Submission on

Draft Abuse of Dominance Guidelines

NATIONAL COMPETITION LAW SECTION
CANADIAN BAR ASSOCIATION

May 2002

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PREFACE

The Canadian Bar Association is a national association representing over 36,000 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the National Competition Law Section of the Canadian Bar Association, with assistance from the Legislation and Law Reform Directorate at the National Office. The submission has been reviewed by the Legislation and Law Reform Committee and approved as a public statement by the National Competition Law Section of the Canadian Bar Association.

Submission on
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I. INTRODUCTION

The National Competition Law Section of the Canadian Bar Association (the "Section") is pleased to have the opportunity to comment on the Competition Bureau's draft Abuse of Dominance Guidelines (the "Guidelines"). The Section strongly supports the Competition Bureau's public education program, including guidelines, bulletins and other interpretative aids made widely available to the business community in Canada.

Overall, the Section agrees with many of positions outlined in the Guidelines and compliments the Bureau's efforts. In this submission, we focus on those aspects of the Guidelines which may be improved. We trust that a revised draft will incorporate these comments.

II. THE GUIDELINES' EXECUTIVE SUMMARY

In this Part, we touch on a number of broad themes, which will be amplified in the detailed commentary in Part III. This Part follows the headings in the executive summary.

A. What Constitutes "Abuse of a Dominant Position"?

The second paragraph states that an ability to raise prices or maintain high prices is strongly indicative of the existence of dominance or market power. [1] The ability to accurately determine when prices are supra-competitive is an extremely difficult task. Indeed, it is an economic challenge of the highest order. While in theory the existence of supra-competitive prices may be indicative of the existence of dominance or market power, in practice it is not.

We encourage the Bureau to replace the words "is strongly" with the words "may be", as there are other reasons why business have the ability to raise prices or maintain supra-competitive prices.

B. How the Bureau Establishes Dominance

The first paragraph defines a product market, focusing purely on the demand side of the equation. In certain marketplaces, that may be the right focus. However, in others, supply-side substitution may be the key factor. In those markets, supply-side substitution may completely undermine what would otherwise be significant market power. The Guidelines should reflect the potential importance of this factor.

In the second paragraph, the Guidelines seem to regard "recent entry or exit" and "barriers to entry" as separate *indicia*. In fact, "entry or exit" would be evidence of whether there are barriers to entry, not a separate factor. [2]

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1 When the Guidelines speak of "high prices", we presume that means supra-competitive price - that is, prices which are beyond those which would otherwise result from a competitive process. Absolute price levels in and of themselves are of no relevance.

2 See discussion of paragraph 33, below.

In the fourth paragraph, the draft Guidelines refer to market share indicators as "generally giving rise" to or being "*prima facie*" evidence of dominance. In our view, pure market share quantitative information cannot usefully serve this function.[3]

The fifth paragraph refers to joint dominance, and outlines five specific considerations which the Bureau will review. We comment on the appropriateness and applicability of these specific *indicia* in our detailed discussion of paragraph 49. These *indicia* apply as much to a single firm as to a joint dominance case.

C. Anti-competitive Acts

The first paragraph indicates that a practice can constitute one act that is sustained. We address the concept of anti-competitive acts, including this concept of a single act which is sustained, in our discussion of paragraph 53. In our view, a single event cannot constitute a practice of anti-competitive acts. The sixth paragraph under this heading deals with the question of efficiency trade-offs.[4] It is unclear why conduct which is obviously efficiency enhancing always needs to be referred to the Competition Tribunal. If it is apparent on its face that the conduct is efficiency enhancing, a Tribunal application should not be necessary.[5]

To characterize conduct as efficiency enhancing may be another way of saying that there are legitimate business justifications for such conduct. Insofar as there are such justifications, it may be difficult to show that the conduct constitutes a practice of anti-competitive acts.

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3 This point is discussed in more detail with respect to paragraphs 37 to 39, below.

4 We deal with this in greater detail in our discussion of paragraph 56, below.

5 The Section holds the same view with respect to mergers.

Finally, and most significantly, the Guidelines should state coherently the Bureau's view of what is encompassed by "legitimate business justifications". Further, they should specify the types of conduct which cannot in any reasonable circumstance be considered to constitute anti-competitive acts. Certain conduct may have the effect of eliminating competitors from the marketplace but can never constitute "anti-competitive acts". These include, for instance, low prices not at the predatory level; low prices which simply meet a competitor's offering; responding to specific customer requests; and product quality enhancements. Such conduct must always be found to be legitimate competition on the merits regardless of the size of the competitor or the competitive result.

D. Test of Substantial Lessening or Prevention of Competition

The first paragraph states that a finding of a substantial lessening or prevention of competition is likely to follow findings of dominance and of a "practice of anti-competitive acts". As a practical matter, that statement may be true in some cases. Nevertheless, the statutory provision contains three tests, all of which must be met for a finding of abuse of dominant market position. The Section is concerned that the approach in the Guidelines effectively reads out one of these – the substantial lessening of competition – which is arguably the key requirement. We agree with the statement in the Guidelines that this requirement is important for keeping the focus on competition rather than competitors. However, it would be more useful for the Guidelines to indicate what matters the Bureau will typically review to determine whether there is a substantial prevention or lessening of competition.

In particular, reduction in the number of competitors ought not to be of any particular persuasive weight. To give meaning to this statutory test, the focus should be on the question of injury to customer or consumer interests.

III. COMMENTS ON THE BODY OF THE GUIDELINES

In this Part, we discuss only the paragraphs which cause us concern.

A. Purpose of the Abuse of Dominance Provisions

Paragraph 7

We encourage the Bureau to delete the expression "level playing field" from this paragraph. It is an ambiguous and frequently meaningless expression. Where the phrase is first used, the amended sentence would read: "The objective of the abuse of dominance provisions is to create a market framework within which all firms have an opportunity to either succeed or fail on the basis of their ability to compete." The next sentence would then read: "Providing such a framework, however, does not mean establishing…" We believe that the expression "tilt the playing field" may be appropriately left in this paragraph. The final sentence of the paragraph should be amended to add "...or penalize those market participants who succeed based on offering superior products, prices, or other consumer or customer benefits, resulting in superior competitive performance on the merits".

Paragraph 9

We believe that the term "marketing practices" in this paragraph may suggest that virtually any marketing practice may be found to be anti-competitive if undertaken by a large firm. We do not believe that this is the intent. The appropriate approach is to use the statutory words "anti-competitive acts". Some acts might be completely innocuous when undertaken by one firm, yet be the basis for an application when undertaken by others. However, no matter the nature of the firm, the conduct must constitute a practice of anti-competitive acts.

B. Examination/Inquiry Process

Paragraph 15

This paragraph points out that allegations of abuse can be examined under various criminal provisions of the *Act* as an alternative to an abuse application. While that is true, the Guidelines should articulate, as much as possible, when conduct is more likely to fall under the abuse provisions, and when it is more likely to attract attack under the criminal provisions. This is the very criticism leveled at the Strategic Alliance Guidelines.

C. Product Market Definition

Paragraph 27

This paragraph notes, firstly, that evidence of price increases is "not the only quantitative indicator used to define product markets". To say they are not the *only* quantitative indicator suggests that they are the typical and usual indicator. In practice, however, the qualitative factors must typically be used, because they are the best evidence available. In our experience, it is rarely if ever possible to apply the "five percent price increase" test as a practical matter.

In footnote 16, the Bureau states: "There are a variety of quantitative techniques available, including price correlation analysis, price elasticity analysis and diversion ratio analysis" to help to define product markets. Perhaps more accurately, they address market power without necessarily defining product markets. The Bureau should articulate examples of its use of these methodologies, the circumstances in which it is inclined to use them and their perceived strengths and weaknesses.[6] Discussion of these methodologies would be very valuable.

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[6] See Lilla Csoro and Margaret Sanderson, "Differentiated Product Mergers: Recent Experience in Canada and the United States", in *Canadian Bar Association Annual Fall Conference on Competition Law 1998* (Ottawa: Juris Publishing, 1999) pp.133-159.

The third bullet point in paragraph 27 notes that functional interchangeability is generally a necessary but not sufficient condition for two products being in the same relevant market. When looking at the demand (rather than the supply) side, it is not clear why functional interchangeability to some degree is not *always* rather than *generally* a necessary condition. Because of supply-side substitution, producers may find themselves in the same market even though there is no functional interchangeability as between their current production. However, on the demand side, such interchangeability would appear to be always necessary for products to be in the same market.

Similarly, the sixth bullet point in this paragraph states: "The absence of a strong correlation in price movements between two products over a significant period of time *generally* suggests that the products are not in the same relevant market".[7] Again, it is difficult for us to imagine how a person could credibly advance an argument that products are in the same market without some reasonably strong correlation in price movements.

The fifth bullet point deals with switching costs. It notes the relevance of considering the extent to which buyers would have to incur costs to obtain supply from an alternate supplier. However that situation already occurs between the two products of the merging parties, to the same or comparable degree that it applies between the products of the merging parties and other suppliers of arguably comparable products. To that extent, these switching costs may not be particularly relevant in determining whether the merger gives rise to substantive competition law concerns.

D. Geographic Market Definition

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7 Emphasis added.

Paragraph 29

Paragraph 29 notes that some of the quantitative techniques for product market definition can be used for geographic market definition. As with product market definition, the Guidelines should elaborate the quantitative techniques used by the Bureau, the way in which they tend to be used and the situations most suitable for their use.

The third bullet point of paragraph 29 refers to switching costs. We repeat our comment under paragraph 27, that those costs may be less significant if they existed between the products of the merging parties in any case. Further, it is difficult to envision the types of switching costs which might exist for products from a different geographic region, as opposed to products which may differ in some physical detail. The Guidelines should illustrate the types of costs that the Bureau has in mind.

E. Cellophane Fallacy

Paragraph 30

In dealing with the cellophane fallacy the Bureau notes that it will work on the assumption that dominance exists. We suggest that the appropriate wording is that the Bureau will work on the assumption that dominance *may* exist. This does not alter the substantive analysis, but the current wording may send the wrong message to the business community that the Bureau presumes that an allegation of abuse of dominance is well-founded.

F. Market Power

Paragraph 31

This paragraph indicates that the Bureau will estimate what the approximate price levels for the product would have been in the absence of market power. This estimate is theoretically attractive, but is almost impossible at a practical level. This paragraph should therefore indicate that the Bureau will approach such an estimate as a theoretical model. The Bureau should also state the basis and evidence upon which such estimates are made.

Paragraph 33

In this paragraph the Bureau lists the *indicia* of market power, including barriers to entry and "recent entry or exit". In fact, recent entry or exit is simply evidence of whether there are barriers to entry. It should not be listed as a separate indicator.

Paragraph 35

This paragraph suggests that in determining market power, the Bureau will consider the extent to which existing or potential competitors are likely to constrain any exercise of market power. It would be more correct to note that the market power analysis will consider the extent to which existing competitors, potential competitors *or other relevant factors* (such as, for example, countervailing customer power) are likely to constrain any exercise of market power.

Paragraph 37

This paragraph uses the term "near-monopoly" as a synonym for high market share. The term "monopoly" implies more than a mere numeric market share analysis. It involves an assessment of monopoly power, which may not exist even with a high market share. We believe that the Guidelines should avoid use of the terms "monopoly" or "near-monopoly" when referring simply to market share.

This paragraph refers to the *Laidlaw* and *Tele-Direct* cases, but appears at least partially to misstate the judgements in those cases. For instance, the reference to *Tele-Direct*

blends two statements found on separate pages of the judgement. The Guidelines suggest that these statements may be generalized, however we would argue that they are limited to the specific marketplace facts in that case. The Guidelines should be careful not to generalize the case-specific findings in *Tele-Direct* or in any other case. Indeed they correctly point out that *Laidlaw*'s finding that a market share below 50 percent did not lead to a finding of dominance should not generalized.

Paragraph 38

If an allegation of abuse of dominance has been made against a firm that has more than 35 percent market share, then, according to this paragraph, "the Bureau would normally continue its investigation".

We assume this is intended to indicate that if a firm has less than a 35 percent market share the Bureau will typically discontinue an investigation. If a firm has more than a 35 percent market share, however, the Bureau should take a "quick look" at the other relevant requirements of the abuse of dominance provision. If they appear not to be present, the investigation should not continue. We presume this is the Bureau's current practice. To state that the Bureau will normally continue its investigation whenever there is more than a 35 percent market share may be misleading. Presumably the Bureau's decision will depend upon the other relevant issues.

Paragraph 39

It is unwise, and indeed inaccurate, to state that any given market share constitutes *prima facie* evidence of dominance. The question can never be divorced from other marketplace factors. Section 92(2) of the *Act* indicates that any such approach is contrary to the required analysis of whether there has been substantial prevention or lessening of competition in the marketplace. Even if a *prima facie* market share threshold could be established in the case of single firm conduct, it would not be possible to

translate that into the 60-65 percent market share threshold for multi-firm conduct under joint dominance. In dealing with joint dominance, the extent of collaboration between the parties falls on a spectrum. At the one end is a lack of collaboration virtually equivalent to a single firm. At the other, there is a level of collaboration which could be described as conscious parallelism plus, with no agreement whatsoever. It is illogical to contemplate that in that broad range of cooperation a single market share could ever constitute *prima facie* evidence of anything.

Paragraph 41

We repeat our comments under paragraph 39.

Paragraph 42

This paragraph again uses the word "monopoly" as a statement of high market share. We repeat our comments under paragraph 37.

Paragraph 43

In this paragraph, the Bureau characterizes the comments in *Tele-Direct* as imposing a burden of proof on the Respondent. We acknowledge that, as a practical matter, prudent respondents seek to adduce evidence of "extenuating circumstances and, in general, ease of entry". However, the case does not speak of a shift in the burden of proof. Throughout the proceeding, the burden of proof remains on the applicant.

Paragraph 44

This paragraph addresses evidence concerning barriers to entry. In addition to reciting some of the findings in the cases, the Bureau should indicate the types of evidence it finds relevant and useful on this issue.

G. Joint Dominance

Paragraph 47

The Guidelines state: "the economics literature indicates that there is little distinction between explicit and implicit agreements, except for the case where the former can be enforced through the courts". This statement leaves important questions unanswered, particularly given that the term "implicit agreements" has been used to define a spectrum of conduct from pure conscious parallelism, with no additional "plus" factors, to conduct where there is no direct evidence of an agreement which is believed to exist. The term "implicit agreement" needs to be carefully defined and cannot be limited to conscious parallelism. The definition should clarify the additional factors necessary for there to be an implicit agreement.

Further, the Guidelines provide no references for the above proposition. If it reflects the Bureau's view, then it should be substantiated by appropriate reference to authority.

Paragraph 48

Again, it is critical that the Bureau articulate the factors which might attract a finding of joint abuse by firms acting in some form of coordinated way. This must be more than mere conscious parallelism.

Paragraph 49

In item (b) of paragraph 49 there appear to be words missing. Perhaps the word "likely" should be inserted between the words "is" and the word "to".

Paragraphs 49(b) (if the word "coordinated" were deleted) and 49(e) add little to the analysis of joint dominance because they could apply to any abuse case. Paragraph 49(b) does not address the question of whether there is the appropriate degree of group

conduct to permit a finding of joint abuse, but instead deals with whether there are anti-competitive acts. Similarly, paragraph 49(e) addresses whether there is market power, not whether there is sufficient coordination for there to be a finding of joint conduct. These paragraphs apply as much to a single firm as to a joint dominance case.

H. Practice

Paragraph 53

The discussion of a single occurrence "practice" should be expanded. What is a "systemic" act? What factors does the Bureau take into account to determine whether an act is "isolated" or "sustained and systemic"? Does this paragraph apply to acts other than contracts, having a continued existence over time such that they might be viewed as an ongoing series of anti-competitive acts?

We have difficulty with the proposition that a single act "that has had a lasting impact on competition", but presumably has never been repeated, could itself constitute a "practice of anti-competitive acts". This proposition does not accord with the language of the statute or existing jurisprudence. As a matter of law, a single, non-recurring event cannot constitute a practice of anti-competitive acts, regardless of the effects of that event.

I. Anti-competitive Acts

Paragraph 55

United States courts have recognized the danger associated with relying on subjective intent. They only use subjective intent to determine the effects of the defendant's actions. The reality is that virtually all businesses want to crush their rivals. Marketing documents in particular are often replete with martial language indicating a desire to crush or dominate the competition. These documents should have no probative value in determining anti-competitive intent. Subjective intent should rarely if ever be used by itself

to support a conclusion on the purpose or intent of an act. Rather, the focus should be on the effects of the impugned actions.

Paragraph 56

In footnote 28, the Guidelines deal with facilitating practices. They indicate that the Bureau is prepared to weigh claims of pro-competitive and anti-competitive purpose and/or effect to determine whether these practices are evidence of joint control. We find it difficult to understand, therefore, why the Bureau is not prepared to do a similar weighing in determining whether an impugned practice is anti-competitive. We strongly believe that the Bureau should evaluate the pro-competitive consequences of all impugned acts. It should not proceed to the Tribunal if, on balance, the acts are not anti-competitive. Tribunal cases are too expensive and disruptive for the Bureau to commence proceedings if it does not believe there is a strong case.

J. Economics of Anti-competitive Acts

Paragraph 62

In this paragraph, the Guidelines refer to the *NutraSweet* decision and note that anti-competitive acts must be predatory, exclusionary or disciplinary. The paragraph then refers to activities which raise rivals' costs, are predatory, or facilitate coordinated behaviour among firms. It is unclear how facilitating coordinated behaviour could be said to be predatory, exclusionary or disciplinary. In the case of joint dominance, these practices may support a determination that there is joint dominance. In a case involving single firm conduct, acts intended to facilitate market transparency arguably will assist a dominant firm in responding to rivals. However, conduct which facilitates coordinated behaviour between rivals cannot be said to be predatory, exclusionary or disciplinary. Indeed, such conduct was found not to be anti-competitive act in *NutraSweet*.

K. Raising Rivals' Costs and Market Foreclosure

Paragraph 66

This paragraph deals with vertical mergers, identifying a number of hypothetical examples which could satisfy the statutory language. This discussion contrasts sharply, however, with the discussion of vertical mergers in the Merger Enforcement Guidelines (MEGs). These state that vertical mergers are rarely anti-competitive and outline the limited scenarios in which there may be an anti-competitive result. The Guidelines should follow the MEGs approach to vertical mergers. Indeed, Appendix III of the Guidelines does follow the MEGs when dealing with vertical price squeezes.

Paragraph 71

This paragraph sets out the Bureau's views on what has been referred to in the United States as the essential facilities doctrine. In *Interac*, the one Tribunal case which dealt most directly with this concept, the Bureau was at pains to avoid reference to that doctrine. Nevertheless, in recent amendments the reluctance to refer expressly to the concept of essential facilities seems to have been overcome.[8] We do not understand, therefore, why paragraph 71 does not refer expressly to the essential facilities doctrine.

The Guidelines also distinguish between regulated and unregulated industries (or recently deregulated industries). Recently deregulated industries were thought to be natural monopolies, but are now moving to a competitive framework due to changing economic or technical circumstances. Essential facilities issues may arise more frequently in these industries. However, this simply reflects the fact that they are industries in which regulation previously existed and in which there are facilities controlled by one or more dominant participants. The Section is not aware of any particular reason for treating a

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8 See section 78(l)(k) of the *Act*, and recently released regulations respecting anti-competitive acts of persons operating a domestic service (section 2(l)).

regulated industry differently in an essential facilities analysis. The structure of an industry may have previously attracted regulation and may now attract marketplace circumstances in which the application of essential facilities antitrust doctrine is relevant.

Paragraph 74

This paragraph discusses "abuse of judicial process" as an anti-competitive act. While the Tribunal made such a finding in *Laidlaw*, the Section is concerned about its apparent endorsement in the Guidelines. Is it the Bureau's view that a dominant firm commits an anti-competitive act if it strictly insists on its valid legal rights? Can such an anti-competitive act exist independently of anti-competitive contractual provisions? If so, what would be the remedy? Could the Tribunal ever prohibit general access to Canadian courts where the dominant firm has valid legal claims? It is noteworthy that the Tribunal in *Laidlaw* did not order a remedy for abuse of the judicial process.

L. Predatory Conduct

Paragraph 78

This paragraph discusses the first stage of the Bureau's consideration of alleged predatory pricing. There are areas of ambiguity in this discussion, however, that should be clarified. First, the paragraph indicates that the Bureau will examine whether the dominant firm will be able to recoup the costs of the lower prices either in the market where prices had been lowered or "in other markets". This seems to suggest a cross-subsidization theory in which the "profits" from one market are used to "subsidize" another market. How does recoupment occur in the "high priced" markets?

Second, the term "predation" in the final sentence of the paragraph is unclear. Is "predation" synonymous with "low pricing", or does it mean "pricing below cost"? If it

means the former, this is exactly the argument that the Tribunal explicitly rejected in *Tele-Direct*. The paragraph should be clarified to reflect the *Tele-Direct* case.

Paragraph 79

This paragraph deals with the second stage of the Bureau's approach to alleged predatory pricing – a consideration of whether the dominant firm is pricing at some measure below costs. Without drawing much attention to the fact, the Bureau appears to be introducing a new measure of costs into the price-cost equation – namely, "avoidable" costs. This change is noteworthy for a number of reasons.

First, an established body of cases and legal literature exists in both Canada and the U.S. dealing with the price-cost relationship. The generally accepted view is that average variable cost is usually the appropriate proxy for marginal costs. Indeed, the Commissioner's own Predatory Pricing Guidelines adopt this approach.

Second, the change lacks detail. What is an "avoidable" cost? How does a party determine which costs are avoidable? The Guidelines should expand the discussion of "avoidable" costs, particularly as it is a departure from past approaches.

Finally, the Guidelines do not say why a new approach is necessary or how the new approach differs from the old. Moreover, the Guidelines do not say whether this new approach will also be applied to predatory pricing under subsection 50(1)(c). Significant changes in interpretation of important provisions in the *Act* should be fully detailed and debated before they are adopted.

M. Facilitating Practices

Paragraph 83 and 84

Paragraphs 83 and 84 deal with "facilitating practices". This discussion appears to be purely theoretical, as the paragraphs contain no statutory or case support. Cited examples of these practices include pre-announced price increases, published price lists, delivered pricing and basing-point pricing. According to these paragraphs, each of these practices increases transparency to other firms. At the same time, we note that each of these practices increases transparency to consumers. The Guidelines should clarify the circumstances in which the Bureau believes that facilitating practices are no longer benign.

N. Limitations and Exceptions

Paragraph 94

Paragraph 94 purports to deal with subsection 79(5). However, it provides no guidance on the interface between section 79 and the exercise of intellectual property rights. This absence is particularly disconcerting given that *Tele-Direct* dealt with this issue at length. We believe that there should be a more detailed discussion.

Paragraph 96

Paragraph 96 purports to deal with subsection 79(7). However, it simply paraphrases the statutory language and does not give any guidance on how the Bureau would determine whether to proceed under sections 45, 79 or 92. Such guidance would assist the business community and the practising bar.

O. Appendices

Appendix IV

Appendix IV attempts to summarize the six abuse of dominance decisions rendered by the Tribunal. Almost all of these decisions are long, detailed and complex. They virtually

defy a concise synopsis. Without going into detail, the summaries contained in this appendix are so brief that they fail to present an accurate legal summary of the cases. It would be more valuable to cite the published reports of the cases, which contains a headnotes summarizing the case. In addition, the Appendix should refer to relevant Tribunal decisions concerning other provisions of the *Act*. For example, the Tribunal's decisions on the merger provisions (e.g., *Southam, Hillsdown* and *Superior Propane*) are instructive on the subjects of market definition, market power and the substantial lessening or prevention of competition.

IV. SUMMARY AND CONCLUSION

The Section commends the Bureau for producing useful guidance on the Bureau's approach to the *Act*. While we have been critical of some of the Guidelines, we broadly support the effort to create them. The Section agrees with most of the detail and content of the Guidelines. For this reason, we have been able to provide more detailed comment on the specifics, which we think may be improved by a subsequent draft. We look forward to any further opportunity for input.