

The Canadian Competition Bureau has recently offered new draft guidelines on the abuse of dominance that, in the area of joint dominance, depart from the existing guidelines in two ways: first, the bureau no longer considers as a potential abuse of joint dominance the adoption of practices that facilitate supra-competitive pricing in an oligopoly; second, while in the past some form of explicit coordination was required for an assessment of joint dominance, the bureau now considers parallel abusive conduct by jointly dominant firms as potentially infringing the abuse provisions. The first change, which we attribute to case law rather than to the bureau, is undesirable. The adoption of facilitating practices can lessen competition, and is practically remediable. Facilitating practices should be considered potential abuses of joint dominance. On the other hand, the second change is sensible: oligopolists may profitably adopt exclusionary practices in parallel without coordination. Parallel exclusionary practices may lessen competition even when no single firm has a dominant market share, and this problem is amenable to a practical remedy. The bureau's new approach is welcome on this front.

Keywords: abuse of joint dominance/oligopoly/exclusion/Canadian Competition Bureau

I Introduction

The central purpose of antitrust law in a market economy is to align firms' incentives with the social interest by encouraging vigorous competition within markets. More competitive markets generally produce better outcomes, because prices are closer to marginal cost and because the appropriate qualities and product varieties are typically offered. Where prices remain above marginal cost because of a lack of competition in a market, the net social benefits of the market are reduced: some individual units of a good that are valued more than the cost of production should be exchanged but are not. This lowers social surplus.

Well-designed antitrust laws, apart from regulating mergers, constrain anti-competitive conduct on the part of firms. Conduct is restricted mainly in two areas. In the area of cartels or horizontal collusion, anti-

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trust laws (in Canada, s. 45 of the Competition Act¹) limit the exercise of market power through prices that are excessive as a result of explicitly coordinated action among competitors. In the area of abuse of dominance (ss. 78 and 79 of the Competition Act), the laws constrain strategies that lessen competition by excluding rivals from a market, disadvantaging rivals by raising their costs, or inducing their exit through predatory strategies.²

This article analyses the law and economic foundations of an area of antitrust policy at the intersection of abuse of dominance and cartels: the abuse of joint dominance. Abuse of joint dominance is defined as anti-competitive conduct not by a single dominant firm but by a group of firms with a collectively dominant market share. The firms in an abuse of joint dominance case are not constrained by competition within the group, perhaps because of tacit coordination; nor, perhaps because of strategic behaviour, are they constrained by competition from outside the group.

An exclusionary abuse of joint dominance involves generally the same strategies as single-firm abuse of dominance – exclusionary strategies, raising rivals’ costs, disciplinary strategies, or predation – but in joint dominance cases these strategies are adopted by firms in an oligopoly rather than by a single dominant firm. To this set of exclusionary, predatory, or disciplinary strategies one can in the case of multiple firms add ‘facilitating practices,’ strategies that, if adopted by all firms in a cartel, render the cartel more stable. Facilitating practices, as the name suggests, facilitate the exercise of market power rather than representing the abuse or exercise of market power directly. These practices can obviously be harmful and may be best dealt with under the joint abuse area of anti-trust law, as we discuss. In this article, we focus on exclusionary strategies, exemplified by long-term contracts and exclusivity restrictions, as well as on facilitating practices.

Given its position at the intersection of antitrust laws against collusion and against abuse of dominance, the design of optimal regulation on abuse of joint dominance confronts the challenges of both areas. For example, an oligopoly that exercises joint dominance and adopts exclusionary strategies must deal with two kinds of free-rider problem. There is a tendency for each firm to cheat on an implicit or explicit agreement on prices by cutting price and selling more (*i.e.*, each firm is tempted to free-ride on the high prices of others); in addition, it may appear that any one firm has incentives to free-ride on the costly exclusionary efforts of other firms. Can this additional free-rider problem be overcome? In other words, is it far-fetched to theorize that firms in an oligopoly can

1 R.S.C. 1985, c. C-34.

2 See, *e.g.*, *Canada (Director of Investigation and Research) v. NutraSweet Co.* (1990), 32 C.P.R. (3d) 1 (Comp. Trib.) [*NutraSweet*].

coordinate on both prices and entry-deterrence strategies? If not, then exclusionary abuses of joint dominance should, as a matter of theory, not be important.

We argue that anti-competitive exclusionary or predatory strategies on the part of an oligopoly cannot be ruled out. It can be profitable, even in a narrowly self-interested sense (without regard for the threat of retaliation), for individual firms to engage in exclusionary practices. And in a wider set of circumstances, a complementarity arises between strategies that facilitate the coordination of a cartel and the exclusion of potential entrants to a market that would discipline the cartel: the same strategies can be successful in both maintaining high prices and deterring entry. We provide in this article a high-level outline of the economic logic, rather than a formal argument. In addition, our analysis finds empirical support in a case, *Waste Services*,³ which we discuss based on facts that can be inferred from the consent agreement in this case.

This is an opportune time to review the law of the abuse of joint dominance and outline the economic foundations of optimal policy in this area. As we discuss in the Part II below, the approach of Canada's Competition Bureau has changed between its Enforcement Guidelines on the Abuse of Dominance Provisions (2001) and its Draft Updated Enforcement Guidelines on the Abuse of Dominance Provisions (Sections 78 and 79 of the Competition Act) (2009). An independently (not explicitly coordinated) but jointly adopted strategy in an oligopoly that might abuse joint dominance was not an antitrust violation in the 2001 Canadian guidelines but is a violation in the 2009 draft guidelines; an independently but jointly adopted facilitating practice was a possible violation in 2001 but is not in 2009.⁴ The new position on independent (*i.e.*, not explicitly coordinated) abusive exclusionary practices finds support in our analysis. Explicit coordination of exclusionary practices is not necessary as there are good reasons to believe that implicit coordination of these practices is possible. The new position on facilitating practices is one to which the Competition Bureau is constrained by the statute

3 *Commissioner of Competition and Waste Services (CA) Inc. and Waste Management of Canada Corporation*, 16 June 2009, CT-2009-003 (Comp. Trib.) [*Waste Services*].

4 Further evidence of the controversy around these questions is found in the variation across US and EU law. Neither independent facilitating practices nor independent abusive practices by non-individually-dominant firms are antitrust infringements in the United States: see, *e.g.*, Section of Antitrust Law, American Bar Association, *Antitrust Law Developments (Sixth)* (2007) at 318. In Europe, independent facilitating practices are a possible infringement, and there is controversy as to whether independent abusive practices by firms that are jointly dominant infringe the EC Treaty: see, *e.g.*, Barry Hawk & Giorgio Motta, 'Oligopolies and Collective Dominance: A Solution in Search of a Problem' (November 2008), online: SSRN <<http://ssrn.com/abstract=1301693>>.

and precedent. But the statute and precedent are wrong on this point, in that they exclude from antitrust scrutiny anti-competitive practices that the law may potentially remedy.

II *The law on joint abuse of dominance*

There are two legal questions on which we focus here. First, how does the law respond to facilitating practices? And, second, how does the law respond to joint exclusion? The Competition Bureau has recently changed its approach to both questions. Section 79 of the Competition Act allows the Competition Tribunal to make an order where a dominant firm or firms engage(s) in a practice of anti-competitive acts that have the effect of substantially lessening competition. Only a handful of contested cases have been brought under this provision since its adoption in 1986, so the Competition Bureau has promulgated guidelines to give the competition community a sense of its approach to the matter. Such guidelines are not legal authority, nor are they even binding on the bureau itself.⁵ Nevertheless, the Competition Bureau plays a very important role in enforcing the law on abuse of dominance. The commissioner of competition is the sole party with standing to complain before the Competition Tribunal about a possible abuse. Thus, if the commissioner does not consider a particular practice an abuse of dominance, this is the final say on the matter, since private parties have no capacity to argue otherwise before the tribunal or the courts. If the commissioner does consider a particular practice by a firm or firms to be an abuse of dominance, the firm(s) in question may either negotiate with the commissioner or engage in costly, lengthy litigation. Many choose the former; only five abuse cases have been contested since 1986. And if the Competition Bureau and the parties negotiate a consent order, under s. 105 of the Competition Act, this order is as binding as if it had been rendered by the tribunal.

In its Enforcement Guidelines on the Abuse of Dominance Provisions (2001), the Competition Bureau stated that it would potentially consider the adoption of facilitating practices under the abuse of dominance provisions of the Competition Act, taking the position that if facilitating practices serve to support supra-competitive pricing, the bureau could invite an order under s. 79.⁶ In its 2009 Draft Updated Enforcement Guidelines

5 In the Superior Propane merger litigation, ultimately decided in *Canada (Commissioner of Competition) v. Superior Propane Inc.*, 2003 F.C.A. 53, the Competition Bureau deviated from its own Merger Enforcement Guidelines in arguments before the Competition Tribunal.

6 Industry Canada, *Enforcement Guidelines on the Abuse of Dominance Provisions (Sections 78 and 79 of the Competition Act)* (Hull, QC: Competition Bureau, July 2001) at 24.

on the Abuse of Dominance Provisions, however, the bureau rejects this approach.⁷ Building on prior case law, the bureau's view of 'anti-competitive acts' is limited to those acts that have an 'exclusionary, predatory or disciplinary' negative effect on a competitor.⁸ Facilitating practices have a beneficial effect on competitors, and are thus omitted from the scope of s. 79.

The Competition Bureau also reverses course on a second potential abuse of joint dominance whereby firms independently, but in parallel, adopt practices that exclude other firms from the market. In the 2001 Guidelines, the bureau noted that the case law to that point had considered exclusionary joint dominance only in settings where joint dominance was obvious because of an agreement between the parties. In *Interac*, for example, a consent order was made against a group of banks that had acted collectively through the Interac association to exclude other banks from participating in the network.⁹ Paragraph 3.2.1 of the 2001 Guidelines analogizes to explicit agreements in cartels and concludes that

something more than mere conscious parallelism must exist before the Bureau can reach a conclusion that firms are participating in some form of coordinated activities. The ability of a group of firms to coordinate actions without entering into an explicit agreement can be addressed under the abuse provisions.

Thus, it is apparent that coordination is required under the 2001 Guidelines to ground a finding of joint dominance, and coordination requires something more than mere conscious parallelism.¹⁰

The 2009 Draft Guidelines, in contrast, make no reference to coordinated action in assessing joint dominance. Rather, the test for joint dominance is based on the firms' actions and the market conditions themselves, without regard to coordination. Paragraph 3.2.1(d) states that

7 Industry Canada, *Updated Enforcement Guidelines on the Abuse of Dominance Provisions (Sections 78 and 79 of the Competition Act) Draft for Public Consultation* (Hull, QC: Competition Bureau, January 2009).

8 See, e.g., *NutraSweet*, supra note 2.

9 *Canada (Director of Investigation and Research) v. Bank of Montreal*, (1996), 68 C.P.R. (3d) 527 (Comp. Trib.).

10 See Davies Ward Phillips & Vineberg LLP, 'Canadian Competition Bureau Steps Up Enforcement against Joint Abuse of Dominance' (18 June 2009), online: Davies Ward Phillips & Vineberg LLP <http://www.dwpv.com/images/Perspective_Canadian_Competition_Bureau_Steps_Up_Enforcement_against_Joint_Abuse_of_Dominance.pdf> at 2: '[T]he Bureau's current abuse of dominance enforcement guidelines clearly indicated that some form of coordinated activities – at least more than consciously parallel conduct – would be required to establish joint control of a market.'

where these firms are each engaging in similar practices alleged to be anti-competitive, and they appear to together hold market power based on their collective share of the market, barriers to entry or expansion, and other factors . . . , the Bureau will consider these firms to hold a jointly dominant position.

The decision by the Competition Bureau not to require coordination in assessing joint dominance is not of merely academic significance. The bureau recently entered into a consent agreement with Waste Services (CA) Inc. and Waste Management of Canada Corp. that requires both firms to cease including a variety of terms, including exclusivity and high liquidated damages terms, in their contracts with customers.¹¹ Neither Waste Services nor Waste Management is dominant in its own right, but together the consent agreement reports them as holding 80 per cent of the market. Nothing in the consent agreement suggests coordinated action on the part of the firms; it is apparent that their collective market share and the exclusionary effect of their contracts were sufficient for the bureau to make an order. We discuss this case in detail below.

In summary, the Canadian Competition Bureau until recently considered facilitating practices as potentially abusive of joint dominance but now does not, and until recently required coordinated action beyond conscious parallelism among oligopolists to find joint dominance but now does not. The bureau's views are summarized in Table 1, along with our recommended policy approach, with YES indicating a possible antitrust infringement and NO the opposite.

We turn in Part III to explaining our conclusion on optimal policy, beginning with an analysis of abuse of single-firm dominance that is necessary to assess the prospect of joint dominance.

III *Abuse of single-firm dominance*

The decision in *NutraSweet*¹² held that abusive trade practices are exclusionary, predatory, or disciplinary. Among these classes of practices, we focus here on exclusionary strategies; in Part IV below we discuss facilitating practices as well.

Exclusionary strategies on the part of a single firm with a dominant market share generally involve contracts with either downstream buyers or upstream suppliers. If a dominant firm signs long-term exclusive contracts with downstream buyers, for example, then an entrant into the industry must rely on finding buyers at the end of their contracts or

11 *Waste Services*, supra note 3.

12 *Supra* note 2.

TABLE 1

	Independent Facilitating Practices	Independent Exclusionary Abuse of Joint Dominance
2001 Guidelines	YES	NO
2009 Draft Guidelines	NO	YES
Our recommendation	YES	YES

buyers whose need for the product is new. If the entrant bears fixed costs in entering the market or maintaining the flow of production, the scarcity of available buyers will make entry less profitable. The entrant will have to incur a longer period of negative-profit operations while it gathers sufficient buyers as their contracts end. Where buyers purchase only one unit at a time or there are other technical efficiencies from dealing with only one seller at a time, a simple long-term contract with liquidated damages can have the same effect.

Other contracts have similar effects. Consider, as another example, a contract requiring notification of any offer received by the buyer, combined with a right of first refusal on the part of the seller to match the offer. This contract can deter entry because it provides for an automatic and immediate response by the incumbent to any attempt by the entrant to establish a presence in the industry by undercutting the incumbent's current prices. Knowing that such contracts are in place would deter a potential entrant from entering the market.

Is the potential exclusionary benefit of these contracts to the incumbent an adequate explanation of the contracts? Is it an adequate basis on which to base antitrust policy (keeping, for now, within the simple context of single-firm dominance)? The traditional, or pre-Chicago, view was yes. A monopolist in a market has market power – including the power to impose contracts on consumers that are not in consumers' interest. If a set of contracts can help the incumbent maintain a monopoly in the industry and serve no other purpose, then of course the contracts are profitable and anti-competitive.

This traditional view is wrong. Any contract is entered into voluntarily by both seller and buyer(s). In virtually any commercial contract, there is the opportunity for the buyer and seller to transfer lump sums of wealth between them. A contract, apart from the price itself, must therefore be explained in terms of maximizing the *sum* of the pay-offs to the contractual parties, not in terms of the power of one party to impose the contract on the other. If another contract offered a higher sum of pay-offs, then the parties could move to that contract, sharing the gain in total pay-offs, regardless of bargaining power.

The Chicago School concluded that since contracts maximize joint surplus between buyer and seller, and since anti-competitive contracts reduce buyer and joint surplus, the fact that a buyer agrees to an exclusive contract implies that it is not anti-competitive.¹³ But the fact that a contract maximizes the pay-offs to contractual parties does not mean that the contract is efficient. A contract can have a negative impact on parties outside the contract. This is the basis for the modern economic theory of anti-competitive, exclusionary contracts (sometimes referred to as the post-Chicago theory). The seminal article in this literature is by Phillippe Aghion and Patrick Bolton¹⁴ and offers two specific theories as to why exclusionary contracts might be entered into by a dominant seller and (voluntarily) by buyers.

The more important of these theories involves a collective-action problem across buyers with respect to their decisions to accept the contract offer by the incumbent. Suppose that an incumbent monopolist, selling to a number of buyers each of whom demands only one unit of a product, faces the threat of entry by a new firm. Suppose further that, as is common, the entrant faces a sunk cost of entry into the industry or a fixed cost that must be incurred continuously as long as the entrant is in the industry. Then the entrant will not enter unless there are enough buyers available that its fixed costs can be covered or its investment in entry costs into the industry can be justified. Suppose that the number of free buyers required is fifteen, for example. The incumbent, knowing this, can offer long-term contracts – exclusive contracts or contracts with liquidated damages – to enough buyers that the remaining number of ‘free buyers’ is too small to justify the entrant’s investment. The incumbent seller, having the first-mover advantage in offering contracts, can offer contracts to all but thirteen of the buyers, and if the buyers accept, the entrant is shut out.

Why would buyers accept such contracts? The old Chicago argument is that the incumbent supplier must compensate the buyers fully for the cost to them of exclusivity – the cost to them of the loss in competition when the entrant is excluded – because otherwise the buyers will reject the contract. But consider the buyers’ decisions to accept the contract. If all other buyers accept the contract, then the decision of a particular buyer has no effect on the entry decision; a decision to reject the contract by a particular buyer would still leave only fourteen free buyers, not enough to justify entry. Each buyer is in the same position. If the seller

13 See, e.g., Robert H. Bork, *The Antitrust Paradox: A Policy at War with Itself* (New York: Basic Books, 1978).

14 Philippe Aghion & Patrick Bolton, ‘Contracts as a Barrier to Entry’ (1987) 77 *Am.Econ.Rev.* 388.

offers even a small 'bribe' in terms of a reduction in price for entering the long-term contract, then acceptance by all buyers is a Nash equilibrium in the 'sub-game' of simultaneous buyer acceptance decisions.¹⁵ The seller can achieve exclusion with only a small bribe to each buyer by exploiting the buyers' collective-action problem: buyers individually are better off by accepting the contract, but collectively they would be better off if all rejected the contract. Contracts can be exclusionary and anti-competitive even when entered into voluntarily by all market participants, because each buyer ignores the impact of its decision on other buyers.

The use of exclusionary contracts is illustrated by *Nielsen*, which involved contracts by an incumbent monopolist in the Canadian market for scanner-based market information.¹⁶ The case involved both contracts with upstream suppliers (suppliers of raw data) and contracts with downstream buyers (producers of grocery products). The downstream contracts are the more useful illustration here. Initially, Nielsen's contracts with buyers were short-term, with commitments of less than one year. As soon as the IRI's plans for entry into the Canadian market became clear, Nielsen struck longer-term contracts, of up to five years, with the thirty or so buyers that it was most vulnerable to losing to the potential entrant. These new long-term contracts had liquidated damages and offered the buyers some discount in prices, but the necessary discount would have been small. The long-term contracts were struck down as part of the remedy imposed by the Competition Tribunal.

A challenge in any case where long-term contracts are at issue as an abuse of dominance is to distinguish empirically between the hypothesis of an anti-competitive explanation and the hypothesis of an efficiency explanation of these contracts. Long-term contracts are an efficient way to organize economic activity whenever they are needed to protect the returns on specific investment by one party or the other in a contract and when the coordination of such investment and planning is necessary because of uncertainty in the evolution of the economic environment.¹⁷ Almost all long-term contracts are efficient, so clear evidence must be available to reject the efficiency hypothesis.

15 The bribe is not necessary for the outcome to be a Nash equilibrium, but it does ensure a Nash equilibrium in which acceptance is a strictly best response on the part of each buyer.

16 *Canada (Director of Investigation and Research) v. The D&B Companies of Canada Ltd.* (1996), 64 C.P.R. (3d) 216 (Comp. Trib.) [*Nielsen*].

17 See Paul Joskow, 'Contract Duration and Relationship-Specific Investment: Empirical Evidence from Coal Markets' (1987) 77 *Am.Econ.Rev.* 168; Oliver Williamson, *Markets and Hierarchies: Analysis and Antitrust Implications* (New York: Basic Books, 1975).

IV *Horizontal coordination: The oligopoly problem*

The second strand of antitrust economics that joint dominance policy draws upon is oligopoly pricing – specifically, coordination by firms in a tight oligopoly to maintain supra-competitive prices. There is a basic tension for the firms in an oligopoly: collectively they are better off if they suppress competition, but individually they may be better off by competing vigorously. There is a danger that such firms will explicitly commit to one another not to compete vigorously and thus realize greater profits for the collective. It is a core matter for antitrust law to deter such explicit agreements. The law makes it illegal, indeed criminal, for competitors to explicitly agree on price. Aside from deterring covert agreements in ‘smoke-filled rooms’ that would help oligopolists coordinate their behaviour, such anti-conspiracy rules prevent firms from entering into overt contracts to keep prices high. This is significant in itself, because in the absence of such enforceable agreements there will be incentives for each oligopolist to cheat on the agreement – a successful cartel raises marginal revenue above marginal cost, and thus each firm individually is better off if it raises output. Unenforceable agreements require informal punishment for deviations, including price wars, or a permanent return to competitive pricing. Since informal punishment may or may not be effective, the law against explicit agreements is effective in deterring a range of anti-competitive behaviours.

There is, however, wide scope for parallel pricing behaviour across firms that falls short of an explicit agreement. The difficulties in regulating this behaviour are illustrated by *Atlantic Sugar*.¹⁸ In this case, three collectively dominant sugar companies had maintained similar relative market shares for decades, each firm realizing the same market share it had been allocated during a World War II quota program. The firms were charged with conspiracy. At trial, it became clear that the competitors relied on two pieces of information to maintain parallel, less than aggressively competitive pricing behaviour: their historical market shares, and the posted prices in the lobby of one firm, Redpath, that its competitors could view. The applicable law then, as now, prohibited agreements between competitors to reduce competition. Did the conduct in *Atlantic Sugar* amount to an unlawful agreement?

At trial, the Quebec Superior Court found that the conduct with respect to the price list was simply parallel behaviour, while there was a tacit agreement, and hence possible breach of the law, over historical market shares. The Supreme Court of Canada held that merely parallel behaviour was not a basis for a conviction for conspiracy, and thus

18 *Atlantic Sugar Refineries Co. Ltd. v. Canada (A.G.)* (1980), 54 C.C.C. (2d) 373 (S.C.C.), [1980] 2 S.C.R. 644 [*Atlantic Sugar*].

agreed with the trial judge's holding with respect to the price list. The Court also rejected the finding of a potentially unlawful agreement with respect to historical market shares, recasting the trial judge's finding of a tacit agreement as 'parallelism by tacit agreement.' It further held that to ground a finding of tacit agreement, there must be evidence of communication of an offer and tacit acceptance of that offer.

While doing violence to the concept of a 'tacit agreement' both in its recharacterization of the trial judge's finding and in its description of a communicated offer, the Supreme Court reached an entirely defensible outcome from a policy perspective: merely parallel pricing behaviour is not subject to antitrust punishment; rather, some kind of explicit agreement is necessary. There is no practical remedy for purely parallel pricing behaviour. Suppose that the Court had found that the historical market shares supported an unlawful agreement. How would the three sugar firms behave going forward? Would they ignore their historical shares and their collective interest in maintaining them? Asking profit-maximizing entities not to behave in a profit-maximizing way is not a successful policy strategy. In the end, the only possibly effective remedy for parallel behaviour among oligopolists is price regulation. Unless the state is willing to assume responsibility for setting prices in a vast range of industries with possibly oligopolistic tendencies, the law should refrain from intervention in almost all cases of purely parallel pricing behaviour.¹⁹

A variety of practices exist that do not reflect or encourage explicitly collusive behaviour between would-be competitors but, rather, discourage vigorous competition between the competitors even if adopted unilaterally. Facilitating practices are strategies adopted by oligopolists that facilitate supra-competitive prices in an industry. There is no exhaustive list of such practices, but the following are some examples. In a market with otherwise difficult to detect prices, sellers may adopt policies that publicize prices. Redpath's posting of a price list in its lobby, for example, rendered pricing more transparent, which facilitated more cooperative pricing outcomes among the oligopolists. Sellers might also offer price-matching guarantees. These serve two purposes: first, they enlist buyers

19 There is only one context in which antitrust law can and does address purely independent but parallel behaviour (the so-called oligopoly problem): competition policy can take steps to ensure that an oligopoly structure that gives rise to the threat of parallel behaviour does not emerge in the first place. While breaking up existing oligopolies is wholly impractical, merger review allows the authorities to prevent a merger that would allow a significantly greater risk of anti-competitive parallel behaviour. Merger review is not without its challenges, in that it is anything but straightforward to determine the likely competitive impact of a merger, but it does offer one practical remedy for the oligopoly problem in those cases where a concentrated market would, in the absence of antitrust regulation, come about through mergers.

as monitors of rivals' prices; and, second, they commit the seller to punishing the rival for dropping its price by responding with an equally low price. The latter effect is even stronger if the seller commits to beat the rival's price by some percentage. Sellers might also offer most-favoured-nation (MFN) clauses to buyers, guaranteeing to the buyer that it will receive as low a price as that paid by any other customer, even on a going-forward basis. Such clauses reduce the seller's incentive to lower prices to future buyers: the seller must not only sell at lower prices to the future buyer but also must rebate the past buyer with the MFN clause. By raising the cost of price cuts, MFN clauses collectively adopted by an oligopoly can stabilize high prices.²⁰

It is important to appreciate that such practices are not always, or even often, used to facilitate supra-competitive prices. Rather, they all have efficiency motivations – in particular, reducing the buyer's risk of overpaying relative to market conditions – that make them unobjectionable in most cases. But facilitating practices can dampen competition and raise prices in oligopolies in some circumstances.

Facilitating practices raise policy questions that are distinct from those engendered by the basic problem of parallel but non-collusive oligopoly pricing behaviour. The crucial difference between policy toward facilitating practices and policy toward direct high pricing is that there is a clear remedial choice with the former: the authorities can order a practice to stop, or not. In the case of prices, it is obvious that the remedy is not a binary matter. Firms need to set prices; the question is what price is too high. This effectively requires the constant monitoring and industry expertise associated with price regulation. Just as authorities can order a single dominant firm to cease to impose exclusionary clauses in its contracts (see, *e.g.*, *Nielsen*²¹), the authorities have a clear remedial target with facilitating practices. As a consequence, there is reason for antitrust law to restrict adoption of facilitating practices where they lessen competition, recognizing that authorities should be cautious in reaching such a conclusion.

There is a caveat. The fact that remedies are available with respect to facilitating practices does not ensure a solution to the oligopoly problem; parallel pricing may survive even in the absence of any given facilitating practice. The point of the remedy, however, is to make the probability of an uncompetitive outcome smaller. This is a perfectly valid basis on which to order a remedy, and it is consistent with other antitrust areas. Exclusive contracts, for example, may be sufficient but not

20 See Edward Iacobucci, 'Most-Favoured Nation Clauses and Competition Policy' [1997] *Can.Comp.Rec.* 27.

21 *Supra* note 16.

necessary to deter entry, yet antitrust authorities make orders against them nevertheless.²²

v *Joint dominance: Oligopoly and exclusion*

We know from our discussion above that there is a basis for regulating exclusionary contracts entered into by a single dominant firm and buyers (alternatively, upstream suppliers) that are, from case evidence, exclusionary and anti-competitive. We also know that within a tight oligopoly high prices can be stable as a result of explicit or tacit coordination among firms in circumstances where there are exogenous or inherent barriers to entry. An exclusionary abuse of joint dominance case arises where oligopoly members both keep prices high *and* are able to establish and maintain entry barriers via exclusionary contracts or other devices to protect their supra-competitive profits. A theory of an exclusionary abuse of joint dominance is a theory of oligopoly with endogenous entry barriers. This theory is relevant where inherent barriers to entry are not sufficient to deter entry, so jointly dominant firms exert some effort to raise barriers to entry or to induce the exit of firms outside the jointly dominant group.

Exclusionary joint abuse of dominance would appear, then, to introduce an additional dimension beyond price that requires oligopoly coordination: member firms must jointly establish contracts that would not otherwise be struck (*i.e.*, that would not otherwise be efficient for the contracting members). The additional dimension of coordination needed for joint abuse would appear to invite an additional dimension of free-riding by cartel members and, therefore, reduced stability of the cartel.

The key question in this area is the same for both positive economics and antitrust policy: Does the additional dimension of coordination

²² The *Nielsen* case, *ibid.*, illustrates this point. In that case Nielsen entered into exclusive supply contracts for a key input, scanner-based data from supermarkets, and this was itself sufficient to ensure that a rival, Information Resources Inc., could not enter the market. In response to this exclusionary behaviour, the Competition Tribunal found an abuse of dominance and, *inter alia*, ordered Nielsen to stop agreeing to exclusive supply contracts with the supermarkets. While the contracts Nielsen had with the supermarkets were no longer exclusive, the supermarkets did not sell to IRI and thus facilitate competition downstream. Collectively, the supermarkets were likely better off continuing to realize a share, perhaps the larger share, of Nielsen's downstream monopoly profits than facilitating a duopoly downstream that would have lower total profits to share. Thus, while the remedy in *Nielsen* allowed the possibility of competition, it could not guarantee it. This was not a reason not to make the order in that case, and it is not a reason not to make orders against facilitating practices where they are determined to increase the probability of uncompetitive behaviour.

needed for joint abuse by an oligopoly, in the form of erecting contractual barriers, diminish the probability of success to the extent that joint dominance should not be an important policy concern? Or can an oligopoly sustain cooperative behaviour both in the dimension of pricing within the market and in establishing contractual barriers to entry? Here and in Part VI below, we bring both theory and case evidence to bear on these questions. The key theoretical argument is that the additional dimension of free-riding may be minimal or non-existent and that, therefore, joint abuse of dominance is plausible.

Two specific arguments capture the general point that abuse of joint dominance is plausible. Our first proposition is that under some circumstances, the best response by any individual cartel member to the adoption of exclusionary contracts by other cartel members will be to adopt the same contracts. By 'best response' here we mean the response that maximizes immediate profits. The dynamics, in particular the threat of reversion to intense competition, that support the coordinated equilibrium in a classic tacitly coordinated oligopoly are not necessary.

To develop this proposition, consider the example in Part III above in which an entrant needs at least fifteen free buyers to cover the fixed costs of production, and the single incumbent firm signs up all but thirteen buyers (or even more buyers) to long-term contracts at the cost of only a small bribe to each. Replace the single firm in this explanation with two incumbents who are successful at (tacitly²³) coordinating their pricing within the market. The entry of an additional firm would at a minimum require the two incumbents to share the profits from coordinated pricing and would also jeopardize the stability of supra-competitive pricing. The offer of long-term contracts by each incumbent, the total of such long-term contracts being sufficient to deter entry, is a Nash equilibrium, because it is in the individual interest of each incumbent to deter entry. The costs of deterring entry via long-term contracts are small, in this example of exclusionary contracts, because of the collective-action problem across buyers: a free-rider problem among buyers induces buyers to accept exclusivity in exchange for a trivial benefit. The free-rider problem related to the establishment of barriers to entry can be small or non-existent.

Our second proposition is that in a broader range of circumstances, contracts or strategies that are adopted by cartel members as facilitating devices to aid in sustaining the cartel price can serve simultaneously to deter entry. As one example, consider a right-of-first-refusal clause in which the seller has the opportunity to match any offer a buyer receives from a rival seller. Such clauses tend to keep prices high by informing

23 We focus on tacit coordination because explicit coordination is a clear violation of conspiracy laws, rendering the question of joint abuse less relevant.

each oligopolist of price cuts by rivals and by allowing sellers to match their rivals and thus punish any attempt to steal business. Moreover, the clauses tend to exclude new entrants, for the same reason: incumbents have the right to match prices and exclude competitors, which discourages attempts at entry. There is no cost to an individual seller from adopting such a clause, and thus there is no free-rider problem among firms in exercising joint dominance in this manner. There is, however, a collective-action problem for buyers: each may accept the right-of-first-refusal clause, despite its anti-competitive effects, reasoning that its individual acceptance will have little effect either on market prices or on entrants.

A second example of a practice that combines cartel facilitation and entry deterrence is the staggering of contracts. The term 'staggered contracts' refers to the design of *some* contracts as long term with the effect that not all contracts terminate on or near the same dates. Staggered contracts enhance the stability of a cartel, because a cheater on the cartel cannot capture the entire market in the short run by reducing price; it can capture only those consumers free of long-term contractual obligations. The share of consumers captured by cheating before the cheating is detected may be small when contracts are staggered.²⁴ Staggered contracts can also act as a barrier to entry. If all contracts ended at or near the same date, then an entrant could capture a substantial market share in a short time through a low-price offer, justifying the investment in entry costs; but when contracts are staggered, the entrant may be forced to wait longer to accumulate enough customers to cover its fixed cost. The staggering of contracts was an issue in *Nielsen* (although in this case it was the upstream contracts with suppliers, not the downstream contracts with buyers, that were staggered). Note that the staggering of contracts would potentially be remedied not through a requirement that all contracts end on the same date but by a prohibition on long-term contracts.

We have found that exclusionary abuse of joint dominance is, as a matter of theory, possible in any market that meets both (1) the conditions allowing tacit coordination of prices and (2) the conditions that would allow exclusionary strategies in the hypothetical case of a single firm. That is, the 'jointness' of the dominance does not necessarily introduce an important new free-rider problem in the oligopoly – beyond, that is, the traditional free-riding problem that constrains coordination *within* the market.

In fact, under some conditions the incentive to deter entry may be *stronger* when there are multiple incumbents. There are at least two arguments supporting this conjecture. First, it may be that a cartel collectively has more to lose from entry than a monopolist would. The stability of a cartel or tacit

24 The game-theoretical basis for this claim is provided in a recent working paper: James Dana & Yuk-fai Fong, 'Long-Lived Consumers, Intertemporal Bundling, and Tacit Collusion' (Northwestern University, 2008) [unpublished].

agreement is decreasing in the number, n , of members of the cartel or agreement, since the incentives to cheat on the agreement are higher with increasing n : the percentage increase in market share that can be captured by cheating is higher, and, in addition, the chance that other firms will want to disrupt the market by punishing the cheater is greater. It may well be, for example, that a tacit agreement could be sustained between two firms but not three. In this case, therefore, the prospect of a third firm's entering the market is particularly costly to the incumbents, and the incentive to deter entry via abusive practices may be stronger with two incumbents than with only one. Second, multiple incumbents may have stronger incentives to exclude because cartel members have incentives to adopt exclusionary facilitating practices, such as staggered contracts, in order to coordinate a cartel, while a monopolist clearly does not need such practices to stabilize pre-entry pricing. Oligopolists, but not monopolists, may be motivated to adopt practices that exclude entrants even without considering their effect on entry.

As we discussed in Part IV above, competition policy is impotent in the face of tacit coordination, because there is no remedy that can be practically implemented in this context; firms cannot be ordered to price more competitively or to ignore their rivals' strategies. By contrast, as we have shown, in cases of the abuse of joint dominance there is a basis for restricting exclusionary practices on the part of oligopoly members even when these practices relate to tacit coordination.

VI Case study

Based on facts that can be inferred from the consent agreement in *Waste Services*,²⁵ the facts of this case support the predictions of the theory. Under the commissioner's theory, two firms, operating in a market in which a single firm had historically been found liable for abuse of dominance,²⁶ were dominant in several markets for commercial waste services.²⁷ The consent order requires the firms to refrain from various contractual practices such as contract terms greater than two years or renewal terms greater than one year, lengthy and limited termination notice periods for buyers, rights of first refusal, obligations to divulge information about offers from third parties, substantial liquidated damages, and requirements to provide notice of and reasons for any increase in price.

25 *Supra* note 3.

26 See *Director of Investigation and Research v. Laidlaw Waste Systems Ltd.* (1992), 40 C.P.R. (3d) 289 (Comp. Trib.).

27 None of the competition commissioner's conclusions was admitted to by the firms that were party to the consent agreement.

The contractual terms that were in place, as inferred from the agreement, can potentially serve as both facilitating devices and exclusionary devices, in that they deter significant entry or growth by firms other than the two dominant firms. The right of first refusal protects each firm against undercutting, both by its rival within the market and by other, smaller firms or new entrants. The obligation to inform a supplier about offers from other parties both enhances the stability of the within-market coordination (by shortening the time required to detect 'cheating') and frustrates any attempt to enter or expand on the part of a small firm. The longer contract terms ensure the staggering of contracts, which can dampen the competition between the two incumbent firms in the market by lessening the incentive for each to undercut the other, as the short-term gains from undercutting are reduced by the limited number of free buyers. And the staggered contracts limit the ability of entrants and small firms to achieve a significant market share even when these firms have costs no higher than the incumbents'.

VII *Conclusion: Evaluating the law and the 2009 Guidelines*

The 2009 Draft Guidelines reversed course with respect to non-exclusionary facilitating practices, removing them from scrutiny as a potential abuse of a jointly dominant position. The 2009 Draft Guidelines also reversed course with respect to joint exclusionary practices, holding that merely parallel behaviour is sufficient to attract a remedial order where the practices in question substantially lessen competition. The second reversal is appropriate from a policy perspective: firms may have incentives independently to adopt strategies that deter entry or otherwise harm rivals and competition, and these strategies, such as exclusive contracts, are susceptible of remedies. These contentions are illustrated by the *Waste Services* case and the consent agreement that resulted.

The decision to exclude non-exclusionary facilitating practices from scrutiny for joint abuse, on the other hand, does not have a sound basis. If facilitating practices are not reviewed under abuse of dominance, there is no legal justification for making an order against them. Section 45 concerns conspiracies and agreements,²⁸ and facilitating practices need not manifest an agreement, nor do they necessarily facilitate an agreement within the meaning of that section and the case law (see, e.g., *Atlantic Sugar*²⁹). But facilitating practices may lessen competition,

28 Section 90.1 on civil agreements was recently added to the Competition Act. It speaks of 'agreements and arrangements' between the parties, which also contemplates some kind of explicit coordination between the parties. Thus, while we focus on s. 45 in the text, the same analysis would apply to s. 90.1.

29 *Supra* note 18.

are plausible in practice, and are remediable. It therefore does not make sense for antitrust authorities never to consider them. Canada used to get it right in its abuse guidelines by considering facilitating practices as a possible abuse of joint dominance. Now Canadian law gets it wrong.

It is important, however, to recognize the source of the problem. The Competition Bureau is bound by its statute and by precedent; and s. 45 and precedents such as *Atlantic Sugar* suggest that facilitating practices cannot be considered under the conspiracy provision, at least without an accompanying explicit agreement. There is thus no legal room in Canada for the authorities to address facilitating practices under s. 45. Moreover, precedent also renders facilitating practices outside the ambit of s. 79. Section 78 lists a non-exhaustive, illustrative list of practices that could amount to an abuse of dominance. The Competition Tribunal, in interpreting ss. 78 and 79 together, concluded that the common feature of the enumerated practices in s. 78 is that they have an intended effect on rivals that is exclusionary, predatory, or disciplinary.³⁰ The Competition Tribunal moves from this observation to a conclusion that any act *not* enumerated in s. 78 that is alleged to be an abuse of dominance pursuant to s. 79 must also have an effect on rivals that is exclusionary, predatory, or disciplinary.

The problem with the tribunal's approach is that it potentially excludes anti-competitive behaviour that benefits a group of potential rivals collectively at the expense of their customers. That is, behaviour that is collusive or otherwise dampening of price competition is outside the scope of s. 79 on the tribunal's approach. For example, in *NutraSweet*, there was a complaint that NutraSweet, which had a clearly dominant position in the market for the artificial sweetener aspartame, had abused its dominant position by entering into an agreement with a potential rival, Ajinomoto, according to which Ajinomoto would not enter the Canadian market. The Competition Tribunal rejected the complaint, noting that cooperative behaviour is outside the scope of the abuse provisions, since it does not have an intended negative exclusionary, disciplinary, or predatory effect on a rival. Under this interpretation of ss. 78 and 79, there is no room for the Competition Bureau to bring a complaint against facilitating practices adopted by a group of firms, since facilitating practices have a beneficial, not a negative, effect on rivals.³¹ The bureau's reversal on facilitating practices in the 2009 Draft Guidelines is therefore not justified from a policy perspective, but it is consistent with prevailing case law.

30 See, e.g., *NutraSweet*, supra note 2.

31 It might be argued that certain facilitating practices, such as meeting-competition clauses, support higher prices by having a disciplinary effect on rivals. But the rivals who are subject to this discipline welcome it, since it helps stabilize supra-competitive pricing, which removes such a clause from consideration as a disciplinary practice that has negative effects on a competitor.

The Tribunal's interpretive approach is by no means dictated by ss. 78 and 79. Section 78 provides only a non-exhaustive list of potential abuses of dominance, so does not on its face exclude facilitating practices as a potential abuse of dominance. Given that s. 79 is a catchall provision that explicitly contemplates anti-competitive conduct by jointly dominant firms, that there is no other provision that addresses facilitating practices, and that facilitating practices can allow jointly dominant firms to substantially lessen competition, it would be preferable to interpret s. 79 in a more purposeful, substantive way that would address facilitating practices.

It is apparent, however, that the Competition Tribunal and the courts are unlikely to deviate from this narrow approach to s. 79 at this point. *Canada Pipe* illustrates the formalistic approach that dominates s. 79 jurisprudence.³² In that case, the Federal Court of Appeal carefully parsed each subsection of s. 79, coming to some remarkable conclusions. For example, s. 79(1)(b) asks whether a dominant firm (or firms) has committed a practice of anti-competitive acts, while s. 79(1)(c) contemplates an order by the tribunal wherever the practice lessens competition substantially. In *Canada Pipe*, a dominant firm argued that its marketing scheme, which had been alleged to be abusive of dominance, was designed to bring efficiency benefits to its customers. The Court held that a positive effect on consumers does not negate a finding of an anti-competitive act under s. 79(1)(b), since it would not negate an intended exclusionary, predatory, or disciplinary effect of that practice, which is the subject of investigation under s. 79(1)(b). Efficiency motivations are considered only under the substantial lessening of competition analysis that arises under s. 79(1)(c). By parsing the language of the statute in such a formalistic way, the Federal Court of Appeal established a precedent that allows a finding of a practice of anti-competitive acts under s. 79(1)(b) that is beneficial to consumers and does not lessen competition under s. 79(1)(c). As Michael Trebilcock forcefully argues, this precedent is wrong-headed.³³

With such a formalistic precedential backdrop to s. 79 interpretation, it was appropriate for the Competition Bureau to omit facilitating practices as a potential abuse of joint dominance in its 2009 Draft Guidelines. But this does not mean that such a move has a strong basis in policy. Either through a rethinking by the courts of their jurisprudence or through a statutory amendment, the law should evolve in a manner that allows it to address facilitating practices. As of this moment, there is an unfortunate lacuna that reform should address.

³² *Canada (Commissioner of Competition) v. Canada Pipe Co. Ltd.*, 2006 FCA 233.

³³ Michael Trebilcock, 'Abuse of Dominance: A Critique of *Canada Pipe*' [2007] Can.Comp.Rec. 1.

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