

The Purpose, Operation and Effect of the Export Exemption Provisions of the Combines Investigation Act (Section 32(4) and (5))

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Commentary

Citation Information

McIntyre, Robert D. "The Purpose, Operation and Effect of the Export Exemption Provisions of the Combines Investigation Act (Section 32(4) and (5))." *Osgoode Hall Law Journal* 3.1 (1964) : 106-115.
<http://digitalcommons.osgoode.yorku.ca/ohlj/vol3/iss1/10>

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THE PURPOSE, OPERATION AND EFFECT OF THE EXPORT EXEMPTION PROVISIONS OF THE COMBINES INVESTIGATION ACT. (SECTION 32(4) and (5)).

The export exemption provisions, section 32(4) and (5) of the *Combines Investigation Act* resulted from political, economic and legal circumstances which must be delineated in order to understand the intended operation of the provisions. This purpose will be accomplished by stating the problem which arises from the export exemption provision, outlining the historical reasons for its enactment, examining its operation, and comparing its content briefly with the United States Webb-Pomerene Act.

(a) *Problem*

The export exemption provisions permit Canadian firms to cooperate for the promotion of their exports. The provisions state generally that the court shall not convict the accused if the concerted arrangement relates only to the export of articles from Canada, providing the arrangement does not result in restraint on any exporter not a member of the arrangement, or in a lessening of competition unduly in relation to an article in the domestic market.¹

Proponents, on the one hand, would state that as Canada is necessarily one of the largest trading nations in the world, we must keep abreast of the mid-twentieth century economy and recognize that it is only by some concerted arrangement that Canadian industries faced by foreign cartelization, as exemplified by the European and Japanese giants, can obtain the larger production runs necessary for competitively priced products; consequently the export exemption provisions are a recognition of economic reality.² They might state, too, that the export amendment is also a statutory articulation of implicit law, and taken by itself, could be regarded as a contribution to increased certainty in the anti-combines policy.³

Critics, on the other hand, would state that the export exemption in subsection (4) of section 32 is so restricted by the qualifications of subsection (5) that it renders the former virtually useless except as a source of future litigation. They contend that the amendment has weakened the general attitude of the business community to the legislation⁴ (through the probable effect on the domestic market) and replaced the former uncertainty with a certainty, which has resulted in a weakening of the entire legislation.⁵

In the middle, are those who would assert that in the past there have been no prosecutions of combinations entered into for export

¹ Combines Investigation Act, R.S.C., 1952, c. 314 as am. by 1953-4, c. 51 and 1960, c. 45, s. 32(4) and (5). Note: Appendix "A" of this article.

² H. of C. Debates, 1960, vol. VII, 6974.

³ Brecher, *Combines and Competition: A Re-appraisal of Canadian Public Policy* (1960), 38 Can. Bar Rev. 523, 592.

⁴ H. of C. Debates, 1960, vol. VII, 7361.

⁵ Brecher, *supra*, footnote 3, at pp. 592-3.

purposes; thus an export exemption provision is unwarranted in light of history. They also point out that the general test of illegality found in section 32(1) is sufficient to cover export combinations. Or, in the alternative, assuming clarity and certainty are desired, *ad hoc* exemptions should be permitted when circumstances indicate that export trade would in fact be promoted by allowing co-operation.⁶

(b) *Development*

In the House of Commons in 1960, the Hon. Davey Fulton, the then Minister of Justice, introduced amendments to the *Combines Investigation Act*.⁷ After stating the policy of the Conservative government which prompted the amendments, Mr. Fulton explained what the bill sought to accomplish.⁸

First it is designed to improve the existing provisions of the legislation by way of clarification and consolidation, and second, it is designed to bring the law in important particulars into line with the twentieth century developments and to adapt it to the problems and situations of the twentieth century economy.⁹

After the third reading, assent was given to the export exemption provisions which are now found in sections 32(4) and (5) of the Act. The Minister explained the proposal in part as follows:¹⁰

. . . First, whether we like it or not, in international trade there is a tendency toward association or cartelization, and whether we like it or not this is the situation within which our industry must compete for markets in international trade.

Second, and even more imponderable but I think even more serious, is the fact that in international trade we are now coming into a situation where we are faced with the massive communist organization, represented by the Union of Soviet Socialist Republics, as a competitor and increasingly this great force is entering into international trade with the whole weight of the state behind it. This state organization is prepared to do anything to obtain markets for its exports and to eliminate markets for exports from other countries, particularly the western world with which, ideologically, the Soviets are in conflict.

They (Canadian industry) have represented to us that if laws are retained in all their rigidity which certainly raises a very real question about the legality of the right to organize in export trade, then they are going to be at an increasing and permanent disadvantage.

The problem, rather, is one of disagreement on the desirability of doing something to remedy the situation, one of finding some method of amending our legislation so as to make it clear that what may be done in the export field may be legitimate but must not be allowed to spill over and have adverse effects on the domestic economy.

⁶ Brewster, *Antitrust and American Business Abroad*, 1958 at p. 354.

⁷ H. of C. Debates, 1960, Vol. IV, 4340. Mr. Fulton stated that "what we have presented to the house, are amendments to the combines legislation, not a general revision," and further ". . . that a general revision would require, possibly a Royal Commission and at least a study of the principles of the legislation by a parliamentary committee." The Bill, he stated, "proceeds on the inherent soundness of the principles of the present anti-combines legislation."

⁸ H. of C. Debates, 1960, vol. IV, 4341.

⁹ *Ibid.*, at p. 4345.

¹⁰ H. of C., Debates, 1960, vol. VII 6971-2. See also D. H. W. Henry Q.C. Notes for an address to the International Business Management Course, Waterloo University, March 1963, at p. 11.

The result of this discussion has been that we have been able to devise an amendment which I believe will accomplish the result of making it clear that arrangements entered into by Canadian industry, having effect exclusively with relation to their activities in the export markets, may be exempted from the operation of this act, provided again that they do not have the indirect result, whether intentional or unintentional, of producing a disadvantage to Canadian consumers.

Considering the political and economic context alluded to in the speeches of Mr. Fulton and other members of the House of Commons, the curious element is the fact that the emphasis for discussion purposes centred around primary industries, namely lumber and fishing. Yet, one would have thought that more emphasis in the discussion would have been placed, in general, on secondary industries and, in particular, on small businessmen as important benefactors of an export exemption amendment.

In order to appreciate better the operation of the provisions, they will be looked at in the context of their development. The Minister of Justice explained that the proposed subsection (4) of the amendment made it clear that in general a charge under this act may be defended if it relates to activity or arrangements concerned with the export of articles from Canada.¹¹

Mr. Fulton, in discussing subsection (5) (a) stated:

Since industry says . . . that they are concerned in increasing their success and increasing the volume of Canada's export trade, we think it would be most unsound for us to leave them an umbrella under which they might in fact make merely a comfortable arrangement by which they establish their position based upon present demand for sales in the export market but do not bother to compete for an increased share in it. The arrangement must not be allowed to freeze or decrease the volume of exports from Canada."

Referring to paragraph (b), he stated:

If we do not provide that (*i.e.* subsection (5) (b)) it might be the case that unscrupulous persons would be able to make their own arrangements in the export field, under the protection of sub-clause (4), and then having worked out a comfortable arrangement say this: We are not going to have competition; we do not like you so you must stay outside. Then ultimately they would be able to drive that person out of competition at least in the export field if not, indeed, in the domestic field.

Referring to paragraph (c), he stated:

The object of the protection (*i.e.* subsection (4)) is to encourage industry in export and to enable them to improve their position. Therefore it must not be allowed to be used by them to prevent somebody else from getting into this field because that would have the opposite effect to the purpose for which it was designed.

Referring to paragraph (d) he stated:

It must not be allowed to operate or they must not be able to get protection under it if in fact the result of their arrangements is to lessen or is likely to lessen competition unduly in relation to an article in the domestic market. I think that last paragraph speaks for itself¹²

¹¹ H. of C. Debates, 1960, vol. VI at p. 6973.

¹² *Ibid.*

(c) *Operation*¹³

The first major point to consider in connection with any proposed concerted arrangement for export purposes is whether or not such an arrangement will, in fact, bring about the desired results. Such desired results may be as follows: a reduction of the average export sales cost per firm, a resultant broader product base to draw on, a better ability to supply those foreign buyers who require a continuous substantial volume of the products or products, a better bargaining position to compete with or deal with foreign cartels and a possible expansion of the volume of production of each of the members which may achieve certain economies of scale, such as the lowering of the cost of the product or products.

The three general types of export organizations that may be used are as follows: (1) one in which the association serves as a central selling agent for all of the members, taking orders, negotiating sales, and handling shipment of the goods; (2) one in which the association directs the activities of its members and retains certain functions in export trade, but the orders are placed by agents already established by the members abroad (in this case the export department of one member may handle foreign orders for several members); and (3) the export company formed for the purpose of buying the members' products and reselling them abroad at terms agreed upon by the members. The first and second methods of selling may be combined, the members using their established agents for some markets and the association sales office for new markets or those in which the trade is not well developed.¹⁴

Assuming at this stage that an export arrangement has been agreed on it is now time to test it against the *Combines Act*. To do so requires an examination of section 32 of the Act.¹⁵ The prohibition against combinations and conspiracies in restraint of trade is to be found only in section 32(1). The prohibitions with which export agreements are mainly concerned are found in the essence of the offence which is stated, in general, to be combinations that prevent or lessen unduly competition in the production, purchase, sale, storage, rental, transportation or supply of commodities. Very broadly speaking, as the courts interpret the Act, whether an agreement to restrict does so *unduly* depends on the extent of market control achieved or sought to be achieved by the agreement and the method of control of such market. If the arrangement is not in breach of this provision, then there is no need to look to the remainder of the section for relief.¹⁶

¹³ D. H. W. Henry Q.C., *supra*, footnote 10.

¹⁴ Brewster, *op cit.*, *supra*, at p. 112.

For a practical application in Ontario of an export consortium formed by businessmen in the fruit and vegetable industry and called FAVPEP, reference D. H. W. Henry's address to the Waterloo Conference, *op. cit. supra*, at p. 19.

¹⁵ For a fuller discussion on this point see D. H. W. Henry, Q.C., *supra*, footnote 10.

¹⁶ D. H. W. Henry, Q.C., *op. cit. supra*, at p. 13.

Subsection (2) of section 32 permits certain defences which in effect are exemptions from subsection (1). Yet even if the arrangement fell within one of the enumerated exceptions it would be permitted to function only as far as it did not lessen competition unduly as expressed in subsection (3).

Subsection (4) states that the court shall not convict the accused if the arrangement relates only to the export of articles from Canada. It is to be noted that this subsection is in the form of a type of defence which assumes firstly that the parties are caught by subsection (1), and secondly that the parties will not be convicted if the agreement relates *only* to the export of articles from Canada.

Subsection (5) limits the defence provided in subsection (4) by stating, in general, that subsection (4) does not apply if the arrangement results or is likely to result in reducing the volume of exports of an article, injuring the export business of any domestic competitor not a member of the arrangement, restricting a person from entering into the export business in Canada or lessening competition unduly in relation to an article in the domestic market. Thus, it can be seen that it was Parliament's intention to assist in the increase of exports from Canada without placing other Canadian exporters at a disadvantage or hurting those companies in the domestic market who are not parties to the combinations.

The question arising at this point is whether or not subsection (5) places such restrictive qualification on subsection (4) so as to render it virtually useless. At present there is no case law on the interpretation of these subsections. On this question D. H. W. Henry Q.C., the Director of Investigation and Research, has stated:

... as an administrator I am obliged to assume that Parliament intended some meaning to be given to the amendment, that it intended the section to be workable and that the limitations on it are not absolute. It is my own view that a *bona fide* scheme to encourage exports can be worked out taking advantage of this provision.¹⁷

It can only be hoped that the courts will give these export exemptions a meaningful interpretation by allowing some latitude in the incidental effect which may occur on the domestic market.¹⁸

Finally, the solicitor, as a practical matter, should advise his client that the client may discuss the proposed arrangement with officials of the Combines Branch if he so desires. On the one hand the client may not wish to reveal his plans and may trust that he will escape detection under our peculiar enforcement policy. On the other hand the client may desire to discuss his concerted arrangement with a view to being informed as to whether or not the combination

¹⁷ D. H. W. Henry Q.C. Notes for an address to The Canadian Manufacturers' Association, 1964, at p. 13.

¹⁸ For a United States decision on this point see *United States v. Minnesota Mining and Manufacturing Company*, 92 F. Supp. 947 (D.C. Mass. Sept. 20, 1950).

is of such a nature that the Director would have to commence an inquiry if the arrangement were undertaken.

(d) *The United States Webb-Pomerene Act of 1918*¹⁹

The Webb-Pomerene Export Trade Act of 1918 was a deliberate effort to allow exporters to band together to pit their combined power to countervail the foreign buying cartels.²⁰ The Act provides that the antitrust laws are not to be construed as declaring to be illegal "an association entered into for the sole purpose of engaging in export trade and actually engaged solely in such export trade, or an agreement made or act done in the course of export trade by such association, provided that such association, agreement or act is not in restraint of trade within the United States, and is not in restraint of the export trade of any domestic competitor of such association." The Act appears to be parallel in its wording to our section 32, subsections (4) and (5).

Any export combination in the United States seeking the benefits of the exemption has to file its articles of agreement with the Federal Trade Commission as well as its annual report on January 1 of each year. The Commission has authority to investigate the activities of associations claiming Webb-Pomerene status and to make recommendations for their reform.²¹ To this extent there is a form of regulatory authority given by the Act to the Commission. The Commission is also obliged to report breaches of their recommendations by the respective combinations to the Department of Justice for possible prosecution. However the Department of Justice can prosecute under the antitrust laws without prior investigation and recommendation by the Commission.²²

In Canada the statute gives no regulatory authority in the sense that it is not provided that a group of businessmen may come to the Director of Investigation and Research or the Restrictive Trade Practices Commission and having disclosed its plan receive a permit or licence or other official sanction for the proposed operations,²³ nor is it necessary to register an export agreement. The Director only moves when he has reason to believe an offence has been committed or is about to be committed and, depending upon the circumstances of his investigation, he can decide whether to take the matter to the Restrictive Trade Practices Commission or to the Attorney-General of Canada.

¹⁹ 1918 Webb-Pomerene Act (15 U.S.C. 62, 63, 65).

Note: This sub-heading is included to bring the reader's attention to the Webb-Pomerene Act—for further discussion of the limited amount of case law under the Webb-Pomerene Act and criticisms of the Act refer to Brewster, *op. cit. supra*, footnote 6.

²⁰ Brewster, *op. cit.* at p. 24.

²¹ *Ibid.* at p. 108.

²² *Ibid.*

²³ D. H. W. Henry, Q.C., *op. cit. supra* footnote 10 at p. 17.

The practical result has been that in the United States there have been very few export combinations formed and only four prosecutions by the Department of Justice as against comparative inaction in Canada. The respective Acts do differ somewhat in their formal requirements and administrative techniques. Still it is submitted that the reason for the inaction is the fact that, whether there is a regulatory authority or not, the *bona fide* export combinations hesitate to execute a concerted arrangement since they are constantly vulnerable from their inception.²⁴

(e) *The Effects of the Export Exemption Provisions*²⁵

Canada is facing serious competitive disabilities in the world markets. Because of this fact, if Canada is to become a dynamically growing industrial nation, Canadian businessmen must turn their attention to the need for more export-oriented patterns of Canadian manufacturing production. Coupled with this is the further fact that Canadian manufacturing industries are relatively small-scale operations.²⁶ With this situation in mind it would seem logical that industry, in particular secondary industry, would take advantage of the export provisions; however, this has not been the case.²⁷ The question why has this not been the case, is as obvious as the answer is obscure.

The general starting point, it may be suggested, is the question of private business control versus government control. Perhaps private business is not able to compete with foreign state control (whether it be either direct cartelization, as in the communist countries, or indirect control, for example, a marketing board, as in some western countries); consequently the government may have to step in and fight state control with state control. However, as Brecher has indicated, most Canadians have thus far chosen to

²⁴ This does not mean necessarily that there should be granted permissive licences to contravene antitrust laws; but what it does mean is recognition of the fact that businessmen desire more certainty in this area of the law. *Quaere* whether this can be obtained?

²⁵ It has been suggested that the export exemption amendment is relatively new and as such there has not been time for it to register any significant effects through its use. Whatever be the reason or reasons for the lack of effects it makes it difficult to draw conclusions. Rather than attempt conclusions it was considered more appropriate to pose for consideration the various areas wherein difficulties may lie. To obtain material for this end the author is grateful to the lawyers and businessmen, involved in this field, who expressed their views when interviewed.

²⁶ Arthur J. Smith, *Trade Prospects for Canada*, Address to the Osgoode Hall Law School Conference on The European Common Market and the Canadian Trade and Investment 1963, at p. 5.

²⁷ For example, suppose company X is one of the members of an "Export Company". Company X has fixed and variable costs to produce 100,000 units of production. Yet, under that same overhead, it can produce another 30,000 units at an expense of only the actual cash costs. This means a larger production run and a lower cost factor; consequently company X can export the 30,000 units at a lower price which it necessarily has to do in order to meet the foreign cartelized competitors in the world market. Also, assuming company X is an Ontario manufacturer, it might well be cheaper to ship to England by boat than it would be to ship to the Canadian west by rail.

believe that private decision-making in competitive industry is the superior general technique for promoting consumer welfare.²⁸ Any extension of direct government operation would have to be justified on solid grounds of public interest. The full measure of adverse potential in the scheme for government-business collaboration is that, if it did not mean ultimate business control, it would probably involve an unlimited and arbitrary exercise of government power.²⁹ Stated roughly it means that government interference is like pregnancy—you can't have just a little of it.

But more specifically one might consider finding the difficulties, which have resulted in a limited use of the export exemption provisions, in one or more of the following three areas—economic, business, or legal. Mr. Henry suggests “that the major obstacles to schemes such as this are economic rather than legal and I can only assume that the apparent lack of activity in this field arises . . . from uncertainty as to whether combining for export is indeed an effective way of penetrating a foreign market where formidable competition exists.”³⁰ Added to this overall factor may be a difficulty for small companies, already hard pressed for capital, to arrange financing for large export orders.

The difficulties in the business area could be divided into two parts. The first problem will be termed an “independent competitive philosophy.” This manifests itself in the businessman who guards his goodwill, trademark, and trade information with great secrecy. As a result it is most difficult to gather together these independent-minded competitors into a concerted arrangement particularly, for example, where they might have to submerge their products beneath a common label. The second problem is that of export organization and documentation; this would include familiarity with import and export permit regulations, customs tariffs and valuation for duty, marking and labelling requirements, packaging and the “paper” work involved in documentation. Canadian businessmen may be unable to cope with these problems whether through ignorance or possible lack of facilities. What may be needed is a process of re-thinking in terms of the export markets and not just the domestic market. The point to note is that if an “Export Company” was formed, by the members pooling their resources, this export company could collectively handle these problems whereas the individual member could not.

The difficulties in the legal area are much too wide to be dealt with in detail for the purposes of this article. By this is meant that the export exemption provisions as an integral part of the *Combines Act* are necessarily affected by the criticisms businessmen and lawyers levy against the Act in general. This includes the philosophy behind the Act, the method of its enforcement, the constitutional

²⁸ Brecher, *op. cit.*, *supra*, footnote 3, at p. 580.

²⁹ *Ibid.*, at pp. 580-1.

³⁰ D. H. W. Henry, Q.C., *op. cit.*, *supra*, footnote 17 at p. 13.

problem, and the idea of discrimination. Businessmen are becoming increasingly aware of the effect of the *Combines Act* and are shying away from any arrangement which might breach its provisions and place them under investigation where they may be left in limbo for some time. It follows, therefore, that this condition would keep them away from the export exemption provisions which are primarily a form of defence. Perhaps the main legal difficulty is a lack of judicial interpretation of the provisions. Under certain market conditions an export combination might innocently have a limited effect on the domestic market.³¹ If and when the courts look at problems of this nature, assuming the export combination was formed *bona fide* to encourage exports and not as a colourable device to accomplish an otherwise unlawful purpose, it is to be hoped that the courts will give meaning to the exemption provisions and allow some latitude in the incidental effect.

Conclusion

The discussions, under the sub-headings, have been in general terms for the purpose of communicating an awareness of the overall circumstances which surround the export exemption provisions. It is submitted that the economic premises on which the provisions stand are sound; however, is the law in which they operate sound? If there is a weakness in the law with regard to the export exemption provisions is it to be found specifically therein or within the whole of the *Combines Act*? The limited effect of these provisions, to date, may possibly indicate an inherent flaw. Although there may be present weaknesses surrounding the export provisions, they are still in their infancy and whether they reach maturity will depend on *bona fide* use by businessmen, proper guidance by lawyers and intelligent judicial interpretation by the courts.

ROBERT D. McINTYRE.*

³¹ Assume an "Export Company" has sold 25% of its future production run to Y, a foreign buyer. Suppose through natural causes, for example, drought in the case of natural products or labour problems in the case of manufactured products, the optimum output of the "Export Company" is only 75%. When the seller honours his contract he is going to create a shortage on the domestic market and depending upon the demand possibly increase prices. It is this innocent effect on the domestic market that the courts should look at with some latitude.

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APPENDIX "A"

COMBINES INVESTIGATION ACT

PART V

OFFENCES IN RELATION TO TRADE

32(1) Every one who conspires, combines, agrees or arranges with another person

- (a) to limit unduly the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any article,
- (b) to prevent, limit or lessen, unduly, the manufacture or production of an article, or to enhance unreasonably the price thereof.
- (c) to prevent, or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, storage, rental, transportation or supply of an article, or in the price of insurance upon persons or property, or
- (d) to restrain or injure trade or commerce in relation to any article, is guilty of an indictable offence and is liable to imprisonment for two years.

(2) Subject to subsection (3), in a prosecution under subsection (1) the court shall not convict the accused if the conspiracy, combination, agreement or arrangement relates only to one or more of the following:

- (a) the exchange of statistics,
- (b) the defining of product standards,
- (c) the exchange of credit information,
- (d) definition of trade terms,
- (e) co-operation in research and development,
- (f) restriction of advertising, or
- (g) some other matter not enumerated in subsection (3).

(3) Subsection (2) does not apply if the conspiracy, combination, agreement or arrangement has lessened or is likely to lessen competition unduly in respect of one of the following:

- (a) prices,
- (b) quantity or quality of production,
- (c) markets or customers, or
- (d) channels or methods of distribution,

or if the conspiracy, combination, agreement or arrangement has restricted or is likely to restrict any person from entering into or expanding a business in a trade or industry.

(4) Subject to subsection (5), in a prosecution under subsection (1) the court shall not convict the accused if the conspiracy, combination, agreement or arrangement relates only to the export of articles from Canada.

(5) Subsection (4) does not apply if the conspiracy, combination, agreement or arrangement

- (a) has resulted or is likely to result in a reduction or limitation of the volume of exports of an article;
- (b) has restrained or injured or is likely to restrain or injure the export business of any domestic competitor who is not a party to the conspiracy, combination, agreement or arrangement;
- (c) has restricted or is likely to restrict any person from entering into the business of exporting articles from Canada; or
- (d) has lessened or is likely to lessen competition unduly in relation to an article in the domestic market.