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Dear Ms. Galipeau:

Information Bulletin on Regulated Conduct Defence

Thank you very much for providing us with an opportunity to submit comments on the Competition Bureau's 2002 *Information Bulletin on the Regulated Conduct Defence* ("RCD Bulletin").

In 2003, we were co-authors of a paper entitled, "The Regulated Conduct Defence: Time for Legislative Action?" 21:3 Can. Comp. Rec. 52 (2003). A copy of our paper is appended to this letter for your reference. We were also among the principal drafters of the Canadian Bar Association's ("CBA") September 8, 2003 *Submission Concerning the Competition Bureau's Information Bulletin on the Regulated Conduct Defence*.

In our 2003 paper, we attempted to provide an objective review of the current state of the common law jurisprudence which forms the basis of the regulated conduct doctrine[1] ("RCD") and to explore the scope and limitations of the RCD under the then current jurisprudence. Our paper also contained a critique of the RCD Bulletin. More recently, we have re-examined some of the conclusions in our paper in light of the recent judgment of the Supreme Court of Canada in *Garland v. Consumers' Gas ("Garland")*[2]. This letter will outline some revised conclusions respecting the scope of the RCD in light of the *Garland* case, will set out our thoughts about how

[1] The regulated conduct "defence" is sometimes more accurately described as an "exemption" or "exclusion" from the *Competition Act* than as a defence, since the doctrine may be invoked as a preliminary jurisdictional issue in litigation, prior to there being any need for an accused or respondent to defend on the merits of the case. Of course, regulated conduct may also be pleaded as a defence. For purposes of this letter, we have chosen to use the broader terminology "regulated conduct doctrine", which captures the broad range of manners in which regulated conduct may be invoked in enforcement proceedings.

[2] 2004 SCC 25.

the RCD Bulletin might be revised to more accurately reflect the state of the existing law, and will also comment on the desirability of legislative reform in this area, more particularly if proposals to create a *per se* prohibition on hard core cartels currently under consideration are ultimately implemented.

A. Implications of *Garland*

1. Application of the RCD to federally regulated conduct

In our 2003 paper we questioned whether the RCD was available in the case of federally-regulated conduct. In our view, the recent judgment of the Supreme Court of Canada in *Garland* reinforces the view that *as a purely legal matter*, the RCD is limited to provincially regulated conduct (see in particular paras. 76, 77 and 78 where the SCC reviews the scope of the RCD in federal/provincial terms and also examines its case law under the Criminal Code relating to the issue of when "approval by a provincial body could displace a criminal charge" (para 78)).

Nonetheless, the practical import of the conclusion that the RCD is available only in the case of provincially regulated conduct should not be overstated. The reality may be that the doctrine has not developed in the federal sphere of authority simply because it is not *necessary* to resort to the RCD in order to determine whether the CA applies to federally regulated conduct. In the provincial sphere, it was necessary to develop the RCD in order to overcome the general rule of paramountcy of federal law which would otherwise prevail. In the federal sphere, other statutory interpretation principles are available to resolve apparent conflicts between federal regulatory legislation and the CA. In many cases these principles will – and should – lead to the same conclusions as would the application of the regulated conduct defence. For example, in its recent redetermination decision in *Eli Lilly v. Apotex*[3], the Federal Court wrote:

> [W]here an agreement deals only with patent rights and is itself specifically authorized by the *Patent Act*, any lessening of competition resulting therefrom, being authorized by Parliament, is not "undue" and is not an offence under section 45. The two statutes must be read together harmoniously and that can only be done if the meaning of the key word "undue" in section 45 is limited to restrictions on competition which are not specifically authorized by the *Patent Act*.

The Court in *Eli Lilly* made no reference to the RCD, yet used the same reasoning as have the courts in many of the RCD cases – *i.e.*, that conduct authorized by valid federal legislation cannot be "undue" – to determine that there could be no violation of section 45. While there has been some controversy about whether the Federal Court in *Eli Lilly* correctly decided the matter**,** the case nonetheless provides a nice illustration of how a court might resolve conflicts between

[3] 2004 F.C. 1445 (F.C.T.D.) at para 9.

the CA and federal regulatory legislation without there being any need to refer to the RCD line of cases.

The essential rationale for the RCD is that conduct that is mandated or authorized by valid legislation cannot violate the *CA*, and we believe this basic rationale should apply equally in both the federal and provincial regulatory spheres. The fact that a particular form of regulation is allocated in our Constitution to the federal rather than provincial legislator should not change the overall approach of the Bureau to regulation. We therefore support the Bureau's enforcement position, as set out in the RCD Bulletin, that the RCD is available where the conduct at issue is federally regulated. We do not think that the *Garland* case in any way detracts from the validity of this enforcement position.

2. Application of the RCD to the civil provisions

The Supreme Court of Canada in *Jabour*[4] expressly linked the RCD to the then criminal nature of the anti-combines legislation:

> [S]o long as the *CIA* [Combines Investigation Act], or at least Part V, is styled as a criminal prohibition, proceedings in its implementation and enforcement will require a demonstration of some conduct contrary to the public interest. It is this element of the federal legislation that these cases all concluded can be negated by the authority extended by a valid provincial regulatory scheme.

These comments were based on earlier case law which explicitly tied the availability of the RCD to the criminal nature of the federal anti-combines law.[5] In particular, the courts have focussed on the "undueness" standard in the conspiracy provision, a term which has been explicitly equated with the "public interest"[6], and have concluded that provincially regulated conduct could not be undue or contrary to the public interest.

If we accept the premise that the RCD applies only in the federal/provincial context, then there is some basis for restricting it to criminal prohibitions, on the notion that an exception to the general rule of paramountcy of federal law is appropriate only where one's liberty (in the criminal law sense) is at stake.

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4 *Jabour v. Law Society of British Columbia* (1982), 137 D.L.R. (3d) 1 S.C.C. ("*Jabour*").

5 See *e.g.*, *R. v. Chung Chuck*, [1929] 1 D.L.R. 756 (B.C.C.A.), aff'd [1930] 2 D.L.R. 97 (J.C.P.C.); *Reference re: Farm Products Marketing Act*, [1957] S.C.R. 198; *R. v. Simoneau*, [1936] 1 D.L.R. 143 (Que. Ct. Sess.), *R. v. Cherry*, [1938] 1 D.L.R. 156 (Sask. C.A.); *Ontario Boys' Wear Ltd. v. Advisory Committee*, [1944] S.C.R. 349.

6 The court in *R. v. Canadian Breweries Ltd.*, [1960] O.R. 601 (Ont. High Court of Justice) ("*Canadian Breweries*") found that undue connotes "public interest". The "public interest" discussion in *Canadian Breweries* was cited with approval by the Supreme Court of Canada in *Jabour*.

Nonetheless, we believe that the Supreme Court in *Garland* may have created a clearer[7] basis for invoking the RCD under the civil prohibitions of the *CA*, by introducing the concept of whether the federal law creates any "leeway" into the RCD equation. While the Court in para. 79 refers to the fact that "[i]n the previous cases involving the regulated industries defence, the language of 'the public interest' and 'unduly' lessening competition has always been present" and notes that the absence of such language in s. 347 of the *Criminal Code* means the RCD is not available under that provision, in para. 77 the Court's language would appear to be somewhat broader. Para. 77 reads as follows:

> Winkler J. was correct in concluding that, in order for the regulated industries defence to be available to the respondent, Parliament needed to have indicated, either expressly or by necessary implication, that s. 347 of the *Criminal Code* granted leeway to those acting pursuant to a valid provincial regulatory scheme. If there were any such indication, I would say that it should be interpreted, in keeping with the above principle, not to interfere with the provincial regulatory scheme. But s. 347 does not contain the required indication for exempting a provincial scheme.
>
> [emphasis added]

The precise scope of the Supreme Court's language here is not entirely clear. For example, must the "required indication" involve the use of such terms as "unduly" or "against the public interest"? If so, how could Parliament indicate "by necessary implication" (i.e., implicitly) that the provincial regulator was to have leeway? Is the notion of "leeway" restricted to conduct that "unduly" lessens competition (or lessens competition to a degree which is against the public interest), or does it broadly encompass any federal provision with a discretionary element?

In our view, the notion of "leeway" introduced in *Garland* creates a basis for expanding the regulated conduct doctrine beyond the pure criminal law sphere. In particular, we believe that following *Garland*, it is open to argue that the RCD applies to any provision of the *CA* which qualifies the illegality of any action or practice by reference to some required degree of adverse competitive effect (in particular the term "substantially" or similar terms such as "adverse effect" used in the civil provisions of the CA). Moreover, as a policy matter, we believe that under our modern legislation, the terms "substantially prevent or lessen competition" (and therefore the civil provisions) connote the public interest, just like the terms "unduly prevent or lessen competition" in the conspiracy provision.

Therefore, we support the Competition Bureau's position that the RCD applies to both the criminal and civil provisions of the CA. This position is set out in the RCD Bulletin and reflects the enforcement approach taken by the Bureau in previous cases (most notably the *LSUC*[8] case

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[7] As noted in our paper, there is already some authority for extending the RCD into the civil sphere.

[8] *Law Society of Upper Canada v. Canada (Attorney General)* (1996), 67 C.P.R. (3d) 48 (Ont. Ct. Gen. Div.).

where the parties including the then Director of Investigation and Research agreed that the RCD extended to the civil sphere).

3. Implications of Garland for *per se* provisions of the CA

One of the clearer implications of *Garland*, and of the Court's reliance on the concept of "leeway", is that where the federal legislation does not contain any sort of leeway, the RCD is not available. As a result, it is clear that the RCD is not available in the context of existing "*per se*" prohibitions such as the price maintenance provision (s. 61). Perhaps more significantly, the Court's decision in *Garland* suggests that the RCD would not be available to shield regulated conduct from the application of a *per se* prohibition on hard core cartel-type conduct, if such a provision is adopted as part of the reform of section 45 of the *CA*. This is not, in our view, a desirable outcome. In particular, we note that industry agreements on matters such as rate regulation are at the heart of many regulatory schemes. Having a federal competition law that condemns a government (provincial or federal) authorized or mandated industry agreement would serve to undermine the regulatory scheme in question.

Although the *Garland* case did not involve the CA, the Supreme Court gave a fairly unambiguous statement in that case of how it would be inclined to apply the RCD in the context of a case that did involve the treatment of regulated conduct under the CA.

In our view, therefore, there will be a need to amend the CA to add some form of legislative "regulated conduct" defence to a *per se* cartel provision, if and when our conspiracy law is amended to create such a provision. A legislative RCD is also required, in our view, in connection with several other *per se* provisions of the CA (see section 47 (bid rigging), 49 (agreements between federal financial institutions) and 61 (price maintenance)).

B. Legislative amendment more broadly

We also question whether a legislated RCD should extend more broadly to all sections of the CA. As set out in our 2003 paper, legislative reform may be desirable in light of the limited jurisprudence in the area. Various proposals regarding the possibility of codifying the RCD in our legislation were debated in the 1970s. In our view a number of these proposals were unduly restrictive as to the scope of the exemption for regulated conduct; but they nonetheless provide a starting point for consideration of a legislated RCD. There is a significant amount of material from the 1970s that would be worth reviewing as the Bureau moves forward to revise its RCD Bulletin and to consider its enforcement position vis à vis regulated conduct more generally. (See, in particular, the recommendations from the *Skeoch-McDonald Report* referred to in our 2003 paper; the sections of Bills C-256, C-42 and C-13 relating to regulated conduct as appended to our paper, and the various submissions made to, and reports made by, the House and Senate Committees that considered these Bills. We note that, among other things, a number of the written submissions made to the House of Commons Standing Committee on Finance, Trade and Economic Affairs on Bill C-42 focussed on regulated conduct.)

C. Revising the RCD Bulletin

For the reasons set out in our 2003 paper and in the 2003 CBA Submission, we are of the view that the RCD Bulletin as currently drafted does not accurately reflect the existing state of the common law. In particular, we do not believe that the "operational conflict" requirement has played a part in any of the RCD jurisprudence. We also disagree with the Bureau's position that self-governing regulators should be subject to greater scrutiny in assessing whether the RCD applies, since this position is at odds with the jurisprudence, including most importantly the judgment of the Supreme Court in *Jabour*. Moreover, the jurisprudence does not, in our view, support the position that a person subject to regulation may invoke the RCD only where his or her conduct is *mandated or required* by regulation; to the contrary, the case law (again most importantly *Jabour*) clearly establishes that conduct *authorized* by valid regulation may also fall within the RCD.

In redrafting the RCD Bulletin, the Bureau should not lose sight of the fact that while it is outlining its enforcement position on a common law doctrine, it should do so on a basis which reflects the Bureau's best understanding of the state of the current law. In this regard, we would suggest that the Bureau refer to case law in the revised Bulletin. Our review of the jurisprudence establishing the RCD suggests that the essential rationale for the RCD is not overly complicated and that the courts have applied it in a relatively straightforward manner. We would therefore suggest that the revised RCD Bulletin be drafted along the following lines:

- The Bulletin should lead off with a brief review and statement of the basic common law principle underlying the RCD. In our view, the basic common law test can be succinctly stated as follows:

> The regulated conduct doctrine provides that an act authorized or required by a valid regulatory statute cannot be contrary to the public interest or an offence against the state under the CA (cite *Garland*; note that the "required" standard comes from the *Industrial Milk*[9] case). The courts have established four necessary elements or factors that must be met before the regulated conduct doctrine will be accepted by the courts, namely: (i) the relevant legislation or regulation must be validly enacted; (ii) the activity or conduct in question must be authorized (*Jabour*, *Industrial Milk*) or required by the legislation or regulation; (iii) the regulator must have exercised its authority (*Canadian Breweries*), (iv) the conduct in question must not have frustrated the exercise of authority by the regulatory body (*Canadian Breweries*). (It may be worth noting that some of the lower court decisions were cited with approval by the Supreme Court in *Jabour*.)

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9 *Industrial Milk Producers Association et al. v. Milk Board et al.* (1988), 47 D.L.R. (4th) 710 (F.C.T.D.) ("*Industrial Milk*").

- In light of the *Garland* case, the Bureau would have to add the following statement (although to the extent that legislation is introduced to "codify" the RCD in the context of a *per se* section 45 or more broadly, this statement would have to be revised):

> The defence applies only to those criminal and civil provisions of the CA that create "leeway" for the actions of a regulator, and more specifically the RCD does not apply to conduct which is illegal *per se* under the CA (*Garland*).

- The Bureau should retain its position that the RCD may apply to federally- or provincially-regulated conduct. It should also retain its position that the RCD is available under the civil or criminal provisions of the legislation (except *per se* matters, subject to any legislative reform). As noted, these positions may go beyond the current state of the common law, but they are consistent with the principles underlying the RCD and represent a sensible enforcement perspective.

- The Bureau should include its position on the difficult issue of forbearance in the revised Bulletin (we support the position taken in the 2002 RCD Bulletin).

D. Mergers are different

The Bureau may have to give more detailed consideration of its enforcement position in the mergers sphere. We agree with the Bureau's enforcement position that the RCD should extend to mergers. However, in the merger context, two distinct issues are raised, namely: (i) is regulation in an industry sufficient to prevent the existence or exercise of market power post-merger?; and (ii) does the existence of a regulatory regime (which may include parallel merger approval powers) actually remove the Competition Bureau's jurisdiction to decide a merger case?

The first of these issues – regulation as a factor relevant to market power – is likely already considered by the Bureau as part of its merger assessment process (and if not, it certainly should be considered). The second issue is far more difficult, and requires the Bureau to take a careful look at the different regulatory regimes that exist today, at both the provincial and federal levels, and to determine which regulator is best placed to make a decision in a merger case, and whether the Competition Bureau should have a role. We believe that a number of commentators have published views in this area. Once the Bureau has determined its overall approach, it would then have to determine how it would implement such views (e.g., through legislative amendment, inter-agency agreements, and/or through statements in its RCD Bulletin.) However, we would note that, as a matter of principle, the concept of concurrent jurisdiction seems undesirable, at least in cases where the industry regulator has been given more specific jurisdictional authority over the firms subject to regulation, and may be better placed to make determinations about mergers and other industry-specific conditions of competition (e.g. rate regulation, market allocation, access to essential facilities). For example, we note that some regulatory regimes are designed to ensure survival of local or Canadian firms in an industry, and scrutinizing (and

potentially blocking) mergers among regulated firms based on purely competition law principles might serve to undermine the purpose of industry regulation.

E. Moving forward

In light of the fact that some of the issues raised in this letter are not likely to be resolved in the short term – e.g., amendments to the CA in the context of a reformed section 45, the consideration of whether other amendments to the CA are necessary or desirable in the RCD context, and quite possibly the consideration of how mergers in regulated industries should be dealt with – we would recommend that the Commissioner republish the RCD Bulletin in a timely manner, but commit to revising the Bulletin again in the future in light of any relevant future developments. We would also recommend that the Bureau undertake a study of whether legislation to codify the RCD is desirable, and also look more closely at the issues respecting mergers in regulated industries.

In the event that reform of section 45 is likely to involve the creation of a *per se* hard core cartel provision, we would strongly recommend that, at a minimum, the Competition Bureau include in any legislative proposals a specific exemption for regulated conduct that applies at the very least to a *per se* cartel provision, and ideally to the other *per se* provisions in the CA as well.

We thank you again for giving us the opportunity to provide comments on the RCD Bulletin. Please do not hesitate to contact either of us if you have any questions respecting this letter or the attached paper.

Yours very truly,

Janet Bolton and Tim Kennish

JB/TK:jb