# The Price of a Dormant Provision: Revisiting Section 49 of the *Competition Act*

*Marina Chernenko*[*]

Section 49 of the *Competition Act* (the "Act") is a criminal offence prohibiting agreements or arrangements between federal financial institutions with respect to interest rates, customer service charges, loans and other matters. The provision was transferred from the *Bank Act* in 1986 because the subject matter of the offence was generally related to competition law.[1] Contraventions of section 49 are punishable by imprisonment of up to five years and a maximum fine of $10 million.

In 1986, the *Banking Finance Law Review* published commentary on the impact of this new provision, warning that "[t]here should be some concern in banking circles" because the Act could now be contravened by banks engaged in separate but parallel conduct, such as where "[m]arket forces may cause competitive banks to respond to particular events in a similar fashion (for example, interest rate movements)."[2] Decades later, section 49 has proven to be a cause for concern, but for a different reason than the one predicted in 1986.

Reflecting on experience since the 1986 amendments, this paper argues that section 49 has proven to be (1) redundant, due to the co-existence of a conspiracy offence in section 45 in the Act; (2) dormant, due to the lack of enforcement and guidance issued by the Competition Bureau (the "Bureau"); (3) unfair, due to its discriminatory treatment of federal financial institutions vis-à-vis both provincially-regulated financial institutions and other commercial actors; and (4) costly, due to the superfluous constrains imposed on legitimate contracting practices. These constraints are particularly troubling at a time of significant disruption in the banking industry by non-traditional competitors. For these reasons, section 49 should be repealed or, at the very least, detailed enforcement guidance should be provided by the Bureau to provide certainty for federal financial institutions.

## 1. SECTION 49 IS REDUNDANT

The purpose of section 49 is to protect the public interest in preserving a competitive environment for basic financial instruments and services due to the importance of banks to the Canadian economy.[3] At the time that the provision

---

* The author is a member of the Competition and Foreign Investment Review Group at Torys LLP. The comments of Omar Wakil on an earlier draft of this paper are gratefully appreciated.

1 R.S.C. 1985 2nd Supp, c. 19, s. 34.

2 Barry R. Campbell, "The Competition Act — The Special Case of Banks" (1987) 1 B.F.L.R. 225 at 226.

was transferred to the Act, the general conspiracy provision (section 45) required proof that competition had been lessened "unduly," a standard that prevented the effective prosecution of conspiracies in all cases except those involving concentrated industries in which all, or almost all, participants agreed to fix prices.[4]

However, the rationale for a standalone offence for agreements between federal financial institutions was spent in 2009 when the Act was amended to remove the "unduly" requirement in section 45.[5] Under the amended provision, agreements between competitors to fix prices with respect to a product, allocate markets or customers, or restrict output are illegal, regardless of whether the agreement results in any economic harm. The rationale for section 49 is further undermined by the legislative shift away from sector-specific enforcement of competition law, as evidenced by the repeal of airline-specific prohibitions in 2009.

Nonetheless, per the Bureau's *Competitor Collaboration Guidelines* (the "Guidelines"), where an agreement is between federal financial institutions and falls under subsection 49(1) of the Act, the agreement will be assessed under section 49 and not 45.[6] The Guidelines also provide that agreements that fall within the ambit of subsection 49(1), but are exempted by subsection 49(2), will not be assessed under section 45 but may be subject to review under the Act's civil provisions where the agreement at issue is likely to substantially lessen competition (subject to applicable exceptions, such as where the Minister of

---

3 Solway, Hersh & Boswell, *The Big Chill — Competition/Antitrust Law Considerations in the Insurance Industry: MSA's Canadian Insurance Financial Forum* (Toronto, 2013) at 23, online: <www.msaresearch.com/portals/2/docs/2013slides/03_thebigchill_jordan-solway.pdf>.

4 For a discussion of the difficulty of obtaining convictions under the "unduly" standard, see e.g., Wakil & Chernenko, "Bid-Rigging Enforcement Without a Bid-Rigging Provision: A Proposal for the Repeal of Section 47 of the Competition Act" 28(2) Canadian Competition Law Review 16; Paul K. Gorecki, "The Administration and Enforcement of Competition Policy in Canada, 1960 to 1975: An Application of Performance Measurement" (Ottawa: Consumer and Corporate Affairs Canada) at 295-96; Al Gourley, "A Report on Canada's Conspiracy Law: 1889-2001 and Beyond" (2001) at 5, online: Competition Bureau <www.competitionbureau.gc.ca/eic/site/cbbc.nsf/vwapj/gourleyrep.pdf/$FILE/gourleyrep.pdf>; Adam Fanaki, "Cops, Copperweld and Copping Out: Recent Amendments to Canada's Conspiracy Regime" (Paper delivered at the Canadian Bar Association Competition Law 2010 Spring Forum, 17 May 2010) at 7, online: Canadian Bar Association <www.cba.org/cba/cle/PDF/SpComp10_Fanaki_paper.pdf>.

5 Bill C-10, An Act to implement certain provisions of the budget tabled in Parliament on 27 January 2009 and related to fiscal measures, 2nd Sess, 40th Parl, 2009. The new section 45 came into force on March 12, 2010.

6 Canada, Competition Bureau, "Competitor Collaboration Guidelines", Enforcement Guidelines (Ottawa: Competition Bureau, 23 December 2009) at 3, online: <www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/Competitor-Collaboration-Guidelines-e-2009-12-22.pdf/$FILE/Competitor-CollaborationGuidelines-e-2009-12-22.pdf> [*Guidelines*].

Finance has issued a certification for reasons of financial policy). Agreements between federal financial institutions that are not caught by subsection 49(1) may still be assessed under section 45. This legal framework creates an additional, and unjustified, layer of regulatory complexity for federal financial institutions.

While there are anecdotal accounts of consumer complaints received by the Bureau relating to federal financial institutions, section 45 is well suited to addressing them and preserving competitiveness, as it already does for provincially-regulated financial institutions. For instance, arrangements to fix interest rates would be captured by section 45 because loans are "products" supplied by banks and interest rates are the "price" of those products. Finally, both provisions allow for individual liability, preserving all of the enforcement tools currently available to the Commissioner of Competition under section 49.[7] For these reasons, section 49 is a redundant provision.

## 2. SECTION 49 IS DORMANT

To date, there have been no reported decisions, official Bureau guidance or certificates[8] issued under section 49. While section 49 does not appear to be an enforcement priority for the Bureau, it applies, at least as a technical matter, to a broad range of commercial arrangements between federal financial institutions. Among these are commercial activities that would not be problematic under the Act (or from the perspective of economic policy) if engaged in by any other commercial actors.

In practice, however, the fact that the Bureau does not seem to treat other industries differently adds a layer of regulatory uncertainty. This uncertainty creates challenges for lawyers advising Canadian banks about the risk of "technical" breaches of section 49. Despite the Bureau's lack of enforcement, the serious nature of the offence, the magnitude of potential penalties and the low risk tolerance of federal financial institutions mean that the continued existence of this dormant provision is both unfair and costly.

## 3. SECTION 49 IS UNFAIR

There is no legal or economic justification for treating federal financial institutions differently from provincially-regulated financial institutions, such as

---

7 Under section 49, "every director, officer or employee of the federal financial institution who knowingly makes such an agreement or arrangement on behalf of the federal financial institution is guilty of an indictable offence." Per the *Competitor Collaboration Guidelines*, "individual employees who entered into the agreement may be subject to prosecution under section 45 of the Act" through the operation of sections 21 and 22 of the *Criminal Code*.

8 As noted above, subsection 49(2)(h) exempts agreements requested or approved by the Minister of Finance, requiring that the Minister make a certification to the Commissioner of Competition that such request or approval "was for the purposes of financial policy."

credit unions, or other commercial actors. For instance, an agreement with respect to interest rates or customer service terms between provincially-regulated financial institutions, or between a federal financial institution and a provincially-regulated financial institution, would not be subject to section 49.

In addition to creating an arbitrary distinction between federal and other financial institutions, the prohibited conduct in section 49 is not tailored to address the potential harms that may be unique to the banking industry. While the banking industry may have features not present in some other industries (e.g., barriers to entry and market concentration caused by network effects), these features do not justify encroaching on otherwise legitimate and pro-competitive conduct.[9] This disjuncture between the legislative provision and underlying policy begs the question of "why should collusive behaviour among grocery store chains, gasoline retailers, or newsprint companies, to name a few, be treated any more leniently?"[10]

The Act is a law of general application that establishes basic principles for the conduct of business in Canada. Accordingly, with few exceptions,[11] Parliament has sought to establish basic principles to define the parameters of legitimate conduct rather than devising industry-specific standards. Section 49, therefore, undermines the overarching policy objective of the Act to create a level playing field for all marketplace participants.

## 4. SECTION 49 IS COSTLY

The redundancy and unfairness of section 49 is not merely academic. On the contrary, the continued dormancy of section 49 imposes disproportionate transaction costs on federal financial institutions seeking to compete in a rapidly transforming landscape. These disproportionate costs are a result of the fact that section 49, unlike section 45, is not subject to an ancillary restraints defence. This defence saves an agreement (or term of an agreement) that ostensibly contravenes section 45 but that is directly related to, or reasonably necessary for, giving effect to a broader and lawful agreement.

There are at least two circumstances in which section 49 may be contravened in the context of negotiating and implementing ordinary course purchase and sale agreements that would otherwise be saved by the ancillary restraints defence:

- **Non-compete provisions** are standard restrictive covenants used in agreements to limit, within certain parameters, post-closing competition between the buyer and the seller to preserve the value of acquired assets.

---

9 See e.g., Department of Finance "Balancing Oversight and Innovation in the Ways We Pay: A Consultation Paper" (2015), online: <https://www.fin.gc.ca/activty/consult/onps-ssnp-eng.asp>.

10 Michael J. Trebilcock, *The Law and Economics of Canadian Competition Policy*, (Toronto: University of Toronto Press 2003) at 110-111.

11 For example, section 48 prohibits conspiracies relating to professional sport. There has been very little judicial consideration of the provision.

The Bureau takes the position that a non-compete clause that is ancillary to an agreement for the purchase of assets or shares will not be assessed under section 45.[12] However, since the ancillary restraints defence is not available to federal financial institutions, an otherwise legal non-compete clause in a purchase agreement between federal financial institutions would contravene section 49.

- **Interim covenants and transitional services provisions** are contractual clauses requiring a selling party to refrain from making material changes to a business pending the consummation of a merger or the ability of the buyer to independently operate the acquired business. Section 49 (due to its lack of an ancillary restraints defence) prevents the straightforward use of such provisions in agreements. For instance, where Bank A acquires the credit card portfolio of Bank B, Bank A will not be able to issue cards or accept payment prior to a mass migration of records and technological adaptation. Bank A is prohibited from requiring that Bank B adopt Bank A's risk assessment policies with respect to new credit cards issued that it will ultimately be acquiring, thereby hampering Bank A's ability to maintain the value of its acquired assets during the transitional period.

No compelling policy rationale exists for denying federal financial institutions the benefit of the ancillary restraints defence and thereby hampering their ability to engage in standard contracting practices. Such hampering is particularly problematic due to the increasing participation of non-traditional entities such as technology companies in the banking industry. In fact, recent studies have concluded that maintaining a level playing field with non-traditional competitors, who are not subject to the same regulatory burden, is a chief challenge facing Canadian banks today.[13]

In these circumstances, federal financial institutions (and their lawyers) are faced with the choice of either avoiding otherwise legitimate commercial conduct or devising unnecessary and complex legalistic solutions to avoid technical breaches of section 49. In light of the ongoing transformational changes in the industry, it is worth considering whether federal financial institutions should be allocating time and resources to anticipating and navigating the challenges posed by a dormant provision.

---

[12] *Guidelines*, *supra* note 6 at 12.

[13] See e.g. PWC, Canadian Banks 2015: Perspectives on the Canadian Banking Industry (2015), online: <https://www.pwc.com/ca/en/banking-capital-markets/publications/pwc-canadian-banks-2015-en.pdf>; David Berman, "Canadian banks see threat in tech companies offering mobile payments" *The Globe and Mail* (31 March 2015), online: <http://www.theglobeandmail.com/report-on-business/big-banks-see-threat-in-technology-companies-offering-mobile-payments/article23720027/>; Tim Kiladze, "Too Big To Disrupt?" *The Globe and Mail*, online: <http://www.theglobeandmail.com/report-on-business/feature-too-big-to-disrupt/article22163574/>.

## 5. CONCLUSION

In 1986, it was anticipated that section 49 would give rise to potentially frequent investigations and proceedings involving federal financial intuitions. This concern has not materialized. Although section 49 does not appear to be an enforcement priority for the Bureau, it is applicable, at least in theory, to a wide range of commercial arrangements between federal financial institutions. As a result, the continued existence of this dormant criminal provision in the Act imposes unnecessary transaction costs on federal financial institutions increasingly competing with non-traditional actors.

Since 2010, the subject matter of section 49 could be better addressed by the general conspiracy provision of the Act which would allow federal financial institutions to rely on the ancillary restraints defence. To ensure that legitimate commercial activity and pro-competitive competitor collaborations are not stifled by over-regulation, section 49 should be repealed or, at the very least, detailed guidance should be provided by the Bureau setting out the circumstances in which it will be enforced. Until then, section 49 will continue to be a cause for concern in banking circles.