

File No.: CT-2008-004
Registry Document No.:

COMPETITION TRIBUNAL

IN THE MATTER of the *Competition Act*, R.S.C. 1985, c. C-34, as amended

AND IN THE MATTER of an Application by Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited for an Order pursuant to section 75 of the *Competition Act*.

BETWEEN:

**NADEAU FERME AVICOLE LIMITÉE/
NADEAU POULTRY FARM LIMITED**

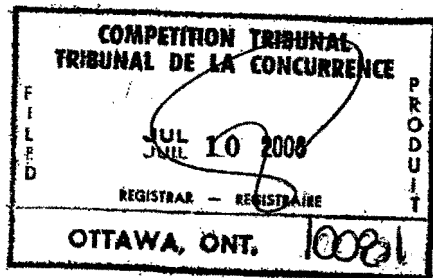
Applicant

AND

**GROUPE WESTCO INC. AND GROUPE DYNACO, COOPÉRATIVE
AGROALIMENTAIRE AND VOLAILLES ACADIA S.E.C. AND
VOLAILLES ACADIA INC./ACADIA POULTRY INC.**

Respondents

REPLY PURSUANT TO SECTION 75 OF THE *COMPETITION ACT*



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AND IN THE MATTER of an Application by Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited for an Order pursuant to section 75 of the Competition Act.

BETWEEN:

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NADEAU POULTRY FARM LIMITED**

Applicant

AND

**GROUPE WESTCO INC. AND GROUP DYNACO, COOPÉRATIVE
AGROALIMENTAIRE AND VOLAILLES ACADIA S.E.C. AND VOLAILLES ACADIA
INC./ACADIA POULTRY INC.**

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**REPLY PURSUANT TO SECTION 75
OF THE *COMPETITION ACT***

1. The Applicant ("**Nadeau**") admits only those allegations contained in the Responses delivered by the Respondents, which constitute admissions of matters alleged by Nadeau in its Notice of Application and accompanying Statement of Grounds and Material Facts. Nadeau otherwise denies each and every allegation contained in the Responses delivered by the Respondents.

2. Nadeau repeats and reaffirms the allegations contained in its Notice of Application and the accompanying Statement of Grounds and Material Facts. Nadeau adds the following in specific reply to certain of the allegations made in the Responses of the Respondents.

A. THE PARTIES

3. Nadeau is the sole Applicant in these proceedings. It is a private, stand alone company which has its own management and employees, and conducts its own procurement, sales, and operations. Nadeau is a wholly owned subsidiary of Maple Lodge Holding Corporation. Maple Lodge Holding Corporation ("**Maple Lodge**") is a holding company which does not itself carry on any operating business.

4. The Respondents are not independent of each other. Among other things:

(a) the Respondents Groupe Westco Inc. ("**Westco**") and Groupe Dynaco, Coopérative Agroalimentaire ("**Dynaco**") together own 55% of the Respondents Volailles Acadia S.E.C. and Volailles Acadia Inc. (collectively, "**Acadia**");

(b) an additional 30% of Acadia is owned by La Coop fédérée, which is the majority owner of Olymel S.E.C. ("**Olymel**"), Westco's "partner" in the proposed business described by Westco in its Response;

(c) Westco has an ownership interest in Dynaco;

(d) one or more of the Respondents have directors or officers in common with each other; and

(e) the Respondents have acted in concert with respect to the subject matter of these proceedings.

5. The Respondents directly own or control over 74% of New Brunswick's chicken production quota. In addition, the Respondent Dynaco co-owns Cormico Inc., which holds about

5% of New Brunswick's chicken production quota. Of 33 nominal quota holders in New Brunswick, only 7 are independent of the Respondents. As such, the Respondents exercise an effective monopoly over the production and supply of live chicken in New Brunswick.

6. Nadeau agrees that it operates the only chicken processing plant in New Brunswick (the "**St-François Plant**"). However, under no circumstances can Nadeau be considered to be a "monopolist", as alleged by the Respondents. This is because, among other things:

- (a) Nadeau competes in the processing market with numerous other processors located in Eastern Canada (Québec and Nova Scotia);
- (b) there is vigorous competition among processors in this market;
- (c) in contrast with the legislative controls over the production sector, there is no legislative limit or prohibition on new entrants into the processing market;
- (d) a number of Nadeau's competitors, including Olymel, have a competitive advantage in that they have a legislatively guaranteed live chicken supply under the supply management system as operated by the chicken board of Québec;
- (e) Nadeau currently has no such legislatively guaranteed supply; and
- (f) Olymel's "partnership" with the Respondents guarantees it access to additional live chicken supply, over and above the supply already granted to it by the Québec chicken board.

7. Nadeau is very vulnerable to the anti-competitive conduct of the Respondents, and in particular, to the Respondents' proposed refusal to supply. Contrary to the allegations made by Westco in its Response, the Respondents' conduct is motivated not by a wish to "vertically integrate", but by a desire to hamper or limit competition.

B. THE CHICKEN MARKETING SYSTEM

8. The Respondents refer to and rely upon the decision of the Supreme Court of Canada in *Québec v Pelland*, 2005 SCC 20. That decision upheld the constitutional validity of the Québec component of the federal-provincial chicken marketing scheme.

9. The Supreme Court noted (at para. 4) that the purpose of the chicken marketing scheme is to "ensure effective marketing and a dependable supply of chicken to Canadian consumers". The Court described the function of the federal body (the Chicken Farmers of Canada) as being "to assess the national market and set a global production quota for each province" (at para. 7).

10. Since the scheme contemplates setting periodic supply quotas based on assessment of consumer need, the global amount of chicken that can be produced nationally (and hence provincially) is not subject to any *a priori* limitations. For this reason, chicken is, and will continue to be, in ample supply. As stated by the Supreme Court (at para. 38):

"The quota system is an attempt to maintain an equilibrium between supply and demand and attenuate the inherent instability of the markets".

11. Although the global number of chickens produced can grow based on consumer demand, the number of producers is limited. As stated in *Pelland* (para. 33), "a producer must be allotted an individual production quota in order to produce chicken in the province". Once possessed of a quota, the producer may (subject to the relevant legislation) market both intra-and extra-provincially. Only producers owning or controlling quota may produce chicken. There is therefore insufficient competition at the production (supply) level of the chicken marketing

system. The system creates a sanctioned monopoly in favour of existing quota-holders or owners, such as the Respondents.

12. In New Brunswick, the provincial component of the system is administered by the Chicken Farmers of New Brunswick ("CFNB"). The Marketing Orders of the CFNB reiterate the goals and objectives of the system, and reinforce the regulatory protection offered by the system to existing producers such as the Respondents. For example:

(a) Marketing Order I (1) describes the object of the marketing plan as:

"...to control the number of chickens raised for marketing within the Province, in such a manner:

(a) As to ensure there is an adequate supply of New Brunswick grown chicken available to the consumer.

(b) To provide an opportunity for the maximum number of residents in New Brunswick to earn a living in the marketing of chicken.

(c) To ensure a reasonable rate of return from the sale of chicken and to ensure a continuity of supply.

(d) To avoid the development of monopolies which could result in excessive cost to the consumers of chicken.

(e) To avoid a curtailment of the overall supply in the event one or more producers cease to market chicken."

(b) Marketing Order III (11) provides that the Province's marketing quota "shall be allocated by the Board on a *pro rata* basis to *existing* producers" (emphasis added).

(c) Marketing Orders VII and IX deal with the prices to be paid by processors, and other conditions for the sale of chicken by a producer to a processor. These Orders provide that the minimum prices paid shall be those fixed from time to time by the CFNB.

13. As a result, existing producers are fully protected in New Brunswick, in that the producer board (the CFNB) sets minimum prices and uniform terms and conditions of sale, which are intended to ensure "a reasonable rate of return", and new entrants are essentially barred from the producer end of the market.

14. The system does not contemplate that producers like the Respondents will use their protected monopoly to attack competition at the unprotected processing level of the market. The Respondents are working in concert for the purpose of driving Nadeau out of business. Once Nadeau is gone, this leaves the field open for Olymel, together with Westco and its cohorts, to corner the processing market in Eastern Canada from a base of the "guaranteed supply" provided by the system to the Respondents.

C. THE CONDUCT OF THE RESPONDENTS

15. The Respondents or their predecessors have been doing business with Nadeau since 1989. Over that period of time Nadeau has:

- (a) always purchased all of the chicken produced by them;
- (b) always paid *at least* the price fixed by the CFNB (usually at least 6.5¢ more per kilogram than the prices set by chicken boards in the neighbouring provinces); and
- (c) offered market incentives from time to time (such as for smaller birds, or for relocation of production facilities closer to the St-François Plant).

16. These long-term supply arrangements have allowed the Respondents to grow and prosper. Westco, for example, has been able to become, according to its own literature, "an example of success and profitability" and "one of the biggest poultry producing companies in Canada".

17. Contrary to the allegations made by Westco in its Response, at no time was Westco interested in any genuine partnership with Nadeau.

18. At a meeting which took place on January 25, 2007, Westco advised Nadeau that:

- (a) Westco was interested in buying or investing in the St-François Plant; and
- (b) Westco wanted a price increase or additional incentives.

19. Nadeau responded that:

- (a) its shareholders would likely not be interested in selling the St-François Plant;
- (b) a structure that would result in Westco owning a percentage of the St-François Plant and retaining 100% of their live production assets would result in non-aligned shareholder interests and likely eventually lead to conflicts over time. If Nadeau were to pursue discussions for a sale of the St-François Plant, the structure needed to be such that shareholders had the same aligned interests; and
- (c) even though the negotiated market price for live chicken in New Brunswick was 6.5¢ per kg. higher than the negotiated market price in Québec, Nadeau would consider a market based incentive plan for New Brunswick producers.

20. Nadeau subsequently:

- (a) advised Westco that Nadeau would be prepared to look at an ownership structure where the Nadeau and Westco assets would be pooled and Westco and Maple Lodge would each own a part of the combined operations; and
- (b) developed an incentive plan which resulted in additional payments to the Respondents totalling \$830,000 through the end of 2007.

21. Westco did not respond to Nadeau's offer to pool assets. Rather, it proceeded, as early as March, 2007, to enter into a "partnership" with Olymel. The "partnership" thereafter took steps

aimed at destroying Nadeau. Nadeau was advised that if it did not sell the St-François Plant to the "partnership" at a price that took no account whatsoever of Nadeau's accumulated business and goodwill, its chicken supply would be cut off. The details of the conduct of Westco, Olymel and the other Respondents, are set out in Nadeau's Statement of Grounds and Material Facts herein.

22. With regard to Westco's allegations that it intends to build a processing plant in New Brunswick, as of June, 2008, Westo had not:

- (a) purchased any land;
- (b) paid for any equipment;
- (c) obtained any permits or approvals;
- (d) signed any contracts in connection with construction; or
- (e) determined whether the supposed plant would be in New Brunswick or Québec.

23. If Westco intends to build a plant at all, which is not admitted but denied, any such plant will not be operational before the year 2010, at the earliest.

D. QUASI-JURISDICTIONAL ISSUES

24. The Respondent Westco argues (for example, in paragraphs 6 and 10 of its Response), that the order sought by Nadeau is an indirect attempt to obtain a plant supply guarantee, which has so far not been provided to it under New Brunswick law.

25. The Respondent Acadia alleges (paragraphs 51-56 of Acadia's Response) that the passage in New Brunswick of Bill 81 (which has been passed but not proclaimed) has, in effect, "occupied the field" in this case. ("À partir du moment où le législateur occupe un champ, le

pouvoir judiciaire doit, sur le même objet, agir avec grande déférence et ne pas provoquer de choc entre les deux pouvoirs d'intervention.")

26. The Respondent Dynaco suggests (Dynaco Response, paragraphs 24-29) that the Tribunal ought to "read down" its powers ("interprète de manière atténué") in order to preserve constitutional equilibrium ("afin de préserver l'équilibre constitutionnel canadien").

27. Nadeau denies the legal validity of the foregoing arguments, and says that they are in any event inapplicable to the case at bar.

28. As noted above, a guaranteed supply to processing plants in Ontario and Québec is a feature of the operation of the supply management system in those provinces, but does not currently exist in New Brunswick.

29. If, and to the extent that, any legislatively guaranteed supply to the St-François Plant is actually implemented in New Brunswick before the hearing in this matter, that supply can and will be taken into account as a fact in these proceedings. If, on the other hand, no guaranteed supply is actually implemented, then this Tribunal can and should determine the issues based on the Respondents' proposed refusal to supply, which would remove 271,350 chickens per week from Nadeau, that is, removal of 100% of the live chicken that has been historically supplied to Nadeau by the Respondents.

30. The actions, or the failure to act, by provincial authorities in New Brunswick are otherwise wholly irrelevant to these proceedings.

31. To the extent that the arguments made by the Respondents amount to a jurisdictional challenge to the Tribunal's authority or discretion in these proceedings, they are contrary to well-

established authority. That authority makes it clear that the Tribunal has plenary jurisdiction to make the order sought herein by Nadeau. There is no legal impediment to the exercise by the Tribunal of its jurisdiction under section 75 of the *Competition Act*.

E. NADEAU MEETS THE TESTS SET OUT IN SECTION 75

(i) Substantial Effect (s. 75(1)(a))

32. It is undisputed that the Respondents' refusal to deal will deprive Nadeau of 271,350 chickens *per week*, or about 48% of Nadeau's current production of 565,800 chickens per week. Even in the absence of anything else, this would satisfy the test under s. 75 (1)(a).

33. Each 100,000 chickens represent approximately 150,000 kgs. of saleable product with a selling value of approximately \$3 per kg., or \$450,000. The profit on this volume, in fiscal 2007, was approximately \$.50 per kg., or \$75,000. Accordingly, the removal of Westco's 186,230 birds alone would cause revenue loss of over \$830,000 *per week*. Because of the high level of fixed costs, loss of the Westco birds alone would reduce profits by about 50% on an annualized basis.

34. If Westco, Acadia and Dynaco cut off Nadeau's supply, the St-François Plant will only be able to run at 40% of capacity (just over $\frac{3}{4}$ of 1 shift). Nadeau would be unable to continue to employ its employees. A majority of the 340 jobs would be lost immediately, and the viability of the whole plant would be severely compromised.

35. Nadeau supplies reliable and predictable amounts of chicken to its customers, in a timely manner, that meet specific weight requirements for each individual customer. Nadeau requires a full range of chickens of specified gender, weights and ages, in order to be able to continue to meet volume and size commitments.

36. Interruption of supply would create an immediate inability to fulfill the needs of Nadeau's customers. This would cause immediate damage to the relationships Nadeau has built with its customers over the last 18 years. More specifically, this would result in: a loss of confidence, a loss of goodwill, a potential loss of market share, and a potential loss of customers.

37. The refusal to deal in this matter would clearly have a direct and very substantial effect on Nadeau's business.

(ii) *Inability to Obtain Adequate Replacement Supplies (s. 75(1)(a))*

38. If the Respondents remove their birds from Nadeau, it will be unable to obtain adequate supplies of live chicken anywhere in the relevant market on usual trade terms.

39. The Respondents say that the current Nova Scotia (160,000) and P.E.I. (40,000) birds being supplied to Nadeau can be treated as replacements for the threatened refusal to deal of the Respondents. This is incorrect. Nadeau seeks an order requiring continuation of supply from a base of its *existing* business, which processes about 565,800 chickens per week (inclusive of the Respondents' supply and the Nova Scotia and P.E.I. birds). The relevant measure under s. 75(1)(a) of the *Competition Act* is Nadeau's *existing* business, and its *existing* supply.

40. In any event, Nova Scotia and P.E.I. chickens are *not* an adequate replacement for the Respondents' (New Brunswick) birds, because:

- (a) these birds are only being processed by Nadeau as a short-term measure following the closure in April, 2007, of one of the two processing plants in Nova Scotia, because the remaining plant cannot handle them. Contrary to the Respondents' allegations, these supplies will cease once there is a local plant capable of processing these birds; and

(b) it is hard to transport live chickens over long distances, especially in the cold of winter and in the heat of summer. Nadeau has problems transporting chicken from Nova Scotia, including logistical problems, increased transportation costs, higher rates of attrition, occasional unacceptable death rates in transit, and concerns raised under laws governing livestock handling. There are major advantages to Nadeau in maintaining all of its historic New Brunswick supply, including increased efficiency, reduced costs, and the ability to closely match production of live chicken to anticipated processing needs.

41. Accordingly, the relevant geographic market for supplies of live chicken for the purposes of s. 75(1)(a) is New Brunswick. There are no replacement supplies available from New Brunswick producers.

42. In the alternative, if the relevant supply market under section 75(1)(a) extends beyond New Brunswick, which is not admitted but denied, it encompasses only those producers in Québec:

- (a) who are not bound by express or implied contracts with other processors;
- (b) who are willing and able to supply chicken to Nadeau at a price that is equal to or lower than the New Brunswick price (inclusive of transportation and other corollary costs);
- (c) whose facilities are within 7 hours by truck (including in winter) from the St-François Plant; and
- (d) who are able to grow chicken of the size and quality required by Nadeau's customers.

43. There are nowhere near enough producers who meet the above criteria, to permit replacement of the Respondents' supply. Nadeau is therefore unable to obtain adequate replacement supplies of chicken.

(iii) Insufficient Competition (s. 75(1)(b))

44. To the extent that the relevant market for the purposes of s. 75(1)(b) is New Brunswick, the Respondents have an effective monopoly, as described above. There is therefore insufficient competition within the meaning of s. 75(1)(b).

45. In the alternative, even if the relevant market extends to production facilities in neighbouring provinces, there is insufficient competition among producers. This is because, as described above, the supply management system: limits new entrants; matches production to expected demand; and sets (minimum) prices. Accordingly, producers have ready markets for all their chicken, and need not compete with each other on price. There is no meaningful competition at the production level of the market at all.

(iv) Willingness to Meet Usual Trade Terms (s. 75(1)(c))

46. Nadeau has always met the usual and customary trade terms set by the CFNB and the Respondents. There is no evidence to the contrary.

(v) Ample Supply (s. 75(1)(d))

47. The Respondents allege that there is not an "ample supply" of chicken because the supply management system creates limits on supply. This is not correct. Supplies allocated to existing producer quotas are adjusted every eight weeks following a consultative process between the federal body (Chicken Farmers of Canada) and the provincial producer boards (such as the CFO and the CFNB). The process is intended to ensure that there is an ample supply of chicken to meet consumer needs.

48. In fact, production of chicken has increased substantially over time. In New Brunswick alone, chicken production increased by close to 60% in the period from 1990 to 2000. There are no *a priori* limits on production.

49. Westco also argues that its production is "promised" to Olymel. However, since Westco's chickens are actually sold to the "partnership", there is no innocent third party whose interests need to be considered.

50. Westco relies upon paragraphs 18 – 21 of the decision in *Quinlan's* in connection with its argument concerning "ample supply". In that case, the Tribunal refused to require the Respondent to supply Harley-Davidson motorcycles to the applicant by way of interim order, because they were not in "ample supply". However, that was a special case. All of the supply of 2005 Harley-Davidson motorcycles in that case had been ordered from the Harley-Davidson factory and allocated to independent third party dealers in March, 2004 (the interim application was heard in October, 2004). The motorcycles had actually begun arriving at these other dealerships in August, 2004. The evidence was that any interim order would "not only harm [the respondent], but will harm other independent dealerships as well". Clearly, the decision in *Quinlan's* was driven by the fact that pre-existing customers, innocent third parties, would be deprived of product already sold to them. The equities in that case favoured the refusal of an order.

51. By contrast, in this case, there is no innocent third party. Olymel is not independent, and was present at all of the key meetings with Nadeau. Indeed, it is a co-conspirator with Westco in the attempt to destroy Nadeau by refusing chicken supplies. At the August 19, 2007 meeting, Réjean Nadeau of Olymel was present with Mr. Soucy when Nadeau was told that, if Nadeau

would not sell the St-François Plant to Olymel/Westco at a price acceptable to it, then all of the chicken produced by Westco would be diverted to Québec, and Olymel/Westco would build its own plant. Westco has admitted this.

(vi) Effect on Competition (s. 75(1)(e))

52. As noted above, the relevant geographic market for the purposes of s. 75(1)(e) is Québec and the Maritimes.

53. The Respondents' refusal to supply will render Nadeau unable to effectively continue in business, since other competing processors, and in particular Olymel, are not being denied supplies. The disappearance of Nadeau, coupled with guaranteed supply from Westco, Dynaco and Acadia, would undoubtedly strengthen Olymel at the cost of other players in the processor market, and would enable it to raise prices and limit supply. This will have a substantial effect on competition in the market, and on customers.

54. Further, even if someday Olymel/Westco do build a new plant in New Brunswick, which is not admitted but denied, this would by no means be a replacement for Nadeau. In fact, such would simply serve to further strengthen Olymel's position and increase Westco's dominance, with the adverse effects on competition noted in the Statement of Grounds and Material Facts herein. As stated by the Tribunal:

"...for a refusal to deal to have an adverse effect on a market, the remaining market participants must be placed in a position, as result of the refusal, of created, enhanced or preserved market power".

*Ref: B-Filer Inc. et al v The Bank of Nova Scotia,
2006 Comp. Trib. 42, at para. 208*

55. As well, since there are a limited number of producers in each province, if any Québec producers divert supply to Nadeau, those producers' pre-existing processor customers will be forced to retaliate by further increasing prices to their own or other processors' producers. This would create huge additional costs for all processors. These additional costs, if they cannot be passed on to consumers, may drive other processors out of business, thus further reducing competition at the processor level of the chicken market.

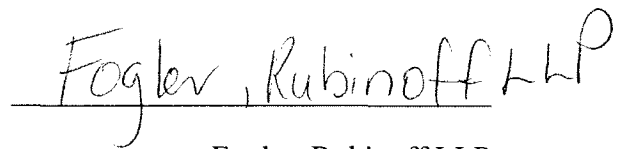
F. CONCLUSION

56. Nadeau says that this is an appropriate case for the exercise of the Tribunal's discretion, and that an order should be made under section 75 of the *Competition Act*, as requested in the Notice of Application herein. Nadeau also seeks its costs of these proceedings.

57. Nadeau opposes the Respondents' request that the hearing be conducted solely in French. Nadeau asks that it be conducted in English.

Respectfully Submitted

July 10, 2008



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