenged by the Director before the National Markets Board. No precise criteria or bases for challenging rationalization agreements are set out.

4. *Industrial and Intellectual Property*

In general, the position taken by Skeoch and McDonald toward patents, trademarks, industrial designs and copyrights is that the enforcers of the *Combines Investigation Act* should take as given the property rights conferred by the various industrial property statutes. "In principle, industrial property rights should not be treated differently from any other assets so far as competition policy is concerned."⁹⁴ They observe that it is only "fortuitous" that an industrial property right, in specific cases, "defines a meaningful degree of monopoly power for purposes of market analysis."⁹⁵ The authors refuse to get drawn into a discussion of the reform of the law as it relates to industrial property. However, if the application of property rights in patents, trademarks and copyrights goes beyond what is contemplated or provided for in the statutes (e.g. special exclusionary or anticompetitive effects), they argue that remedies should be available under the *Combines Investigation Act*. They draw a "fundamental distinction between the exercise of a right conferred expressly or by necessary implication under an industrial property statute and a claim deriving only from a contract that involves such a right."⁹⁶ They give the example of a tie-in arrangement with a licensee in which the sale of an unpatented product is tied to the sale of the patented product. These tying arrangements and also those involving exclusive dealing, should be subject to the *Combines Investigation Act*. They propose similar treatment of licences of industrial property which are aimed at price discrimination. On the other hand, where the industrial property statutes provide for licences extending territorial or field of use restrictions, these should be exempted from the refusal to deal and market restriction sections of the *Combines Investigation Act*.

⁹³ *Id.* at 175.

⁹⁴ *Id.* at 181.

⁹⁵ *Id.* at 179.

⁹⁶ *Id.* at 184.

Licensing or the assignment of industrial property rights should remain subject to the conspiracy provision of the *Combines Investigation Act*. "Licence requirements persisting by contract after the expiry of the statutory right, inclusion of 'no contest' clauses in licences or unjustified threats of infringement actions are examples of conduct that could, on the facts, constitute misuse [of monopoly power] within the meaning of the Combines Investigation Act."⁹⁷

Skeoch and McDonald assert that failure to work a patent or refusal to licence where the owner does not work the patent significantly, where the firm holds a dominant position, may require a compulsory licensing order by the National Markets Board. However, they recommend that the power to order a licence "constitutes a form of divestiture" and should be employed by the Board "only on a last resort basis" as it would in the case of other abuses of monopoly power. They propose, in light of these recommendations, that section 29 of the *Combines Investigation Act* be repealed. Finally, they recommend that no special remedial powers be provided in the case of "know-how" agreements, these being adequately protected by the common law of contracts.

5. *Corporate Interlocks*

The report argues that the only overlap between boards of directors relevant to competition policy is that in which the interlocked enterprises are actual or potential competitors or have another market connection, e.g., a buyer-seller relationship. "Concentration of general economic power by means of interlocks is . . . not of direct concern to competition policy; it is an essentially different matter."⁹⁸ The formulation of public policy toward interlocks, they assert, should be guided by the following considerations: (i) "There is no reliable evidence that interlocks have in fact harmed competitive processes in Canada in any generally significant way";⁹⁹ (ii) generalizations about interlocks are difficult, because circumstances vary between industries; (iii) "the principle of minimum government interference requires that no restraint be imposed that is not clearly required, and that no more be prohibited than is clearly undesirable";¹⁰⁰ and (iv) "managerial skill and entrepreneurial talent are so scarce and so important to economic health that any unnecessary restriction or inhibition against selecting the best people for each particular industry could be counterproductive."¹⁰¹ No positive arguments are presented supporting legislation which would constrain corporate interlocks. In general, Skeoch and McDonald see the existing common law and statutory provisions relating to the duties of directors as adequate to deal with conflicts of interest. They list seven specific difficulties in formulating effective legislation dealing directly with interlocks.¹⁰² The report points out that "the under-

⁹⁷ *Id.* at 186.

⁹⁸ *Id.* at 190.

⁹⁹ *Id.* at 191.

¹⁰⁰ *Id.* at 192.

¹⁰¹ *Id.*

¹⁰² *Id.* at 195-96.

lying concern is substantive and yet the rules would look only to a particular formal mechanism" and concludes that a general statutory prohibition of specific types of interlocks is not justified in Canada. However, it proposes that the National Markets Board should have the power "to prohibit a particular interlock or defined types of interlocks between specific enterprises, in a situation where an undesirable practice or effect has been found to exist that was or was probably [or is likely to be] caused or facilitated by the interlock."¹⁰³ The authors see such prohibitions as probably within the scope of sections 30(1) and 30(2) of the existing *Combines Investigation Act*.

6. Price Discrimination

In general, Skeoch and McDonald wish to direct public policy toward a position in which real economic advantages in purchasing and distribution can be fully utilized. They recognize that price discrimination has both desirable and undesirable economic effects; it is both pro- and anti-competitive depending on the circumstances. They argue that the origin of the existing legislation was in the Depression and in periods of severe structural change. The time has come to make policy in light of more normal conditions. After a careful canvass of the important issues, the authors conclude there is *no* real case for protecting small business with legislation relating to price discrimination which has the effect of limiting the full exploitation of real economies. In any event, small business is not demonstrably pro-competition. In summary, they reject the idea that public policy should be aimed at "structural balance." They recognize that if large scale purchasing power cannot be fully utilized directly it may well be used in less desirable ways.

Skeoch and McDonald propose to delete section 34 as a criminal offence from the *Combines Investigation Act* and to write in a new "general section permitting the National Markets Board to prohibit discriminatory pricing behaviour by either *buyers* or *sellers*."¹⁰⁴ The essence of the offence will be sales "at less than the reasonably anticipated long-run average cost of production and distribution," where such sales have "the effect of adversely affecting competition."¹⁰⁵ They are sharply critical of historical accounting costs as useful measures of the economic concepts they wish to see implemented by the National Markets Board. They seem quite sanguine about the ability of the Board to develop a consistent approach and appraise the cost calculations of those called before it.

Predatory conduct based on high levels of market power is to be included within the concept of "abuse of monopoly power" discussed above. Presumably, this proposal is designed to replace the existing section 34(1)(c).

Several "supplementary considerations" to the general price discrimination provisions are set out:

- 1) a good faith defence of meeting competition even when the price of a competitor is itself discriminatory¹⁰⁶

¹⁰³ *Id.* at 196-97.

¹⁰⁴ *Id.* at 217; emphasis added.

¹⁰⁵ *Id.* at 217-18.

¹⁰⁶ *Id.* at 222.

- 2) retention of the equal treatment of goods and services of "like quality and quantity"¹⁰⁷
- 3) while not retaining the concept of requiring "a practice" or "policy" of discriminating before tackling the problem, the Board should consider a case "as long as it is of significant proportions whether or not it amounts to a practice."¹⁰⁸

The report recommends that section 35, dealing with discrimination in advertising and promotional allowances, be "retained in its present form but recast to place it within the jurisdiction of the Board."¹⁰⁹

The only dissenting view in the entire report is expressed by Reuben M. Bromstein on the proposals with respect to price discrimination. He wants to retain sections 34 and 35 as criminal provisions and to have the National Markets Board's jurisdiction over the proposed civil remedies be supplementary to the existing legislation. He argues that while "there is no record of judicial enforcement," these sections act as "a demonstrative deterrent."¹¹⁰ Mr. Bromstein expresses his concern for the position of small business in the economy. Skeoch's reply all but dismisses Bromstein's concern and he marshals some empirical data to support the proposition that small business' share of retail sales is virtually unchanged since the 1930's.

7. *Basing-Point Pricing*

The authors point out that basing-point pricing is one case of a general set of delivered pricing schemes. They recognize that it may be an essential element in collusive price setting through cooperative formula pricing. They point out its presence in the *R. v. British Columbia Sugar Refining Co. Ltd.*¹¹¹ and *R. v. Armco Canada Ltd.*¹¹² cases. However, the report urges "due caution" regarding changes in public policy to promote or modify the use of delivered pricing systems.

Skeoch and McDonald argue that strict f.o.b. mill pricing could result in a series of local/regional monopolies with varying degrees of price discrimination as freight absorption is used to enlarge individual firms' markets. In particular, they are concerned about its impact on the realization of real economies of scale. They emphasize that they "do not lay great stress on the price discrimination element in the public policy appraisal of the basing-point system."¹¹³ In general, "the test should be whether the substitution of some

¹⁰⁷ *Id.*

¹⁰⁸ *Id.* at 223.

¹⁰⁹ *Id.* at 224.

¹¹⁰ *Id.* at 353.

¹¹¹ *Supra*, note 41.

¹¹² *R. v. Armco Drainage and Metal Products of Canada Ltd.*, (Unreported) Supreme Court of Ontario, Toronto, November 13, 1959, Bureau of Competition Policy mimeo 54-1. More recently a number of these firms were convicted of price-fixing in a scheme incorporating zonal delivered pricing. See, *R. v. Armco Canada Ltd.* (1975), 6 O.R. (2d) 521; 21 C.C.C. (2d) 129; 17 C.P.R. (2d) 211; sentencing, *Re R. and Armco Canada Ltd.* (1976), 8 O.R. (2d) 573; 24 C.C.C. (2d) 147; 19 C.P.R. (2d) 273; 24 C.P.R. (2d) 145 varying (*sub. nom. R. v. Armco Canada Ltd.*).

¹¹³ *Supra*, note 1 at 240.

system of freight absorption for a basing-point system will reduce costs (the net result of production and transportation cost changes) and increase output."¹¹⁴

Where a basing-point scheme has been used to facilitate price fixing, the report recommends that, in addition to the fine, the firms be ordered to give buyers the f.o.b. mill option. In summary, the report does *not* propose any new legislation in respect of basing-point pricing.

8. *Loss-Leader Selling*

The report begins by pointing out that agitation for legislation in respect of loss-leader selling has occurred in waves and is associated with the introduction of new methods of distribution, recession, excess entry and occasionally with trials of strength among major retailers. The authors indicate that what is meant by a loss-leader ranges from sales below regular price to selling at prices below the firm's net acquisition cost. They argue that "the low-cost seller should not be prevented from using his advantage to increase his turnover by quoting lower prices and thus lowering his cost still further."¹¹⁵ They obviously believe there are unexploited economies of scale in many areas of retailing.

Skeoch and McDonald would reject any public policy which would require a uniform markup type of pricing.¹¹⁶ Consistently with their general approach to facilitating change in the economy, they conclude that, "[i]t is obvious that price structures should be sufficiently flexible over time to reflect and encourage changes in technology which may reduce costs and prices. These cost and price reductions are the very essence of progress in the industry."¹¹⁷

Three possible policy alternatives are outlined:

- 1) the prohibition of sales at prices less than net acquisition cost¹¹⁸
- 2) the prohibition of sales below acquisition cost plus a specified minimum markup¹¹⁹ and,
- 3) the prohibition of "cut-throat" competition¹²⁰

All are rejected.

The authors view loss-leader selling as part of the long-run dynamic process of technological and organizational changes, and propose *no new* legislation dealing with loss-leader selling. But the implications of their analysis are difficult to determine. Currently, loss-leader selling is included in the *Combines Investigation Act* under section 38(9) (a) and (b) where it is a defence to a charge of refusal to supply. Under section 38(9) (a), where a sup-

¹¹⁴ *Id.* at 240-41.

¹¹⁵ *Id.* at 246.

¹¹⁶ *Id.* at 247.

¹¹⁷ *Id.* at 251.

¹¹⁸ *Id.* at 256.

¹¹⁹ *Id.* at 256-57.

¹²⁰ *Id.* at 258.

plier believes that a seller "was making a practice of using [the supplier's] products . . . as loss-leaders, that is to say, not for the purpose of making a profit thereon but for purposes of advertising," he may successfully defend a charge of refusal to supply. Apparently this loss-leader defence is to remain as the report did not indicate that it should be removed. One might argue that loss-leader selling could be attacked under the present section 34(1)(c) which prohibits a seller from engaging "in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have such effect." However, the authors propose to delete the present section 34, as they wish to bring the price discrimination sub-sections 34(1)(a) and (b) under the National Markets Board civil procedures. Section 34(1)(c) apparently is to be subsumed by predatory conduct, but which would only be prohibited by the Board if it amounted to "misuse of dominant position."

9. *Cost Justification and Economic Policy*

This section should be viewed as part of the theoretical rationale underlying Skeoch and McDonald's analysis of price discrimination, basing-point pricing and loss-leader selling. It is a lecture on the folly of the general approach of "cost plus a reasonable profit" or "public utility pricing" as applied to what we usually refer to as the unregulated sectors of the economy. The authors point out that the approach of regulating monopoly was aimed at protecting the level and stability of certain people's incomes and that such a policy is backward looking and creates barriers to economic change. Like such predecessors as Professors Adams and Gray,¹²¹ they recognize the importance of the fine hand of the government in creating and maintaining private monopoly power.

Their analysis of the vagaries of cost accounting should be required reading for all economists, especially those who use such data uncritically.

As a general public policy, Skeoch and McDonald want the government to eliminate the use of cost-justification criteria in evaluating economic performance for they are "contributing to the steady erosion of the market-oriented sector."¹²² With respect to predatory pricing they reject the Turner-Areeda proposal that firms be prohibited from selling at "a price below reasonably anticipated average variable cost."¹²³ They prefer long run marginal or average cost "because of its fundamental anticipatory bias."¹²⁴

10. *Administration and Adjudication*

The implementation of their proposals, the authors maintain, requires the resolution of three basic issues: the specificity of standards and criteria

¹²¹ Walter Adams and Horace M. Gray, *Monopoly in America, the Government as Promoter* (New York: Macmillan, 1955).

¹²² *Supra*, note 1 at 272.

¹²³ *Id.*

¹²⁴ *Id.* at 273.

set out in the statute; the types of evidence and judgments required to apply the standards; and the character of the decision-making body.

In the Introduction to their report, Skeoch and McDonald conclude that the total reliance upon criminal law and criminal remedies "has been increasingly and widely recognized as a serious obstacle to effective implementation of competition policy."¹²⁵ The use of the criminal law, they argue, depends "upon a substantive prohibition that is defined sufficiently precisely in advance that a person has fair notice, before engaging in the conduct, that it is against the law and the public interest for him to do so."¹²⁶ Since the provisions of competition policy "cannot realistically define many undesirable events except in terms of their economic effect or likely economic effect"¹²⁷ exclusive reliance on the criminal law approach is inappropriate.

The heart of the report's administration and adjudication recommendations is the creation of a specialized adjudicating body, the National Markets Board, which will make decisions and establish remedies in the context of *civil* procedures. Critics will undoubtedly recall the Competitive Practices Tribunal proposed in the ill-fated Bill C-256 (the *Competition Act*) in June of 1971.¹²⁸ The policy which the authors "believe will maximize the long-run flexibility and effectiveness of the Canadian economy . . . depends critically upon the existence of a decision-making authority capable of dealing perceptively and impartially on a case-by-case basis with the complex issues of fact and remedy that will frequently require analysis and prescription."¹²⁹ They argue that the "courts should continue to play a vital role," but "the case for placing these additional powers [adjudicative powers respecting mergers, misuses of market power, price discrimination and rationalization, specialization and export agreements] in the hands of a specialized adjudicator is very strong."¹³⁰

They stress the necessity to strike a careful balance between specificity and general applicability of statutory provisions. In the Canadian context, they assert, it is not appropriate to have many "mechanical" *per se* rules. While such rules may provide predictability they will probably not result in "economically realistic decisions."¹³¹ They clearly opt for the "case-by-case" approach, asserting: "Predictability is not the paramount, let alone the sole, concern of the law."¹³²

By proposing to set out a clear statement of the objectives, (in sharp contrast to the existing policy), which will become the fundamental guidelines

¹²⁵ *Id.* at 39.

¹²⁶ *Id.*

¹²⁷ *Id.* at 39-40.

¹²⁸ B. C. McDonald's views of the *Competition Act's* use of a Tribunal are contained in his paper, "The Central Legal Issues Raised by the Government Proposals" in L. A. Skeoch, ed., *Canadian Competition Policy*, *supra*, note 21 at 10-17.

¹²⁹ *Supra*, note 1 at 279.

¹³⁰ *Id.* at 280.

¹³¹ *Id.* at 284.

¹³² *Id.* at 281.

for the National Markets Board, the authors of the report hope to resolve the issue of who is to make policy: the elected representatives or the judges. In adopting a case-by-case approach, which they anticipate will be responsive to a changing environment, Skeoch and McDonald recognize that "the use of precedent becomes somewhat more sophisticated than in the usual court proceedings."¹³³

Before discussing the details of the report's proposals regarding enforcement procedures and the National Markets Board it may be useful to see how the total system would look if their proposals were adopted. A schematic representation is given in Figure 1.

(a) The National Markets Board (NMB)

(i) Composition

The NMB is to be a superior court of record with a Chairman who is to be an experienced superior court judge. It will consist of a minimum of four full-time members appointed for a term of less than ten years, and minimum of four part-time members appointed for a term of less than three years. The authors lay particular stress on the qualifications of the lay members of the NMB: the majority of both the full-time and part-time members "should have had extensive private sector experience (as distinguished from, though perhaps in addition to, civil service or university experience)."¹³⁴ They stress that they "place more faith in experience and informed common sense than in cloistered 'expertise'. "¹³⁵ Finally, they warn: "If, however, the government in making the appointments were to be influenced by any grounds other than personal qualifications for the job, the results could be considerably more damaging than leaving the law as it is."¹³⁶

It is anticipated that the NMB will work in panels of three or more (with a minimum of one full-time member). The authors believe that this should prevent both large backlogs of cases and with the turnover in membership "prevent balkanization of any ingrained convictions or aberrational views."¹³⁷

(ii) Functions and Powers

The NMB, it is proposed, will have substantive civil jurisdiction with respect to mergers, misuses of monopoly power, price discrimination, rationalization, specialization and export agreements along with the list of "reviewable matters" (see Figure 1) which were assigned to the Restrictive Trade Practices Commission by the 1975 amendments to the *Combines Investigation Act*. The RTPC is to be abolished. The NMB will *not* be a U.S. type regulatory agency, e.g., the Federal Trade Commission. It will not perform any research

¹³³ *Id.* at 285.

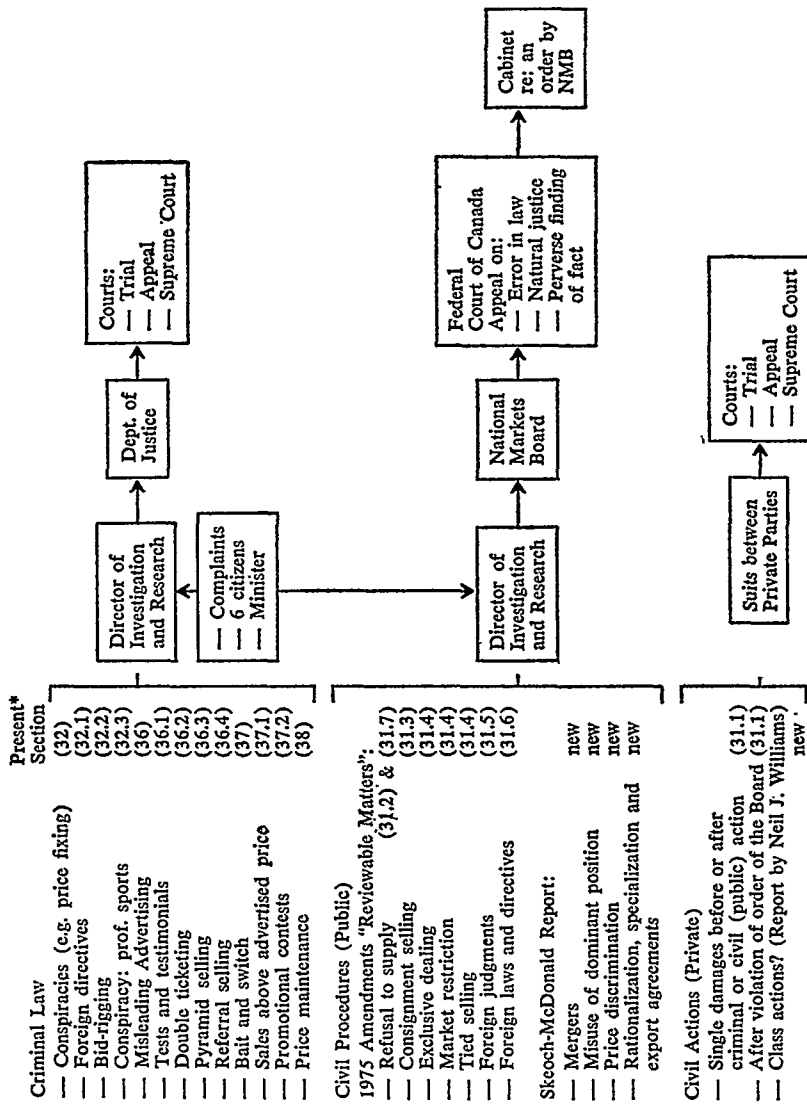
¹³⁴ *Id.* at 294.

¹³⁵ *Id.* at 295.

¹³⁶ *Id.*

¹³⁷ *Id.* at 297.

FIGURE 1
Competition Policy: Proposed Administration and Enforcement



**Combines Investigation Act*, R.S.C. 1970, c. C-23, as amended by c. 10 (1st Supp.); c. 10 (2nd Supp.); 1974-75-76, c. 76.

activity, it will not have any general rule-making authority and it will not have any power to initiate investigations which could eventually come before it for adjudication.

The Board will have the power to issue orders of prohibition which are both injunctive and remedial. Skeoch and McDonald propose that the NMB be given the new powers given to the RTPC in the 1975 amendments. They stress that "the Board ought not [to] make any order that does not tell the businessman with reasonable certainty just what is and what is not covered by the order,"¹³⁸ because both private civil and criminal actions can ensue from violations of an order by the Board. At the same time, they also propose that the Board "confine itself to saying 'no' to business proposals or activities, and avoid giving detailed direction as to how the persons before it ought to conduct their business affairs in the future."¹³⁹ The report proposes that the NMB be given the power to order the dissolution of a merger and the power to order divestiture of assets only as an "extreme remedy" on a "last resort basis" for the repetitive misuse of market power. In the case of the latter, such an order would be subject to review by the Federal Court of Canada.¹⁴⁰

The Board would be given the power to issue interim prohibition orders but these would be subject to review by the courts within 90 days. The NMB would not be given the power to order continual returns of information.

(iii) Procedures

The NMB would have all the powers, rights and privileges of a superior court of record and, as such, would be subject to the rules of natural justice. It would have the power to establish its own rules of practice and be able to implement its own pre-hearing procedures. However, the report recommends that sole hearing officers, whether or not they are members of the Board, not be used. With three exceptions, all actions brought before the Board would be initiated by the Director of Investigation and Research (see Figure 1). The exceptions are (1) application by a person subject to an order to rescind or vary an order, (2) application by a person seriously injured by a practice over which the NMB has jurisdiction where the matter is too urgent to proceed via the Director's office, and (3) applications for approval of rationalization, specialization or export agreements.

Interested parties would be entitled to intervene in proceedings before the Board. However, parties to the proceedings would become liable to pay costs ordered by the Board. Conversely, the Board could order costs paid to such parties. Hearings by the Board should be in public, "except to the extent it deems it necessary to protect a legitimate business interest. . . ."¹⁴¹

Skeoch and McDonald recommend that the "basic burden of persuasion should be placed on the person who seeks the order."¹⁴² But, "[i]nsofar as

¹³⁸ *Id.* at 301.

¹³⁹ *Id.* at 300.

¹⁴⁰ *Id.* at 302.

¹⁴¹ *Id.* at 307.

¹⁴² *Id.*

relevant matters are peculiarly within the knowledge and capacity of private parties to demonstrate, . . . it is reasonable to rely on those parties to furnish the evidence."¹⁴³ As to the quantum of proof, the authors propose that it be "the normal civil standard which it usually described as the 'balance of probabilities'."¹⁴⁴ The Board's decisions should be accompanied by written reasons which should be made public.

(iv) Finality of Decisions

The authors argue it is "undesirable to give any body or court the power to interfere with the content of the factual or remedial decisions" made by the NMB.¹⁴⁵ However, the NMB would come under the supervision of the Federal Court of Canada, and appeals from the Board's decisions could be made upon three grounds as provided in Section 28 of the *Federal Court Act*:¹⁴⁶ failure to observe a principle of natural justice; an error in law; and an erroneous finding of fact made in a perverse or capricious manner. Therefore, the "courts will have the ultimate power to decide as a matter of law what the critical words in the statute mean" and to resolve disputes as to the extent of the powers and authority of the NMB.¹⁴⁷ They stress that it would "risk defeating the entire purpose of the specialized Board to permit the courts to substitute their views as to proper judgments concerning facts, market definition, or the design of the remedy."¹⁴⁸

Skeoch and McDonald argue there is need for a "safety valve" and also for a means to effect "an over-riding coordination of national policies."¹⁴⁹ Hence, they propose to allow appeals to the Cabinet within sixty days on any order of the Board. They also propose that the Cabinet "be required to make its decision and reasons public at the time of any decision to interfere with a Board order."¹⁵⁰ It is at this level that the "raw political questions" will be resolved.¹⁵¹

(b) Enforcement

(i) By the Director

The authors charge the Director of Investigation and Research with the responsibility for coordinating and making consistent both the criminal and civil provisions which would result from the 1975 amendments and their proposals. They specifically reject the idea that the Director be able to prosecute criminal cases either independently of the Department of Justice or after that Department has expressed an unwillingness to proceed to court. Yet they "see no legal reason" why the Director, "if he felt frustrated by delay or

¹⁴³ *Id.* at 308.

¹⁴⁴ *Id.*

¹⁴⁵ *Id.* at 309.

¹⁴⁶ R.S.C. 1970, c. 10 (2nd Supp.).

¹⁴⁷ *Supra*, note 1 at 310.

¹⁴⁸ *Id.*

¹⁴⁹ *Id.* at 314.

¹⁵⁰ *Id.* at 315.

¹⁵¹ *Id.* at 314.

an unwise decision” of the Attorney-General of Canada, could not send a copy of his Statement of Evidence to a provincial attorney general.¹⁵² But the authors do reject the idea that if the Department of Justice refuses to proceed, that the Statement of Evidence be made public where it might be of assistance in private civil actions.

When the Director uses his compulsory investigative powers and intends to go before the NMB, the report recommends that there be, in advance of the hearing, and in addition to any pre-hearing discovery, “comprehensive disclosure” of the proposed evidence, a narrative of the relevant facts, at least outlines of testimony to be given by witnesses, (expert or otherwise), copies of documents to be introduced and “a statement of positions to be taken on matters such as market definition, the nature of public harm involved and, on a tentative basis, remedies.”¹⁵³ At the pre-hearing discovery the defendant would also be expected to make a fairly extensive disclosure of his position.

(ii) By Private Persons

The authors take the position that “[p]rivate actions are an integral part of the total law enforcement apparatus. . . .”¹⁵⁴ They see the Act as both a sword and a shield. As a sword, private civil actions are designed to effect compensation of those disadvantaged by restraints of trade and to prevent unjust enrichment of those who perpetrate illegal restraints.

In considering any additional proposals for multiple damages, class actions and litigation assistance for private plaintiffs, Skeoch and McDonald urge “that policy decisions in this area . . . must be made in the light of comprehensive and long-run criteria, and that short-run immediate interests should not blind policy-makers to the ultimate objective of making markets work more effectively.”¹⁵⁵

With respect to the use of the Act as a shield, Skeoch and McDonald propose that section 39 be amended to clarify its existing wording that nothing in the Act should be construed to deprive any person of any civil cause of action and also to “provide that no action shall be based on a contractual provision or brought in furtherance of a plan or scheme that contravenes a requirement of Part V of the Act or an order of the Board.”¹⁵⁶ The purpose of the latter provisions is to ensure that a defence of illegality or public policy is available.

They recommend that the NMB *not* be given jurisdiction on applications by the Director to declare private covenants in restraint of trade to be unenforceable. Similarly, the NMB is not to be given any authority with respect to unjustified threats of patent infringement. Both of these matters are to be left to the courts.

(c) Advance Clearance

The authors view the current programme of compliance (i.e., the Director’s

¹⁵² *Id.* at 319.

¹⁵³ *Id.* at 322.

¹⁵⁴ *Id.* at 323.

¹⁵⁵ *Id.* at 327.

¹⁵⁶ *Id.* at 328.

“open door policy”) as a “necessary evil rather than a virtue.”¹⁵⁷ They wish to avoid the process of the Director appearing to “negotiate” with businessmen over restrictive trade practices. It is argued that “it would not be desirable to formalize the program of compliance by giving the Director powers to grant legally effective clearance.”¹⁵⁸ It appears that Skeoch and McDonald envisage the “withering away” of compliance activities. They propose, however, to permit the Director to issue advance clearances for proposed mergers and for rationalization agreements. “Clearance of a merger would insulate the firms involved from any further proceedings before the Board challenging the merger. In the case of a rationalization agreement, clearance would be available to clarify the status of the agreement.”¹⁵⁹ These exceptions are made to the general approach, because they involve “non-recurring transactions” which involve “substantial reorganization of assets, contractual relations, and methods. . . .”¹⁶⁰

Following a written application, the Director has thirty days to undertake an informal investigation and decide whether to launch a *formal* inquiry. The proposal will be deemed to be approved at the expiry of the thirty day period unless the Director indicates to the applicant he wishes to hold a formal inquiry. He then has an additional sixty days to investigate and decide upon the advance clearance. If the Director proposes to challenge the merger or rationalization agreement he must do so before the end of the sixty day period or the application is deemed to be approved. Clearance is a binding safeguard “only if there were no significant omissions from the original application.”¹⁶¹ With respect to mergers that come within the purview of the Foreign Investment Review Agency, the report recommends that “the matter not proceed to cabinet until the evaluation under the Combines Investigation Act [advance clearance provisions] is completed.”¹⁶²

(d) The Research Function

The research function is to be lodged entirely within the Bureau of Competition Policy. The NMB, unlike the RTPC, will have *no* role to play in generating research. Studies done by the Bureau should be published directly by the Bureau without any outside approval. The authors point out that the “very ambitious program of research” envisaged by the MacQuarrie Committee in its Report¹⁶³ in 1952 has not come about. In what must be a severe understatement they observe, “something more might have been expected than has been achieved.”¹⁶⁴

The authors of the report have great doubts about the ability of organized groups, particularly those in government, to produce creative research. It is their view that “[o]nly research of superior quality is worth doing at all; . . .

¹⁵⁷ *Id.* at 326.

¹⁵⁸ *Id.* at 335.

¹⁵⁹ *Id.* at 334.

¹⁶⁰ *Id.* at 337.

¹⁶¹ *Id.* at 338.

¹⁶² *Id.* at 341.

¹⁶³ *Report of the Committee to Study Combines Legislation and the Interim Report on Resale Price Maintenance* (Ottawa: Queen’s Printer, 1952).

¹⁶⁴ *Supra*, note 1 at 344.

A small staff marked by intellectual excellence and ability to produce respected studies should be the aim rather than a larger group with general 'service' responsibilities in the Bureau.¹⁶⁵ They suggest there should be two separate units: an economic analysis section to support the Bureau's enforcement efforts, and "[a] small research group which would undertake independent studies, as well as joint studies" with top people in academia, business and other government departments.¹⁶⁶ The research programme and output should be subject to external review. They also recognize the benefits of the Bureau engaging in legal research for competition policy as the nexus of the disciplines of both economics and law. With respect to research studies by the Bureau, Skeoch and McDonald propose that they be available for sixty days during which interested parties could submit comments to the Director. "The Director would then prepare a brief summary of such comments for inclusion as an appendix to the research study."¹⁶⁷ They see little need for the Director to use his formal powers of search or examination of witnesses under oath to prepare research studies.

D. APPRAISAL AND CRITIQUE

1. *The Choice of Objectives*

Skeoch and McDonald indicate that the objectives of competition policy ought to be directed toward facilitating long-run dynamic change, the adoption of real-cost economies and the discouragement of artificial restraints based on market power rather than superior economic performance. But the most important objective is taken to be the encouragement of dynamic change. In 1969, the Economic Council of Canada stated that the objective of competition policy legislation "should be the promotion of dynamic efficiency, flexibility and good all-around performance in the Canadian economy."¹⁶⁸ A few pages later in their discussion the Council refined their position:

Essentially, we are advocating the adoption of a single objective for competition policy: the improvement of economic efficiency and the avoidance of economic waste. . . .¹⁶⁹

In adopting this position, the Council pointed out that it did not wish to disparage other objectives such as a more equitable distribution of income or the diffusion of economic power. Rather it felt that a competition policy concentrated on a single objective "is likely to be applied more consistently and effectively," and that the tax-transfer system was better equipped to deal with these other objectives.¹⁷⁰ The Council also pointed out that the pursuit of multiple goals (e.g., efficiency and the diffusion of power) may result in a conflict of objectives, and that the pursuit of efficiency and the reduction of economic waste could also result in furthering other objectives. It is interesting that in the Preamble to Bill C-256, the proposed *Competition Act*, competition is seen to be "the best means of allocating resources [and] of enhancing efficiency in

¹⁶⁵ *Id.* at 346.

¹⁶⁶ *Id.*

¹⁶⁷ *Id.* at 350.

¹⁶⁸ Economic Council of Canada, *Interim Report on Competition Policy*, *supra*, note 4 at 5.

¹⁶⁹ *Id.* at 19.

¹⁷⁰ *Id.* at 20.

the production and distribution of goods and services . . .” and of furthering “individual enterprise by decentralizing economic power. . . .”¹⁷¹ This point is reiterated in the “Explanatory Notes” that accompany Bill C-256.

In economic terms, competition policy is designed to ensure that Canada makes the most efficient use possible of its resources. . . . But the considerations of competition policy go well beyond economics alone. Concentrations of power, which can serve to restrict opportunity and individual freedom, are not acceptable in today’s social and political environment and a major objective of competition policy must be to ensure that such concentrations of power are not allowed to develop.¹⁷²

The report may be criticized for its failure to even consider alternative objectives toward which competition policy might be directed. Even in the context of the small (by the standards of the U.S. and a number of Western European countries) Canadian economy where the conflict between the number of competitors and efficiency (economies of scale) is most poignant, it is not unreasonable to weigh the larger social implications of opting in one direction or the other. As noted above in the discussion of interlocking directorates, Skeoch and McDonald assert that the concentration of general economic power is not one of direct concern to competition policy. An examination of the trade-off, in terms of all social costs, between numbers and efficiency is particularly relevant if one is skeptical that, consumers, for whose benefit Adam Smith told us the economy ought to be run,¹⁷³ will in fact receive the benefits of dynamic change and real-cost economies. This point is specifically addressed in the Preamble to Bill C-256:

it is also recognized that in cases where a market is too small to support a sufficient number of independent firms of efficient size to promote effective competition, alternative means of promoting maximum efficiency may be required but that where such an alternative means is adopted, it is necessary to ensure that the resultant benefits will be transmitted in substantial part and within a reasonable time to the public. . . .¹⁷⁴

Repeatedly in their report, Skeoch and McDonald emphasize the necessity to take a long-term view of economic processes and repeatedly we are asked to opt for policies the benefit of which will only be realized in the long run. Such proposals are rational only if the social rate of time preference is low or, alternatively, if the future payoffs from “dynamic change” are so enormous that their present value offsets the short run costs that may be imposed on consumers as we allow firms to work out their destiny.

But let us look at “dynamic change” in its own terms. The report fails to

¹⁷¹ Bill C-256, *The Competition Act*, first reading, June 29, 1971.

¹⁷² Department of Consumer and Corporate Affairs, *The Competition Act: Explanatory Notes*, *supra*, note 5 at 8-9.

¹⁷³ In 1776 Adam Smith argued:

Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer. The maxim is so perfectly self-evident, that it would be absurd to attempt to prove it.

Of course, the formal proof of this proposition was not given for over 150 years. Smith was quick to point out that “in the mercantile system, the interest of the consumer is almost sacrificed to that of the producer: and it seems to consider production, and not consumption as the ultimate end and object of all industry and commerce. . . .” (*The Wealth of Nations*, Book IV, Chapter VIII).

¹⁷⁴ *Supra*, note 171.

emphasize that dynamic change is not the end of competition policy, but rather the means by which the rate of economic growth, as measured by real income per capita, is to be increased.¹⁷⁵ Their approach is almost visionary. As the authors see it, through the workings of the international technocracy embodied in private business firms, the optimal rate of technological change and innovation in economic organization will occur so long as governments seek only to strike down "artificial" restraints that may be imposed by the odd unenlightened competitor. Since they take existing market structures as given, they would appear to imply that such structures are the ones best suited to facilitate the process of change. There is absolutely no discussion of the determinants of technological change, except to note that government efforts have been largely unsuccessful, and in particular on the relationship between industry structure and economically significant innovation.

Given that we already have a highly concentrated economy¹⁷⁶ whose apparent rate of technological innovation is low,¹⁷⁷ it is hard to see how the acceptance of the structural status quo, coupled with some new prohibitions on business conduct will unleash the horses of "dynamic change." In a report on the forces of economic change, it is interesting that the authors did not once refer to a single work on technological change and innovation. Although it would be entirely consistent with their stance, Skeoch and McDonald have not specifically embraced Schumpeter's position that market power is necessary for innovation and that innovation is the core of effective competition.¹⁷⁸ They give no indication as to what configuration of market structure best facilitates dynamic change.¹⁷⁹ But this is symptomatic of the antistructuralist position taken in the entire report.

¹⁷⁵ A. Milton Moore, *How Much Price Competition?* (Montreal: McGill-Queen's University Press, 1970) at 127, makes the point with admirable directness: "The general objective of a national competition policy is, of course, to increase income per capita by increasing productivity. The role of a competition policy is to force change and efficiency upon industries."

¹⁷⁶ *Industrial Organization and Concentration in the Manufacturing, Mining, and Logging Industries* (Ottawa: Statistics Canada, 1976) (Cat. No. 31-514).

¹⁷⁷ The Senate Special Committee on Science Policy has stated:

The available evidence on Canadian R&D output, although incomplete, is sufficient to justify the conclusion that Canada's innovative performance is low compared with that of most other industrially advanced countries.

in *A Science Policy for Canada* (Ottawa: Queen's Printer, 1970) at 138. Two additional volumes were published by the Committee in 1972 and 1973. More generally see, Pierre L. Bourgault, *Innovation and the Structure of Canadian Industry*, Science Council of Canada Special Study, No. 23 (Ottawa: Information Canada, 1972); Science Council of Canada, *Innovation in a Cold Climate: The Dilemma of Canadian Manufacturing* (Ottawa: Information Canada, 1971); Andrew H. Wilson, *Governments and Innovation*, Special Study, No. 26, Science Council of Canada (Ottawa: Information Canada, 1973); and Arthur J. Cordell, *The Multinational Firm, Foreign Direct Investment, and Canadian Science Policy*, Special Study No. 22, Science Council of Canada (Ottawa: Information Canada, 1971).

¹⁷⁸ See, E. S. Mason, *Schumpeter on Monopoly and the Large Firm* (1951), 33 *Review of Economics and Statistics* 139.

¹⁷⁹ Debate abounds on this issue. For a useful short summary of the literature see, Morton I. Kamien and Nancy L. Schwartz, *Market Structure and Innovation: A Survey* (1975), 13 *Journal of Economic Literature* 1.

2. *The Significance of Market Structure in Determining Conduct and Performance*

The authors see little value in either the theoretical or empirical work which seeks to relate the characteristics of market structure to aspects of business behaviour and economic performance in terms of public policy. For example, they state that "the industrial concentration hypothesis in any of its variants is currently the subject of so much fundamental controversy that it provides a very unstable basis for any important public policy initiatives."¹⁸⁰ This generalization is not supported by a single reference. Similarly, their summation of the econometric investigations is neither supported by any discussion in the text of the report or by any reference to empirical work which would either support or deny their conclusion. Their position is put as follows:

Generalizations from empirical cross-sectional investigations of size and innovation performance, size and barriers to entry, size and scale economies, have so far related to larger economies and the results even there have been so inconclusive that it would be hazardous to conclude that firms below a given size (or a given market share) consistently presented no monopoly problems, or that firms above a given size (or market share) could be reliably presumed to present such problems.¹⁸¹

Perhaps they did not have the opportunity to read Leonard Weiss' comprehensive discussion, "The Concentration-Profits Relationship and Anti-trust"¹⁸² or to review the work on the Canadian economy by McFetridge, Jones *et al.*, Orr, de Silva, Bloch, Dooley and others.¹⁸³ Weiss' conclusion, following his review of forty-six empirical studies must serve to severely challenge Skeoch and McDonald's view:

To summarize, the theory of the dominant firm unequivocally points to high prices

¹⁸⁰ *Supra*, note 1 at 215.

¹⁸¹ *Id.* at 138.

¹⁸² This paper is found in Goldschmid *et al.*, eds., *supra*, note 179 at 184-232.

¹⁸³ D. G. McFetridge, *Market Structure and Price-Cost Margins: An Analysis of the Canadian Manufacturing Sector*, [1973] *Canadian Journal of Economics* 344; J. C. H. Jones, L. Laudadio, M. Percy, *Market Structure and Profitability in Canadian Manufacturing Industry: Some Cross-Section Results*, [1973] *Canadian Journal of Economics* 356; Robert R. Kerton, *Price Effects of Market Power in the Canadian Newspaper Industry*, [1973] *Canadian Journal of Economics* 602; Dale Orr, *The Economic Determinants of Entry into Canadian Banking: 1963-7*, [1974] *Canadian Journal of Economics* 82; Dale Orr, *The Determinants of Entry: A Study of the Canadian Manufacturing Industries* (1974), 56 *Review of Economics and Statistics* 58; G. F. Mathewson, *A Note on the Price Effects of Market Power in the Canadian Newspaper Industry*, [1972] *Canadian Journal of Economics* 298; K. E. A. de Silva, *Industrial Concentration and Price Changes in Canadian Manufacturing Industries, 1961-67*, [1971] *Quarterly Review of Economics and Business* 80; Harry Bloch, *Prices, Costs and Profits in Canadian Manufacturing: The Influence of Tariffs and Concentration*, [1974] *Canadian Journal of Economics* 594; Peter C. Dooley, *Retail Oligopoly: An Empirical Study of the Structure, Conduct and Performance of the Grocery Trade on the Prairies*, Study No. 3 for the Royal Commission on Consumer Problems and Inflation (Regina: 1969); K. Dennis, "Market Power and the Behaviour of Industrial Prices" in *Prices and Incomes Commission, Essays on Price Changes in Canada* (Ottawa: Information Canada, 1973); D. G. McFetridge, "Market Structure and Price Behaviour: Empirical Studies on the Canadian Manufacturing Sector," Unpublished Ph.D. thesis, University of Toronto, 1972; D. G. McFetridge, *The Determinants of Price Behaviour: A Study of the Canadian Cotton Textile Industry* (1973), 22 *Journal of Industrial Economics* 141.

and suggests high profit rates for dominant firms. Our assorted oligopoly theories are more equivocal in their details, but all of them that have not been discredited point to higher margins in concentrated industries once more. Our massive effort to test these predictions has, by and large, supported them for "normal" years such as the period 1953-1967, though the concentration-profits relationship is weakened or may even disappear completely in periods of accelerating inflation or directly following such periods. By and large the relationship holds up for Britain, Canada, and Japan, as well as in the United States. In general the data have confirmed the relationship predicted by theory, even though the data are very imperfect and almost certainly biased toward a zero relationship.¹⁸⁴

All of this is not to say that the report's insistence on a most careful case-by-case (industry-by-industry) approach, which will take full account of the substantial variation found in the relationship between structure and performance and structure and conduct, is undesirable. But I am most skeptical of the ability of senior businessmen, who will apparently make up the National Markets Board, to recognize the problem of the inefficient oligopoly which does not exhibit consistent excess profits and undesirable trade practices if they have no *a priori* theory, supported by respectable empirical studies, to guide their decision-making.

By enshrining existing market structures and a wide variety of protected positions as unassailable, and by accepting rather unquestioningly the argument that Canadian firms can only compete internationally by getting much larger, the implementation of their proposals will result in a significantly more concentrated economy. Since they see little real benefit in tariff reductions as a means of both forcing firms to be efficient and internationally price-competitive, it is not obvious that the benefits of dynamic change will in fact be made available to consumers. We may end up with a potentially more efficient and more highly concentrated industrial structure which simply results in higher profits and/or higher costs from inadequate competitive pressures.

3. *The Significance of Mergers*

On the basis of empirical evidence both limited and at least 15 years old, Skeoch and McDonald assert that

it would appear that the *general* merger movement in Canada has not given rise to any important consequences for the economy.¹⁸⁵

The failure to consider even gross merger behaviour in the decade and one-half following Reuber and Roseman's work¹⁸⁶ epitomizes their neglect of available empirical research or their unwillingness to produce any new research of their own. More effort is devoted to a discussion of the Swedish experience than our own.

Even a brief review of the gross merger data would appear to challenge the report's conclusion. In every five-year period between 1945 and 1974 the number of mergers in Canada (foreign and domestic) increased significantly as can be seen in Table 1.

¹⁸⁴ In Goldschmid *et. al.*, eds., *supra*, note 179 at 231.

¹⁸⁵ *Supra*, note 1 at 56 [emphasis in original].

¹⁸⁶ *Supra*, note 35.

Table 1

Foreign and Domestic Mergers
in Canada, 1945-1975¹⁸⁷

Period	Foreign		Domestic		Both	
	Total	Annual Avg.	Total	Annual Avg.	Total	Annual Avg.
1945-49	76	15.2	213	42.6	289	57.8
1950-54	113	22.6	285	57.0	398	79.6
1955-59	271	54.2	427	85.4	698	139.6
1960-64	379	75.8	580	116.0	959	191.8
1965-69	571	114.2	998	199.6	1572	314.4
1970-74	610	122.0	1282	256.4	1892	378.4
1975 prelim.	109	109	155	155	264	264

Between 1945 and 1949 mergers were occurring at a rate of fifty-eight per year. By 1955-59 the annual average had more than doubled to 140 and by 1965-69 it had more than doubled again to an average of 314 per year. Between 1970 and 1974 the annual average increased to 378. In the six years between 1968 and 1973 the number of foreign and domestic mergers in Canada averaged 417 per year.

Admittedly the data in Table 1 represent only the total number of mergers. The significance of the six-fold increase in the number of mergers in Canada in the post-war period is harder to determine. However, the Economic Council's *Interim Report* gives us a clue. For the period 1945-1961, the Council estimated that between eight and seventeen per cent of all mergers (accounting for thirty-four to forty-nine per cent of the total value of assets acquired) "might have qualified for a public interest examination."¹⁸⁸ If we assume the lower percentage is applicable, then between 1970 and 1974 about thirty mergers per year might have come under examination. This number is significantly higher than the number actually investigated by the Director of Investigation and Research. From the data presented, it is not possible to clearly refute their conclusion, but these statistics appear to suggest a far less sanguine conclusion than that reached by Skeoch and McDonald.

Having told us on the basis of inadequate knowledge not to take a negative view of virtually unrestricted merger behaviour of firms in Canada, the authors have committed the reverse sin. It is not possible to correctly assess the economic impact of mergers by referring to data at the high level of aggregation that they do. We need to know at the level of the theoretical industry what impact mergers have had on both the many faceted industry structure and on the various dimensions of economic performance. While they do look at Reuber and Roseman's data at the level of the industry subdivision,

¹⁸⁷ Sources: Grant L. Reuber and Frank Roseman, *The Take-Over of Canadian Firms, 1945-61*, *supra*, note 35 at 192; *Report of the Director of Investigation and Research, Combines Investigation Act for the year ended March 31, 1976*, *supra*, note 9 at 39.

¹⁸⁸ *Supra*, note 4 at 86.

they still fail to relate the number of mergers by "industry" grouping to, for example, their impact on the level of concentration in theoretical industries. Why, for example, have they not reviewed at least the published reports of the Restrictive Trade Practices Commission to see what impact the absence of any deterrent to mergers in Canada has had? A look at some of these "case studies" might be useful.

(a) Zinc Oxide¹⁸⁹

Prior to 1954 there were only two producers of zinc oxide in Canada; a third entered in 1954. The market shares, in terms of domestic sales, were as follows:¹⁹⁰

	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>
Zinc Oxide Co.	50.6%	53.4%	59.1%	59.8%
Durham Industries	35.5	33.9	23.9	20.4
Canadian Felling	—	1.5	9.1	14.2
Imports	13.9	11.2	7.9	5.6

Assisted by discriminatory discounts from its supplier, the Zinc Oxide Co. engaged in a price war with its rivals between January 1955 and February 1956. In June 1955 it acquired the shares of Durham Industries and unsuccessfully tried to acquire Canadian Felling. As a result, the Zinc Oxide Co. accounted for eighty per cent of domestic sales in 1956.

Regrettably the Director was more concerned about the price discrimination aspects of the case than he was about the merger. The RTPC gave only passing mention to the effects of a merger in a three firm industry with high entry barriers. It did not make any recommendation with respect to the merger. No prosecution followed.

(b) Yeast¹⁹¹

In June 1955 Standard Brands acquired Best Yeast Limited, reducing the number of yeast producers in Canada from three to two. The market shares of the Canadian producers were as follows:¹⁹²

	1955			1956	
	<u>Dried*</u>	<u>Fresh*</u>	<u>Total†</u>	<u>Eastern Region†</u>	<u>Canada</u>
Standard Brands	86.5%	70.5%	76.0%	80.7%	77.0%
Best Yeast	7.5	7.4	8.8	14.9	6.5
Lallemand	6.0	22.1	15.2	4.4	16.5

* shipments

† sales

¹⁸⁹ Restrictive Trade Practices Commission, *Report Concerning the Production, Distribution and Sale of Zinc Oxide* (Ottawa: Queen's Printer, 1958).

¹⁹⁰ *Id.* at 166.

¹⁹¹ Restrictive Trade Practices Commission, *Report Concerning the Manufacture, Distribution and Sale of Yeast* (Ottawa: Queen's Printer, 1958).

¹⁹² *Id.* at 67, 38-40.

Following the merger, Standard Brands had become the only manufacturer of fresh consumers' yeast, and almost the sole producer of both bakers' and consumers' dried yeast in the Eastern Region. In the fresh bakers' yeast market, in spite of Lallemand's rising share, it still had seventy-five per cent of this market. Imports were negligible despite modest tariffs.

The director took a structural approach in his appearance before the RTPC and indicated that there were no economies of production or distribution to compensate for the reduction in competition.¹⁹³

The RTPC was "not convinced that the public interest has been so affected as to justify recommending action to alter the integration of manufacturing operations . . . or the dissolution of the merger."¹⁹⁴ They did, however, recommend that Standard not be permitted to acquire Lallemand or any new competitor who entered. The Department of Justice did not prosecute.

(c) Vancouver Newspapers¹⁹⁵

Prior to the merger there had been one morning newspaper (the *Herald*) and two evening newspapers (the *Province* and the *Sun*) under three independent ownerships. The Southam interests bought the *Herald* and closed it down. The *Sun* and *Province* were merged into Pacific Press.

The result was that the city was left with two papers owned by the same firm, which was owned equally by Sun Publishing and Southam. Substantial economies and a stronger morning newspaper were promised.

Large national advertisers were not significantly affected by the combination advertising policy, but local advertisers were adversely affected. Except for the increase in rates, local retail advertisers were not significantly affected. The RTPC concluded that the combined rate was detrimental to local advertisers, but that the increase in rates by the *Sun* "was nothing exceptional."¹⁹⁶

An agreement was made purportedly to establish and maintain the editorial independence of the two papers. On the matter of "an independent press and the public interest" the RTPC noted that, "when all the newspapers in a city come under single management, then the dangers of a single channel of communication become clearly evident."¹⁹⁷ But the Commission stated it "must accept the evidence . . . that as a business enterprise the *Province* did not have prospects of earnings which would lead its owners to continue its operations indefinitely."¹⁹⁸

Despite the claim of the general manager of Pacific Press after the merger, of savings of \$500,000 per year, the RTPC found that "An examina-

¹⁹³ *Id.* at 3-4.

¹⁹⁴ *Id.* at 79.

¹⁹⁵ Restrictive Trade Practices Commission, *Report Concerning the Production and Supply of Newspapers in the City of Vancouver and Elsewhere in the Province of British Columbia* (Ottawa: Queen's Printer, 1960).

¹⁹⁶ *Id.* at 160.

¹⁹⁷ *Id.* at 171.

¹⁹⁸ *Id.* at 175.

tion of the monthly and consolidated statements does not reveal any significant economies because of the consolidation of operations."¹⁹⁹ But the two papers jointly did earn higher profits than they had separately. No action was taken.

(d) Meat Packing²⁰⁰

The RTPC report followed an investigation by the Director of Investigation and Research which arose because of the acquisition in 1955 of Calgary Packers (the tenth largest meat packer in Canada) and Wilsil Ltd. (the fourth largest meat packer in Canada) by the largest packing firm, Canada Packers. Prior to 1955, Canada Packers together with the other two national packers, Burns and Swift, accounted for over fifty-three per cent of the total commercial slaughter (over sixty per cent of the cattle and over fifty per cent of the hogs) in Canada. By 1959 the big three accounted for over sixty per cent of both cattle and hogs.²⁰¹ Between 1955 and 1957 Canada Packers and its subsidiaries accounted for between 28.1 per cent and 29.7 per cent of the total commercial production of red meats in Canada.²⁰² In addition, very detailed evidence was presented showing a high degree of vertical integration by Canada Packers.²⁰³ The firm was the initiator in consulting competitors about price policy since the early 1930's. It had a history of coercive actions against competitors in all regions aimed at depressing meat prices or bidding up cattle prices. Since it was formed in 1927 as a combination of four firms, Canada Packers' published statements indicated profits much higher than the average for all firms in the meat-packing industry in Canada and the U.S.²⁰⁴ Plant economies of scale were found not to be significant. Nor were there significant economies of multiplant operation; the individual plants and divisions of Canada Packers were found to be run largely as separate businesses.²⁰⁵

The RTPC concluded that the two acquisitions

significantly lessened the competition previously existing in the trade in livestock on the markets where the purchases of Calgary Packers and Wilsil Limited were made and because of the inter-relationship of markets could be expected to lessen the competitive effect resulting from such independent buying on Canadian livestock markets generally. It also appears to the Commission to be likely that competition in the distribution of meat products was also lessened as a result of such acquisitions.²⁰⁶

The Commission recommended, in light of the *Beer* and *Sugar* decisions²⁰⁷ that a court order be obtained dissolving the mergers, or if unsuccessful, that an order be obtained prohibiting Canada Packers from making further

¹⁹⁹ *Id.* at 156.

²⁰⁰ Restrictive Trade Practices Commission, *Report Concerning the Meat Packing Industry and the Acquisition of Wilsil Limited and Calgary Packers Limited by Canada Packers Limited* (Ottawa: Queens Printer, 1961).

²⁰¹ *Id.* at 411.

²⁰² *Id.* at 447.

²⁰³ *Id.*, Ch. VII to XIV.

²⁰⁴ *Id.* at 389-407.

²⁰⁵ *Id.*, Ch. XX.

²⁰⁶ *Id.* at 427.

²⁰⁷ *Supra*, notes 40 and 41.

acquisitions which would lessen competition in the meat packing industry.²⁰⁸ After having the report reviewed by two outside counsel the Department of Justice declined to prosecute.

(e) Acquisition of Wilson Boxes by Bathurst Power and Paper²⁰⁹

In 1958 Bathurst and St. Lawrence Corporation, both integrated firms, accounted for sixty per cent of total shipments of shipping containers in Eastern Canada and were also important on the Prairies. These two were also the leading box-board mills. In 1954 Bathurst, St. Lawrence and Hinde and Dauch (wholly owned by St. Lawrence) supplied seventy-seven per cent of total domestic shipments made in Canada.²¹⁰

In December 1958, Bathurst bought a minority position in Maritime Paper Products, one of the two container plants in the region; the other was Wilson. For twenty years Bathurst and Wilson had an understanding that the former would have the right of first refusal if Wilson were put up for sale. In the Maritimes region the respective market shares were as follows:²¹¹

	<u>1959</u>	<u>1960</u>
Maritime Paper Products (minority interest held by Bathurst)	52.4%	47.6%
Wilson Boxes	45.3	38.6
Hygrade	2.4	13.9

In light of the decisions in the only two litigated merger cases, the RTPC concluded: "On the basis of shipping container production therefore, Bathurst as a result of acquiring Wilson, was not in a position to carry on its business virtually free from the influence of competition,"²¹² despite the fact that it controlled eighty-six per cent of production in 1960.

The Commission stated that the dissolution of mergers could not be relied upon to effect the restoration of competitive conditions in the shipping container industry.²¹³ As in the *Shipping Containers Report*,²¹⁴ the RTPC recommended changes be made in tariffs to restore competitive conditions. The Crown neither prosecuted nor lowered the tariffs.

(f) Propane²¹⁵

The RTPC report was concerned with merger and monopoly by Rockgas Propane and its parent Great Northern Gas Utilities as well as a combination

²⁰⁸ *Supra*, note 200 at 430.

²⁰⁹ Restrictive Trade Practices Commission, *Report Concerning the Acquisition by Bathurst Power and Paper Company Limited of Wilson Boxes, Limited* (Ottawa: Queen's Printer, 1962).

²¹⁰ *Id.* at 4.

²¹¹ *Id.* at 13.

²¹² *Id.*

²¹³ *Id.* at 14.

²¹⁴ Restrictive Trade Practices Commission, *Report Concerning the Manufacture, Distribution and Sale of Paperboard Shipping Containers and Related Products* (Ottawa: Queen's Printer, 1965).

²¹⁵ Restrictive Trade Practices Commission, *Monopoly in Distribution of Propane — British Columbia* (Ottawa: Queen's Printer, 1965).

and conspiracy by Rockgas and Shell to obstruct a new entrant: Western Propane in the Lower Mainland and Fraser Valley.

Between 1953 and 1961 Rockgas acquired five propane distributions in B.C.²¹⁶ One of the acquired firms, Bibby's, was about the same size as Rockgas and they were in close competition in all major market areas. The two combined had 90 per cent to 100 per cent of the five major markets in 1956. After Rockgas acquired Bibby's the only competitors were Industrial Propane in North Burnaby and Duncan Rockgas on Vancouver Island. Duncan Rockgas was purchased in 1958 leaving Rockgas with a monopoly on Vancouver Island as Industrial Propane was selling to special use customers. The result of these acquisitions was to give Rockgas a monopoly position in several markets.

The RTPC ruled "through their acquisition of competitors, Great Northern and Rockgas obtained substantial or complete control over the propane market . . ."²¹⁷ in five markets at various times between 1957 and 1961. In 1957 these regional markets made up 67.2 per cent of total propane sales in B.C. However, the RTPC made no recommendations as to the application of remedies provided in the *Combines Investigation Act*. The Crown did not prosecute.

(g) Cast Iron Soil Pipe²¹⁸

The RTPC Report was concerned with Anthes Imperial Ltd., the largest producer in Canada (its share of national market increased from 34.7 per cent in 1960 to 39.5 per cent in 1962 to 48.7 per cent in 1964) and Associated Foundry Ltd. (3.98 per cent in 1960, 9.02 per cent in 1963 and 11.11 per cent in 1964) in which Anthes held shares.

Canadian tariffs effectively insulated the domestic manufacturers. From 1960 to 1965 imports ranged from 0.6 to 2.6 per cent of domestic production.

In late 1962 Associated bought S.P. & F. Foundry Limited giving Associated a virtual monopoly in B.C. In May 1963 Anthes bought a one-sixth interest in Associated. It increased this to twenty per cent in December 1964 and received a seat on the board of directors.

On the basis that Anthes' share of the market from the Lakehead through Alberta increased from seventy-two per cent (1960) to seventy-eight per cent (1963) to ninety-two per cent (1964) the RTPC concluded that "Anthes was in substantial or complete control of the business of cast iron soil pipe and fittings manufacture [in the region] in the period January 1, 1952 to June 30, 1965."²¹⁹ With respect to Anthes' purchase of an interest in Associated the RTPC stated that it "eliminated possible competition between the two companies in British Columbia and in the Prairie market."²²⁰ They concluded

²¹⁶ *Id.* at 18.

²¹⁷ *Id.* at 69-70.

²¹⁸ Restrictive Trade Practices Commission, *Cast Iron Soil Pipe* (Ottawa: Queen's Printer, 1967).

²¹⁹ *Id.* at 78.

²²⁰ *Id.* at 87.

it "was a merger detrimental to the public," and recommended that Anthes be required to "divest itself of all interest in Associated."²²¹

On February 22, 1973 the Crown obtained an Order of Prohibition preventing Anthes from acquiring an interest in Associated (Anthes, after the release of the RTPC report, had sold its shares) and requiring it to licence competitors to manufacture its patented mechanical joints.²²²

(h) Discontinued Inquiries

During the period 1960/61 to 1974/75 a random sample of fifty per cent of the discontinued inquiries of the Director of Investigation and Research, were analyzed in some detail. Listed in Table 2 are data on the *completed* mergers which were *not* challenged by the Director. Because of confidentiality requirements, the firms, the industry or the year cannot be identified. The purpose of the list is to indicate, crudely at least, the impact of such mergers on the level of concentration in the relevant market.

Table 2
Impact of Mergers in Canada,
A 50% Sample of Discontinued Inquiries, 1960-1975²²³

Merger	Market Share of		Change in Concentration
	acquiring firm	acquired firm	
A	28%	39%	67/2 to 67/1
B (i)	18	11	83/3 to 94/3
(ii)	25	12	79/3 to 91/3
C (i)	18	6	n.a.
(ii)	23	18	n.a.
D	new entrant	m 90+	95/3 to 95/1
E (i)	31	9	n.a.
(ii)	21	9	n.a.
(iii)	40	15	n.a.
F	n.a.	n.a.	100/8 to 80/1
G	12	9	n.a.
H	44	16	73/3 to 84/3
I	<1	m 21	still low
J	48	7	low, imports very significant
K	62	10	100/3 to 100/2
L	12	4	n.a.
M	33	49	96/3 to 96/2
N (i)	35	26	n.a.
(ii)	43	18	n.a.
(iii)	50	11	n.a.

Notes: n.a. = not available; m = more than one firm acquired at same time; (i), (ii) etc. = various regional markets.

²²¹ *Id.*

²²² *Report of the Director of Investigation and Research, Combines Investigation Act for the year ended March 31, 1973, supra, note 9 at 47.*

²²³ Source: This was completed as part of a larger study on the administration and enforcement of the *Combines Investigation Act* being conducted by the author and Paul K. Gorecki of the Bureau of Competition Policy.

While these are but summary statistics, the market share of the firm resulting from the merger in many of the cases would surely qualify as economically significant and worthy of a more detailed investigation. However, given the unfavourable decisions in the *Beer* and *Sugar* cases,²²⁴ the Director did not prosecute. In light of the data in Tables 1 and 2, and the seven case studies discussed above, it seems that the report's assertion that mergers in Canada have not given rise to important consequences for the economy is open to serious challenge.

One might add another point to their treatment of mergers. Skeoch and McDonald see mergers occurring as the result of the pressure of exogenous market forces impelled by fundamental changes in technology, organization and shifts in tastes. Yet the drive for size (independently of profitability), the role of merger promoters, stock market booms, and purely pecuniary tax considerations all play a prominent role in the analysis of major merger movements. Reuber and Roseman state that for the period 1945-1961 about ninety-two per cent of the year-to-year variation in the number of foreign mergers in Canada can be explained by the number of mergers occurring in the U.S., the supply of internally generated corporate funds in Canada and the number of commercial failures in Canada.²²⁵ Only two variables, variations in Canadian stock market prices and variations in the supply of internally generated funds in Canada, explain eighty-nine per cent of the year-to-year variation in the number of domestic mergers.²²⁶

The authors place considerable emphasis on the economic benefits associated with mergers. Reuber and Roseman indicate that "[n]egligible or no economies were reported in fifty-six per cent of the foreign acquisitions and in forty-one per cent of the domestic acquisitions."²²⁷ Of the reported reasons for the merger, "to achieve economies of scale or to reduce costs" was ranked as the most important reason in only 1.3 per cent of foreign mergers and 5.0 per cent of domestic mergers. Of all the reasons given, (allowing for multiple reasons) economies of scale or reduction of costs accounted for 4.7 per cent of the reasons given for foreign mergers and 7.1 per cent of those for domestic mergers.²²⁸ Where such economies or cost reductions did occur they most frequently took the form of "economies in administration."²²⁹ As for the significance of economies or cost savings Reuber and Roseman conclude that they were not an important consideration.²³⁰

²²⁴ *Supra*, notes 40 and 41.

²²⁵ *Supra*, note 35 at 28. For another view, see C. J. Maule, *Anti-Trust and Take-Over Activity of American Firms in Canada* (1968), 11 *Journal of Law and Economics* 423. Reuber's comment is contained in (1969), 12 *Journal of Law and Economics* 405; Maule's rejoinder in (1969), 12 *Journal of Law and Economics* 419; and Reuber's reply in (1970), *Journal of Law and Economics* 257.

²²⁶ *Id.* at 29.

²²⁷ *Id.* at 96.

²²⁸ *Id.* at 78.

²²⁹ *Id.* at 95.

²³⁰ *Id.* at 97.

Finally, Skeoch and McDonald appear to be incapable of recognizing a possible divergence between the social desirability of at least some business combinations and the private benefits accruing only to the participants. As Milton Moore has pointed out, it is usually assumed that there is an efficiency basis for corporate mergers: "specifically that the purpose is to increase the profits of the acquiring company or the two companies both of whom voluntarily merge by lowering costs or effecting other economies."²³¹ But, he goes on, "while the profit motive is usually present, it is not necessarily the profit of shareholders and more importantly that effecting economies in production is rarely realized or intended . . . the objectives are increased market power, the increase or protection of market shares, conglomerate size and diversification and sometimes capital gains for those who manage the merger or engineer the takeover."²³² With respect to the market for business enterprises, Moore argues:

Almost any evidence supporting the conclusion that the market for companies operates to the benefit of the public interest is accepted, but proof positive beyond the peradventure of a doubt is required for evidence of public detriment to be accepted.²³³

If the social benefits of mergers are significant, let them be demonstrated at least in terms of pragmatic predictions. But more importantly, let them be shared with consumers. Skeoch and McDonald's draft legislation makes no requirement that the alleged benefits of mergers be passed on to the public as was the case in Bill C-256. It provided that a merger would not be dissolved if it "has led, is leading or likely to lead to a significant improvement in efficiency . . ." and "a substantial part of the benefits derived or to be derived from such improvement of efficiency are being or are likely to be passed on by the market or by order of the Tribunal, to the public within a reasonable time in the form of lower prices or better products."²³⁴ The weighing of enhanced artificial restraints against real-cost economies as the result of a merger recognizes the double-edged nature of many mergers in this country. But if we are to tolerate enhanced artificial restraints, the effects of which will be passed on to the public, we should also insist that the offsetting real-cost economies also be demonstrably passed on.

4. *Mergers and Foreign Ownership*

With exception of their brief critique of the *Foreign Investment Review Act*,²³⁵ one could *not* tell from reading the Skeoch and McDonald report that the extensive foreign ownership of the Canadian economy has been a major

²³¹ Milton Moore, "Mergers and Price Agreements," in *Canada's Competition Policy* (Ottawa: The Conference Board in Canada, 1972) at 25.

²³² *Id.* at 25, 26.

²³³ Milton Moore, *How Much Price Competition?*, *supra*, note 175 at 10.

²³⁴ Bill C-256, *The Competition Act*, first reading June 29, 1971, s. 34(3).

²³⁵ *Foreign Investment Review Act*, 1973-74, c. 46.

issue in the political economy of the nation in the last decade. Skeoch and McDonald are oblivious to the issues raised in the Watkins' Report,²³⁶ the Wahn Committee Report,²³⁷ and the Gray Report.²³⁸ The same could be said of the writings of Safarian,²³⁹ Levitt,²⁴⁰ Litvak and Maule,²⁴¹ Hymer,²⁴² and Rotstein.²⁴³ The point is that when Skeoch and McDonald argue that take-overs of Canadian enterprises by foreign firms should be handled in exactly the same way as domestic mergers with their emphasis on the efficacy of market forces, they ignore the trade-off between efficiency and foreign control many Canadians seem to wish to make. They imply, in the context of a complex, multi-attribute decision problem, that a dominant solution exists, namely theirs. They apparently view the preferences of nation states as another artificial restraint imposed by government upon the inexorable forces of the market, operating through the multinational and national enterprise, to bring us all the good things of life through dynamic change. The report argues strongly against the use of doctrinaire theory and praises informed judgement as a means of weighing a variety of complex uncertain costs and benefits. Yet, the authors ignore the issue of foreign ownership, one which the majority of Canadians would consider most important. They ignore the socio-political opportunity cost of adopting their merger rules in an economy where foreign ownership, rightly or wrongly, is an issue which competition policy must take into account.

²³⁶ Report of the Task Force on the Structure of Canadian Industry, *Foreign Ownership and the Structure of Canadian Industry* (Ottawa: Queen's Printer, 1968).

²³⁷ *Eleventh Report of the Standing Committee on External Affairs and National Defence Respecting Canada-U.S. Relations* (Ottawa: Queen's Printer, 1970).

²³⁸ Government of Canada, *Foreign Direct Investment in Canada* (Ottawa: Information Canada, 1972).

²³⁹ A. E. Safarian, *Foreign Ownership of Canadian Industry* (Toronto: McGraw-Hill, 1966); ———, *The Performance of Foreign-Owned Firms in Canada* (Montreal: Private Planning Association of Canada, 1969).

²⁴⁰ Kari Levitt, *Silent Surrender: The Multinational Corporation in Canada* (Toronto: Macmillan, 1970).

²⁴¹ I. A. Litvak and C. J. Maule, eds., *Foreign Investment: The Experience of Host Countries* (New York: Praeger, 1970); ———, *The Multinational Firm and Conflicting National Interests* (1969), 3 *Journal of World Trade Law* 309; I. A. Litvak, C. J. Maule and R. D. Robinson, eds., *Dual Loyalty: Canadian-U.S. Business Arrangements* (Toronto: McGraw-Hill, 1971).

²⁴² Stephen Hymer, "International Operations of National Firms — A Study of Direct Foreign Investment," Unpublished Ph.D. Dissertation, Massachusetts Institute of Technology, 1960; ———, "National Policies Toward Multinational Corporations," Background Paper for *Foreign Ownership and the Structure of Canadian Industry*, *supra*, note 235.

²⁴³ Abraham Rotstein, *Continentalism vs. Nationalism* (Toronto: The Ontario Woodsworth Memorial Foundation, 1967); Abraham Rotstein and Gary Lax, eds., *Independence: The Canadian Challenge* (Toronto: The Committee for an Independent Canada, 1972). Additional contributions in the same vein include, Gunnar Adler-Karlsson, *Reclaiming the Canadian Economy: A Swedish Approach Through Functional Socialism* (Toronto: House of Anansi, 1970); D. W. Carr, *Recovering Canada's Nationhood* (Ottawa: Carr Publishing Company, 1971); D. Godfrey and M. Watkins, eds., *Gordon to Watkins to You: A Documentary: The Battle for Control of Our Economy* (Toronto: New Press, 1970); W. H. Pope, *The Elephant and the Mouse: A Handbook on Regaining Control of Canada's Economy* (Toronto: McClelland and Stewart, 1971).

5. *The Acceptance of Monopoly Power*

Characteristic of the authors' conservative approach to competition policy is their complete acceptance of the existing concentrations of economic power and protected positions. We are given six reasons why it is not possible to attack existing centres of market power, but not one argument why it may be desirable to do so. The status quo with all its attendant effects on efficiency and distribution is safe, provided the holders of monopoly power do not abuse it. The approach and the language is remarkably similar to Mackenzie King's when he introduced the first *Combines Investigation Act* in 1910:

I would like the House to understand that in introducing this legislation no attempt is being made to legislate against combines, mergers, and trusts as such. . . .²⁴⁴

The legislation would permit the examination of firms "where there is reason to believe that a combine is operating to an undue disadvantage of the public."²⁴⁵ Note that the disadvantages to the public must become "undue" before action is to be taken.

As Milton Moore has remarked, a "most formidable barrier to social change is the disposition to stay with the devil we know rather than the devil we don't know. The costs of change tend to be overestimated."²⁴⁶

Having endorsed the abuse theory of monopoly power, Skeoch and McDonald propose to attack some of its symptoms (undesirable business conduct) while leaving its fundamental cause (market structure) untouched. While it is possible that the effective prohibition of conduct restraints may, given sufficient time, result in a withering away of monopoly power, it will be a slow process. "Dynamic change" may require the patience of Job. What about the dominant firm, or group of firms, which does not "create or enhance significant artificial restraints," but rather exists behind important product differentiation barriers to entry? This situation would appear to be beyond the reach of their proposals.

The report's treatment of monopoly and the misuse of dominant position, including their draft legislation, suffers from a disease identified by one of the authors in respect of the *Interim Report on Competition Policy*. B. C. McDonald asserted that "the single most striking feature of the Report is the generality with which it deals with central substantive issues. It is imperative to generalize, of course, but usually impractical to stop at generalities."²⁴⁷ Despite this diagnosis and prescription, Skeoch and McDonald's thirty page discussion of monopoly has but one reference to a specific Canadian case and that is to a marketing board decision. Their proposed legislation is not assessed in terms of such significant cases as *R. v. Canadian General Electric*

²⁴⁴ Cited in L. A. Skeoch, *Restrictive Trade Practices in Canada* (Toronto: McClelland and Stewart, 1966) at 23-24.

²⁴⁵ *Id.* at 24.

²⁴⁶ *Supra*, note 175 at 11.

²⁴⁷ Bruce C. McDonald, *Canadian Competition Policy: Interim Report of the Economic Council of Canada* (1970), 15 Antitrust Bulletin 529.

Co.,²⁴⁸ *Propane*,²⁴⁹ *R. v. K. C. Irving Ltd.*,²⁵⁰ *Zinc Oxide*,²⁵¹ *R. v. Hoffman-La Roche Ltd.*,²⁵² *R. v. Canada Safeway Ltd.*,²⁵³ *R. v. Allied Chemical Ltd.*,²⁵⁴ *Pesticides*,²⁵⁵ *Erco*,²⁵⁶ and *Ammunition*.²⁵⁷ McDonald's criticism of the *Interim Report* is equally appropriate here:

In view of its generality in several areas which cry out for more specific treatment, the Report has a hollow ring when it pleads for clarity and precision in the law.²⁵⁸

The failure to address specific Canadian cases in their analysis of monopoly and the power of dominant firms is unsatisfactory. The draft legislation is very general and subject to great discretion in interpretation.

Finally, what are the implications of the National Markets Board's remedial orders? It is highly unlikely that they will strike at the structural characteristics which engender the monopoly power. Rather, one would expect them to be aimed at prohibiting certain forms of business conduct. It is unlikely that many of these orders will be effective. To make them effective will require the kind of detailed intervention and regulation of business actions that Skeoch and McDonald find most abhorrent. There are simply too many ways to get around the typical injunction if the benefits of the restraint of trade are sufficiently alluring.

6. *Rationalization, Specialization and Export Agreements*

Export agreements are now permitted, with certain exceptions, under section 32(4) of the *Combines Investigation Act*.²⁵⁹ This provision would

²⁴⁸ Restrictive Trade Practices Commission, *Electric Large Lamps* (Ottawa: Queen's Printer, 1971); *R. v. Canadian General Electric Co. Ltd.* (Unreported) Supreme Court of Ontario, Toronto, September 2, 1976, Bureau of Competition Policy, mimeo 253-1.

²⁴⁹ *Supra*, note 215.

²⁵⁰ *R. v. K. C. Irving Ltd.* (1974), 45 D.L.R. (3d) 45; 16 C.C.C. (2d) 49; 13 C.P.R. (2d) 115; 7 N.B.R. (2d) 360. Rev'd. (1975), 62 D.L.R. (3d) 157; 23 C.C.C. (2d) 479; 20 C.P.R. (2d) 193; 11 N.B.R. (2d) 181. Supreme Court of Canada, (Unreported), November 16, 1976, Bureau of Competition Policy, mimeo 135-5.

²⁵¹ *Supra*, note 189.

²⁵² *R. v. Hoffman-La Roche Limited*, (Unreported), Provincial Court (Criminal Division), Judicial District of York, May 20, 1976, Bureau of Competition Policy, mimeo 252-1.

²⁵³ *R. v. Canada Safeway Ltd.* (1973), 12 C.P.R. (2d) 3.

²⁵⁴ *R. v. Allied Chemical Ltd.* (1975), 6 W.W.R. 481.

²⁵⁵ Restrictive Trade Practices Commission, *Distribution and Pricing of Pesticides* (Ottawa: Queen's Printer, 1965).

²⁵⁶ Restrictive Trade Practices Commission, *Trade Practices in the Phosphorous Products and Sodium Chlorate Industries* (Ottawa: Queen's Printer, 1966).

²⁵⁷ Restrictive Trade Practices Commission, *Report Concerning the Manufacture, Distribution and Sale of Ammunition in Canada* (Ottawa: Queen's Printer, 1959).

²⁵⁸ *Supra*, note 247 at 543.

²⁵⁹ The exceptions are cases where the conspiracy, combination, agreement or arrangement (a) has resulted or is likely to result in a reduction or limitation of the volume of exports of a product; (b) has restrained or injured or is likely to restrain or injure the export business of any domestic competitor who is not a party to the conspiracy; (c) has restricted or is likely to restrict any person from entering into the business of exporting products from Canada; or (d) has lessened or is likely to lessen competition unduly in relation to a product in the domestic market. S. 32(5).

not be affected by the report's proposals in this regard. The trouble with export agreements is that it is impossible to see how an agreement to fix prices in a foreign market could possibly result in lower prices to domestic consumers. Despite the condition that such agreements must not lessen domestic competition unduly, one must be mindful of Adam Smith's maxim that men of the same trade seldom meet together, even for merriment or diversion, but that it ends in a conspiracy against the interest of the public!

By placing the initiative for creating rationalization and specialization agreements on the firms, Skeoch and McDonald may well be adopting a cynical, but highly desirable approach. As D. H. W. Henry pointed out in 1969, what businessmen seem to have in mind by such agreements

is some form of agreement or understanding whereby, perhaps with the assistance of government, the industry, as opposed to individual firms, will somehow be re-organized on such a basis that the economies of scale are achieved. This . . . seems to call for an allocation of markets between the existing firms so that each would specialize in particular products . . . hopefully achieving economies of scale. . . . Such an agreement, however, would require that the various firms should not step outside their allocated product or market areas. . . . In the few proposals that I have seen, this would result in a virtual monopoly of particular products by particular firms . . . [and] would quite clearly raise grave questions under the Combines Act. . . .²⁶⁰

Skeoch and McDonald may be cynical, because of the difficulty, without government initiative or assistance, in formulating such agreements *and* in satisfying the constraints they propose. Mr. Henry, whose programme of compliance and "open door" policy put him in a good position to know, has observed:

This is a field . . . in which there has been a great deal of talk and no action. Businessmen have extolled in generalities gains to be achieved by this type of rationalization, but except in a very few cases have not taken the trouble to sit down and work out exactly what arrangements are both feasible and likely to be successful.²⁶¹

In the event that a rationalization and specialization agreement does come forward, it is presumptively legal until challenged by the Director of Investigation and Research. However, the report does not specify the criteria by which such agreements are to be appraised. While greater efficiency may be attained, a laudable allocative objective, what guarantees are there that consumers will share in the benefits?

7. Basing-Point Pricing

The authors underestimate the significance of delivered pricing schemes (including basing-point systems) as devices to facilitate oligopolistic coordina-

²⁶⁰ D. H. W. Henry, *Mergers, Rationalization and Specialization Agreements* (1969), 8 *Western Ontario Law Review* 123 at 131-32.

²⁶¹ *Id.* at 132. For an example of business' views on rationalization and specialization agreements see, Douglas I. W. Bruce, "Rationalization and Foreign Ownership under Bill C-256," in *Canada's Competition Policy*, *supra*, note 231 at 34 and 39. An academic's view is given by H. E. English, "Specialization and Export Agreements: Their Potentials and Limitations," in L. A. Skeoch, ed., *Canadian Competition Policy*, *supra*, note 21 at 28.

tion in the form of uniform delivered prices. Such schemes are most significant when the number of basing points is much smaller than the number of plants, where the product is homogeneous (or nearly so) and where freight costs are a significant part of the delivered price. Moore argues that "mandatory f.o.b. pricing be made applicable only where the freight cost exceeds 5 per cent of the wholesale price."²⁶² Skeoch and McDonald are too quick to reject mandatory f.o.b. pricing or at least requiring that the buyer have the option. Professor Moore asserts:

[M]andatory f.o.b. pricing would create conflicts of interests among the members of an oligopoly industry, which would tend to weaken the adherence to cooperative pricing practices and thus introduce some degree of price competition. A firm could not increase its sales except by decreasing its milldoor prices.

All forms of basing-point pricing result in wasteful cross-hauling. . . . Basing-point pricing often imposes obstacles in the way of the attraction of additions to plant capacity to their least-cost locations.²⁶³

Having carefully reviewed the issue of conscious parallelism in Canadian combines cases,²⁶⁴ it is apparent that basing-point and related delivered pricing schemes are an integral part of the serious problem of non-collusive oligopolies. In *R. v. Canada Cement Lafarge Ltd.*,²⁶⁵ Camblin, Prov. Ct. J. indicated that prior to the mutual adoption of a basing-point pricing scheme price competition was active. As he put it, "one finds the marketing arrangements to be in a somewhat chaotic condition due, among other problems, to the incongruous freight allowances."²⁶⁶ In *R. v. Armco Canada Ltd.*,²⁶⁷ price competition was eliminated for almost four years following the adoption of an open pricing policy coupled with delivered pricing in three zones in Ontario. Mr. Justice Lerner stated:

[the] producers divided Ontario into three zones and all prices quoted were a "delivered" price in each zone rather than FOB plant. All prices were uniform in any zone regardless of the distance of the plant of the particular manufacturer from the geographical point of delivery.²⁶⁸

In the recent case of *R. v. Atlantic Sugar Refineries Co. Ltd.*,²⁶⁹ all six Eastern refiners, led by the big three with ninety per cent of the market, used basing-point pricing. Three cities where the major refineries are located, Toronto, Montreal and St. John act, as basing-points. For all practical purposes, identical delivered prices prevail throughout the country as B.C. Sugar, which has a monopoly from Manitoba west, uses the same system. The system was defended by Mackay J.:

The abolition of the basing point pricing and freight absorption system would probably result in Atlantic's confinement to the Maritimes, St. Lawrence com-

²⁶² *Supra*, note 175 at 165.

²⁶³ *Id.* at 166.

²⁶⁴ W. T. Stanbury and G. B. Reschenthaler, *Oligopoly and Conscious Parallelism: Theory, Policy and the Canadian Cases* (1977), 15 Osgoode Hall L.J. (forthcoming).

²⁶⁵ (1973), 12 C.P.R. (2d) 14.

²⁶⁶ *Id.* at 14.

²⁶⁷ *Supra*, note 112.

²⁶⁸ *Id.*, (1975), 6 O.R. (2d) at 565.

²⁶⁹ *R. v. Atlantic Sugar Refineries Co. Ltd.*, (Unreported), Superior Court of Quebec (Criminal), December 19, 1975, Bureau of Competition Policy, mimeo 243-1.

peting with Redpath only in Quebec, and the latter in sole control of the lucrative Ontario market. Whatever be the validity of the criticism of this system as it operates in the United States, by such eminent American economic authorities as Messrs. Joel Dean and F. M. Scherer, who believed that it is preferable to restrict manufacturers to their own manufacturing areas, we in Canada believe that manufacturers in the Atlantic Provinces and in the West ought to have access to the lucrative Quebec and Ontario markets, access which is but only imperfectly achieved by the basing point and freight absorption system. Judicial support for the system may be found in the *B.C. Sugar Case* . . . and in *Regina v. Canada Cement Lafarge*. . . .²⁷⁰

At the very least, delivered pricing schemes ought to be a reviewable trade practice such as refusal to supply, consignment selling, market restriction etc. Why should it be necessary, as Skeoch and McDonald propose, to first convict a group of firms of a conspiracy to lessen competition unduly before finding that oligopolistic coordination is facilitated by such schemes?

8. *Administration and Adjudication*

By far the most praiseworthy proposal advanced by the report is its strong recommendation that civil procedures be introduced into the implementation of competition policy. The concept, structure, and powers of the specialized adjudicating body are generally unobjectionable. It is time that the analysis of the cases and the remedies made economic sense. After all, these are economic offences in restraint of trade. The authors' insistence that the Board operate with the benefit of a clear statement of objectives, as difficult as they may be to implement in practical terms, makes a policy analyst's heart warm. However, some of the details of their proposals might be questioned.

First, apparently in a desire to make "the tribunal" acceptable to businessmen, Skeoch and McDonald wish to see the majority of the Board comprised of business executives. Who else will have the requisite "extensive private sector experience" and will have the necessary "informed common sense," rather than simply "cloistered expertise"? Academics specializing in the field of industrial organization and competition policy might find it hard not to feel defensive about the report's repudiation of their kind. At last report the distinguished professors sitting on the Monopolies Commission in the U.K. were not thought to be wildly impractical and incapable of understanding the ways of the business world. Skeoch and McDonald's emphasis on having businessmen on the NMB seems to fall prey to what Robert Solo has called "the myth of the borrowed businessman."

In times of trouble when society demands action and politicians need guidance, there will always come, according to the myth, the good dollar-a-year man to be borrowed from business to do the job. He knows his stuff. Only ask his advice, or bring him in and turn him loose. Make a "czar" of him. In his goodwill, skill, and wisdom, he is sure to put things right.

In sum, when the politicians are finally cornered and the President is at the end of his tether, and the answers cannot be found either in the law books or at the polls, then the "know-how" that is required to plan for and deal with the or-

²⁷⁰ *Id.* at 96.

ganizational sector can always be borrowed from or hired out of the entities that compose that sector.²⁷¹

Without at least some theoretical economic expertise how will the Board be able to implement, for example, the proposed criteria for determining whether price discrimination has occurred? They define it to be when sales are made "at less than the reasonably anticipated long-run average cost of production and distribution"²⁷² and where such sales have adversely affected competition. Where informed judgement and considerable discretionary powers are to be exercised it does not seem unreasonable that at least a significant minority of the NMB have a strong conceptual and analytical bent coupled with a modicum of specialized knowledge. But the issue is more general as Solo points out:

More fundamentally, the competence itself — the knowledge, skills, and outlook as these develop; and the strategies of action and the criteria of choice as these are learned through the experience of business management and agency operations, or ingrained through training and in the winnowing process of recruitment and promotion — is of a wholly different character and quality than that which is needed for social and economic planning and control in the public interest. Both the operations manager and the social-economic planner will require some mastery of the relevant technologies, and of the sciences related to them, but the two capabilities need to develop separately in the context of different outlooks oriented toward different purposes, drawing upon different reference values, and incorporating different criteria of evaluation.²⁷³

Skeoch and McDonald would, of course, reject the notion that members of the NMB will be "social-economic planners." Yet they will have great discretion in their interpretation of legislation which is expressed in rather general terms. The potential impact of their decisions, for good or evil, will be significant. Is it desirable that the views of "practical businessmen" be given this much weight?

Second, one wonders whether prohibition orders and even remedial orders are sufficient remedies to make restraints of trade unprofitable. If a firm or group of firms can reap substantial economic gains before they are investigated, "tried," and made subject to a prohibition order, is the latter sufficient to both stop the undesirable behaviour and to deter other potential offenders or repetition of the offence? Will the economic sanctions available to the NMB be sufficient? Elsewhere, this writer has argued that "crime," in the form of illegal restraints of trade, is profitable.²⁷⁴ Can the Board's conduct-oriented remedies be enforced in practical terms? Who will oversee its orders? If the supervision of consent decrees in the U.S. is any guide we should not be optimistic about the proposed procedures.²⁷⁵

²⁷¹ Robert A. Solo, *The Political Authority and the Market System* (Cincinnati: South-Western Publishing Co., 1974) at 304. By the "organizational sector," Solo is referring to "large scale manufacturing where the primary producing-distributing agencies are very large corporations, each employing many thousands of persons."

²⁷² *Supra*, note 1 at 217-18.

²⁷³ *Supra*, note 271 at 305.

²⁷⁴ W. T. Stanbury, *Penalties and Remedies Under the Combines Investigation Act, 1889-1976* (1976), 14 Osgoode Hall L.J. 571.

²⁷⁵ Mark J. Green *et. al.*, *The Closed Enterprise System* (New York: Bantam Books, 1972), Ch. 6, "When Winning is Losing: Civil Enforcement."

Third, the authors' discussion of private civil actions, including class actions,²⁷⁶ is disappointing. While refusing to get drawn into a proper debate on the efficacy of such actions in regard to the deterrence of restraints of trade and the prevention of unjust enrichment, they nevertheless specify a number of their concerns over such procedures and urge great caution in implementing them.

Care must be taken that [private civil actions] not be structured on the basis of oversimplified notions of pricing processes, the working of markets and the application of business revenues, lest some enormously difficult questions calling for quite arbitrary judgments be imposed upon the courts.²⁷⁷

Again, the whole tone of their discussion is overwhelmingly negative. Because the issues are complex, the status quo is not to be disturbed. On this point McDonald's earlier criticism of the Economic Council is applicable: "the Report is somewhat unimaginative on the subject of enforcement and remedies. There is practically no discussion of the role private initiative can play in the total enforcement effort. . . ." ²⁷⁸

Fourth, Skeoch and McDonald have endorsed the Department of Justice's monopoly on the initiation of criminal prosecutions in the Federal government on the grounds that it may be used too aggressively by single-minded investigators and policymakers. But how is the public, the victim of illegal restraints of trade, to be protected against the demonstrated lack of enthusiasm of the Department of Justice for combines cases or their extensive capacity to repeatedly "review" and delay justifiable prosecutions? It is apparent that senior officials in the Bureau of Competition Policy have been frustrated by Justice's diffidence and delay in pressing cases. Combines work forms a very small proportion of Justice's total workload. The small absolute number of such cases (excluding misleading advertising cases) per year means that few Crown prosecutors have much knowledge in the area or much sympathy for combines cases. As such cases are usually complex (e.g., requiring lawyers to become familiar with certain aspects of economics) and frequently protracted, they reduce the apparent "output" of Crown lawyers. Competition policy cases would be better served by having the Director of Investigation and Research develop a small specialized legal staff (together with selected outside counsel) and permitting him to lay charges directly. If he oversteps his prosecutorial role and brings cases without merit no doubt the judges at the Preliminary Hearings will make this point painfully apparent. At the very least, the Director ought to be able to proceed to court on his own if the Department of Justice takes an inordinate amount of time to decide on whether it should proceed.

Fifth, in their proposal to allow appeals to the Cabinet within sixty days on any order of the National Markets Board, Skeoch and McDonald are inviting the companies affected by the order to marshal their lobbying and public opinion forces to reverse rulings which are likely to have a significant

²⁷⁶ *Supra*, note 1 at 324-27.

²⁷⁷ *Id.* at 324-25.

²⁷⁸ *Supra*, note 247 at 538.

impact. We will observe the pushing and shoving of organized interest groups as such "raw political questions" are resolved.²⁷⁹ Appeals on the grounds provided by the *Federal Court Act* are necessary and desirable, but in the report's own words, it would "risk defeating the entire purpose of the specialized Board to permit [the Cabinet] to substitute [its] views as to proper judgments concerning . . . the design of the remedy."²⁸⁰ If the cumulative irritation with the decisions of the Board is sufficient, it will be abolished or significantly modified by the Government, existing or newly elected. In the meantime responsibility should remain with the Board.

E. SUMMARY

The criticisms articulated in the last half of this paper should be placed in a larger context. Compared to existing legislation and its operational impact, the report's proposals with respect to mergers, monopoly and the market power of dominant firms, price discrimination and the process of administration and adjudication represent a desirable set of changes. While they move in the right direction, they do not go far enough. A close reading of the litigated cases, RTPC reports, the inquiries discontinued by the Director, the Canadian empirical work in industrial organization and various studies of Canadian industries makes it clear that a stronger approach to competition policy is warranted.

²⁷⁹ See, W. T. Stanbury, *Business Interests and the Reform of Canadian Competition Policy, 1971-1975* (Toronto: Methuen, 1977).

²⁸⁰ *Supra*, note 1 at 310.