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Canada Pipe Prevails in Abuse of Dominance Case Commissioner of Competition to Appeal

By Kim Alexander-Cook

On February 14, 2005 the Competition Tribunal released its decision in the abuse of dominance and exclusive dealing case brought by the Commissioner of Competition against Canada Pipe in 2002.¹ The main conduct at issue was a loyalty program comprised of rebates and purchase discounts to distributors who offered Canada Pipe's Bibby Ste-Croix division exclusivity in supplying their cast iron drain, waste and vent (DWV) requirements. The Commissioner alleged that this program worked to substantially prevent competitors from gaining access to Canada Pipe's distributors and sought an order that would eliminate the program. The Tribunal accepted that Canada Pipe held a dominant position in the relevant markets, but concluded that Canada Pipe's conduct was not intended to have a negative effect that was predatory, exclusionary or disciplinary on competitors, did not prevent or lessen competition substantially, and was not likely to do so. On March 8, 2005, the Commissioner announced her intention to appeal the Tribunal's decision in the case.

While the Tribunal's decision in Canada Pipe does not significantly alter abuse of dominance or exclusive dealing law in Canada, it does reinforce the evidentiary burden on the Commissioner to demonstrate to the Tribunal that the alleged anti-competitive behaviour has or is likely to have substantial adverse effects on competition in order for the conduct of a dominant competitor to be found to violate the *Competition Act* (the *Act*). In Canada, dominance and exclusivity programs alone are not enough to constitute "abuse." The Tribunal's position is consistent with the

BILL C-19: off again-on again

On March 9, 2005 The House of Commons Standing Committee on Industry, Science and Technology resumed consideration of Bill C-19, which proposes to amend the *Competition Act* by creating, among other things, stiff fines for abuse of dominance and misleading advertising practices.

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¹ Commissioner of Competition v. Canada Pipe Company Ltd., 2005 Comp. Trib. 3 (Competition Tribunal).

general approach of U.S. courts in recent cases concerning exclusive dealing and loyalty programs (see, for example, *Dentsply*² and *Virgin Atlantic*³). It can be contrasted, perhaps, with the approach taken in some European cases, wherein it has been held that “it is not necessary to demonstrate that the abuse in question had a concrete effect on the markets concerned” but only that it is capable of or likely to do so.⁴

Markets and Market Power

The Commissioner successfully argued that the markets for cast iron DWV products are distinct from those of plastic DWV products. In this regard, the Tribunal was convinced that there were certain applications in which cast iron products were favoured and enjoyed a significant price advantage, and that price competition between plastic and cast iron products was weak as compared to price competition amongst cast iron products. The Tribunal also found that within the cast iron DWV category there existed three distinct markets – pipe, fittings and MJ couplings. As for geographic markets, the Tribunal concluded that there existed substantial price variations across different regions in Canada, such that six regional markets in Canada were indicated.

The Tribunal came to the conclusion, based on both direct and indirect evidence, that Canada Pipe had market power in all six regions for all three products. The Commissioner provided direct evidence of both relatively high profit margins for two of the three DWV products as well as differential pricing across regions, correlated with the degree of competition in each. As for indirect evidence, the Tribunal found that while the evidence of barriers to entry was not conclusive, Canada Pipe’s high market shares of 80-90%, its range of products, its national presence and the limited penetration by competitors in this low-growth market were sufficient to establish that Canada Pipe controlled a substantial part of each market.

Practice of Anti-Competitive Acts

Under s.79 of the *Act*, the Commissioner is required to show that the dominant competitor has engaged in a “practice of anti-competitive acts” resulting in or likely to result in a substantial lessening of competition. The main allegation of the Commissioner was that the “Stocking Distributor Program” (SDP) of Canada Pipe “locked in” distributors, foreclosing competitors from distribution in each of the relevant markets. The Commissioner also alleged that past acquisitions and associated restrictive covenants had foreclosed competition. The Tribunal dismissed these latter allegations rather summarily. It noted that the last acquisition of Canada Pipe had occurred in 1998 and that new competitors had since entered the market and others had increased their sales. As regards the covenants restricting key individuals from acquisition targets from competing with Canada Pipe, the Tribunal found nothing out of the ordinary or unreasonable about their duration and scope.

The SDP rewarded a stocking distributor with rebates and discounts if it stocked exclusively Canada Pipe DWV products. The discounts varied across products and regions, but could result in a reduction of more than 40% in the price paid by the distributor. Quarterly and annual rebates could amount to more than 15% in some cases. The SDP did not involve a signed contract, but did require a minimum purchase that applied equally to small and large distributors.

The key issues the Tribunal addressed in concluding that the SDP did not comprise a practice of anticompetitive acts were the contractual nature of the SDP, its business justification, its impact on Canada Pipe’s competitors and switching costs.

² *United States v. Dentsply International, Inc.*, No. 03-4097 (3d Cir. 2005).

³ *Virgin Atlantic v. British Airways, PLC*, 257 F.3d 256 (2d Cir. 2001).

⁴ See, for example, *British Airways plc v. Commission*, T-219/99 [2003] E.C.R. 00000, 2003 E.C.J. CELEX LEXIS 659 (Dec. 17, 2003) at para. 293. This case is currently under appeal.

In the Tribunal's view, the SDP did not pose a significant contractual obstacle for distributors that wished to switch suppliers. While remaining or leaving the program would involve a cost-benefit analysis, the terms were transparent and there were no legal repercussions for leaving. The Tribunal also found that Canada Pipe has a *bona fide* business justification in using the SDP. While the Tribunal rejected as irrelevant Canada Pipe's argument that the SDP encourages competition between distributors (because it does not disadvantage smaller distributors), it accepted that the SDP was instrumental in allowing Canada Pipe to maintain more complete product lines. This meant that certain products were made available to distributors and end-customers through the SDP that might not have been made available without it.

As regards switching costs, which experts from both sides agreed would be the determining factor, the Tribunal found that although the SDP was an attractive program for a distributor, it did not prevent the distributor from considering other options, or from purchasing elsewhere if it were more advantageous to do so. Canada Pipe successfully argued that switching costs were zero at the end of each year of the SDP, and relatively low at the end of each quarter. In addition, the Tribunal found that distributors stayed with Canada Pipe for reasons other than the SDP, such as reliability, and that the size of the market did not warrant searching for another supplier.

Finally, the Tribunal found the "most striking argument" against the Commissioner's allegations to be the fact that the SDP had not prevented competitive entry from occurring in certain regions. In particular, it had not prevented an increase in imports of cast iron DWV products and even the emergence of a new manufacturer of the products. While the Tribunal found that entry might be difficult, the difficulty was not related to the SDP, but to other factors – namely that Canada Pipe is a known manufacturer with a complete product line and that the market for cast iron DWV products is not a growth market. Based on these findings, the Tribunal concluded that the SDP did not constitute a practice of anti-competitive acts, and thus no order was justified.

Substantial Lessening or Prevention of Competition

On the theoretical assumption that the Tribunal had erred in this assessment, it also went on to find that even if the SDP did constitute a practice of anti-competitive acts, it did not substantially lessen or prevent competition in any of the eighteen separate markets. In this regard, the Tribunal identified that there was significant evidence of competitive pricing in some regions due to imports and the emergence of a new manufacturer, and insufficient evidence about competition in other regions to support a conclusion that the SDP had lessened or prevented competition there.

Exclusive Dealing

In addition to abuse of dominance under s.79 of the *Act*, the Commissioner had alleged a violation of the exclusive dealing provision under s.77 of the *Act*. The Tribunal found that the SDP indeed constituted a practice of exclusive dealing. However, for the same reasons that it rejected the Commissioner's s.79 allegations, it also found that the Commissioner failed to establish that the exclusive dealing practice impeded entry, was likely to impede entry, or had substantially lessened competition in the relevant markets.

Competition/Antitrust Group Activity

Members of Stikeman Elliott LLP's Competition/Antitrust Group will be attending the **53rd Spring Meeting of the ABA Section of Antitrust Law** on March 30 – April 1, 2005 in Washington, DC.

Paul Collins, Chair of Stikeman Elliott's Competition Law practice group, will speak at **The Canadian Institute's Advanced Forum on Mergers & Acquisitions** being held April 14th-15th, 2005 at the Marriott Bloor Yorkville, 90 Bloor Street East (Toronto, Ontario). The session is entitled "Impact of the Competition Act and Investment Canada Act on Your Transaction"

On April 18, 2005 Mr. Collins will be in Toronto at the **2005 CCCA National Spring Conference**. He will be speaking on "International Competition Law Compliance for Multinational Operations."

Susan Hutton, a partner with Stikeman Elliott's Competition Law practice group in Ottawa, will speak at the **Essentials of Competition Law Conference** sponsored by the Ontario Bar Association, to be held on May 9, 2005 at the OBA Conference Centre at 20 Toronto Street, Toronto, Canada. Go to www.softconference.com/oba for more information or to register on-line.

Mr. Collins will also be at the **International Competition Law Conference** sponsored by Insight, to be held on June 16 and 17, 2005 at the Hotel Inter-Continental in Montreal, Canada. Go to www.insight.com for more information.

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