Submission on Draft Guidelines on Unreasonably Low Pricing

NATIONAL COMPETITION LAW SECTION
CANADIAN BAR ASSOCIATION

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PREFACE

The Canadian Bar Association is a national association representing over 37,000 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 by the Executive Officers as a public statement by the National Competition Law Section of the Canadian Bar Association.

Submission on Draft Guidelines on Unreasonably Low Pricing

I. INTRODUCTION

The National Competition Law Section of the Canadian Bar Association (the Section) welcomes the opportunity to comment on the *Draft Enforcement Guidelines for Illegal Trade Practices: Unreasonably Low Pricing Policies under Paragraphs 50(1)(b) and (c) of the Competition Act* (the Guidelines) issued by the Competition Bureau. The Section strongly supports the Bureau's continuing efforts to clarify its enforcement policy by publishing enforcement guidelines, information bulletins, press releases and other interpretative aids to the business community in Canada.

The Section agrees with the Bureau's assessment that the 1992 Predatory Pricing Guidelines (the 1992 Guidelines) need revision. However, we question the appropriateness of the Bureau's timeline for such a revision in light of the pending *Air Canada* case before the Competition Tribunal and the recommendation of the House of Commons Standing Committee on Industry, Science and Technology that the predatory pricing provisions be repealed and dealt with as civil abuses of dominant position.

The Section is very concerned about the Bureau's recommendation to eliminate recoupment as an essential prerequisite to find that a firm has engaged in predatory conduct. We are not aware of any change in the law that would be a basis for this significant change in enforcement policy.

II. TIMING CONCERNS

We recognize that the Bureau's enforcement policies and interpretation of the *Competition Act* will change in response to developments in economic theory, market conditions, judicial pronouncements and legislative amendments. The utility of the Bureau's enforcement guidelines depends crucially on ensuring that they are regularly reviewed and updated to keep pace with such developments. As a result, we agree that it is appropriate to revise the 1992 Guidelines. However, we note that the Competition Tribunal's decision in the pending *Air Canada* case may have a significant impact on the interpretation and enforcement of the predatory pricing provisions – particularly as they may relate to the acceptance and clarification of an avoidable cost test.

Accordingly, in the Section's view, the Bureau should wait for the Competition Tribunal's decision in the *Air Canada* case prior to issuing the Guidelines in final form. That way, the Guidelines could reflect the Competition Tribunal's decision. Moreover, since the Guidelines were released, the House of Commons Standing Committee on Industry, Science and Technology has recommended that the criminal predatory pricing provisions be repealed and dealt with as civil abuses of dominant position. We believe that the Bureau should wait to see whether a consensus develops on eliminating or retaining the predatory pricing provision in its current form prior to issuing new guidelines on the enforcement of such a provision.

III. THREE PRINCIPAL CHANGES FROM THE 1992 GUIDELINES

The Guidelines reflect the following three principal changes to the Bureau's approach concerning allegations of unreasonably low pricing. First, the ability to recoup losses would no longer be considered the primary screening criterion. Second, in carrying out the cost-revenue analysis to determine whether a price is unreasonably low, the Bureau would use an "avoidable cost" standard as opposed to an "average variable cost" or "average total cost" standard. Third, the

Guidelines would include a new section dealing specifically with unreasonably low pricing resulting from market expansion.

The Section welcomes the statement that deals specifically with the application of the predatory pricing provisions where a new entrant into a market engages in low pricing. However, the Section is opposed to the Bureau's position that recoupment be eliminated as a pre-requisite to establish a violation under paragraphs 50(1)(b) and (c) of the *Act*. Further, it is difficult for the Section to comment meaningfully on the Bureau's recommendation to adopt the avoidable cost standard – as opposed to average variable cost – in the cost revenue analysis used to determine below-cost price selling. This is because the Guidelines provide very little guidance on the meaning of avoidable costs. The Section's concerns with these two principal changes from the 1992 Guidelines are discussed below.

A. Recoupment is an Essential Element of Predation

The essence of the economic theory of predatory pricing is best illustrated by the example of a dominant firm setting its prices so low over a sufficient period of time that the firm may drive one or more of its competitors from the market or deter other companies from entering the market. Once competitors exit the market or are successfully deterred from entering (thereby creating a less competitive market), the predator would be expected to raise prices significantly in an attempt to recover the costs incurred (i.e. losses or foregone profits) during the period of predation.

The economic literature provides a number of specific theories of predatory pricing by a dominant firm, demonstrating that in theory the practice can be rational. The theory of financial market predation, for example, provides a foundation for the argument that established firms have greater internal capital and access to capital markets than do potential "prey" and can therefore last out a

(below-cost) price war.[1] In such a situation, a dominant firm might price below cost to eliminate its rival through the depletion of internal capital, and then raise prices to monopoly levels.[2]

From a policy perspective, it is important to recognize that there may be instances where firms are removed from the market, or are prevented from entering, but where consumer prices remain the same or decline. Thus, while the interests of consumers and competitors may coincide in certain circumstances, it is not sufficient to state that consumers will necessarily be harmed simply because some firms are eliminated and the market thereby becomes more concentrated. The Bureau has therefore indicated that its enforcement approach will focus on the impact on competition when examining predation complaints.

In keeping with economic principles, the 1992 Guidelines indicated that predatory pricing would only be considered harmful if the preying firm raised or was expected to raise prices significantly to recover its losses or foregone profits after its low prices had caused a competitor to exit or had deterred the entry of new competitors. Accordingly, the Bureau would not take enforcement action against a low-pricing firm unless the firm had market power (i.e., the ability to maintain prices above competitive levels for a significant period of time).

While an ability to recoup losses will continue to be a factor to be considered, the Guidelines indicate that it is not a precondition to establish the offence of predation under the *Act*. This represents a fundamental change to the

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[1] Patrick Bolton and David Scharfstein, "A Theory of Predation Based on Agency Problems in Financial Contracting" (1990) 80 *American Economic Review* 93.

[2] In signaling theories of predation, a better-informed predator sells at low price to mislead its rival into believing that market conditions are unfavourable. For example, in cost-signaling models, a predator drastically reduces price to induce beliefs on the part of the prey that the predator has lower costs, when in fact the predator has no cost advantage. (Januscz A. Ordover and Garth Saloner, "Predation, Monopolization and Antitrust," in *Handbook of Industrial Organization* (Richard Schmalensee and Robert Willig, eds.) (New York: Elsevier Science Publishing, 1989) at 537. The beliefs of lower cost discourage entry or induce exit on the part of the prey.

interpretation and enforcement of Canada's criminal predatory pricing law for which there is no basis in the jurisprudence. The Section is strongly opposed to the Bureau's interpretation. It is also inconsistent with established economics – predatory pricing would result in a substantial lessening of competition only if there were some reasonable prospect for recoupment. Thus, recoupment is a necessary condition for determining that predatory actions are having the effect of or tending to substantially lessen competition.

In dealing with the meaning and significance of the recoupment concept, the language of the Guidelines is confusing. Recoupment may not be a necessary condition if the enforcement approach is geared to preventing pricing activity that is having the effect of or tending to *eliminate a competitor*. However, recoupment clearly is required if the enforcement approach is geared to preventing pricing activity that is having the effect of or tending to *substantially lessen competition*. As the Guidelines indicate that the Bureau's enforcement objective is to safeguard competition, then recoupment plays a larger role in the analysis than simply being another factor for consideration.

An example of this confusion is found at paragraph 64 where the Bureau articulates its rationale for abandoning recoupment as a primary screening criterion as follows:

> Low-pricing behaviour can also be motivated by reasons other than recoupment. For example, it may be rational for a firm to adopt a low-pricing policy and sacrifice present profits in order to preserve the long-term stability of an existing market structure. Additionally, a low-pricing policy could assist in establishing an industry standard to exclude others or maintain market control.[3]

The examples described above are in fact examples of recoupment. Preserving the long-term stability of an existing market structure presumably means preserving prices that are above competitive levels, thereby recouping the costs involved during the period of low pricing. Similarly, if the firm maintains market

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[3] Footnotes excluded.

control, this again indicates that it has achieved market power and has set prices above competitive levels – again allowing the firm to recoup any forgone revenues or losses incurred during the low-pricing period.

By providing such an explanation for why recoupment may not be necessary, the Guidelines appear to be adopting a narrow definition of recoupment. Recoupment should be defined in the Guidelines as the ability to recover forgone revenue or losses incurred during the low pricing period. This requires the alleged predator to have market power in the period when recoupment is occurring.

To the extent that the Bureau is actually abandoning recoupment as a necessary element of criminal predation, the approach contradicts economic evidence relating to predation and is in stark contrast to the United States law on predation. In the Section's view, abandonment of recoupment as an essential element of establishing the offence of predation will criminalize legitimate aggressive pricing behaviour and competitive rivalry to the detriment of consumers and the Canadian economy. It is simply not rational for a firm to engage in below-cost pricing unless the firm has a reasonable expectation of recouping its investment in below-cost prices. This concept was succinctly stated by the United States Supreme Court in *Brooke Group LDT v. Brown & Williamson Tobacco Corp.*:

> For the investment to be rational, the [predator] must have a reasonable expectation of recovering, in the form of later monopoly profits, more than the losses suffered." *Matsushita supra, at 588-589.* Recoupment is the ultimate object of an unlawful predatory pricing scheme. It is the means by which a predator profits from predation. Without it, predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced. Although unsuccessful predatory pricing may encourage some inefficient substitution towards the product being sold at less than its cost, unsuccessful predation is in general a boon to consumers.

> That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured: it is axiomatic that the antitrust laws were passed "for the protection of competition, not competitors".…Even an act of pure malice by one business competitor against another does not, without more, state a claim under the federal antitrust laws;…
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> For recoupment to occur, below-cost pricing must be capable, as a threshold matter, of producing the intended effects on the firm's rivals, whether driving them from the market, or as was alleged to be the goal here, causing them to raise their prices to supracompetitive levels within a disciplined oligopoly. This requires an understanding of the extent and duration of the alleged predation, the relative financial strength of the predator and its intended victim, and their respective incentives and will… The inquiry is whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb. If circumstances indicate that below-cost pricing could likely produce its intended effect on the target, there is still the further question whether it would likely enter competition in the relevant market. The plaintiff must demonstrate that there is a likelihood that the predatory scheme alleged would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation, included the time value of money invested into it. As we have observed on a prior occasion, "in order to recoup their losses, [predators] must obtain enough market power to set higher than competitive prices, and then must sustain those prices long enough to earn in excess profits what they earlier gave up in below-cost prices". *Matsushita 475 U.S. at 590-591.*[4]

For the reasons discussed above, recoupment is critical to the success of any predatory pricing endeavour. The failure to prove recoupment is fatal to a predatory pricing claim.

The significance of recoupment to a predatory pricing claim was recently commented on by William Kolasky, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice as follows:

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[4] 509 U.S. 209 at 224 (1993).

> We view recoupment as an essential element of the test because, as the Supreme Court has said, "cutting prices in order to increase business often is the very essence of competition". There are many legitimate, procompetitive reasons for charging prices that are below cost, and there is no rational reason to deny consumers the benefits of lower prices in the absence of any realistic prospect for recouping short-term losses through later supracompetitive pricing.[5]

B. Clarification of the Avoidable-Cost Standard is Required

Under the 1992 Guidelines, a price above average total cost would not be considered unreasonably low. A price below average variable cost was likely to be regarded as unreasonably low unless there was a clear justification, such as the need to sell off perishable inventory. The Bureau's conclusion about the reasonableness of a price between average total cost and average variable cost would depend on the circumstances.

It is important that the Bureau's analysis of whether a price is unreasonably low consider "more than just the amounts of the prices or the relationship to costs". However, it is equally important that the Guidelines provide sufficient certainty to avoid deterring vigorous and aggressive price competition.

The Bureau now proposes to use an avoidable cost standard in determining whether a price is unreasonably low. The Guidelines define avoidable costs as "all costs that could have been avoided by a firm had it chosen not to sell the product(s) in question".

Apart from indicating that avoidable costs may differ depending on the time period in question and generally do not include sunk costs (i.e. costs that have already been incurred and could not be recovered in a wind-up of a firm's

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5 William J. Kolasky, Deputy Assistant Attorney General Antitrust Division U.S. Department of Justice, *North Atlantic Competition Policy: Converging Toward What? Speech before the BIICL Second Annual International and Comparative Law Conference London*, England May 17, 2002 [footnotes excluded], available at http://www.usdoj.gov/atr/public/speeches/11153.htm.

operations), there is very little guidance on the meaning of avoidable costs. In contrast, section 2.2.2 of the 1992 Guidelines included specific examples of costs which would be considered variable and the *Draft Enforcement Guidelines on the Abuse of Dominance in the Airline Industry* contained a very detailed discussion of avoidable costs. If the Guidelines are to have an educational impact and be of practical utility, it is critical that the meaning of avoidable costs be clarified and, in particular, that the Guidelines include an explanation of how avoidable costs differ from variable costs. We suggest that predictability is uniquely important here, because pricing decisions typically have to be made quickly and companies should be encouraged to price aggressively and promptly. Relatively objective standards that can be applied upfront are not only essential for business decisions, they also facilitate summary disposition by regulators and adjudicators.

The Bureau indicates at paragraph 75 of the Guidelines that "the time period over which the cost based analysis is carried out and the time period over which the costs of the firm are avoidable may be different". The Section questions this. In our view, costs should only be considered avoidable if they are avoidable over the time period covered by the Bureau's examination.

The Section agrees that in some circumstances common costs incurred in the production of more than one product would not be considered avoidable. However, the Guidelines should clarify whether this would still be the Bureau's position if a firm is not covering the variable costs of producing any of its products. Moreover, the Guidelines give no indication of the complexity and variety of issues that would arise in applying an avoidable cost concept in relation to various production and distribution scenarios. For example, the utility or appropriateness of "avoidable cost" is questionable in manufacturing and distribution scenarios where multiple products are derived from a common raw material. The economic effects of applying the test to this scenario differ in many ways from the effects of the test as applied to a transportation network. As the Guidelines would have general application to all industries and trades, the Bureau

should understand and articulate how the avoidable cost test would apply in all foreseeable situations. The use of multiple examples would be helpful.

IV. GENERAL COMMENTS

The preface to the Guidelines indicates that transparency and certainty of enforcement process is essential in the context of today's fast-paced, global economy. To enhance certainty, the Guidelines should clearly indicate that they will inform and reflect the Bureau's enforcement policy until they are amended following a period of public consultation or unless the court or the Competition Tribunal directs otherwise. Similarly, transparency and certainty would be enhanced if the Bureau refrains from challenging conduct which adheres to the 1992 Guidelines until the new Guidelines are finalized.

As recognized in the introduction to the Guidelines, low pricing is generally not anti-competitive. In fact, it is one of the principal objectives of maintaining competitive markets. While section 50 of the *Act* contains the phrase "unreasonably low pricing", in some cases the Guidelines refer to "low pricing" in a negative way. To avoid any suggestion that "low pricing" is presumptively or likely anti-competitive, this language should be avoided throughout the text.

On page 3, the Guidelines indicate that the courts have concluded that selling prices which are above costs can never be unreasonable. However the Guidelines do not sufficiently emphasize this point. The "avoidable cost" test introduced in the preface is not discussed or referred to in the body of the Guidelines until page 16. In our view, the below-cost test is central to an analysis of predatory or unreasonably low pricing and warrants greater emphasis. Perhaps the phrase "below-cost pricing" could be used instead of "low pricing".

In various places, the Guidelines refer to a practice of strategically low pricing in order to deter entry. In our view, there is nothing improper or unlawful about such a practice. In establishing a price which is expected to maximize its profits, an

incumbent firm is entitled to consider the likely response to that price by actual and potential competitors. Such behaviour is lawful, economically rational and, to the extent it results in lower prices, beneficial to consumers. While an incumbent which reduces its prices below cost in response to a specific threat of entry may be engaged in predation, the Guidelines should not discourage incumbent firms from considering potential entrants in establishing above-cost prices. The key is whether the pricing activity results in competitive harm. Accordingly, all references to "strategic pricing behaviour" should be changed. All pricing decisions are strategic, and strategic pricing behaviour is not *per se* (or even presumptively) unlawful.

V. SPECIFIC COMMENTS

The Section's comments on specific sections of the Guidelines are set out below. For ease of reference, we have assigned paragraph numbers to the text in the body of the Guidelines (see attached Appendix "A") and refer to those paragraph numbers in these comments.

A. Interpretation

The statement that the Guidelines "supersede all previous statements of the Commissioner or other officials of the Bureau" should be narrowed to refer only to statements on the interpretation and enforcement of section 50(1) of the *Act*, including the 1992 Guidelines.

B. Introduction (Part 1)

The Introduction recognizes the benefits of low prices stemming from legitimate competitive rivalry and the difficulty of distinguishing them from low prices resulting from anti-competitive behaviour. This is an important point and should be further emphasized. The Bureau should make it clear that it will err on the side of caution and pursue low pricing investigations only in the clearest of circumstances. Overzealous intervention may discourage the vigorous price

competition which is a hallmark of competitive markets. If firms start to face competitor complaints and detailed information requests from the Bureau every time they cut prices, these firms may be discouraged from reducing prices. This will result in greater price stickiness and increased conscious parallelism (when the unilateral actions of firms coincide without there have been any form of communication among them). Inappropriate intervention in the marketplace by the Bureau may have the unintended and perverse effect of encouraging higher prices and less price volatility.

The Introduction states that "unreasonably low pricing…means involvement in a policy of selling below cost in order to deter entry into a market, or to force competitors out of a market". This is different from the way the illegal trade practices are defined in section 50(1). The Bureau should clarify that it is taking the position that intent is a prerequisite to enforcement activity. The jurisprudence indicates that intent to lessen competition or eliminate a competitor is an essential element of the crime. This results from the meaning that is given to the word "policy" in paragraph 50(1)(c) of the *Act*.

C. Enforcement Considerations (Part 3)

Paragraphs 11 and 12 suggest that the Bureau's low-pricing enforcement activities are complaint driven. The Guidelines should provide some perspective on the extent to which a "low price" complaint is likely to result in a finding that the price is "unreasonably low". It would assist to include updated statistics on the number of complaints received by the Bureau and the number which have resulted in enforcement activity.[6] If the Bureau engages in significant independent monitoring of pricing activity, this should also be described. Information on the factors considered by the Bureau in prioritizing its cases would also be helpful.

[6] This might also help to discourage unmeritorious complaints.

Paragraph 16 indicates that as a "threshold" matter, the Bureau assesses the likelihood that the behaviour "will harm competition, and therefore consumers and businesses". It would certainly be inappropriate to continue an investigation into behaviour that will not likely harm competition. At the same time, it should be noted that not all lessening of competition is unlawful. The prohibition in the *Act* involves substantially lessening competition or eliminating a competitor. Also, the Guidelines should clarify that "consumer harm" must be established and that the term consumer includes business customers.

The safe harbours for firms with market shares of less than 35% and industries with low barriers to entry are relatively clear and will provide some certainty to certain businesses. However, the exception for a firm whose market share is less than 35% but "considerably greater than its rivals" is less clear. The Guidelines should set out what is meant by "considerably greater" (e.g. a 10% gap, double the next highest share) and whether a *de minimis* threshold will be applied (e.g. less than a 10% share). The Bureau should also consider whether there should be a similar four-firm concentration threshold (60% or 65%). In addition, the last sentence states that "the Bureau usually will pursue cases where the low-pricing incumbent firm has a market share of more than 35%". The policy should be stated in the negative – i.e. "the Bureau will generally not pursue cases where the low-pricing incumbent firm has a market share of 35% or less".

The section on "preliminary examination" (paragraph 17) states that the Bureau considers the "duration, frequency, depth and pattern of the low-pricing behaviour". The Bureau should clarify whether price reductions of longer duration, greater frequency and greater magnitude are more or less likely to be considered anti-competitive. Also, it is important for the Bureau to recognize and take into account that it only has information provided by the complainant. This information may not be credible. The Bureau should be cautious and alert to strategic behaviour by complainants which may chill competitive rivalry.

D. Elements of Unreasonably Low Pricing (Part 4)

Part 4 of the Guidelines explains how the Bureau interprets the specific elements that must be proved to establish a violation of paragraphs 50(1)(b) and 50(1)(c) of the *Act*. For the reasons discussed above, the Section strongly disagrees with the change in the Bureau's enforcement approach that recoupment is not a necessary element. In addition, as previously discussed, the Section believes that the meaning of avoidable cost needs to be clarified.

Following are the Section's specific comments on Part 4 of the Guidelines. For ease of reference, we have used the headings and sub-headings used in Part 4 of the Guidelines.

(i) Policy of Selling Products

Paragraph 36 refers to markets "where infrequent large tender calls constitute a significant portion of market transactions". The Guidelines should expressly indicate that in such markets customers are likely to have significant countervailing power and that it is therefore unlikely that a low-pricing policy will have anti-competitive effects. Some jurisdictions, notably Europe, have found "bid markets" to be competitive given countervailing power even though the winning bidder may obtain a 100% market share.

Paragraph 37 seems misplaced and more appropriately related to the section on "effect or tendency of substantially lessening competition". The paragraph states that "the Bureau is of the view that it should not have to wait to take action until an unreasonably low pricing policy has had a noticeably anti-competitive impact". This statement should be amended to clarify that if the policy has not had an anti-competitive "effect", the Bureau will not take action unless the policy has or is likely to have an anti-competitive "tendency" or "design".

(ii) Competitive Impact

The discussion of paragraph 50(1)(b) in paragraph 39 refers to "geographic markets". Although the *Act* refers to selling "in any area of Canada", we believe that the effects of any such policy should be evaluated with reference to relevant geographic antitrust markets. Eliminating a competitor in one "area" of a geographic market will have no impact on competition if there are no barriers to the expansion of competitors in other areas. The Guidelines should clarify that this will be the Bureau's policy.

(iii) Effect or Tendency of Substantially Lessening Competition

Paragraph 44 suggests that the effect of a low-pricing policy will be evaluated based on whether it prevents or lessens competition substantially – i.e. whether it creates, preserves or enhances market power. Paragraph 46 then states that "the ability to engage in conduct which is predatory, exclusionary or disciplinary can itself be a good indication of the presence of market power." It would be circular reasoning to point to a low-pricing policy as evidence of market power and then conclude that because the firm has market power the low-pricing policy must be predatory. Anyone can institute a low-pricing policy. This does not mean it will be profitable or that the person has market power. In other words, conduct can be exclusionary without being an indication of market power. For example, consider the exclusionary nature of franchise arrangements. Such contractual arrangements are indicative of the franchisor's or franchisee's market power. Only the ability to recoup lost profits is indicative of market power.

The above quoted sentence should be deleted from the Guidelines, as it is likely to be misleading. The Guidelines should clearly indicate that low prices will not be considered evidence of market power.

The Guidelines should also refer to the more comprehensive discussion of the evaluation of market power and the delineation of relevant markets in the *Merger Enforcement Guidelines*.

(iv) Conditions of Entry and Exit – Behavioural Barriers

The reference to "excessive" investment in research and development or advertising in paragraph 58 should be explained or deleted, particularly as it is generally the policy of Industry Canada to encourage additional investment in research and development.

Paragraph 59 deals with natural or regulatory barriers to exit, not barriers created by firm behaviour. The paragraph should be moved to the section on "structural barriers" (after paragraph 56). The point that "barriers to exit…increase the prospects that competitors will increase prices as opposed to exiting the market" is significant. In certain circumstances a predatory pricing policy may substantially lessen competition without inducing exit.

This section of the Guidelines should comment on the circumstances in which contracts and contractual practices may be considered as behavioural barriers.

(v) Conditions of Entry and Exit – Reputational Barriers

The discussion of "reputational barriers" refers in various places to the effect of a reputation for "unreasonably low pricing". The Guidelines should not discourage firms from establishing a pattern or reputation of low pricing as such behaviour will generally be pro-competitive. It would be helpful to emphasize in this section that pricing at or above cost, no matter how low, will never be considered anti-competitive.

Paragraph 63 should follow paragraph 51 as it is relevant to more than just reputational barriers. It should also be amended. Why would the time period during which the potential for new entry is evaluated be shortened if the industry is one "where only minimal investment and expertise is required and where there is a history of rapid effective entry"? The prospects for entry are relevant because if a firm expects entry before it could recoup its costs then it would not be rational to engage in predation. Adjusting the relevant time period based on the ease or

history of entry in the manner described makes it more likely that predation will be found in industries where it is least likely to occur, and vice versa.

(vi) Conditions of Entry and Exit – Ability to Recoup Losses

The Guidelines state that "a firm can recoup losses incurred in one market by exercising market power in another product or geographic market(s)". In our view, it is critical that such a conclusion be reached only after the application of a rigorous analytical theory to the specific facts. For example, absent reputation effects, predation in one market will have no impact on a firm's ability to raise prices in another market, so there can be no "recoupment". While it is possible for a firm with market power to set off profits in market A against losses in market B, this behaviour is not economically rational unless the firm expects to recoup the losses in market B through bundling or future price increases.

The examples at the end of the paragraph (preserving long-term stability of an existing market structure and establishing an industry standard to exclude others or maintain market control) are examples of preserving market power through predation. Contrary to what the Guidelines indicate, they are examples of low pricing behaviour motivated by the prospect of recoupment. This is another instance of where the Guidelines appear to be confused about the meaning of recoupment.

(vii) Effect or Tendency of Eliminating a Competitor

As indicated above, strategic low-pricing behaviour which deters entry is lawful and pro-competitive as long as there is no competitive harm. In other words, low pricing may be competitive pricing. This section should be clarified.

(viii) Designed to Substantially Lessen Competition or Eliminate a Competitor

Paragraph 68 indicates that a policy designed to substantially lessen competition or eliminate a competitor may contravene section 50 even if it is "entirely

ineffective". We agree with the statement in paragraph 37 that a low-pricing policy with an anti-competitive "tendency" or "design" is subject to enforcement action even before it has had a noticeably anti-competitive impact. However, a policy which is unlikely to have – or is incapable of having – an anti-competitive impact should not be subject to enforcement action regardless of the policy's design. A corporation with no market power should never be found to violate the unreasonably-low-pricing provisions of the *Act*, even if the corporation's marketing documents reflect a desire to "crush" a rival.

(ix) Prices Lower than Those Exacted Elsewhere in Canada

As indicated under "Competitive Impact", above, the Section believes that the effects of a policy of selling products at different prices in different areas of Canada should be evaluated with reference to relevant geographic antitrust markets. The Guidelines should make it clear that this will be the Bureau's policy.

(x) Prices that are "Unreasonably Low"

We repeat our concerns under the above discussion on avoidable cost standard.

The Guidelines should emphasize that above-cost pricing will never be considered unreasonably low and that a price below an appropriate measure of cost will only be considered unreasonable is there is no valid business justification for it.

It is unclear how charging a low price would enable a firm to build inventory. This example should be deleted.

E. Low Pricing Resulting From Market Expansion (Part 5)

The third bullet in paragraph 82 should refer to the requirement in the *Act* that the conduct would substantially lessen competition or eliminate a competitor (not simply "would harm competition").

F. Enforcement Outcomes (Part 6)

Paragraph 86 indicates that a fine may be imposed in lieu of a prison term for a violation of paragraph 50(1)(b) or 50(1)(c). As this penalty is not prescribed by the *Act,* the Guidelines should indicate the authority for imposing a fine (e.g. sections 734 and 735 of the *Criminal Code*). It should also clarify that for a person other than a corporation a fine can be imposed in addition to a prison term.

The discussion of other remedies should refer to the possibility of proceeding under section 79 of the *Act*.

VI. CONCLUSION

The Section appreciates the opportunity to provide its comments concerning the Guidelines. As is evident from the above discussion, we have some significant concerns with the Guidelines. We look forward to having an opportunity to comment on any further revision.