CT-2017-02

THE COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act,* RSC 1985, c C-34, as amended;

AND IN THE MATTER OF an arrangement between HarperCollins Publishers L.L.C., Hachette Book Group Inc., Verlagsgruppe Georg von Holtzbrinck GMBH, Holtzbrink Publishers, LLC d/b/a Macmillan, Simon & Schuster Inc. and Apple Inc.;

AND IN THE MATTER OF an application by the Commissioner of Competition pursuant to section 90.1 of the *Competition Act.*

BETWEEN:

THE COMMISSIONER OF COMPETITION

Applicant

- and -

HARPERCOLLINS PUBLISHERS L.L.C., and HARPERCOLLINS CANADA LIMITED

Respondents

AFFIDAVIT OF MICHAEL TAMBLYN

(Request for Leave to Intervene by Rakuten Kobo Inc.)

I, **MICHAEL TAMBLYN**, of the City of Toronto in the Province of Ontario, MAKE OATH AND SAY:

1. I am the President and Chief Executive Officer of Rakuten Kobo Inc. ("**Kobo**"), and as such I have personal knowledge of the matters set out below.

Introduction and Summary of Position

2. Kobo is seeking leave to intervene in the Application by the Commissioner of Competition (the "**Commissioner**") against HarperCollins Publishers L.L.C. and HarperCollins Canada Limited (collectively, "**HarperCollins**").

3. Kobo is directly affected by the Application. Granting the Commissioner's Application will have the effect of radically altering Kobo's contractual relationship with HarperCollins and forcing it to operate under a distribution model that it does not want to use for the sale of HarperCollins titles. Kobo would be directly negatively affected in a legal and financial manner by the proposed order, despite the fact that it is an innocent third party that has not been alleged to have participated in any conspiracy.

4. Further, the granting the Commissioner's Application is also likely to harm competition in the market for the retail sale of E-books and E-book Devices.

5. As an E-book retailer that has been involved in the E-books investigation and litigation to date, Kobo is uniquely positioned to provide the Tribunal with a valuable perspective, including in respect of: (i) whether the shift to agency in Canada arose as a result of a U.S.-based conspiracy and, if so, whether the Tribunal has jurisdiction to determine a case under s. 90.1 in respect of the conspiracy; (ii) the procompetitive effects Kobo, as a retailer, observed as a result of the adoption of agency terms; and (iii) the impact of the Commissioner's proposed orders on E-book retailers like Kobo and on competition in the retail market in Canada.

Kobo

6. Kobo is an E-book company with headquarters in Toronto, Ontario. Its primary business is the retail sale of E-books and the development, manufacturing and sale of E-book Devices; it is not an E-book publisher.

7. As an E-book retailer, Kobo operates an E-book retail store through which customers can purchase E-books. E-books are electronically formatted books designed to be read on a computer, a handheld device or any other electronic device capable of visually displaying E-books.

8. Kobo has agreements with authors, publishers and distributors that grant it rights to sell E-books in Canada, including HarperCollins and the other E-book publishers identified in para. 11 of the Commissioner's Application.

9. Should the Commissioner be successful in the Application, Kobo will be directly affected in that it will be forced to change its contracts with HarperCollins and suffer financial harm as a result.

Background to the E-books Investigation and Litigation

10. The Commissioner began the investigation into the E-books market in Canada in the summer of 2012, around the time that the U.S. Department of Justice publicly launched its case against Apple and was finalizing its settlements with the E-book publishers.

11. The investigation included gathering information from market participants, including Kobo, through voluntary Requests for Information. Kobo cooperated with the Commissioner's investigation, including by responding to a lengthy request for sales data, contracts, and other information.

12. In February 2014, the Commissioner entered into consent agreements with Hachette Book Group Canada Ltd., Hachette Book Group, Inc., and Hachette Digital, Inc., Holtzbrinck Publishers, LLC, Simon & Schuster Canada and HarperCollins Canada Limited (the "**2014 Consent Agreements**").

13. Kobo successfully obtained a stay of the 2014 Consent Agreements on the grounds that Kobo was directly affected and would suffer irreparable harm as a result of the Consent Agreements.

14. Kobo ultimately succeeded in having the 2014 Consent Agreements rescinded.

15. On January 19, 2017, the Commissioner filed consent agreements (collectively, the "**2017 Consent Agreements**") with Hachette Book Group Canada Ltd., Hachette Book Group, Inc., and Hachette Digital, Inc.; Holtzbrinck Publishers, LLC; and Simon & Schuster Canada, a division of CBS Canada Holdings Co. to resolve what the Commissioner has purported to conclude is a violation of s. 90.1 of the *Act*, the civil conspiracy provision.

16. That same day, the Commissioner filed the Application against HarperCollins.

17. Through the Application, the Commissioner seeks to effectively achieve against HarperCollins what was achieved with the other publishers through the 2017 Consent Agreements (albeit with the modification of some of the remedial provisions).

18. Granting the Commissioner's Application will have the effect of radically altering Kobo's contractual relationship with HarperCollins and forcing it to operate under a distribution model that it does not want to use for the sale of HarperCollins titles. Kobo would be directly negatively affected in a legal and financial manner by the proposed order, despite the fact that it is an innocent third party that has not been alleged to have participated in any conspiracy.

19. On February 17, 2017, Kobo filed an Application for Judicial Review with the Federal Court, seeking to have the 2017 Consent Agreements declared invalid and quashed. A copy of Kobo's Notice of Application for Judicial Review is attached hereto as **Exhibit "A"**.

Matters in Issue That Directly Affect Kobo

20. The matters in issue in this Application that directly affect Kobo relate to:

(a) whether the shift to agency in Canada arose as a result of a U.S.-based conspiracy and, if so, whether the Tribunal has jurisdiction to determine a case under s. 90.1 in respect of the conspiracy;

(b) the procompetitive effects Kobo, as a retailer, observed as a result of the adoption of agency terms; and

(c) the impact of the Commissioner's proposed orders on retailers like Kobo and on competition in the retail market in Canada.

21. Kobo seeks to present its perspective, as an E-book retailer in Canada, as to how and why it came to use agency agreements in Canada, why agency agreements are procompetitive, and why it is that the Tribunal lacks jurisdiction to make orders under s. 90.1 in respect of the alleged conspiracy. Kobo's perspective as an E-book retailer who has distribution contracts with all the publishers who are alleged to have participated in the conspiracy is relevant to determining whether the introduction of agency in Canada came about because of the conspiracy.

22. Kobo also seeks to present its perspective on the proposed remedies. In particular, the remedies in this case are overly broad and punitive, affecting and punishing market participants like Kobo who are not alleged to have participated in any conspiracy. The legal and financial consequences imposed on Kobo, and the restrictions on its contracting practices, are relevant to the determination of the appropriate remedy, in the event the Tribunal deems a remedy to be necessary.

23. The above matters in issue affect Kobo, are within the scope of the Tribunal's consideration and are relevant to the Tribunal's mandate. Furthermore, the representations Kobo is seeking to make are relevant to the issues raised by the Commissioner in his Application and the Respondents in their Response.

Kobo's Unique Perspective

24. Kobo brings a unique and distinct perspective to these proceedings:

(a) Kobo is a directly affected third party, in that if the Commissioner's proposed remedies are accepted by the Tribunal, Kobo's contract with HarperCollins will be radically changed, altering its ability to operate under an agency model and removing the MFN clause that exists in its contract.

(b) Kobo's perspective is that of an E-book retailer, seeking to compete in the E-books market in Canada. In contrast, the Commissioner's case is against HarperCollins, an E-book publisher who will not suffer the same financial consequences as E-book retailers will, if the proposed remedies are accepted.

(c) Kobo's position as a retailer who has entered into agency agreements with multiple publishers will give the Tribunal a perspective that it will otherwise not have if it is only presented with HarperCollins' experience of how agency came to be adopted in Canada.

(d) Kobo's experiences of the competitiveness of the Canadian E-book market prior to and during the introduction of agency in the Canadian market and its analogous experiences in the United States.

(e) Kobo's demonstrable and significant interest in the outcome of the Commissioner's E-book's investigation, having initiated the litigation in respect of the 2014 Consent Agreements and having initiated a judicial review of the Commissioner's decision to enter into the 2017 Consent Agreements.

Competitive Consequences

25. Kobo is one of Canada's key retailers of E-books in Canada, and HarperCollins is one of the largest publishers with whom Kobo deals.

26. If the matters referred to in the preceding section are determined in a manner that would result in E-book retailers being unable to operate on agency terms with an MFN with HarperCollins, Kobo anticipates that its competitors, and in particular Amazon, the world's largest E-book retailer, and one of the world's largest online retailers in all consumer goods, will take full advantage of the discounting allowed to price HarperCollins' books at unsustainably low and unprofitable prices, to the detriment of competitors, competition and, ultimately, consumers in Canada.

27. Kobo will suffer significant losses on HarperCollins titles for the ten-year period during which agency and MFNs would be prohibited, affecting its ability to compete in the Canadian market, and setting the stage for others to engage in predatory conduct for the sale of HarperCollins' titles in Canada.

28. The Commissioner asserts that the proposed remedy will resolve a substantial lessening or prevention of competition. Through its intervention, Kobo proposes to show why there has been no anticompetitive behaviour that needs resolving, and why the proposed remedies are likely to negatively affect competition.

The Party Whose Position Kobo Intends to Support

29. Kobo's intention in seeking leave to intervene is to assist the Tribunal in better understanding the retail market for the sale of E-books and E-book Devices and the likely effect of the Commissioner's proposed remedies. If granted leave to intervene, Kobo will generally support HarperCollins' position.

Description of How Kobo Proposes to Participate in the Proceedings

30. I confirm, on behalf of Kobo, that Kobo is requesting to participate in the Application on the following terms, insofar as they relate to the topics in relation to which Kobo seeks leave to intervene:

(a) to participate in any motions by providing non-repetitive written and oral submissions and having access to any documents, records or submissions made in respect of those motions, including attending at any cross-examinations on affidavits and asking any non-repetitive questions of affiants.

(b) to review any discovery transcripts and access any discoverable documents of the parties and to be present and ask any non-repetitive questions during oral discoveries;

(c) to adduce non-repetitive evidence for and at the hearing of the Application and any related motions;

(d) to conduct non-repetitive examinations and cross-examinations of witnesses;

(e) to file and receive expert evidence within the scope of its intervention in accordance with the procedures set out in the *Competition Tribunal Rules*;

(f) to attend and make representations at any pre-hearing motions, case conferences or scheduling conferences;

(g) to make written and oral argument, including submissions on any proposed remedy; and

(h) in such further and other manner as Kobo may request of the Tribunal and the Tribunal may grant.

Procedural Matters

31. I confirm, on behalf of Kobo that, if permitted to intervene, Kobo:

(a) undertakes to conduct and coordinate its intervention so as not to be repetitive or duplicative of the representations of the parties to this proceeding or of other interventions to whom leave may be granted;

(b) will not seek its costs for participating in this Application and requests that it not be liable to pay the costs of any other party;

(c) undertakes to comply with the *Competition Tribunal Rules* and with any direction of the Tribunal with respect to the conduct of this proceeding.

SWORN before me at the)
City of ,)
in the)
this day of March, 2017.)
)
_____) _____
) **MICHAEL TAMBLYN**
Commissioner for Taking Affidavits, etc.)

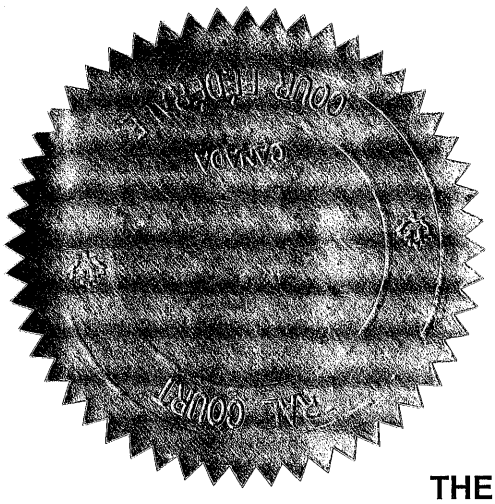
This is **Exhibit "A"** referred to in the affidavit of Michael Tamblyn,

sworn before me this _____ day of March, 2017

_____

A Commissioner for Taking Affidavits, etc.

T-219-17



Court File No.

FEDERAL COURT

RAKUTEN KOBO INC.

Applicant

- and -

THE COMMISSIONER OF COMPETITION,
HACHETTE BOOK GROUP CANADA LTD.,
HACHETTE BOOK GROUP, INC.,
HACHETTE DIGITAL, INC.,
HOLTZBRINCK PUBLISHERS, LLC and
SIMON & SCHUSTER CANADA, A DIVISION OF CBS CANADA HOLDINGS CO.

Respondents

Application Under Section 18.1 of the *Federal Courts Act*

NOTICE OF APPLICATION

TO THE RESPONDENTS:

A PROCEEDING HAS BEEN COMMENCED by the applicant. The relief claimed by the applicants appears on the following page.

THIS APPLICATION will be heard by the Court at a time and place to be fixed by the Judicial Administrator. Unless the Court orders otherwise, the place of hearing will be as requested by the applicant. The applicant requests that this application be heard at Toronto.

IF YOU WISH TO OPPOSE THIS APPLICATION, to receive notice of any step in the application or to be served with any documents in the application, you or a solicitor acting for you must prepare a notice of appearance in Form 305 prescribed by the Federal Courts Rules and serve it on the applicant's solicitor, or where the applicant is self-represented, on the applicant, **WITHIN 10 DAYS** after being served with this notice of application.

Copies of the Federal Courts Rules information concerning the local offices of the Court and other necessary information may be obtained on request to the Administrator of this Court at Ottawa (telephone 613-992-4238) or at any local office.

IF YOU FAIL TO OPPOSE THIS APPLICATION, JUDGMENT MAY BE GIVEN IN YOUR ABSENCE AND WITHOUT FURTHER NOTICE TO YOU.

Date: February 17, 2017

Issued by: M. Sepe
Senior Registry Officer
(Registry Officer)

Address of Local Office: 180 Queen Street West
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APPLICATION

This is an application for judicial review in respect of three consent agreements (collectively, the "**2017 Consent Agreements**") entered into by the respondent Commissioner of Competition (the "**Commissioner**") and the respondent E-book Publishers, Hachette Book Group Canada Ltd., Hachette Book Group, Inc., and Hachette Digital, Inc. (the "**Hachette Consent Agreement**"); Holtzbrinck Publishers, LLC (the "**Holtzbrinck Consent Agreement**"); and Simon & Schuster Canada, a division of CBS Canada Holdings Co. (the "**S&S Consent Agreement**"). The 2017 Consent Agreements were filed with the Competition Tribunal (the "**Tribunal**") on January 19, 2017, and made public by the Commissioner and the Tribunal on January 20, 2017.

THE APPLICANT MAKES APPLICATION FOR:

1. a declaration that the 2017 Consent Agreements are unlawful and invalid;

2. an order quashing the 2017 Consent Agreements;

3. an order restraining the respondents or others acting at their direction or on their behalf from taking further steps pursuant to the 2017 Consent Agreements;

4. an interlocutory order staying the registration of the 2017 Consent Agreements pending the determination of this application for judicial review;

5. costs of the proceedings; and

6. such further and other relief as may be sought and this Honourable Court may permit.

THE GROUNDS FOR THE APPLICATION ARE:

The Applicant

1. Rakuten Kobo Inc. ("**Kobo**") is an E-book[1] company with headquarters in Toronto, Ontario. Its primary business is the retail sale of E-books; it is not an E-book Publisher.

2. As an E-book Retailer, Kobo operates an E-book retail store through which customers can purchase E-books. E-books are electronically formatted books designed to be read on a computer, a handheld device or any other electronic device capable of visually displaying E-books.

3. Kobo has agreements with authors, publishers and distributors that grant it rights to sell E-books in Canada. These agreements are at the heart of this judicial review.

The Respondents

4. The Commissioner is the head of the Competition Bureau and is responsible for the administration and enforcement of the *Competition Act* (the "**Act**").

5. Hachette Book Group Canada Ltd., Hachette Book Group, Inc., and Hachette Digital, Inc. (collectively, "**Hachette**"); Holtzbrinck Publishers, LLC ("**Holtzbrinck**"); and Simon & Schuster Canada, a division of CBS Canada Holdings Co. ("**Simon & Schuster**") (collectively, the "**Respondent Publishers**")

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[1] Unless otherwise stated, we adopt the definitions set out in the 2017 Consent Agreements.

are three of the five major E-book Publishers in Canada, along with HarperCollins Canada Limited ("**HarperCollins**") and Penguin Random House Canada ("**Penguin**").

6. These companies are all affiliates or subsidiaries of international counterparts. For ease of reference and unless otherwise noted, we use the same defined terms within to refer to counterparts operating in Canada, the U.S., or internationally.

Overview

7. On January 19, 2017, the Commissioner filed the 2017 Consent Agreements to resolve what the Commissioner has purported to conclude is a violation of s. 90.1 of the Act, the civil conspiracy provision. The Tribunal has never adjudicated a s. 90.1 case. As such, neither the Tribunal nor the Federal Courts have previously determined the scope of the Commissioner's jurisdiction under this section of the Act.

8. The 2017 Consent Agreements, if allowed to stand, will have the effect of radically altering Kobo's contractual relationships with the Respondent Publishers and inflicting significant financial harm on Kobo, despite the fact that Kobo is an innocent, but directly affected, third party. Kobo is not alleged to have participated in any conspiracy.

9. Kobo seeks to have the 2017 Consent Agreements declared invalid and quashed by this Honourable Court, on the grounds that:

(a) the Commissioner acted without jurisdiction by entering into the 2017 Consent Agreements to remedy a conspiracy that was entered into in the U.S., not in Canada, and that was resolved by the U.S. courts and antitrust enforcers in 2012/2013;

(b) in the alternative, the Commissioner acted without jurisdiction by entering into the 2017 Consent Agreements to remedy "an arrangement," within the meaning of s. 90.1 of the Act, that never existed. He has based his decision to enter into the 2017 Consent Agreements on erroneous findings of fact that he made without regard for the material before him, and which led him to act without jurisdiction; and

(c) in the further alternative, if "an arrangement," within the meaning of s. 90.1 of the Act, did once exist, the Commissioner acted without jurisdiction by entering into the 2017 Consent Agreements to remedy "an arrangement" that was not "existing or proposed" at the time he entered into 2017 Consent Agreements, given the passage of time and the resolutions of the U.S. courts and antitrust enforcers. In doing so, he based his decision to enter into the 2017 Consent Agreements on erroneous findings of fact that he made without regard for the material before him, and which led him to act without jurisdiction by entering into the 2017 Consent Agreements.

Outline of the Application for Judicial Review

10. This application is organized under five headings that immediately follow, dealing with the following topics:

(a) the industry for the sale of E-books in Canada, and the differences between the "Wholesale", "Agency", and "Agency Lite" distribution arrangements between E-book Publishers and E-book Retailers;

(b) the civil conspiracy between E-book Publishers in the U.S. and E-book Retailer Apple Inc. ("**Apple**"), and the resulting settlement agreements and enforcement proceedings by the U.S. Department of Justice ("**U.S. D.O.J.**") in 2012/2013;

(c) the Commissioner's E-books investigation, which began in 2012 and resulted in a consent agreement in 2014, which was challenged successfully by Kobo and rescinded by the Tribunal in 2016;

(d) the terms and effect of the 2017 Consent Agreements, which were entered into after the Tribunal rescinded the 2014 Consent Agreement; and

(e) a summary of the s. 18.1 grounds under which Kobo brings this application for judicial review.

(A)
Wholesale, Agency, and Agency Lite E-Book Distribution Arrangements

11. E-book Publishers seeking to sell E-books through Kobo typically opt to negotiate either "wholesale" or "agency" terms, described below. Kobo continues to sign agreements under both models. Negotiation and modification of contractual terms for both agency and wholesale agreements is common, and the negotiation process can last several months, or, as it has in some cases, more than a year. These negotiations are done one-on-one between Kobo and each Publisher.

12. "**Wholesale**" agreements are typically non-exclusive agreements whereby Kobo acquires from the E-book Publisher the right to sell an E-book at a price set by Kobo. Typically, the E-book Publisher sets a suggested retail price for the title, and Kobo pays the E-book Publisher 50% of the suggested retail price for each E-book Kobo sells. Within this model, Kobo determines the price to be paid by the customer, and provides the E-book Publisher with a monthly sales report, identifying for the E-book Publisher how many copies Kobo sold.

13. When Kobo first began operations, all of its agreements were under the Wholesale model, as this was the model that had traditionally applied in the bricks and mortar world of bookselling.

14. Agency Agreements are typically agreements whereby Kobo is appointed as a non-exclusive agent for the marketing and delivery of E-books on the E-book

Publisher's behalf. In these agreements, the E-book Publisher sets the price at which the E-book must be sold, and Kobo receives a commission for each E-book it sells. Typically, that commission is 30% of the price paid by the customer. Often (but not always), Kobo's Agency Agreements will also contain a Most Favoured Nation ("**Price MFN**") clause, which ensures that if another E-book Retailer is instructed to sell an E-book at a particular price, the E-book Publisher will similarly set Kobo's price.

15. Kobo first entered into an Agency Agreement for the sale of E-books in Canada with Hachette on March 31, 2010. It later entered into Agency Agreements for the sale of E-books in Canada with Penguin Group (Canada) Inc. (April 1, 2011); Simon & Schuster (April 21, 2011); HarperCollins (June 15, 2011); Penguin Group (USA) Inc. (June 20, 2011); Holtzbrinck (June 24, 2011); and Random House of Canada Ltd. (February 28, 2012). Each of these contracts was negotiated separately.

16. "**Agency Lite**" agreements are those whereby the E-book Publisher sets the price of E-books and the E-book Retailer is permitted to reduce the final price paid by customers by a certain amount—generally, from the amount of the commission the E-book Retailer receives over the course of a period of time. The discounting comes entirely from the E-book Retailer's commission; the E-book Publisher retains its 70% cut of the original price it had set, irrespective of any permitted discounting undertaken by the E-book Retailer.

17. The Agency Lite model came to exist as a result of a U.S. enforcement action against the E-book Publishers and Apple that is described below, and it is also the model that is contemplated by the 2017 Consent Agreements. If the 2017 Consent Agreements are allowed to stand, Agency Agreements will be prohibited for a period of nine months and Price MFNs will be prohibited for three years.

18. The imposition of Agency Lite in the U.S. harmed Kobo's U.S. operations, and will similarly cause significant and irreparable financial harm to Kobo in Canada if the 2017 Consent Agreements are allowed to stand.

(B)
The Shift to Agency in the U.S. and Termination of the U.S. Agency Agreements

(i) The U.S. Settlements and Court Decision

19. In the U.S., the U.S. D.O.J. alleged – and the U.S. District Court (the "**U.S. Court**") found – that Apple had conspired with certain E-book Publishers, in violation of Section 1 of the Sherman Act, to eliminate retail price competition in order to raise E-book prices by agreeing to shift all of their contracts simultaneously in early 2010 to an Agency model and provide to Apple and other E-book Retailers a Price MFN (the "**Conspiracy**"). Those E-book Publishers are the same major E-book Publishers identified above at paragraph 5.

20. According to the findings of the U.S. Court, the Conspiracy developed through negotiations and meetings in New York City in December 2009 and January 2010. The timing was motivated by the scheduled launch of Apple's iPad on

January 27, 2010; Apple hoped to announce its iBookstore the same day, but would only do so if it had agreements in place with all the E-book Publishers before that date. Apple did not want to compete with Amazon on E-book prices; similarly, the E-book Publishers wanted to act collectively to end Amazon's $9.99 prevailing price point. The U.S. Court found that Apple took advantage of the tight window of opportunity created by the impending launch of the iPad to finalize Agency Agreements with Price MFNs with each of the E-book Publishers.

21. As is further described below, none of these circumstances existed at the time of Agency's adoption in Canada. The adoption of Agency in Canada came about later, in a staggered fashion lasting over a period of nearly two years. It did not come about simultaneously with all E-book Publishers as a result of any conspiracy; it came about gradually, with some E-book Publishers implementing a change to the Agency model far more slowly than they had in the U.S.

22. The E-book Publishers settled with the U.S. D.O.J. and consented to Final Judgments (the "**U.S. Settlements**") in 2012 (Hachette, HarperCollins, and Simon & Schuster) and 2013 (Penguin and Holtzbrinck), which terminated their existing agreements with E-book Retailers, prohibited them from entering into Agency Agreements for two years (22 months for Holtzbrinck), but permitted Agency Lite distribution agreements. The U.S. Settlements also prohibited Price MFNs for a period of five years.

23. The U.S. Settlements apply to the settling E-book Publishers "and all other Persons in active concert or participation with any of them".

24. The U.S. Settlements also provided that the U.S. Court "retains jurisdiction to enable any party to apply to [the U.S. Court] at any time for further orders and directions as may be necessary or appropriate to carry out or construe this Final Judgment, to modify any of its provisions, to enforce compliance, and to punish violations of its provisions."

25. Apple did not settle, and the U.S. Court issued an Opinion and Order against Apple Inc. on July 10, 2013, and a Final Judgment on September 5, 2013 ("**Apple Decision**"), which was upheld on appeal.

26. At no point has there been any allegation that the E-book Publishers failed to abide by their U.S. Settlement obligations.

27. The Agency prohibitions were time-limited. The trial judge confirmed that Agency Agreements are not themselves improper: "What was wrongful was the use of those components to facilitate a conspiracy [between Apple and] the Publisher Defendants."

28. The prohibitions on Agency in the U.S. have all since expired, although the Price MFN prohibition will continue until September 2017 for Hachette, HarperCollins, and Simon & Schuster, until May 2018 for Penguin, and until August 2018 for Holtzbrinck.

29. In the U.S., the prevailing distribution model with all the E-book Publishers has since returned to an Agency model.

(ii) The Effects of the U.S. Settlement Agreements on Kobo and the E-book Market

30. As a result of the U.S. Settlements, several of Kobo's contracts with E-book Publishers for the sale of E-books in the U.S. were altered. Its contracts with Hachette, HarperCollins, Simon & Schuster, and Holtzbrinck that were previously Agency Agreements were shifted to the "Agency Lite" model, described above, whereby E-book Publishers continued to set the retail price of E-books and continued to retain 70% of that price, but where discounting was permitted, with the discount coming solely from the E-book Retailer's 30% commission.

31. The prohibition on Agency led to two perverse results. First, from a financial standpoint, the alleged conspirators were left whole. Under Agency, they received 70% of the price they set for the book, and under Agency Lite, they continued to receive the same 70% share. Retailers like Kobo, who played no role in the conspiracy, were the ones to suffer, as any discounting had to take place from their 30% commission.

32. The move to an Agency Lite model had a negative impact on Kobo's U.S. market share and revenues. Amazon took full advantage of the discounting allowed under that model, pricing books at unsustainably low and unprofitable prices. Kobo shed significant revenues as it was being forced to discount titles to match the deep discounting it faced. Despite these efforts to protect its market share by lowering prices, Kobo saw its position in the U.S. market dwindle. Kobo stopped

making significant investments in the U.S. market, closed its office in the country, and even to today has not replaced the U.S. sales staff that it terminated.

33. Second, whereas under the Agency model, the retail playing field was level—with E-Book Retailers like Kobo being able to innovate, compete on product offerings, and gain customers and grow sales—the Agency Lite model allowed Amazon, the world's largest E-Book Retailer, and one of the world's largest online retailers in all consumer goods, to price its E-books at unprofitably low levels, forcing its smaller competitors like Kobo out of the market. Although competition laws are meant to protect the market against predatory conduct, the U.S. Settlements set the stage for precisely that.

(C)
The Commissioner's E-books Investigation and the Litigation over the 2014 Consent Agreement

(i) The Commissioner Opens an Investigation and Enters into the 2014 Consent Agreement

34. The Commissioner began an investigation into the E-books market in Canada in the summer of 2012, around the time that the U.S. D.O.J. publicly launched its case against Apple and was finalizing its settlements with the E-book Publishers.

35. The investigation included gathering information from market participants, including Kobo, through voluntary Requests for Information. Kobo cooperated with the Commissioner's investigation, including by responding to a lengthy request for sales data, contracts, and other information.

36. About a year and a half later, on February 7, 2014, the Commissioner filed with the Tribunal a consent agreement with the Respondent Publishers and HarperCollins (the "**2014 Consent Agreement**"). The 2014 Consent Agreement, which is substantially similar to the 2017 Consent Agreements, was modelled on the U.S. Settlements. The 2014 Consent Agreement imposed a ban on Agency (for 18 months) and Price MFNs (for four years and six months), but allowed E-book Publishers to enter into Agency Lite contracts with E-book Retailers.

37. Kobo spoke with the Competition Bureau investigators the evening before the 2014 Consent Agreement was filed. Despite having cooperated fully with the investigation, and despite the obvious harm that the 2014 Consent Agreement would have on Kobo, the Competition Bureau did not inform Kobo of the pending filing and only let Kobo know after it had already filed the 2014 Consent Agreement.

(ii) Kobo Succeeds in Having the 2014 Consent Agreement Stayed

38. As a directly affected third party, Kobo filed an application pursuant to s. 106(2) of the Act ("**s. 106(2) Application**") on February 21, 2014, seeking to have the 2014 Consent Agreement varied or rescinded. Kobo alleged that the 2014 Consent Agreement was deficient on its face, and also raised substantive arguments as to why the Commissioner lacked jurisdiction to enter into the 2014 Consent Agreement.

39. Simultaneously, Kobo sought a temporary stay of the 2014 Consent Agreement pending determination of its s. 106(2) Application, as the termination of its

Agency Agreements with the Respondent Publishers and HarperCollins would cause Kobo significant irreparable harm.

40. The then-Chair of the Tribunal, Justice Rennie, granted the stay, finding that:

(a) Kobo had raised serious issues related to the interpretation of subsection 106(2);

(b) Kobo would suffer irreparable financial harm arising from the shift to Agency Lite. The Chair accepted internal Kobo financial projections and the evidence of Kobo's experiences with Agency Lite in the U.S., and noted that the Federal Court of Appeal has recognized that an applicant's inability to claim damages from the Commissioner in the event it is successful in its application contributes to the irreparable nature of the financial harm; and

(c) The balance of convenience favoured granting the stay, noting:

> While maintaining the status quo might have the effect of depriving consumers of lower E-book prices in the short term, not granting the stay will certainly have a profound impact on the usefulness of Kobo's application. In the event that Kobo is successful in its application and the Tribunal finds that the Consent Agreement ought to be rescinded or varied, Kobo would have already suffered loss and there would be no way to wind back the clock.

41. As a result, Kobo was permitted to continue to operate under the Agency model on an interim basis while its s. 106(2) Application was considered.

(iii) The Commissioner Brings a Reference that Restricts the Tribunal's Review Powers under s. 106(2)

42. Kobo's s. 106(2) Application alleged both substantive and formal deficiencies with the 2014 Consent Agreement.

43. Before Kobo's s. 106(2) Application could be heard, the Commissioner brought a Reference to have the Tribunal determine the scope of its review power under s. 106(2).

44. Chief Justice Crampton heard the Reference and ruled on it in September 2014 ("**Reference Decision**"). The Reference Decision, which was upheld on appeal, determined that the Tribunal's review power under s. 106(2) was limited to reviewing consent agreements on their face to ensure they met certain criteria.

45. The Tribunal found that it did not have jurisdiction under s. 106(2) to consider Kobo's substantive arguments, i.e., arguments that challenged whether the Commissioner exceeded his jurisdiction in entering into a consent agreement at all. It held that it was not open to Kobo to attempt to establish that one or more of the substantive elements set forth in s. 90.1 were not met, "including whether there is an agreement or arrangement – whether existing or proposed – between persons two or more of whom are competitors. Disputes with respect to these and other substantive elements, such as whether an agreement is likely to prevent or lessen competition substantially, are beyond the scope of subsection 106(2)."

46. The Tribunal also stated that it did not have jurisdiction to consider matters such as an excess of jurisdiction on the part of the Commissioner, but that "it would be potentially open to a party to raise them before the Federal Court on an application for judicial review brought pursuant to section 18.1 of the *Federal Courts Act* ... Indeed, the Commissioner recognized this possibility during the hearing of this Reference."

47. On appeal, the Federal Court of Appeal confirmed that, "Even where the Tribunal has review powers under the Act, the possibility of judicial review exists."

48. Kobo was therefore not permitted to advance jurisdictional arguments before the Tribunal. The jurisdictional arguments are at the heart of this judicial review application.

(iv) The Commissioner Forces Kobo to Produce Further Documents and Information

49. While the litigation of Kobo's s. 106(2) Application before the Tribunal was ongoing, the Commissioner obtained orders from the Federal Court for the production of records and written returns of information pursuant to s. 11 of the Act ("**s. 11 orders**") against Kobo and Indigo Books & Music Inc. ("**Indigo**") on January 22, 2015. The wide-ranging s. 11 order against Kobo required Kobo to produce over five years' worth of documents and written returns from 2009 to 2015.

50. The Commissioner had previously obtained a s. 11 order against Penguin in March 2014.

51. On March 23, 2015, Kobo produced over 160,000 documents (fully indexed) and sales data for every single E-book it had sold from September 1, 2009 to January 22, 2015 pursuant to the s. 11 order.

52. Included in the records produced to the Commissioner were a variety of records that showed that the shift to Agency in Canada did not take place as a result of a conspiracy or s. 90.1 arrangement and that it had in fact occurred very differently than it had in the U.S. (the U.S. circumstances are described above at paragraph 20):

(a) the shift in Canada occurred in a staggered manner over a period of 23 months;

(b) when Agency first came to Canada, not all E-book Publishers shifted to Agency, and when they did, not all of their E-book Retailer partners shifted to Agency;

(c) by the time the Agency Agreements began to be entered into, the iPad and iBookstore had already launched;

(d) at the time that Kobo shifted to Agency in Canada, Amazon had not yet launched a Canadian presence for E-books, although it did sell some E-books into Canada from the U.S.;

(e) in Canada, Kobo had to (separately) encourage several E-book Publishers to move to the Agency model. With Simon & Schuster,

HarperCollins, and Random House of Canada Ltd. (separately), Kobo advocated for the move to Agency. The Agency model with these E-book Publishers came about as a result of Kobo's desire for a more sustainable distribution model, not out of a backroom deal among the E-book Publishers.

(v) The 2014 Consent Agreement Is Rescinded

53. Kobo's s. 106(2) Application went forward within the parameters set by the Reference Decision. As such, none of Kobo's substantive challenges to the Commissioner's jurisdiction could be considered; the case proceeded on the basis solely of the terms of the 2014 Consent Agreement on their face. The hearing was held on April 25, 2016, and reasons were delivered on June 10, 2016.

54. The Tribunal rescinded the 2014 Consent Agreement for not meeting the criteria set by the Tribunal in the Reference Decision, as well as for not disclosing certain basic contextual information that the Tribunal held should be present in all consent agreements.

55. The rescission of the 2014 Consent Agreement in June 2016 meant that Kobo could continue to operate under the Agency model, which it had theretofore been permitted to do on an interim basis pursuant to Justice Rennie's 2014 stay decision.

(D)
The 2017 Consent Agreements

56. The 2017 Consent Agreements now under review were entered into by the Commissioner and each of the Respondent Publishers and were filed with the Tribunal on January 19, 2017, pursuant to s. 105 of the Act. They are in relation to an alleged "arrangement among competitors" contrary to s. 90.1 of the Act. The Commissioner also filed a consent agreement with Apple and Apple Canada Inc. the same day in relation to the same alleged conduct. The Commissioner and the Tribunal made the Consent Agreements public the following day.

57. Although HarperCollins was a party to the 2014 Consent Agreement, it is not a party to the any of the 2017 Consent Agreements. Instead, the Commissioner has filed a Notice of Application against HarperCollins pursuant to s. 90.1 of the Act. It is anticipated that HarperCollins will contest the application.

58. Section 105 of the Act provides that the Commissioner and a person in respect of whom the Commissioner has applied or may apply for an order under Part VIII of the Act may sign a consent agreement, which consent agreement shall be based on terms that could be the subject of an order of the Tribunal against that person. Upon registration of the consent agreement, it has the same force and effect as if it were an order of the Tribunal. The Tribunal has no authority to reject a consent agreement that the Commissioner files, and plays no role in reviewing its terms before registration.

59. Section 90.1 of the Act provides:

> 90.1 (1) If, on application by the Commissioner, the Tribunal finds that an agreement or arrangement — whether existing or proposed — between persons two or more of whom are competitors prevents or lessens, or is likely to prevent or lessen, competition substantially in a market, the Tribunal may make an order:
>
> > (a) prohibiting any person — whether or not a party to the agreement or arrangement — from doing anything under the agreement or arrangement; or
> >
> > (b) requiring any person — whether or not a party to the agreement or arrangement — with the consent of that person and the Commissioner, to take any other action.

60. The 2017 Consent Agreements state that the Commissioner has concluded that the Respondent Publishers entered into an arrangement, within the meaning of s. 90.1 of the Act, in the U.S. with competitor E-book Publishers in the market for E-books, in relation to the retail sale of E-books in the U.S. and Canada.

61. As was the case with the 2014 Consent Agreement, the 2017 Consent Agreements impose Agency and Price MFN prohibitions on the E-book Publishers, compelling them to alter or terminate their contracts with E-book Retailers, including Kobo.

62. There are some subtle differences between each of the 2017 Consent Agreements, but they are identical in all material respects, including in respect of the Commissioner's conclusions. In the recitals, the Commissioner concludes, and the Respondent Publishers agree not to contest solely for the purposes of the 2017 Consent Agreements, that:

(a) an arrangement was entered into in or about January 2010 in the U.S. (the "**Arrangement**");

(b) the Arrangement was in relation to the retail sale of E-books in the U.S. and Canada;

(c) each of the Respondent Publishers was a party to the Arrangement or was a Canadian affiliate of a party to the Arrangement, and implemented the Arrangement in Canada;

(d) the Arrangement provided that the Respondent Publishers would enter into agreements with E-book Retailers in Canada which included provisions to restrict the ability of E-book Retailers to discount the retail price for E-books, and provided that the Respondent Publishers would include a Price MFN clause in their agreements with Apple Inc. or its subsidiary;

(e) the Arrangement continued to exist as at the date of the 2017 Consent Agreement; and

(f) the Arrangement prevents or lessens, or is likely to prevent or lessen, competition substantially in the retail market for E-books in Canada.

63. The recitals also state that the Commissioner and Respondent Publishers have reached an agreement to resolve the Commissioner's concerns.

64. As is discussed further below, the Commissioner erred in reaching the above conclusions in respect of the Canadian market. He did not consider material that

was placed before him that demonstrates that, in Canada, the shift to Agency did not arise as a result of the Conspiracy. As Kobo's productions to the Commissioner showed, the Conspiracy was implemented in relation to the U.S. market simultaneously and as a result of the unique factors set out in paragraph 20, above. In contrast, in Canada, the shift to Agency came about later and in a more staggered manner and not by way of an E-book Publisher-led conspiracy.

65. The material obligations imposed on the Respondent Publishers by the 2017 Consent Agreements are described in the paragraphs below. These are identical to the prohibitions contained in the now-rescinded 2014 Consent Agreement, and differ only in the length of time that the prohibitions are meant to last.

66. In paragraph 2, the Respondent Publishers are prohibited from restricting, limiting or impeding any E-book Retailer's ability to set, alter or reduce the Retail Price of any E-Book, or to offer discounts or promotions ("**Agency Prohibition**"). Effectively, this prohibits the Agency model. The Agency Prohibition is to commence within either 50 days (Hachette Consent Agreement) or 120 days (Holtzbrinck and S&S Consent Agreements) after the registration of the 2017 Consent Agreements, and expires nine months later.

67. In paragraph 3, they are prohibited from entering into any agreement with an E-book Retailer that contains a Price MFN ("**MFN Prohibition**"). The MFN Prohibition is to commence immediately after the registration of the 2017 Consent Agreements and expire three years later.

68. Paragraph 4 compels them to terminate, not renew and not extend their current agreements with E-book Retailers insofar as such agreements contain Agency clauses or Price MFNs. Alternatively, the Respondent Publishers can:

(a) within 50 days (Hachette and S&S Consent Agreements) or 120 days (Holtzbrinck Consent Agreement), agree with the E-Book Retailers to amend the contracts to remove any Price MFN clauses or ensure that such clauses would not be enforced; and

(b) within 50 days (Hachette Consent Agreement) or 120 days (Holtzbrinck and S&S Consent Agreements), agree with the E-Book Retailers to amend the contracts to remove any Agency terms or ensure that such terms would not be enforced for nine months.

69. Notwithstanding paragraphs 2-4 of the 2017 Consent Agreements, paragraph 5 allows for "Agency Lite", whereby the E-book Publisher would continue to set the Retail Price of E-books so long as the E-book Retailer was permitted to reduce the final price paid by customers by an aggregate amount defined as the "**Agreed Funds**", which was "equal to the total commissions the [E-book Publisher] pays to the E-book Retailer, over a period of at least nine (9) months, in connection with the Sale of the [E-book Publisher's] E-books to consumers in Canada". The Commissioner has admitted that this model allows E-book Retailers to price E-books below cost, or even "at a penny".

70. This Agency Lite model is materially identical, other than length of time, to the model that Justice Rennie concluded in 2014 would cause Kobo irreparable harm.

(E)
Summary of the Section 18.1 Grounds for Judicial Review

(i) The Commissioner lacks jurisdiction over the Conspiracy

71. The Commissioner acted outside his jurisdiction by entering into the 2017 Consent Agreements to remedy a Conspiracy in the face of his own admission that it was entered into in the U.S., not in Canada. Moreover, this Conspiracy was resolved by the U.S. courts and antitrust enforcers in 2012/2013.

72. Federal legislation like the Act is presumed not to apply extra-territorially to persons, things or events outside the boundaries of the enacting jurisdiction. While the Federal Government is not prohibited from passing legislation with extra-territorial application, that intention must be expressed in the legislation.

73. While Parliament expressly intended that the *criminal* conspiracy provisions of the Act would have some extra-territorial application (by virtue of s. 46 of the Act), it did not express a similar intention when it enacted s. 90.1, the *civil* conspiracy section. The Commissioner has erred in attempting to exercise jurisdiction that Parliament has not conferred on him.

(ii) The Commissioner based his decision on erroneous findings which led him to act without jurisdiction to remedy an arrangement that does not exist

74. In the alternative, the Commissioner acted outside his jurisdiction by entering into the 2017 Consent Agreements to remedy "an arrangement," within the meaning of s. 90.1 of the Act, that never existed. He has based his decision to enter into the 2017 Consent Agreements on erroneous findings of fact that he made without regard for the material before him, and which led him to act without jurisdiction.

75. The 2017 Consent Agreements are premised on a theory that the Arrangement is merely the implementation of the Conspiracy in Canada. This theory does not hold true in light of the material the Commissioner obtained from Kobo as a result of the s. 11 order. Insofar as the Conspiracy took place, it did not contemplate Canada. The Commissioner's conclusions, set out at paragraph 63, above, were arrived at in error and without regard to the information supplied by Kobo, which was plainly ignored.

76. The evidence that the Commissioner gathered from Kobo through the s. 11 order, had it been considered, should have led to the conclusion that in Canada, Agency came about in an organic, measured, and non-conspiratorial manner.

77. However, the Commissioner did not once (other than asking for certain translations), following the receipt of Kobo evidence, follow-up with Kobo with respect to the content of the s. 11 materials. To that end, the Commissioner did not seek Kobo's explanation or perspective on, for example:

(a) correspondence with one of the Respondent Publishers – eight months prior to switching to Agency with that E-book Publisher – in which Kobo complained that, by keeping Kobo on a Wholesale model, the E-book Publisher was leaving Kobo "twisting in the wind"; the E-book Publisher was apologetic about the lack of progress on shifting to Agency;

(b) correspondence with another E-book Publisher in which Kobo urged the E-book Publisher to "move quickly to an agency model".

78. Insofar as the Commissioner's investigation into E-books continued after Kobo's response to the s. 11 order, the Commissioner ignored evidence that would contradict his theory of the case, and did not once invite Kobo to discuss with him or his staff any of the material that was furnished that would disprove his case. There is nothing on the public record, including in the 2017 Consent Agreements, to demonstrate that the Commissioner weighed this important evidence or even considered its probative value.

79. In proceeding in this manner, he erroneously concluded that there was an arrangement in Canada without regard for the material before him, and based his decision to enter into the 2017 Consent Agreements on this and other erroneous findings of fact. The Commissioner does not have jurisdiction to enter into the 2017 Consent Agreements, because there is no "arrangement" within the meaning of s. 90.1 of the Act.

(iii) Even if the Conspiracy contemplated Canada, the U.S. enforcement action brought the conspiracy to an end

80. In the further alternative, if "an arrangement," within the meaning of s. 90.1 of the Act, did once exist, the Commissioner acted outside his jurisdiction by entering into the 2017 Consent Agreements to remedy "an arrangement" that was not "existing or proposed" as at the time he entered into 2017 Consent Agreements, given the passage of time and the resolutions of the U.S. courts and antitrust enforcers. In doing so, he based his decision to enter into the 2017 Consent Agreements on erroneous findings of fact that he made without regard for the material before him, and which led him to act without jurisdiction by entering into the 2017 Consent Agreements.

81. Section 90.1 requires that the agreement or arrangement forming the substance of the Commissioner's complaint must be "existing or proposed" at the time of the filing. By the time the Commissioner filed the 2017 Consent Agreements, there was no Arrangement, existing or proposed; the Arrangement that the Commissioner relies on simply no longer exists, if it ever did in respect of Canada.

(iv) Other conclusions that were reached without regard to the material before the Commissioner

82. The Commissioner has also erroneously concluded that the 2017 Consent Agreements will remedy competition concerns, when in reality, they will set the stage for predatory pricing to take place in the E-books market in Canada. In particular, the Commissioner has admitted that the Agency Lite paragraph of the

2014 Consent Agreement (which, other than with respect to time, is identical to the Agency Lite paragraph of the 2017 Consent Agreements) would allow an E-book Retailer who can engage in "predatory pricing profitably over a long-term period" to enter into an agreement with an E-book Publisher whereby "it could sell its books for a penny". Otherwise put, the Commissioner admitted that the Agency Lite paragraph of the Consent Agreement could allow for "limitless discounting", and "below cost".

83. He has therefore erroneously concluded that the Consent Agreements will resolve competition concerns (when in fact they will create competition concerns), without regard for the material before him and the numerous attempts Kobo has made to raise this issue with the Commissioner. Despite having this concern raised in discoveries and filed in the hearing that led to the rescission of the 2014 Consent Agreement, the Commissioner has at no time since the rescission invited Kobo to discuss with him or his staff any of the concerns about predatory pricing, which would re-evaluate his conclusion that the 2017 Consent Agreements are resolving competition concerns.

84. This is all the more troublesome given the European Commission's investigation of Amazon's alleged abuse of dominance and restrictive business practices, and the Commissioner's own recent conclusion in an unrelated matter that Amazon engaged in false and misleading representations.

85. Finally, the Commissioner has ignored Kobo's concerns that in crafting the consent agreements (both in 2014 and 2017) in the way that he has, he has

imposed sanctions against Kobo for an alleged Conspiracy to which it was not a party. Meanwhile, the E-book Publishers, who were ostensibly the subjects of his conclusions regarding an Arrangement, will be left financially whole, continuing to reap the 70% share of the price that they set.

Legislation Relied On

86. *Competition Act*, R.S.C., 1985, c. C-34 including ss. 45, 46, 90.1, 105, 106.

87. *Federal Courts Act*, R.S.C., 1985, c. F-7, including ss. 18.1, 18.2.

88. *Interpretation Act*, R.S.C., 1985, c. I-21, including s. 8.

THIS APPLICATION WILL BE SUPPORTED BY THE FOLLOWING MATERIAL:

1. The affidavit of Michael Tamblyn, to be sworn, and the exhibits thereto;

2. Such further and other material as counsel may advise and this Honourable Court may permit.

The Applicant requests the Commissioner to send a certified copy of the following material that is not in the possession of the Applicant but is in the possession of the Commissioner to the Applicant and to the Registry:

1. The entirety of the Commissioner's investigative file relating to the Commissioner's inquiry into the E-books market in Canada that gave rise to the 2017 Consent Agreements, including notes, memoranda, analyses and summaries, and any written submissions received from any E-book Publishers, subject to recognized privileges.

Date: February 17, 2017

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THE COMMISSIONER OF COMPETITION et al.

Respondents

Court File No.

I HEREBY CERTIFY that the above document is a true copy of the original issued out of / filed in the Court on the FEB 17 2017 day of Feb 17 2017

Dated this ____ day of ____ 20__

FEDERAL COURT

Proceeding commenced at Toronto

Application under Section 18.1 of the *Federal Courts Act*

NOTICE OF APPLICATION FOR JUDICIAL REVIEW

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Applicant

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Respondents

Court File No. CT-2017-02

COMPETITION TRIBUNAL

APPLICATION UNDER SECTION 9(3) OF THE *COMPETITION TRIBUNAL ACT*

AFFIDAVIT OF MICHAEL TAMBLYN

(Request for Leave to Intervene by Rakuten Kobo Inc.)

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