

Competition Tribunal



Tribunal de la Concurrence

CT-1997/003 – Doc # 22

IN THE MATTER OF an application by the Director of Investigation and Research pursuant to section 75 of the *Competition Act*, R.S.C. 1985, c. C-34;

AND IN THE MATTER OF an inquiry relating to the refusal of Warner Music Canada Ltd. and its affiliates, Warner Music Group Inc. and WEA International Inc., to deal with BMG Direct Ltd.

B E T W E E N:

**The Director of Investigation and Research**

Applicant

- and -

**Warner Music Canada Ltd.  
Warner Music Group Inc.  
WEA International Inc.**

Respondents



**REASONS AND ORDER  
ON RESPONDENTS' MOTION TO STRIKE  
DIRECTOR'S APPLICATION**

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**Dates of Hearing:**

December 4-5, 1997

**Members:**

McKeown J. (presiding)  
Simpson J.  
Mr. Lorne R. Bolton

**Counsel for the Applicant:**

**Director of Investigation and Research**

D. Martin Low, Q.C.  
Duane Schippers

**Counsel for the Respondents:**

**Warner Music Canada Ltd.**  
**Warner Music Group Inc.**  
**WEA International Inc.**

John F. Rook, Q.C.  
David Stratas  
Mahmud Jamal

**COMPETITION TRIBUNAL**  
**REASONS AND ORDER**  
**ON RESPONDENTS' MOTION TO STRIKE**  
**DIRECTOR'S APPLICATION**

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*The Director of Investigation and Research*

v.

*Warner Music Canada Ltd. et al.*

**I. INTRODUCTION**

The Director brought an application alleging that the respondents' refusal to grant copyright licences to make sound recordings from their master recordings to a company, BMG (Canada), which needs such licences to compete in the mail order record club business in Canada, contravenes section 75 of the *Competition Act*. The Director alleged no anti-competitive objectives nor that the existing licences include any anti-competitive provisions. The Director in his proposed order was prepared to have BMG (Canada) obtain the licences on the usual trade terms which were to be at least as favourable as the existing licences to Columbia House (Canada), a company in which one of the respondents holds a 50 percent partnership interest. The respondents moved to strike out the Director's application.

The issue is whether, in the circumstances, the Tribunal has jurisdiction under section 75 to hear the application.

## **II. BACKGROUND**

### **(a) The Parties**

The three respondents described hereafter will be referred to collectively as the "respondents". The business of the respondents and their affiliates includes contracting with a wide variety of artists to record their performances on Warner master recordings. These master recordings are then used to manufacture sound recordings of various types including tapes, compact disks and records.

The respondent Warner Music Canada Ltd. ("Warner Canada") is an Ontario corporation which has its head office in Scarborough, Ontario. It has, *inter alia*, the right to grant licences to manufacture, distribute and sell in Canada sound recordings of performances by Canadian artists which have been recorded on Warner master recordings.

The respondent WEA International Inc. ("WEA (U.S.)") is a Delaware corporation which has its head office in New York City. It has, *inter alia*, the right to grant licences to manufacture, distribute and sell in Canada sound recordings of performances which have been recorded on Warner master recordings by non-Canadian artists.

The respondent Warner Music Group Inc. ("Warner Music (U.S.)") is a Delaware corporation which has its head office in New York City. It is involved in the business of managing companies affiliated with Warner Communications Inc., including the respondents

Warner Canada and WEA (U.S.). Warner Music (U.S.) is alleged to be the party responsible for negotiating licences granted by Warner Canada and WEA (U.S.).

The Columbia House Company in Canada ("Columbia House Canada") is an equal partnership of Warner Canada and Sony Music Entertainment (Canada) Inc., and is located in Scarborough, Ontario. It operates a mail-order record club business throughout Canada which offers its customers sound recordings in most music categories.

BMG Direct Ltd. ("BMG (Canada)") is a wholly-owned subsidiary of BMG Direct Marketing Inc. ("BMG (U.S.)") and is located in Mississauga, Ontario. It commenced a national mail-order record club business in Canada in December 1994. With the entry of BMG (Canada), Columbia House (Canada) ceased to be the only mail-order record club in Canada offering sound recordings in most music categories.

**(b) The Director's Application**

The Director of Investigation and Research ("Director") made the application to the Competition Tribunal ("Tribunal") pursuant to section 75 of the *Competition Act* ("Act").

In the application, the Director alleges that, contrary to section 75 of the Act, the respondents have refused to deal with BMG (Canada) by refusing to grant it licences to make

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<sup>1</sup>  
R.S.C. 1985, c. C-34.

sound recordings from Warner master recordings. The Director alleges that BMG (Canada) needs such licences in order to compete in the mail-order record club business in Canada. However, the Director does not allege that the respondents' conduct in refusing to grant licences is motivated by anti-competitive objectives, and does not allege that the respondents' existing licences include anti-competitive provisions.

In the application, the Director seeks an order from the Tribunal to compel the respondents to issue licences to BMG (Canada). The order sought in paragraph 67 of the application requires that:

- (i) the Respondents accept BMG Direct Ltd. ("BMG") as a customer on usual trade terms for the supply of licences to manufacture, advertise, distribute and sell sound recordings made from master recordings owned or controlled by the Respondents or any of their affiliates;
- (ii) the terms of the licences sought in (i) above be at least as favourable in all respects as the terms of any comparable licence or licences to The Columbia House Company in Canada ("CHC"). For greater certainty, the licences sought in (i) above shall provide BMG with the right to at least an equal number and variety of Warner master recordings as are supplied to CHC by the Respondents or any of their affiliates;
- (iii) the licences referred to above be supplied within 30 days of the issuance of the Tribunal's Order; and
- (iv) such further or other Order as the Tribunal may consider appropriate.

### **III. THE PRESENT MOTION**

The respondents' motion is to strike out the Director's application against all the respondents on the basis that section 75 of the Act does not give the Tribunal jurisdiction to compel the respondents to issue licences for the manufacture, distribution and sale of sound recordings of the performances on the Warner master recordings. The respondents also take the

position that the Tribunal does not have jurisdiction over WEA (U.S.) and Warner Music (U.S.), that the Act does not have extraterritorial application, that effective service on WEA (U.S.) and Warner Music (U.S.) has not been accomplished, that this motion is timely and that this is a proper case for a reference to the Federal Court of Appeal under sections 18.3 and 28(2) of the *Federal Court Act*.

The Director opposes the motion saying that the Tribunal has jurisdiction to order a licence under section 75, that the Tribunal has jurisdiction over WEA (U.S.) and Warner Music (U.S.), that the question of the extraterritoriality of the Act is not in issue since the Director is only seeking redress in respect of the respondents' business activities in Canada, that proper service has been effected, that this motion is premature and that a reference to the Federal Court of Appeal would also be premature.

At the hearing of the motion, the Tribunal heard the jurisdictional argument and arguments about the prematurity of this motion and the extraterritorial application of the Act. The parties maintained their positions in respect of a reference to the Federal Court of Appeal but did not argue the issue, preferring to rely on their memoranda.

The Tribunal adjourned *sine die* without hearing submissions on the other issues. As these reasons disclose, the Tribunal has decided that the motion is not premature and that a reference to the Federal Court of Appeal will not be ordered. The Tribunal has also concluded that it lacks jurisdiction to grant the relief sought by the Director in his application. For this

reason, the issues of extraterritoriality, proper service and jurisdiction over the person will not be addressed.

#### **IV. THE FACTS**

For the purpose of this motion, the Tribunal relies on the following undisputed facts:

- (1) WEA (U.S.) has a licence agreement with Columbia House (Canada) entitling Columbia House (Canada) to manufacture, distribute and sell in Canada sound recordings made from Warner master recordings of performances by non-Canadian artists.
- (2) Warner Canada has licensed Columbia House (Canada) to manufacture, distribute and sell in Canada sound recordings made from Warner master recordings of performances by Canadian artists.
- (3) When BMG (Canada) commenced its direct mail-order record club business in Canada, it had obtained reproduction, distribution and sales licences for a number of record labels, but it had not reached an agreement with Warner Music (U.S.) respecting Warner Canada and WEA (U.S.) reproduction and sales licences, and no such agreement has since been reached. It is the respondents' refusal to grant these licences on terms similar to those found in the licences to Columbia House (Canada) that triggered the Director's application. There is no issue that BMG (Canada) can purchase the respondents' manufactured CDS, tapes and records at the wholesale level. However, the



prices at wholesale are too high to enable BMG (Canada) to compete in the mail-order record club business. To compete in that business, BMG (Canada) must obtain the cost savings that are possible if it manufactures the Warner sound recordings itself under licences from the respondents.

(4) BMG (Canada) is unable to offer its customers the broad range of sound recordings which is available through Columbia House (Canada), because only Columbia House (Canada) carries sound recordings of performances by artists on Warner master recordings.

(5) The respondents concede, for the purpose of this motion, that if BMG (Canada) is unable to obtain licences for the reproduction and sale of sound recordings made from Warner master recordings, it will be substantially affected and will be unable to continue its mail-order record club business in Canada.

## **V. ISSUE AND QUESTIONS**

The issue is whether the Tribunal has jurisdiction, pursuant to section 75 of the Act, to make an order compelling the respondents to licence BMG (Canada) to manufacture, distribute and sell sound recordings of performances on Warner master recordings. It is worth emphasizing that the Tribunal was only asked to order that a compulsory license be granted to BMG (Canada) where the respondents refused to do so upon BMG (Canada)'s request. The Tribunal was not

asked to find that a physical product was in short supply in the market due to a refusal to grant a copyright licence.

Section 75 of the Act reads as follows:

75. (1) Where, on application by the Director, the Tribunal finds that

(a) a person is substantially affected in his business or is precluded from carrying on business due to his inability to obtain adequate supplies of a product anywhere in a market on usual trade terms,

(b) the person referred to in paragraph (a) is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market,

(c) the person referred to in paragraph (a) is willing and able to meet the usual trade terms of the supplier or suppliers of the product, and

(d) the product is in ample supply,

the Tribunal may order that one or more suppliers of the product in the market accept the person as a customer within a specified time on usual trade terms unless, within the specified time, in the case of an article, any customs duties on the article are removed, reduced or remitted and the effect of the removal, reduction or remission is to place the person on an equal footing with other persons who are able to obtain adequate supplies of the article in Canada.

(2) For the purposes of this section, an article is not a separate product in a market only because it is differentiated from other articles in its class by a trade-mark, proprietary name or the like, unless the article so differentiated occupies such a dominant position in that market as to substantially affect the ability of a person to carry on business in that class of articles unless that person has access to the article so differentiated.

(3) For the purposes of this section, the expression "trade terms" means terms in respect of payment, units of purchase and reasonable technical and servicing requirements.

The issue raises the following questions, which will be discussed in turn:

- (1) What is the nature of the respondents' intellectual property interest in the Warner master recordings?
- (2) Could a copyright right be a "product" pursuant to the definitions in section 2 of the Act?
- (3) Is it reasonable to conclude that a licence is a "product" as that term is used in section 75 of the Act?
- (4) Does the Tribunal have sufficient evidence to decide the issue on this motion?

## VI. DISCUSSION

Counsel for the respondents indicated that he would be focusing on the respondents' copyright rights in the Warner master recordings for the purposes of this motion, although he mentioned in passing that other intellectual property rights also exist.

The Director did not dispute that the respondents hold Canadian copyright in the Warner master recordings which are the subject of the application. Even so, counsel for the respondents made detailed submissions which satisfied the Tribunal that, under the *Copyright Act*, the respondents have the exclusive right to reproduce musical works and to make the contrivances (i.e., records, tapes, CDS, etc.) for the performance of musical works. In particular, section 3 of the *Copyright Act* defines copyright as the sole right to produce or reproduce the work or any substantial part thereof in any material form whatsoever, and, for the purposes of this motion, the musical works are subject to copyright and the copyright includes the right to make a sound recording as provided under section 3. Copyright subsists in Canada for Warner Canada by reason of subsection 5(1) of the *Copyright Act* and in Canada for WEA by reason of the treaty provisions referred to in section 5. Since 1993, there has been no provision in the *Copyright Act* which limits the copyright holder's sole and exclusive right to licence. These conclusions mean that as a matter of copyright law the respondents have the right to refuse to licence the Warner master recordings to BMG (Canada).

The Director's counsel submitted that the definitions of "article" and "product" in section 2 of the Act are broad enough to encompass a copyright right as a form of personal property.

Counsel for the respondents agreed and the Tribunal accepts this submission. However, this conclusion does not answer the next question, which is whether the licences are products within the meaning of section 75 of the Act.

The Director's position is that the respondents' manufacturing, distribution and sales licences are the "product" for the purpose of section 75 and that the market for the purpose of the section is Canada. The Director says that, given these definitions and, in the absence of language which excludes the recognition of intellectual property rights in section 75, the section clearly applies to the facts of this case.

With regard to paragraph 75(1)(a), the Director notes that the respondents do not dispute, for the purposes of this motion, that BMG (Canada) is being substantially affected in its business by reason of their refusal to grant it licences to manufacture, distribute and sell sound recordings of the Canadian and non-Canadian performances on the Warner master recordings. The Director further says that paragraph 75(1)(b) applies because BMG (Canada)'s inability to obtain adequate supplies is caused by insufficient competition among suppliers of the product in the market, i.e., among Warner Canada, WEA (U.S.) and Warner Music (U.S.). Further, with regard to paragraph 75(1)(c), the Director acknowledges that there is only one supplier of each licence (Warner Canada and WEA (U.S.)) and that the only two licences in place in Canada are the two respondents' licences to Columbia House (Canada). However, the Director says that the Tribunal may have regard to the terms of licences granted by other comparable licensors throughout North America in order to reach a conclusion about what might be usual trade terms in Canada if additional licences were to be granted by the respondents. Finally, on the subject of paragraph

75(1)(d), the Director submits in paragraph 16 of his application that, because the two licences to Columbia House (Canada) are non-exclusive, there could be further licences if the respondents were willing to grant them. Accordingly, the product is in ample supply. For all these reasons, the Director says that section 75 can be sensibly read to apply to a refusal to grant a copyright licence.

The Director is also of the view that policy considerations favour the application of section 75. He states that, if a refusal to grant a licence is not caught by section 75, the effect will be that intellectual property rights will be seen to "trump" competition law. He submits that dire consequences will follow a finding that the Tribunal has no jurisdiction in this case. He is concerned that all distribution arrangements involving the licensing of manufacturing rights will be beyond the Director's reach in cases where an alleged refusal to supply is accomplished by a refusal to licence. He also suggests that this problem will augment because businesses will rearrange their affairs to increase their reliance on licence arrangements.

On the other hand, the respondents say that the language of section 75 has been "tortured" by the Director to force it to apply to this case. They submit that the Director's interpretation of the section ignores the respondents' copyright rights. For example, licences are only in ample supply if one assumes that the respondents do not have the right to refuse to grant them. Similarly, to find that usual trade terms may exist ignores the reality that Columbia House (Canada) is the only licensee in Canada, and that Canada is the market as defined by the Director. Furthermore, even if granted, any future licences must be negotiated. In these circumstances, the respondents submit that one could not find that there are usual trade terms.

The respondents also counter the Director's position by saying that nowhere in the Act is the Tribunal given the power to override the simple exercise of intellectual property rights and that, for this reason, any grant of such a power must be based on clear and unequivocal language. This is particularly true in their submission in view of the provisions of section 32 of the Act. Section 32 deals, *inter alia*, with situations in which the use of exclusive copyright rights prevents, or lessens, unduly competition in the manufacture or sale of an article. In such situations, jurisdiction is given to the Federal Court of Canada to make a wide range of orders including directing the grant of a licence.

Section 32 differs from section 75 in that: (i) it is specifically directed to the use of copyright rights; (ii) a competition impact test must be met before an order will be made; (iii) the Attorney General of Canada and not the Director is the applicant and; (iv) there is a defence based on treaty provisions. Section 32 reads as follows:

32. (1) In any case where use has been made of the exclusive rights and privileges conferred by one or more patents for invention, by one or more trade-marks, by a copyright or by a registered integrated circuit topography, so as to

- (a) limit unduly the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any article or commodity that may be a subject of trade or commerce,
  - (b) restrain or injure, unduly, trade or commerce in relation to any such article or commodity,
  - (c) prevent, limit or lessen, unduly, the manufacture or production of any such article or commodity or unreasonably enhance the price thereof, or
  - (d) prevent or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, transportation or supply of any such article or commodity,
- the Federal Court may make one or more of the orders referred to in subsection (2) in the circumstances described in that subsection.

(2) The Federal Court, on an information exhibited by the Attorney General of Canada, may, for the purpose of preventing any use in the manner defined in subsection (1) of the exclusive rights and privileges conferred by any patents for invention, trade-marks, copyrights or registered integrated circuit topographies relating to or affecting the manufacture, use or sale of any article or commodity that may be a subject of trade or commerce, make one or more of the following orders:

- (a) declaring void, in whole or in part, any agreement, arrangement or licence relating to that use;

- (b) restraining any person from carrying out or exercising any or all of the terms or provisions of the agreement, arrangement or licence;
  - (c) directing the grant of licences under any such patent, copyright or registered integrated circuit topography to such persons and on such terms and conditions as the court may deem proper or, if the grant and other remedies under this section would appear insufficient to prevent that use, revoking the patent;
  - (d) directing that the registration of a trade-mark in the register of trade-marks or the registration of an integrated circuit topography in the register of topographies be expunged or amended; and
  - (e) directing that such other acts be done or omitted as the Court may deem necessary to prevent any such use.
- (3) No order shall be made under this section that is at variance with any treaty, convention, arrangement or engagement with any other country respecting patents, trade-marks, copyrights or integrated circuit topographies to which Canada is a party.

The respondents argue that, in the absence of clear language, it would be wrong to conclude that the Tribunal, as an inferior tribunal, has been given the power to ignore intellectual property rights and order the respondents to grant what are, in effect, compulsory licences in favour of BMG (Canada) when the Federal Court can make such an order only after the applicant meets a competition impact test and only after any defences based on international treaty rights are considered.

The respondents also rely on subsection 79(5) of the Act, which deals with abuse of dominant position and which provides, *inter alia*, that acts engaged in only pursuant to the exercise of rights under the Copyright Act are not anti-competitive acts. In the respondents' submission, because Parliament expressly excluded the simple exercise of copyright rights from the definition of anti-competitive acts in section 79, one cannot reasonably find jurisdiction over such matters in section 75 without a clear statement to that effect.

Having considered the submissions discussed here and the additional points in the parties' memoranda, the Tribunal has concluded that on the facts of this case the licences are not a

product as that term is used in section 75 of the Act, because on a sensible reading section 75 does not apply to the facts of this case. Although a copyright licence can be a product under the Act, it is clear that the word "product" is not used in isolation in section 75, but must be read in context. The requirements in section 75 that there be an "ample supply" of a "product" and usual trade terms for a product show that the exclusive legal rights over intellectual property cannot be a "product" -- there cannot be an "ample supply" of legal rights over intellectual property which are exclusive by their very nature and there cannot be usual trade terms when licences may be withheld. The right granted by Parliament to exclude others is fundamental to intellectual property rights and cannot be considered to be anti-competitive, and there is nothing in the legislative history of section 75 of the Act which would reveal an intention to have section 75 operate as a compulsory licensing provision for intellectual property.

As well, the Tribunal has accepted the respondents' submissions that, when considered in the context of sections 32 and 79(5) of the Act, the term "product" in section 75 cannot be read to include these copyright licences. These submissions are discussed above and need not be repeated here.

Although the Tribunal was commenting on section 79 and intellectual property (trade-marks) in *Director of Investigation and Research v. Tele-Direct (Publications) Inc.*, we are of the view that its statement is very compelling in the circumstances of the motion before us:

The respondents' refusal to licence their trade-marks falls squarely within their prerogative. Inherent in the very nature of the right to license a trade-mark is the right for the owner of the trade-mark to determine whether or not, and to whom, to grant a licence; selectivity in licensing is fundamental to the rationale behind protecting trade-



goodwill in the marketplace. The decision to license a trade-mark -- essentially, to marks. The respondents' trade-marks are valuable assets and represent considerable share the goodwill vesting in the asset -- is a right which rests entirely with the owner of the mark. The refusal to license a trade-mark is distinguishable from a situation where anti-competitive provisions are attached to a trade-mark licence. 4

The *Copyright Act* is similar to the *Trade-marks Act*, in that it allows the trade-mark owner to refuse to license and it places no limit on the sole and exclusive right to license.

Finally, the Tribunal adopts Rothstein J.'s response to the Director's argument about dire policy consequences in his decision regarding the Tribunal's jurisdiction over certain undertakings made to the Director pursuant to the consent order in the *Imperial Oil* case:

The *Competition Act* does not confer open-ended jurisdiction on the Tribunal to deal with any and all competition issues. It is given specific powers which are set out in the *Competition Act* and in the *Competition Tribunal Act*. It may only act where it has been given the power to do so. 6

Finally, on the issue of the prematurity of this motion, the Director's counsel pressed the Tribunal to adopt a cautious approach and to avoid making a decision without the benefit of all the relevant facts. However, when pressed in turn about what facts were missing which would be relevant to the issue of jurisdiction, counsel responded that the Tribunal needs to hear facts concerning the terms of the Columbia House (Canada) licences and similar licences in North America. When asked why these would be relevant, counsel for the Director indicated that they might support an inference of anti-competitive motive on the respondents' part.

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<sup>5</sup> R.S.C. 1985, c. T-13.

<sup>6</sup> *Director of Investigation and Research v. Imperial Oil Limited* (10 November 1994), CT8903/463, Reasons for Decision Regarding Jurisdiction Over Undertakings at 14-15, [1994] C.C.T.D. No. 23 (QL) (Comp. Trib.).

There are two problems with this submission. Firstly, section 75 says nothing about motive and, secondly, the Director has not pleaded anything about motive in his application. This being the case, it is clear that the missing facts would not be relevant at a hearing on the merits as this case is presently conceived. Accordingly, the absence of such facts should not forestall a decision on this motion at this time.

The Director's counsel also indicated that the Tribunal needed more information about the nature of the direct mail-order record club business. He submitted that once the Tribunal was in possession of such information, it would accept that in this business the licence is a "product" because it is just a surrogate for the manufactured records, tapes and CDS which are produced pursuant to the licence. However, Director's counsel conceded that in all cases where licences grant a right to manufacture, the licence could be seen as a surrogate for the finished goods.

In spite of these submissions, the Tribunal has not been persuaded that it lacks any information about the nature of the direct mail-order record business which would contribute to a decision on the issue of its jurisdiction under section 75 of the Act in the circumstance of this motion.

## **VII. CONCLUSIONS**

As the *Competition Tribunal Rules* do not deal with this motion, the Tribunal has had regard to the Federal Court Rules, wherein Rule 419 (striking a pleading for disclosing no cause

of action) and Rule 474 (preliminary determination of a question of law) seem most apt. The Federal Court of Appeal considered Rule 474 in *Berneche v. Canada* and said:

What Rule 474(1)(a) requires is that the Court be satisfied (1) that there is no dispute as to any fact material to the question of law to be determined; (2) that what is to be determined is a pure question of law, and (3) that its determination will be conclusive of a matter in dispute so as to eliminate the necessity of a trial or, at least, shorten or expedite the trial. <sup>8</sup>

In the Tribunal's view, the respondents have met these tests and have also made out a plain and obvious case for striking out the application as required under Rule 419. Accordingly, the Tribunal has concluded that section 75 of the Act does not give it jurisdiction to make the order sought by the Director in his application. An order will therefore be made granting this motion and striking out the Director's application against the respondents.

## **VIII. ORDER**

FOR THESE REASONS, THE TRIBUNAL ORDERS THAT the Director's application pursuant to section 75 of the Act, filed with the Tribunal on September 30, 1997 against the respondents, be struck.

DATED at Ottawa, this 18<sup>th</sup> day of December, 1997.

SIGNED on behalf of the Tribunal by the presiding judicial member.

(s) W.P. McKeown  
W.P. McKeown

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<sup>7</sup> C.R.C. 1978, c. 663.

<sup>8</sup> [1991] 3 F.C. 383 at 388.