

Oligopoly and Conscious Parallelism: Theory, Policy and the Canadian Cases

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OLIGOPOLY AND CONSCIOUS PARALLELISM: THEORY, POLICY AND THE CANADIAN CASES

By W. T. STANBURY†
and
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The nature of modern markets dictates certain parallel conduct areas among oligopolists, irrespective of law, of the existence of conspiracies or of business intent.¹

A complete generation of economists has pointed out the idiocy of the charge of conscious parallelism.²

"Conscious parallelism" is nothing more than a very fancy term to describe the situation where two (or more) persons are doing the same thing with the knowledge that the other is following similar policies or has made a similar decision. . . . "Conscious parallelism" does not prove a conspiracy in the absence of other evidence which shows the seller's pricing was not explainable in terms of their individual self-interest and their independent business judgment.³

A. INTRODUCTION

One of the most perplexing problems in competition policy and in the general area of public policy toward industrial concentration arises with respect to the behaviour of industries in which a relatively small number of firms account for a large proportion of output⁴ and develop a strong bond of mutual dependence. In closely coordinated oligopolies, both the interfirm behaviour and economic performance may deviate significantly from that expected under competitive market conditions because firms in such oligopolies are able to act upon their interdependence.

If the firms are selling a relatively undifferentiated product, it is likely that all firms will charge almost the same prices or set prices which reflect differences in the value of services provided, including intangible services such as provision of a dependable source of supply. Little price deviation is expected. No firm will attempt to charge more than the established industry price since, under normal circumstances, no customers will pay the higher price. Producers will be discouraged from charging less by an awareness that major competitors, faced with the threat of market share erosion, will immediately match the lower prices. As Donald Eldon points out, "the simple awareness of the probable actions of competitors . . . tend[s] to limit price competition in markets of a few sellers."⁵ This type of industrial structure will normally produce identical list prices and virtually identical transactions prices. Price adjustments upward may occur almost simultaneously, without any formal agreement.

¹ R. E. Low, *Modern Economic Association* (Homewood: R. D. Irwin, 1970) at 255.

² Martin Shubik, *Strategy and Market Structure* (New York: John Wiley and Sons, 1959) at 285-86.

³ E. E. Pollock, *Commentary* (1975), 44 Antitrust L.J. 235 at 236.

⁴ In manufacturing, mining, finance, food retailing and other sectors oligopoly or concentrated industries are all but ubiquitous. See, for example, *Industrial Organization and Concentration in the Manufacturing, Mining and Logging Industries, 1972*, Catalogue 31-402 (Ottawa: Statistics Canada, 1977); E. P. Neufeld, *The Financial System of Canada* (Toronto: MacMillan, 1972); Reference Paper No. 6, Bruce Mallen, *A Preliminary Paper on the Levels, Causes and Effects of Economic Concentration in the Canadian Retail Food Trade: A Study of Supermarket Market Power* (Ottawa: Food Prices Review Board, 1976) and C. Marfels, *Concentration Levels and Trends in the Canadian Economy, 1965-73* (Ottawa: Royal Commission on Corporate Concentration, 1977).

⁵ Donald Eldon, *The Oligopoly Problem in Competition Policy*, Background Study for the *Interim Report on Competition Policy* (Ottawa: Economic Council of Canada, 1970) at 151 (mimeo).

In industries where there are a sufficient number of firms to minimize the effect of interdependence, there is less need to closely coordinate interfirm behaviour. The large number of competitors also makes coordination more difficult. Under such circumstances, more formal arrangements are usually necessary to coordinate the firms' behaviour and to provide assurance that participants in the agreement abide by it. Such express agreements are susceptible to attack under existing anti-combines legislation. Formal meetings and/or the exchange of documents are likely to be involved; these are the elements usually relied upon to prove the existence of a criminal conspiracy. Even where an express agreement is not found, it may be possible from the circumstantial evidence to infer an agreement.

However, some of the most serious instances of the joint exercise of market power by a small number of firms involve behaviour which may not constitute an agreement within the definition of a criminal conspiracy. This is the phenomenon of conscious parallelism in which the behaviour of the leading firms in an oligopoly is closely coordinated without overt collusion or agreement.

1. *Definition of Conscious Parallelism*

The term "conscious parallelism" does not have a single definition. Economist R. B. Heflebower states that "[c]onscious' refers to awareness of rivalry with particular firms and of their action, or nonaction, from which emerges 'parallelism', or the advisability of doing as rivals do."⁶

The U.K. Monopolies Commission, in its report on parallel pricing, described the phenomenon in a very general way "as the practice by which two or more sellers change their prices at or about the same time and by the same or similar amount or proportion."⁷ The Commission points out that in oligopolies, "[p]rice changes may be initiated only when there is good reason to expect that all sellers will benefit from a similar change, whether the change is upwards or downwards."⁸ This is in contrast to markets populated by a large number of sellers, where "each will change his prices independently if it is in his own best interests to do so without conscious consideration of the decisions of others."⁹

In an oligopoly, the awareness of interdependence by the leading firms is well-recognized. "However, the crucial fact which the sellers must face when each has a significant share of the market is that the decisions of all the sellers in the industry are interdependent, but information about rival sellers' intentions is imperfect."¹⁰ The Monopolies Commission report argued

⁶ R. B. Heflebower, "Conscious Parallelism and Administered Prices" in Almarin Phillips, ed., *Perspectives on Antitrust Policy* (Princeton: Princeton University Press, 1962) at 91.

⁷ United Kingdom Monopolies Commission, *Parallel Pricing: A Report on the General Effect on the Public Interest of the Practice of Parallel Pricing*, (1973, Cmnd. 5330) at 2.

⁸ *Id.* at 3.

⁹ *Id.*

¹⁰ *Id.* at 6.

that it is this need for information about rivals' intentions that may result in the domination of the common interest over the interest of individual firms.

J. P. Dunn emphasizes the point that firms, through conscious parallelism, seek to coordinate their behaviour without an agreement in the legal sense.

. . . [C]onscious parallelism means action by one competing enterprise, A, similar in detail to that of another business, B, or other businesses, B and C, each one, A, B and C, relying on the fact that such action is similar and that it will be in the interest of each to continue that behavior, and yet refrain from communicating directly with the other for the purpose of entering into a full-blown agreement.¹¹

In the absence of communication, Dunn argues, the behaviour does not constitute an agreement that is subject to the usual conspiracy provisions. B. F. Turner also defines conscious parallelism as interfirm coordination without agreement, i.e., it is "the conscious or knowledgeable adoption of uniform business practices, without any agreement or understanding, by competitors in a particular market."¹²

We do not wish to overemphasize the point that closely parallel behaviour by oligopolists always refers to situations where an agreement (in the legal sense) is present. In fact, we shall develop the argument, formulated by Carl Kaysen, that, "[l]ong continued uniformity of action, extended through a variety of situations amid changing circumstances, can . . . be taken as a basis for inferring, with a high degree of certainty, the existence of at least an 'agreement to agree.'"¹³

2. *The Problem for Competition Policy*

Milton Moore defines the conundrum for competition policy when he states:

The key assumption in the analysis of their behaviour is that most oligopolies engage in conventional pricing practices that are indistinguishable from the tacit collusion that is almost universally disapproved.¹⁴

Moore then points out:

Formal collusion is susceptible to regulation, but conscious parallel action is extremely difficult to detect and even more difficult to prove, and it is impossible to prevent independent action on the recognition of mutual dependence. But the effects of all three are similar.¹⁵

While the practice of conscious parallelism may not exhibit predatory content or the customary elements of a formal or even tacit agreement, as

¹¹ John Purinton Dunn, *Conscious Parallelism Reexamined* (1955), 35 Boston U.L.Rev. 225 at 228.

¹² B. F. Turner, *Conscious Parallelism in the Pricing of Gasoline* (1960), 32 Rocky Mountain L. Rev. 206 at 211.

¹³ Carl Kaysen, *Collusion Under the Sherman Act* (1951), 65 Quarterly Journal of Economics 263 at 268.

¹⁴ Milton Moore, *How Much Price Competition?* (Montreal and London: McGill-Queen's University Press, 1970) at 3.

¹⁵ *Id.* at 5 (emphasis added).

defined by the courts, the economic effects may be as pernicious as those associated with the more traditional price or market conspiracy. Prices may be maintained, over considerable periods of time, at a level significantly above those which would result if the industry were effectively competitive.¹⁶ Innovation and technological change may be inhibited or introduced at a slower rate.¹⁷ Excess capacity may continue to exist over long periods of time, not only constituting a burden to the consumers of the industry's output, but also acting as a barrier to entry to new competitors. In addition, conscious parallelism may have the effect of shifting the major firms' cost curves upwards due to inefficiency in production and distribution because of the absence of competitive pressures.¹⁸ This results in a loss to society as a whole as more resources are used than are necessary with the best available production process. Even in the absence of technical inefficiency, there is a "deadweight burden" to society that occurs when oligopolists jointly restrict output below the competitive level.¹⁹ In addition, in many cases of oligopoly, the firms involved must invest considerable sums to attain or defend their position of market power. Such expenditures may take the form of advertising and product differentiation activities, and lobbying efforts to obtain or maintain favourable antitrust legislation. As Professor Tullock has remarked, "As a successful theft will stimulate other thieves to greater industry and require greater investment in protective measures, so each successful establishment of a monopoly or creation of a tariff will stimulate greater diversion of resources to attempts to organize further transfers of income. . . . [T]he total costs of monopoly should be measured in terms of the efforts to get a monopoly [more generally, a position of market power] by the unsuccessful as well as the suc-

¹⁶ Fortunately, in most markets the ability to maintain supra-competitive prices is constrained by a variety of market forces. These constraints on pricing include the elasticity of product demand, availability of substitute products, possibility of entry by new domestic firms, threat of imports, costs of communications, cost differences among firms, product heterogeneity, lumpiness and infrequency of orders, and technological change.

There can be little doubt that these factors impose constraints on the ability of even closely-coordinated oligopolists to extract supra-competitive prices on a continuous long term basis. However, the fact that there may be some limits is little consolation to Canadian consumers who must pay supra-competitive prices over an extended period of time. Heflebower, *supra*, note 6 at 93, points out:

There is one unequivocal meaning of competitive price behaviour: each firm, without a significant degree of concern about rivals' reactions, adjusts its volume and prices so as to maximize its profits in a very short span of time.

¹⁷ There is considerable uncertainty about this point. See Morton I. Kamien and Nancy L. Schwartz, *Market Structure and Innovation: A Survey* (1975), 13 *Journal of Economic Literature* 1.

¹⁸ W. S. Comanor and H. Liebenstein, *Allocative Efficiency, X-Efficiency and the Measurement of Welfare Losses* (1969), 36 *Economica* 304 and C. K. Rowley, *Antitrust and Economic Efficiency* (London: MacMillan, 1973), Chap. 5 at 25-32. This view is questioned by David Schwartzman, *Competition and Efficiency: Comment* (1973), 81 *Journal of Political Economy* 756.

¹⁹ See D. R. Kamerschen, *An Estimation of the "Welfare Losses" from Monopoly in the American Economy* (1965), 4 *Western Economic Journal* 221 at 236; F. M. Scherer, *Industrial Market Structure and Economic Performance* (Chicago: Rand McNally, 1970), Chap. 17.

cessful."²⁰ It should be apparent that the resources expended in seeking or maintaining market power represent a social waste.

B. ECONOMIC ASPECTS OF CONSCIOUS PARALLELISM

When the size distribution of firms in an industry is such that a small number account for a relatively high proportion of industry sales, assets, employment or value added, individual firm behaviour is constrained by each firm's need to be sensitive to the interdependence of its interest and that of the group. The actions of a single firm can no longer be viewed in isolation. The impact of its pricing and distribution policies is of such a magnitude that other firms in the industry can be expected to react readily to its marketing initiatives. In such a situation of mutual dependence, firms will tend to adopt parallel policies, particularly if the product is undifferentiated. Within limits, they will match price initiatives of each other. One rival will not initiate a price increase unless he expects others to match; failure of others to match price initiatives will almost certainly result in prompt revocation of the price increase by the initiating firm.

Before a firm initiates a price increase, it may communicate indirectly with its rivals. An example of this type of behaviour is found in "independent"²¹ statements by executives of various companies in a market to the media or to trade groups pointing out the need for price increases. Often such statements are phrased in terms of the pressure of rising costs and coincide with new wage settlements in the industry. If there are no expressions of dissent, one of the firms may proceed to initiate the price increase. If the others do not follow, the initiating firm will be compelled by the threat of erosion of its market share to drop back to previous price lists.

Businessmen, and often economists, argue that parallel action by oligopolists, particularly in the case of homogeneous products, is necessary and evidences the forces of competition. For example, in their joint submission on Bill C-42, the Stage II amendments to the *Combines Investigation Act*,²² twelve of Canada's largest corporations stated that conscious parallelism "may be the result of acts which are completely independent and which are undertaken by persons engaged in active competition by similar means."²³ The brief of the Canadian Pacific group of companies stated that conscious parallelism "connotes both a normal and a natural feature of competition in the marketplace. True competitors ordinarily seek unilaterally to meet or match

²⁰ G. Tullock, *The Welfare Costs of Tariffs, Monopolies and Theft* (1967), 5 *Western Economic Journal* 224 at 231-32.

²¹ The meaning of "independent behaviour" in the context of a concentrated oligopoly will be discussed below.

²² R.S.C. 1970, c. C-23 as am. c. 10 (1st Supp.); c. 10 (2d Supp.); 1974-75-76, c. 76; 1976-77, c. 28.

²³ "Submission of Abitibi Paper Company, Algoma Steel Corporation, Canada Packers, Cominco, John Labatt, Macmillan Bloedel, The Molson Companies, Moore Corporation, Noranda Mines, Power Corporation, The Steel Company of Canada, with respect to Bill C-42" (1977, mimeo) at 35.

as much as possible each other's prices, terms and products."²⁴ The Investment Dealers Association brief argued, "competitive considerations *dictate* parallel policies within many oligopolies. . . ."²⁵ The brief of Imperial Oil Limited stated:

In an oligopoly market, firms normally must recognize their mutual interdependence because of their fewness. They also are often compelled to follow "closely parallel policies or closely matching conduct." For example, if they are selling in the same market, any seller must match a lower price offered by a competitor or risk losing customers. If demand is buoyant and costs rising, a seller who does not follow a competitor in raising prices risks losing profits. If one seller advertises in a market, his competitors normally must do so also.²⁶

These themes were repeated in at least a dozen other briefs.

1. *Interfirm Coordination in an Oligopoly*

To this point, we have minimized the difficulty experienced by the leading firms in an oligopoly in reconciling conflicting perceptions of industry conditions, differences in costs of production and distribution, and opportunities for independent behaviour not available to rivals, to arrive at a mutually satisfactory solution in respect of price and other variables. It is not immediately apparent that a group of mutually dependent firms will be able to move smoothly toward the maximization of collective industry profits. The essence of oligopoly is that the firms possess at least a modicum of discretionary economic power. Failure to coordinate their behaviour effectively can, in the extreme, result in bouts of commercial "warfare" in which the price, profit and output of the oligopoly closely resemble that of a competitive industry. On the other hand, perfectly coordinated behaviour can result in a cartel which exhibits the performance characteristics of a monopoly.

Unlike the accepted theory of perfect competition or that of pure monopoly, there are many theories of oligopoly behaviour. To the extent that they are deterministic, they rely upon unrealistic assumptions. To the extent that they are behaviourally rich in their assumptions, they are non-deterministic in terms of the price, profit and level of output they predict. R. B. Heflebower writes:

Economists have not been able to develop a theory of price behaviour for [manufacturing industries with few sellers] for when sellers are few they tend to be "jointly acting oligopolists" because of the "conjectural interdependence" among them. Each seller's behaviour is restrained by his expectations as to how his rivals will react to a price-change by him. There is a circularity in sellers' reactions and there is no definitive theory of how the circle is broken except by some collusive device.²⁷

In *Industrial Market Structure and Economic Performance*,²⁸ F. M. Scherer

²⁴ "Brief of the Canadian Pacific Group of Companies on Bill C-42" (1977, mimeo) at 22.

²⁵ "Submission by the Investment Dealers Association of Canada to the Hon. Anthony C. Abbott, Minister of Consumer and Corporate Affairs" (May 17, 1977, mimeo) at 14. (emphasis added).

²⁶ "Submission of Imperial Oil Limited re Bill C-42" (1977, mimeo) at 111.10.

²⁷ Heflebower, *supra*, note 6 at 89-90.

²⁸ Scherer, *supra*, note 19, Chapters 7 and 8.

purposely did not review a number of the models of oligopoly. Rather, his approach was to describe the conditions which facilitate oligopolistic coordination and those which limit it.

So far we have argued that in a concentrated industry, where firms are interdependent, firms will be reluctant to cut the price in the hope of increasing their output and profits. Such an action will have a discernible effect on rivals' sales and these rivals will retaliate. Matching price reductions by all the leading sellers will result in reduced profits for all of the firms. As Posner emphasizes, this formulation of the problem depends upon certain assumptions:²⁹ (a) that there is no appreciable time lag between the initial price cut and the responses of rivals; (b) that the price cut cannot be concealed, at least for some time; (c) that rivals will respond without hesitation by matching the price cut;³⁰ and (d) that the price cutter is not able to practice price discrimination, i.e., cut the price to some of his customers but not others. In actual fact, however, many of these assumptions do not hold.

Posner also argues that, depending on the price elasticity of demand, a proportion of the price cutter's increase in sales volume will come from new customers formerly outside the market as well as from those of his rivals.³¹ He also points out that a relatively large increase in a leading firm's output is needed to produce a significant effect on the market shares of rivals. Further, the reluctance of oligopolists to reduce price is a matter of concern only if the existing level of prices results in supracompetitive profits.³² Scherer spells out a fairly large number of other conditions which limit oligopolistic coordination: (i) the number and size distribution of sellers, i.e., as the number of sellers increase, the probability that individual sellers will ignore their rivals increases as do the odds of getting a maverick. The presence of a competitive "fringe" inhibits coordination among the leading firms; (ii) product heterogeneity, i.e., the greater the heterogeneity, the more difficult coordination; (iii) the dynamic implications of cost structures, i.e., where overhead costs are high, pricing discipline tends to break down during recessions; (iv) the size and frequency of orders, i.e., close coordination is easier if orders are small, frequent and regular; and (v) the nature of the industry's social structure.³³

To the extent that some of the conditions which limit oligopolistic coordination exist in the real world, the simple interdependence theory of inter-firm coordination alone resulting in consistent supracompetitive pricing and profits is subject to challenge.³⁴ If interdependence, although recognized, is insufficient to overcome the conditions that inhibit coordination, what other techniques are available?

²⁹ Richard A. Posner, *Oligopoly and the Antitrust Laws: A Suggested Approach* (1969), 21 *Stan.L.Rev.* 1562 at 1566.

³⁰ There is also a question as to how rapidly the firm can expand output after it has decided to do so, e.g., the extent of its excess capacity.

³¹ *Supra*, note 29 at 1567.

³² *Id.* at 1568.

³³ *Supra*, note 19 at 183-212.

³⁴ *Supra*, note 29 at 1569.

There are a wide variety of means which oligopolists may use to obtain greater benefits from their market power. These include collusion, both overt and tacit, conscious parallelism (often reinforced by the use of "plus factors"), mergers to reduce the number of competitors, various forms of price leadership and even cutthroat competition to eliminate competitors and to reinforce the need for less aggressive forms of interaction. Overt collusion is almost universally condemned by antitrust law.³⁵ Tacit collusion is both harder to effect and harder to detect, but is also condemned by the conspiracy provisions of the antitrust laws. Mergers represent the ultimate form of interfirm coordination, but they, too, come under the baleful eyes of the antitrust authorities—particularly in the United States. Price wars to discipline aggressive competitors are an expensive way to induce "harmony" in an oligopoly. Since the distinction between the various forms of price leadership and conscious parallelism is not great, we will consider them together. We focus on conscious parallelism because it is a common form of interfirm coordination in oligopoly, and, *per se*, is immune from prosecution by the U.S. and Canadian anti-trust authorities.³⁶

But parallel behaviour is insufficient to ensure the stability of those circumstances which produce supracompetitive prices and profits. Posner emphasizes this point when he states, ". . . the conventional formulation of the oligopoly problem, which holds that oligopolists are interdependent as to price and output, is inadequate. . . . [V]oluntary actions by the sellers are necessary to translate the bare condition of an oligopoly market into a situation of non-competitive pricing."³⁷ Although he is a lawyer, Posner takes an economic approach to the matter of collusion among oligopolists. He sees it as "a rational and effective business strategy only if its returns exceed its costs."³⁸ These costs include those of "bargaining to agreement and of enforcing the agreement to prevent cheating."³⁹ Posner is correct when he asserts, ". . . it seems improbable that prices could long be maintained above cost in a market, even a highly oligopolistic one, without *some* explicit acts of communication and implementation."⁴⁰ Donald F. Turner, formerly head of the U.S. Anti-trust Division, agrees. He notes that in most situations, the economic conditions facing specific firms are not identical. For example, their cost functions are not identical, product/service combinations are not completely standardized, and information about competitors is imperfect. In such circumstances, Turner points out, "[f]or a pattern of noncompetitive pricing to emerge . . .

³⁵ Criminal condemnation has not, of course eliminated the existence of collusion. Between 1889 and 1974/75 the Crown brought 83 cases of conspiracy to fix prices before the courts and won 70 of them. See Paul K. Gorecki and W. T. Stanbury, *Canada's Combines Investigation Act: The Record of Public Law Enforcement* (paper presented at the National Conference on Competition Policy, University of Toronto, May 12, 13, 1977), Table 10. In the fiscal year 1975/76, the Crown laid charges in another four conspiracy cases and in 1976/77 it did so in seven cases.

³⁶ This point will be discussed in Section D, below.

³⁷ *Supra*, note 29 at 1575.

³⁸ *Id.* at 1569.

³⁹ *Id.* at 1571.

⁴⁰ *Id.* at 1574.

requires something which we could, not unreasonably, call a 'meeting of minds,' or to use Professor Kaysen's phrase, an 'agreement to agree.'⁴¹

Posner's conclusion for public policy, with which Turner might not agree, is as follows:

Perhaps in an extreme case no explicit acts of collusion or enforcement are necessary for [the translation of interdependence into noncompetitive pricing], only a tacit understanding on restricting output [thus raising price], and perhaps in a larger number of cases explicit acts are necessary but completely concealable. There is no need to distinguish these categories. Both can be considered forms of tacit collusion (or, synonymously, noncompetitive pricing by oligopolists), since that is how they would appear to a trier of fact. The essential point, in any event, is that tacit collusion thus defined is very like express collusion.⁴²

Posner argues that the following types of behaviour are proof of the existence of tacit collusion as he defines it:⁴³ joint systematic price discrimination (including highly simplified systems which fail to reflect cost differences); prolonged excess of capacity over demand; relatively low frequency of changes in price; disproportionate response of price to changes in cost; abnormal profits; price leadership (the last two in a qualified form); the existence of fixed market shares; identical sealed bids for nonstandard items; refusal to offer discounts in the face of substantial excess capacity; the announcement of price increases far in advance without legitimate business justification for so doing; and public statements as to what a seller considers the right price for the industry to maintain.

The need for interfirm coordination in an oligopoly is greatest in disequilibrium situations. Heflebower points out that the response by oligopolists to a disequilibrating development

... may be delayed or averted by direct communication among rivals or by 'props' that have been erected by [conscious act or evolution] on the market stage—pricing systems and price leadership are examples—or signals made by the players. The latter include publicized statements as to what ought to happen, and announcements of cutback in output. But where sellers are very few and have similar costs and the product is standardized and sold to expert buyers, such procedures are less necessary [to avert price competition], for 'quasi-agreement' by conjectural interdependence alone is relatively easy.⁴⁴

As one moves along the marketplace continuum from perfectly competitive towards duopoly, attempts at nonformal "agreements" become more probable but also more difficult. Heflebower indicates that a variety of "devices," "special props" and "signalling devices" will be found such as, for example, trade association activities, block booking by film distributors, zone pricing of durable goods, delivered pricing, and functional discounts.⁴⁵ He points out such practices tend to be institutionalized and generally have a stabilizing

⁴¹ D. F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal* (1962), 75 Harv. L.Rev. 655 at 664.

⁴² *Supra*, note 29 at 1575.

⁴³ *Id.* at 1578-82. See also his article, *A Program for the Antitrust Division* (1971), 38 U. of Chic. L.Rev. 500 at 516-23.

⁴⁴ *Supra*, note 6 at 105.

⁴⁵ *Id.* at 111.

influence on prices and market shares. For example, a sort of "quasi-agreement" on the base price level may not be too difficult to achieve, but it is the props which enshrine the price structure and which could not exist in the absence of a consciously parallel course of action.⁴⁶

In summary, when one examines cases of conscious parallelism more closely one is likely to find that the close coordination of interfirm behaviour has been aided by one or more "plus factors" designed to ensure that independent behaviour is minimized.

2. *Parallelism and Independent Decisions*

Businessmen argue that parallel action or matching conduct should not be subject to legislative sanctions because it is the result of the independent decisions of the firms involved. Unless there is a proven agreement among the leading firms to adopt closely parallel policies, it is argued, business firms should not be subject to civil or criminal penalties for independent decisions to match the price or other behaviour of rivals. But this begs the question: what is meant by "independent" decision-making in the context of an oligopoly?

The dilemma for anti-combines enforcement is that the parallel behaviour which is witnessed when all the firms in an industry announce identical price changes within a short period of time may be a reflection of a formal conspiracy, or it may simply reflect a series of independent decisions in the market. For example, costs of materials may have risen for all firms in an industry such that a price increase is necessary if a reasonable profit is to be maintained. All firms are aware that costs have risen and a price increase is deemed necessary. One firm announces a price increase; all others follow the lead and raise their prices, aware that if they are selling substantially similar products, their prices must be comparable. No conspiracy in the legal sense has occurred. Each firm has made its own decisions, but it has done so in response to a common motivating factor, fully aware of the interdependence of the major firms in the market. On the other hand, the process may only be a façade, a means by which to maintain supracompetitive prices, using the announcement of increased costs as a coordinating device. Typically, there is no assurance of which is the correct interpretation. How is the policy maker to deal with the problem?

Discussions of conscious parallelism usually stress that the situation is immune to attack because each firm has acted independently and there is no evidence of an agreement in the legal sense. It is argued that there is not even a tacit agreement and, moreover, that one cannot even *infer* a tacit agreement from the existence of conscious parallelism. But we must examine more closely the theory of independent decision-making in the context of an oligopoly. At least two quite different interpretations arise: each firm makes the best decision it can, taking full account of the context in which the firm operates, *without any attempt to communicate* with other members of the industry, or, alternatively, each firm makes the best decision it can *without* reference to its position of interdependence. Depending on what is meant by "independent," this latter proposition results in a *non sequitur* in the case of an

⁴⁶ *Id.* at 112.

oligopoly. Among the dictionary definitions are the following: "not subject to the authority of another; autonomous; self determining; not dependent on or part of some large group [or] system; not affected or influenced in action, opinion etc. . . ." ⁴⁷ The essence of an oligopoly is that the number of firms is sufficiently few that they are mutually dependent; a change in the price or output of any firm has a detectable effect upon all the firms in the relevant market. Plainly, if an oligopolist is going to exist over time he cannot be "self-determining" or "autonomous." He is, in fact, dependent on and is part of some larger group or system. He is affected by and influenced in his choice of action by others, namely the other members of the industry.

Turner argues that "conscious parallelism is devoid of anything that might reasonably be called an agreement when it involves simply the independent responses of a group of competitors to the same set of economic facts—independent in the sense that each would have made the same decision for himself even though his competitors decided otherwise."⁴⁸ It is the last part of the sentence which is crucial to the distinction between behaviour which might properly be called a tacit agreement and that which should be called rational decision-making by an oligopolist.

We conclude that, in the context of an oligopoly, "independent" behaviour by the individual firms can only mean that they make their decisions without any attempt to communicate with other firms in the industry—except by their actions, which of course contain information. To ask an oligopolist to behave independently in the sense of not taking into account the actions and reactions of his competitors is to ask him to behave irrationally.

To prohibit oligopolists from matching the prices of rivals is to significantly revise the established rules of the marketplace and might simply cause firms to adopt insignificant price spreads to be offset by marginal service differentials.

In industries in which a standardized product is sold, buyers with some monopsonistic power will often try to put pressures on list prices, but in most cases the quoted off-list prices also turn out to be identical. This similarity may be due to the fact that sales representatives of major companies instruct customers to contact them for a new price quotation before buying at lower prices quoted by a competitor. In either case, to prohibit the publication of list prices does not solve the fundamental problem, though it is possible that price stability in some industries would be undermined by such a requirement.

3. *Phillips' Model of Interfirm Coordination*

In more highly concentrated oligopolistic markets, interfirm coordination is characterized by tacit, rather than overt or express, agreements. There is recognition of a group identity and an acknowledgement that for industry

⁴⁷ *Funk and Wagnall's Standard College Dictionary* (Toronto: Fitzhenry and Whiteside, 1974) at 684.

⁴⁸ *Supra*, note 41 at 663.

stability to be attained, some decisions must be group decisions.⁴⁹ As such, they are likely to be based on compromise among the participants. Generally speaking, the study of group behaviour has been eschewed by economists and left to the sociologists, social psychologists and other behavioural scientists. However, since the writing of Chamberlin,⁵⁰ there has been an appreciation of the element of mutual dependence in most industrial markets. Henderson explains the ubiquitous nature of interdependence in other than perfectly competitive markets:

There may be thousands of grocers, yet each grocer will be intimately affected by a very small number of neighboring grocers—who may be close geographically, or similar in the type of customer to whom they cater. Among dozens of makers of electrical machinery, each will have his own small group of particular rivals. An industry is like a forest: each tree is far from almost all the rest, but each has some close neighbors. What looks, at first sight, like an imperfectly competitive industry turns out to be a series of linked oligopolies.⁵¹

Almarin Phillips has borrowed from the literature of the sociologists and applied group theory to explain the behaviour of firms in an oligopolistic market.⁵² According to Phillips' model, special recognition of interdependence develops within oligopolistic markets in which parallel action reflects realization by the producers, or sellers, that they are members of a group. Within the group, a leader emerges, and a written or unwritten code develops which establishes rules of conduct for the group members vis-à-vis each other and non-group members. Conflict within the group is likely to be closely regulated by the code. Thus within the oligopoly, price leadership is common, and there is likely to be a noticeable absence of the most threatening form of intra-group conflict: price competition. However, non-price competition, as a form of benign rivalry, may be accepted. The industry as an organization, like the firm as an organization, is perceived to have rules; this is not to say that failure and success for individual participants are considered undesirable. This market stabilizing behaviour may result in either shared monopoly or market segmentation with each firm exercising dominance in a sub-market.

In Phillips' framework:

The group, as opposed to its individual members, does have a general objective—the objective of providing and enforcing such standards of conduct as will eliminate the indeterminacy which accompanies markets in which firms are mutually interdependent. Without some such group action, each firm will be worse off in terms of its own subgoals. Thus, while the group goal may be closely related to the firms' subgoals, being a member of the market group involves the surrender

⁴⁹ The U.K. Monopolies Commission writes, "Parallel pricing behaviour is the outcome of an appreciation by the sellers in an [oligopolistic] industry that the interests of each member of the group might be best secured by the co-ordinated pursuit of the interests of the group as a whole." *Supra*, note 7 at 34.

⁵⁰ Edward Chamberlin, *The Theory of Monopolistic Competition* (Cambridge: Harvard University Press, 1933).

⁵¹ Alexander Henderson, *The Theory of Duopoly* (1954), 68 *Quarterly Journal of Economics* 565 at 565.

⁵² Almarin Phillips, *Market Structure, Organization and Performance* (Cambridge: Harvard University Press, 1962).

of *some* amount of the firm's sovereignty and of its freedom to seek its own subgoal to the detriment of other firms.⁵³

But Phillips goes on to point out:

Unilaterally pursued, more profit to one frequently means less to another; a larger market share for one, a smaller share for another. Retaliatory action—rivalry—may mean that the subgoals of none are achieved. The interfirm organization—tacit and informal in the case of simple oligopoly—acts to resolve these conflicts to the mutual advantage of all if to the unique advantage of none.⁵⁴

Within this group framework, an increase in the size of the group will threaten the effectiveness of implicit agreements, and increase the need for a formal agreement. In Canada, the most elaborate conspiracies have involved eight or more parties.⁵⁵

Some problems of cohesion may be overcome by the existence of a group leader. Differences in power positions can potentially provide a stable social order within the group. Leadership becomes a substitute for formal organization and assures the subordination of subgroup goals to group goals.⁵⁶

Phillips' behavioural orientation and acceptance of the logic and, indeed, the desirability of establishing reasonable rules of the game for group behaviour, is aptly reflected in his observation that:

The important questions in conscious parallelism cases do not concern whether the firms involved have reached an "agreement" or whether they have "communicated" with respect to price and other matters of rivalry. Because of the smallness of the group of firms in simple oligopolistic markets, the conclusion is certain (if an obvious price war is not in existence) that the firms have—in a behavioural sense—communicated and, to a degree, agreed on certain aspects of conduct. Rivalry is bound to be limited within the group and behaviour is directed and tempered by their informal interfirm organization. Their agreement, while varying in subject matter, duration and effectiveness, may be as complete as that reached through the use of explicit and overt communication and a formal organization in markets in which firms are many. The important questions, then, relate to the effectiveness of the organization in restraining rivalry and to the probable impact such restraint has on market performance.⁵⁷

To Phillips, the focus of oligopolistic group behaviour is on cooperative competition: the limiting of the boundaries of rivalry and the avoidance of excessive or destructive rivalry. In an oligopoly, the participants recognize the

⁵³ *Id.* at 28.

⁵⁴ *Id.* at 29.

⁵⁵ Of the 48 conspiracy convictions in Canada between 1889 and 1974/75 resulting in fines, excluding those in which only individuals or an association was the subject of the prosecution, twenty-one involved eight or more firms. In some of the more elaborate conspiracies a considerably larger number of firms were convicted, as in *Container Materials, Ltd. v. The King*, [1942] S.C.R. 147; 1 D.L.R. 529; 77 C.C.C. 129, in which nineteen firms were convicted. See also, *Howard Smith Paper Mills, Limited v. The Queen*, [1957] S.C.R. 403; 8 D.L.R. (2d) 449; 118 C.C.C. 321; 26 C.R. 1 (twenty-eight firms); *R. v. Abitibi Power and Paper Company, Limited* (1961), C.C.C. 201; 36 C.P.R. 188 (seventeen firms); *R. v. Canadian Coat & Apron Supply Ltd.* (1967), 2 Ex. C.R. 53; 2 C.R.N.S. 62; 52 C.P.R. 189 (eighteen firms); and *R. v. St. Lawrence Corp. Ltd.*, [1969] 2 O.R. 305; 5 D.L.R. (3d) 263; C.C.C. 263; 59 C.P.R. 97 (twenty firms).

⁵⁶ *Supra*, note 52 at 31.

⁵⁷ *Id.* at 73.

importance of the behaviour of each of the major firms to the other firms with a significant market share. Appreciating their mutual dependence, they will individually recognize that mutual benefit is to be derived from the adoption of non-competitive pricing conduct. A unity of purpose or a common design and understanding emerges and a collective monopolization ensues without overt agreements. For Phillips, consciously parallel behaviour is natural behaviour which may not be detrimental to the public interest.

C. REVIEW OF THE CANADIAN CASES

Before commencing a detailed review of the relevant cases, it should be noted that conscious parallelism cases, more so than ordinary conspiracy cases, turn on the precise nature of the facts rather than the interpretation of the law, although it is evident that old law is being interpreted in the light of new economic facts.

1. *R. v. Canada Cement Lafarge*

Not until 1973, over three-quarters of a century since the passage of the first anti-combines legislation in Canada, did the issue of conscious parallelism become the subject of a judicial proceeding.⁵⁸ In the first case, *R. v. Canada Cement Lafarge Ltd.*,⁵⁹ four cement producers were discharged at a preliminary hearing concerning an alleged violation of section 32 (1) (c) of the *Combines Investigation Act*. Provincial Court Judge Camblin ruled that:

the resulting prices set by the companies are the result of conscious parallelism and the companies are therefore discharged.⁶⁰

He apparently based his ruling on a speech given in October, 1962 by D. H. W. Henry, then Director of Investigation and Research under the *Combines Investigation Act*. Mr. Henry said, in part:

Conscious parallelism, if conducted without collusion among the members of the industry, is not an offence. This is because if such collusion is not present, there is not the element of agreement or arrangement necessary to constitute the offence of conspiracy. I must emphasize, however, that this is so only in the absence of collusion.⁶¹

Mr. Henry stepped out of his appointed role as chief investigator of restraints of trade in Canada to make a pronouncement on the law which was to have wider implications than he might have expected. Some months after he made the 1962 speech, the Canadian Steel Warehousing Association published a pamphlet entitled "Permissible Trade Practice in Conformity with the Combines Investigation Act" in which his discussion of oligopoly and conscious

⁵⁸ In the U.S., the conscious parallelism cases date from the 1940's.

⁵⁹ *R. v. Canada Cement Lafarge Ltd.* (1973), 12 C.P.R. (2d) 12.

⁶⁰ *Id.* at 17.

⁶¹ *Id.* at 15. The speech was originally given to the Public Buyers Group of British Columbia (Vancouver: October 12, 1962; mimeo) at 8. The entire quotation in the judgment consisted of almost two pages of fine print. In his *Report of the Director of Investigation and Research, Combines Investigation Act*, for the year ended March 31, 1961 (Ottawa: Queen's Printer, 1961) at 23-24, Mr. Henry dealt in similar terms with the problem of identical tenders submitted by oligopolists producing homogeneous products.

parallelism is cited.⁶² Over a decade later, in the *Alcan* case,⁶³ the decision of Camblin J. was relied upon in the discharge of four aluminum extruders. The words of Mr. Henry dealing with price leadership without collusion were quoted by the judge in that case.⁶⁴

The facts of the *Canada Cement Lafarge* case are interesting in that they provide a profile of a concentrated oligopoly producing a homogeneous product (Portland cement) in a regional market (Ontario). Camblin J. pointed out that Canada Cement had about forty per cent of the market, while the other three major producers had about twenty-five per cent, twenty per cent and twelve per cent respectively. He indicated that between 1955 (when the investigation began) until the middle of 1959, "one finds the marketing arrangements to be in a somewhat chaotic condition due, among other problems, to the incongruous freight allowances. . . . [C]ommencing in 1959, an element of harmony was detected."⁶⁵ Identical tenders were received for large government contracts and the prices charged by all the major companies in different areas were, with very few exceptions, found to be identical. The Crown alleged that such harmony was the result of an illegal conspiracy. Camblin J. concluded:

Defence counsel, I am sure, will agree that the Crown has established that the companies involved are using a base freight factor pricing which did not come about by mere coincidence.⁶⁶

He then went on to quote Mr. Henry's words on the nature of oligopoly, conscious parallelism (which Henry defined to be "the tendency on the part of a small group of firms constituting an industry to act more or less in a uniform manner"),⁶⁷ and the ubiquity of identical tenders and identical selling prices. Although he appears to have concluded that the mutual adoption of a basing point pricing scheme occurred as a result of an illegal agreement (tacit or overt), Camblin J. proceeded to adopt Mr. Henry's views in deciding that conscious parallelism is not prohibited by the *Combines Investigation Act*.⁶⁸

Primarily because the alleged conspiracy to establish the basing point scheme (which would result in identical prices by all suppliers to any customer) occurred in 1959, and because the information was not laid until December 1, 1972, the Crown did not proceed by way of preferred indictment. This decision must be viewed as at least a minor victory for users of a basing point pricing scheme.

⁶² *R. v. Armco Canada Ltd.* (1974), 6 O.R. (2d) 521; 21 C.C.C. (2d) 129; 17 C.P.R. (2d) 211; at (C.C.C.) 148, 149, 150.

⁶³ *R. v. Aluminium Co. of Canada Ltd.* (1975), 22 C.P.R. (2d) 216. (Preliminary Hearing).

⁶⁴ *Id.* at 221.

⁶⁵ *Supra*, note 59 at 14.

⁶⁶ *Id.*

⁶⁷ *Id.*

⁶⁸ The case was reported in an American academic journal: (1974), 19 *Antitrust Bulletin* 55.

2. *R. v. Armco Canada Ltd.*⁶⁹

To date, the most significant combines decision in Canada with respect to conscious parallelism is that of Mr. Justice Lerner in the *Armco* case, handed down on September 19, 1974.

a. Summary of the Facts

Ten corporations were charged with violating section 32 (1)(c) of the *Combines Investigation Act* in a conspiracy to fix the price of corrugated metal pipe culverts throughout Ontario and Quebec during the period November 1962 through August 1967. Eleven individuals, a trade association and five firms were named as co-conspirators. The case provides an excellent illustration of the process by which competitors in an oligopoly move, through "spontaneous coordination" aided by exhortations to follow an "open pricing policy," from the recognition of their mutual dependence to the ability to act upon the recognition of their interdependence.

In 1958, sales of metal culverts in Canada (in tons) increased by six per cent over the previous year. In 1959 they increased by eleven per cent, but in 1960 they fell by over seventeen per cent relative to the 1959 output. Total Canadian sales in 1961 were up almost eighteen per cent over the 1960 output.⁷⁰ In November of 1961, the Corrugated Metal Pipe Institute was incorporated. By late 1962, nine eastern producers and one western firm were active members and three large steel makers, suppliers of the basic raw material, were associate members. Apparently, significant overcapacity existed in the early 1960's. In 1957, there were fifteen producers operating thirty-seven plants; in 1962 there were twenty-two producers with forty-nine plants. An Armco executive testified that, in 1963, the industry was operating at only thirty per cent of capacity. He also indicated the ease of entry: a capital investment of only \$40,000 to \$50,000 was required, indicating that "this kind of manufacturing could even be carried on in a barn."⁷¹ The president of the Institute, who was also president of Armco, the largest producer, described the situation as "cutthroat competition." Lerner J. concluded that, in the fiscal years of 1962 and 1963, the contracts awarded by the Department of Highways of Ontario (DHO) "reflect active competition among the corrugated steel pipe producers. . . ."⁷² The Restrictive Trade Practices Commission (RTPC) reported "the relative positions of firms having their head offices in Ontario in the Canadian market" in 1963 as follows: Armco 42.3 per cent, Rosco 14.2 per cent, Westeel 12.5 per cent, Robertsteel 7.5 per cent, Pedlar 7.1 per cent, Ontario Culvert 3.5 per cent and six others whose shares ranged from 0.8 per cent to 1.5 per cent.⁷³ Apparently competition was intensified by the fact that concrete pipe producers were making inroads in the supply of pipe for sewers and drainage.

⁶⁹ *Supra*, note 62.

⁷⁰ *The Metal Culvert Industry, Ontario and Quebec* (Ottawa: Restrictive Trade Practices Commission, 1970).

⁷¹ *Supra*, note 62 at (C.C.C.) 136.

⁷² *Id.* at 135.

⁷³ *Supra*, note 70 at 29.

In November of 1962 an executive of Robertsteel, Mr. Turney, introduced the subject of an open price policy at a meeting of the Corrugated Metal Pipe Institute. Subsequently, in a letter to the directors of the Institute, Mr. Turney proposed that the Institute might follow a similar policy to the one employed by the Canadian Steel Warehousing Association, of which Robertsteel was a member. Lerner J. described the policy in this way:

The "open price policy" advocated that each firm openly set out its prices in written or printed form, including discounts, terms of credit, and make these available to all customers, competitors and the public.⁷⁴

But, as the judge pointed out, the real objective was, in Turney's words, "that prices will adjust themselves to the requirements of the individual producers and ultimately reflect the true state of the market through the natural forces of known competition."⁷⁵ Lerner J., however, recognized this attempt to frustrate the mechanisms of a free market: "an 'open price policy' would be the means of preventing price-cutting competition by all manufacturers for customers."⁷⁶ Not only would active price competition be abolished, but in the open price policy the Institute would have found a legal means of obtaining the desired result. This point was stressed in a speech by Mr. Yeo, the president of the Canadian Steel Warehousing Association, the text of which was sent, with Turney's letter, to the major metal culvert manufacturers. Yeo's words indicate the problem of conscious parallelism for competition policy:

The test [of legality] is whether the uniform price has come about by the freely competitive and independent actions of the individual members of an industry, and not by agreement.⁷⁷

In other words, if the firms are able to coordinate their actions spontaneously without collusion or a conspiracy or even tacit agreement, they cannot be convicted under the existing section 32. Lerner J. articulated the prosecution's problem: ". . . any finding of an agreement . . . would have to be from inferences to be drawn based on the rule in *Hodge's Case*⁷⁸ . . . that there was a

⁷⁴ *Supra*, note 62 at (C.C.C.) 138.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ *Id.* at 141.

⁷⁸ *Hodge's Case* (1838), 2 Lewin 227; 168 E.R. 1136.

While the Supreme Court of Canada, in *R. v. Cooper* (1977), 37 C.R.N.S. 1, held that it is no longer "an inexorable rule of law in Canada" that the trial judge must direct the jury according to the rule in *Hodge's Case*, (*per* Ritchie J. at 18), there is nothing to prevent the trier of fact from continuing to evaluate circumstantial evidence in the light of that rule. In *R. v. Mitchell*, [1964] S.C.R. 471 the Court held that "[t]he direction in *Hodge's Case* [does] not add to or subtract from the requirement that the proof of guilt in a criminal case must be beyond a reasonable doubt." (*per* Spence J. at 479). In *Cooper*, Laskin C.J.C. (dissenting on another point) said "The time has come to reject the formula in *Hodge's Case* as an inexorable rule of law in Canada. Without being dogmatic against any use of the formula of the charge in *Hodge's Case*, I would leave the matter to the good sense of the trial judge . . . with the reminder that a charge in terms of the traditional formula of required proof beyond a reasonable doubt is the safest as well as the simplest way to bring a lay jury to the appreciation of the burden of proof resting on the Crown in a criminal case." (at 21-22). (We are indebted to Prof. M. T. MacCrimmon for this point).

tacit agreement between or among the accused.”⁷⁹ The crux then is the application of that rule, which provides that when the proof of a conspiracy must be inferred from circumstantial evidence, the inferences drawn from the acts and words of the accused or their agents must be consistent only with the establishment of an illegal or unlawful arrangement or agreement and be inconsistent with any other rational conclusion.

Having promoted the open price policy before the Steel Warehousing Association, A. D. Russell of Russell Industries addressed the Corrugated Metal Pipe Institute on the same subject in February 1962. He exhorted his audience of fifty, representing fifteen companies, to see the benefits of price stabilization, describing competitive price cutting as “unintelligent competition . . . and no theory of economics *nor any law in the country requires unintelligent competition.*”⁸⁰ He pushed the idea that open price lists disclosed facts which businessmen were entitled to use in the formulation of their own merchandising decisions, but he also indicated they were not entitled to use them with competitors “in the formulation of joint merchandising decisions however intelligent they may seem.”⁸¹ It seems clear that businessmen recognize the value of such open price lists as a device to facilitate the coordination of interfirm behaviour and so enable them to act on the recognition of their mutual dependence. Mr. Russell alluded to the words of John Donne in trying to convince the members of the industry to act on the recognition of their interdependence:

. . . [I]t becomes necessary through a process of *education* within an industry to establish clearly in the minds of all members that no man is an island unto himself and that every action great or small will eventually cause a counteraction⁸²

He concluded that “the right of price leadership . . . does not belong to a select few but can be assumed at will, even by the smallest and weakest member.”⁸³ There is much economic sense in Mr. Russell’s remarks. As Milton Moore reminds us, the price leader in the context of a homogeneous-good oligopoly is the firm least disposed to raise prices and most disposed to lower them.⁸⁴

In the month following Russell’s speech, Mr. B. C. Pepper, counsel for the Institute, wrote a letter to D. H. W. Henry in which he, in Lerner J.’s terminology, “put up a trial balloon.” Pepper had told the members of the Institute that “they would be on dangerous ground to endeavour to introduce the [open price] policy by tacit or express agreement.”⁸⁵ He went on to say with respect to firms not adopting the policy: “It is one thing to educate or to exhort. It is quite another to persuade by inducement or compulsion.”⁸⁶

⁷⁹ *Supra*, note 62 at (C.C.C.) 141-42.

⁸⁰ *Id.* at 144.

⁸¹ *Id.*

⁸² *Id.* at 145.

⁸³ *Id.* at 146.

⁸⁴ *Supra*, note 14 at 31-36.

⁸⁵ *Supra*, note 62 at 146.

⁸⁶ *Id.*

The legality of the emergence of an open pricing policy was put by Mr. Pepper as follows:

If all the members of the metal culvert industry publish identical prices and subsequently make identical tenders, how does one persuade the objective outsider, that is to say a Supreme Court judge, that those prices have been arrived at independently and not by collusion?⁸⁷

Prior to Mr. Pepper's letter, Mr. Russell consulted with Mr. Henry "because some members of the Canadian Steel Warehousing Association were not adhering to the open price policy in that industry and Mr. Russell was concerned as to how far he might be able to go in dealing with dissidents."⁸⁸ What better place to go to get advice on the matter than to the head of the agency charged with enforcing the anti-combines legislation?⁸⁹ Mr. Henry replied in part that, "efforts to educate must not involve any attempts at collusion or at coercion or threat of reprisal."⁹⁰

It is worth examining this statement closely. It appears to imply that, if through "education," the members of the industry are able to establish common prices, the Director of Investigation and Research assures them they are beyond the reach of the law. Could such advice not be construed as a tacit invitation to engage in extensive efforts at education to facilitate "spontaneous coordination" in a way that would not involve an illegal conspiracy?

However, Mr. Henry did point out to Mr. Russell that a court may find a collusive arrangement to exist on the basis of

inference from surrounding circumstances rather than from an examination of direct evidence of agreement or understanding. In such circumstances, successive steps, each of which looked at independently and in isolation might be regarded as lawful, can bring the participants closer to the brink of illegality.⁹¹

Mr. Henry went on to say,

*It seems to me that once the activities of the Association go beyond education and explanation and take the form of direct persuasion and implied coercion of individuals, it can scarcely be said that the industry members have independently adopted the policy in question.*⁹²

In the same letter, Henry criticized Mr. Russell's address to the Steel Warehousing Association.

It is one thing for such oligopoly characteristics [price leadership or conscious parallelism] to develop of themselves without collusion; *it is quite another matter for members of an industry to make a conscious effort collectively to bring them about.*⁹³

On May 2, 1963 the directors of the Corrugated Metal Pipe Institute met and

⁸⁷ *Id.*

⁸⁸ *Id.* at 147.

⁸⁹ See *Report of the Director of Investigation and Research, Combines Investigation Act*, for the year ended March 31, 1965 (Ottawa: Queen's Printer, 1965) at 15.

⁹⁰ *Supra*, note 62 at (C.C.C.) 147.

⁹¹ *Id.*

⁹² *Id.*

⁹³ *Id.* at 147-48.

discussed the merits of an open price policy. The Institute's counsel, Mr. Pepper, "strongly pointed out that such pricing had to be reached 'individually and independently' by each member, but that the Institute was within its legal rights to undertake 'purely educational' action on benefits of such policies to the industry."⁹⁴ A formal resolution was passed which averred that "potential benefits could be derived by individual members of the industry from the adoption of the open pricing policy."⁹⁵ Shortly thereafter, a memo implying that the Institute had completed its investigation of the matter and proposed to take no further action went to all existing and prospective members of the Institute. It was accompanied by a copy of Turney's "Report of Investigation into an Open Price Policy for the Highway Drainage Industry," the pamphlet prepared by the Steel Warehousing Association on the open price policy, and a copy of Mr. Henry's letter to Mr. Russell. Despite the extensive communications aimed at achieving conscious parallelism, Lerner J. stated:

At this stage of the chronology . . . an agreement or tacit agreement to lessen competition unduly by instituting an open price policy could not be inferred beyond a reasonable doubt.⁹⁶

In June 1963, at the urging of Mr. Turney, Robertsteel published an open price list. But Robertsteel was a leader without followers as Armco continued to give discounts. The largest producer and the first to produce helically formed pipe, Armco offered to sell up to twenty-four inch diameter pipe for five per cent less than its previous list prices and offered quantity discounts. While Armco did not follow the leader, Ontario Culvert wrote to Carleton Culvert, "The enclosed Robertsteel price lists will be used, effective immediately until further notice."⁹⁷ One week later this was retracted. Robertsteel's effort to establish price leadership with an open price policy had not succeeded.

Some time after September 2, 1963, two vice-presidents of Dofasco and Stelco, two of Canada's largest steel companies, who were also directors of the Institute, undertook to do a report on the problems of the metal culvert industry. Their report, described as the Craig-Allan report, was sent by Mr. Allan directly to all members of the Institute. The report began by stating that it was "a review *by an impartial source* of the market problems presently confronting the producers of corrugated metal pipe in Canada. . . ."⁹⁸ The authors of the report were not indicated in the body of the report. Lerner J. remarked, "If there was no design to lead the industry into an agreement on the open price policy, it would not have been necessary to try to give this report credibility by indicating that it was from an impartial source."⁹⁹ He noted that "Dofasco and Stelco had a real interest in developing the corrugated pipe

⁹⁴ *Id.* at 148.

⁹⁵ *Id.*

⁹⁶ *Id.* at 148-49.

⁹⁷ *Id.* at 152.

⁹⁸ *Id.* at 155.

⁹⁹ *Id.*

industry."¹⁰⁰ The report advocated open pricing as the means to avoid the evils of price cutting.

Price stability is synonymous with published pricing and the latter *must be adopted* and cherished by this industry . . . It is the only legal way of *communication* among members of the industry providing it is done without collusion.¹⁰¹

How the benefits of this policy were to be achieved was specified as follows:

It should be possible with a *series of changes in published prices and appropriate leadership by certain management relative thereto* that proper price levels . . . can be achieved within two to three months.¹⁰²

Lerner J. indicated that he saw the report as an exhortation to price leadership-followership.¹⁰³ Presumably to ensure uniform prices to various customers, the report recommended *delivered* pricing by area.

Clearly, executives in the industry realized that the independent issuance of uniform price lists and identical tenders by all producers and the voluntary adoption of an open price policy were implausible. As Mr. Campbell, the president of Armco, said in a handwritten memorandum found in Robertsteel's offices, this was "[a] rather ideal condition to expect without persuasion or coercion from others."¹⁰⁴ These words had been stroked out.

On December 2, 1963, Robertsteel published another price list. It was immediately adopted by all members of the Corrugated Metal Pipe Institute. Of particular interest to Mr. Justice Lerner was the fact that ten days later, several manufacturers bid on a Ontario Highways contract on the basis of Robertsteel's price per lineal foot well in advance of the effective date of their own or any other company's published price list.¹⁰⁵ For almost four years, uniform prices prevailed in the market for corrugated metal pipe, during which period several changes and increases in price were accomplished smoothly. With respect to the construction projects of the Department of Highways of Ontario, only three contracts out of 342 during this period "contained unequal, different or a variety of bids."¹⁰⁶ The vagaries of different plant and buyer locations and freight costs were carefully taken into account. Lerner J. states:

. . . [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.¹⁰⁷

It was not until TPL Industries entered the market late in 1967 and began selling at prices considerably less than the industry prices from 1964 to 1967 that the uniformity of prices was broken.

¹⁰⁰ *Id.*

¹⁰¹ *Id.* at 156.

¹⁰² *Id.*

¹⁰³ *Id.* at 157.

¹⁰⁴ *Id.* at 158.

¹⁰⁵ *Id.* at 159.

¹⁰⁶ *Id.* at 162.

¹⁰⁷ *Id.* at 173.

b. The Inference of an Agreement

Mr. Justice Lerner ruled that a tacit agreement had to have been made (presumably between June, 1963, when the first attempt at open price leadership failed, and December of that year when it succeeded) in order for the industry to have maintained identical prices and tenders from December 1963 to September 1967.¹⁰⁸ He inferred the existence of an agreement for three reasons: first, the fact that it was Robertsteel who published the December 2, 1963 price list, having published a similar list in June and having seen that it was not followed by most of its competitors. He said: "Repetition by Robertsteel reinforces the inference that the others were aware that Robertsteel was about to do this again and that they had agreed on 'followership'. . . ." ¹⁰⁹

Second, Mr. Turvey of Armco, the firm which had previously set prices reflecting its superior efficiency, admitted that his firm suddenly altered its strategy on December 12, 1963 and "adopted the position of followership" in order to "make a contribution towards the stabilization of price to the Department of Highways. . . ." ¹¹⁰ In addition, the firm stopped giving DHO a volume discount. The judge also pointed out that while other executives had been proponents of the open pricing policy, "nowhere in the evidence can it be found that [Mr. Turvey] was originally a proponent of the open price policy." He concluded, ". . . there had to be dialogue between Armco and Turney of Robertsteel some time in the latter half of 1963, before Robertsteel would try to experiment again, since Armco had been an earlier holdout to the open price policy." ¹¹¹

Third, the executives who, for about a year, had campaigned for the independent but universal adoption of the open pricing policy by means of "open discussion short of agreement," failed to obtain the desired result by "proselytizing." Therefore, a tacit agreement had to be the means by which the arrangement came about.¹¹²

c. The Evolution of Conscious Parallelism

Does it follow that establishment of the open price policy, which was adopted by all the producers of metal culverts almost immediately after Robertsteel published its second price list on December 2, 1963, had to occur as a result of a tacit agreement? Clearly it did not. Let us consider the problem in a slightly larger context. By what means can conscious parallelism, resulting in identical prices over a considerable period of time, occur in an oligopoly producing a homogeneous good, characterized by easy entry and extensive excess capacity? It could come about by at least three means:¹¹³

¹⁰⁸ *Id.* at 179.

¹⁰⁹ *Id.* at 178.

¹¹⁰ *Id.*

¹¹¹ *Id.* at 180.

¹¹² *Id.* at 179. One wonders why Lerner J. described the relationship between the accused as a "tacit" agreement; why not simply an agreement? There was evidence of direct communication between the parties.

¹¹³ This list is not meant to be exhaustive, but indicative of possible ways that conscious parallelism may evolve.

- (i) *Collusion*: The firms involved may make an express or tacit agreement to follow a designated price leader or to jointly adopt a specified price structure.

The persistence of identical tender prices for a period of over three years in an industry where entry was easy and the number of competitors exceeded a dozen, together with the multiple-zone delivered pricing system, necessarily leads to the conclusion that almost perfectly parallel action came about by collusion. Accordingly, Mr. Justice Lerner drew the correct conclusion.

- (ii) *Exhortation and Successive Attempts at Price Leadership*: Conscious parallelism may be accomplished without agreement in the legal sense following an active campaign of education and exhortation by industry participants or by third parties (in *Armco*, by the suppliers of the basic raw material). Having experienced the costly process of the action-reaction and competitive price cutting, firms soon realize the advantages of acting in recognition of their interdependence. When one firm publishes its price list for all to see, it is an invitation to follow. The announcement of the open price list by one firm may have the effect of stopping the process of competitive price cutting rather than speeding it up. Where significant excess capacity exists and firms exhibit differential costs of production, several unsuccessful attempts at leadership (perhaps by different firms) may be required before stability (identical prices) is obtained. The important point in this case is that no agreement, tacit or express, is necessary. Firms make independent decisions to lead or follow as the case may be. But they do so having been "educated" to see the folly of playing the action-reaction game and the potential benefits of price stability.
- (iii) *Collective Self-Instruction*: Conscious parallelism may be accomplished without an attempt by industry members or by outsiders to campaign for an open price policy. Nor is there any need for an agreement, tacit or express. Instead, the major firms in an industry (in the metal culverts case the top four firms accounted for about 76 per cent of total sales) having experienced competitive price cutting and periods of short-term price stability, not only recognize their interdependence but also seek ways to be able to act on it. The learning process may take many months or even a few years to occur. During the process, perhaps by chance, "quasi-agreements" (but not in the legal sense) occur, then they break down. Perhaps aggressive "mavericks," i.e., corporations most willing to cut prices and least willing to raise them, have to be replaced with more accommodating types following periods of "cutthroat" competition. In any event, and entirely without direct communication, the major participants are looking for a way out of their dilemma characterized by low and unstable prices and profits. Independently, one firm makes a move, e.g., publishing its prices, hoping the others will follow. Some firms may not follow—as *Armco* did not in the first instance. Price stability is not established. The same or another firm makes a similar attempt, again without even tacit understandings with the others. It may take several "failures" before the firms finally adopt common prices. This process of spontaneous coordination results in conscious parallelism as leadership-

followership is firmly established. Where entry is easy, excess capacity persists, and the number of competitors exceeds a handful, stable inter-firm coordination may never come about or, at most, will be ephemeral.

A related issue is the interpretation of identical tenders. In addition to drawing the inference that there had been a tacit agreement among the firms to follow Robertsteel's December 2, 1963 price list, Mr. Justice Lerner concluded that the very high percentage of identical tenders was hardly the result of chance.

The identical tenders to D.H.O. and others are remarkable because the great detail required for same would force one beyond any reasonable doubt to the conclusion that there was a complete exchange of information and understanding with meticulous attention that all bids on all tenders be identical.¹¹⁴

His reasoning is not flawless. Once all the culvert manufacturers adopted Robertsteel's detailed price list, the "complex" tenders usually broke down to being able to identify each item properly, take its posted unit price, multiply and add up the total. Since the list specified delivered prices in each of the three zones, the failure to attain identical bids would only occur if someone could not multiply, add or type correctly or the tender required a bid on an item not on the pricelist, i.e., some custom-made product unique to the buyer. In 1963, Hydro Quebec received six identical tenders of \$14,394,537.12 for 4800 miles of ACSR cable. Despite an intensive investigation, the Director of Investigation and Research could not find evidence of collusion.¹¹⁵ What had happened, apparently, was that each bidder took the appropriate unit price from its price list, identical to all firms, and correctly multiplied by the required volume to arrive at the amount of the bid.

The conclusion that identical sealed bids can occur without collusion applies only to circumstances where all firms quote list prices for standard items sold from inventory. If some installation cost must be incurred, which surely varies from job to job, or the product is an infrequently-bid, non-standard item, identical bids are usually indicative of collusion.

d. Parallelism and the Nature of the Arrangement

The cumulative effect of all of the evidence convinced Lerner J. "that there was a tacit agreement to maintain identical prices."¹¹⁶ He very rightly asked:

[W]hat possible purpose could this whole effort towards establishing the open price policy be if it were not to arrange something that would achieve stability of prices, eliminating competition and resulting in orderly marketing as against what was presently the situation that the industry found intolerable?¹¹⁷

Mr. Justice Lerner discussed at length the topic of "open price policy and conscious parallelism." At the outset he observed that:

The "open price policy" is an ambitious theory and if effected and if carried out

¹¹⁴ *Supra*, note 62 at (C.C.C.) 182.

¹¹⁵ *Report of the Director of Investigation and Research, Combines Investigation Act*, for the year ended March 31, 1968 (Ottawa: Queen's Printer, 1968) at 43-46.

¹¹⁶ *Supra*, note 62 at (C.C.C.) 183.

¹¹⁷ *Id.* at 184.

successfully, would achieve the ultimate and still not offend the *Combines Investigation Act*. Even if it were to result in unduly lessening competition, it would not offend the Act because there would have been no agreement or arrangement, direct or tacit. Once all members of the industry understood and recognized the value of this approach to marketing there would be a universal conscious effort on the part of all to actively follow the price lists and ancillary or collateral marketing devices [e.g. delivered pricing] of the "leader". There would result a conscious effort to "parallel" or follow the leader.¹¹⁸

The judge then summarized the testimony of Dr. J. A. Sherbaniuk¹¹⁹ on the nature of a homogeneous good oligopoly, which appears to have been couched in terms very similar to Mr. Henry's. But on one very important point Lerner J. was unsatisfied:

If price stability would come (if not naturally), then by the economic forces as expressed by Mr. Sherbaniuk in this ideal oligopoly situation, it suggests the query (which I find was never answered by the defendants) — why was it necessary for the Institute, Campbell, Turney, *et al.*, to spend the several months in 1962 and 1963, . . . to bring the results that form the basis of this prosecution?¹²⁰

While the judge rejected the theory that the "leadership" and "followership" occurred without conspiracy, we may posit another, but perhaps less likely, answer to his question. The purpose of the exhortation and education by Campbell, Turney and others was to provide the catalyst which would bring about the desired effect of price stability. Price cutting in an industry characterized by easy entry and excess capacity is expensive to the firms. The advocates of the open price policy were attempting to quicken the awareness of mutual dependence and the advantages relating thereto. Lerner J. concluded that the advocates became impatient with mere exhortation and the failure of the firms to coalesce around Robertsteel's published prices in June 1963; accordingly they arranged a tacit understanding that all members of the industry would adopt Robertsteel's price list on the second attempt (December 2, 1963). Lerner J. said, ". . . by way of *obiter*, economists to the contrary, I fail to see on a common-sense basis how conscious parallelism could be achieved without a conspiracy on the part of the accused to come to an agreement or arrangement beforehand."¹²¹ He then restated his conclusion:

After the 11-month period had passed with no effective results, suddenly without any other explanation "leadership" and "followership" appeared. I am convinced . . . that there had to be an understanding, arrangement or agreement to adopt the open price policy. This conclusion is the only rational inference that I can draw from the evidence and which is inconsistent with any other rational conclusion on the evidence.¹²²

The period of exhortation and education was not without some effect. First,

¹¹⁸ *Id.* at 187.

¹¹⁹ In the judgment Sherbaniuk is incorrectly referred to as "Cherbaniuk." See James Sherbaniuk, *Identical Bids Usually Result of Market Forces*, Financial Post, May 5, 1973 at C-1, C-2.

¹²⁰ *Supra*, note 62 at 188.

¹²¹ *Id.*

¹²² *Id.* at 189. Note the application of the rule in *Hodge's Case* in the last sentence. James Leavy, *Market Power and Public Policy: A Comparison of North American and European Legislation* (1977), 9 Ottawa L.Rev. 1 at 15, n. 74, states: "the Court specifically refrained from equating conscious parallelism with conspiracy."

Lerner J. cited evidence that a number of executives in the course of the eleven months became proponents of the open price policy.¹²³ Second, in June of 1963 Robertsteel tried to initiate the scheme by publishing its price list. Some firms adopted it, but because Armco did not, the first attempt did not "take." Both of these occurrences might be interpreted as helping to set the stage for the next attempt to arrive at parallel behaviour. As we discussed above, a number of "trials" may be necessary before the conscious parallelism comes about. However, in view of the specific characteristics of the metal culvert industry at the time (excess capacity, easy entry and Armco's position as technological and cost leader) and in view of the relative complexity of the parallel policies adopted (the three-zone delivered pricing scheme), the evidence was sufficient to overcome the "beyond a reasonable doubt" burden, notwithstanding the circumstantial nature of the evidence.

Not only did Mr. Justice Lerner infer a conspiracy entirely on the basis of circumstantial evidence but he also sought to extend the Canadian law by borrowing the broader concept of "arrangement" from an English combines case, *British Basic Slag Ltd. v. Registrar of Restrictive Agreements*.¹²⁴ Lerner J. quoted the words of Willmer L.J. in that decision:

For when each of two or more parties intentionally arouses in the others an expectation that he will act in a certain way, it seems to me that he incurs at least a moral obligation to do so. An arrangement as so defined is therefore something "whereby the parties to it accept mutual rights and obligations."¹²⁵

In the same case, Diplock L. J. first quoted from the judgement of Cross J. in the High Court:

[A]ll that is required to constitute an arrangement not enforceable in law is that the parties to it shall have communicated with one another in some way, and as a result of the communications each has intentionally aroused in the other an expectation that he will act in a certain way.¹²⁶

Then Lord Diplock gave his own definition of an "arrangement":

[I]t is sufficient to constitute an arrangement between A and B, if (1) A makes a representation as to his future conduct with the expectation and intention that such conduct on his part will operate as an inducement to B to act in a particular way, (2) such representation is communicated to B, who has knowledge that A so expected and intended, and (3) such representation or A's conduct in fulfilment of it operates as an inducement, whether among other inducements or not, to B to act in that particular way.¹²⁷

As we shall see, the adoption of these definitions by Mr. Justice Lerner was rejected by the Appeal Court, although his decision was upheld.

e. The Appeal Court Decision

On February 2, 1976, the Ontario Court of Appeal unanimously upheld the Trial Court's decision with respect to seven of the ten corporations

¹²³ *Supra*, note 62 at (C.C.C.) 180.

¹²⁴ *British Basic Slag v. Registrar of Restrictive Agreements*, [1963] 1 W.L.R. 727.

¹²⁵ *Id.* at 739, quoted in *Armco, supra*, note 62 at 191.

¹²⁶ *Id.* Diplock L.J. was quoting Cross J.'s decision in the case at the High Court (Chancery) level: *Re British Slag Ltd.'s Agreements*, [1962] 3 All E.R. 247 at 255.

¹²⁷ *Supra*, note 124 at 747, quoted in *Armco, supra*, note 62 at 191.

(lowering the fine imposed in one instance) in a judgment written by Houlden J.A.¹²⁸ However, the importance of the case lies in the ruling of Houlden J.A.:

If, however, the parties have acted in the manner described by the English Court of Appeal in *British Basic Slag*, there is not necessarily an "arrangement" within the meaning of s. 32(1)(c) . . . for s. 32(1)(c) there must be the mutual arriving at an understanding or agreement, and under the *British Basic Slag* test, this element of mutuality is not necessarily present.¹²⁹

While concluding that the trial judge was "wrong . . . to refer to the *British Basic Slag* definition,"¹³⁰ the Appeal Court would not overturn the judgment. Houlden J.A. cited eight specific passages from Lerner J.'s judgment in which the trial judge "had made clear and unequivocal findings that the parties had entered into an agreement or arrangement to prevent or lessen competition."¹³¹ He ruled that the reference to the *British Basic Slag* definition of arrangement was "mere surplusage"¹³² and "was unnecessary and did not affect the result at which [the trial judge] arrived."¹³³

The corporations also attacked, in their appeal, the application of the rule in *Hodge's Case*, saying Lerner J. drew incorrect or improper inferences from the evidence. Houlden J.A. ruled that while some of the findings of fact and inferences drawn "might have been more aptly expressed and some are undoubtedly wrong (it would have been astounding if this were not so in a trial of this magnitude), there is still an abundance of circumstantial evidence to support the trial Judge's conclusion that an agreement or an arrangement had been entered into to prevent or lessen competition unduly."¹³⁴ The rule in *Hodge's Case* had been correctly applied.

3. *The Atlantic Sugar Case*

On December 19, 1975 Mr. Justice Kenneth Mackay handed down his decision in *R. v. Atlantic Sugar Refineries Co. Ltd.*¹³⁵ in which he acquitted the three largest sugar refiners in Eastern Canada of violating section 32(1) of the *Combines Investigation Act*. Part of his decision dealt with the issue of conscious parallelism. In particular, it was argued, as part of the second count alleging an undue lessening of competition as opposed to the unreasonable enhancement of price involved in the first count,

[t]hat in 1960, Redpath [formerly Canada and Dominion Sugar] adopted the base stock system for the pricing of refined sugar. This was derived from matching the refined sold with the replacement cost of a similar quantity of raw sugar on the day of the sale, plus freight, duty, the preferential premium of 75 cents per hundredweight and a refiners' margin. To this was then added freight charges from the refinery nearest the customer to the latter's plant or warehouse. The

¹²⁸ *Re The Queen and Armco Canada Ltd.* (1976), 24 C.P.R. (2d) 145.

¹²⁹ *Id.* at 153.

¹³⁰ *Id.* at 154.

¹³¹ *Id.*

¹³² *Id.*

¹³³ *Id.* at 155.

¹³⁴ *Id.* at 156.

¹³⁵ *The Queen v. Atlantic Sugar Refineries Co. Ltd.* (1976), 26 C.P.R. (2d) 14.

price list based on this formula was invariably, simultaneously and exactly followed, item by item, by the other two accused, although actual freight costs differed for each refiner.¹³⁶

With respect to this charge of price fixing during the period 1960 through May 1973, Mr. Justice Mackay set out the Crown's argument as follows:¹³⁷

1. The accused agreed with the Commonwealth sugar producers' cartel to price raw sugar on the basis of the London Daily Price, a price which was unrelated to the actual market price of sugar.
2. They also agreed that a preference clause be included in raw sugar contracts fixing the preferential premium at 75 cents and recognizing that figure as a non-negotiable factor, thus preventing the amount of the preference rebated to the producers from being established by competition between buyer and seller.
3. They adopted a unique system of pricing their refined sugar—the base stock system—which was based on raw sugar prices unrelated to the market price.
4. The accused, who controlled at least 90% of the eastern Canadian market, arranged to adopt identical price lists based on this pricing system and the result was undue prevention or lessening of competition.

He then summarized what he believed to be the defence theory:¹³⁸

1. The L.D.P. is an internationally recognized index for the determination of the price of raw sugar on the free world market.
2. The preference clause was written into raw sugar purchase contracts by both buyer and seller and was never intended to freeze the premium at 75 cents but was simply intended to protect the accused under existing contracts, should the tariff preference have been reduced before delivery, by limiting the rebate to 75%.
3. The base stock system, regardless of its merits, was conceived solely by Tate and Lyle and its subsidiary, Redpath, and was simply copied by the other two accused.
4. Identical price lists are not necessarily evidence of collusion to fix prices; they may be, as in this instance, an example of price leadership without prior arrangement, tacit or otherwise.

Mackay J. noted that both sides agreed that the Commonwealth Sugar Association is a cartel which its members euphemistically call a "club." As early as 1954, it had limited price competition on sales to Canada in order to maintain a 75 cents per hundredweight preference (premium) above the world price. Prior to 1960, raw sugar was priced on a cargo-by-cargo or parcel-by-parcel basis. In the early 1960's, the system of deferred pricing of raw sugar was introduced under which the Canadian buyer would pay the London Daily Price (LDP) plus 75 cents per hundred pounds less a freight equalization factor. The result was that raw sugar could be priced at the time it was drawn from the refiner's warehouse, or at the time the contract was signed or the date the raw sugar was delivered whichever was most advantageous to the refiner. The adoption of this new system by the three big eastern refiners was negotiated by a senior official of Tate and Lyle, the giant English sugar producer and refiner, which in 1959 had obtained effective

¹³⁶ *Id.* at 61.

¹³⁷ *Id.* at 90.

¹³⁸ *Id.* at 91.

control of Redpath Industries. The new formula permitted hedging by the refiners to reduce the risk of changes in the price of raw sugar.¹³⁹ The pricing of raw sugar on a deferred basis was also incorporated into the pricing of refined sugar.

The judge acknowledged, "[i]t may well be true that the L.D.P. is not an accurate reflection of the actual market price of raw sugar, since spot sales form a very small proportion of the 5,000,000 tons traded annually on the London Exchange."¹⁴⁰ Yet he went on to conclude, "even if, as the Crown contends, the L.D.P. is an artificial price it is a universally accepted index for pricing raw sugar and no blame can accrue to the accused for using it."¹⁴¹

Since the price for refined sugar is calculated directly from the LDP for raw sugar and all the refiners follow Redpath's refined sugar price list, agreement to follow the LDP constitutes the first step in establishing the whole plane of prices for refined sugar. Furthermore, the LDP is influenced by the fact that Tate and Lyle is not only a major producer of raw sugar, but also dominates the market for refined sugar in the United Kingdom. The importance of Tate and Lyle's activities as a producer became apparent when the judge observed that while the other two eastern Canadian refiners made "strenuous efforts . . . continually to chisel away"¹⁴² at the 75 cents preference paid to Commonwealth producers of raw sugar, Redpath, owned by Tate and Lyle, did not do so. The judge said Redpath "was anxious to preserve for the producers 75 cents of the [original \$1.00] preference. . . ."¹⁴³

In 1960, the base stock system of pricing refined sugar was introduced at Redpath by Tate and Lyle representatives. It replaced the average cost of inventory method, which continues to be used by United States refiners.¹⁴⁴ Redpath's price of refined sugar under the base stock system is calculated as follows:¹⁴⁵

$$\begin{array}{l}
 \text{Redpath's price of} \\
 \text{refined sugar FOB} \\
 \text{Toronto and Montreal} \\
 \text{basing points}
 \end{array}
 =
 \begin{array}{|l|}
 \hline
 \text{LDP price of raw} \\
 \text{sugar per 100 lbs.} \\
 \text{CIF (includes 75¢} \\
 \text{preference)} \\
 \hline
 \end{array}
 +
 \begin{array}{|l|}
 \hline
 \text{freight, in-} \\
 \text{surance, and} \\
 \text{discharge} \\
 \text{costs} \\
 \hline
 \end{array}
 +
 \begin{array}{|l|}
 \hline
 \text{import} \\
 \text{duties} \\
 \text{(28.7¢ per} \\
 \text{100 lbs.)} \\
 \hline
 \end{array}
 \\
 +
 \begin{array}{|l|}
 \hline
 \text{adjustment for} \\
 \text{7\% loss on re-} \\
 \text{fining} \\
 \hline
 \end{array}
 +
 \begin{array}{|l|}
 \hline
 \text{refining} \\
 \text{margin} \\
 \hline
 \end{array}$$

Because of the deferred pricing of raw sugar purchases, the Canadian refiners were able to purchase their raw sugar at the LDP price on the date when the raw sugar was to be refined even though they had contracted for

¹³⁹ *Id.* at 105-08. It also permitted the firms to amass huge profits in offshore corporations (beyond the reach of Revenue Canada) from trading in raw sugar futures.

¹⁴⁰ *Id.* at 93.

¹⁴¹ *Id.*

¹⁴² *Id.* at 94.

¹⁴³ *Id.* at 59.

¹⁴⁴ *Id.* at 95.

¹⁴⁵ *Id.* at 58-59.

the raw sugar months earlier. Even if all refiners adopted the same formula their price of refined sugar would not be the same, for as Mackay J. pointed out, "refining and other expenses would not normally have been identical for each refinery."¹⁴⁶ Redpath, which had been the admitted industry price leader between 1949 and 1959,¹⁴⁷ continued to hold this position because the other refiners set their list prices exactly parallel to Redpath's. Mackay J. described the method of price determination from 1960 to 1973 as follows:

[the other refiners'] sales managers said that instead of making their own price calculations, they simply followed Redpath's price lists which were posted each day in the lobby of Redpath's offices and were communicated to them by sugar brokers, customers or even telegraph company employees with whom they had friendly relations or others unidentified. Whenever they learned of changes in Redpath's prices, they immediately issued new price lists of their own.¹⁴⁸

It should be noted that the base stock pricing system, a device for communicating appropriate price changes for refined sugar in a fluctuating market for raw sugar, was adopted by Redpath shortly after the refiners were the subject of a Restrictive Trade Practices Commission report; the report concluded "that the practices engaged in by the three eastern refiners with respect to common basis prices, equalized freight rates, common packages differentials and the use of price concessions have limited competition in the eastern sugar refining industry to the detriment of the public."¹⁴⁹ In addition, there was evidence that the refiners conspired with foreign suppliers to restrict the importation of refined sugar. In March of 1962, the big three eastern refiners were charged with conspiring to lessen competition unduly in the production of refined sugar under the *Criminal Code*. All three subsequently pleaded guilty and were convicted. Each was fined \$25,000 and made subject to an order prohibiting the continuation or repetition of the offence.¹⁵⁰

One can view Redpath's adoption of the base stock method of pricing refined sugar as a benefit to the eastern refiners. It provided the means of coordinating their pricing in the face of the price fluctuations of raw sugar without resort to collusion, of which they had previously been convicted. As the president of Atlantic Sugar Refineries Co. Ltd. put it, ". . . I applauded the management of Redpath at the time for finding this basis of relating refined to the LDP . . . we were very happy to follow that."¹⁵¹ Coordination in this industry was much easier in a number of respects than in the case of metal culverts. While excess capacity existed, entry into the industry was

¹⁴⁶ *Id.* at 96.

¹⁴⁷ *Id.* at 99.

¹⁴⁸ *Id.* at 96.

¹⁴⁹ *Report Concerning the Sugar Industry in Eastern Canada* (Ottawa: Restrictive Trade Practices Commission, 1960) at 312.

¹⁵⁰ *Report of the Director of Investigation and Research, Combines Investigation Act*, for the year ended March 31, 1963 (Ottawa: Queen's Printer, 1963) at 16. Atlantic Sugar appealed the terms of the Prohibition Order. A final decision upholding the Crown and the original terms of the order was not rendered until July 21, 1967 by the Quebec Court of Appeal. Although the indictment specified only the period 1950 to 1953, the Restrictive Trade Practices Commission indicated in their report that it had "extended over a considerable number of years." (*Supra*, note 149 at 9).

¹⁵¹ *Supra*, note 135 at 95-96.

expensive in terms of time and capital. More important, in the early 1960's there were only three sellers of refined sugar in eastern Canada.¹⁵² Finally, the industry was characterized by a stability of demand and, hence, during recessions the pressure of high fixed costs did not lead to price cutting.

Mackay J. pointed out that "price conformity and identical price lists are characteristic of an oligopolistic industry" and that they may well be consistent with independent competitive decisions" or be the result of an agreement.¹⁵³ Citing Lerner J. in the *Armco* case,¹⁵⁴ he stated:

. . . if conformity is the result of price leadership by the industry leader and a conscious effort by other members of the industry to follow the leader, to parallel its prices, then, although the result might be an undue prevention of competition, "it would not offend the [Combines Investigation] Act because there would have been no agreement or arrangement, direct or tacit."¹⁵⁵

Mr. Justice Mackay clearly indicated that conscious parallelism without collusion does not violate the Act. He stated: "I am of [the] opinion that while identical price lists might give rise to an inference of arrangement to fix prices, such inference is unwarranted where it is shown that conformity of prices was not arrived at as a result of collusion."¹⁵⁶ He cited and apparently adopted D. H. W. Henry's view of price changes of staple commodities.

Except during brief periods of change, the price of any homogeneous commodity will tend to be the same for all sellers and buyers in a given market area. At the first suggestion of any permanent differential, buyers will switch their custom to the company offering the lowest price and sellers therefore will have to bring their prices to meet that of the lowest competitors. Consequently, in those commodity markets where sellers are few and many sales are made daily to wholesalers, retailers and consumers, a price change instituted by any one seller will usually be communicated within the hour to his competitors and the necessary adjustments made almost instantly.¹⁵⁷

After reviewing the testimony of executives of all the other eastern sugar refiners, Mr. Justice Mackay concluded:

Since the Act does not prohibit a member of an industry from taking into account and following his competitors' price changes, be they up or down, it follows that he is not prohibited from taking into account and following the system upon which these price changes are made.¹⁵⁸

By 1973 a total of six refiners served the market from Ontario to Newfoundland, but coordination in this oligopoly was even easier than the number suggests. Quebec Sugar Refinery sells all its output in a semi-refined form to Redpath. Cartier Sugar is a wholly owned subsidiary of Steinberg's Limited

¹⁵² There were four producers but Quebec Sugar Refinery sold all its output to Redpath. Cartier Sugar did not begin operation until 1963.

¹⁵³ *Supra*, note 135 at 96.

¹⁵⁴ *Supra*, note 62 at 187.

¹⁵⁵ *Supra*, note 135 at 97.

¹⁵⁶ *Id.* at 98.

¹⁵⁷ *Id.* The words originally come from *Report of the Director of Investigation and Research, Combines Investigation Act*, for the year ended March 31, 1966 (Ottawa: Queen's Printer, 1966) at 13.

¹⁵⁸ *Id.* at 100.

which absorbs a substantial portion of its output; Westcane Sugar is a wholly-owned subsidiary of George Weston Limited whose retail and manufacturing operations are also large buyers of sugar. The big three (Atlantic, Redpath, and St. Lawrence) jointly account for over ninety per cent of the market.¹⁵⁹ The remainder of the country is subject to the complete monopoly of B.C. Sugar, which in turn, bases its prices on the lowest list price issued by the eastern refiners plus freight from its basing points.¹⁶⁰ Unlike the metal culvert manufacturers, oligopolistic coordination in sugar did not apparently require exhortation, education or tacit agreement. The big three have jointly dominated the market since before the turn of the century. They are highly experienced and practiced oligopolists. They achieved through conscious parallelism that which had previously required collusion.

a. Price Shading and Market Sharing

Having ruled that price leadership-followership is not prohibited by the *Combines Investigation Act*, Mr. Justice Mackay went on to review the testimony of a number of large industrial purchasers of sugar, accounting for sixty per cent of all sugar consumption. He observed: "although all Canadian refiners had identical price lists there were . . . exceptions when the actual sales prices varied as a result of customers' discounts, not including discounts for prompt payment. . . . Testimony of the officers of . . . industrial sugar users . . . was to the effect that the refiners' quotes invariably differed appreciably."¹⁶¹

Two important points should be made here. First, when a few sellers face a relatively small number of large buyers the outcome in terms of price and output is indeterminate. The fact that such large buyers obtained their sugar, or a portion thereof, at less than the list price is a reflection of their *oligopsony* power. It is a fairly common occurrence for large industrial buyers to be served at negotiated prices while smaller buyers pay the higher list price. A related phenomenon may also be present—price discrimination. With differential price elasticities and some degree of separability between the industrial and consumer markets, sellers with market power may find it more profitable to charge a different markup, above the relevant marginal costs, to different customers. However, lower prices to big buyers may not involve price discrimination, but rather the recognition of their buying power together with the fact that the costs of serving such customers are lower than those for smaller purchasers.

Second, the industry-wide adoption of Redpath's prices, which included a large refining margin, provided a safe plane from which deviations, such as lower prices to large buyers, did not seriously erode profitability and essential price stability. Evidence of the high refining margin in Canada is provided in

¹⁵⁹ This figure was calculated from the following plant capacities (in thousands of pounds per day): Atlantic, 2,400; Redpath, 4,300; St. Lawrence, 1,900; Quebec Sugar Refinery, 350; and Cartier, 500. Westcane (900) did not come into full operation until the end of 1974. See *Sugar Prices II: The Canadian Refining Industry* (Ottawa: Food Prices Review Board, 1975) at 6.

¹⁶⁰ *Supra*, note 135 at 96.

¹⁶¹ *Id.* at 100-01.

a Tariff Board Report on sugar published in 1971.¹⁶² In eight of the years between 1961 and 1970 the Canadian refiners' margin exceeded that of their American counterparts. In all ten years the Canadian margin exceeded that in the United Kingdom. Despite rather substantial differences in costs of production all refineries in Canada earned rates of return well above other industries. In the late 1960's, the sugar refiners' before tax profits, as a percentage of sales, were more than double the average in manufacturing. Apparently, any discounts from list prices given to industrial buyers did not prevent the sugar refiners from enjoying the economic benefits of their oligopoly position.

In addition to the allegation of price fixing, the Crown argued in *Atlantic Sugar* that there was an agreement among the companies in the industry as to the market share to be enjoyed by each. The shares allotted to the firms during World War II and their shares in 1949 were as follows:¹⁶³

	W.W. II	1949
Atlantic	35.5%	35.6%
Redpath	43.0	42.7
St. Lawrence	21.5	21.7

Mackay J. then described what happened with respect to market shares:

During the next decade, the market shares varied slightly. But in 1958, Redpath having just opened its Toronto refinery and being anxious to increase sales and recoup some of the heavy expenses involved, surreptitiously began to cut prices in the Toronto area. Atlantic felt the loss of sales in that area and so began to cut its prices there, although this represented a serious expense, due to the absorption by Atlantic of the unsubsidized portion of the freight from the refinery in St. John to the nearest basing point which was now Toronto instead of Montreal as it had been before the new refinery was constructed. The price war spread to include St. Lawrence. There were two results—first: Redpath increased its market share at the expense of the others from 42.8% in 1957 to 46.6% in 1958. Secondly: it lost the price war against its two well-funded opponents, and having sustained serious financial losses it was ripe for a take-over by Tate and Lyle.

Thereafter, each of the accused settled down to a policy of maintaining their traditional market shares.¹⁶⁴

Mackay J. drew the following conclusion: "Although each stressed that this was the result of an independent decision, one would be ingenuous not to be aware that there was and continues to be a tacit agreement to this effect."¹⁶⁵ He then went on to expand on this point, saying,

On the evidence, I find that the maintenance of traditional market shares—which were adjusted but in the same proportion when Cartier came on stream—was the result of a tacit agreement between the accused. But in my opinion, it has not been shown that this agreement was arrived at with the intention of

¹⁶² *Report by the Tariff Board (Ref. No. 146: Sugar)* (Ottawa: Information Canada, 1971) at 68, Table 24.

¹⁶³ *Supra*, note 135 at 101-02.

¹⁶⁴ *Id.* at 102.

¹⁶⁵ *Id.* It is very hard to imagine how conscious parallelism with respect to the price of 40% of the industry's output and negotiated prices to large buyers who account for most of the other 60%, could result in such highly stable market shares without at least a tacit agreement.

unduly preventing or lessening competition. The reason for maintaining traditional market shares was to avoid a price war which would have resulted had the accused taken the only method of increasing them by price cutting through extensive discounts. Nor am I able to infer from the totality of the evidence on this point, including overt acts, that market shares were maintained for the purpose of stifling competition.¹⁶⁶

His reasoning may be challenged on several points. First, where the accused jointly account for over ninety per cent of the market it seems impossible that any market sharing agreement could be other than undue. Mackay J. appears to have agreed with this proposition earlier in his judgment:

Where the accused at the beginning of the period controlled 99.8% of the eastern Canadian market, an agreement to lessen competition would be tantamount to extinction, and so would be undue. The extinction of competition would in those circumstances require the combined action of all the accused to be effective, for if one decided to allot a portion of its market share to a newly arrived competitor, whatever the other two planned would be for nought.¹⁶⁷

With respect to this last statement, the defendants' gentlemanly accommodation of Cartier, whose entry added less than six per cent to the capacity of the industry at the time, is proof of their ability to coordinate their behaviour so as to avoid effective price competition and lessen competition unduly.

Second, the Crown should not be required to prove that the accused entered into an agreement with the intent to lessen competition unduly, but only that they entered an agreement, which if carried out, would lessen competition unduly. This point was made by Kerwin J. in *Container Materials Ltd. v. The King* where he said,

It was argued that it was not sufficient for the Crown to show an agreement or arrangement, the effect of which would be unduly to prevent or lessen competition, but that the agreement or arrangement must have been intended by the accused to have that effect. This is not the meaning of the enactment upon which the count is based. *Mens rea* is undoubtedly necessary but that requirement was met in these prosecutions when it was shown that the appellants intended to enter, and did enter, into the very arrangement found to exist.¹⁶⁸

Mackay J. used this passage only to support the proposition that: "It need not be shown that if the agreement was put into effect, that prices were enhanced, but simply the agreement must have been intended to have that effect."¹⁶⁹

For both of these reasons, it is difficult to accept Mackay J.'s conclusion that there was a market-sharing agreement, but that it did not unduly lessen

¹⁶⁶ *Id.* at 103 (emphasis added).

¹⁶⁷ *Id.* at 30.

¹⁶⁸ *Container Materials, Ltd. v. The King*, [1942] S.C.R. 147; 1 D.L.R. 529; 77 C.C.C. 129 at (C.C.C.) 140.

¹⁶⁹ *Supra*, note 135 at 23. Perhaps Mackay J. was exhibiting great prescience. On April 29, 1977 in *Aetna Insurance Company v. The Queen* (1977), 34 C.C.C. (2d) 157, the majority of the Supreme Court of Canada, *per* Ritchie J., accepted the view that "what is criminal is an agreement that is intended to lessen competition improperly, inordinately, excessively, oppressively or one intended to have the effect of virtually relieving the conspirators from the influence of free competition," at 170. The Chief Justice, with Judson J. and Spence J. concurring, wrote a dissenting opinion citing the words of Kerwin J. as we have done.

competition. There is other evidence to suggest, in the case of Cartier, that tougher tactics having failed to prevent entry, accommodation to preserve oligopolistic stability was the strategy employed.¹⁷⁰

4. *The Large Lamps Case: R. v. Canadian General Electric Company Ltd.*

Canadian General Electric Company Limited (CGE), Westinghouse Canada Ltd., and GTE Sylvania Canada Limited were charged with two counts of monopoly and one of conspiracy during the period January 1, 1959 to August 25, 1967.¹⁷¹ It is the conspiracy charge, under section 32(1)(c) of the *Combines Investigation Act*, which is germane to this discussion of conscious parallelism cases in Canada. Mr. Justice Pennell summarized the Crown's charge of conspiracy as follows:

. . . the accused conspired to lessen unduly competition by an agreement or arrangement to adopt simultaneously and follow religiously a virtually identical sales plan for the distribution and pricing of electric large lamps through the medium of consignment agents, *inter alia*, and the practice of inducing distributors to maintain sales prices. . . .¹⁷²

The defendants contended that there was no agreement among themselves to adopt and follow the sales plan first put forward by CGE in 1959 and modified in 1961. Pennell J. stated their position:

. . . the behaviour under attack represents no more than rational individual decisions in the light of relevant economic facts; that this industry is an oligopoly with a homogeneous product; that natural oligopolistic pricing does not violate the Act; that the structure of the market demanded the published price list of the competition and thus prices could not be different for a substantial period of time; and that the actions of the accused were based on pure, non-collusive, oligopolistic parallelism of action, a practice described by the term "conscious parallelism."¹⁷³

Describing conscious parallelism as "one of the great battlefields of anti-combines litigation," Pennell J. defined it as the "pricing that emerges out of an oligopolistic market setting without communication or agreement

¹⁷⁰ Mackay J. indicated that Cartier Sugar's initial difficulties (until it was purchased by Steinberg) were not due to its inability to obtain a share of the market. Earlier the judge had cited the testimony of a Cartier executive that it followed Redpath's price list in which he said "if I had a lower price, I would be swamped [with orders] and I wouldn't be able to satisfy my customers." (at 100) The point the judge ignored (although he reviewed the testimony earlier in his opinion) was the effort by Atlantic Sugar's president to have Cartier's entry "nipped in the bud" (at 89) by Senator Salter Hayden, who was also a director of Atlantic and Chairman of the powerful Standing Senate Committee on Banking, Trade and Finance. The major refiner's efforts to block the entry, and later to reduce the competitive effectiveness of Cartier, are set out in a 60-page letter, dated December 11, 1970, to the Minister of Finance by Robin Austin (the founder of Cartier). Their tactics, (according to Austin) included: attempts to block financing, attempts to cut off the supply of raw sugar, bomb threats, threats of refusal to deal with suppliers who dealt with Cartier, and sabotaging raw sugar cargoes with bailing twine.

¹⁷¹ *R. v. Canadian General Electric Company Limited* (1976), 29 C.P.R. (2d) 1; 34 C.C.C. (2d) 489.

¹⁷² *Id.* at (C.C.C.) 498. All further references will be to the C.C.C. report of the case.

¹⁷³ *Id.* at 499.

among the sellers."¹⁷⁴ He went on to say, "The crux of the theory of conscious parallelism is . . . that the oligopolists are interdependent in their pricing: they base their pricing decisions in part on anticipated reactions to to them."¹⁷⁵

a. Facts of the Case

In his findings of fact, Pennell J. held that electric large lamps, which include incandescent, fluorescent and mercury lamps, were an essentially homogeneous product; that they constituted a distinct segment of the lamp industry in terms of manufacture and sale; that the market for such lamps was national; and that the three accused accounted for ninety-five per cent of domestic sales and manufacture. He asserted that the difference between the ninety per cent share admitted by the defendants and his finding of ninety-five per cent was "purely academic."¹⁷⁶

The motivation for the establishment of the large lamp sales plan of 1959 was that prior to that time, "the industry had gone through a period of intense pricing cutting."¹⁷⁷ Although such competition had not resulted in losses,¹⁷⁸ CGE anticipated that the plan would reduce price competition and increase profits. CGE's first sales plan, dated January 6, 1959, "covered all aspects of distribution, sales and supply of large lamps by CGE to its agents and distributors and by such agents and distributors to their trade customers and to customers who purchased by tender."¹⁷⁹ The price to each of the various distributors and customers was determined by the specified list price less the discount set out for each distributor and type of customer. Agents accounting for three-quarters of CGE large lamp sales were put on consignment.¹⁸⁰ By January 19, both Westinghouse and Sylvania had obtained copies of the sales plan which was not to become effective until April 1, 1959. The Crown argued that the advance circulation of the 1959 plan was to allow the market leader to signal to its competitors a change in market strategy. To this CGE replied that common sense required advance publication in order for CGE to ascertain whether its competitors would follow.¹⁸¹ Both Westinghouse and Sylvania did adopt plans very similar, but not identical, to CGE's. As a result, two-thirds of Westinghouse's lamp sales were made on consignment.¹⁸² Beginning in the summer of 1963 and ending in the spring of 1964 Sylvania placed its agents selling to the commercial and industrial market, representing 75 per cent of its sales, on consignment.¹⁸³ Following

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Id.* at 502.

¹⁷⁷ *Id.* *Electric Large Lamps* (Ottawa: Restrictive Trade Practices Commission, 1971) at 7 indicates that such price cutting occurred during 1956, 1957 and 1958.

¹⁷⁸ *Supra*, note 171 at 504.

¹⁷⁹ *Id.*

¹⁸⁰ *Id.* at 505.

¹⁸¹ *Id.* at 506.

¹⁸² *Id.* at 507.

¹⁸³ *Id.*

the introduction of CGE's 1959 sales plan, "[t]he price lists and discounts under the three plans were substantially identical to the knowledge of the accused."¹⁸⁴

While the 1959 plan sharply reduced the extent of price competition a certain amount of hidden discounting did occur. Mr. Justice Pennell concluded: "a survey of the prices of the three accused as published and as reflected in actual sales, shows remarkable stability and co-ordination over the alleged conspiratorial period. By contrast, the conditions in the market-place prior to 1959 were chaotic."¹⁸⁵ There were also problems in discount structure for various types of distributors; the market was not perfectly segmented.¹⁸⁶ Again CGE acted as the industry leader, announcing its 1961 sales plan at a meeting of the Canadian Electrical Distributors Association in April 1961. The plan, based on net prices, became effective on September 1, 1961. If the 1959 plan was good for CGE, the 1961 plan would be even better. As one CGE internal communication put it:

. . . if we can introduce this new Large Lamp Sales Plan as it stands and maintain our present volume of business, we should increase our profits something like \$300,000.00 annually.¹⁸⁷

The author of this statement, a top CGE sales executive, concluded: "These are big stakes and I am sure you will agree, well worth taking some short term risks for."¹⁸⁸

CGE's 1961 plan was distributed to its own agents on or about July 5, 1961. As in 1959, both Westinghouse and Sylvania "came [to] an early decision . . . to coordinate their activities and implement substantially similar plans based on the same distribution scheme and price schedules and with the same commencement date. . . ."¹⁸⁹ Although Westinghouse did not distribute its own plan until November 1961, it followed the CGE plan from the date of its introduction, September 1, 1961.

Through the use of price schedules based on net prices, the lamp manufacturers hoped to completely eliminate price competition that might occur by design or as the result of error. After the introduction of the 1961 plan, even greater efforts were made by all manufacturers to ensure that the prices established in their plans were enforced. As Pennell J. put it: "The three defendants strictly and closely monitored their agents in all their dealings"; he went on to assert, "the presence of enforcement activities may be relevant to a consideration of a charge of conspiracy."¹⁹⁰ Westinghouse agents were required to calculate their price quotations to three decimal places. Agents who cut prices were threatened with the loss of their franchises. CGE re-

¹⁸⁴ *Id.* at 508.

¹⁸⁵ *Id.* at 509.

¹⁸⁶ *Id.* at 510.

¹⁸⁷ *Electric Large Lamps*, *supra*, note 177 at 69.

¹⁸⁸ *Id.*

¹⁸⁹ *Supra*, note 171 at 511-12.

¹⁹⁰ *Id.* at 513.

quired its agents to withdraw tenders which did not exactly conform to prices set out in the sales plan.

Defence counsel cited the ruling in *R. v. Canada Cement Lafarge Ltd.*¹⁹¹ that conscious parallelism without collusion is not an offence. However, Pennell J. refused to accept the idea that conscious parallelism has read conspiracy out of section 32 of the *Combines Investigation Act*. He said, "I am of the opinion that the theory of oligopoly pricing is irrelevant to the determination of whether or not the accused have offended the proscription on them under the conspiracy section of the Act."¹⁹² Later he stated: "I do not say that proof of parallel business behaviour conclusively establishes an agreement contrary to the provisions of the *Combines Investigation Act*."¹⁹³

b. Finding of an Agreement

Mr. Justice Pennell found the three lamp manufacturers guilty of the conspiracy charge. He found an agreement among the defendants, later held to be an undue lessening of competition, on the basis of at least eight pieces of documentary evidence, including letters to competitors. For example, after one of CGE's agents won a tender by quoting a five per cent discount for cash rather than the two per cent specified in the sales plan, a CGE executive wrote to the Westinghouse district manager indicating that the agent would receive no profit on the transaction as the difference between the tender price and the franchised dealer's price was to be donated to charity! The CGE executive described this as "the only fair solution to the problem" and invited the Westinghouse executive to call him if further information was required.¹⁹⁴ Pennell J. drew the following conclusions:

It contradicts experience that a man occupying the position of a sales manager of C.G.E. should inform his competitor of a breach of C.G.E.'s sales plan by a C.G.E. agent *unless there was an arrangement between the competitors*.¹⁹⁵

Describing the letter as "a document which speaks volumes" the Judge went on to say:

Genuine competitors do not make reports of their business transactions to their rivals. . . . This was not the conduct of a competitor but of a sales manager who believed that the accused were united in an agreement, express or implied, to act together and pursue a common purpose.¹⁹⁶

He then quoted a Sylvania inter-office memorandum which indicated that Sylvania had notified Westinghouse and CGE about a \$60.00 "error" in a quotation to the Vancouver School Board. Mr. Justice Pennell asked the following questions:

Why should there be need to inform a competitor of an error made within one's

¹⁹¹ *Supra*, note 59.

¹⁹² *Supra*, note 171 at 517. It is unclear from the context to what "them" refers.

¹⁹³ *Id.*

¹⁹⁴ *Id.* at 518.

¹⁹⁵ *Id.* (emphasis added).

¹⁹⁶ *Id.*

own marketing system? What right would a competitor have to complain to a rival's head office of genuine competition?¹⁹⁷

He then points out, "the document is very intelligible if there was an agreement among the accused to abide by their sales plans."¹⁹⁸

Similar letters and memoranda are cited. In one, a CGE executive, in reference to tenders submitted to the Federal Government, stated: ". . . it is obvious that Sylvania is not operating under the policy we established many years ago."¹⁹⁹ In another, a Sylvania executive, concerned over some anomalies in the various pricing schedules stated: "Propose that someone will be in touch with their friends up the river [Westinghouse] regarding these differences and an understanding will be reached before any action is taken."²⁰⁰ A confidential Sylvania memorandum of October 3, 1963, would appear to indicate that the agreement between the big three lamp makers restricted the variety of lamps to be produced. It stated:

. . . we are all in agreement that this [the addition of more 750 hour lamps] would not be in keeping with our main objective of recent years to reduce the number and quantity of types that have to be supplied to the C&I [commercial and industrial] market.²⁰¹

After reviewing the eight pieces of documentary evidence, Mr. Justice Pennell noted that there were sound business reasons for Westinghouse and Sylvania to adopt the CGE sales plans.²⁰² He also noted that all three were "sophisticated companies" and "through a sophisticated set of signals, the defendants had the potential to communicate effectively with one another and co-ordinate their activities without conspiratorial meetings."²⁰³

Mr. Justice Pennell concluded that the published price lists of Sylvania and Westinghouse were aligned to those of CGE and that "list prices were usually—but not invariably—the market price."²⁰⁴ Because CGE did not initiate all the price changes, which were immediately followed by all firms, it could only be considered a "barometric" price leader.

He also concluded "[t]hat the continuing communications among the defendants went far beyond the alleged business purpose of purchasing lamps from one another."²⁰⁵ Pennell J. was most concerned about the substance of these communications. In addition, "there were intra-defendant company communications, direct and indirect, at several levels of the distribution system, checking on deviations by competitors on price quotations and on prices charged by competitors for like products."²⁰⁶

¹⁹⁷ *Id.* at 519.

¹⁹⁸ *Id.*

¹⁹⁹ *Id.* at 520.

²⁰⁰ *Id.*

²⁰¹ *Id.* at 521.

²⁰² *Id.* at 522.

²⁰³ *Id.*

²⁰⁴ *Id.* at 523.

²⁰⁵ *Id.* at 524.

²⁰⁶ *Id.*

In general, Mr. Justice Pennell was not able "to reconcile the substantial unanimity of action taken by the accused with price conscious parallelism."²⁰⁷ In other words, the defendants' actions were more closely coordinated than would result from non-collusive oligopoly through conscious parallelism without communication among the firms. He went on to assert:

Communication is the essence of every conspiracy for only by it can common purpose be proved . . . Sustained consideration of the evidence brings conviction to my mind that there was an agreement among the accused to introduce and maintain an industry sales plan, thereby eliminating and suppressing price competition among themselves.²⁰⁸

Quaere whether Mr. Justice Pennell would have found that an agreement existed in the absence of the documentary evidence described above. It should be apparent that oral or written communication is not necessary for firms in an oligopoly to effectively communicate with one another. Actions often speak louder than words. Donald F. Turner writes

. . . there is no reason to exclude oligopolistic behavior from the scope of the term agreement simply because the circumstances make it possible to communicate without speech. It is not novel conspiracy doctrine to say that agreement can be signified by action as well as by words.²⁰⁹

One obvious form of indirect communication occurred when CGE announced its new sales plan in 1959 almost three months before it was to become effective. Its 1961 plan was announced in April to become effective in September. Such announcements were bids by CGE to become the price leader. The lead times are designed to ensure that potential followers have enough time to evaluate the proposal and indicate their acquiescence or disapproval, possibly by indirect means. Other evidence of non-verbal communication can be found in the fact that each of the three firms closely policed their distributors and punished price cutters. Word of this would reach rivals. Such actions are aimed at reassuring rivals that price competition is still held in very low regard and that they should not retaliate with an aggressive pricing policy. Compared to the behaviour in the *Armco* case, the various acts in this case would require a greater inferential leap to arrive at a finding of conspiracy, but not so large as to fail to meet the test in *Hodge's Case*.

c. Competition Lessened Unduly?

Having found that an agreement existed, Mr. Justice Pennell had to determine whether it lessened competition "unduly." In reviewing the interpretation of "undue" in Canadian jurisprudence, he considered the following cases: *R. v. Elliott*,²¹⁰ *Weidman v. Shragge*,²¹¹ *per* Duff J., and *R. v. Howard Smith Paper Mills Ltd.*,²¹² *per* Cartwright J. The virtual monopoly doctrine enunciated by Mr. Justice Cartwright in 1957 was not followed in *R. v.*

²⁰⁷ *Id.*

²⁰⁸ *Id.*

²⁰⁹ Turner, *supra*, note 41 at 665.

²¹⁰ (1905), 9 O.L.R. 648; 9 C.C.C. 505.

²¹¹ (1912), 46 S.C.R. 1.

²¹² *Howard Smith Paper Mills Limited v. The Queen*, [1957] S.C.R. 403; 8 D.L.R. (2d) 449; 118 C.C.C. 321.

*Abitibi Power & Paper Ltd.*²¹³ or by Laskin J.A. in his dissent in *R. v. J. J. Beamish Construction Co. Ltd.*²¹⁴ Pennell J. then reviewed the behaviour of the defendants during the course of the conspiracy, finding that the allegations of predatory conduct were untenable and that imports had not been impeded.²¹⁵ He also held that consignment contracts are not illegal, but he indicated that the test under the *Combines Investigation Act* "looks past the form of the arrangement to the use which is being made of that arrangement."²¹⁶ Pennell J. stated that "[t]he distinctive feature of the agreement was not the advance announcement of sales plans or prices but a requirement of adherence without deviation to the prices and terms publicly announced. . . . The surveillance of the consignment system is significant as it shows the degree to which the accused were concerned to escape the influence of the competitive market."²¹⁷ He held:

Any one of the accused acting alone perhaps might legitimately have required total adherence to its sales plan. An act harmless when done by one takes on the form of conspiracy when done by three dominating the market and acting in concert.²¹⁸

Pennell J. ruled that as a result of the three firms adopting very similar sales plans, including the consignment system, "price competition was stifled When the product is homogeneous, price is *a fortiori* the most important aspect of competition."²¹⁹ He acknowledged that while price competition did occur, more so during the 1959 plan, it was of the "sporadic hit-and-run" variety and not the "free and open competition to which the public is entitled."²²⁰ In holding the lessening of competition to be undue, Mr. Justice Pennell adopted the words of Cartwright J. that "the accused had arrogated to themselves the power to carry on their activities virtually unaffected by the influence of competition."²²¹

5. *R. v. Aluminum Company of Canada Limited*²²²

a. The Preliminary Hearing

The decision in the *Canada Cement Lafarge* case was cited with approval to support the discharge, in May 1975, of four aluminum extruders accused of violating section 32(1)(c) of the *Combines Investigation Act* in the *Alcan* case. Joncas J. noted that the four accused accounted for about eighty-six per cent of aluminum extrusions produced in Canada and that

²¹³ *R. v. Abitibi Power & Paper Company, Limited* (1961), 131 C.C.C. 201; 36 C.P.R. 188.

²¹⁴ *R. v. J. J. Beamish Construction Company Ltd.*, [1968] 1 O.R. 5; 65 D.L.R. (2d) 260; [1968] 2 C.C.C. 5; 53 C.P.R. 43.

²¹⁵ *Supra*, note 171 at 528-30.

²¹⁶ *Id.* at 530.

²¹⁷ *Id.*

²¹⁸ *Id.*

²¹⁹ *Id.* at 531.

²²⁰ *Id.* at 533.

²²¹ *Id.* All of the accused were acquitted on both monopoly counts.

²²² *Supra*, note 63.

the Aluminum Company of Canada Limited (Alcan), the largest producer, was the price leader in the industry. The judge described the situation as follows:

In 1967, the co-accused abided by Alcan's new price list and so informed their clients. Alcan followed its competitors' activities closely and noted that some of them occasionally did not follow the price list. In January, 1967, Alcan had itself increased the cost of its aluminum ingot by .01¼ per pound.

In 1968, Alcan increased its prices again, followed by the co-accused. Alcan continues to follow the market closely. The raw material increased in price again by .01¼ per pound.²²³

Judge Joncas cited a letter written to an Alcan executive, by an executive in a firm which was named as a co-conspirator, and was the parent company of one of the accused corporations which stated:

You will recall that it was you, Alcan, that approached me early in the year re a new list and we went along with you step for step.²²⁴

He asked, "Is it possible to conclude from the evidence that there was collusion to the detriment of the public?" He concluded: "Alcan, the leader, twice increased its prices, and the co-accused, and Daymond [a co-conspirator], followed suit," and then he said: "It appears from the evidence that competition between the accused was very strong before, during and after the increases."²²⁵

In a preliminary hearing, a judge is obliged to commit the accused for trial under section 475 of the *Criminal Code*, "if in his opinion . . . the evidence is sufficient . . ."²²⁶ Joncas J. put the point as follows:

If the evidence made before this Court was presented to a reasonable and properly instructed jury, would it on such evidence render a guilty verdict?²²⁷

He concluded that the evidence was not strong enough to warrant committing the accused for trial and discharged the four accused companies. It is difficult to make sense of his decision because of its disjointedness. Despite the representations by the defendants to the Department of Justice, after the strong urgings of officials in the Bureau of Competition Policy, the Crown proceeded by way of preferred indictment and a trial on the merits was held in the fall of 1976.

b. The Trial Court's Decision²²⁸

In a decision rendered on November 22, 1976, Mr. Justice Rothman acquitted all five defendants of a single count brought under section 32(1)(c)

²²³ *Id.* at 220.

²²⁴ *Id.*

²²⁵ *Id.* at 221.

²²⁶R.S.C. 1970, c. C-34.

²²⁷ *Supra*, note 222 at 221.

²²⁸ *R. v. Aluminium Company of Canada Limited* (1976), 29 C.P.R. (2d) 183.

In the final indictment, five companies were named: Aluminum Co. of Canada, Reynolds Extrusion Company Limited, Indalex Limited, Kaiser Aluminum Chemicals of Canada Limited and Daymond Company Limited. The latter was named as a co-conspirator in the original information resulting in the Preliminary Hearing.

of the *Combines Investigation Act*. He concluded that the Crown had not succeeded in "proving beyond a reasonable doubt that there was an agreement between Alcan and Indalex as alleged . . .".²²⁹ While it was unnecessary to do so, Rothman J. considered the question whether, assuming there was an agreement, it unduly lessened competition. He said:

I have no doubt that any agreement to which [the accused] were all parties and which, if carried into effect, would have substantially lessened competition would have been undue. All of the [five] accused together accounted for over 80% of the total Canadian market while Alcan and Indalex alone accounted for well over 90% of the market in British Columbia. Alcan and Reynolds were the only Canadian sources of extrusion ingot and Alcan alone supplied far more of the aluminum metal [primary aluminum ingot] than all of the other sources of supply combined.²³⁰

The issue of conscious parallelism was of minimal concern in the Trial Court's reasoning, but the judgment is significant in that it indicates the demanding requirements for finding an agreement under the conspiracy section, section 32, even where direct communication on prices has taken place.

The Crown alleged that in June of 1968 the five aluminum extruders conspired to pass on to their customers an increase in the price of billet or aluminum extrusion ingot. On June 3, Alcoa in the United States, followed by Kaiser Aluminum & Chemicals Canada Limited and Reynolds Extrusion Company Limited, announced an increase of 1¢ per pound in the price of aluminum ingot and an increase of four per cent in most fabricated products.²³¹ On June 4, executives of Alcan met to decide what should be done in Canada. A memorandum of that meeting stated:

In all the circumstances, Mr. Culver [an Alcan executive] felt that we should not miss this special opportunity, in a highly competitive market to achieve the increase in the ingot price we have wanted for a long time in order to improve our return on capital.²³²

Alcan proposed to increase the price of extrusion ingot by 1.2 cents per pound effective June 5. The Crown alleged the conspiracy took place on June 5 as a result of a series of telephone calls by Mr. G. K. Clement, manager of the Extrusion Division of Alcan, to a number of extruders.²³³ In Rothman J.'s words, the "cornerstone" of the Crown's case was the following memorandum, Document 15406, dated June 5, 1968, which was sent by Clement to an Alcan vice-president.

I have talked to everybody on basis of 1.2 cents/pound extrusion ingot price increase across the board and carried over into extrusion [shapes] prices. All have agreed to implement accordingly. Bob Weber [Reynolds] in favour of any in-

²²⁹ *Id.* at 209.

²³⁰ *Id.* at 209-10. The phrase "substantially lessened competition" is of some importance in the definition of "unduly." Rothman J. rejected the virtual monopoly doctrine of Cartwright J. in the *Howard Smith* case, *supra*, note 212 at (S.C.R.) 426, and endorsed the position of Batshaw J. in *Abitibi*, *supra*, note 213 at (C.C.C.) 251, saying, "It is sufficient, in my view, if it is established that the agreement would have the effect of lessening competition substantially."

²³¹ *Id.* at 197.

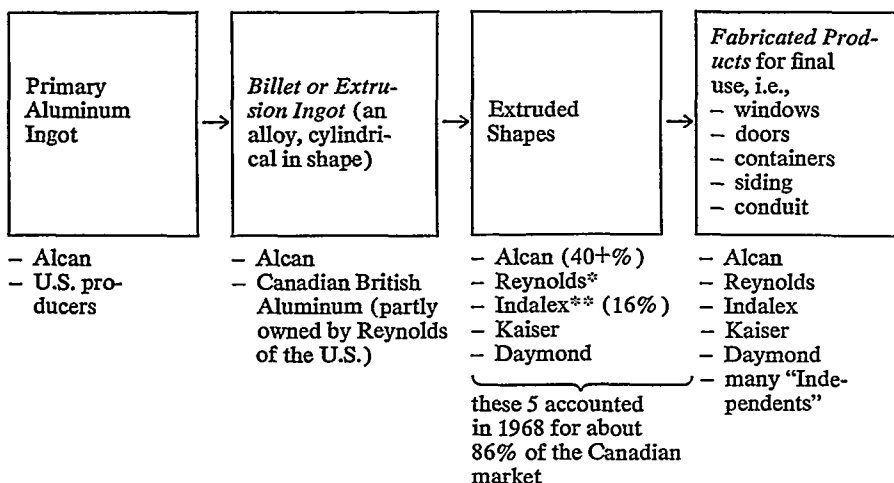
²³² *Id.*

²³³ *Id.*

crease; J. Erickson [Kaiser] agrees that there is little point in trying for additional extrusion [shapes] price increase; W. Stracey [Indalex] feels we are brave to try to increase at this time. John Parsons of Daymond is happy and will go along. Tony Kingsmill [Alcan's western manager] will follow same.²³⁴

A better understanding of the relationship of the various companies and the stages of production may be reached by examining Figure 1.

FIGURE 1
EXTRUDED ALUMINUM MARKET IN CANADA



* owned by Reynolds of the U.S.

** until March 1968, 20% held by Alcan

Alcan operates at all levels in the aluminum product chain, from ingot to fabricated products. The central issue is whether Alcan reached an agreement with its competitors in the production of extruded shapes to increase their prices to reflect the increase of 1.2 cents per pound in extrusion ingot. Note that Alcan's competitors in extruded shapes are its customers for extrusion ingot.

In addition to the memorandum quoted above, the Crown introduced two handwritten notes of Mr. Clement prepared a few days after June 5, 1968. They stated:²³⁵

Check with Reynolds, Kaiser, Daymond, Indalex—three out of four suggest the most you can do is pass on metal cost.

Check with Kaiser, Indalex, Daymond, Reynolds—three out of four agree you cannot up price further now.

These notes, said Rothman J., are "susceptible to a different interpretation as to the subject-matter of these conversations."²³⁶ He concluded,

Neither of these documents suggest an "agreement" to increase extrusion prices

²³⁴ *Id.*

²³⁵ *Id.* at 197-98.

²³⁶ *Id.* at 197.

any more than they suggest an "agreement" in the sense of similarity of opinion that the market could not absorb a price increase beyond the increase in metal cost.²³⁷

In other words, these documents could be interpreted as evidence of an agreement or simply as evidence of an "exchange of views" to use the words of Mr. Clement of Alcan.²³⁸ In terms of the theory of conscious parallelism of action, the Alcan executive was getting information about the likely response of competitors to a change in prices. He was seeking to facilitate the smooth coordination of behaviour by all the leading firms. Clement testified that one purpose of the calls was to obtain evidence for his view that the Canadian market would not support an across-the-board increase of four per cent which had been adopted in the United States.²³⁹

Although the document quoted above indicates that Clement talked to four executives in other companies and one in his own, he testified at the trial that he did not make all of the calls personally, but rather they were made by his staff. At the earlier Restrictive Trade Practices Commission hearings, he testified that he had spoken to the individuals named in Document 15406.²⁴⁰ The indicated recipients of the calls had no recollection of any call from Clement. Rothman J. concluded that "there is at least a reasonable doubt that Clement made these calls himself."²⁴¹ Despite Clement's explanation of the document as reflecting his responsibility for the calls, the Trial Court very narrowly construed the evidence as not being indicative of agreement. Once again, we find oral evidence vastly outweighing documentary evidence. Rothman J. concluded that "very little weight" could be attached to Document 15406 because if Mr. Clement "did not himself speak to some of these people [he testified he did speak personally to Mr. Stracey of Indalex], he would be unable to give direct evidence of any 'agreement' made with them so that it is difficult to conceive how the document can be accepted as proof of such an agreement."²⁴² Rothman J. ruled that section 45 of the *Combines Investigation Act*, which provides in part that a document proved to have been in the possession of a participant is *prima facie* proof that anything recorded in or by the document as having been done, said or agreed upon by any participant, was done by the participant, does not overrule the general prohibition against hearsay evidence.²⁴³

As additional evidence of the existence of a conspiracy, the Crown pointed to the fact that the accused had announced increases in their extrusion prices after June 5, 1968; that the accused tended to use and follow

²³⁷ *Id.* at 198.

²³⁸ *Id.*

²³⁹ *Id.*

²⁴⁰ *Id.* at 199.

²⁴¹ *Id.* at 200.

²⁴² *Id.*

²⁴³ On this point, he followed Pennell J. in *R. v. Canadian General Electric*, *supra*, note 171 at 494.

Alcan's price list; and that all of the accused were on Alcan's mailing list for its price lists. Rothman J. also indicated that "the Crown contends that the evidence of intense competition in the industry," together with the other factors, "tend to support the conclusion that a conspiracy existed and that there was a common design."²⁴⁴ While intense competition might well motivate the companies to seek an agreement, it is difficult to see how it could be evidence of an agreement to increase prices by the same amount. Rothman J. evaluated the evidence on each of these points, including that of Dr. D. E. Armstrong of McGill University who testified for the defendants. The Judge's findings are implicit in his conclusion:

Given the relatively small number of producers, the importance of raw material cost in relation to total cost [about 50%] and the dissimilarity of prices actually charged to customers, I do not consider one can safely presume that the price increases of 1.2¢ per pound announced by Alcan, Reynolds, Daymond and Indalex within a few weeks following June 5, 1968, could have resulted only from agreement on their part. On the evidence, it would not be unreasonable to conclude that the increases announced by the accused resulted not from an agreement but from independent decisions to cover increases in metal cost.²⁴⁵

In view of the communication between Alcan as major supplier of extrusion ingot and its customers/competitors in the extruded shapes market, their decision to pass on the 1.2 cents per pound increase in ingot prices is hardly "independent." We concluded above that independent behaviour by oligopolists can only mean that they make their pricing and other decisions without any attempt to communicate, not that they fail to recognize their mutual dependence. The effect of the exchange of views as to the state of the market was to permit the leading firm in an oligopoly to act on the interdependence inherent in the situation with a high degree of confidence that others would act in a parallel fashion.

In the absence of the exchange of views, Alcan's 1.2 cents per pound increase in extrusion ingot might not have been passed on to the buyers of extruded shapes. In fact, the intensity of competition might have forced the extruders to absorb part or all of the increase in ingot prices.²⁴⁶ The fact that actual transaction prices varied considerably below Alcan's list prices both before and after the 1.2 cents per pound increase of June 5 does *not* mean the "consensus building" exercise between Alcan and its customers/competitors was without real economic effect. The probable effect of the communications among the accused was to shift the average price received by the extruders up by as much as 1.2 cents per pound over what it would have been in the absence of interfirm communication.

²⁴⁴ *Supra*, note 228 at 201.

²⁴⁵ *Id.* at 203.

²⁴⁶ At page 204 of the judgment, Rothman J. states "Kaiser did not issue any announcement increasing its prices, and . . . it seems doubtful that the ingot price increase was in fact carried through into extrusion prices. Although Mr. Erickson [of Kaiser] recalled that Kaiser attempted to increase extrusion prices to reflect the billet increase, he felt that the attempt was not very successful." In terms of the law, it is irrelevant whether or not the conspiracy succeeded in raising prices once an agreement to do so is shown and that such an agreement was "undue."

FIGURE 2.

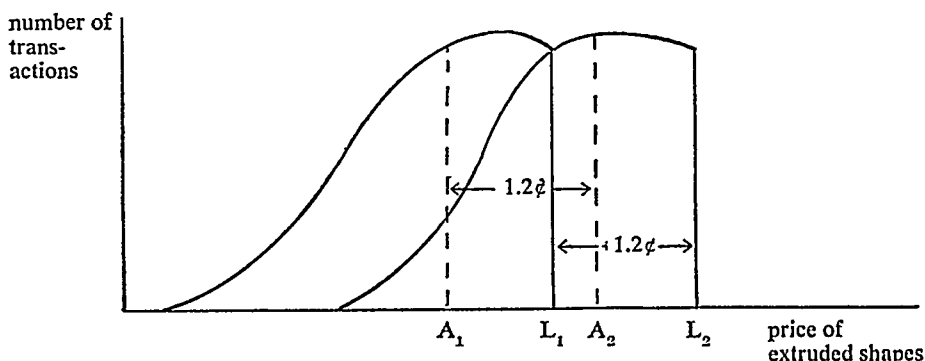


Figure 2 has been drawn on the assumption that all price deviations consisted of price cuts below Alcan's list prices. L_1 represents Alcan's list price for a given type of extrusion prior to the increase of June 5, 1968.²⁴⁷ A_1 represents the average price received by the five major extruders based on Alcan's list price of L_1 . The effect of the communication among the firms was to shift the new Alcan list price to L_2 . Assuming the same variance in actual as opposed to list prices due to competition, we find the average price received by the extruders after the increase (A_2) has shifted up by 1.2 cents per pound.²⁴⁸ This point was not taken by Mr. Justice Rothman, for after noting the Crown's allegation that the accused agreed to pass along a price increase, rather than fix a common price, he said, ". . . in the absence of any evidence of agreement to follow it or that it had some relationship to real prices, it is difficult to see how the use of the Alcan's price list as a guide can have much relevance."²⁴⁹ The point is that Alcan's price list set the plane of prices from which competitive deviations were calculated and the plane may well have been shifted up by 1.2 cents per pound from what it would have been otherwise.²⁵⁰ Mr. Justice Rothman would obviously disagree for

²⁴⁷ An executive of Reynolds "confirmed . . . that the list prices were simply a point of departure or maximum from which salesmen and customers would negotiate real prices according to a variety of factors." *Id.* at 205.

²⁴⁸ It might be argued this would have occurred without interfirm communication. Mr. Clement of Alcan testified that most of the ongoing contracts with extrusion customers had "escalator" clauses providing for an increase in extrusion prices in the event of an ingot price increase and that it was almost automatic that the 1.2¢/lb increase would be passed along. If this is the case why was it necessary to call Alcan's customers to see if they would be sufficiently unhappy to try to develop other sources of supply? He testified he was looking for support among the other extruders to resist the 4% increase (about 1.7¢/lb) proposed by his superiors. *Id.* at 198.

²⁴⁹ *Id.* at 202.

²⁵⁰ Figures for the average selling price received by Kaiser appear to contradict this argument. First, one should note that the average prices are not adjusted for changes in the composition of output over time which is unknown. Second, these are the prices Kaiser received, not the average for the industry. Third, if holding the composition of output constant, the average price received was constant or declined, the exchange of information (opinions) about the state of the market may have prevented an increase or an even greater decline than was observed in the price data. The point is that the exchange of information raised the plane of prices by 1.2 cents over what it would have been in the absence of the establishment of consensus. *Id.* at 205.

he said, "there is no indication whatever that the proposed increase was to have any relationship to real prices."²⁵¹

The evidence of the relationship between Alcan and Indalex was highly complex and comprehensive²⁵² (e.g., Clement of Alcan and Stracey of Indalex confirmed they talked to each other on June 5 and that on other occasions Indalex had exhorted Alcan to maintain prices and avoid price-cutting), yet Rothman J. concluded that "motives and desires and even intentions are insufficient to constitute a conspiracy."²⁵³ He then set out the test which must be met: "there must be evidence [beyond a reasonable doubt] of mutual consent to a common design or purpose and there must be an agreement by both parties to carry the design into effect."²⁵⁴

Near the outset of his judgment Rothman J. noted that in cases of conspiracy to be proved by circumstantial evidence, it "need [not] be proved that the parties actually met or corresponded or that they even knew each other if it can be concluded, beyond reasonable doubt, that their conduct and their actions could only have resulted from the pursuit of a common design."²⁵⁵ In the final analysis, he has imposed what appears to be a tougher standard, buttressed by an exaggerated faith in the testimony of businessmen seeking to closely coordinate the activities of their firms in an oligopoly without appearing to have executed an agreement to do so.²⁵⁶

6. Summary

To date, the decided cases in Canada offer relatively little by way of a guide to the determination of whether the present conspiracy provisions, if intelligently interpreted, are adequate to combat at least some of the undesirable implications of conscious parallelism in an economy whose markets are predominately oligopolistic in character.

In summary, this body of jurisprudence is not adequate to either confirm or deny the utility of the current section 32 in attacking a typical case of conscious parallelism. Some possible implications of the application of the conspiracy provision to conscious parallelism can be obtained by an analysis of the interpretations of section 1 of the *Sherman Act*²⁵⁷ in the United States.

²⁵¹ *Id.*

²⁵² *Id.* at 206-09.

²⁵³ *Id.* at 209.

²⁵⁴ *Id.*

²⁵⁵ *Id.* at 191.

²⁵⁶ The judgment has some other disconcerting characteristics. The Trial Court argued that there are three parts to an offence under section 32: (a) the establishment of an agreement; (b) proof that the agreement would prevent or lessen competition; and (c) that this prevention or lessening of competition was "undue." *Id.* at 191-94. The Court found there was no agreement, but then proceeded to pronounce on the other two parts of the offence. The Court concluded that the behaviour of the accused did not lessen competition but, at the same time, concluded "I have no doubt that any agreement to which [the accused] were all parties and which, if carried into effect, would have substantially lessened competition would have been undue." *Id.* at 209.

²⁵⁷ 15 U.S.C. 1.

D. REVIEW OF THE AMERICAN CASES

The application of the American law on conspiracy to the problem of conscious parallelism will be reviewed as part of the determination of appropriate public policy in this difficult area. It does not seem desirable to erect a new legal framework if one can utilize current and reasonably anticipated interpretations of the existing rules to ameliorate the problem at hand. Not only have more cases been decided, but also a far wider range of facets of the conscious parallelism problem have been considered by the American courts. Section 1 of the *Sherman Act* and section 32 of the *Combines Investigation Act* both prohibit combinations, conspiracies, or agreements in restraint of trade. Under both statutes the crime lies in the conspiracy or agreement. While section 1 is interpreted as prohibiting price fixing and market sharing agreements *per se*,²⁵⁸ section 32 requires that such agreements lessen competition unduly before they are illegal. Since the "agreement" aspect of the offence is the one most relevant to conscious parallelism, the differences between sections 1 and 32 do not detract from the value of American cases as an aid in developing public policy in Canada.

1. *What Constitutes An Agreement?*

The use of either the *Sherman Act* or the *Combines Investigation Act* to strike at conscious parallelism requires that the court find an agreement existing between two or more firms. This agreement may be overt or tacit; it may be found by way of documentary or oral evidence or it may be inferred on the basis of circumstantial evidence. If an agreement can be established by documentary evidence, the case becomes a more routine conspiracy charge. This was the situation in the *Large Lamps* case. The central issue is to determine what type and how much circumstantial evidence is required before a judge can properly infer an agreement. Proof of conspiracy outside the field of antitrust entirely by the use of circumstantial evidence is, of course, not new, "but the matter of what kinds of indirect evidence will be judicially recognized as probative of conspiracy is important." James A. Rahl continues:

Inferences drawn from documents, gestures, paradoxical behavior and other indicia of a state of mind are one thing. Inferences drawn from purely external market data and analysis demonstrating non-competitive uniformity of action, but not necessarily any particular subjective facts, are something else.²⁵⁹

Because the law on conspiracy is interpreted in terms of "a meeting of minds," "concerted action," "unity of purpose," "common design" or "collusion," it is essential to discover their analogy in cases of conscious parallelism. A. D. Neale points out:

The underlying issue is what, at the minimum, constitutes that 'meeting of the minds' which must be directly or circumstantially established; what degree of mutual knowledge and confidence among businessmen amounts to a common

²⁵⁸ See *Addyston Pipe and Steel Company v. U.S.*, 175 U.S. 211 (1899); *U.S. v. Trenton Potteries*, 273 U.S. 392 (1927); *Appalachian Coals, Inc. v. U.S.*, 288 U.S. 344 (1933); *U.S. v. Socony-Vacuum Oil Co. Inc.*, 310 U.S. 150 (1940).

²⁵⁹ J. A. Rahl, *Conspiracy and the Antitrust Laws* (1950), 44 Ill. L. Rev. 743 at 757-58.

understanding and hence, if there is a restrictive effect on competition, to an illegal conspiracy [within the meaning of the statute]²⁶⁰

The definition of this minimum is crucial in determining whether the old legislation has sufficient range to deal successfully with the new disease. A discussion of a number of conscious parallelism cases in the United States and the standards implied by the judicial rulings although not exhaustive,²⁶¹ is indicative of the range of jurisprudence on the issue under section 1 of the *Sherman Act*.

a. *Interstate Circuit*²⁶² (1939)

This case, one of the earliest and most ambitious cases to use the conspiracy provisions of the *Sherman Act* in attacking cases of conscious parallelism, reached the U.S. Supreme Court in 1939. It involved two groups of defendants: eight distributors of motion pictures which accounted for seventy-five per cent of the first class movies in the industry, and two large affiliated cinema circuits operating in Texas and New Mexico. *Interstate Circuit Inc.* had an almost complete monopoly of first-run theatres in six Texas cities. The manager of both circuits sent to each of the eight distributors an identical letter naming all of the distributors as addressees and making two demands: first, that the distributors maintain a minimum admission price of twenty-five

²⁶⁰ A. D. Neale, *The Antitrust Laws of the U.S.A.* (2d ed. Cambridge: Cambridge University Press, 1970) at 81.

²⁶¹ This survey does not examine the cases brought by the Federal Trade Commission under section 5 of the *F.T.C. Act* which simply states: "Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are declared unlawful." (15 U.S.C. 45 (1958)). We do so because in *F.T.C. v. Beech-Nut Packing Co.*, 257 U.S. 411 (1922) the F.T.C. ruled that a violation of section 5 could occur even though the restraint of trade falls short of conspiracy. More recently, the Supreme Court in *F.T.C. v. Sperry and Hutchinson Co.*, 405 U.S. 233 (1972), held that the F.T.C. is empowered under section 5 of the *F.T.C. Act* without regard to whether such practices violate the *Sherman* or *Clayton Acts*.

In the *Cement Institute* case (333 U.S. 683 (1948) at 708), the Supreme Court held that

[I]ndividual conduct, or concerted conduct which falls short of being a Sherman Act violation may as a matter of law constitute an "unfair method of competition" prohibited by the Trade Commission Act. A major purpose of that Act, as we have frequently said, was to enable the Commission to restrain practices as "unfair" which, although not yet having grown into Sherman Act dimensions, would most likely do so if left unrestrained.

In other words, it is possible for cases of conscious parallelism to violate section 5 of the *F.T.C. Act*, but not section 1 of the *Sherman Act*. The important cases under section 5 are: *F.T.C. v. Salt Producers Association*, 34 F.T.C. 38 (1941), 134 F. 2d 354 (1943); *F.T.C. v. Cement Institute*, 333 U.S. 683 (1948); *F.T.C. v. Triangle Conduit and Cable Co.*, 38 F.T.C. 534 (1944), 168 F. 2d 175 (1948) affirmed *per curiam subnom Clayton Mark & Co. v. F.T.C.*, 336 U.S. 956 (1949)—known as the *Rigid Steel Conduit* case. These cases are reviewed in Sumner S. Kittrelle and George P. Lamb, *The Implied Conspiracy Doctrine and Delivered Pricing* (1950), 15 Law and Contemporary Problems 227. This survey also does not examine the early "information dissemination" cases in which some writers find elements of conscious parallelism. A useful review of these cases is contained in L. A. Sullivan, *Handbook of the Law of Antitrust* (St. Paul: West Publishing, 1977) at 265-73. See also, G.B. Richardson, *Price Notification Schemes* (1967), 19 Oxford Economic Papers 359.

²⁶² *Interstate Circuit Inc. v. U.S.*, 306 U.S. 208 (1939).

cents on subsequent runs of pictures first shown in theatres of the two circuits; second, that these pictures not be shown as part of a double feature in subsequent showings. These demands were backed up by the threat that Interstate would refuse to place the distributor's films in their first-run theatres. After the letters there followed conferences between Interstate and the distributors as a result of which Interstate's demands were met.

Even though there was no evidence of any oral or written communication or agreement between the distributors, the Trial Court inferred the existence of a price fixing conspiracy and convicted the distributors. The Supreme Court affirmed the decision saying that the Trial Court properly inferred the existence of an agreement from

. . . the nature of the proposals made on behalf of Interstate and Consolidated; from the manner in which they were made; from the substantial unanimity of action taken upon them by the distributors; and from the fact that appellants did not call as witnesses any of the superior officials who negotiated the contracts with Interstate or any official who, in the normal course of business, would have had knowledge of the existence or non-existence of such an agreement among the distributors.²⁶³

The letter from Interstate named all the distributors as addressees. Each knew that the others had received the same demands. The Supreme Court, therefore, concluded that "without substantially unanimous action with respect to the restrictions for any given territory there was risk of a substantial loss of business and good will of the subsequent-run and independent exhibitors, but that with it there was the prospect of increased profits."²⁶⁴

The conspiracy was inferred from the course of conduct of the defendants. The Supreme Court, *per* Mr. Justice Stone, said:

It taxes credulity to believe that the several distributors would . . . have accepted and put into operation with substantial unanimity such far-reaching changes in their business methods without some understanding that all were to join, and we reject as beyond the range of probability that it was the result of mere chance. . . .²⁶⁵

The Court also ruled that the District Court's finding of an agreement need not be shown.

It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that co-operation was essential to successful operation of the plan It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators. Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act.²⁶⁶

To some observers, this decision constituted the high water mark in cases

²⁶³ *Id.* at 221.

²⁶⁴ *Id.* at 222.

²⁶⁵ *Id.* at 223.

²⁶⁶ *Id.* at 226-27.

dealing with conscious parallelism.²⁶⁷ Peter Asch writes that, in *Interstate Circuit*, "it appeared that proof of conspiracy was divorced from questions of overt or formal agreement; the issue had become one of judging the market behaviour of competing firms."²⁶⁸ A violation could occur, "if such behaviour seemed consistent only with a mutual understanding of some kind."²⁶⁹

According to Rahl, the decision demonstrated that "[t]he conspiracy may creep into existence from the merging of unilateral actions upon a common course if at some time stage, not necessarily simultaneously, the defendants take on the feeling of common cause."²⁷⁰ Neale, on the other hand, argues that Mr. Justice Stone's words, "clearly show that in his view the Court was doing no more than infer [sic] collusion from circumstantial evidence."²⁷¹ Particularly damning to the accused was the fact that they failed to present witnesses to explain their uniformity of behavior and to argue that no agreement had been made. As Asch points out, "the court could not reconcile the actions of the eight distributors with an assumption of independence."²⁷²

b. *Masonite*²⁷³ (1942)

The Masonite Corporation began production of its patented hardboard building product in 1926. In 1933 and 1934 Masonite invited each of its competitors to become *del credere* agents for its products. Each agency agreement, which contained a price fixing clause, was made independently. However, as in the *Interstate Circuit* case, each firm knew of the terms of the agreements made with its rivals.

The District Court dismissed the government's complaint on the ground that the *del credere* agency agreements were true agency contracts.²⁷⁴ Therefore, the price fixing through consignment selling arrangements was not in restraint of trade.

The Court of Appeal, citing Mr. Justice Stone in *Interstate Circuit*, reversed the Trial Court and convicted Masonite and the other nine companies. It ruled that through the series of agency agreements, "it is clear that, as the arrangement continued, each [competitor] became familiar with its purpose and scope."²⁷⁵ The Appeal Court found that through its agency agreements, Masonite had the power to fix prices and that such power "is a powerful inducement to abandon competition . . ." It concluded that "the

²⁶⁷ See Michael Conant, *Consciously Parallel Action in Restraint of Trade* (1954), 38 Minn. L. Rev. 797 at 801; B. F. Turner, *supra*, note 12 at 212. L. A. Sullivan, *supra*, note 261 at 315, calls it "the leading case on conscious parallelism."

²⁶⁸ Peter Asch, *Economic Theory and the Antitrust Dilemma* (New York: John Wiley, 1970) at 269.

²⁶⁹ *Id.*

²⁷⁰ Rahl, *supra*, note 259 at 759.

²⁷¹ Neale, *supra*, note 260 at 94.

²⁷² Asch, *supra*, note 268 at 269.

²⁷³ *U.S. v. Masonite Corp.*, 316 U.S. 265 (1942).

²⁷⁴ 20 F. Supp. 868 (N. D. Texas, 1937).

²⁷⁵ 306 U.S. 208 at 227 (1939).

power of this type of combination to inflict the kind of public injury which the *Sherman Act* condemns renders it illegal per se."²⁷⁶

In discussing the *Interstate* and *Masonite* cases, J. P. Dunn argues that both involved a "link," i.e., "the parties to the parallel behaviour were related through their common ties."²⁷⁷ He continues: "the 'link' was an established conspiracy and the court held that by joining in the scheme and adhering to its principles by parallel behaviour the joiners became conspirators."²⁷⁸ He notes that in the *Interstate* case, the link was not a pre-existing conspiracy, but rather a common exhibitor. Michael Conant says the two cases "initiated the trend away from stress upon the agreement aspect of Section 1 of the *Sherman Act* . . . to group adherence to an unreasonable restraint of trade, the illegal objective of Section 1."²⁷⁹

c. *Goldman v. Loew's*²⁸⁰ (1944)

The Trial Court held that refusals by distributors of first-run motion pictures to deal with a theatre not controlled by a Warner Brothers subsidiary, with whom all the defendant distributors had exclusive working arrangements, did not violate section 2 of the *Sherman Act*.²⁸¹ The Court ruled that the behavior did not unreasonably restrain trade and that a concert of action had not been established.

Following the *Interstate* decision, the Court of Appeal found evidence of concerted action and observed that the defendants jointly controlled more than eighty per cent of feature pictures in the United States. It ruled that

Uniform participation by competitors in a particular system of doing business where each is aware of the other's activities, the effect of which is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the statutes before us.²⁸²

The decision does not appear to support the conclusion that parallel action, *per se*, amounts to conspiracy. The Appeal Court stated earlier in its decision that, "We think there must have been some form of informal understanding. . . . Here, the conclusion is justified that defendants acted in concert in excluding the plaintiff."²⁸³ This finding was reinforced by the defendants failure to testify that there was no agreement among themselves.

d. *American Tobacco*²⁸⁴ (1946)

The three largest tobacco producers in the United States were charged with conspiracy in restraint of trade, monopolization, attempts to monopolize

²⁷⁶ *Id.* at 282.

²⁷⁷ Dunn, *supra*, note 11 at 231.

²⁷⁸ *Id.*

²⁷⁹ Conant, *supra*, note 267 at 802.

²⁸⁰ *William Goldman Theatres, Inc. v. Loew's Inc.*, 150 F. 2d 738 (3rd Cir., 1945).

²⁸¹ 54 F. Supp. 1011 (E.D. Pa., 1944).

²⁸² 150 F. 2d 738 at 745 (3rd Cir., 1945).

²⁸³ *Id.* at 743.

²⁸⁴ *American Tobacco Co. v. U.S.*, 328 U.S. 781 (1946). Conflicting views of this case can be found in Turner, *supra*, note 12 and Posner, *supra*, note 29.

and conspiracy to monopolize under sections 1 and 2 of the *Sherman Act*. The market share of the "big three" declined from ninety-one per cent of cigarette sales in 1930 to sixty-eight per cent in 1939 in the face of competition from cheaper brands. As in other conscious parallelism cases, there was no evidence of an express agreement; the existence of a conspiracy was inferred from wholly circumstantial evidence.

The case revealed a wide variety of behavior by the defendants which was impossible to describe as independent and from which the conspiracy to monopolize was inferred: (i) they entered the market for low grade tobacco and bid up the price to raise the costs of firms producing the cheaper "10¢ brands." It was not known what the "big three" did with this type of tobacco which was not used in the manufacture of their own brands; (ii) each of the accused refused to bid at raw leaf auctions unless the others were present. Each set strict limits on the maximum price it would pay and it was believed that these prices were the same for all three. The total effort in purchasing tobacco was to ensure that all paid the same price; (iii) from 1923 to 1928 the prices charged by each of the "big three" to its wholesalers were substantially identical, from 1928 to 1940 they were absolutely identical. In the latter period only seven price changes were made. In all cases they were first announced by Reynolds; (iv) in 1931, when tobacco prices had dropped to their lowest point in over two decades, Reynolds raised the price of its "Camel" brand from \$6.40 to \$6.85 per thousand cigarettes. The same day the other two big companies raised the price of their major brand to the new price. The market share of the "10¢ brands" increased from .3 per cent in June 1931 to 22.8 per cent in November 1932. The "big three" reduced their prices to \$5.50 per thousand and two firms lost money on their leading brands. By May 1933, the share of the "10¢ brands" was only 6.4 per cent of the market. The "big three" raised their price to \$6.10 in January 1934; and (v) the "big three" used a variety of threats and inducements to have retailers maintain a differential of not more than three cents per package over the "10¢ brands."

The central issue decided by the U.S. Supreme Court was whether actual exclusion of competitors was required to show monopolization under section 2 of the *Sherman Act*. The Court, *per* Mr. Justice Burton, said it was not. It was required only that the,

parties . . . combine or conspire to acquire or maintain the power to exclude competitors from any part of the trade or commerce among the several states or with foreign nations, provided they also have such a power that they are able, as a group, to exclude actual or potential competition from the field and provided that they have the intent and purpose to exercise that power.²⁸⁵

The decision was hailed as providing a precedent with which to attack classical oligopoly behavior. This was certainly the view of Professor W. H. Nicholls.²⁸⁶ More recently, Sullivan reminds us that "the evidence of concert-

²⁸⁵ 328 U.S. 781 at 809 (1946).

²⁸⁶ William H. Nicholls, *The Tobacco Case of 1946* (1949), 39 *American Economic Review* 284.

edness entailed far more than non-collusive, interdependent conduct . . ."²⁸⁷
As Mr. Justice Burton himself stated:

No formal agreement is necessary to constitute an unlawful conspiracy. Often crimes are a matter of inference deduced from the acts of the person accused and done in pursuance of a criminal purpose. Where the conspiracy is proved, as here, from the evidence of the action taken in concert by the parties to it, it is all the more convincing proof of an intent to exercise the power of exclusion acquired through that conspiracy. The essential combination or conspiracy in violation of the Sherman Act may be found in a course of dealing or other circumstances as well as in an exchange of words.²⁸⁸

A close reading of these words, together with the entire decision, suggests that while some new language is employed, e.g., "course of dealing," the Supreme Court is still grounding its decisions firmly in the law of conspiracy. It may be argued that the inferential leap, based entirely on circumstantial evidence, is greater than in other cases, but the decision evolves quite naturally from the law of conspiracy.

e. *U.S. v. Paramount*²⁸⁹ (1948)

The defendants, eight motion picture producers and distributors, were charged with monopolization and with conspiracy to restrain and monopolize trade in the distribution and exhibition of motion pictures. The defendants had engaged in a number of parallel business practices, but the conspiracy aspects of the case focussed on their price-fixing behaviour and on their imposition of unreasonable clearances between first and subsequent runs in their copyright licencing contracts.

The District Court rejected the monopoly charge but made the following observations with respect to the conspiracy to restrain trade:

[the defendants'] licenses are in effect price-fixing arrangements among all the distributor-defendants, as well as between such defendants individually and their various exhibitors . . . [Thus] there was a general arrangement of fixing prices in which both distributors and exhibitors were involved.²⁹⁰

. . . the [motion picture distributors] acted in concert in the formation of a uniform system of clearances for the theatres to which they license their films and that the exhibitor-defendants have assisted in creating and have acquiesced in this system . . . in violation of the Sherman Act.²⁹¹

The Court ruled that tacit participation in a general scheme to control prices

²⁸⁷ Sullivan, *supra*, note 261 at 361.

²⁸⁸ *Supra*, note 285 at 809-10.

The Court of Appeal reviewed carefully the evidence as to the finding of a conspiracy and concluded that the jury's inference was justified. The Appeal Court ruled:

The agreement may be shown by a concert of action, all parties working together understandingly, with a single design for the accomplishment of a common purpose It is the common design which is the essence of the conspiracy or combination; and this may be made to appear when the parties steadily pursue the same object, whether acting separately or together, by common or different means, but always leading to the same unlawful result.

(147 F. 2d 93 at 107 (6th Cir. 1944))

²⁸⁹ *U.S. v. Paramount Pictures Inc.*, 334 U.S. 131 (1948).

²⁹⁰ 66 F. Supp. 323 at 334-35 (1946).

²⁹¹ *Id.* at 343.

is as violative of the *Sherman Act* as an explicit agreement. Hence, the separate contracts between the distributors and exhibitors, individually executed, did not prevent a finding of illegality. Mr. Justice Douglas endorsed the lower court's finding of conspiracy "inferred from the pattern of price-fixing disclosed in the record." He continued:

It is not necessary to find an express agreement in order to find a conspiracy. It is enough that a concert of action is contemplated and that the defendants conformed to the arrangement.²⁹²

With respect to the uniform system of clearances, Mr. Justice Douglas did not indicate that the evidence involved a "meeting of minds." He concluded:

The evidence is ample to support the finding . . . that the defendants either participated in evolving this uniform system of clearances or acquiesced in it and so furthered its existence. That evidence . . . is therefore adequate to support the finding of a conspiracy to restrain trade. . . .²⁹³

With respect to the first passage, presumably Justice Douglas meant that it is not necessary to find evidence of a direct agreement to sustain a conviction for conspiracy. With respect to the second passage, as Neale has pointed out, " 'to participate in evolving' a system or to 'acquiesce' in a system and so 'further its existence' are tests that seem to fall well short of a 'meeting of the minds.' "²⁹⁴ Therefore, the *Paramount* decision moves further from the requirement that a conspiracy be inferred from the parallel behavior of the defendants than any of the earlier cases.

f. *Ball v. Paramount*²⁹⁵ (1948)

Like *Goldman v. Loew's*, this case involved uniform refusals to deal by the distributors of first run films. The Appeal Court also reversed the trial court's decision²⁹⁶ and held that there did exist an inference of conspiracy among the distributors. In doing so, the Appeal Court relied on the decisions in *Goldman v. Loew's*, *Interstate Circuit* and *Paramount*. J.P. Dunn argues that this case is "a stronger authority for the *per se* rule than is *Goldman*."²⁹⁷ But he also notes that the Appeal Court ruled that ". . . conspiracy may be inferred when concert of action could not possibly be sheer coincidence."²⁹⁸ In other words, it appears that the decision rests more on the inference of an agreement than it does on the idea that conscious parallelism *per se* is illegal under section 1 of the *Sherman Act*.

g. *Pevely Dairy*²⁹⁹ (1949)

This case provides authority for the proposition that conscious paral-

²⁹² 334 U.S. 131 at 142 (1948).

²⁹³ *Id.* at 146-47.

²⁹⁴ Neale, *supra*, note 260 at 167, n. 3.

²⁹⁵ *Ball v. Paramount Pictures Inc.*, 169 F. 2d 317 (3d Cir., 1948).

²⁹⁶ 67 F. Supp. 1 (W.D. Pa., 1946).

²⁹⁷ Dunn, *supra*, note 11 at 235.

²⁹⁸ *Id.* at 236.

²⁹⁹ *Pevely Dairy Co. v. U.S.*, 178 F. 2d 363 (8th Cir., 1949), *cert. denied*, 339 U.S. 942 (1950).

lelism alone is not equivalent to an agreement and that evidence of parallel behavior may be explained on the basis of common economic factors which would predispose the defendants to parallel action.³⁰⁰ Pevely and its co-defendant milk distributor accounted for about sixty-three per cent of the market in the St. Louis area. They charged the same price and changed prices by the same amount at the same time.

No evidence of a written or oral agreement was introduced. The defendants were convicted at trial, but this was reversed by the Court of Appeal. It was adduced that the quality of the product was specified by a St. Louis ordinance and that the cost of the milk to the dairies was fixed by government regulation. Both dairies were organized by the same union and subject to the same wage rates. Each price change was associated with changes in costs. Jardner J. stated:

The milk as handled by appellants was a standardized product. Its cost items being substantially identical for both appellants, uniformity in price would result from economic forces.³⁰¹

He went on to say that

. . . every price change was made, not as the result of any understanding or agreement, but because of economic factors, and the same economic factors prompting a change by one of the appellants were equally applicable to the other.³⁰²

In conclusion, he ruled that uniformity of prices of a standardized commodity is itself not evidence of a violation of section 1 of the *Sherman Act*.

h. *Milgram v. Loew's*³⁰³ (1951)

Milgram, the owner of a new drive-in theatre in Allentown, Pennsylvania, alleged that eight motion picture distributors conspired in refusing to supply him with first-run films even though he offered to pay more than the prevailing price for such films. The distributors argued that they had reached their decisions independently and that their classification of theatres was based on independent business judgment taking into account the limited drawing power of a drive-in, the susceptibility of the business to seasonal and weather changes, and the reduction in prestige and income if first-runs were shown in drive-ins. They held to their refusal to deal despite the fact that Milgram's theatre was an excellent facility within the city limits and despite the fact that none of the downtown theatres were owned by the distributors.

The Trial Court found the distributors guilty of a violation of section 1 of the *Sherman Act*. The trial judge asserted that, "It is incredible that each [distributor] proceeded in ignorance of how the others were dealing with it . . . it is simply not possible that branch managers did not keep track of

³⁰⁰ Asch, *supra*, note 268 at 275.

³⁰¹ 178 F. 2d 363 at 368.

³⁰² *Id.* at 369.

³⁰³ *Milgram v. Loew's Inc.*, 192 F. 2d 579 (3d Cir., 1951), *cert. denied*, 343 U.S. 929 (1952).

what their competitors were doing."³⁰⁴ The Trial Court apparently adopted the *per se* approach to parallel behaviour:

It may be taken as settled that proof of concert of action is of itself sufficient evidence from which an 'agreement', as that term is used in the Act, may be found. In practical effect, consciously parallel business practices have taken the place of the concept of meeting of the minds which some of the earlier cases emphasized. Present concert of action, further proof of actual agreement among the defendants is unnecessary, and it then becomes the duty of the Court to evaluate all the evidence in the setting of the case at hand and to determine whether a finding of a conspiracy to violate the Act is warranted.³⁰⁵

Alternatively, agreement is traditionally necessary to establish a conspiracy; conscious parallelism shows an agreement; conscious parallelism to restrain trade may amount to conspiracy under the *Sherman Act*.³⁰⁶

The Third Circuit Court of Appeal upheld the decision in language very similar to that used in the *Interstate Circuit* case:

Uniform participation by competitors in a particular system of doing business, where each is aware of the other's activities, the effect of which is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy. . . .³⁰⁷

At the same time the Appeal Court noted:

This does not mean, however, that in every case mere consciously parallel business practices are sufficient evidence, in themselves, from which a court may infer concerted action.³⁰⁸

In this case, the Appeal Court gives with one hand and, if it does not take away with the other, it surely limits the application of its *dicta* with respect to conscious parallelism *per se* being a violation of the *Sherman Act*. Dunn argues that "the case ultimately holds not that a *per se* rule is the law, but only that conscious parallelism may serve as the basis for an inference of agreement."³⁰⁹

Hastie J.'s dissent provides a useful analysis of the relationship between conscious parallelism and a finding of conspiracy. He asserted that the District Court erred in its conclusion that a conspiracy existed. For example, he said, "I think it is clear that the court repeatedly used the phrase 'concert of action' to mean no more than 'consciously parallel business practices'" Hastie J. continues:

[T]he court seems to have reasoned that it is permissible to proceed to a legal conclusion of conspiracy in restraint of trade from an ultimate factual finding of "consciously parallel action" without any finding of a "meeting of the minds" . . . in the sense of agreement upon a common course of action reached by collabora-

³⁰⁴ 94 F. Supp. 416 at 418 (E.D. Pa., 1950).

³⁰⁵ *Id.* at 419.

³⁰⁶ *Supra*, note 11 at 237.

³⁰⁷ *Supra*, note 280 at 745, as quoted in *Milgram*, *supra*, note 303 at 584.

³⁰⁸ *Milgram*, *id.* at 583.

³⁰⁹ *Supra*, note 11 at 238. Neale, *supra*, note 260 at 85, argues that this case "goes furthest in purporting to develop the law of conspiracy." He notes that the Court of Appeal "did, however, feel it necessary to hedge somewhat on the [trial] judge's statement that conscious parallelism had 'taken the place' of meeting of the minds as the criterion of conspiracy." (at 86).

tion, however effected. This reasoning was decisive here because on the evidence the court was unable to conclude that there had been even the most informal collaboration among the defendant distributors.³¹⁰

The dissenting justice argued that section 1 of the *Sherman Act* required a "finding of actual, if informal agreement" for the words "conspiracy" and "combination" in the section "connote collaboration and agreement both in understanding and as normally applied in anti-trust cases."

i. *C-O-Two Fire Equipment*³¹¹ (1952)

Four manufacturing corporations of portable carbon dioxide fire extinguishers and three individuals were charged with violating section 1 of the *Sherman Act* between the beginning of 1947 and mid-1949 in the Southern California area. The defendant companies charged identical prices to all purchasers for identical size and design of extinguishers by using a delivered price system. At various times the accused published and distributed price lists. In addition, they submitted identical bids to public agencies and had uniform licensing agreements to fix price, terms, and conditions of sales with their distributors. Their sales accounted for more than ninety per cent of the market. Each defendant pleaded guilty except C-O-Two Fire Equipment and one of its executives. Both were convicted at trial.

Upon appeal, the defendants challenged the point that the evidence presented by the government did not prove beyond a reasonable doubt that they conspired to fix prices. They argued that the product was "naturally standardized" and therefore resulted in price uniformity. The court disagreed. It held that the product was artificially standardized, to the point where the only difference was the label, by adhering to the requirements set up by Underwriters Laboratories. The Court also noted the detailed parallelism in the companies business practices and their history of coordination. The Appeal Court found the set of facts not only consistent with the existence of an agreement, but also inconsistent with any other reasonable hypothesis.

In this case, the term "plus factors" was introduced. The Court stated that it

regarded this evidence [of artificial standardization] as being another one in a series of "plus factors" which, when standing alone and examined separately, could not be said to point directly to the conclusion that the charges of the indictment were true beyond a reasonable doubt, but which, when viewed as a whole, in their proper setting, spelled out that irresistible conclusion.³¹²

Other "plus factors" mentioned by the Court were association meetings, price increases in periods of excess supply, the publication and distribution of price lists at various times and the use of a uniform delivered price system.³¹³

³¹⁰ *Supra*, note 303 at 590-91.

³¹¹ *C-O-Two Fire Equipment Co. v. U.S.*, 197 F. 2d 489 (9th Cir., 1952), *cert. denied*, 344 U.S. 892 (1952).

³¹² *Id.* at 493.

³¹³ This case is contrasted to *Pevely Dairy* by Sullivan, *supra*, note 261 at 318.

j. *Theatre Enterprises*³¹⁴ (1954)

Although in a number of decisions, beginning with the Supreme Court's ruling in *Interstate Circuit* in 1939, the courts had begun to convict on little more than evidence of conscious parallelism, Mr. Justice Clark's decision in this case retreated to a stricter, more traditional interpretation of the law on conspiracy. He ruled that:

The crucial question is whether [the defendants'] conduct . . . stemmed from independent decision or from an agreement, tacit or express. To be sure, business behavior is admissible circumstantial evidence from which the fact finder may infer agreement But this Court has never held that proof of parallel business behavior conclusively establishes agreement or, phrased differently, that such behavior itself constitutes a Sherman Act offense. Circumstantial evidence of consciously parallel behavior may have made heavy inroads into the traditional judicial attitude toward conspiracy; but "conscious parallelism" has not yet read conspiracy out of the Sherman Act entirely.³¹⁵

The case resulted from a private treble-damage action by the owner of a suburban Baltimore theatre against the eight largest film distributors in the United States. The distributors, approached individually by the owner, who had a new, high quality theatre, had refused to provide first-run films. The distributors owned three of the eight theatres in downtown Baltimore to which they supplied first-run films.

All the defendants asserted the same reasons for denying the plaintiff's offers: the plaintiff's theatre would provide additional competition for the downtown theatres; the suburban location of the theatre had less than one-tenth of the drawing area of a downtown theatre; and that the downtown theatres permitted the full exploitation of first-run movies and gave opportunities for widespread advertisement which maximized overall returns.

The jury at the trial found for the distributors. The Fourth Circuit Court of Appeal affirmed this decision.³¹⁶ The Supreme Court upheld the Appeal Court's decision holding that the crucial question was ". . . whether [the distributors'] conduct toward [the theatre owner] stemmed from an independent decision or from an agreement, tacit or express."³¹⁷ Since there was no evidence of a direct agreement and the distributors provided evidence of independent action which refuted the inference of conspiracy, the Supreme Court ruled in favor of the distributors. The decision was consistent with the dissenting judgment of Hastie J. in *Milgram v. Loew's* a few years earlier.

Neale summarizes the significance of the Supreme Court's decision as follows: ". . . it is clear that the attempt to extend the meaning of 'conspiracy' to cover parallel courses of action—an attempt intended to enable antitrust to be brought to bear more easily on oligopoly situations—has failed."³¹⁸

³¹⁴ *Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.*, 346 U.S. 537 (1954).

³¹⁵ *Id.* at 540-41.

³¹⁶ 201 F. 2d 306 (1953).

³¹⁷ *Supra*, note 314 at 540.

³¹⁸ Neale, *supra*, note 260 at 87.

In contrasting Mr. Justice Stone's ruling in *Interstate Circuit* with that of the Court of Appeals in *Milgram v. Loew's* and with Mr. Justice Clark's decision in this case, Neale argues, "the root of the trouble is ambiguity in the use of apparently simple terms like 'know' and 'mutual awareness'. . . . Whenever there is a plan, there is mutual awareness among the participants; but it does not follow that whenever there is mutual awareness, there is a plan."³¹⁹ It is Neale's contention that "a plan implies some assurance of reliable action in the future . . ."³²⁰ and that its breakdown will result in reproach. However, conscious parallelism is without this "quasi-moral element."³²¹

Dunn's view of *Theatre Enterprises* is that the Supreme Court "is saying consciously parallel action is, at most, only evidence which, in conjunction with other evidence, (such as complexity of pricing formulae, number of firms, past history, etc.) may support an inference of agreement. Thus, the element of agreement must still be dealt with and some species of that creature found."³²² Nye points out that while the decision holds that conscious parallelism, *per se*, will not compel an inference of conspiracy, the trial court is still permitted to draw that inference from such evidence.³²³

k. *Orbo Theatre*³²⁴ (1957)

This case was a private treble-damage action by a Rockville, Maryland theatre owner against a number of film distributors. He alleged that in refusing to grant him fourteen day clearances and offering him only the regular practice in the Washington, D.C./Maryland area of twenty-one day clearances, the distributors violated section 3 of the *Sherman Act*. This section is identical to section 1 except that it applies to the District of Columbia.

The identical request for films on a fourteen day clearance basis was made to each of the distributors, but none of the letters indicated that the same demand was being made to any other distributor. The trial judge pointed out that to have yielded to the demand would have resulted in discrimination against a successful drive-in theatre nearby which operated nine months of the year. Each distributor refused the demand, but instead offered a system of competitive bidding between the plaintiff's theatre and the drive-in on the basis of a twenty-one day clearance.

At trial, the branch managers of the defendant distributors, other executives and house counsel who participated in the decision gave evidence and were subjected to cross examination. The trial judge concluded from the evidence: "There was no evidence, direct or circumstantial, oral or documentary, from which an inference of even remote cooperation among the defendants in this matter could be derived."³²⁵

³¹⁹ *Id.* at 88.

³²⁰ *Id.*

³²¹ *Id.*

³²² Dunn, *supra*, note 11 at 228.

³²³ Stephen A. Nye, *Can Conduct Oriented Enforcement Inhibit Conscious Parallelism?* (1975), 44 *Antitrust L.J.* 206 at 207. See also, Asch, *supra*, note 268 at 277.

³²⁴ *Orbo Theatre Corp. v. Loew's Inc.*, 1957 Trade Cases, Par. π 68,869, 73516.

³²⁵ *Id.* at 73520.

Citing *Theatre Enterprises* and five other cases for support, the trial judge ruled as follows:

The fact that parallel action was taken by alleged conspirators may under certain circumstances justify the Court in drawing the conclusion that the parallel action was concerted action. Such an inference is permissible, but is not compelled. Whether to reach it in any particular case depends on the remainder of the evidence and the surrounding circumstances. Parallel action may indeed be concerted action, but may also be due to the fact that the persons concerned arrived at the same simple solution of a common business problem. Here the problem was a comparatively simple one, and the solution reached was more or less obvious. If the various officers and employees involved in the decision refrained from testifying on this point, the court might well draw an adverse inference. On the other hand, considering the fact that there was absolutely no evidence of the alleged conspiracy, beyond the taking of parallel action; that each of the participants denied any communication or consultation with any of the co-defendants; and that none of the witnesses was in any way impeached or gave any testimony that was inherently incredible, several of them being members of the bar, the Court is not justified in finding that the actions were jointly planned or concerted.³²⁶

The Court of Appeal affirmed the decision;³²⁷ *certiorari* was denied by the U.S. Supreme Court.³²⁸

1. *Salk Vaccine Case*³²⁹ (1959)

The five pharmaceutical companies licenced to manufacture and sell the Salk polio vaccine were charged with a "continuing agreement, understanding, plan and concert of action" to "submit uniform price quotations," "adopt uniform and noncompetitive terms and conditions for sales" and "adopt uniform and noncompetitive methods" for pricing the vaccine in sales to government agencies.³³⁰ The government charged that the agreement could be inferred from circumstances ranging from uniformity in pricing sales to government agencies, to the defendants' proclivity to discuss prices to variations in prices and terms quoted to foreign purchasers. In each instance, the trial judge decided there was a reasonable explanation of the defendants' behavior which was consistent with a finding of "not guilty." For example, with respect to price uniformity, he accepted the argument that the "most favored nation" clauses in the contracts produced the uniformity. He refused to accept the government's contention that uniform behavior together with a number of "plus factors" provided the basis for an inference of conspiracy.

In deciding against the Department of Justice, the District Court appears to have gone beyond the rule in *Hodge's Case*, for it stated:

. . . The Government [must] not only prove the defendants' guilt based on a reasonable hypothesis beyond a reasonable doubt, but also . . . simultaneously eliminate every other reasonable hypothesis of innocence.³³¹

³²⁶ *Id.*

³²⁷ 261 F. 2d 380 (D.C. Cir., 1958).

³²⁸ 359 U.S. 943 (1959).

³²⁹ *U.S. v. Eli Lilly & Co.*, Crim. No. 173-58 D.N.J., Nov. 30, 1959 at 54, as cited in Almarin Phillips and George R. Hall, *The Salk Vaccine Case: Parallelism, Conspiracy and Other Hypotheses* (1960), 46 *Virg.L.Rev.* 717.

³³⁰ *Id.* at 718.

³³¹ *Id.* at 717.

Almarin Phillips and George Hall argue that such a test is "unrealistic" and that "it limits the doctrine of conscious parallelism to the point that it is virtually indistinguishable from overt agreements in restraint of trade."³³²

m. *Delaware Valley Marine Supply*³³³ (1961)

Delaware Valley, a newly formed tax-free seller of liquor and tobacco to foreign trade vessels entering the Port of Philadelphia, sued the five largest tobacco companies in the U.S. and an established tax-free seller alleging violation of section 1 of the *Sherman Act*. When approached by the new firm, all the tobacco companies refused the new firm a "direct listing" to enable it to purchase cigarettes on a tax-free basis. The new firm never commenced business.

There was no direct evidence of a conspiracy, i.e., concerted refusal to deal. Two of the firms denied the application by letter, two did not even answer Delaware Valley's letter and one refused orally after an initial interview and adhered to its decision after an extensive investigation and valuation. All but one defendant denied that they had knowledge that Delaware's application had been or would be denied by any other company.

After reviewing the evidence, the Appeal Court found it "sufficient to support a finding by a jury of conscious parallelism," but that the type of behavior shown, "standing alone," was insufficient to sustain a finding of conspiracy.³³⁴ The Court noted that the tobacco companies' actions were limited to saying "yes" or "no." Therefore, "the suspicion which would be created by the unlikelihood of numerous firms reaching one of many conclusions is lacking"³³⁵ What is more, it was the plaintiff's contention that to be successful, a tax-free outlet must have all major brands available for sale. The refusal by one major cigarette producer could cause the enterprise to fail.

With respect to the application of section 1 to conscious parallelism, the Appeal Court stated:

. . . it is a fact that conspiracy remains an essential ingredient of a case based on Section 1. Conscious parallelism . . . is of aid in demonstrating the existence of sophisticated and silent agreements which so often have injuriously restrained trade. But conscious parallelism is not yet a conclusive legal substitute for proof of conspiracy.³³⁶

The Court relied on the Supreme Court's decision in *Theatre Enterprises* and on its own decision in *Milgram v. Loew's*.

³³² *Id.*

³³³ *Delaware Valley Marine Supply Co. v. American Tobacco Co.*, 1961 Trade Cases, Par. π 70, 170, 78682.

³³⁴ *Id.* at 78687.

³³⁵ *Id.*

³³⁶ *Id.* at 78685. In *U.S. v. FMC Corp.* (1969 Trade Cases, Par. π 72,901, 87405 at 87431) the District Court held that "proof of an agreement, express or implied, is essential to proving a conspiracy in violation of Section 1 of the Sherman Act."

n. *Naumkeag Theatres*³³⁷ (1965)

The Appeal Court's decision, affirming the District Court's directed verdict for the defendants (six film distributors and two theatres), follows the major line of cases in the wake of Mr. Justice Clark's ruling in *Theatre Enterprises* over a decade earlier. The decision is interesting for two reasons: an observation as to what constitutes conscious parallelism, and its statement in respect to the "conscious parallelism plus" approach.

The defendants argued that there was not even any evidence of conscious parallelism. The Appeal Court recognized the serial nature of oligopolistic interdependence and replied:

This argument, that it did not appear that any distributor knew what the others' decision "would be" at the time when it made its own decisions, overlooks the obvious fact that decisions (to act or not to act) are made continuously and not once and for all. A defendant at all times could look at the past inactivity of its competitors and eventually draw conclusions that if it did not change, neither would they.³³⁸

With respect to the test to be applied, the Appeal Court stated:

. . . conscious parallelism is concededly not enough [citing two cases]. Plaintiff's burden is to show that there was evidence warranting a finding of something additional from which a reasonable inference of conspiracy may be made, or, as it puts it, of conscious parallelism "plus."³³⁹

The key "plus factor" in this case, the plaintiff argued, was the fact that its theatre was ranked behind the two defendants' theatres—even though it was not in substantial competition with them. However, the Court found that "the plaintiff's contention that placing it behind [the defendant theatres] was contrary to defendant exhibitors'³⁴⁰ best financial interests, independently considered, totally unsubstantiated."³⁴¹ The other "plus factor," the Court concluded, showed a departure from parallelism, conscious or otherwise. The Supreme Court denied *certiorari*.³⁴²

o. *Wall Products*³⁴³ (1971)

This case was a treble-damage action by a group of building supply and wallboard dealers against three manufacturers of gypsum wallboard who in 1968, accounted for sixty-one per cent of the U.S. market. The producers were alleged to have violated section 1 of the *Sherman Act*. There were two main elements to the case: (i) exchanges of price information which the producers argued were necessary to verify prices to protect themselves against buyer

³³⁷ *Naumkeag Theatres Co., Inc. v. New England Theatres, Inc.*, 1965 Trade Cases, Par. π 71,455, 80994.

³³⁸ *Id.* at 80995.

³³⁹ *Id.*

³⁴⁰ *Id.* From the text, it is clear that "distributors" should be substituted for "exhibitors."

³⁴¹ *Id.* at 80997.

³⁴² 382 U.S. 906 (1965).

³⁴³ *Wall Products Co. v. National Gypsum Co.*, 1971 Trade Cases, Par. π 73,523, 90121.

misrepresentations to avoid violations of the *Robinson-Patman Act* and (ii) "interdependent conscious parallel action" by the producers whereby they withdrew all exceptions to published list prices, ignored competition from single-plant producers, centralized pricing decisions in one officer and withdrew extended credit terms. The first element should be classified as an "information dissemination" case and will not be dealt with here, but the second is of interest in the development of jurisprudence on conscious parallelism.

The defendants' expert described the industry as "a classic type of undifferentiated oligopoly."³⁴⁴ Between 1960 and 1968 industry capacity rose by about thirty per cent. The number of single-plant producers tripled during the period and their share of the market increased from 3.8 per cent to 7.8 per cent of industry capacity. In 1968, the time at which the alleged conspiracy began, the industry had fourteen producers. The two largest producers accounted for 56.4 per cent of sales; the five largest accounted for 68.3 per cent. In both the San Francisco Bay Area and the nation, the market shares of United States Gypsum (USG), which was the largest producer with 33.2 per cent nationally in 1968, and those of the other defendants experienced a "substantial decline." A similar decline occurred in the rate of return of USG and National Gypsum, the two largest producers. District Court Judge Zirpoli concluded that "the overwhelmingly important factor influencing the buyer's decision as to which brand of wallboard to buy is price."³⁴⁵

In the spring of 1965, USG decided to change its policy of "defensive pricing." The period 1964-65 had been a period of price cutting by the wallboard producers as single-plant producers who, lacking the services available from established multi-plant firms, undercut list prices. The established firms matched and the single-plant firms cut again. Mill net prices in mid-1965 were lower than at any time since the mid-1950's. USG hoped that by withdrawing "P.A.'s" (price deviations) to meet competition and republishing its prices at lower levels, prices would stabilize. In addition, USG decentralized pricing authority, limited P.A.'s to five per cent off list price for volume purchasers and extended its zone pricing system throughout the rest of the United States.

USG expected its competitors to follow. They did not; the five per cent discount was given to all accounts and prices continued to decline. By September 1965, USG was selling below its list price to thirty-eight per cent of its dealers to meet competition. The firm's gross profit in 1966 was anticipated to be \$29,000,000 below that of 1964.

In October and November USG developed a new strategy to stop the erosion of its prices, profits and market share. On November 17, 1965, it mailed announcements to the trade that, effective December 15, 1965, it would withdraw all price exceptions and adhere strictly to its published list prices. Two parts of the strategy were not made public: (i) that USG would not meet the prices of single-plant producers, and (ii) that pricing authority

³⁴⁴ *Id.* at 90127.

³⁴⁵ *Id.* at 90130.

would be centralized in two senior officials (the Chief Executive Officer and the Vice-President of Marketing) with no delegation of authority.

Within two weeks, the other defendant producers refused to meet the competition of single-plant producers and centralized their pricing authority in their Chief Executive Officer. Judge Zirpoli noted, with emphasis, that USG's witnesses unanimously testified that the success of the new pricing policy was dependent upon its other major competitors following USG's initiative. The defendants adhered to the new policy until the end of 1967.

Judge Zirpoli said that the behavior of the defendants went beyond "mere conscious parallelism" and he concluded that the wallboard producers conspired to stabilize and maintain the price level of their product "through a course of interdependent conscious parallel action pursuant to a tacit understanding by acquiescence coupled with assistance . . ." ³⁴⁶ from USG's three-part policy of December 15, 1965. But he also cited evidence which indicated that more than a tacit understanding existed. With respect to National Gypsum, there was documentary evidence that its "Plan of Action," incorporating the unannounced features of USG's plan, was written prior to November 17, 1965. ³⁴⁷ On the basis of this and other evidence, Judge Zirpoli concluded that "National had advance notice of USG's action; [and] had agreed to follow a similar policy . . ." ³⁴⁸ This constituted a *per se* illegal conspiracy in violation of the *Sherman Act*.

With respect to the actions of another defendant (Kaiser Gypsum, 6.5 per cent of the market in 1968), Judge Zirpoli recognized how "offer and acceptance" of an oligopolistic agreement can occur. Prior to USG's announcement in November 1965, the chief executive of Kaiser had requested that USG and National stop deviating from list price. After quoting the ruling in *Interstate Circuit*, Judge Zirpoli stated:

Thus, when [the chief executive of Kaiser] suggested to his competitors that they cease granting off-list prices he was effectively conveying his offer to participate in a plan to withdraw discounts and fix prices at list. An exchange of words is not required. ³⁴⁹

He then quoted the following rule from the Ninth Circuit Court of Appeal's decision in *Esco v. United States*:

Written assurances it concedes, are unnecessary. So are oral assurances, if a course of conduct, or a price schedule, once suggested or outlined by a competitor in the presence of other competitors, is followed by all—generally and customarily—and continuously for all practical purposes, even though there be slight variations. ³⁵⁰

If "outlined by a competitor in the presence of other competitors" extended to the public announcement of a price list (or changes in an established price list), this last ruling could have real force. Why should it be

³⁴⁶ *Id.* at 90149.

³⁴⁷ *Id.* at 90144.

³⁴⁸ *Id.* at 90145.

³⁴⁹ *Id.* at 90146.

³⁵⁰ 304 F. 2d 1000 at 1008 (1965).

necessary for competitors to be present in the same room as they were at trade association meetings when the metal culvert producers were exhorted to follow an open price policy in the *Armco*³⁵¹ case? Why, too, should the rule be limited to a competitor suggesting or outlining a course of conduct or price schedule? In the *Armco* case, officials of two major suppliers to the industry met with the metal culvert producers individually apparently to advocate adoption of an open price policy.

To return directly to *Wall Products*, *quaere* why it was necessary for Judge Zirpoli to add to the plethora of terminology by using the term "interdependent conscious parallelism." Clearly, he wanted to indicate that the behaviour in the case went beyond "mere conscious parallelism." Almost by definition, conscious parallelism grows out of the interdependence of firms in an oligopoly, particularly those products homogeneous products.

p. *Bogosian v. Gulf Oil*³⁵² (1975)

Here the plaintiffs wished to test "whether pleading no more than interdependent consciously parallel action is sufficient to support a claim under Sherman Act S.1. . . ."³⁵³ The District Court rejected the argument that "the critical factor is that Sherman Act S.1 requires concerted action" and that the phrase "interdependent conscious parallel action' fails to satisfy [section 1]."³⁵⁴

The plaintiffs relied on *Wall Products*, but the District Court pointed out that in that case "a classic Sherman Act S.1 combination, contract, or conspiracy could be found without resorting to interdependent conscious parallel action."³⁵⁵ The Court then reviewed *American Tobacco*, discussed *supra*, and summarized its own position as follows:

In its usual contest [*sic*, context] conscious parallelism or interdependent conscious parallelism is circumstantial evidence of agreement. While interdependent conscious parallelism may often be based upon agreement such business behavior may be the result of rational individual decisions of competitors. The latter, if without any agreement, is not actionable . . . interdependence is merely additional circumstantial evidence or indicia of an agreement. Conscious parallelism has become a shorthand term for parallel business behavior where a Sherman Act S. 1 violation is attempted to be proven without benefit of a formal agreement. It is not necessary to burden the language of antitrust law with another nonoperational term, viz., interdependent consciously parallel action.³⁵⁶

2. Summary

The importance of judicial rulings in specific cases is dependent upon a considerable number of factors: (i) the specific facts of the case—individual rulings are not based on issues submitted for consideration in the abstract, they are made in the context of a set of facts virtually unique in each instance. Generalizations must be made with care; (ii) the rulings are seldom unadorned

³⁵¹ *Supra*, note 62.

³⁵² *Bogosian v. Gulf Oil Corp.*, 1975 Trade Cases, Par. π 60,284, 66104.

³⁵³ *Id.* at 66107.

³⁵⁴ *Id.*

³⁵⁵ *Id.* at 66108.

³⁵⁶ *Id.* at 66109.

by qualification; they are often accompanied by contradictory statements within the same case. This is why different passages within the same case can be cited to sustain conflicting statements; (iii) interpretations are given at a specific moment in time and can only reflect the cumulative thinking of previous cases. Therefore, an appreciation of the significance of a ruling is very much time-dependent. Statements as to what the law is must be time-related.

L. A. Sullivan points out that the government, in order to succeed in a conscious parallelism case under the conspiracy provisions of the *Sherman Act*, must show more than mere parallelism of action. The evidence must be sufficient for the judge or jury to conclude "that the participants have become a group acting together, rather than individual competitors who happen at the moment to be doing the same thing."³⁵⁷ The evidence as a whole must indicate there has been common conduct. He argues that the evidence must reveal "that they have, in one way or another, communicated, and given assurances, one to another."³⁵⁸

E. THE OPTIONS FOR CANADIAN PUBLIC POLICY

Conscious parallelism, particularly in the form of closely coordinated oligopoly behaviour without apparent collusion, constitutes one of the major problems of competition policy. The Canadian courts have, to date, refused to condemn even consistent and closely parallel action by members of an oligopoly unless the Crown can show that there was, or the Court can infer, either a tacit or express agreement. While the law on conspiracies has long held that direct proof of an agreement is unnecessary and that it may be inferred from the whole of the circumstantial evidence, an inference prejudicial to the accused must be based, not simply on the basis of whether the facts are consistent with the accused's guilt, but on whether they are inconsistent with any other rational conclusion. Although it may be difficult, using economic analysis, to meet the second part of the test, it may be quite easy for Canadian judges to find other "rational" explanations of parallel behaviour by businessmen.

One must recognize that oligopoly involves a mixture of interdependency and conflict. In game theory terms, it is a variable-sum, mixed-motive game, the outcome of which is determined by bargaining and quasi-bargaining behaviour.³⁵⁹ While it may be too strong to define "solutions" to oligopoly conflict and cooperation as "agreements" in the usual legal sense, they do involve mutual recognition and acquiescence through complementary actions and reactions. Conflict may never be reconciled in the sense of a "permanent" peace, but a *modus vivendi* does occur through actions which coordinate inter-firm behaviour where the firms either "cannot or will not negotiate explicitly or when neither would trust the other with respect to any agreement explicitly reached."³⁶⁰

³⁵⁷ Sullivan, *supra*, note 261 at 317.

³⁵⁸ *Id.*

³⁵⁹ This view is adapted from T. C. Schelling, *The Strategy of Conflict* (London: Oxford University Press, 1969) at 89.

³⁶⁰ *Id.* at 53.

In oligopoly, as in life, all behaviour is communication.³⁶¹ Apparently unilateral behaviour by oligopolists contains information relevant to other firms who "decode" it and utilize it in choosing their own actions, which also convey information. Information and communication are unavoidable in the situation itself.³⁶² In the mixed-motive game of oligopoly, "hardly anything epitomizes strategic behaviour . . . so much as the advantage of being able to adopt a mode of behaviour that the other party will take for granted."³⁶³ Schelling points out that in a mixed-motive game:

. . . two or more centers of consciousness are dependent on each other in an essential way. Something has to be communicated, at least some spark of recognition must pass between the players. There is generally a necessity for some social activity, however rudimentary or tacit it may be; and both players are dependent to some degree on the success of their social perception and interaction. Even two completely isolated individuals, who play with each other in absolute silence and without knowing each other's identity, *must tacitly reach some meeting of minds.*³⁶⁴

It is generally observed that public policy formation proceeds in a disjointedly incremental fashion.³⁶⁵ Changes in policy tend to be small relative to existing policy and they are often initiated by a number of actors whose actions are often ill-coordinated. A common failing of the policy formulation process is that few alternatives are articulated and the evaluation of their potential consequences is inadequate,³⁶⁶ even recognizing the costs of information and limitations in the cognitive capacities of analysts and decision makers.

With these concerns in mind, we offer the following alternative public policy approaches to the problem of conscious parallelism in Canadian industry:

1. No new legislation, make do with section 32 of the *Combines Investigation Act*.
2. Adopt the joint monopolization provisions of the proposed *Competition Act* of 1977.
3. Direct intervention by the government in industries where the performance of firms is unsatisfactory.
4. Adopt new civil legislation which would condemn persistent conscious parallelism when accompanied by one or more specified "plus factors."
5. Adopt a program of time-staged tariff reductions for all concentrated industries which exhibit long-term poor economic performance.

³⁶¹ The proposition that all behaviour is communication comes from Gregory Bateson, *Steps to an Ecology of Mind* (St. Albans: Paladen, 1973) at 334-45.

³⁶² *Supra*, note 359 at 115.

³⁶³ *Id.* at 160.

³⁶⁴ *Id.* at 163 (emphasis added).

³⁶⁵ David Braybrooke and Charles E. Lindblom, *A Strategy of Decision* (New York: The Free Press, 1970) Chapters 5, 6.

³⁶⁶ See R. M. Cyert and J. G. March, *A Behavioral Theory of the Firm* (Englewood Cliffs: Prentice-Hall, 1963) and Herbert A. Simon, *Models of Man: Social and Rational* (New York: John Wiley & Sons, 1957).

6. Establish a *per se* proscription of all forms of refusal to deal and exclusive territorial distribution systems together with a *per se* prohibition of selective geographic price discrimination by dominant firms.

We will now discuss the nature of each alternative approach in more detail and assess its potential effectiveness. It should be apparent that alternatives one to four are mutually exclusive, but five and six could be adopted in conjunction with any of the other approaches.

1. *No New Legislation*

In the face of vociferous and well-organized business opposition to all changes in Canadian competition policy which would inhibit the use of market power by firms,³⁶⁷ soldiering on with section 32, as it now exists, is an alternative which would be relatively easy to implement. The *Armco* case³⁶⁸ could be used to support the argument that section 32 is adequate to combat cases involving conscious parallelism. This argument, of course, ignores the fact that in *Armco*, it was necessary for the trial judge to *infer* the existence of an agreement before a violation of section 32 could be found.

What is apparent is that the courts are beginning to grapple seriously with the problem of oligopoly without direct agreement as they become cognizant of the subtleties of oligopolistic competition. The *Atlantic Sugar* case³⁶⁹ illustrates the difficulty of attacking a close knit oligopoly with the conventional legal tools of conspiracy. Agreement in the legal sense was unnecessary. The three dominant firms were able to obtain the same result by consciously parallel behaviour. When the number of firms with significant shares of the market is small and the product is homogeneous, each firm without communicating verbally or in writing is able to independently arrive at the same price structure. All exhibit very similar behaviour patterns and interfirm competition is confined to activities which are unlikely to really hurt financially. As Donald Eldon points out, an oligopoly

. . . tends to develop a plane of competition, some recognition by the group of sellers as to the forms which competition will ordinarily take. Marked cutting of prices tends to occur only when the stable pattern of the industry is temporarily broken, as by the entry of a new firm into the market or by a determined bid by an established firm for a larger share of the market.³⁷⁰

The effect, in terms of prices, profits and productive efficiency of a typical collusive oligopolistic solution is unlikely to be different from an oligopolistic arrangement obtained by conscious parallelism. Closely coordinated behaviour, achieved by "independent" action through conscious parallelism is apparently beyond the reach of section 32 of the *Combines Investigation Act*.

For the present conspiracy provisions to be of real effect in conscious

³⁶⁷ See W. T. Stanbury, *Business Interests and the Reform of Canadian Competition Policy, 1971-1975* (Toronto: Carswell/Methuen, 1977); H. G. Thorburn, *Pressure Groups in Canadian Politics: Recent Revisions of the Anti-Combines Legislation* (1964), 30 *Canadian Journal of Economics and Political Science* 157.

³⁶⁸ *Supra*, note 62.

³⁶⁹ *Supra*, note 135.

³⁷⁰ *Supra*, note 5 at 151.

parallelism cases there is a need to reinterpret the traditional legal concept of agreement. Conant puts the point this way:

Although [firms engaging in conscious parallelism] do not meet or communicate directly, theirs is a "meeting of the minds" that each will be non-aggressive in price or marketing policies in the then existing manner as long as his rivals are of the same mind. There is a "unity of purpose" to keep prices stable, not to spoil the market, and to avoid "cutthroat" competition. And this same purpose may be called a "common design," though reached independently by each firm in adjusting to the presence and possible reactions of his rivals in the market.³⁷¹

If this view was accepted, the requirements of finding an agreement would be more easily met and persistent conscious parallelism could be successfully attacked. Phillips and Hall emphasize that an agreement can be effected without verbal communication:

Economists and lawyers have recognized for many years that firms in oligopolistic markets may behave as though there were an agreement restraining trade when there has been no verbal communication among them. This recognition is the very essence of the conscious parallelism doctrine. Parallel behavior cannot be explained as chance or random behavior, yet there is no discernable way to explain it as open agreement . . . it is pointless to ask if the parallel behavior of oligopolists is the result of communication and agreement. Their indirect, nonverbal communication is both effective and inevitable. Their agreement, while varying in subject matter, duration and effectiveness, may be as complete as that reached through the use of explicit and overt communication . . .³⁷²

From the point of view of economic effects it does not matter whether they were achieved by direct agreement or sophisticated conscious parallelism. However, it is a large step to infer that the traditional interpretation of the law of conspiracy should thereby be changed to successfully attack the new forms of behaviour. Would it not be preferable to pass new legislation aimed at the new problem?

If we do not pass new legislation, but rather continue to rely on section 32, what can we expect? In our view, the best that we could hope for is that, in time, the Canadian courts will adopt interpretations like those of the U.S. courts following the *Interstate Circuit*³⁷³ case in 1939 and prior to the *Theatre Enterprises*³⁷⁴ case in 1954. As we have seen, after that time the U.S. courts reasserted the view that the parallel behaviour together with the ancillary evidence must be sufficient for the jury to infer that an agreement has been made by the defendants for a conviction to be registered.

It is unlikely that the more "liberal" interpretation of the U.S. courts between 1939 and 1954 will be followed in Canada. More recent U.S. interpretations go against the Supreme Court's view in *Interstate Circuit*. What is more, Canadian judges seem less willing to innovate in the interpretation of anti-combines law than those in the United States.

There is a more important reason for not relying on section 32. If it is to be used to strike at most conscious parallelism cases, it will be necessary for the courts to "stretch" the well-established interpretation of the law of

³⁷¹ Conant, *supra*, note 267 at 817.

³⁷² Phillips and Hall, *supra*, note 329 at 726-27.

³⁷³ *Supra*, note 262.

³⁷⁴ *Supra*, note 314.

conspiracy. Rather than do this, it is preferable to introduce new legislation aimed specifically at conscious parallelism and retain section 32 to deal with direct agreement or those that can properly be inferred according to the long established rule in *Hodge's Case*.³⁷⁵

2. *Adopt the Joint Monopolization Provisions of the Proposed Competition Act*

On March 16, 1977 the Stage II amendments to the *Combines Investigation Act*, Bill C-42, were given first reading in the House of Commons.³⁷⁶ Included in the Bill was a new civil provision, section 31.73, dealing with "joint monopolization." Joint monopolization was defined to mean a situation where (i) a small number of firms (not all affiliated) achieve or seek to achieve substantial control of a market; (ii) these firms do so by adopting closely parallel policies or closely matching conduct; and (iii) the policies or conduct have the effect of restricting entry, foreclosing a competitor's sources of inputs or sales outlets, eliminating a competitor by predatory pricing, coercing or disciplining a competitor or restraining economic activity by other means. Section 31.73(3) provides that a finding of joint monopolization could be made "notwithstanding that the parallel policies or matching conduct . . . was based on nothing more than a mutual recognition of . . . interdependence and that there was no agreement or arrangement between or among [the firms]."³⁷⁷ Where joint monopolization is found, the Competition Board, the proposed quasi-judicial tribunal, is empowered to issue a prohibition or remedial order or, where these would fail to restore competition, to require dissolution or divestiture as specified. However, no order shall be made where the Board "is satisfied that the policies or conduct [of the person] solely reflects superior efficiency or superior economic performance."³⁷⁸

Business reaction, as indicated by the many briefs from trade associations and individual firms to the House of Commons Standing Committee on Finance, Trade and Economic Affairs, was almost uniformly hostile to section 31.73.³⁷⁹ An analysis of 50 of the approximately 80 business briefs indicated

³⁷⁵ *Supra*, note 78.

³⁷⁶ *Proposals for a New Competition Policy for Canada, Second Stage* (Ottawa: Dept. of Consumer and Corporate Affairs, 1977). For a review of the Bill, see Martin J. Rochweg, *Proposed Stage II Amendments to Canadian Combines Legislation—Bill C-42* (1977), 15 *Osgoode Hall L.J.* 51.

³⁷⁷ *Proposals*, *id.* at 192.

³⁷⁸ *Id.* at 193, section 31.73(5) *errata*.

³⁷⁹ The Committee received a total of 147 briefs, 38 of which were accompanied by testimony at the hearings on Bill C-42. The following indicates the distribution of the briefs by source: individual business firms (43); trade organizations (38); farm organizations (12); marketing boards (22); academics (8); provincial governments or their departments (6); individuals (8); lawyers/Canadian Bar Association (5); union/Canadian Labour Congress (2); consumer organizations (2); and other (1). The briefs from farm organizations, marketing boards and provincial governments were almost exclusively devoted to objections to sections 4.5, 4.6 and 27.1 of Bill C-42. These sections deal with regulated conduct, the conditions for the exemption of federal and provincial marketing boards, and the power of the Advocate to intervene in a matter before any federal board; they accounted for 81 of the 147 briefs; with the exception of the Canadian Bar Association's brief, the other four from lawyers should be classified as "business briefs."

that one-half requested that section 31.73 be deleted from the bill. Much of the criticism of the section was based on the view that any parallel conduct could be reviewable by the Competition Board. The House Committee in its report on Bill C-42 emphasized that ". . . it is not parallel conduct *per se* that is subject to review but only parallel conduct that restrains economic activity in the manner described in subsection 31.73(1)."³⁸⁰ The House Committee recommended only two relatively minor amendments. However, the Standing Senate Committee on Banking, Trade and Commerce recommended that section 31.73 be deleted entirely.³⁸¹

On November 18, 1977, Bill C-13, the successor to Bill C-42, was given first reading in the House of Commons. It embodied some seventy amendments, including some to section 31.73. The cumulative effect of the changes in the joint monopolization section is to weaken its ability to strike at parallel behaviour which has a predatory or exclusionary effect. For example, Bill C-13 defines joint monopolization as a situation where a small number of firms "achieve substantial control or entrench such control . . .", whereas C-42 used the words "achieve or seek to achieve substantial control. . . ." Is C-13 aimed at joint monopolization in its incipency or only after it is an accomplished fact? Second, section 31.73 of Bill C-13 describes the reviewable behaviour as "adopting closely parallel policies or closely matching conduct of an exclusionary character . . ." which has the effect of restricting entry, foreclosing a competitor's outlets or sources of supply, and so on. Bill C-42 did not require that the parallel policies be of an "exclusionary character." Such words may be construed by defence counsel so as to require the Competition Board to examine the *intent* of the firms involved. This will add another hurdle for the Crown to overcome. Third, the subsection specifying that the Board can make an order against joint monopolization, even if there was no agreement among the firms involved, has been retained. But the words, "based on nothing more than a mutual recognition of their interdependence . . ." have been deleted. Fourth, the efficiency defence has been made easier to sustain. Bill C-42 prevented the Board from making an order if it was satisfied "that the policies or conduct . . . solely reflect superior efficiency or superior economic performance." In C-13 the word "clearly" replaces the word "solely." Fifth, the range of remedies for joint monopolization is restricted in Bill C-13 to partial divestiture. In Bill C-42, the Competition Board could make an order "to dissolve the monopoly or reduce the degree of monopoly . . ." as alternatives to divestiture. In addition to these changes in section 31.73, under section 31.91 of Bill C-13, defendants faced with a partial divestiture order for joint monopolization may appeal to the Cabinet,

³⁸⁰ *Proposals for Change*, Fourteenth Report of the Standing Committee on Finance, Trade and Economic Affairs Respecting Stage II Competition Policy (Ottawa: Supply and Services Canada, 1977) at 63. A critique of the amendments proposed by the Committee in respect to administration and enforcement is found in M. T. MacCrimmon and W. T. Stanbury, *Policy Death by Administrative Restriction: The House Committee's Report on Bill C-42, The Competition Act of 1977* (1977), 15 Osgoode Hall L.J. 485.

³⁸¹ Can. Senate Standing Committee on Banking, Trade and Commerce, *Proceedings*, (July 6, 1977).

upon the recommendation of the Minister of Consumer and Corporate Affairs, to annul the order.

Although Bill C-13's treatment of joint monopolization is less stringent than Bill C-42's, it goes well beyond the existing legislation in dealing with parallel policies or coordinated behaviour in oligopoly. Its scope, however, is limited to situations where the parallel policies have one or more predatory or exclusionary effects. Ordinary parallel behaviour which does not have such an effect, but which still might result in excess profits and/or inefficiency, would not be within the purview of the proposed legislation. The fact that joint monopolization is to become a civil reviewable matter is highly desirable. The scope of remedies available is enlarged and the standard of proof is on the basis of the balance of probabilities, rather than on proof beyond a reasonable doubt as required for criminal offences.

As desirable as section 31.73 is, in that it moves in the right direction, it does not go far enough. The law should permit the Competition Board to take action in cases of conscious parallelism in a larger variety of instances of restraint of trade than simply those which involve predatory or exclusionary action. Skeoch and McDonald deal with a broader conception of joint monopolization under their proposal in respect of "misuse of dominant position":

- (a) "dominant" means the power to choose the rate of profits or share of the market to be enjoyed by the person or group of persons possessing the power, largely undeterred by any existing ability of rivals to compete away those profits or share of the market by offering for favorable terms to customers;
- (b) "misuse" means 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.³⁸²

The focus of the Skeoch and McDonald proposal is on both unsatisfactory conduct and on unsatisfactory performance. While it appears to reach behavior not reached by the proposed 31.73 we feel that the conscious parallelism plus approach outlined in the fourth alternative is preferable. If this alternative is politically infeasible, but section 31.73 can be made into law, then we should be pleased to see it as a complement to the existing section 32.

3. *Direct Government Intervention*

Direct intervention by the government in light of undesirable economic performance by an industry or group of firms, would represent a major departure in Canadian public policy. Combines law has historically been conduct or behaviour oriented. For example, in conspiracy cases the approach might be characterized as "once undue then *per se* illegal." That is, the judges, once proof of a conspiracy has been established by direct evidence or by proper inference, have specifically refused to consider the economic perform-

³⁸² L. A. Skeoch and B. C. McDonald, *Dynamic Change and Accountability in a Canadian Market Economy* (Ottawa: Information Canada, 1976) at 156.

ance which has or would have resulted from the illegal agreement.³⁸³ The determination of what constitutes an agreement to restrain or lessen competition unduly has been based on the proportion of the market which has been subject to the conspiracy. While Canadian judges have not espoused any specific structural standard, by inference from the decided cases it would appear that if one-half or more of the output in the relevant market is produced by firms party to the arrangement, it will constitute an undue lessening of competition.³⁸⁴

David Cayne has suggested that the most serious deficiency of the judge-made combines law in Canada has been the development of "rigid rules which vary with the form of industrial conduct rather than with its substance or consequences. . . ." ³⁸⁵ He goes on to say:

. . . judicial rejection of the concepts of market power and economic efficiencies in the evaluation of the behaviour of firms has led to the failure to apply similar standards to horizontal integration effected through different means.³⁸⁶

Cayne's term "horizontal integration" includes both mergers and oligopolistic interdependence. With respect to the latter, he points out that the only difference between price leadership and conscious parallel action in an oligopoly

³⁸³ In general, two points are being made here. First, it is irrelevant whether or not the agreement was necessary for the protection of the business interests of the parties to it. This point was first established by Anglin J. in *Weidman v. Shragge* (1912), 46 S.C.R. 1 at 42-43, where he said,

under [S. 498] the prime question certainly must be, does [the agreement], however advantageous or even necessary for the protection of the business interests of the parties, impose improper, inordinate, excessive, or oppressive restrictions upon that competition the benefit of which is the right of everyone?

These words were quoted and adopted by Mignault J. in the second Supreme Court case, *Stinson-Reeb Builders Supply Co. Ltd. v. The King* (1929), 52 C.C.C. 66 at 69 and also by Kerwin J. (Rinfret J. concurring) in *Container Materials Ltd. v. The King*, *supra*, note 168 at (C.C.C.) 140-41.

Second, Canadian judges refuse to consider the reasonableness of prices subject to the agreement or to evaluate the behaviour in terms of the economic conditions facing the industry. The classic statement was given by Spence J. in *R. v. Howard Smith Paper Mills Ltd.*, [1954] O.R. 543; 4 D.L.R. 161; 109 C.C.C. 65; 19 C.R. 1 at (C.C.C.) 95-96:

Surely the determination of whether or not an agreement to lessen competition was "undue" by a survey of one industry's profits against profits of industry generally, and a survey of the movement of the prices in that one industry against the movement of prices generally, would put the Court to the essentially non-judicial task of judging between conflicting theories of economy and conflicting political theories. It would entail the Court being required to conjecture—and by a Court it would be nothing more than mere conjecture, since the Court is not trained to act as an arbitrator of economics—whether better or worse results would have occurred to the public if free and untrammelled competition had been permitted to run its course.

Mr. Justice Spence later stated, at 97:

. . . I am not free to find that the lessening intended was not undue on the basis of any necessity of the industry, reasonableness of prices resulting or reasonableness of profits obtained.

³⁸⁴ *Supra*, note 213.

³⁸⁵ David Cayne, *Market Power, Efficiencies, and the Public Interest in Canadian Combines Law* (1970), 16 McGill L.J. 488 at 489.

³⁸⁶ *Id.*

and other forms of collusive action is that "the communication [among competitors] can take place indirectly through the market system itself."³⁸⁷ He argues that since the effects are the same, "it is meaningless to predicate the legality of the resulting market power upon the character of the communicative process itself."³⁸⁸ A policy of direct intervention based on performance criteria would overcome this difficulty.

However, government intervention in cases of "unsatisfactory" economic performance obviously begs the question of what measures of performance should be used. Many industrial organization economists would include at least the following elements of market performance: level and variability of prices and profits, technical efficiency (including the question of X-inefficiency), allocative efficiency, rate of innovation and technological change, the nature and persistence of excess capacity and the types of restrictive trade practices (e.g., price discrimination, resale price maintenance, etc.) that exist in the industry. This list is not exhaustive. With multiple criteria, problems of commensurability arise, and the necessity to make tradeoffs is obvious. What is the minimum socially acceptable level of performance for each of the measures of firm and industry performance? What do we do if an industry exhibits significant excess profits over a span of five to ten years, while at the same time is perceived as an aggressive innovator in methods of production and in introducing new products? These are difficult questions. They must be answered correctly before a policy of direct intervention has any hope of success.

Certainly not the least of our problems with this approach is to determine the appropriate remedy if the government deems performance to be unsatisfactory. Simple injunctions prohibiting parallel conduct may be ineffective. Neale argues:

It is no good telling the businessman to stop conspiring if all that is meant by 'conspiring' is reacting intelligently to the situation in which he finds himself. How can he make decisions independently if the very structure of his industry makes him and his main rivals interdependent?³⁸⁹

The U.K. Monopolies Commission, in its 1973 report on parallel pricing, perceived the remedy in terms of limiting the extent of the damage to the public interest. First they proposed to restrict the development of situations where the practice could arise, i.e., careful scrutiny of mergers which in themselves could significantly increase concentration ("a prerequisite of parallel pricing") or could trigger a series of mergers having the same effect.³⁹⁰ Second, "to ensure that, where it has arisen and is found to be operating contrary to the public interest, either pressure be introduced of a kind likely to force the sellers concerned into more active competition or, failing this, steps are taken to reduce the damage which might flow from the continuation of the practice."³⁹¹ The Commission recognized the very limited utility of breaking up the leading firms, rather it spoke of tariff reductions, the weakening of

³⁸⁷ *Id.* at 519.

³⁸⁸ *Id.*

³⁸⁹ Neale, *supra*, note 260 at 176.

³⁹⁰ *Supra*, note 7 at 37.

³⁹¹ *Id.*

entry barriers and of direct supervision of prices (and possibly of costs) in the industry concerned.³⁹²

In its report on the breakfast cereal industry, in which the largest firm accounted for sixty per cent of the market and the next two a combined thirty per cent, the Commission opted for the direct supervision of prices:

We see no practical means of changing the structure of the industry or the nature of competition in the industry in such a way as to ensure the maintenance of price restraint on Kellogg. . . . We therefore recommend that Kellogg's profit rates should be kept under review and that Kellogg should be required to seek Government approval before making any increase in the prices of its breakfast cereals.³⁹³

It is difficult to generate any enthusiasm for additional direct government intervention in the economy.³⁹⁴ This is not simply because the problem of defining remedies is difficult for it is difficult in every alternative proposed, or because the administrative mechanism to carry out the surveillance and intervention is hard to specify. The central issue is the potential costs and benefits of direct intervention as opposed to the other alternatives public policies available. Anyone concerned with diffusion of power and the efficacy of government intervention in the economy must look askance at any proposal that would increase it.

4. *Conscious Parallelism Plus*

Under this alternative, Canada would adopt new legislation which would make reviewable in civil proceedings those cases of persistent conscious parallelism which are accompanied by one or more specified "plus factors." These factors would include various kinds of economic conduct which have the effect of facilitating the close coordination of interfirm behaviour in an oligopoly or other undesirable aspects of economic performance. While the following list is not exhaustive, it does indicate the behaviour which should be defined as a "plus factor".³⁹⁵

(a) *Conduct Factors:*

- contrived or exaggerated product standardization
- exchange of detailed price and transaction data either *ex ante* or *ex post*
- use of uniform basing points in delivered pricing schemes
- uniform refusal to deal (by buyers or sellers)
- uniform exclusive territorial agreements
- uniform licencing arrangements
- parallel buying activity to collectively support the price of a substitute or an input used by competitors

³⁹² *Id.* at 38.

³⁹³ United Kingdom Monopolies Commission, *Report on Breakfast Cereals*, (1973) at para. 102.

³⁹⁴ See Skeoch and McDonald, *supra*, note 382.

³⁹⁵ These lists were compiled from the relevant Canadian and American cases as well as from Posner, *supra*, notes 29 and 43 and Nye, *supra*, note 323.

- price leadership—long continued uniform prices
- any conduct individually irrational but collectively profit maximizing
- exhortation (direct and indirect) to maintain or increase prices
- advance notification of price changes without legitimate business justification

(b) *Performance Factors:*

- persistent excess profits by the group (not explained by proper use of intellectual property rights)
- persistent excess capacity (allowing for seasonal and cyclical swings)
- submission of identical tenders on non-standard items or on large orders of standard items (relative to the producer's annual output)
- systematic price discrimination
- long term fixed market shares
- perverse price movements, e.g., price increases during periods of excess capacity

We must recognize that the single most important industrial phenomenon facing competition policy—closely coordinated oligopoly without collusion—is beyond the reach of legal tools originally fashioned, not to deal with the economic behaviour and effects of oligopoly, but to deal with agreements among individuals to commit acts clearly defined to be illegal. Eldon puts the issue this way:

The root of the [oligopoly] problem lies partly in the fact that antitrust law in North America antedates the time economists became generally greatly concerned with oligopoly. As a result, the law is designed in the less sophisticated terms of pure monopoly and perfect, pure or free competition.³⁹⁶

The point of the conscious parallelism plus approach is to obtain price and output combinations closer to the competitive equilibrium than would occur if we left non-collusive oligopoly alone. Since, in many oligopolies, the close coordination of interfirm behaviour is facilitated or even brought about by the type of “plus factors” indicated above, one practical alternative for public policy is to attempt to severely inhibit their use of these aids. It is unnecessarily pessimistic to say that nothing can be done, outside of preventing collusive agreements, to upset the high price-high profit, and perhaps inefficient, oligopolistic equilibrium. We believe that energetic and consistent attacks on cases of conscious parallelism accompanied by one or more of these “plus factors” (and any new ones that may be developed) will result in greater variability in prices and, on average, lower prices than would occur if the authorities permitted oligopolists to use these coordinating devices. Conant points out that

. . . an oligopolistic market structure need not necessarily result in market performance that fails to approach the competitive ideal. Dynamic market factors may induce rivalry whose consequence is effectively competitive market performance.³⁹⁷

³⁹⁶ Eldon, *supra*, note 5 at 150.

³⁹⁷ Conant, *supra*, note 267 at 812.

The object of public policy is to ensure that the potential dynamic factors are not inhibited. While we are not sanguine that the result will closely approximate the outcome if a genuinely competitive market structure prevailed, we are confident that the benefits outweigh the costs.

Support for the conscious parallelism plus approach is not hard to find. Stephen Nye, a Commissioner of the Federal Trade Commission remarks:

I suspect that in almost every instance of prolonged uniform pricing among oligopolistics, it is possible to uncover evidence of measures taken by the industry members and calculated, it may fairly be inferred, to ensure the smooth working of a system of administered pricing.³⁹⁸

In our discussion of interfirm coordination in an oligopoly we noted that a number of factors tend to limit the close coordination of oligopolists. We also noted that persistent, non-competitive parallel behaviour by oligopolists can only occur if one or more "props" are used to permit firms to act on the recognition of their mutual dependence. While Posner labels persistent conscious parallelism accompanied by one or more plus factors as evidence of "tacit collusion,"³⁹⁹ there is no substantive difference between the approach he advocates and the one we call "conscious parallelism plus." In his 1971 article, Posner describes "noncompetitive pricing by oligopolists without detectable collusion" as "nothing more than a special case of cartelization. . . ."⁴⁰⁰ He proposes a two-stage inquiry.⁴⁰¹ First, he would identify those markets whose characteristics predispose them toward price fixing, e.g., oligopoly structure, a homogeneous product for which there are no close substitutes, infrequent entry etc. Second, he would apply certain tests in suspect markets to determine if output was, or was likely to be, restricted significantly. Posner would look, *inter alia*, for evidence of fixed market shares, economic discrimination, exchanges of price information, and identical bids on non-standard items.⁴⁰²

Even Donald F. Turner would support the "conscious parallelism plus" approach although he argues that conscious parallelism is not evidence of agreement unless there is evidence that "the decisions of the alleged conspirators were *interdependent*, that the decisions were consistent with individual self-interest of those concerned only if they all decided the same way."⁴⁰³

Turner observes that "in reality a stable and firm pattern of non-competitive prices is rarely achieved without some kind of agreement."⁴⁰⁴ He notes that parallel delivered pricing systems, for example,

are adopted primarily to eliminate a kind of uncertainty that is a potent force disrupting stable noncompetitive oligopoly pricing . . . rigid price systems are

³⁹⁸ Nye, *supra*, note 323 at 210-11.

³⁹⁹ Posner, *supra*, note 29 at 1578-82.

⁴⁰⁰ Posner, *supra*, note 43 at 509.

⁴⁰¹ *Id.* at 514-15.

⁴⁰² *Id.* at 516-22.

⁴⁰³ Turner, *supra*, note 41 at 658.

⁴⁰⁴ *Id.* at 662.

adopted in order to make parallel oligopoly pricing possible, to prevent the necessity of pricing competitively.⁴⁰⁵

This is precisely the sort of plus factor, which, if used to facilitate persistent conscious parallel pricing, would be subject to attack under this policy proposal. However, it is important to be mindful of the fundamental public policy dilemma with respect to oligopoly. If we condemn conscious parallelism, price leadership and other forms of legally non-collusive oligopoly behaviour and require that firms behave independently, to the extent of ignoring their self-interest in the context of their mutual dependence, we are asking them to behave irrationally. But one of the characteristics of firms operating in an oligopoly is that they are motivated both to compete and to cooperate on the recognition of their mutual dependence. The "conscious parallelism plus" approach seeks to ensure that oligopolists compete more actively by striking at the means by which cooperative behaviour is effected. Since the plus factors include both performance and conduct elements, firms which are able to effect close coordination without one of the conduct "props" will still be subject to attack. This approach is justified by the theory of Posner,⁴⁰⁶ Turner,⁴⁰⁷ and Nye:⁴⁰⁸ that persistent excess profits, inefficiency, fixed market shares or identical tenders for non-standard items are not the result of "pure interdependence," but rather the result of non-detectable collusion. In effect, collusion may be inferred in such cases, even though it may not be appropriate to do so under section 32 of the *Combines Investigation Act*.

The determination of appropriate remedies, however, raises difficult problems. In the Canadian setting, in which the small size of the domestic market, together with economies of scale,⁴⁰⁹ results in a relatively small number of domestic producers in many industries, structural remedies will rarely be feasible. Injunctive orders, in theory, prevent the use of conduct plus factors, but businessmen will find other means of coordinating their behaviour. Such orders will have to be broadly framed and directed to the *purpose* of these plus factors, rather than their specific form. In the case of tariff-protected oligopolies, a potentially useful remedy would be to lower tariffs and increase the opportunities for foreign producers. Government procurement policies can be used to "reward" firms who deviate from parallel pricing or price leadership in oligopolies. In some cases, it may be necessary to consider direct regulation of prices, advertising expenditures or additional capital investment. In any event, we must recognize that while the remedies available may ameliorate the present problem, they are unlikely to provide simple solutions to the complex problem of conscious parallelism.

5. *Tariff Reductions*

There is an old saying attributed to the organizer of the great U.S. sugar

⁴⁰⁵ *Id.* at 674.

⁴⁰⁶ *Supra*, notes 29 and 43.

⁴⁰⁷ *Supra*, note 41.

⁴⁰⁸ *Supra*, note 323.

⁴⁰⁹ See Paul K. Gorecki, *Economies of Scale and Efficient Plant Size in Canadian Manufacturing Industries* (Ottawa: Department of Consumer and Corporate Affairs, 1976).

trust of 1887 that "the tariff is the mother of trusts."⁴¹⁰ Industrial organization economists have long sought to use the tariff as an active instrument of competition policy.⁴¹¹ Because of Canada's small domestic market, coupled with important economies of scale, the number of domestic producers must, for efficiency reasons, be small in many Canadian industries.⁴¹² Under such conditions we expect that the domestic producers will practice limit pricing: the price set by domestic producers will be equal to the price of the closely substitutable products made abroad plus tariffs and transportation costs. Where the effective rate of protection is such that the limit price permits inefficiency or excess profits, there is a strong case for reducing or eliminating it. Currently, under section 28 of the *Combines Investigation Act*, the Cabinet is empowered to reduce tariffs in conspiracy, merger and monopoly cases where the "disadvantage to the public is presently being facilitated by the duties of customs imposed on the article or on any like article. . . ."⁴¹³ This potentially powerful weapon has been used in only one case.⁴¹⁴ Skeoch and McDonald challenge the idea that tariff reductions alone will assure long term dynamic efficiency.⁴¹⁵ They state that the available evidence from other countries suggests that tariff reductions are unlikely to result in the rationalization of Canadian industry, enabling firms to meet import competition and expand their export opportunities. They cite Britain and Sweden as historical examples to buttress their point.⁴¹⁶ To achieve their objective of dynamic economic change, "freer trade requires to be used, with appropriate timing, in combination with positive and prohibitory measures to facilitate, and to create pressures favouring the process of economic change in terms of the firm and the market."⁴¹⁷

The efficacy of staged tariff reductions in oligopolistic industries whose longer term economic performance has been unsatisfactory is an empirical question. Policymakers should test the idea; the fact that a remedy is limited should not deter the government from using it at all.

6. *Per Se Prohibition of Refusal to Deal*

The policy actions outlined in this alternative have been proposed by Milton Moore.⁴¹⁸ Essentially, Moore proposes to challenge many of the traditional "rights" of business firms. Refusal to deal would be prohibited *per se* as "it is in direct conflict with the consumers' interests, and . . . is a necessary condition for increased efficiency and reduction in the major forms of eco-

⁴¹⁰ Hans B. Thorelli, *The Federal Antitrust Policy* (Stockholm: Norstedt and Soner, 1954) at 72.

⁴¹¹ F. W. Taussig, *Some Aspects of the Tariff Question* (Cambridge: Harvard University Press, 1915).

⁴¹² See Gorecki, *supra*, note 409.

⁴¹³ *Supra*, note 22.

⁴¹⁴ This case is described in V. W. Bladen, *An Introduction to Political Economy* (Toronto: University of Toronto Press, 1941) at 202.

⁴¹⁵ Skeoch and McDonald, *supra*, note 382 at 38.

⁴¹⁶ *Id.* at 35-36.

⁴¹⁷ *Id.* at 36.

⁴¹⁸ *Supra*, note 14 at 130-78.

conomic waste."⁴¹⁹ This rule would apply to sales to both retailers and distributors. Second, Moore would prohibit regional price discrimination *per se*, for "the main hope for inducing a steady pressure upon price levels of any oligopoly lies in the strengthening of the position of the small company, whose only effective competitive strategy consists of under-cutting the prices of its established rivals."⁴²⁰ Third, Moore would impose mandatory f.o.b. pricing "if the product is fairly homogeneous and where freight costs are a substantial proportion of the wholesale price excluding sales taxes—say, 5 percent."⁴²¹ He emphasizes that this rule must be accompanied by the ban on price discrimination to a single class of customers who compete with each other.

Moore's recommendations also apply to forms of economic behaviour other than conscious parallelism. He argues that competition policy actions should be judged by two criteria: the rule of consumers' sovereignty and the rule of fair competition among companies.⁴²² The former specifies that the consumer is entitled to be provided with the goods and services of his choice at the lowest attainable cost, to be offered as much or as little service with a commodity as he wishes to buy and to be accurately informed. The latter holds that no party in the economic process is to have a privileged position, that each person is free to engage in the business of his choice, subject to the efficient operation of the price system, and that competitive advantages should rest solely upon superior efficiency.

Like the tariff, Moore's proposals do not constitute a complete remedy to the problem of closely coordinated oligopoly without collusion. Used in conjunction with the first, second or fifth alternative, however, they offer a potentially useful, if limited, remedy.

7. Conclusion

In 1960, appearing before the House of Commons Standing Committee on Banking and Commerce in regard to proposed amendments to the *Com-bines Investigation Act*, Professor Skeoch made the following statement:

. . . in the United States they have had cases in which they tried to condemn what they call conscious parallelism of action . . . They have not really enjoyed much success. I am always a believer that there is a good deal of competition, as long as you do not overtly try to eliminate it. You cannot force businessmen, as one Swedish industrialist said in an article, to tear at one another's throats like wolves—and I do not think you have to. But price leadership practice, the whole range of these intermediate problems, the oligopoly behavior—that is what we call it technically—this conscious parallelism, as the Americans have it . . . are, I think, on the borderline of anti-trust. We have plenty of other problems to keep us busy, I think for quite a long while before we turn our attention to that.⁴²³

Time has, however, exacerbated the problem of conscious parallelism in Canada. It should now be near the top of our competition policy agenda. Of

⁴¹⁹ *Id.* at 143.

⁴²⁰ *Id.* at 155.

⁴²¹ *Id.* at 167.

⁴²² *Id.* at 68-75, 127.

⁴²³ Can. H. of C. Standing Committee on Banking and Commerce, *Proceedings*, No. 7 (June 30, 1960) at 461.

the six alternatives discussed, the most effective appears to be that of adopting new civil legislation, which would condemn persistent conscious parallelism accompanied by one or more conduct or performance "plus factors." Next best would be the enactment of section 31.73, as proposed by Bill C-13. If this was accompanied by the use of tariff reductions in appropriate cases and the adoption of Moore's proposals, valuable improvements might be made.

Regrettably, a public policy attack on the plus factors necessarily implies that policy actions will be aimed mainly at business conduct rather than at the structural causes of the ability of firms to closely coordinate their behaviour. The mutual dependence of firms in an oligopoly is unavoidable. Our policy actions must be aimed at reducing their ability to act on the recognition of their interdependence to the detriment of the public interest.