Competition Tribunal Tribunal de la Concurrence

CT - 1994 / 003 – Doc # 204a

IN THE MATTER OF an application by
the Director of Investigation and Research
under sections 77 and 79 of the *Competition Act*,
R.S.C. 1985, c. C-34.

B E T W E E N :

The Director of Investigation and Research

Applicant

\- and -

Tele-Direct (Publications) Inc.
Tele-Direct (Services) Inc.

Respondents

\- and -

Anglo-Canadian Telephone Company
NDAP-TMP Worldwide Ltd. and
Directory Advertising Consultants Limited
Thunder Bay Telephone

Intervenors

REASONS AND ORDER

Dates of Hearing:

September 5-8, 11-14, 27-29; October 2-3, 5-6, 10-13, 16-20, 23-27; 30;
November 2-3, 6-10, 14-17, 20-22, 24, 27-30; December 1, 4, 6-8, 1995;
January 22-26; February 12-16, 23, 26-29; March 1, 1996

Members:

Rothstein J. (presiding)
Frank Roseman
Christine Lloyd

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VIII. TIED SELLING (cont'd)

GUIDE TO ACRONYMS

ASR	authorized selling representative
CANYPS	Canadian Yellow Pages Service
CCS	cost of customer service
CMR	Certified Marketing Representative
CPI	consumer price index
CPM	cost per thousand
CRTC	Canadian Radio-television and Telecommunications Commission
DAC	Directory Advertising Consultants Limited
DSP	Dial Source Plus, Inc.
GSF	general sales force
NAM	national account manager
NAR	national account representative
NDAP	NDAP-TMP Worldwide Ltd.
NYPSA	National Yellow Pages Service Association
RRC	raising rivals' costs
telco	telephone company
TPA	Total Performance Assessment
TYP	Talking Yellow Pages
VAN	Value-Added Network

VIA	Very Important Advertiser
YPPA	Yellow Pages Publishers Association

COMPETITION TRIBUNAL

REASONS AND ORDER

The Director of Investigation and Research

v.

Tele-Direct (Publications) Inc. et al.

I. INTRODUCTION

This application is concerned, broadly speaking, with two aspects of telephone directory or, as it is commonly referred to "Yellow Pages", advertising. The first aspect is the provision of advertising space in a published directory or the publishing business. This aspect of the business encompasses activities such as the compilation, printing and distribution of the directory. The second aspect is the provision of the advertising services required to create a finished advertisement for publication in a directory. The services aspect of the business includes such elements as locating customers, selling advertising space, and providing advice and information to customers on the design, content, creation and placement of directory advertising.

The applicant in this case is the Director of Investigation and Research ("Director"), the public official charged with enforcement of the *Competition Act* ("Act").[1] The Director brings an application against the respondents, Tele-Direct (Publications) Inc. and Tele-Direct (Services) Inc., under sections 77 and 79 of the Act, the provisions dealing with, as they are commonly known, tied selling and abuse of dominant position:

> 77. (1) For the purposes of this section . . .
> "tied selling" means
> (*a*) any practice whereby a supplier of a product, as a condition of supplying the product (the "tying" product) to a customer, requires that customer to
> (i) acquire any other product from the supplier or the supplier's nominee, or
> (ii) refrain from using or distributing, in conjunction with the tying product, another product that is not of a brand or manufacture designated by the supplier or the nominee, and
> (*b*) any practice whereby a supplier of a product induces a customer to meet a condition set out in subparagraph (*a*)(i) or (ii) by offering to supply the tying product to the customer on more favourable terms or conditions if the customer agrees to meet the condition set out in either of those subparagraphs.
>
> (2) Where, on application by the Director, the Tribunal finds that . . . tied selling, because it is engaged in by a major supplier of a product in a market or because it is widespread in a market, is likely to
> (*a*) impede entry into or expansion of a firm in the market,
> (*b*) impede introduction of a product into or expansion of sales of a product in the market, or
> (*c*) have any other exclusionary effect in the market,
> with the result that competition is or is likely to be lessened substantially, the Tribunal may make an order directed to all or any of the suppliers against whom an order is sought prohibiting them from continuing to engage in . . . tied selling and containing any other requirement that, in its opinion, is necessary to overcome the effects thereof in the market or to restore or stimulate competition in the market.
>
> 79. (1) Where, on application by the Director, the Tribunal finds that
> (*a*) one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,
> (*b*) that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and
> (*c*) the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market,
> the Tribunal may make an order prohibiting all or any of those persons from engaging in that practice.

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[1] R.S.C. 1985, c. C-34.

In relation to section 77, the Director alleges that the respondents have engaged in a practice whereby, as a condition of supplying advertising space in telephone directories, they have required or induced customers seeking advertising space in telephone directories to acquire another product from them, namely telephone directory advertising services. As the respondents are allegedly major suppliers of advertising space, this practice of tied selling has allegedly impeded entry into or expansion of firms in the market because advertising agencies or others would provide the services or would expand to provide increased services, were space and services not tied together by the respondents. The result, it is alleged, is that competition has been, is, or is likely to be lessened substantially.

With respect to the alleged abuse of dominant position, the Director alleges that the respondents substantially or completely control the classes or species of business they engage in, namely the provision of advertising space and the provision of advertising services. The respondents, it is alleged, have engaged in or are engaging in a practice of anti-competitive acts in each of the markets for space and for services. In the advertising space market, the alleged practice focuses on the actions taken by the respondents upon entry by competing publishers of telephone directories into some of their markets. In the services market, the alleged practice includes acts directed by the respondents against alternative or independent suppliers of services. The acts alleged to be anti-competitive in the services market cover a wide gambit, including, among others, refusal to deal directly with certain service suppliers as agents for advertisers, providing space to independent service suppliers on less favourable terms than to the respondents' internal sales staff, "squeezing" the return available to independent service providers by restricting the availability of commission over time, and refusing to license its Yellow Pages trade-marks to competing service suppliers. These practices allegedly have had, are having, or are likely to have the effect of preventing or lessening competition substantially in the markets for the provision of advertising space in telephone directories and advertising services, respectively.

The respondent Tele-Direct (Publications) Inc. is owned by Bell Canada and BCE Inc. It is comprised of two parts: a "directory" division and an "other business" division. The directory division embraces the directory publishing operations for Bell Canada in its territory, which covers most of Quebec and Ontario. The other business division is made up of various companies partly or wholly owned by BCE Inc., one of which is Tele-Direct (Services) Inc.[2] Tele-Direct (Services) Inc. publishes telephone directories under contract for non-Bell Canada telephone companies ("telcos") with discrete territories within Ontario,[3] for Télébec (owned by BCE Inc.) in parts of Quebec, and for other telcos outside of Ontario and Quebec. Tele-Direct (Services) Inc. also has international operations and includes Tele-Direct (Media) Inc., an accredited advertising agency specializing in Yellow Pages created by Tele-Direct in 1994. There is overlap between Tele-Direct (Services) Inc. and Tele-Direct (Publications) Inc. at the officer level but Tele-Direct (Services) Inc. has its own employees who run its business. In these

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[2] Others include the remaining portion of Bell Canada, Télébec, Maritime Tel & Tel, etc.

[3] E.g., the Corporation of the City of Thunder Bay, Amtelecom Inc. (Aylmer, Straffordville and Port Burwell), the Corporation of the Town of Kenora.

reasons, except where the context requires separate identification, the two respondents will be referred to together as "Tele-Direct" or the respondents.

The respondents deny each of the allegations in the Director's application. In particular, regarding the tied selling allegation, the respondents' primary position is that advertising services and advertising space form an inseparable package for reasons of efficiency and revenue growth. In response to the abuse of dominance allegations, the respondents maintain that they do not substantially or completely control, or have market power in, the alleged market as there are many adequate substitutes for telephone directory advertising, namely other local advertising media. With respect to the specific alleged anti-competitive acts, the respondents take the position that the allegations relate to acts directed at three specific groups operating in separate markets: other directory publishers, Tele-Direct's accredited agents and non-accredited service providers. Save for publishers, they assert that they are not in competition with the groups against whom their acts are said to be directed.

Five requests for leave to intervene were received and granted in this proceeding although two of those were later discontinued.

NDAP-TMP Worldwide Ltd. ("NDAP") and Directory Advertising Consultants Limited ("DAC") are accredited Yellow Pages advertising agencies which provide services to clients who wish to advertise in telephone directories, particularly those published by or for the various telcos across Canada. They arrange for the preparation and placement of the advertisements in these directories on behalf of their clients. They presented final argument on the issues relevant to the role of agencies in the market.

The Anglo-Canadian Telephone Company ("Anglo-Canadian"), through one of its divisions, publishes Yellow Pages directories in British Columbia for BC Tel and in parts of Quebec for Quebec Tel. Anglo-Canadian licenses the Yellow Pages trade-marks from the respondents. Anglo-Canadian presented final argument only on the issues related to the possible compulsory licensing of the Yellow Pages trade-marks requested by the Director as part of the abuse of dominance case.

InfoText Limited ("InfoText"), a subsidiary of Newfoundland Tel, and Thunder Bay Telephone supply subscriber listing information to Tele-Direct for directory publication for subscribers in Newfoundland and Labrador and in the city of Thunder Bay, respectively. InfoText subsequently discontinued its intervention. Both InfoText and Thunder Bay Telephone requested intervenor status only to place their requests for leave to intervene on the record, which the Tribunal allowed.

White Directory of Canada, Inc. ("White") is a non-telco publisher of telephone directories in St. Catharines, Niagara Falls and Fort Erie. White discontinued its intervention prior to the commencement of the hearing.

Preliminary Comments of the Presiding Judicial Member

The notice of application in this matter was filed on December 22, 1994. The hearing commenced in September 1995 and ended at the beginning of March 1996. This decision has taken over 11 months to issue. In view of the Tribunal's usual practice of dealing with matters before it more expeditiously, some explanation is warranted.

There is no doubt that this has been the most complex case presented to the Tribunal since its inception. In addition to a strongly contested question of market definition, the case, in reality, consists of five cases, each requiring the Tribunal to address substantial competition issues (tied selling, abuse of dominance in respect of agents, consultants and publishers and trade-marks). Each of the five cases involves a multitude of sub-issues. Many of the Director's numerous specific allegations were multifaceted. To each allegation, the respondents raised a host of defences.

The record in this case provides a telling indication of its complexity. It consists of almost 15,000 pages of transcript taken over 70 days and involving 58 witnesses, including five expert witnesses. There were 36 volumes of documents produced in the joint book of documents alone. A further 156 exhibits not included in the joint book were entered in evidence by the parties. The parties submitted over 600 pages of written argument and oral argument took 11 days.

In many respects, the approach of the Director and respondents to this case does not result in a joining of issues. Counsel for the Director referred to their respective positions as "ships passing in the night". The result is that the Tribunal has often been left to identify and define, as well as resolve, the issues.

Indeed, the appropriate conceptual frameworks for the various issues have been very difficult to determine. The application included novel allegations of anti-competitive acts (for example, "targeting" in respect of publisher entrants) and inter-relationships between issues, such as the alleged anti-competitive acts against agents in the abuse of dominance case and tying, which required considerable deliberation.

Finally, there was the troubling issue of tying. This is the first case in which tying has been raised as a "principal" or substantial allegation.[4] This is a particularly difficult issue when related to services. There has been considerable debate among competition lawyers, economists and jurists about the difficulty of addressing alleged anti-competitive activity without adversely affecting efficiency in the context of tying, and the Tribunal was squarely faced with these issues in this case.

[4] Tying was a minor portion of the case in *Director of Investigation and Research v. The NutraSweet Company* (1990), 32 C.P.R. (3d) 1, [1990] C.C.T.D. No. 17 (QL).

Summary of Conclusions

1. Telephone directory advertising is a distinct advertising medium without close substitutes and is therefore the relevant product market. Geographic markets are local, corresponding roughly to the scope of each of Tele-Direct's directories. Tele-Direct has an overwhelming share of the product market in all relevant local markets.

2. Tele-Direct has control or market power since the condition of easy entry required to overcome the presumption of market power arising from Tele-Direct's extremely large market share is not satisfied. Direct indicators of market power, such as the level of profits and methods of pricing, reinforce this conclusion.

3. With respect to the allegation of tied selling, telephone directory space and telephone directory advertising services constitute two products solely for national and regional advertisers and Tele-Direct has tied the supply of advertising space to the acquisition of advertising services for these customers. We have prohibited the practice of tied selling.

4. The allegation that Tele-Direct has engaged in a practice of anti-competitive acts against entrants into telephone directory publishing, particularly in the Sault Ste. Marie and Niagara regions, is rejected.

5. The allegation that Tele-Direct has engaged in a practice of anti-competitive acts directed against agents and resulting in substantial lessening of competition is rejected.

6. The allegation that Tele-Direct has engaged in a practice of discriminatory anti-competitive acts against consultants which have or are likely to result in a substantial lessening of competition is accepted. Tele-Direct is ordered to cease the practice. Other allegations respecting consultants are rejected.

7. The allegation that Tele-Direct's refusal to license its trade-marks to certain competitors is a practice of anti-competitive acts is rejected because the refusal is protected from being an anti-competitive act by subsection 79(5) of the *Competition Act* as a legitimate exercise of its rights under the *Trade-marks Act*.

II. BACKGROUND FACTS

A. TELEPHONE DIRECTORY ADVERTISING

A white pages telephone directory is a comprehensive list of all telephone subscribers in a specified area. A listing includes a name, address and telephone number. A classified telephone directory, historically printed on yellow paper (hence "Yellow Pages"),[5] includes all business telephone subscriber listings plus advertising arranged by heading or descriptive category. There are often multiple headings under which a directory user might search in order to find a certain type of business.

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[5] The words "Yellow Pages" and "Pages jaunes" are registered trade-marks of the respondents in Canada although they are considered generic or descriptive in the United States. Tele-Direct licenses its trade-marks to other telco directory publishers in Canada but not to non-telco directory publishers.

Tele-Direct's Yellow Pages directories generally cover the same geographic area as the corresponding white pages. Some white pages directories, however, cover a much broader area than the Yellow Pages; in those cases, there would be several different Yellow Pages directories for a single white pages. Tele-Direct also publishes even more narrowly-scoped Yellow Pages directories for individual "neighbourhoods" in Montreal and Toronto.

Telcos are required by the Canadian Radio-television and Telecommunications Commission ("CRTC") to distribute the appropriate up-to-date telephone directory for their district, both white and Yellow Pages, to telephone subscribers at no additional charge. Tele-Direct pays the various telcos for subscriber listing information and the right to publish and distribute the directories to subscribers. It makes its profits from the net advertising revenues. Tele-Direct publishes directories annually.

Every business telephone subscriber is entitled to receive in its Yellow Pages directory one light-type listing free of charge under the heading of its choice. Any features added to a listing, for example, bold type or extra lines, a second heading or another directory must be purchased. Actual advertisements in the Yellow Pages must, of course, also be purchased. For Tele-Direct's purposes, an "advertiser" is a subscriber who has a paid item in either the white pages (an enhanced listing) or Yellow Pages of a directory. Revenues from Yellow Pages advertising is far greater than any "advertising" expenditures in the white pages.[6]

[6] Approximately 10 percent of Tele-Direct (Publications) Inc. 1994 directory revenue came from expenditures in the white pages.

Approximately 50 percent of business subscribers are "advertisers". The remainder are called "non-advertisers" or "non-ads". The percentage of advertisers is smaller in the largest centres such as Montreal and Toronto and larger in smaller centres. Excluding neighbourhood directories and agency clients,[7] average advertising expenditures in 1994 in Tele-Direct (Publications) Inc. directories were approximately $1,700, with advertisers spending that amount or less constituting around 30 percent of revenues but over 80 percent of advertisers. At the other end of the spectrum, the top 30 percent of revenues comes from only about two percent of advertisers, those who spend more than approximately $10,000 annually. A few very large advertisers spending an average of $113,000 provide 6.5 percent of revenues but represent only 0.1 percent of advertisers by number.

A number of different types of advertising can be purchased in a Tele-Direct Yellow Pages directory. Apart from the basic upgrades to its initial free listing (e.g., second heading, bold type), a business may purchase "in-column" or "display" advertising. The pages in Tele-Direct's directories are generally divided into four columns; an "in-column" advertisement fits within the confines of one of the columns with the variation being in the height of the advertisement. In-column advertisements are arranged alphabetically, interspersed among the simple listings.

A variation on the in-column advertisement is the trade item advertisement, including the trade-name, trade-mark and custom trade-mark advertisements (usually referred to together as

[7] The very small and the very large accounts.

"trade-marks" or "trade-mark advertisements"). In order to place this type of advertisement, the listed businesses must have authorization to use the trade-name or mark in their directory advertising. The trade-name or mark acts as the heading for the advertisement, followed by one or more listings of specific businesses.

Display advertisements range in size from a quarter column (1/16 of a page) to a full page. The placement of these advertisements is loosely alphabetical, as space on a page permits. Options like various types of borders, red, other colours, "white knockout" (white background instead of yellow) may be added to both in-column and display advertisements. They also feature a variety of design and layout techniques, print styles and sizes and graphics.

B. PUBLISHERS

Revenues from the telephone directory business in Canada amount to about $900 million to $1 billion annually. The vast majority of these are generated by the telco-affiliated directories. Apart from the Tele-Direct directories and other directories published by or on behalf of telcos, there are over 250 "independent" directories published in Tele-Direct's territory. These directories are independent in the sense that they have no connection to the provider of telephone service. They come in a wide variety of formats (size, subject, colour of paper) but can, generally, be characterized as two types: "niche" and "broadly-scoped" directories.

Niche directories operate in geographic areas which are substantially smaller than the areas covered by the corresponding telco directories. These directories have a generally smaller, more tightly-scoped distribution area than the telco directory, allowing a local retailer to advertise to a smaller geographic area at a lower cost. Niche directories are often directed at a particular religious, ethnic or demographic group.

Two independent publishers of broadly-scoped directories currently produce directories in parts of Tele-Direct's territory. White, which was for a brief time an intervenor in this proceeding, has published directories in the Niagara region since 1993. Dial Source Plus, Inc. ("DSP") publishes a directory in the Sault Ste. Marie area and has also done so since 1993.

C. SERVICE SUPPLIERS

Telephone directory advertising services, including the sale of space in Tele-Direct's directories, are provided by three groups: Tele-Direct's internal sales force, advertising agencies and consultants. More detail on each of these groups and their particular method of operation will be provided as appropriate throughout these reasons. For the moment, the following should suffice to introduce the various players.

The internal sales force of Tele-Direct consists largely of unionized sales representatives who are remunerated through a combination of salary, commission and other incentives. Services similar to those provided by Tele-Direct's internal sales force are also offered by outside advertising agencies. These include general advertising agencies which, if they deal with Yellow Pages at all, usually have a department devoted to that function, advertising agencies specializing in Yellow Pages only and in-house advertising agencies.

Agencies are not remunerated directly by the advertiser but, rather, through a commission paid by the publisher as a percentage of the value of the advertising purchased. While the agency receives commission, the agency's employees earn salary for providing services to the agency's clients. Agencies are restricted in the accounts that they can service as Tele-Direct only pays commission on accounts which meet certain criteria. Tele-Direct's commissionable account definition has undergone a number of changes over the years which will be discussed in further detail later. It is not controversial that fewer accounts meet the current criteria than met prior definitions. The current criteria were adopted in 1993 and are sometimes referred to as the "national" account definition.[8] In order to receive the 25 percent commission payable on these accounts, the agency placing the advertising must be accredited as a Certified Marketing Representative or "CMR" in accordance with the standards set by the Yellow Pages Publishers Association ("YPPA").

Services are also provided by Yellow Pages consultants. Consultants create advertisements for Yellow Pages advertisers and advise them on where and to what extent they should advertise in the Yellow Pages. Typically, consultants obtain cost savings on behalf of

[8] Under this rule, in very general terms, to qualify for commission, an account must involve advertising in at least 20 Yellow Pages directories within Tele-Direct's territory and at least 20 percent of the total value of the advertising must be placed in directories of another publisher outside Tele-Direct's territory.

advertisers by advising the purchase of smaller or less colourful advertisements, more limited geographic placement of advertisements or by redesigning the advertising. They are not recognized by Tele-Direct, which refers to them by the less complimentary term of "cut agents". Consultants do not receive commission. In general, consultants are paid by the advertiser out of the savings in advertising expenditures resulting from the adoption of the consultant's advice.

III. TIME LIMITATIONS

The respondents argue that the Director is subject to three time constraints which limit the allegations of anti-competitive acts that can be advanced for the purposes of the Director's case under section 79. These arguments are that: the *Competition Act* is not retrospective; the Director's allegations are statute-barred by the *Crown Liability and Proceedings Act*;[9] and subsection 79(6) of the *Competition Act* further limits those allegations. Each argument will be dealt with in turn.

The particular allegations that are challenged relate to Tele-Direct's requirement of "issue billing" (payment from CMRs required at the time of issue of a directory as opposed to monthly payments when advertisers deal with Tele-Direct's general sales force) and its restricting of the commissionability criteria applicable to CMRs. The actual words at paragraph 65 of the application are:

[9] R.S.C. 1985, c. C-50.

> . . . the Applicant says that the Respondents have engaged in the following anti-competitive acts:
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> . . .
>
> (c) providing advertising space to independent advertising agencies on less favourable terms and conditions than to its own sales staff, including: . . .
>
> (ii) requiring that such independent agencies pay the total amount outstanding for a year's insertion of advertising in a given directory, while customers placing orders through internal sales staff may pay such amount monthly over the course of the year without interest charges; . . .
> (d) squeezing the return available to independent advertising agencies by acts which include:
>
> . . .
>
> (iv) further restricting the availability of commission to such agencies over time.

A. RETROSPECTIVITY

There is no apparent difference between the parties with respect to the broad legal principles regarding retrospectivity. The general rule is that statutes are not to be construed as having retrospective operation unless such a construction is expressly or by necessary implication required by the language of the particular statute.[10] Côté, one of the authorities cited by the respondents, states that a retrospective effect occurs when a new statute is applied "in such a way as to prescribe the legal regime of facts entirely accomplished prior to its commencement." He further states that it is *not* retrospective operation when a statute is applied to ongoing facts which began prior to the statute's commencement.[11] The Driedger text, also referred to by the respondents, describes ongoing facts or "continuing facts" as

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[10] *Gustavson Drilling (1964) Limited v. M.N.R.* (1975), [1977] 1 S.C.R. 271 at 279.

[11] P. Côté, *The Interpretation of Legislation in Canada*, 2d ed. (Quebec: Yvon Blais, 1991) at 118, 123.

> . . . one or more facts that endure over a period of time, such as ownership or imprisonment or residency. A continuing fact can be any state of affairs or status or relationship that is capable of persisting over time. . . .[12]

The dispute between the parties is whether the allegations advanced by the Director regarding issue billing and commissionability criteria imply retrospective application of the *Competition Act*.

The respondents submit that since no concept of an "anti-competitive act" existed before 1986, when the *Competition Act* came into force, no act which occurred prior to 1986 can now be characterized as anti-competitive for purposes of section 79. They also argue that section 79 on its terms can *only* be applied to discrete acts or events, of which there must be multiple instances to constitute a "practice".

With respect to commissionability, the respondents argue that the Director is alleging that they "narrowed" the definition by discrete acts which occurred in 1975 and again in 1993. The 1975 "narrowing" cannot be anti-competitive and the 1993 "narrowing" alone is only one act and cannot amount to a "practice". Likewise, they say that the Director has alleged that Tele-Direct's "decision" to require issue billing, another discrete act which took place long before 1986, cannot be an anti-competitive act. The fact that these decisions resulted in allegedly restrictive policies that have been applied continuously ever since, they submit, is irrelevant because there is no "new act" of "requiring issue billing" or of "narrowing" besides 1993.

[12] *Driedger on the Construction of Statutes*, 3d ed. by R. Sullivan (Toronto: Butterworths, 1994) at 514-15.

The Director argues that the respondents have mischaracterized the pleadings. The Director submits that the current situation, the day-to-day restricted state of the commissionable market and the ongoing requirement of issue billing, are the focus of the allegations of anti-competitive acts, rather than the original decisions to implement these policies. The pre-1986 events, the Director submits, shed light on history, intent and progress. Thus, the Director says there is no question of retrospectivity.

We are of the view that section 79 is not restricted in its application to discrete acts or events as opposed to an ongoing course of conduct or state of affairs. The meaning of "practice" in subsection 79(1) was considered by the Tribunal in the *NutraSweet* case.[13] There, the Tribunal found that a practice may exist where there is more than an "isolated act or acts". It also observed that the examples of anti-competitive acts listed in section 78 could entail both a course of conduct over time as well as discrete acts:

> . . . The anti-competitive acts covered in s. 78 run a wide gamut. Some almost certainly entail a course of conduct over a period of time, such as freight equalization in para. 78(*c*), whereas others consist of discrete acts, such as the setting of product specifications in para. 78(*g*). The interpretation of "practice" must be sufficiently broad so as to allow for a wide variety of anti-competitive acts. Accordingly, the tribunal is of the view that a practice may exist where there is more than an "isolated act or acts". For the same reasons, the tribunal is also of the view that different individual anti-competitive acts taken together may constitute a practice.[14]

[13] *Supra* note 4.

[14] *Ibid*. at 35.

We are satisfied that the practice contemplated by subsection 79(1) must be more than an isolated act or acts but can include a number of individual anti-competitive acts taken together or a course of anti-competitive conduct over time.

Clearly, the Director's pleadings contemplate the violation of subsection 79(1) of the *Competition Act* by a current practice of anti-competitive acts by the respondents. The fact that the act or acts giving rise to the current practice took place prior to 1986 does not make application of the subsection retrospective. In this case, the Director is not challenging the initial decisions by Tele-Direct to commence issue billing and to restrict commission in 1975 as discrete anti-competitive acts in and of themselves. Requiring payment from CMRs at time of issue of a directory may have been instituted in 1959 but it continued after 1986 and existed when the Director's application was filed. Similarly, the "narrow" commissionability market which commenced with a change in the commissionability rules in 1975 continued after 1986. While it may have been narrowed further in 1993, it is not the discrete act of narrowing that is in issue in this case. Rather, it is the ongoing narrow commissionability rules that existed when the Director's application was filed and that were, in the view of the Director, exacerbated in 1993 with further narrowing, that are the focus of the allegations of anti-competitive conduct. As such, there is no retrospective application of the *Competition Act* in this case.

Nor is it inappropriate in these circumstances to have regard to events occurring prior to 1986 to consider fully the allegations made under section 79. We take guidance from the approach adopted by the Supreme Court in *Gamble v. R.* Wilson J., speaking for the majority, states:

> . . . Frequently an alleged current violation [of the *Charter*] will have to be placed in the context of its pre-*Charter* history in order to be fully appreciated. . . . Charter standards cannot be applied to events occurring before its proclamation but it would be folly, in my view, to exclude from the Court's consideration crucial pre-*Charter* history.[15]

It is clear from the words of the application, and from the way the case developed before the Tribunal, that the current state of affairs is the focus of the Director's allegations of anti-competitive conduct. The respondents have not argued that the Director's pleadings misled them regarding the case they had to meet and that therefore they have suffered prejudice in preparing or presenting their case. Indeed, such an argument could not be advanced given the detailed and inclusive record regarding not only the current situation in the market but also the historical context.

B. *CROWN LIABILITY AND PROCEEDINGS ACT*

The respondents' second limitation argument is based on section 32 of the *Crown Liability and Proceedings Act* which reads:

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[15] [1988] 2 S.C.R. 595 at 625-26.

> Except as otherwise provided in this Act or in any other Act of Parliament, the laws relating to prescription and the limitation of actions in force in a province between subject and subject apply to any proceedings by or against the Crown in respect of a cause of action arising in that province, and proceedings by or against the Crown in respect of a cause of action arising otherwise than in a province shall be taken within six years after the cause of action arose.

The respondents argue that the *Crown Liability and Proceedings Act* statutorily bars the Crown (here, the Director) from acting on a cause of action which arose more than six years before the issuing of the application, that is, prior to December 22, 1988. Thus, they argue, all references to changes made in commissionability criteria or any other alleged anti-competitive act after 1986, when sections 78 and 79 were enacted, but prior to December 22, 1988 (six years before the application was filed), are statute-barred.

The respondents did not press this point and it will be dealt with summarily. First, as argued by the Director, the respondents cannot rely on the *Crown Liability and Proceedings Act* as they did not plead it in their response. The law is clear that a limitation period does not terminate a cause of action but provides a defendant with a procedural means of defence which must be pleaded in the defence.[16]

Second, section 32 of the *Crown Liability and Proceedings Act* is simply not applicable to this case. The opening words of section 32 indicate that if there is a specific limitation period in the statute governing the cause of action involved, here the *Competition Act*, that limitation period applies.[17] It is only in the absence of a specific provision that either a provincial limitation

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[16] *Kibale v. Canada* (1990), 123 N.R. 153 (F.C.A.). See also rule 409 of the Federal Court Rules.

[17] *Canada v. Maritime Group (Canada) Inc.*, [1993] 1 F.C. 131 (T.D.)

period or the six-year limitation period in section 32 is considered. Subsection 79(6) of the *Competition Act*, to which the respondents have also made reference, provides a limitation period for proceedings brought under that section.

C. SUBSECTION 79(6)

Subsection 79(6) of the *Competition Act* states:

> No application may be made under this section in respect of a practice of anti-competitive acts more than three years after the practice has ceased.

Again, the respondents did not plead this limitation period. Further, while they refer to subsection 79(6), the respondents made no effort to argue how it applies in this case. No more need be said.

IV. IMPACT OF THE CONSENT ORDER

The respondents argue that the Director is estopped from bringing this application before the Tribunal to the extent that it deals with issues adjudicated by the Tribunal in a previous proceeding. On November 18, 1994, the Tribunal issued an order, the terms of which were agreed to by the parties, as a result of an application brought by the Director against the Yellow Pages publishers in Canada.[18] We will refer to that order as the Consent Order. The respondents in the present proceedings were among the respondents named in that order.

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[18] *Director of Investigation and Research v. AGT Directory Limited et al*., CT-94/2.

In the application which resulted in the Consent Order, the Director alleged that the respondents in those proceedings had jointly engaged in a practice of anti-competitive acts within the meaning of sections 78 and 79 of the Act. The specific allegations levied against those respondents and found at paragraph 74 of the application were as follows:

> . . . it is the Director's submission that the Respondents engaged in the following anti-competitive acts to impede or prevent a competitor's entry into or eliminating a competitor from a market. The anti-competitive acts of the Respondents constituted a practice of anti-competitive acts by the Respondents which had the effect of substantially preventing or lessening competition in the relevant product market of the Selling of National Advertising into Telephone Directories in Canada. The Respondents:
>
> (i) agreed that only Publishers could Sell National Advertising directly into Telephone Directories;
>
> (ii) appointed each other as their exclusive Selling Companies for the Selling of National Advertising in Telephone Directories in each of their respective territories and therefore did not compete with such exclusive Selling Companies in those territories;
>
> (iii) agreed to a Head Office Rule, thus precluding the National Advertiser from either placing the advertisement directly with all the Respondents which actually published the advertisements or using an entity unrelated to any of the Respondents to place the advertising directly in each Respondent's Telephone Directories.

The Consent Order contains prohibitions designed to prevent the respondents who agreed to it from engaging in certain acts in the selling of national advertising in Yellow Pages telephone directories, including:

> With regard to the sale of national advertising in Yellow Pages telephone directories, each respondent shall be prohibited from:
>
> . . .
>
> (f) agreeing with any other respondent on the criteria for determining which national advertising accounts are commissionable;
>
> (g) agreeing with any other respondent on the rate of commission

> payable, except during a transition period ending June 30, 1995 during which a minimum commission of 25% will be available to selling companies for national advertising which meets the commissionability criteria established by each respondent. . . .[19]

The parties appear to be in agreement with respect to the law of issue estoppel. The doctrine of issue estoppel precludes an action being brought against a party with respect to an issue which was already decided in an earlier proceeding. There are three requirements to be met before issue estoppel applies so as to bar a new proceeding. First, there must have been an earlier proceeding in which there was a determination of the same issue. Second, the determination of the issue in the earlier proceeding must have been a final decision. Finally, the parties to each of the two proceedings must be the same.[20] The doctrine of issue estoppel applies equally to issues decided in consent orders and in contested orders.[21]

The Supreme Court of Canada has held that the decision upon which a party relies for issue estoppel must have dealt directly and necessarily with the issue which is being raised for a second time:

> . . . It will not suffice if the question arose collaterally or incidentally in the earlier proceedings or is one which must be inferred by argument from the judgment. . . . The question out of which the estoppel is said to arise must have been "fundamental to the decision arrived at" in the earlier proceedings.[22] (references omitted)

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[19] *Director of Investigation and Research v. AGT Directory Limited* (18 November 1994), CT-94/2, Consent Order at para. 3, [1994] C.C.T.D. No. 24 (QL).

[20] *Angle v. M.N.R.* (1974), [1975] 2 S.C.R. 248.

[21] G. Spencer Bower & A.K. Turner, *The Doctrine of Res Judicata*, 2d ed. (London: Butterworths, 1969) at 37.

[22] *Supra* note 20 at 255.

Tele-Direct argues that the issues relating to its commissionability criteria alleged by the Director in this case, namely, that its policy of offering commission only on accounts which meet its "national" definition is an anti-competitive act and constitutes tied selling, were dealt with by the Tribunal in the Consent Order. Tele-Direct's position is that the Director is estopped from re-litigating these issues in the present proceeding. According to Tele-Direct, the Director, and the Tribunal by virtue of its issuance of the Consent Order, were satisfied that any substantial lessening of competition in the sales of national advertising would be alleviated by the terms of the order. If the Director seeks to vary the Consent Order, the Director can only do so by following the procedure for rescission and variation of consent orders which is governed by section 106 of the Act; this course was not pursued by the Director.

The respondents further argue that, by implication, the Consent Order authorizes them to set their own commissionability criteria without interference as long as they do not agree on the rate with any other publisher. Accordingly, they say that it is inconsistent for the Director to bring this proceeding, which could result in the Tribunal interfering with Tele-Direct's decisions relating to its commissionability criteria for national advertising.

The Director's position is that the issues raised in the two proceedings are not the same and that, therefore, the doctrine of issue estoppel does not apply. According to the Director, the anti-competitive acts which were the subject of the Consent Order were certain *joint* practices of the Canadian Yellow Pages Service ("CANYPS") members (the telco publishers) regarding the manner in which national advertising could be placed in their directories. It was the agreements between the respondents to the Consent Order which constituted the anti-competitive acts and resulted in a substantial lessening of competition which were remedied by the order. In the present proceeding, however, it is alleged anti-competitive acts of Tele-Direct itself which are the subject of review. There was no decision in the earlier proceedings regarding how Tele-Direct sets its own commissionability criteria or how it otherwise deals with independent agencies located in its territory.

The requirements for issue estoppel are not met in this case. While the Consent Order was a final decision of the Tribunal, the terms of which are binding on Tele-Direct, the issues which were dealt with in that proceeding are not the same as those in the present case. This is clear from the application and supporting documentation and the Consent Order. It was the substantial lessening of competition resulting from the respondents' joint practice of anti-competitive acts or joint abuse of dominance that the Director sought to remedy by the Consent Order. The instant case deals with entirely separate allegations of anti-competitive acts of Tele-Direct acting alone. The Consent Order prohibits the respondents named in it from agreeing amongst themselves on the rate of commission payable. That order does not address the commissionability criteria which an individual publisher may set. Nothing in the Consent Order limits the jurisdiction of the Tribunal to review the commissionability criteria set by Tele-Direct.

V. TRADE-MARKS

The Director alleges that the respondents, by "refusing to licence [their] trade-marks, such as the words `Yellow Pages' and `Pages Jaunes' and the walking fingers logo, to competing suppliers of advertising services", have engaged in a practice of anti-competitive acts contrary to section 79 of the Act. In particular, the Director seeks to prohibit the respondents' alleged practice of "selective licensing" whereby certain competitors are refused licences, allegedly arbitrarily or pursuant to an anti-competitive intent, and others are not. As a remedy, the Director seeks an order "that the respondents licence, at the request of independent advertising agencies, including consultants, and on commercially reasonable terms and conditions, the trade-marks registered for the respondents' own use in relation to telephone directories."

The Director's submissions raise two issues. First, the Tribunal must determine whether the refusal to license a trade-mark to certain persons or groups of persons is an anti-competitive act. Second, if it is an anti-competitive act, the Tribunal must determine whether it has jurisdiction to order the respondents to license their trade-marks. Having carefully considered the evidence and the submissions of counsel, the Tribunal is of the view that the selective refusal to license a trade-mark is not an anti-competitive act. Accordingly, the second question need not be answered.

The facts concerning the respondents' refusal to license their trade-marks are not disputed. The respondents license the use of their trade-marks to CMRs and other telco-affiliated directory publishers; they do not license other advertising agencies or consultants. The respondents aggressively defend their trade-marks against what they perceive to be infringement but they do not pursue every perceived infringement with equal zeal. The evidence is that Tele-

Direct overlooks certain uses of its trade-marks but threatens to, or institutes, legal action against the use of its trade-marks by, for instance, consultants.

Both the *Trade-marks Act*[23] and the *Competition Act* are relevant. The purpose of a trade-mark is to distinguish the wares or services of the owner from those of others.[24] The *Trade-marks Act* provides that the owner of a trade-mark has the exclusive right to its use.[25] Further, the owner of a trade-mark may license another to use that trade-mark, and that use is deemed to have the same effect as use by the owner.[26] Subsection 79(5) of the *Competition Act* provides:

> For the purpose of this section, an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the *Copyright Act*, *Industrial Design Act*, *Integrated Circuit Topography Act*, *Patent Act*, *Trade-marks Act* or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act.

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23 *Trade-marks Act*, R.S.C. 1985, c. T-13.

24 A "trade-mark" is defined in s. 2 of the *Trade-marks Act* as "a mark that is used by a person for the purpose of distinguishing or so as to distinguish wares or services manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others. . . ."

25 *Trade-marks Act*, s. 19.

26 S. 50(1) of the *Trade-marks Act*, as am. S.C. 1993, c. 15, s. 69, provides:

> For the purposes of this Act, if an entity is licensed by or with the authority of the owner of the trade-mark to use the trade-mark in a country and the owner has, under the licence, direct or indirect control of the character or quality of the wares or services, then the use, advertisement or display of the trade-mark in that country as or in a trade-mark, trade-name or otherwise by that entity has, and is deemed always to have had, the same effect as such a use, advertisement or display of the trade-mark in that country by the owner.

The Director submits that subsection 79(5) does not preclude a finding that "abuses" of intellectual property rights are anti-competitive acts. It is the Director's position that Tele-Direct's practice of selective licensing is an abuse of Tele-Direct's trade-mark rights. The Director asserts that an owner's "exclusive right to use" its trade-mark is not unlimited. The Director relies upon case law which has defined "use" not to include activities which are for purposes other than distinguishing wares or services of the owner from the wares or services of others.[27] Accordingly, the Director submits that the respondents' position that "any written use of the words `Yellow Pages' would be dealt with" and the fact that the respondents have used their "superior resources" to assert this claim successfully is evidence of the respondents' exclusionary intent in respect of their trade-marks.

Tele-Direct argues that, as owner of the trade-marks, it has the statutory right to decide to whom it will or will not license those trade-marks, including the right to refuse to licence where it is not in its best interest to do so. It argues that there is no evidence that it has adopted a policy of refusing to license trade-marks to competitors for the purposes of restraining competition; rather, it does not make sense for Tele-Direct to license its trade-marks to consultants whose businesses are based on the premise that Tele-Direct "rips-off" its customers.

In support of his position, the Director relies on the decision of the United States District Court in *Car-Freshener Corp. v. Auto-Aid Manufacturing Corp.*, where the Court stated that

[27] E.g., comparative advertising or use of trade-mark in a merely descriptive sense, for example, does not constitute infringement: see *Clairol International Corp. v. Thomas Supply & Equipment Co.*, [1968] 2 Ex. C.R. 552 at 556; *Syntex Inc. v. Apotex Inc.* (1984), 1 C.P.R. (3d) 145 (F.C.A.).

there was "no doubt that a trade-mark may be utilized in such a manner as to constitute a violation of antitrust laws"[28] and offered several examples: the use of a strong trade-mark to unlawfully tie a weaker product, unlawful price discrimination exercised with respect to a trade-mark, or other illegal anti-competitive practices. The Tribunal is in agreement with the Director that there may be instances where a trade-mark may be misused. However, in the Tribunal's view, something more than the mere exercise of statutory rights, even if exclusionary in effect, must be present before there can be a finding of misuse of a trade-mark. Subsection 79(5) explicitly recognizes this.

The respondents' refusal to license 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-marks. The respondents' trade-marks are valuable assets and represent considerable goodwill in the marketplace. The decision to license a trade-mark -- essentially, to 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.

The owner's exclusive jurisdiction over licensing accords with the scheme of the *Trade-marks Act*. There is no statutory means by which a person can petition the Registrar of Trade-

[28] 483 F.Supp. 82 at 86-87 (1977).

marks for a licence to use a trade-mark, implying that the decision to license rests with the owner of the mark. Furthermore, the licensing provisions of the *Trade-marks Act* provide that, in order to constitute a valid licence, the trade-mark owner should have "direct or indirect control of the character or quality of the wares or services" to which the licensee was attaching the mark. Indeed, in *Unitel Communications Inc. v. Bell Canada*,[29] the Court expunged trade-marks owned by Bell Canada, in part because Bell Canada had failed to exercise control over the use of its trade-marks by an independent telco. In the case at bar, the lack of control over the quality of the goods or services is particularly relevant since the Director is suggesting that the respondents' trade-marks should be licensed to consultants with whom the respondents do not share identity of interest.

While the evidence suggests that Tele-Direct is motivated, at least in part, by competition in its decision to refuse to license its trade-marks, the fact is that the *Trade-marks Act* allows trade-mark owners to decide to whom they will license their trade-marks. The respondents' motivation for their decision to refuse to license a competitor becomes irrelevant as the *Trade-marks Act* does not prescribe any limit to the exercise of that right.

The respondents' legitimate desire to protect the value of the goodwill vested in their trade-marks by refusing to license them does not amount to an anti-competitive act. In view of the strength of their trade-marks, the respondents can be expected to be, and are entitled to be, protective of their rights. Indeed, if the respondents did not protect their marks, they would risk

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[29] (1995), 61 C.P.R. (3d) 12 (F.C.T.D.).

having them lose their distinctiveness, as in *Unitel*. This is a real concern, given that the Yellow Pages trade-marks are no longer registered in the United States.

While independent advertising agencies and consultants may wish to use the respondents' trade-marks, there is simply no basis for granting an order requiring the respondents to license their trade-marks.[30] Although the respondents may have been zealous in protecting their trade-marks, both in refusing to license and in threatening litigation for infringement, the irrefutable fact is that the respondents have been, through the provisions of the *Trade-marks Act*, accorded the right to refuse to license their trade- marks, even selectively. The exercise of this right is protected from being an anti-competitive act by subsection 79(5) of the Act.

VI. MARKET DEFINITION

A necessary first step in deciding this case is to define the relevant market. This must be done for purposes of section 79 in order to determine if Tele-Direct, as alleged by the Director, "substantially or completely control[s], throughout Canada or any area thereof, a class or species of business". The Tribunal decided in *Director of Investigation and Research v. D & B Companies of Canada*[31] that "class or species of business" means product market and "control" means market power. The remaining phrase, "throughout Canada or any area thereof", refers to

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[30] In fact, neither the Director nor the respondents directed the Tribunal to any cases where a party was ordered to license a trade-mark.

[31] (1995), 64 C.P.R. (3d) 216, [1995] C.C.T.D. No. 20 (QL) (Comp. Trib.).

the geographic market. Therefore, in order for section 79 to apply, the Tribunal must first conclude that Tele-Direct has market power.

A market must also be defined in order to consider the allegation of tying, brought under section 77. Under subsection 77(2), the Tribunal must find that "tied selling, because it is engaged in by a major supplier of a product in a market . . . is likely to" have a number of detrimental effects. If Tele-Direct is found to have market power, it would qualify as a "major supplier".

A. PRODUCT MARKET

The argument and the evidence presented to us regarding the relevant product market focus on whether there are close substitutes for telephone directory advertising. The Director includes in his relevant market advertising in Tele-Direct's Yellow Pages directories and in telephone directories produced by independent (non-telco affiliated) publishers.

The respondents concede that advertising in independent directories is in the same relevant market as advertising in Yellow Pages directories. Their position is that both independent and Yellow Pages directories form part of a broader product market comprised of all local advertising media. The respondents define "local advertising" in this context as advertising designed to promote business at a particular location. They would include, for example, direct mail, outdoor signage, community newspapers, daily newspapers, catalogues, trade magazines, flyers, radio, television -- in fact advertising in any medium as long as the advertising is designed to promote a particular location.

It is important to keep in mind that our goal in defining the relevant market in this case is to determine whether other local advertising media provide competitive discipline for Tele-Direct in respect of its Yellow Pages pricing[32] and output decisions. The Director argues that they do not. The respondents argue that they do.

(1) Substitutability -- The Basic Test

The parties agree that the fundamental test or "touchstone" for determining the boundaries of the relevant product market is substitutability, as the Tribunal has consistently held in previous decisions, including three abuse of dominant position cases.[33] Products must be close substitutes in order to be placed in the same product market. The parties also agree that the appropriate approach to or framework for market definition is set out in the Federal Court of Appeal decision in *Director of Investigation and Research v. Southam Inc*.[34] Both parties quote the same passage from that decision:

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[32] Or surrogates such as service, quality, etc.

[33] *NutraSweet, supra* note 4; *Director of Investigation and Research v. Laidlaw Waste Systems Ltd.* (1992), 40 C.P.R. (3d) 289, [1992] C.C.T.D. No. 1 (QL); *D & B, supra* note .

[34] [1995] 3 F.C. 557 (C.A). An important issue in *Southam* was whether the two Pacific Press dailies and various community newspapers, all owned by Southam, were in the same product market. The Tribunal found that they were not; the Court of Appeal reversed on this point. An appeal to the Supreme Court is pending.

> Products can be said to be in the same market if they are close substitutes. In turn, products are close substitutes if buyers are willing to switch from one product to another in response to a relative change in price, i.e. if there is buyer price sensitivity. Direct evidence of substitutability includes both statistical evidence of buyer price sensitivity and anecdotal evidence, such as the testimony of buyers on past or hypothetical responses to price changes. However, since direct evidence may be difficult to obtain, it is also possible to measure substitutability and thereby infer price sensitivity through indirect means. Such indirect evidence focusses on certain practical *indicia*, such as functional interchangeability and industry views/behaviour, to show that products are close substitutes.[35] (reference omitted)

It is also common ground between the parties that this approach does not represent a radical departure from the approach used by the Tribunal in previous decisions.

(2) The *Southam* Decision

The *Southam* decision is the first Court of Appeal decision to deal in any depth with market definition under the Act.[36] That the parties differ considerably on how the general approach stated by the Court of Appeal in *Southam* is to be applied to the facts of the case before us is evident from the broad product market proposed by the respondents and the narrow product market proposed by the Director.

(a) Direct Evidence of Substitutability

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35 *Ibid*. at 632-33.

36 *Southam* was followed in *R. v. Clarke Transport Canada Inc.* (1995), 130 D.L.R. (4th) 500 (Ont. Ct. (Gen. Div.)), (1995) 64 C.P.R. (3d) 289. While the Director referred to that decision, it was not argued in any detail nor, apparently, relied on by either side.

There is no dispute that, first, we must consider any direct evidence of substitutability. In *Southam* the Court of Appeal states:

> To the extent that it is possible to adduce statistical evidence of high demand elasticity, such evidence is virtually conclusive that two products are in the same product market. Evidence of price sensitivity can also come in anecdotal form which is a less conclusive, although still a persuasive factor tending to show that products are close substitutes.[37]

The Director did not adduce any statistical evidence. The respondents mention the two "Elliott" reports, studies conducted for Tele-Direct in early 1993 for purposes other than this proceeding, as "statistical data" on advertisers' reaction to relative price increases.[38] The Elliott reports were general surveys of "customer satisfaction" which did not deal with price sensitivity of advertisers between different media.[39] Even if they had dealt with relative prices of various different media, in our view the Elliott reports would not qualify as the type of direct statistical evidence of demand cross-elasticity that was intended by the Court of Appeal. Such a study would have to be undertaken for the purpose of determining cross-elasticity between the products alleged to be in the market, be conducted in an appropriately rigorous fashion and meet tests of statistical significance. While the Elliott reports do not qualify as statistical evidence of demand cross-elasticity, they will be considered as part of the indirect evidence of substitutability.

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[37] *Supra* note 34 at 633.

[38] Confidential exhibit CJ-14 (blue vol. 5), tab 173; confidential exhibit CJ-19 (blue vol. 10), tab 285 (Newfoundland).

[39] The participants were asked if they would shift their advertising from Tele-Direct to an independent *directory* in response to a 15 percent increase in Tele-Direct's prices.

Although the Director called a number of buyers or advertisers as witnesses in this case, he does not rely on their evidence as "anecdotal evidence" of price sensitivity, from his point of view, low price sensitivity. He refers to their evidence as indirect evidence under various rubrics. The respondents likewise treat the testimony of the advertisers as indirect evidence. We will therefore not address the question of whether that testimony provides any direct evidence of price sensitivity or a lack thereof.

In the absence of direct evidence regarding buyer price sensitivity, we must therefore proceed to examine the available indirect evidence or "practical indicia" to draw inferences about price sensitivity.

(b) Indirect Evidence of Substitutability

The Director has organized the evidence of product market definition using headings similar to those set out in the *Merger Enforcement Guidelines*:[40] end use, physical and technical characteristics, views, strategies, behaviour and identity of buyers, trade views, strategies and behaviour ("inter-industry competition"), price relationships and relative price levels and switching costs. The respondents have also used the same headings to organize their evidence, although in a slightly different order. The *Merger Enforcement Guidelines* are not sacrosanct.

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[40] Consumer and Corporate Affairs Canada, Director of Investigation and Research, *Merger Enforcement Guidelines*, Information Bulletin No. 5 (Supply and Services Canada, March 1991).

But, as the parties are agreed that the evidence may be organized according to those guidelines, we accept that this is a practical and useful way in which to proceed.

The parties may use the same organizational structure but they do not agree on the respective roles to be accorded to the various practical indicia. In particular, they take different positions on the way in which the indicia of "functional interchangeability" and "inter-industry competition" should be employed in defining a product market based on the Court of Appeal decision in *Southam*. They also differ, of course, on the nature of the evidence and the conclusions to be drawn therefrom that should be considered under each heading. A detailed review of the evidence and the arguments under each heading will follow. We must first address, however, the arguments regarding the general approach to the practical indicia or indirect evidence of substitutability.

The Director submits that the Court of Appeal in *Southam* found that functional interchangeability is a "vital feature" and a "central part of the framework" of market definition, although it is not a sufficient condition for two products to be in the same market. The Director argues that the Court of Appeal did not state that functional interchangeability and inter-industry competition were the "sole" or "driving" factors in market definition but only found that *ignoring* those factors was an error of law.

The respondents in their written argument agree that the Tribunal must consider the evidence with respect to functional interchangeability and that it is central but alone does not conclusively demonstrate that two products belong in the same relevant market -- other factors must be considered. They point out that the additional factor that was "very important" to the Court of Appeal in *Southam* was inter-industry competition. During oral argument, counsel took the stricter position that the Court of Appeal held that if functional interchangeability and "broad" inter-industry competition are found, then it is an error not to place the products under consideration in the same market. If the two indicia mentioned are present, the Tribunal *must* infer price sensitivity and therefore a single product market.

The Tribunal must determine whether the Court of Appeal prescribed, as a matter of law, the role and importance of the factors or indicia of "functional interchangeability" and "inter-industry competition". With respect to functional interchangeability as one of the indirect indicia, the Court of Appeal stated that it was "not simply one of many criteria to be considered but a critical part of the framework." It also confirmed that functional interchangeability will generally be regarded as a "necessary but not sufficient condition to be met before products will be placed in the same market." With respect to inter-industry competition, the Court of Appeal found that evidence of "broad" competition, namely that the two types of newspapers were striving to reach many of the same advertisers with significant success by the community newspapers which, in turn, preoccupied Southam and generated responses by it, was sufficient to show competition "in fact".[41]

[41] *Supra* note 34 at 635, 637-38.

A finding that the products alleged to be in the same market serve the same relevant purpose is a necessary first step in the analysis. A finding of functional interchangeability, however, is not alone sufficient to place the products in the same market. As the Court stated:

> . . . There are other factors which may tend to reinforce, or undermine, a finding that two products are functionally interchangeable.[42]

With respect to evidence of "broad" inter-industry competition, we do not understand the Court to be saying that the presence of such evidence, along with evidence of functional interchangeability, will, in every case, dictate that the products in question should be placed in the same product market. If the Court intended to confine the analysis to these two practical indicia and effectively negate consideration of other factors, like, for example, the views, strategies and behaviour of buyers, the Court would have done so explicitly. It did not do so. In *Southam*, the Court confined its conclusions to the matter before it:

> While evidence of substitutability through functional interchangeability and inter-industry competition was adduced, the Tribunal ultimately ignored such evidence. In doing so, the Tribunal adopted an overly narrow approach to substitutability as it dismissed "broad" conceptions of interchangeability and inter-industry competition. In doing so, the Tribunal erred in focusing predominantly on price sensitivity. *In this case, the similarity of use between Pacific Dailies and community newspapers, and the competitiveness which existed between them, is sufficient to place both in the same product market.*[43] (emphasis added)

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[42] *Ibid*. at 637.

[43] *Ibid*. at 640.

We conclude that consideration of functional interchangeability is essential in assessing indirect evidence of whether two or more products are in the same market. But this does not exclude other relevant evidence which may reinforce or undermine what functional interchangeability implies.

In considering the whole of the evidence, the Tribunal will bear in mind the ultimate reason why the market is being defined. In this case, the goal is to determine if the respondents have market power (or are "major suppliers"), that is, if the alleged close substitutes, other local advertising media, provide competitive discipline for Tele-Direct in making price (or quality) and output decisions.

(3) Functional Interchangeability

The Director submits that two headings from the *Merger Enforcement Guidelines*, "end use" and "physical and technical characteristics", are both related to the question of functional interchangeability. Certain characteristics of directories are, he argues, key factors which dictate the end use of a directory as a directional reference tool and which thus limit the "functional interchangeability" of directory advertising with directional advertising in other media.

The respondents argue that all local advertising has the same end use: to increase business at a particular location. They submit that the characteristics of the various media should not be considered as part of the determination of functional interchangeability.

Regarding functional interchangeability, the Court of Appeal in *Southam* says:

> . . . But the fact that community newspapers are more local in nature does not go to the question of functional interchangeability, but to the behaviour of buyers as to preference for geographical scope. This latter *subjective* factor should not be mingled with the purely *objective* factor of functional interchangeability which focusses on use or purpose.[44] (emphasis added)

The Court imposes the constraint that the views of buyers should not enter when functional interchangeability is being decided because they are "subjective". Only "objective" factors should enter at this point.

Under the criterion "end use", the *Merger Enforcement Guidelines* refer to the extent to which two products are "functionally interchangeable in end use". That is the way in which the term will be used in this decision. Physical and technical characteristics, along with other indicia, serve to determine whether the products found to be functionally interchangeable in end use are close substitutes. Rather than considering physical and technical characteristics as part of the determination of functional interchangeability, as the Director proposes, the Tribunal will treat them separately from functional interchangeability.

The Director and one of his economics expert witnesses, Richard Schwindt,[45] have defined the relevant end use of telephone directory advertising to be use as a "directional" medium. ("Directional" and "directive" were used interchangeably in the material before us.)

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[44] *Ibid*. at 636-37.

[45] Associate Professor of Economics and Business Administration at Simon Fraser University.

Two elements are said to characterize a directional advertising medium: (a) consumers consult the medium when they are at a point in the buying cycle when they are ready to buy, and (b) the medium is used as a reference tool. Directional advertising is distinguished from creative advertising, which is widely acknowledged to be used for creating or stimulating demand. The Director admits that other advertising media besides Yellow Pages might be considered directional but names catalogues, direct mail and classified newspaper advertising as the only candidates.

The respondents and their economics expert witness, Robert Willig,[46] take the view that all "local" advertising[47] has the same end use, to attract customers to a particular establishment. Thus, they argue, advertising in the Yellow Pages and advertising in other local media are functionally interchangeable. In response to the Director's argument, they argue that directionality is not generally regarded as encompassing the element of use as a reference tool. They further argue that the directional/creative dichotomy is not valid. They take the position that there is no such sharp distinction in the advertising done by local advertisers. In their submission, directional means only that the advertising directs consumers to a particular establishment -- which can be done in any medium. Given the respondents' definition of "local" advertising, all advertising by a local advertiser necessarily has a directional component. Similarly, since they are of the view that all local advertising, including advertising in telephone

[46] Professor of Economics and Public Affairs at Princeton University.

[47] As opposed to "national" or "brand awareness" advertising which promotes a product wholly apart from *any* location.

directories, has as its goal the stimulation of demand at a location, all local advertising necessarily has a creative component.

Since the respondents have defined "local" advertising as advertising designed to promote business at a particular location, it follows that the purpose of all local advertising is to attract customers to a business. Such a definition is at a high level of generality. While we recognize that the "end use" indicia acts as a "filter" or a "first stage" in the analysis only, it should still cast some light on the ultimate question to be determined, i.e., whether all "local" media are *close* substitutes providing sufficient competitive discipline among themselves that they should be considered to be part of the same product market in this case. We find the words of Gibson J. in *R. v. J.W. Mills & Sons Ltd.*, which the Court of Appeal in *Southam* found "worthy of replication", to be instructive on this point:

> Defining the relevant market in any particular case, therefore, requires a balanced consideration of a number of characteristics or dimensions to meet the analytical needs of the specific matter under consideration.
>
> At one extremity, an ill-defined description of competition is that every service, article, or commodity, which competes for the consumer's dollar is in competition with every other service, article or commodity.
>
> At the other extremity, is the narrower scope definition, which confines the market to services, articles, or commodities which have uniform quality and service.
>
> In analyzing any individual case these extremes should be avoided and instead there should be weighed the various factors that determine the degrees of competition and the dimensions or boundaries of the competitive situation. For this purpose the dimensions or boundaries of a relevant market must be determined having in mind the purpose for what it is intended. For example, two products may be in the same market in one case and not in another.[48]

[48] [1968] 2 Ex. C.R. 275 at 305-306.

The criterion of functional interchangeability in end use should not be treated at such a high level of generality that it precludes objective yet contextual analysis. To say that, for example, automobiles and bicycles are in the same product market because they both provide a means of transportation would make the level of generality so high that no meaningful analysis could be performed as a result of it. Some consideration must be given to context.

To put functional interchangeability in end use in context in this case, it is important to look at the buying cycle and which types of media are generally regarded as directional and thus particularly effective in reaching consumers who are at the end of the buying cycle. These consumers are "ready to buy" but must decide which commercial establishment to patronize. The question is which types of media effectively bring the particular establishment to the consumer's attention in those circumstances.

The respondents referred us to a number of American cases which, they argue, support their broad conception of end use. We do not find these authorities particularly helpful. First, and most importantly, the product market that is arrived at in a particular case is very much dependent on the facts of that case and the context in which the case is brought, that is, the alleged anti-competitive wrong that the plaintiff is seeking to cure. As Gibson J. stated in the passage quoted above, "two products may be in the same market in one case and not in another." Therefore, the mere fact that another court did or did not find that directory advertising was in the same market as other local media is not in itself compelling. Some of the cases cited by the respondents were not antitrust cases.[49] Others did not deal with directory advertising.[50] In addition, counsel for the Director was able to bring to our attention a number of other American cases in which the courts, either explicitly or implicitly, used Yellow Pages advertising as a relevant market.[51] Further, while the reasoning with respect to market definition in another case might provide us with some insight, one would have to be reasonably certain that the court in question was applying the same conceptual framework or "test" as we have adopted. These considerations all highlight the futility of looking for a simple, neat answer to market definition in the case law.

Based on the evidence, particularly materials created by the respondents themselves outside of the context of this proceeding, which we will review in more detail below, we accept the Director's position that the distinction between creative and directional media is a valid one for determining the end use of Yellow Pages and other local advertising. A fair consideration of the evidence, which will shortly be addressed, supports the position that creative advertising creates awareness of and demand for goods and services at the beginning of the buying cycle and that directional advertising refers to advertising to consumers who are at the end of the buying cycle which "directs" them where to buy a product or service. This effectively limits the number of media that can be considered to be directional.

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[49] Respondents' Book of Authorities, vol. 6, tabs A,B.

[50] Respondents' Book of Authorities, vol. 6, tabs C, D; vol. 3, tab 41.

[51] Respondents' Book of Authorities, vol. 3, tabs 38, 47; Director's Book of Authorities in Reply, tabs 6, 7, 9.

Although the respondents argued that directional advertising simply means advertising (in any media including those traditionally considered creative) that contains a name, address or phone number to "direct" a consumer to particular establishment,[52] this was not Tele-Direct's view outside of this case. In the Multimedia Training Course created by Tele-Direct for its sales representatives, directional advertising is defined as:

> Media used by the advertiser to direct the buyer where to buy or use a product or service. Examples: Yellow Pages, catalogues, direct mail. Directive media complements and supports creative media.[53]

The three examples used suggest that directional media, in fact, have very specific characteristics beyond simply including a name, address or phone number. All are print media and in each case there is no editorial or entertainment content. The consumer has no reason to consult these media other than a reason related to making a purchase, i.e., at the end of the buying cycle.

The course material also discusses and sets out in chart form the role of the various media at the various stages of the buying cycle: awareness, interest, comprehension, trial, purchase and repurchase. The text explains:

> . . . [S]uch traditional advertising media as TV, Radio and Magazines are by their nature designed to generate awareness for products and services. The impact or intrusion qualities of this advertising creates an interest for the products and services and has the ability to demonstrate the benefits to the consumer and is ultimately designed to create a need or desire in the mind of the consumer.

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[52] This is, of course, co-extensive with their definition of local advertising.

[53] Confidential exhibit CJ-16 (blue vol. 7), tab 215 at 118727.

. . .
Although creative advertising is crucial at the awareness, interest and comprehension stage of the buying cycle, it loses impact at the actual purchase stage because of the time or distance between the initial awareness and the purchase.[54]

At the purchase stage, newspaper, direct mail, outdoor, radio and Yellow Pages are all considered to have some strengths. Television and magazines are not. Of those with strength at the purchase stage, only newspapers and direct mail (and Yellow Pages), however, are described as "directive". The strength of outdoor advertising at the purchase stage is as a "reminder message". The strength of radio at that stage is to offer price points and convey a "sense of urgency". Again, this course material supports the view that directionality imports something more than the ability to provide a consumer with a name and address. All of television, newspapers, direct mail, outdoor, radio and Yellow Pages are capable of including this information in advertising, yet Tele-Direct did not consider them all to be directional.

This interpretation is further supported by the letter sent to the Director by Tele-Direct during the course of the Director's investigation into the industry (referred to as the "Bourke letter"). The letter was intended to provide industry background.[55] It states that:

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[54] *Ibid*. at 118801.

[55] At the hearing, counsel for the respondents attempted to convince the Tribunal to attribute less weight to the letter than we otherwise might on the grounds that it was not prepared with the assistance of an economist and that it was produced in a compressed period of time. The letter was written by Tele-Direct's Vice-president of Marketing with the assistance of a number of lawyers from counsel's office. We have no information as to the extent of the economic background of any of those lawyers. It is signed by the President of Tele-Direct. During the discovery process the respondents resisted production of the letter on the grounds that it was protected by settlement negotiation privilege. The Tribunal ruled that the letter did not fall within that privilege and ordered it produced. We have no hesitation, for the purposes for which we refer to the letter, of attributing significant weight to it.

> The Yellow Pages traditionally is viewed as a "directional" or "considered purchase" advertising medium, which provides consumers with information on where they can purchase the goods and services they want. . . . Directional advertising is most attractive to local advertisers, particularly local retailers, who seek to motivate customers to visit their stores or to use their services. *Other directional media include direct marketing, catalogues, trade magazines, and specialty supplements to newspapers or magazines*.[56] (emphasis added)

There is no mention made of outdoor or television and radio as directional media. When Thomas Bourke, Tele-Direct's President, testified at the hearing he confirmed that the basic strength of Yellow Pages was to provide information on where to buy, as stated in the letter. In the list of directional media, he would, however, now include the classified sections of daily and community newspapers and specialty and other classified directories.

The letter continues:

> By contrast, the other major advertising media - outdoor, newspapers, radio, television and magazines - are classified as "creative" advertising media, which create awareness of and demand for products and services. Creative advertising assists advertisers who are either trying to sell a product or service, or promote their name. This service is attractive to major manufacturers or suppliers, who usually do not have a preference as to where the consumer buys its product or services.[57]

Since names, addresses and phone numbers could just as easily be included in advertising in the regular part of a newspaper and a magazine as in a special supplement or classified section, something more is involved in the way that the participants in the industry view directionality. As in the training material, all the examples of directional media are characterized by the absence of general editorial content. The characteristic that specialty supplements and classified sections in newspapers or magazines, other directories, catalogues and direct mail

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[56] Exhibit J-5 (green vol. 3), tab 239 at 86008.

[57] *Ibid*.

share with Yellow Pages is that the advertising in those media will be totally ineffective unless it is consulted by people who are "in the market" -- who are looking to make a purchase. As Mr. Bourke put it when describing how Yellow Pages complete the buying cycle, they must be in a "buying frame of mind". Consumers will not be involuntarily exposed to the advertising by virtue of going to the medium for entertainment or other reasons; they must voluntarily decide to consult the Yellow Pages or a catalogue, read the direct mail or an advertising supplement or classified section. These media are not picked up and browsed through idly in a spare moment.

The respondents argue that all directional advertising, even Yellow Pages advertising, has a "creative" component. Otherwise, they submit, no one would pay for a display advertisement in the Yellow Pages. The free business listing could provide a name, address and phone number. Clearly, there is "creativity" involved in designing an eye-catching Yellow Pages advertisement. This is not the same as creative ("creates" *demand*) as opposed to directional ("directs" consumers who are ready to buy) advertising as those terms are used in the industry, according to the evidence.

Mr. Bourke, echoing Raymond Greimel, Executive Director of YPPA, testified that the new attitude in the industry is that Yellow Pages are *both* directional and creative. He was unable, however, to explain how Yellow Pages advertising "creates awareness of and demand for products and services" in the words of the Bourke letter, as he recognized that people do not consult the Yellow Pages unless they already have a need for some product or service. He could only say that Yellow Pages advertising "reinforced" or "supported" the advertising in the creative media.

We are not satisfied from the paucity of evidence on the point that directional advertising means that the medium containing the advertising is a "reference tool", as the Director further submits. If this element were proven, virtually all media except directories would be excluded from potentially being part of the relevant product market at this point. We do not consider that the evidence supports narrowing the definition of "directional" in this respect.

Functional interchangeability is simply a preliminary filter to exclude those products which evidently do not have the same end use as Yellow Pages advertising. Nevertheless, certain conclusions can be stated. First, the respondents' position that local advertising in *all* media qualifies as directional is not tenable. In particular, television, radio and outdoor media are clearly not treated as directional in Tele-Direct's own materials. Television is seen as having little relevance to the latter stages in the buying cycle; it is strong in creating awareness and interest at the beginning of the cycle only. While radio and outdoor have a role at the later stages, that role was not to present a directive message but rather to create "urgency" or serve as a "reminder" of other advertising.

This is not to say that these media *cannot* be used for directional advertising in any circumstances. It is a possibility, but in deciding whether various media serve the same end use, one must look to usual uses and not mere possibilities unsupported by the evidence. We are of the view that both the electronic and outdoor media can be excluded at this point as they are not directional media and thus do not have the same end use as Yellow Pages advertising. Since the electronic and outdoor media have not met this "necessary" condition for inclusion in the relevant product market, we will not deal with them further.

Second, there is some doubt as to whether "regular" advertising (as opposed to special supplements or classifieds) in newspapers and magazines is properly included as directional advertising. Based on the list in the Bourke letter, which was updated by Mr. Bourke in his testimony and is therefore, presumably, as comprehensive as Tele-Direct considers it should be, we could exclude "regular" newspaper and magazine advertising at this point. The Multimedia Training Course, however, does refer to "newspaper" advertising, without further details, as directive. Given the preliminary nature of the criteria of functional interchangeability and in light of the overall model used by the respondents to argue their case, we will not exclude newspapers from further consideration. Magazines will not be dealt with further, as they were largely ignored in the remainder of the evidence and argument of both parties.

(4) Other Relevant Indicia

Having determined that some, though not all, local advertising media pass the threshold test of functional interchangeability, we will now consider the evidence and argument on the remaining practical indicia to decide if those media are close substitutes and belong to the same product market as telephone directory advertising.

(a) Physical and Technical Characteristics

Telephone directories are issued annually, are comprehensive both with respect to including all suppliers and being delivered to all telephone subscribers, and they are governed by their own rules with respect to the content of advertising. The Director is of the view that these characteristics set Yellow Pages apart from other media.

The respondents argue that each advertising medium has different "strengths and weaknesses" and can claim to be unique. They submit that a "catalogue" of differences is not alone enough to place two products in separate markets. They state that the relevant question is whether the product is unique in some respect that significantly limits the extent to which *buyers* (here, advertisers) are willing to substitute other products for the product at issue. We agree that to deal with physical and technical characteristics separately from the views and behaviour of buyers is somewhat artificial. It is, however, the way in which the parties have chosen to organize their arguments and the evidence in this case. Therefore, in this portion of the judgment, we will restrict ourselves to the points raised by the parties in their respective arguments under that heading. We recognize that this factor is mainly important in the analysis as providing background for the next section on buyer views and behaviour.

(i) Time Insensitivity/Permanence

Advertisements in the Yellow Pages are finalized several months prior to publication and have to stand for the entire year between directories. This means that Yellow Pages advertising cannot be used to convey time-sensitive information. As noted by Professor Schwindt, for the Director, this sets Yellow Pages apart from other directional media, such as direct mail or supplements to magazines or newspapers, in which time-sensitive information such as prices tends to be featured. In fact, until recently Tele-Direct regulations prohibited the inclusion of prices in Yellow Page advertisements to avoid potential false advertising claims. This ban has now been lifted. It is doubtful whether, in a fast-changing world, price advertising can ever be an important part of telephone directory advertising while directories are a print medium that changes only every year.[58] The evidence of the advertiser witnesses amply supported the conclusion that Yellow Pages are *not* used for time-sensitive advertising.[59]

The fact that Yellow Pages cannot be used to convey time-sensitive information is characterized by the respondents as a "weakness", the "flip side" of which is "permanence", a "strength". Based on a statement by Professor Willig in his rebuttal affidavit,[60] they conclude that a weakness in Yellow Pages does not suggest that advertisers *would not* substitute other media for Yellow Pages; a weakness probably suggests that they *would* substitute other media.

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[58] Apparently there is some experimentation in some American centres with allowing restaurants to run advertisements that include menus. In a relatively stable economic environment firms in such an industry might be willing to risk committing themselves to prices for as long as a year.

[59] See, e.g., the testimony of Jack Forrester of HOJ Car and Truck Rentals, that he does not use Yellow Pages for specials or promotions: transcript at 5:778 (11 September 1995); the testimony of Jean-Yves Laberge of the Turpin Group of automobile sales and leasing businesses, that he puts prices and specials in his newspaper advertisement but not in the Yellow Pages: transcript at 13:2406-407 (3 October 1995); and the testimony of Steve Kantor of Tiremag Corp., who sells wheels and tires, that he cannot use Yellow Pages to advertise seasonal product offerings or prices: transcript at 17:3288-89 (11 October 1995).

[60] Paragraph 24 of Professor Willig's rebuttal affidavit (exhibit R-181) reads:

> . . . As a matter of economics, it is difficult to see how negative characteristics can contribute to a showing of dominance in a narrow relevant market. Instead, negative characteristics contribute to the willingness of buyers to substitute out of the product at issue, and so their recognition should, if anything, argue for a wider market to be relevant, not a narrower one.

Thus, any identified weaknesses are seen as evidence of Yellow Pages vulnerability and not as evidence that the products against which Yellow Pages is being compared may not be close substitutes.

We do not accept that a "weakness" alone provides evidence of or even suggests substitutability. Substitution is not a one-way process. The conclusion on whether there are close substitutes for the firm's products is not based on asymmetrical substitution. We must certainly consider whether there is ready substitution *from* Yellow Pages *to* other media but we must also be satisfied of the reverse, ready substitution *to* Yellow Pages *from* other media.

For the very reason that telephone directories are not suited to time-sensitive information, they are the one source of directional advertising that advertisers can be virtually certain will be retained for a long period by consumers. Apart from catalogues, which often are valid for periods of up to six months, the information in other vehicles is quickly dated and will be discarded. Catalogues, however, generally provide information on a single seller and do not cover the wide range of goods and services found in the Yellow Pages. The relative permanence of directories supports the Director's position that Yellow Pages are unique among directional media in serving as a continuing reference of all available suppliers.

(ii) Comprehensiveness

It is conceded by the respondents that telephone directories are unique with respect to their comprehensive list of suppliers. They argue, however, that comprehensiveness comes from the free listings and that the directory would still be comprehensive even if it contained no display advertisements. That is true. The respondents go on to state that an advertiser values comprehensiveness *only* if the advertiser is targeting customers who contact *all* listed suppliers before making a purchase, in which case the advertiser would not need a display advertisement. The latter statement simply does not follow. The advertiser witnesses who appeared before us made it clear that they value the comprehensiveness of the Yellow Pages because that is a feature that leads consumers in general to use the Yellow Pages. (Since we are talking about a directional medium, we are speaking of consumers who are ready to purchase some good or service and are looking for a supplier.) Once a consumer decides to consult the Yellow Pages because of its comprehensiveness, an advertiser finds it profitable to advertise in the Yellow Pages to cause that consumer to choose its establishment as opposed to that of another supplier.

On the distribution side, the respondents do not dispute that there is no other medium that is so comprehensively distributed. All telephone subscribers, the vast majority of the population, receive a telephone directory. The respondents attempt to counter this fact by pointing out that persons who receive the Yellow Pages, and thus are the potential customers of businesses listed or advertising in the Yellow Pages, are also exposed to other media which do not depend on their active involvement, that is, on their deciding to consult the Yellow Pages. This argument, in effect, simply reiterates the respondents' position that all media have the same end use, since it ignores the fact that the voluntary nature of Yellow Pages (consumers must decide to consult the Yellow Pages to be exposed to the advertising) means that it is *not* used for the same purpose as are the creative media (consumers are involuntarily exposed to the advertising by virtue of using the medium for the entertainment or information value). We have found that Yellow Pages are a directional medium. Exposure to creative media is not relevant as they serve a different purpose.

The respondents also point out that the scope of a particular directory may be too broad for a particular advertiser. That advertiser may wish to reach only a limited geographic area and could do so more cost-effectively with flyers. This will be addressed in the next section when we consider buyer views on whether the unique characteristics of Yellow Pages are significant to them and thus limit their choices among media.

(iii) Other Restrictions

In addition to the restriction on price advertising there are Yellow Pages rules regulating comparative advertising, the use of coupons and the use of superlatives. There is no evidence on the effect of these restrictions. However, their existence does indicate that the publishers of telephone directories were and are willing to create an advertising environment that sets their vehicle apart from others. Clearly Tele-Direct is not concerned that these restrictions make Yellow Pages less attractive such that advertisers would substitute other media.

In summary, all media have strength and weaknesses. Contrary to the respondents' arguments, however, we are of the view that "weaknesses" of the Yellow Pages as a medium do not imply that advertisers will readily switch from it to other media. If pricing information is important to advertisers and they *cannot* use Yellow Pages to convey prices because of restrictive rules or time-insensitivity, then their choice to use newspaper advertising instead cannot be seen as a *substitution of newspapers for Yellow Pages*. Likewise, if advertisers *cannot* achieve their goal of being in a "reference" medium by advertising in newspapers, then their decision to advertise in the Yellow Pages cannot be seen as a *substitution of Yellow Pages for newspapers.* In other words, strengths and weaknesses in areas important to advertisers are really characteristics that tend *against* substitutability. The existence of significant (to advertisers) differences between Yellow Pages and other media would lead to the inference that other media are not close substitutes to the Yellow Pages.

(b) Views, Strategies, Behaviour and Identity of Buyers

Both sides recognize the importance of the identity, views and behaviour of buyers, in this case, Yellow Pages advertisers. Before turning to the more detailed evidence, we first set out the position of each of the Director and the respondents on the question of substitutability from the perspective of the advertisers.

The Director submits that advertisers do not consider that there are any close substitutes for Yellow Pages advertising. He bases this on the testimony of the advertiser and agency witnesses, who although not a representative sample, gave cogent reasons for their views on substitution despite the diverse businesses involved. He argues that the advertisers cannot easily move their advertising spending from Yellow Pages to other media because of the value that they place on certain unique characteristics of Yellow Pages as a medium. In support of this position, he also points to evidence that Yellow Pages spending is not even part of the "advertising" budget at large for many Yellow Pages advertisers.

The respondents conceive of all advertisers, including Yellow Pages advertisers, as operating on a fixed advertising budget which is allocated among various media (the "media mix") based on the highest returns that can be obtained from the advertising expenditures. Decisions about media mix are driven by perceptions of relative cost-effectiveness. Therefore, Yellow Pages spending is vulnerable to reduction (by means of smaller size, less colour) or cancellation in favour of expanded spending on other local media which are perceived as more cost-effective. The respondents' position emphasizes the possibility of significant substitution between media "at the margin".

The respondents argue that the evidence supports the following propositions (although they state them in a somewhat different order):

(1) the businesses that advertise in Tele-Direct's directories ("current Tele-Direct customers") also advertise in a variety of other media;

(2) current Tele-Direct customers perceive that other media provide as good or better value than Yellow Pages advertising and may be assigned as high or a higher priority in the advertiser's media mix;

(3) current Tele-Direct customers in the same line of business may each choose a different media mix, including a different emphasis on advertising in the Yellow Pages (bigger or smaller, black and white or colour Yellow Pages advertisement);

(4) many of the businesses that do not advertise in Yellow Pages ("Tele-Direct non-advertisers") advertise elsewhere;

(5) Yellow Pages advertisers who have cancelled their advertising in Yellow Pages ("former Tele-Direct customers") continue to advertise in other media; and

(6) former Tele-Direct customers are unenthusiastic about the value provided by Tele-Direct in relation to other suppliers.

They submit that these propositions support their theory that advertisers readily shift their spending between media and thus Yellow Pages advertising and advertising in all other local media are in the same product market. The respondents also point to some evidence which they say reflects *actual* switching behaviour by Yellow Pages advertisers to other media.

Two preliminary comments are in order. The first relates to the use of a term such as "at the margin" which, in effect, invites the Tribunal to ignore the cellophane fallacy because of its emphasis on current price levels rather than the competitive price.[61] Any firm or group of firms

[61] It is commonplace economics that a firm with market power will set prices where the demand for its product is elastic; that is, at the point where a further increase in price would cause a reduction in revenue. Some of the reduction in revenue may result from consumers switching to other products which are the closest substitutes *at that price*, but which would not be considered by

that have fully exploited their market power might see some substitution if the relative price of their product goes up further. Their inability to raise their prices without buyer switching "at the margin" is, in these circumstances, because they have already exercised their market power *not* because they have *no* market power because of the presence of close substitutes.

Secondly, with regard to the proposition that advertising budgets are fixed, there is some support in the evidence that this is true for large companies. The situation is not so clear for small companies. We recognize, however, that some percentage of Tele-Direct's revenue is likely derived from advertisers who have advertising budgets that include Yellow Pages. Therefore, we will proceed to address the critical question of whether these advertisers and others treat Yellow Pages and other media as close substitutes. It will be convenient, in this instance, to organize our review of the evidence put forward by the parties by focusing in turn on each of the customer groups mentioned in the respondents' propositions. We will look first at the evidence regarding former Tele-Direct customers, then turn to non-advertisers and finally, current Tele-Direct customers.

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these consumers as substitutes if the firm with market power were pricing its product *at a competitive level*. This so-called "cellophane fallacy" (originating from criticism of the decision of the Supreme Court of the United States in *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956)) can result in the mistaken conclusion that a firm does not have market power because of the presence of substitutes when in fact the reverse is true -- the substitution is occurring *because of* the exercise of market power. In principle markets should be defined at competitive prices.

(i) Former Tele-Direct Customers

This group comprises Tele-Direct customers who have *completely* cancelled their Yellow Pages advertising. One would expect, therefore, that these advertisers would provide the most compelling affirmation of the respondents' theory of ready shifts in spending between media.

At the outset, we note, however, that whatever is learned about former Tele-Direct customers cannot be generalized to the population of Yellow Pages advertisers as a whole. From Tele-Direct's 1994 Corporate Post Canvass Analysis Report we know that former Tele-Direct customers are relatively unimportant in terms of total Tele-Direct revenue, and individually they were spending far less than average annual amounts in the Yellow Pages. The 1993 revenue from advertisers who cancelled their Yellow Pages advertising completely in 1994 represented only 1.3 percent of total 1993 revenue for Tele-Direct (Publications) Inc. The average annual expenditure in the Yellow Pages for these advertisers was about $700.[62]

The respondents rely on the information about former customers provided by the January 1993 Elliott report on customer satisfaction.[63] The report indicates that former customers view Tele-Direct's products and services as "poor value" and generally of fair to poor quality, both absolutely and relative to other suppliers.

[62] Confidential exhibit CJ-28 (black vol. 7), tab 42 at 129284. Customers who disconnected their business telephone service are not included. There was no general price change between 1993 and 1994, although there were a number of incentive plans.

[63] Confidential exhibit CJ-14 (blue vol. 5), tab 173.

Because the former Tele-Direct customers could answer questions about other media suppliers, the results do indicate that *some* Tele-Direct former customers use other media. The study does not reveal what percentage of former customers are, in fact, using other advertising vehicles or which ones they are using. We know from the 1994 Corporate Post Canvass Analysis Report that former advertisers were spending relatively small amounts in the Yellow Pages. This would tend to indicate their options for buying other media on an annual basis with the dollars thus freed up are limited, given the cost of some of the media (particularly newspapers, radio and television) alleged to be close substitutes. The survey also found, not surprisingly, a low level of satisfaction with Tele-Direct among former customers. The study does not provide convincing evidence that a significant portion of former customers transferred advertising spending *from* the Yellow Pages *to* other media or that Yellow Pages is vulnerable to competition from other media as opposed to losing advertisers by virtue of its own failings.

With respect to former Tele-Direct customers the Director refers to two Tele-Direct reports which set out the reasons which customers gave to Tele-Direct sales representatives for cancelling their advertising: the "P.A.R. (Potential Advertiser Retrieval) Summary" report and the "Wipe Out Sampling Summary".[64] One can assume from the fact that the representatives were able to contact the customers that they remained in business and maintained a business listing.

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[64] Confidential exhibit CJ-87 (black vol. 14), tab 111 at 134805; confidential exhibit CJ-33 (black vol. 12), tab 85 at 132815.

Tele-Direct uses the P.A.R. form completed by cancelled customers to attempt to understand why advertising was cancelled. One of the choices on the form for reason for cancellation is "trying other media". Professor Willig found it "notable" that Tele-Direct listed "trying other media" as a choice on the P.A.R. form., i.e., that Tele-Direct was alive to the possibility of its advertisers switching to other media. However, the P.A.R. Summary report printed in September 1995 shows that only four out of 203 former customers (two percent) surveyed stated that they cancelled because they were "trying other media". Professor Willig conceded that this low number would have some significance and would suggest a low level of movement between media if the study were meant to be comprehensive.

To counter the low percentage, the respondents argue that the relevant denominator is actually smaller than 203. To the extent that 56 customers were probably going to go out of business, they should be excluded. If we remove these customers, only three percent of the former customers surveyed gave "trying other media" as their reason for cancelling their Yellow Pages advertising.

The respondents would also exclude a further 84 customers who gave a variety of reasons other than "trying other media" for their cancellation (e.g., "financial reasons", "restructuring", "wouldn't discuss", "clients are mostly from referrals") to bring the sample size to 63. They would also include in the numerator, with those advertisers who answered "trying other media", another 47 advertisers who gave various other responses[65] on the argument that these advertisers

[65] "Non-believers", "inadequate response from advertising" and "don't need large recognition".

were probably already using other media and, therefore, would not say they were "trying" other media when they moved their dollars to what they considered a more effective medium. Thus restructured, they argue that the report yields an 81 percent response rate in favour of substitutability between all media.

There is nothing in the report which supports the changes advocated by the respondents. The inclusions and exclusions are based on speculation, at best. Beyond removing the customers who have gone out of business, the report must be taken as it stands. If it is significant, as Professor Willig maintained, that Tele-Direct wanted to know if former customers were "trying other media", and included it as a possible response for former customers to choose, then it is significant whether they did choose that response or not. Any of the customers who answered could have selected "trying other media" if that were indeed their primary motivation for leaving the Yellow Pages.

On the whole the P.A.R. Summary report demonstrates that only a handful of customers may have discontinued Yellow Page advertising in favour of other advertising vehicles. Even for these customers little can be concluded about substitutability. They said they were "trying other media". Without some follow-up as to whether they found other advertising vehicles more effective in boosting their sales, it is not possible to tell if the other media were close substitutes for them. Indeed, some of these customers may have returned to Yellow Pages because they did *not* find the other media adequate for their purposes.

Similarly, the "Wipe Out Sampling Summary" by Tele-Direct shows only two of 87 (about two percent) former customers "trying other methods of advertising". The respondents attempt to re-interpret these results in the same manner as with the P.A.R. Summary report, i.e., by reducing the denominator. Again, there is no support in the document itself for such re-interpretation. This report tends to support the conclusion from the P.A.R. Summary report that very few customers discontinued Yellow Pages advertising in favour of other advertising vehicles.

(ii) Tele-Direct Non-advertisers

Tele-Direct's overall penetration rate is about 50 percent. This means, as the respondents state, that some businesses do not buy any Yellow Pages advertising. It is probably also true that most businesses advertise in some way. What does the evidence reveal, if anything, about this class of Tele-Direct non-advertisers? Is their advertising spending likely to be easily switched from whatever vehicles they are currently using into Yellow Pages (and vice versa)?

Tele-Direct divides non-advertisers into two groups: poor prospects for Yellow Pages advertising (Market 6)[66] and current non-advertisers with some potential (Market 7). Market 6 accounts are not contacted during a sales canvass; about 85 percent of Market 7 accounts are contacted. Both Valerie McIlroy, Tele-Direct's Vice-president of Marketing until July 1994, and David Giddings, a Vice-president of Sales, described the manner in which Tele-Direct contacts these non-advertisers as a "blitz". During a canvass, one or two days at various times are

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[66] For example, individuals in professions prohibited from advertising, variety stores, construction sites.

designated as "non-ad blitz days" and the telephone sales representatives focus on calling as many non-advertisers as they can each day, up to 20 to 30 calls. Tele-Direct's success in converting these non-advertisers is at most five percent.

If all media are close substitutes and advertising dollars are as fluid as the respondents argue, then Tele-Direct would seem to have a reasonable prospect of luring customers away from those other media and into the Yellow Pages. Yet, Tele-Direct's success rate with non-advertisers is very low. In addition, the approach taken to non-advertisers, namely telephone sales "blitz" days, provides little indication that Tele-Direct considers these non-advertisers "good" prospects which merit spending a lot of time and money to convert. Former Yellow Pages advertisers who have cancelled would presumably be especially good candidates but Tele-Direct does not appear to direct any special effort even to this group.

One of the studies referred to by the respondents that does include some specific information on non-advertisers is the 1990 study by Impact Research.[67] The study consisted of interviews with 36 business people in Montreal and Toronto, half of whom were Yellow Pages "non-advertisers".[68] There is some indication that the non-advertisers were probably using some other media but there is no data on how many advertisers or which media.

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[67] Confidential exhibit CJ-18 (blue vol. 9), tab 249.

[68] Contrary to Tele-Direct's habitual use of the term, the "non-advertisers" studied may have had a bold listing.

The results of the study do not, in any event, support the respondents' contention about the potential to shift advertising dollars between all local media in search of the most "cost-effective" alternative. Seventeen of the 18 non-advertisers did not advertise in the Yellow Pages "mainly because of the *perceived non-use of the Yellow Pages by their potential customers*." Sixteen of the non-advertisers were not going to advertise in the next Yellow Pages edition because they were convinced it was an "*inappropriate medium* for their advertising needs".[69] Two were undecided.

The views of non-advertisers do not support the contention that there is ready substitution between Yellow Pages and all other local media. If anything, the evidence that is available tends in the opposite direction.

(iii) Current Tele-Direct Customers

The respondents place considerable emphasis on the fact that existing Yellow Pages advertisers use a variety of media and that many believe that other media are as good or a better value than Yellow Pages. Because many firms advertise in a number of different advertising vehicles, the respondents argue, they are thus able to shift advertising dollars among them as the returns on them vary.

[69] *Supra* note at 107661, 107681 (emphasis added). One non-advertiser was just starting up his business and could not make the current edition deadline.

The evidence from the Director's advertiser witnesses, as well as from the Tele-Direct surveys,[70] confirms that Yellow Page advertisers tend not to be solely reliant on this one vehicle. Many advertisers use a variety of media. Even within a heading, some Yellow Pages advertisers have smaller advertisements, advertisements without colour or simply a free listing, thus potentially freeing advertising dollars to spend in other media. However, there is little that we can conclude from this fact alone. As acknowledged by Professor Willig, the use of more than one advertising vehicle tells us nothing about whether the vehicles in question are substitutes, complements,[71] or have no relationship whatsoever. To draw conclusions about substitutability there must be evidence that advertisers do *in fact* shift between the various media in response to competitive moves by those media.

The principal evidentiary source referred to by the respondents respecting current customers is the January 1993 Elliott report. As with cancelled customers, current customers were asked to rate Tele-Direct in terms of, among other items, value for money and overall quality. Many existing customers believe that other media provide as good value or better value and quality than Yellow Pages advertising. Thirty-five percent say that the relative value for the money of Yellow Pages is much or somewhat worse than other suppliers while the relative quality is about the same as other suppliers. Likewise, 38 percent of all customers believe that

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[70] E.g., Elliott reports: confidential exhibit CJ-14 (blue vol. 5), tab 173 (January 1993) and confidential exhibit CJ-19 (blue vol. 10), tab 285 (February 1993 - Newfoundland); V.I.A. survey: confidential exhibit CJ-11 (blue vol. 2), tab 89; Yellow Pages Satisfaction Study (Omnifacts Research): confidential exhibit CJ-15 (blue vol. 6), tab 199.

[71] The term "complement" has been used in this context primarily in its ordinary sense and not in its strict economic sense. No one has asserted that the different advertising vehicles are complements in the sense that a reduction in the price of one vehicle would lead to an increase in the price of the other. Rather the term has been used to indicate that Yellow Pages perform a different function than other vehicles and are thus needed to complete an advertising programme.

Yellow Pages are high or very high priced in relation to other suppliers. In the western region (Ontario), 56 percent of large customers believe that Yellow Pages are high or very high priced while only five percent say that Yellow Pages are very low or low priced. The respondents say this evidence shows that Yellow Pages are vulnerable to advertisers switching to other media.

We are of the view that these results tend to contradict rather than support the respondents' premise that all media are close substitutes. It is difficult to conclude that customers who had good substitutes would choose to continue to purchase a product that they believed was too high priced and of poor value. One would expect that, if all media were close substitutes, the medium perceived as providing better value and price would be purchased in preference to the others. Yet, dissatisfied Tele-Direct customers apparently continue to advertise in the Yellow Pages despite their opinion that other media are as good or better value and lower priced. The Elliott report provides more support for the proposition that Tele-Direct has a comfortable cushion of market power that permits it to keep its customers in spite of the fact that significant numbers of them were not complimentary about its service and pricing than it does for the proposition that Tele-Direct competes with other suppliers providing easily substitutable products.

The respondents also refer to a 1994 study by Omnifacts Research in Newfoundland.[72] Four focus group sessions were conducted with a total of 31 Yellow Pages advertisers, two sessions with new advertisers and two sessions with established customers.[73] In-depth interviews

[72] *Supra* note 70.

[73] *Ibid.* New advertisers were generally very small companies; established customers were larger.

were conducted with 16 customers, 10 of whom had reduced their Yellow Pages spending. Many of the customers also used other media, primarily print, in the form of local trade magazines, flyers and direct mail for new customers and flyers and direct mail for established customers.

There was a general view among the participants that they *had* to advertise in the Yellow Pages. They generally found it difficult to judge the effectiveness of the advertising they did, including Yellow Pages. In particular, they expressed considerable uncertainty about the value of larger size and coloured advertisements in Yellow Pages. Established customers ". . . tend to follow the competition when deciding on placement and size of Yellow Pages advertising. Most are clearly not sure whether the advertising in the Yellow Pages actually works, but the consensus is that they have to be there."[74] Some expressed displeasure at the number of headings since they felt compelled to advertise in several headings if their competitors did.

Particularly significant are the results of the interviews with customers who had reduced their Yellow Pages expenditures. The report states:

> Those companies who reported that their expenditures decreased fall into two main groupings: those who decreased as a cost cutting measure and those who decreased primarily because they do not perceive the Yellow Pages to be effective for reaching their target markets.
>
> Those that decreased their expenditures as a cost cutting measure essentially felt that the current economic conditions were affecting their business revenues. . . .

[74] *Ibid.* at 116796.

> Clients who have decreased their Yellow Pages expenditures because they did not consider the Yellow Pages to be effective, reported that their markets are primarily industrial or business-to-business and given the nature of the products and services that they offer, the Yellow Pages are not therefore consistent with their target markets.[75]

There is no indication in either case that customers reduced their Yellow Pages advertising in order to shift dollars into other media.[76]

Turning to the Director's evidence, the viva voce evidence of advertisers and other market participants who represent advertisers strongly supports the position of the Director that advertisers do not regard Yellow Pages and other media as close substitutes. Although several advertisers were approximately average size in terms of spending on Yellow Pages, most were in the top two or three percent of Tele-Direct customers. That is, average expenditures ranged from about $2,000 annually to well in excess of $100,000. For the most part a large percentage of advertising dollars were spent by these advertisers on other advertising vehicles, although a small number of the advertiser witnesses devoted almost all their advertising to Yellow Pages. Advertisers spending relatively large amounts in the Yellow Pages are, nevertheless, well placed to provide evidence on the opportunities for substituting between Yellow Pages and other advertising vehicles.

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[75] *Ibid.* at 116811-12.

[76] In terms of actual switching behaviour, the respondents referred to evidence of a locksmith who cut his Yellow Pages spending and bought brochures, on the advice of a Yellow Pages consultant, and of a photographer who was visited by a newspaper consultant who designed a smaller Yellow Pages advertisement for him. The implications of the existence and practices of the consultants for substitutability will be dealt with in the next section. Both newspaper and Yellow Pages consultants use a similar methodology, in that they attempt to convince an advertiser that a smaller, less expensive Yellow Pages advertisement will be equally effective *in the Yellow Pages*. The Director also provided numerous examples of "non-switching" where increases or decreases in spending on other media were unrelated to spending on Yellow Pages.

Although the circumstances of advertisers and the language used to describe their advertising strategies varied, none of the advertisers indicated that other media could be substituted for Yellow Pages. What they did say was that they use different media for different purposes. They use Yellow Pages advertising for purposes which take advantage of its unique characteristics. They advertise in the Yellow Pages because it is a reference of all available suppliers which is received and retained by most consumers and is consulted by them. They consider that Yellow Pages is cost-effective in this regard and generates a superior level of customer response.

Some, particularly large-budget, advertisers use other media to "create awareness". The witnesses use media other than Yellow Pages to advertise specials, include prices or to target a specific group or occasion. Steve Kantor of Tiremag Corp., who sells aluminum wheels and tires, uses other vehicles to convey a seasonal message, selling the "sporty" look in spring and "safety" in fall. Likewise, Kenneth Flinn, who operates a taxi and courier business (Lockerby Taxi Inc.) and relies almost exclusively on Yellow Pages, uses radio during the holiday season to convey the message "don't drink and drive". Yellow Pages cannot accommodate this time-sensitive advertising.

On this point, the respondents attempted to demonstrate the vulnerability of Yellow Pages to substitution by a review of advertisements in a number of newspapers from Toronto, Thornhill, London, Ottawa, Niagara, Sault Ste. Marie, St. Catharines and Montreal over a three-week period. The purpose was to show that some advertisers were using both Yellow

Pages and newspapers and that they could substitute one for the other.[77] Professor Willig observes that a "limited number" of advertisers employed "much the same" advertisements in both the newspaper and the Yellow Pages. He puts forward only four examples, of which only two are identical. For the other two, "the newspaper ad includes some of the same information presented in the directory display ad, but . . . the newspaper ad also includes some timely information of the kind that a directory ad could not contain, due to its permanence."[78]

The respondents provided three further examples of advertisements that were similar in both the Yellow Pages and a newspaper.[79] These types of advertisements evidently represent a very small percentage of Yellow Pages advertisements. Equally important is the conclusion that the respondents draw from Professor Willig's survey and the other examples, that the advertisements are only "essentially" the same and that where differences arise, they often stem from the *greater timeliness* of the newspaper. For example, the newspaper advertisement contains a price. They did not, however, provide us with any basis for concluding that prices and other time-sensitive information are trivial or unimportant to advertisers.

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[77] Newspaper advertisements were identified for establishments in the businesses represented by the top five Yellow Pages headings in the region's Tele-Direct directories. Then, those establishments with newspaper advertisements were sought in their local Tele-Direct Yellow Pages directories. Overall, the search found 542 newspaper advertisers in these categories. Of this group, 39% had display advertisements in both the searched newspaper and in the local Tele-Direct Yellow Pages directory, while 61% of the newspaper advertisers had no display advertisement in their local Tele-Direct Yellow Pages directory. (The 61% is comprised of 42% who had no Yellow Pages business phone number, and hence no listing in the Tele-Direct Yellow Pages of any kind. Another 12% did have lightface classified listings in the local Tele-Direct Yellow Pages directory, but no advertisement in that directory of any kind. Yet another 6% had a boldface listing in their local Tele-Direct Yellow Pages directory, but no display advertisement in that directory.)

[78] Expert affidavit of R. Willig (17 August 1995): exhibit R-180 at paras. 20-22, appendix 2B.

[79] Exhibit R-116. One of the three contained pricing information in the newspaper and not in the directory.

Time sensitivity for some advertisers cannot mean that those advertisers are likely to *switch from* Yellow Pages *to* newspapers and vice versa. Instead, they will use newspapers to convey time-sensitive information because that is what newspapers are good at doing. Likewise, they will use Yellow Pages to convey a message that is *not* time-sensitive but that takes advantage of other characteristics of Yellow Pages as a medium.

Agents specialized in selling Yellow Pages, general advertising agents, a witness with a large media buying agency and the former Vice-president of Marketing with Tele-Direct also testified that they did not consider other advertising vehicles a substitute for Yellow Pages and had not observed their customers to have ever done so.

Professor Schwindt's evidence supports the Director's argument that certain types of businesses use or do not use the Yellow Pages because Yellow Pages have particular characteristics that set them apart from other advertising vehicles. His evidence showed that businesses providing emergency services (glass repair, contractors, plumbers), infrequently consumed products (lawyers, moving and storage, exterminators), services used by travellers (automobile rental), products for which the use of the telephone is important (pizza), or any combination of these, tend to rely heavily on the Yellow Pages. Professor Schwindt also points out that there are types of businesses (grocers, department stores and theatres) that are known to advertise very heavily in other vehicles such as newspapers and flyers and spend virtually nothing on Yellow Pages.

On the other hand, Professor Willig, for the respondents, pointed out that whether Tele-Direct has market power, i.e., is vulnerable to ready substitution by advertisers to other media, depends on the combined demand of all advertisers, including those who are not necessarily very reliant on Yellow Pages. While he concedes some advertisers are more reliant than others on Yellow Pages advertising and that this affects the *average* elasticity of demand and the ability of Tele-Direct to exercise market power, he is of the view that the presence of advertisers who are willing to switch serves to discipline Tele-Direct's pricing. He acknowledges, however, that his position is subject to exception if Yellow Pages publishers could be shown to have the ability to price discriminate.

Price discrimination allows a firm with market power to secure higher profits (strictly, price less marginal cost) on sales to some customers than on sales to others. A firm without the ability to price discriminate may be disciplined by the ready ability of at least some of its customers to switch if prices are increased and, when considering a price increase, must weigh what it will lose against what it will gain from that action.

However, where a firm has found a way to price discriminate, no weighing need be considered. The prices for customers who might switch will be left at a level where they will continue to purchase. However, for those customers who are so reliant on the firm that they cannot switch, the firm may extract higher prices and therefore higher profits on sales to them. The ability to price discriminate therefore tends to demonstrate that a firm is not, at least in respect to the customers who are subject to the discrimination, vulnerable to those customers substituting other products for that of the firm.

On our assessment of the evidence, Tele-Direct does engage in price discrimination but not as between headings, i.e., it does not charge plumbers (a business likely to be heavily reliant on Yellow Pages) more for the same advertisement than it does grocery stores (likely to be less reliant). Rather, Tele-Direct price discriminates against those who tend to spend more in Yellow Pages by buying larger advertisements[80] or colour. Those customers are charged much more than can be explained by the additional costs associated with producing and servicing the enhanced advertisement. Thus, larger advertisers (by expenditure) under all headings contribute more to Tele-Direct's profits than smaller advertisers. Professor Willig agreed that if customers who use colour value Yellow Pages more than customers who do not, the pricing of colour is a way to price discriminate between customers who value Yellow Pages more and customers who value it less.

Tele-Direct does not have to target these firms; they in effect identify themselves. Firms that are heavily reliant on Yellow Pages are the ones that will buy a larger and more colourful advertisement in order to attract customers away from their competitors in the same Yellow Pages heading. This is indicated by the large average expenditures per subscriber and per advertiser under headings such as "moving and storage" and five other headings that stand out in the top 25 listed by Professor Schwindt in his report. The fact that there are advertisers under

[80] There is an important difference between Yellow Pages and non-classified advertising in other print media (or electronic media, for that matter) that results from the fact that media with editorial or entertainment content usually prefer to have minimum percentage of such content. The effect is to create an opportunity cost to having larger advertisements, because they absorb some of the available space for other content. This consideration is not present in the case of Yellow Pages and should not affect the pricing of larger advertisements.

other headings who are less reliant on Yellow Pages can have no influence on the ability of Tele-Direct to extract higher returns from advertisers who compete heavily within headings.

Moreover, while headings provide an important first indicator of whether a business is likely to be a heavy advertiser, there may be important differences among advertisers within a heading. One advertiser in a heading may have a larger or more colourful advertisement than the advertising by its competition within that heading. This is illustrated by the evidence of Howard Kitchen of Lansing Buildall, whose firm of lumber supply outlets is a relatively large Yellow Pages advertiser in the Toronto area. When asked about the fact that a large new entrant in lumber supply was not advertising in the Yellow Pages, he pointed out that his firm encouraged telephone inquiries while his competitor did not. The pricing of Yellow Pages, therefore, is able to capture the greater need of particular customers within headings as well as between headings. Thus, Tele-Direct's ability to price discriminate causes us to conclude, at least in respect of those larger advertisers who are most reliant on Yellow Pages advertising and therefore purchase large size advertisements or colour, that there is no ready substitutability between Yellow Pages and other media.

(iv) Conclusion

There is little evidence supporting the respondents' position that all media are substitutes for local advertisers. Specifically, the evidence of switching behaviour between Yellow Pages and other media is extremely weak. There is almost no evidence that advertisers regard Yellow Pages as serving the same purpose as other media nor that they regard its purpose in the broad manner put forward by the respondents. While there is evidence of changes in advertising expenditures, they are associated with changes in economic conditions or advertising strategy rather than switching between media in response to competitive moves by those media.

While it is true as a matter of arithmetic that when expenditures are shifted within a fixed budget there will be winners and losers among the media, this fact tells us nothing about the willingness of firms to reallocate expenditures within the budget *as a result of competitive moves by advertising vehicles*. Advertisers' goals, situations and advertising needs are subject to change. Specific physical and technical differences among media limit the way that they can be used to accomplish a specific objective, such as the announcement of a sale, the listing of prices or a promotion related to a change in season and raise doubt about the willingness of advertisers to treat advertising dollars as fluid or as easily substitutable between Yellow Pages and other media. The respondents' proposition that both former and current Yellow Pages advertisers use a variety of advertising vehicles is likely correct. It was also proven that relatively large percentages of former and current advertisers do not think very highly of Yellow Pages. This tells us nothing about whether there is a sufficiently large body of Yellow Pages advertisers who are willing to switch their advertising dollars in the event that Yellow Pages were priced above the competitive level. There must be evidence that advertisers reallocate dollars in reaction to competitive moves by different media. It is insufficient just to demonstrate a fixed budget and changes in allocation by advertisers between media. In other words, there must be evidence in one form or another that advertisers regard other advertising vehicles as close substitutes for Yellow Pages.

The testimony of the advertiser witnesses about why they use Yellow Pages and the importance of Yellow Pages advertising to them is supported by Tele-Direct's own studies of advertisers. Many advertisers believe they *have* to be in Yellow Pages to be in a comprehensive reference tool, particularly if their competition is there. They feel they have no choice. As stated in the Omnifacts study:

> . . . There were numerous comments concerning the fact that the Yellow Pages, like the telco, operates in a monopoly situation where their customers are to some extent captive advertisers, who have really no choice but to place their advertising with Tele-Direct.[81]

If they do not use Yellow Pages it is because it does not suit their purpose, not because they can readily move dollars between Yellow Pages and other media. The views of buyers, therefore, strongly tend to support the view that Yellow Pages and other local media are not close substitutes.

(c) Trade Views, Strategies and Behaviour (Inter-industry Competition)

The Director argues that there is little evidence that Tele-Direct or other market participants consider Yellow Pages to be in competition with other media. Whatever steps Tele-Direct took in relation to other media, he submits, are to be contrasted with its reaction to other

[81] Confidential exhibit CJ-15 (blue vol. 6), tab 199 at 116802.

market participants that it clearly regarded as competition. The other competitors referred to by the Director are consultants, agencies which sell Yellow Pages advertising, and independent publishers of telephone directories.

The respondents argue that Tele-Direct does not compete, for various reasons, with either consultants or agencies in providing *services* to advertisers. They do, however, admit that independent publishers are in the relevant market with Tele-Direct, whether that market includes only directories or all local media. We will, therefore, compare Tele-Direct's reactions to other media to its reactions to independent directory publishers, about which there is no dispute between the parties.

The respondents argue that the evidence reveals "broad competition" or "competition in fact", as referred to by the Court of Appeal in *Southam*, between Tele-Direct and all other local media. They submit that Tele-Direct views other media as competitors and has taken various initiatives to compete with other media. They argue that other media, in turn, view Tele-Direct as a competitor.

The respondents submit that evidence of "broad competition" places all local media in the same product market. The respondents say that differences in the type or intensity of response to different "competitors" should not eliminate some "competitors" from the relevant market. We cannot agree. The type and intensity of the alleged competitive response is an element for consideration in determining if the products argued to be in the same market are close substitutes. Substitutability, as pointed out in the *J.W. Mills* case quoted above, is always a question of degree. Differences in the intensity of the reaction to players admitted to be competitors by Tele-Direct and those alleged to be competitors by Tele-Direct can help us to determine where to draw the line in this case.

(i) Tele-Direct's Views and Behaviour

General

The evidence is unequivocal that other directory publishers have been referred to as competitors by Tele-Direct and the respondents concede that they are. A number of independent publishers not affiliated with a telco produce directories in Tele-Direct's territory. Over the years, Tele-Direct has collected information on and copies of directories of independent publishers. As of 1994, the information was organized into a "competitive database" as part of the creation of a "Sensitive Market Intelligence System". The sales representatives gather information and the marketing department analyzes information on independent publishers as part of this system. Tele-Direct goes to considerable lengths to track and compile data on the revenues, prices, scoping, circulation and other features of independent directories.[82]

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[82] See Competition Database Binder (1994): confidential exhibit CJ-15 (blue vol. 6), tab 205; 1994 Sensitive Market Report: confidential exhibit CJ-29 (black vol. 8), tab 51; Directory Publishers in Tele-Direct Operating Area: confidential exhibit CJ-32 (black vol. 11), tab 77 at 132125-45.

Further, it is not in dispute between the parties that when a broadly-scoped independent directory entered into Tele-Direct's territory in each of the Niagara region and in Sault Ste. Marie, Tele-Direct responded with zero price increases, advertiser incentive programs, promotional campaigns, and improvements to its own directories.[83]

While there are references within Tele-Direct documents to other media as "competitors" and to "competing for the advertising dollar", there was no effort on Tele-Direct's part to track revenues, prices, features or circulation in a comprehensive and detailed a fashion as there was with other directory publishers. When one compares the competition data base and sensitive markets material cited above to the documents put forward by the respondents as showing competition with other media, the difference in intensity is immediately apparent. They refer in their written argument, for example, to two speeches from 1984 and 1985 which refer to "competing with all other types of advertising media" and being in a "constant struggle for the customer's advertising dollar." Considerable emphasis is also placed on a 1993 document entitled "East Office Competition Analysis". The "east office" deals with only a portion of Tele-Direct's territory, namely the Peterborough, Orillia and Barrie areas. The document is a summary of a meeting regarding competition. It lists newspapers, flyers, consultants and television as competitors and canvasses various points of discussion. It does not identify particular competitors, give any detail on revenues likely lost, comparative pricing or features like circulation.

[83] For further details, see the facts set out in the section entitled "C. Market for Advertising Space - Publishing" in chapter "IX. Abuse of Dominant Position", *infra*.

There was likewise no evidence of a Tele-Direct response to other media competition that bears any resemblance to the focused and intense response to the competing directory publishers. The respondents referred us to other initiatives by Tele-Direct that they submit are of particular significance and we will deal with them in further detail below.

Educational Efforts

Educating employees to deal with the existence of competitors might be some evidence of concern by Tele-Direct about the potential for its advertisers to switch to other media. The evidence regarding Tele-Direct's educational efforts indicates, at best, a weak concern about the necessity to compete with other media. The respondents rely on the Multimedia Training Course as the principal Tele-Direct initiative to compete with other media. The only clear evidence we have, which comes from a written answer by the respondents to a question on discovery, is that the course was given once in 1992 for four days to all sales "employees". The oral evidence on the issue was vague, suggesting that the course was not an initiative that was considered significant by Tele-Direct.[84]

Based on the course having been given once in 1992 to all sales representatives, the investment by Tele-Direct was 1880 (470 x 4) person-days. Based on the average remuneration

[84] Mr. Giddings' testimony on this topic was confusing. He testified at various times that the course, or perhaps one module of it (which a discovery answer indicated had never been used for training purposes), was given to new representatives in about 1990 and that it, or some part of it, had been repeated for unknown numbers in 1993 and 1994. However, he also testified that no new premise sales representatives had been hired since 1992 casting doubt as to how many times and to how many persons the course was given.

of a premise sales representative, the cost to Tele-Direct was *at most* $500,000.[85] This was a one-time cost relating to *all* of Tele-Direct's territory with benefits spread over a number of years. By contrast, in reaction to the entry of DSP in Sault Ste. Marie, in one year (1993) in one relatively small market Tele-Direct spent over $215,000. Evidence of educational efforts does not suggest a great concern on Tele-Direct's part about other media competition.

Sales Aids

The respondents point to a variety of "sales aids" produced by Tele-Direct which contain references to other media. They submit that the specific claims made in the documents with respect to other media in relation to Yellow Pages are unimportant. Rather, they say significance lies in the simple fact that Tele-Direct created material which refers to other media to provide to its sales force. They claim that if Yellow Pages were "unique", there would be no need for this type of promotional material.

We are of the view that in examining the documents prepared for use by Yellow Pages representatives, we should consider whether the content of those documents points to the treatment by Tele-Direct of Yellow Pages as a separate advertising medium (the Director's position) versus whether the content indicates signs of competitive activity with other media (the

[85] The use of the average premise remuneration errs on the side of being too high. The other type of sales representative, a telephone sales representative, earns, on average, only about 60 percent of what a premise representative earns. Also, Mr. Giddings did say at one point that this course was given to *new* representatives, who would likely earn less than average in any case.

respondents' position). The mere existence of sales aids which mention other media in some context cannot be solely determinative of the issue.

Two memoranda dated 1983 and 1985, respectively, deal with direct mail (flyers) as an alternative to Yellow Pages and provide visual aids to salespeople. The first concludes:

> We all know that any form of advertising is beneficial in one way or another but direct mail should never be an alternative to Yellow Pages when considering the circulation, permanence, or economy of the two mediums, and these visuals prove that.[86]

The second states:

> Unbelievable.
>
> When comparing the economy of Yellow Pages with the cost of Direct Mail it is hard to imagine why someone would consider Direct Mail an alternative to Yellow Pages advertising.[87]

Despite the fact that Tele-Direct sales representatives may have had, to some extent, to provide arguments on the superiority of Yellow Pages in relation to flyers and, indeed, any other media, the words used suggest non-, or at least low, substitutability between Yellow Pages and the alternative media. The authors of the memoranda appear to express disbelief and incredulity that anyone would ever consider direct mail as an economical alternative to Yellow Pages advertising.

Tele-Direct's Strategic Business Plan for the time period 1983-88 states:

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[86] Exhibit J-2 (red vol. 2), tab 82 at 8833.

[87] *Ibid*., tab 81 at 8827.

> Part of a large, profitable but slow growth industry, the directory advertising business operates from a privileged position in a captive market.[88]

Tele-Direct has characterized its own market as "captive" in this business plan. We infer that this high level document reflects the perception of Tele-Direct management as to competition from other media. It places in context the aforementioned memoranda.

The respondents also refer to a set of documents that was prepared for the 1992 sales canvass which includes comparisons between the cost of advertising in Yellow Pages and two dailies and three community newspapers in the Toronto area. Other documents give the same type of information for other cities and towns. Another similar package compares the cost of Yellow Pages to two Toronto dailies, and shows what could be purchased with the Yellow Pages dollars in television, radio, flyers, calendars, key chains and ball point pens.

When we examine the content of these documents, we find that, as with the direct mail examples, what is being emphasized is the *lack* of comparability between the cost of Yellow Pages and the other media. With respect to the comparisons with newspaper advertising, one document (from 1992), for example, compares a 1/4 page advertisement for 30 days in the Toronto Yellow Pages (circulation over 1.3 million) at $677 with a 1/4 page single insertion in *The Globe and Mail* (circulation about 325,000) at over $7,000. Mr. Giddings described this type of sales pitch as making a comparison to point out that there is *no* comparison between Yellow Pages and newspapers. Newspapers are simply so much more expensive that there is no

[88] Exhibit J-2 (red vol. 2), tab 116 at 13525.

comparability. Another document has a similar tone; it focuses mainly on newspapers for comparisons but also highlights how *little* can be purchased with the Yellow Pages dollars if transferred to television ("2-60 second spots, non-prime time"), radio ("2-1 minute spots") and flyers, calendars, key chains and ball point pens (15,600 flyers, 709 calendars, 1,213 key chains and 1,365 pens while Yellow Pages circulation is over 900,000).

Tele-Direct, unlike other print media, does not use a "CPM" or cost per thousand measure in promoting its product to advertisers. A CPM is a calculation of the cost of the medium per thousand persons reached, which can be applied to the number of copies sold (assuming one reader per copy sold) or read (if that number is known) of, for example, a magazine or newspaper. The CPM allows comparisons between print media. Tele-Direct researched the possibility of developing a CPM for its directories in the late 1980s. Its survey of general and specialized advertising agencies revealed that the agencies thought such a measure

> . . . entirely unnecessary since we [Tele-Direct] are the only ones in this field and there can be no similar comparison (they absolutely cannot imagine comparing us to the other "media").
>
> . . .
>
> In the event of serious competition, all agree that such a tool would be useful.
>
> However, two of the largest agencies already understand the usefulness and even suggest the development of this type of measure to better acquaint people with the Yellow Pages on a "national" level, and to establish ourselves as the unbeatable leader in the industry.[89]

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[89] Confidential exhibit CJ-10 (blue vol. 1), tab 17 at 106527-28.

Although a later study concluded that a CPM measure should be developed for Yellow Pages that would be, to some extent, comparable to other media in order to "contribute to developing a media image for Y.P. directories, and would create a barrier for potential competition", none was developed. Tele-Direct does use a CPM-type formula internally in its pricing to ensure that its directories of similar circulation are priced similarly but CPM is not used as a marketing tool.

Equally relevant to the question of how Tele-Direct views its product in relation to other media is the large volume of Tele-Direct promotional material selling advertisers on the advantages of being dominant *in* a Yellow Pages heading. The virtues of size and colour are extolled in testimonial letters and other promotional material. The "YPROI study", which the respondents argue is a primary tool of their sales force in selling the "value of the medium", starts with a comparison of which media influenced persons who had made a recent purchase,[90] but also includes a page trumpeting the importance of size, colour and "impact" within the Yellow Pages so as to influence the buyer's selection of a firm once he or she consults the Yellow Pages.

The advantage of "standing out" that is being sold to customers is with respect to competitors advertising *in the Yellow Pages*, and not with reference to advertisements in some other medium. As pointed out by one of the Director's economics expert witnesses, Margaret Slade,[91] the amount of advertising a firm does in the Yellow Pages is dependent on how much its

[90] Radio - 4%, television - 6%, other - 11%, newspapers - 19% and Yellow Pages - 60%: confidential exhibit CJ-18 (blue vol. 9), tab 243 at 107177ff.

[91] Professor of Economics at the University of British Columbia.

competitors do. When a Yellow Pages sales representative convinces a customer to increase its expenditures on Yellow Pages advertising, this creates pressure on its competitors to do likewise (referred to as the "prisoner's dilemma"). This phenomenon came through in the comments received from the established customers participating in the Omnifacts study in Newfoundland, that they tend to follow the competition when deciding on placement and size of their Yellow Pages advertising. The pressure on advertisers to observe and to some extent follow what their competitors are doing in the Yellow Pages indicates that Yellow Pages are a distinct medium, a separate arena within which firms seek to stand out.

The respondents stress that competition for the advertising dollar is not so much a matter of whether firms advertise in the Yellow Pages but of how *much* they advertise, primarily whether they buy coloured advertisements and larger advertisements. The number of headings would be an additional factor determining the expenditures of customers. It is noteworthy that the attempts by Tele-Direct to sell colour and size to its advertisers are based on comparisons with black and white advertisements or smaller advertisements *within* Yellow Pages.[92] Thus, the success or failure of Tele-Direct representatives in capturing more of the advertising dollar depends on the extent to which they can convince customers that they need to upgrade their advertisements *to be more effective vis-à-vis the customers' competitors* in the Yellow Pages. It is difficult to perceive of this as "inter-media" competition.

[92] While it is true that price comparisons with the newspapers are used, including different sizes of newspaper advertisements and advertisements with red, the message is that it is cheaper to use the Yellow Pages regardless of the size or colour of the advertisement.

Pricing -- General Policy

Another relevant area in inter-media views and conduct concerns how, if at all, the prices of other media influence Tele-Direct's pricing. Tele-Direct generally establishes its prices about a year and a half to two years in advance, with prices, for example, for the 1995 directories set in late 1993.

The Pricing Policy documents placed on the record reveal that Tele-Direct considers various inputs in setting prices. For example, in the 1993 Pricing Policy produced in October 1991,[93] these included rate/circulation alignment policy,[94] recent Tele-Direct price-ups (1988-92), the consumer price index ("CPI") (1991-93), the paper and allied industry price index (1990-92), the percentage change year-to-year in the number of directory copies printed by Tele-Direct (1991-93), estimated price-ups in other media for 1992 and Tele-Direct's internal rate of inflation (1991-93). Given the timing, much of the information is estimated. The 1994 Pricing Policy is a two-page document only as all 1994 issues had a zero percent price-up. In the brief text, the following are mentioned: relationship with customers, impact on profitability, prevailing economic factors, cost containment including a recent, more favourable printing contract and the rate of inflation or CPI. In the 1995 Pricing Policy, the only change from the 1993 Pricing Policy is to replace the "paper and allied industry price index" heading

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[93] The 1993 prices were revised in February 1992. The respondents rely heavily on this particular exercise; it is reviewed in detail below.

[94] Consistency in cost per thousand of circulation across directories.

with "junked directories".[95] The 1996 Pricing Policy adds two additional items, gross domestic product and personal disposable income and reverts to using an indicator of paper cost increase, as for 1993.

In all cases, the information regarding the forecasted price-ups of other media that is contained in the policies was obtained from general advertising agencies, usually two or three different ones, and is stated as a range. The media included are television, dailies, magazines, outdoor and radio. "Business papers" also appeared in one year and "transit" in one other year.

To obtain insight on how the information with respect to other media entered into pricing decisions, we look to the testimony of Ms. McIlroy, who was intimately involved in the pricing decisions. According to her, the "key drivers" of pricing were, in order of importance: relationship to cost, rate/circulation re-alignment, revenue stream for the sales force and local considerations, both economic and the presence or feared entry of a competitive directory. She stated that there was no direct relationship between the prices of other media and Tele-Direct's pricing. Her view was based on her own experience and a review of all relevant pricing documents on the record, dating from the early 1980s to the 1995 Pricing Policy. Ms. McIlroy did not alter her position regarding the relative unimportance of other media in setting Yellow Pages prices when responding to questions on cross-examination.

[95] Ms. McIlroy explained that the "junked directories" are those that never enter into circulation. Tele-Direct used the volume of junked directories to forecast how many copies should be printed and to ensure that estimate was realistic. If many of the copies printed end up as junked directories, this over-inflates Tele-Direct's circulation figures.

Douglas Renwicke was the Senior Vice-president to whom Ms. McIlroy reported from 1991-94 and was involved in sales or marketing from 1988. He expressed general agreement with Ms. McIlroy's description of the price setting process. He disagreed over certain details that are not germane to the present discussion. However, more importantly, he also disagreed with Ms. McIlroy concerning the relevancy of other media prices in Tele-Direct price setting.

Mr. Renwicke stated that the three "primary" key drivers for pricing in the 1990s are CPI, other media price-ups and local market knowledge. A group of "secondary" key drivers include growth and circulation, gross domestic product and Tele-Direct's internal rate of inflation (costs). He distinguished price setting in the 1980s when the key drivers were circulation, internal costs and, from 1987 to 1990, circulation alignment.

At least for the 1980s, during which Tele-Direct enjoyed exceptional growth, Mr. Renwicke agrees with Ms. McIlroy that factors such as the internal rate of inflation at Tele-Direct and circulation growth were primary determinants of Tele-Direct's prices. He also recognizes that towards the end of the 1980s discrepancies in rates per thousand in different directories became another important concern that entered at the local market level. The attempt to get prices in line across markets was abandoned for a couple of years following the recession but appears to be re-emerging as an ongoing factor. Considering Ms. McIlroy's and Mr. Renwicke's evidence together, we conclude that other media prices were not a "key driver" during the 1980s.

Mr. Renwicke explicitly distinguishes the 1990s and it is here that he appears to take issue with Ms. McIlroy. We will, therefore, look in more detail at the information available to the officers engaged in price setting in 1991, 1993 and 1994 (for 1993, 1995 and 1996).[96]

The 1993 Pricing Policy document sets out the following predicted increases in various items for 1993:

> Increase in CPI for Ontario: 3.6%
> Increase in CPI for Quebec: 3.7%
>
> Tele-Direct internal rate of inflation: 5%
>
> Increase in cost of printing: 4.7%
>
> Increase in copies to be printed: 2.9%
> (proxy for circulation increase)

The ranges of predicted percentage price-ups for other media set out in the document were obtained by Claude Phaneuf, Manager of Marketing Research, from two general advertising agencies and a media buying firm.[97] Notably, these predicted increases are for *1992 only*:

> Television: 0% - 10%
> Dailies: 3% - 7%
> Business Papers: 5% - 8%
> Magazines: 3% - 7%
> Outdoor: 3% - 5%
> Radio: 4% - 7%

[96] The 1992 exercise (for 1994) is not included as prices were not increased.

[97] Information on business papers and outdoor came from only one source.

According to Messrs. Phaneuf and Renwicke the predicted price changes for 1992 were considered relevant even though Tele-Direct was considering price changes for 1993 because the canvass of customers for the 1993 directories was done during 1992. However, Mr. Phaneuf could not explain why predicted changes for other factors such as the CPI were obtained for 1993.

Two notes accompany the information on other media price increases. They state: "Demand Driven Market" and "Anybody's Crystal Ball". According to Mr. Phaneuf, the second note is a warning about the discrepancy in the information received from different sources (as indicated by the wide range of predicted price changes, such as for television). Taking the first note at its face value, it means that the prices that would actually prevail in 1992 would depend on the state of demand at that time.

The average Tele-Direct price increase established in October 1991 for 1993 was five percent, with a minimum of 3.5 percent and a maximum of 5.9 percent for specific directories. The average price increase of five percent for 1993 falls within the range of other media price-ups (not difficult since the range is so large) but the same average increase could just as easily have been arrived at without any reference to other media prices. This observation also applies to the pricing documents for 1995 and 1996 that were used in setting prices in 1993 and 1994.

Several other points emerge from a review of the information available to Mr. Renwicke and other officers. Although Mr. Renwicke stated that he would be concerned about the prices of community and daily newspapers, only the price-up of dailies was collected. While the general agencies that provided the information to Mr. Phaneuf were much more likely to be familiar with dailies than with community newspapers, it is instructive that there is no evidence of any effort by Tele-Direct to obtain pricing information about its other alleged competitors, community newspapers.

Further, no information on flyers or direct mail is included. Other Tele-Direct documents group flyers with Yellow Pages as directional media, indicating that prices for flyers would clearly be relevant, and perhaps more relevant than predicted prices for the electronic media, business papers and magazines. We also note that the information provided by Mr. Phaneuf for television does not reveal whether the prices in question relate to local television, network television or both. When questioned about this Mr. Renwicke was not sure but thought that the predicted price changes related to local television.

We conclude that Ms. McIlroy's view that the prices of other media had little or no influence on Tele-Direct's pricing policy in the 1990s is borne out. Mr. Renwicke's use of the term "key driver" when referring to the prices of other media is disingenuous. The documentary evidence does not support this characterization. Nor, in fact, does the remainder of Mr. Renwicke's own testimony. By a "key driver", he apparently meant a very tenuous relationship between Tele-Direct's price increases and the price increases of other media. He testified that other media prices enter into Tele-Direct's price setting as follows:

> . . . [W]e wouldn't focus this closely on network TV as we would on community or daily newspapers, but we focus on that because we don't want to be way out of line with what newspapers are pricing up at or other comparable media that we feel our advertisers use amongst their choices of how to promote their business.
>
> . . . We feel if the gap was too large and we didn't pay attention to that over time, there could be at least substitution on the margin that could take place.
>
> I think that's a real concern throughout the recession.
>
> . . .
>
> Q. You said you would be concerned if the prices were way out of line. What do you mean by "way out of line"?
>
> A. Frankly, particularly with newspapers, I would consider anything, five percent or greater, to be too much out of line.[98]

A fear of losing *some* advertising dollars to other media if a *relatively large* difference in price *increases* persists over time (and during a recession) confirms only that newspaper or other media pricing provides little or no competitive discipline for Tele-Direct's pricing. Tele-Direct did not ignore the prices of other media; they were a part of the general economic environment. But given the types of media covered and the tentative conclusions that it could derive from the information we cannot conclude that it had the concern of a firm worried about close substitutes.

Pricing -- Revision of 1993 Prices in 1992

The respondents place considerable emphasis on the fact that in February 1992 Tele-Direct, for the first time ever, revised its 1993 prices during the canvass for the 1993 directories

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[98] Transcript at 44:9285-86, 9290 (22 November 1995).

as it ran into advertiser resistance due to the difficult economic times. For the remaining directories not yet canvassed the average price increase was reduced from five percent to 3.2 percent.

The respondents point to a brief statement in the minutes of a sales and marketing executive meeting held in February 1992 which they say reflects the reasons why prices were revised:

> The rates that were implemented for 1993 have been revised to lower levels given the reaction of our customers to our 1992 prices, *the pricing of other media* and the expected rate of inflation in Ontario and Quebec.[99] (emphasis added)

They also rely on the revised Standby Statement for 1993 Pricing which was presented at the meeting and apparently accepted by all concerned. The Statement reads:

> Our pricing policy for 1993 issues of Yellow Pages and White Pages directories has been revised downward to take into consideration the economic conditions prevailing in 1992.
>
> This policy reflects the fact that most prices are on a downward trend for 1992. It is also in step with the advertising industry where media rates for 1992 are expected to be in the 3% to 5% range for daily newspapers, magazines and out-of-home (billboards, etc.). Radio and T.V. are expected to be in the 0% to 5% range with peaks of 10% for T.V. due to high demand for last-minute buying.
>
> All media are expected to increase their rates towards the end of 1992 as the economy picks up. Forecasts for 1993 and 1994 are for prices increases of 10% or more. Based on these forecasts, it is evident that Yellow Pages directory advertising will be one of the media with the lowest price-ups during that period.

[99] Confidential exhibit CJ-12 (blue vol. 3), tab 115 at 109881.

> Finally, our pricing structure must also reflect our own internal cost increases which have been kept to a minimum for 1992 thus allowing us to keep price-ups at their very low levels.[100]

Both Mr. Renwicke and Ms. McIlroy attended the meeting at which the prices were revised. Ms. McIlroy attributed no importance to the Standby Statement as a price setting document, regarding it purely as a document prepared for public relations purposes. Nor did Mr. Renwicke mention other media prices when describing the motivation for the revision in 1993 prices. He emphasized general economic conditions:

> In 1991 we clearly did not project the decrease that would take place in CPI or the recession . . . [I]n February '92, we actually re-did prices for '93 for the books we could still catch and I am thinking of the border markets in particular that were being decimated with cross-border shopping, Niagara Falls, Sarnia, Windsor.
>
> We reduced those all by a percentage point. So, we did our best to try and get back down to a point where we were near CPI because our customers were reading in the paper every day that inflation in Toronto was approaching zero and why were our rates up at four per cent, five per cent, six per cent. Partly it was a function of the lag we had in setting those prices initially and not foreseeing the downturn that did take place in the economy.[101]

Taking into account both the documents and the views of two of the officers involved in the exercise, the 1993 price revision does not change our view that other media prices are not "key drivers" in Tele-Direct's pricing.

New Products

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[100] Confidential exhibit CJ-32 (black vol. 11), tab 76 at 132008-9 (public) (with covering memorandum).

[101] Transcript at 44:9283-84 (22 November 1995).

The respondents list four new product initiatives which they say show competition between Tele-Direct and the other media by the fact of their having been tried. These four products were coupons in directories, AdSpot and BrandSell (creative-type directory advertisements), colour and participation in the "Marketing the Medium" program which is designed to prove the value of Yellow Pages.

There was little evidence about the nature and cost of these programs and why they were launched, which media were considered important competitors in triggering them, what success they achieved in terms of revenue gain or loss for Tele-Direct and if they were discontinued and why. Contrary to the respondents' submissions, we cannot accept that the mere existence of these alleged new products is instructive. Their mere existence is not indicative of substitutability between Yellow Pages and any other advertising medium.

(ii) Newspapers

Newspaper Consultants

The respondents rely on the evidence of the activities of newspaper consultants as proof both of Tele-Direct's response to a "competitor" (daily newspapers) and of an initiative by another medium to compete against Yellow Pages. Newspaper consultants attempt to convince Yellow Pages advertisers that they are spending too much on their Yellow Pages advertising. Once the newspaper consultants have succeeded in persuading the advertiser to cut back on

Yellow Pages spending, they then try to convince the advertiser to place some of the dollars "saved" in newspaper advertising.

Newspaper consultants first became active in Canada in 1987, having previously operated in the United States. One method used by the consultants was to hold seminars, sponsored by the newspaper that hired the consultants, to which Yellow Page advertisers were invited. A second method, apparently employed to a greater extent in recent years, is to locate good "prospects" among Yellow Pages advertisers (those with large or coloured Yellow Pages advertisements) and then visit them.

Newspaper consultant activity is not convincing evidence that newspapers and Yellow Pages are close substitutes. If Yellow Pages and newspapers were close substitutes, the newspaper's sales representatives would be fully familiar with Yellow Pages as part of the competitive environment. If the two media were close substitutes it would not be necessary for newspapers to hire outside "consultants" on a one-shot or periodic basis. Further, it would be expected that price discounting by the newspapers would be a more potent weapon than the rather circuitous approach of the use of consultants in regaining or capturing revenue from the Yellow Pages. The success of newspaper consultants depends on finding customers who are unhappy with Tele-Direct. An unmistakable implication is that such customers do not perceive other media as close substitutes for Yellow Pages, otherwise they would already have stopped or reduced their use of Yellow Pages.

Further, a successful newspaper consultant must convince the advertiser that a different, less costly Yellow Pages advertisement or set of advertisements will work *as well* as the existing Yellow Pages advertising. In other words, the question is how much does that advertiser really need to spend to have an effective advertisement *in the Yellow Pages*? This is borne out by the fact that a consultant's methodology involves two distinct steps. First, the Yellow Pages advertiser must be convinced that he or she can reduce Yellow Pages expenditures without prejudicing the results from the Yellow Pages advertising. Then, the newspaper consultant must try and sell the advertiser on spending the dollars saved elsewhere. But, this is clearly a second step. This is recognized even by Tele-Direct in a document referring to newspaper consultants:

> newspaper reps are recommending down-size YP and don't talk about newspapers (probably will go in later to make pitch).[102]

The advertiser, of course, may simply decide to pocket the savings. This process is not indicative of shifting of spending from one competing media to another. The restriction of the context to the Yellow Pages as the first step taken by newspaper consultants is a critical point in defining the relevant market. It indicates that what is occurring is not the allocation of the advertisers' overall advertising budget between newspapers and Yellow Pages but rather focusing on whether money can be saved in Yellow Pages advertising without regard to other media.

On the whole, the presence of newspaper consultants has been sporadic, sometimes in one local market and sometimes in another. In no case have they been continuously active in any

[102] East Office Competition Analysis: confidential exhibit CJ-13 (blue vol. 4), tab 158 at 115094.

local market. With respect to the actual success of the newspaper consultants, Ms. McIlroy testified that "they were never successful in doing any damage really of any kind, at least that we monitored. I never noticed any significant damage."[103] Mr. Giddings also testified that he could not quantify their impact.[104] This is telling evidence regarding Tele-Direct's response to the alleged "competition". The success of newspaper consultants could be easily tracked. They visit advertisers individually and try to convince them to adopt a specific advertising plan. In these cases it is perfectly clear to the Tele-Direct sales representatives why the customer is making changes in his or her program. No data was gathered by Tele-Direct on the impact of newspaper consultants, which would have been expected had Tele-Direct considered the effort worthwhile. It apparently did not.

Community Newspapers

The respondents called one witness who represented community newspapers. Ginette Allard-Villeneuve of Quebecor testified that, in her opinion, community newspapers and Yellow Pages compete for the advertising budget and that the advertisements placed in each are "somewhat interchangeable". Since Ms. Allard-Villeneuve appeared to have very little familiarity with or knowledge about the Yellow Pages, it is evident that she is referring to a very attenuated form of "competition" between the two. The respondents do not, in fact, seem to be claiming anything more than that.

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[103] Transcript at 20:3827 (16 October 1995).

[104] Transcript at 39:8077-78 (15 November 1995).

(iii) Conclusion

The evidence on inter-industry views and conduct indicates that there was some limited competition between Yellow Pages and other media, principally newspapers. When the form of this competition and Tele-Direct's response to it are contrasted with the kind of head-to-head competition that occurred in Sault Ste. Marie and Niagara Falls, where there was entry of competing broadly-scoped telephone directories, there are pronounced differences in the intensity of Tele-Direct response.[105] The same difference in intensity is found in Tele-Direct's failure to track its successes and failures relative to other media and its assiduous efforts to track the sales volumes of independent publishers that it had identified as competitors. Tele-Direct did collect anticipated prices of other media in setting its prices. However, these were broad estimates and the prices for electronic media, for which there is virtually no evidence of direct competition with Yellow Pages, are included. On the other hand, media which are closer (as opposed to "close") substitutes such as community newspapers and flyers are excluded. It is difficult to see the predicted price changes of other media as an important ingredient in Tele-Direct's pricing. In short, the evidence of inter-media competition supports the Director's position that Yellow Pages and other media are not close substitutes.

[105] As already indicated, Tele-Direct responded with zero price increases, advertiser incentive programs, promotional campaigns and improvements to its own directories.

(d) Price Relationships and Relative Price Levels

There is little evidence that can properly be considered under this heading. Telephone directories and other media do not have a common standard of measurement that would allow valid price comparisons. While price comparisons were prepared for the use of Tele-Direct sales representatives, they were designed to show that Yellow Pages advertising was virtually non-comparable to other media (primarily newspapers). In any event, no common standard of measurement was used.

The respondents refer to two documents which purport to track a weighted average of annual price increases of other media and those of Tele-Direct over approximately a decade, along with the overall rate of inflation.[106] There is no rigorous analysis either in the internal documents of Tele-Direct or by the experts that would allow any conclusion to be drawn from these documents alone. Given that there are common economic forces driving prices even in very disparate industries, one would expect to see some correlation in overall price movement. An attenuated correlation in price movement does not indicate close substitutes. Even a high correlation between two sets of prices is only a *necessary* condition for the two products to be considered to be in the same market. But, it is not a *sufficient* condition to prove they are in the same market because other factors than substitutability may be responsible for the correlation.

[106] Pricing Policy - CPI & Media Price Evolution (1984-1994): confidential exhibit CR-158 at 111314; Tele-Direct Price Up vs. Canada Inflation Rate and Other Media: confidential exhibit CJ-29 (black vol. 8), tab 48 at 129708.

(e) Switching Costs

There is no dispute that the costs of switching from one medium to another are relatively low.

(5) Conclusions Regarding Substitutability

Each of the indicia points in the same direction. We have little difficulty in concluding that telephone directory advertising is a distinct advertising medium without close substitutes. Directory advertising is a directional medium with a function distinct from that of creative media. Within the group of media considered to be directional, a review of the evidence regarding physical and technical characteristics, advertiser perceptions and behaviour, inter-industry competition and price relationships leads us to conclude that telephone directory advertising is a relevant product market.

B. GEOGRAPHIC MARKET

There is no dispute between the parties that the geographic market is local in nature, corresponding roughly to the scope of each of Tele-Direct's directories.

VII. <u>CONTROL: MARKET POWER</u>

The exercise of defining a relevant market is only a step towards answering the critical question of whether Tele-Direct has "control" or market power in that market. As the Tribunal has said on previous occasions, market power is generally considered to mean an ability to set prices above competitive levels and to maintain them at that level for a significant period of time without erosion by new entry or expansion of existing firms. In those cases, the Tribunal also recognized that where the available evidence does not allow the definition of market power to be applied directly, it is necessary to look to indicators of market power, such as market share and barriers to entry.[107]

The Tribunal has never ruled out the possibility, however, that direct indicators of market power might be available as evidence in an appropriate case. Direct indicators of market power relate to the performance of the firm or firms in question or to their behaviour. The broad question that is posed is whether the observed performance results (e.g., profits) or observed patterns of conduct (e.g., pricing policy) are more likely to be associated with a firm or firms that are competitive or with those that have market power. While there are difficulties in applying direct indicators of market power, if the evidence is available this avenue should not be excluded. In this case, the parties addressed both the indirect or structural approach to market power (market share and barriers to entry) and "other evidence" of market power of a more direct nature. The Tribunal will likewise address both avenues in that order.

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[107] *NutraSweet*, *supra* note 4; *Laidlaw*, *supra* note 33; *D & B*, *supra* note 31.

A. INDIRECT APPROACH: MARKET STRUCTURE

Having determined that telephone directory advertising in local areas constitute relevant markets, it remains to determine Tele-Direct's market share and the conditions of entry into those markets. A large market share can support an initial determination that a firm likely has market power, absent other extenuating circumstances, in general, ease of entry.[108]

We will deal with the question of market power in the supply of telephone directory advertising, which includes both publishing and advertising services. The issues relating to the possible "subdivision" of the market into two (or perhaps more) component parts will be canvassed later in these reasons.

(1) Market Share

Based on Tele-Direct's November 1995 revenue estimates for independent publishers operating in its markets and the data on the record regarding its own published revenues for Ontario and Quebec for 1994, Tele-Direct (Publications) Inc. has approximately 96 percent share of telephone directory revenues in Ontario and Quebec.[109] It is instructive to note that, in 1992, a

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[108] *Laidlaw, ibid.* at 325; *D & B, ibid.* at 254-55.

[109] Overview of Other Publishers in Tele-Direct Markets: confidential exhibit CR-170; Tele-Direct (Publications) Inc. - Profitability Study for 1994: confidential exhibit CR-185. Tele-Direct's 1994 published revenues were the most recent available at the time of the hearing. Exhibit CR-170 was put forward by the respondents as their most up-to-date information on independents' revenues and so we will refer to it to the exclusion of the various other numbers and documents brought up during Mr. Renwicke's testimony. Exhibit CR-170 provides two different bottom line totals for number of independent directories and revenue. The difference is accounted for by cessation of publication by one publisher with ten directories and revenues of $1.5 million. The totals that have been used are those that include that publisher and its revenues.

Tele-Direct document estimated the total *potential* sales of independent directories in Ontario and Quebec at $32 million.[110] That would indicate an upper limit on the potential growth of the independents of well under 10 percent of Tele-Direct revenues. The same year, Tele-Direct estimated the *actual* sales of independents at less than one-third of the "potential" amount set out. The November 1995 estimates place the total revenues of the independents at slightly over one-half of what was described as their potential business in 1992. Even in Tele-Direct's worst case scenario regarding growth of independents, it would still be left with a market share of 90 percent.

Although there was no significant disagreement between the parties that the geographic markets are local in nature, largely corresponding to the scope of the relevant Tele-Direct directory, Tele-Direct's information on other publishers was presented for sales throughout the territory of Tele-Direct (Publications) Inc., namely Ontario and Quebec. No local market information was placed on the record except for the revenues of White and DSP in the Niagara and Sault Ste. Marie areas. White publishes a directory in each of Niagara Falls, St. Catharines and Fort Erie, as does Tele-Direct. DSP publishes one directory covering the area bounded by Sault Ste. Marie, Elliot Lake and Wawa in Canada. Tele-Direct publishes three separate directories for that area. On the basis that in each of those two local markets the large independent and Tele-Direct are the only significant players, in the Niagara region based on

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[110] Telephone Directory Competition in Ontario/Quebec: confidential exhibit CJ-13 (blue vol. 4), tab 164; testimony of D. Renwicke: transcript at 46:9679-80 (27 November 1995). This figure was calculated based on a research study conducted in the United States which determined that independents overall had 5.9 percent of telco directory revenues. The 1993 Simba/Communications Trends study places independents at under 7 percent of total national revenues: confidential exhibit CJ-14 (blue vol. 5), tab 174.

1994 revenues, Tele-Direct has a market share of about 85 percent, while in the Sault Ste. Marie region its market share is about 80 percent.[111]

Thus, even in the two markets in which Tele-Direct faces the most significant competition, its market share is still over 80 percent. In the absence of further detailed information on local market shares, which apparently even Tele-Direct does not compile, this fact, allied with Tele-Direct's overwhelming share of sales over its territory as a whole, leads us to conclude that Tele-Direct dominates telephone directory advertising in markets in Ontario and Quebec. *Prima facie,* we are of the view that Tele-Direct has market power based on its large share of the relevant market, absent compelling evidence of easy entry into the supply of telephone directory advertising.

(2) Barriers to Entry

In the absence of barriers to entry, even a single seller cannot exercise market power. Any attempt by the incumbent to price above the competitive level will attract immediate entry by competing sellers. We have concluded that Tele-Direct has a large share of the relevant

[111] According to the respondents' map of other publishers (exhibit R-159), only DSP and Tele-Direct are in Sault Ste. Marie, Elliot Lake and Wawa; only White and Tele-Direct are in St. Catharines and Niagara Falls. There are the Locator and Easy to Read directories in Fort Erie but there is no local revenue information on the record. It cannot be very high based on averages taken from Overview of Other Publishers in Tele-Direct Markets (confidential exhibit CR-170). Niagara calculation: Tele-Direct 1994 published revenues for Niagara Falls, St. Catharines and Fort Erie taken from Tele-Direct's 1994 Corporate Post Canvass Analysis Report (confidential exhibit CJ-28 (black vol. 7), tab 42 at 128980); White's 1994 revenue was stated by Richard Lewis to be 17 percent of Tele-Direct's revenue (transcript at 22:4363-64 (18 October 1995)). Sault Ste. Marie calculation: Tele-Direct 1994 published revenues for the Sault Ste. Marie, Elliot Lake and Wawa taken from Tele-Direct's 1994 Corporate Post Canvass Analysis Report (confidential exhibit CJ-28 (black vol. 7), tab 42 at 128983); DSP 1994 (year 2) revenues taken from DSP - Sault Ste. Marie Directory - Gross Revenue from 1993 to 1995 (confidential exhibit CA-109).

market. Proof of easy entry would overcome the initial determination that Tele-Direct has market power in the supply of telephone directory advertising.

The parties have organized their arguments regarding barriers to entry under three headings, (a) observed entry and exit, (b) sunk costs and (c) incumbent advantages. We will use the same headings.

(a) Observed Entry and Exit

Observed entry into a market can provide some indication of the existence or non-existence and the nature of any barriers to entry. There is no dispute that entry into publishing a "niche" directory appears to be relatively easy. The Director has admitted as much, based on the large number of niche directories and the high level of observed entry and exit.

The Director argues that the smaller directories have captured only a "minuscule" portion of the market and that fact, combined with Tele-Direct's lack of competitive reaction to their presence, confirms that they are of little importance in constraining Tele-Direct's market power. Further, the experience of White and DSP confirms the existence of significant barriers to entry by a broadly-scoped directory.

The respondents submit that entry need not be on a large scale and that many independent publishers have entered on a small scale and then grown slowly, thus avoiding drawing a response from Tele-Direct. Although not directly stated, the implication is that the publishers that chose this strategy have become a competitive force in the market. They also point to White and DSP as proof that broadly-scoped directories have successfully entered, remain in the market and are even profitable.

(i) Niche/Smaller Directories

Relative ease of entry by niche directories is not particularly relevant to an assessment of Tele-Direct's market power as it is clear from the evidence that the presence of these directories has had and can have little competitive impact on Tele-Direct. There is no evidence of any response by Tele-Direct to the presence or entry of a niche directory. There is certainly no evidence that they currently limit Tele-Direct's pricing or encourage better service by their presence.

With the exception of directories published by White and DSP, virtually all of the independent directories cover smaller geographic areas than the directories produced by Tele-Direct. The Director is correct that these smaller directories account for only a small portion of the overall market (less than three percent by revenue). Further, level of activity of each of the smaller independent directories indicates why individually they are not a serious threat to Tele-Direct. If the directories of DSP and White are excluded, there are 279 other independent directories with estimated average annual sales of just over $51,000 each. Of these, the 30 Locator directories had by far the largest estimated average annual sales, of the order of

$200,000 per directory. Mr. Renwicke thought that the largest Locator directory "could" be close to $1 million in revenue, which would make the remaining directories even smaller on average. The remaining 249 directories had estimated average annual sales of approximately $33,000 each. In contrast, in 1995, the broadly-scoped DSP directory had estimated annual revenues of over $1 million while each of White's three broadly-scoped directories averaged over $500,000 in revenues.

The respondents spent some time with their witness, Mr. Renwicke, reviewing examples of directories of three independent publishers in support of their position that, instead of going "head-to-head" with Tele-Direct, an independent could enter small and gradually expand and still be a competitive force in local markets. The respondents referred specifically to the Easy to Read directory, the Locator directories and the Other Book. There are Easy to Read directories in about a dozen, mainly small, Ontario communities. Locator publishes some 30 directories in various small to medium-sized Ontario towns. The Other Book published ten directories, all in the Ottawa area, but is not published anymore.[112]

The argument focuses on the Easy to Read directory in Stratford, Ontario. It is described in the argument as an "impressive" directory. The fact remains, however, that it is of negligible size. The total revenues of all the Easy to Read directories are not even stated separately on the Overview of Other Publishers in Tele-Direct Markets. Presumably they are included in the group

[112] Overview of Other Publishers in Tele-Direct Markets: confidential exhibit CR-170.

of "Other Publishers in Ontario (geographic)" which have average total annual sales of only about $31,000. Tele-Direct's 1994 revenues in Stratford were over 40 times that amount.[113]

Mr. Renwicke pointed out and made favourable comments about the features of the Locator directory entered in evidence, which included postal codes, audiotext[114] and community pages. He also described the Other Book, which had postal codes, amortization tables and a babysitter's guide as some of its features, as a "good-looking book".

Yet, despite the apparent quality of these directories, some of which contain features not offered by Tele-Direct in its directories, the respondents did not refer us to any evidence of Tele-Direct reacting to their presence in a way that would indicate that they were actually a competitive concern, in the sense of providing some discipline on Tele-Direct's quality and pricing. It is indisputable that Tele-Direct is aware of the presence of these independents and to some extent monitors their progress. That is not, in our view, evidence that these directories are a competitive force in the market. There is no indication on the record before us of any positive reaction of the type that occurred when DSP and White entered. Other than the existence of the competitive database and Mr. Renwicke's opinions, the respondents referred only to a 1993 presentation by Mr. Renwicke to the Tele-Direct board which provided information on independents and named White, DSP and Locator.

[113] Tele-Direct's 1994 Corporate Post Canvass Analysis Report: confidential exhibit CJ-28 (black vol. 7), tab 42 at 128982.

[114] Phone numbers that people could call to get anything from up-to-date news, weather and sports, to medical information and their daily horoscope.

Moreover, even if there was evidence of some competitive response by Tele-Direct to niche directories this by itself would hardly be sufficient to conclude that Tele-Direct did not have market power given its overwhelming market share. The smaller or niche directories are, by their very nature, limited in scope and influence. Thus, although entry on this scale is easy, up to a point (since each new entrant must find a new "niche" and there is a limited number), entry by smaller directories does not limit Tele-Direct's market power.

(ii) Broadly-Scoped Independent Directories

The conditions of entry by a broadly-scoped independent directory covering an area similar to the corresponding Tele-Direct directory, which will compete head-to-head with Tele-Direct, are highly relevant to the question of market power. Tele-Direct's responses to the entry of broadly-scoped directories in the Niagara and Sault Ste. Marie areas indicate that only such head-to-head competition has the potential to produce the benefits to consumers that one looks to competition for, namely lower prices and better products and services.

Can entry by publishers of broadly-scoped directories be considered sufficiently easy so that Tele-Direct is unable to take advantage of its large market share? Additionally, assuming that entry of a single competing publisher were to occur, would this assure that Tele-Direct would no longer have market power because of either the intensity of competition or easy entry conditions for additional publishers? The respondents urge us to conclude that because White and DSP managed to enter in particular markets and have remained in business, entry barriers are low enough that Tele-Direct has no market power. We decline to place so much emphasis on two isolated instances of entry in answering these questions. To answer both questions properly, we must review the arguments on entry conditions for broadly-scoped independent directories in some detail.

(b) Sunk Costs

The Director argues that sunk costs are a barrier to entry as they are perceived by potential entrants as unrecoverable if entry is unsuccessful. The respondents submit that, based on the Tribunal's decision in *Southam*, sunk costs alone are not enough. In *Southam*, the Tribunal held that neither sunk costs nor economies of scale were themselves sufficient to create an entry barrier but that together they were.[115] The respondents contend that the other source of a barrier to entry identified by the Director in this case, namely incumbent advantages, is not like economies of scale and does not operate with whatever sunk costs are present to create entry barriers in the sense required by *Southam*.

We agree that *Southam* held that sunk costs or economies of scale individually are not sufficient. That decision, however, should not be taken to mean that the combination of sunk costs and economies of scale is the only way in which sunk costs can form part of a barrier to entry. What is important is whether the market in question is one in which the potential entrant faces the risk that the post-entry conditions will be less favourable than pre-entry conditions

[115] *Director of Investigation and Research v. Southam Inc.* (1992), 43 C.P.R. (3d) 161 at 281-82, [1992] C.C.T.D. No. 7 (QL).

because of the likely response of the incumbent. Thus, in *Southam*, the presence of sunk costs and economies of scale meant that there was a credible threat that the incumbent would maintain output in the face of new entry even if doing so drove prices down towards cost.[116] This acted as a deterrent to entry.

In this case, therefore, it will be necessary to ask, first, whether there are in fact significant sunk costs associated with directory publishing. Then, we must determine whether the nature of the market is such that prospective entrants face a credible threat that the incumbent will respond in a manner that will make entry unprofitable given the existence of the sunk costs.

Sunk costs are defined as the part of the investment required for entry that cannot be recovered in the event that the attempt fails. Assets that are of value only to a specific enterprise are sunk and those that are of value to other firms are not sunk, or only partially sunk. The Director submits that entry into the directory business requires substantial sunk costs: acquiring and compiling subscriber listing information, assembling advertising into the finished directory, canvassing clients to place advertising, publishing the directory (including the cost of enhancements), training the sales force and promoting the directory. The respondents admit that there is no doubt that there are "some" sunk costs associated with publishing a directory for the first time but submit that the Director has overstated the sunk costs. They say the sunk costs are not, in fact, significant. However, the evidence of the witnesses from White and DSP, which was

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[116] The same point is made in P.S. Crampton, *Mergers and the Competition Act* (Toronto: Carswell, 1990) at 435-37.

not contradicted, amply supports the premise that the activities listed must be carried out in order to produce a directory and that the costs incurred are substantial.

DSP and White both entered by publishing a "prototype" directory. With a prototype directory, the publisher offers advertising in the directory at no charge. The prototype is distributed to consumers and the publisher then has a history of usage to give it credibility in selling advertising in its next directory. The respondents argue that the sunk costs are substantially increased when an independent publisher chooses to enter by publishing a prototype because there are no advertising revenues to offset the costs. They say that the extent of the sunk costs is within the control of the entrant and a different entry strategy would generate lower sunk costs.

Establishing usage and selling advertising are inextricably linked for a directory publisher. As stated in the 1993 Simba/Communications Trends study, achieving credibility among local advertisers is one of the biggest hurdles that a publisher must overcome.[117] It was precisely in order to overcome the credibility concerns of advertisers that both DSP and White chose initially to publish a prototype directory. Entering with a paid directory does not eliminate the credibility problem and achieving credibility, by whatever means chosen, involves costs. We have no basis on which to conclude, as urged by the respondents, that it would have been less costly overall for White and DSP to enter first with a paid directory.

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[117] "Lessons of Yellow Pages Competition": confidential exhibit CJ-14 (blue vol. 5), tab 174 at 115924.

The respondents also submit that if the entrant chose to enter with an initial paid directory, it could avoid the cost of publishing entirely if a sufficient volume of business was not confirmed during the canvass and it then abandoned its plans to enter. While we agree that the only way to avoid the costs of producing a directory is to abandon the project, we do not agree that this is a strategy that could be used with impunity by would-be entrants. The mere possibility that such a strategy could be employed exacerbates the credibility problems facing a would-be entrant, and in the event it were employed, would detrimentally affect any prospects for the same firm or other firms to attempt entry in another market.

Recognizing that there are sunk costs involved in entry into directory publishing, do those sunk costs amount to a significant barrier to entry? We are of the opinion that those sunk costs do create a barrier to entry when a broadly-scoped directory is introduced because the entrant publisher is going "head-to-head" with the telco's directory. In those circumstances, the incumbent will respond and post-entry conditions will be less favourable for a would-be entrant than pre-entry conditions. As the Simba/Communications Trends study noted, under the heading "Disadvantages of Large, Head-to-Head Directories", "[u]tilities are willing to `pull out the big guns' to protect large bread-and-butter markets."[118] It is not disputed that when White and DSP entered into Tele-Direct's markets with broadly-scoped directories, Tele-Direct responded with price freezes, incentive programs, enhancements and promotional campaigns. Thus, the combination of sunk costs and likely response by the incumbent create a significant entry barrier

[118] *Ibid*. at 115982.

and entry would not necessarily occur even though Tele-Direct was pricing above competitive levels.

(c) Incumbent Advantages

(i) Subscriber Listing Information

Would-be entrants into the directory business do not have access to subscriber listing information from the telcos on the same terms as Tele-Direct. Access to subscriber listing information by independent publishers has been the subject of some controversy and has been dealt with on several occasions by the CRTC. In 1992, the CRTC ordered greater access to the subscriber listing information in the hands of Bell Canada. Because of the price of the information, and other conditions imposed on its distribution, this decision did not result in commercially viable access to the information. Both White and DSP witnesses testified that they were forced to wait until the Tele-Direct directory was published and then re-key, verify and update the listings to use in their own directories, a costly and time-consuming process.

In March 1995, the CRTC revisited the matter at the request of White and liberalized the availability of listing information, including reducing the price that could be charged by Bell Canada. There was no indication from the White or DSP witnesses who appeared before us of any problem with the 1995 resolution by the CRTC of the price and availability issues. Richard

Lewis, the Executive Vice-president and Chief Executive Officer of White, stated, in fact, that White was very satisfied with that aspect of the decision.

The CRTC added an important proviso, however, when it ruled that consumers who wanted to opt out of having their listings sold to a "third party" could do so. From the point of view of the independent directory publishers, this caused a problem because the CRTC did not distinguish between types of "third parties". Thus, the independent publishers were grouped in with, for example, telemarketers, to whom many consumers would not want their information to be released. The 1995 decision was stayed pending an appeal to Cabinet which, in late June 1996, overturned that portion of the CRTC ruling.

In light of the Cabinet decision, which was rendered after the close of the hearing in this matter, the Tribunal invited further submissions from the parties regarding the impact of that decision on their respective positions. The respondents submit that the Cabinet decision has removed the only barrier to entry into publishing. The respondents point to Mr. Lewis's statement that after a favourable decision from Cabinet, White will proceed with additional directories in the Toronto/Niagara area. The Director agrees that the Cabinet decision will likely reduce *one of* the barriers to entry into directory publishing but maintains that there are still other, significant barriers into the market. The Director refers to the United States situation where, despite access to subscriber listing information for several years, independents have less than seven percent of total industry revenues.

The only evidence before us is that the issues of importance to the independents, availability, price and opting out, have been dealt with satisfactorily to them. We conclude that, at present, subscriber listing information cannot be considered to be a significant barrier to entry.

(ii) Reputation/Affiliation with Telco

An entrant into directory publishing has the related tasks of convincing users of the value of its directory and of convincing advertisers that it is a worthwhile vehicle in which to advertise. The directory will only be widely used if it has a critical mass of advertising in it. If the directory is not widely used, few businesses will advertise in it and, in the absence of advertising by its competitors in a new directory, there is no pressure on a potential customer to advertise itself in the new directory. This is not a problem that Tele-Direct ever had to face because of its (or Bell Canada's) longstanding presence in the market as the only available directory. In addition, Tele-Direct benefits from its affiliation with a large and established telco which lends a certain authenticity.

To overcome the preference of advertisers for the incumbent directory requires enhanced expenditures on advertising and promotion and lower prices by the entrant. There is numerical evidence on the disadvantage of entrants *vis-à-vis* the incumbent only with respect to lower prices. The Simba/Communications Trends study of the directory industry in the United States revealed that in the top 10 competitive markets, the average telco (utility) rate for a double-half column was 53 percent higher than for independent publishers competing head-to-head in those markets. The average cost of advertising, per thousand of circulation, for the utility directories was 46 percent higher than for the independents.[119]

Mr. Lewis of White stated that his company usually plans on pricing about 40 percent lower than the telco directory in a market they are considering entering. Gary Campbell, the General Manager of DSP, testified that on average their prices were 30 percent less than those of Tele-Direct. A comparison of published prices between Tele-Direct and the initial White and DSP directories confirms these general statements although price differences vary considerably between types of advertisements.[120]

In both markets, the entrants had invested in introducing new features (enhancements) into their directories that Tele-Direct had not hitherto introduced. For example, White's Niagara region directories included the following features not previously offered by Tele-Direct: free smaller size copy in addition to the regular size directory (a "mini"), audiotext, extensive community pages which provide information of regional or local interest,[121] larger size print, three column format instead of four, postal codes included in the white pages, additional colour

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[119] *Ibid.* at 115984.

[120] White's prices in 1994 were generally about 25 percent less than Tele-Direct's for in-column, about 40 percent less for display and about 55 less for red display: exhibit A-103. White first published in Niagara in 1993 with a prototype directory in which advertisers could advertise free of charge. The 1994 prices are for its first "revenue" directory in which advertisers paid for their advertising. Likewise, in Sault Ste. Marie, the DSP rates reflected substantial discounts off Tele-Direct's, with greater discounts for display and coloured display than for other types of advertisements: YPPA Rates and Data Information for the period 1992-95: exhibit A-111.

[121] For example, area sports team schedules, seating diagrams for theatres and arenas, a listing of local golf courses, highway access information, historical sites, schedule of events, maps, senior citizens' services listings, human services' listings, "kid's pages", bus routes, customs and goods and services tax information.

in the advertisements. DSP also included many of the same enhancements in its directories plus other, unique, features.[122] Thus, any advantage enjoyed by Tele-Direct clearly stemmed from its incumbency and its affiliation with Bell Canada and not from the superiority of its product.

Based on White's experience in the United States, it appears that the rate differential between the independent and the telco does narrow over time but still remains significant. Mr. Lewis testified that in Buffalo, New York, where White has published for 27 years, its prices are still 25 to 33 percent less than those of the telco directory.

As part of the survey resulting in the January 1993 Elliott report, customers of Tele-Direct were asked if they would advertise in a competing directory if it offered 15 percent lower prices. Only 36 percent said that they would advertise in the new directory and a mere eight percent that they would discontinue advertising in Tele-Direct's directory.[123] As indicated by the United States data and the experience of White and DSP, to attract a significant number of advertisers the entrant would likely have to offer discounts closer to 50 percent than to 15 percent.

Based on both the particular experiences of White and DSP in entering Tele-Direct's markets and the more general evidence relating to the United States experience, it is our

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[122] For example, it is a "flip" directory with the Canadian cities on one side and the neighbouring American cities on the other. The book also includes a "reverse directory" -- listings by phone number first.

[123] Confidential exhibit CJ-14 (blue vol. 5), tab 73 at 115416-18.

conclusion that an incumbent directory publisher's "reputation" or affiliation with a telco constitutes a significant barrier to entry into publishing a competing broadly-scoped directory. An important part of this barrier is the advantage that the incumbent directory has because it already contains the advertisements of a business's competitors. A new entrant must overcome that fact in seeking to persuade the business to advertise in its new directory. New entrants must offer substantial price discounts, even when they are publishing a product with features not included in the incumbent's directory.

(iii) "Yellow Pages" Trade-mark

The words "Yellow Pages" and "Pages Jaunes" and the "walking fingers" logo are both registered trade-marks of Tele-Direct in Canada. Tele-Direct only licenses those marks to publishers which are affiliated with other telcos. The same words and the logo are in the public domain in the United States.

As attested to by Mr. Lewis, it probably would have been easier for White (and DSP or any other entrant) to explain the nature of the product it was seeking to introduce in the Canadian market if it had been permitted to use the marks, which have a high level of public recognition, as it can and does in the United States. In fact, Mr. Lewis would have paid a "substantial" fee to use the marks in Canada. The trade-mark situation appears to confer some marketing advantage on Tele-Direct and reinforces the other barriers already discussed.

(iv) Strategic Behaviour

Under this heading, the Director first refers to the anti-competitive acts being alleged in a later portion of the argument regarding other publishers. Paragraph 120 states that

> . . . It was Tele-Direct's objective to "make competition expensive" and "raising the bar" to entry and it succeeded.

The only way in which we could determine if the strategic behaviour referred to constitutes an entry barrier would be to assess the effects of that behaviour on the market. The Director did not deal with evidence of effects in relation to the issue of market power. The alleged anti-competitive acts regarding publishers will, of course, be dealt with in due course.

The Director also argues that the alleged anti-competitive acts in respect of services are relevant to entry conditions into publishing. It is submitted that one of Tele-Direct's objectives was to reduce the power of the specialized agencies in order to make it harder for new entrants into publishing to gain market share. If it had been proven that some Tele-Direct policy or initiative against agents did indeed have a deleterious effect on new publishing entrants, this would be relevant to our assessment of entry barriers. We are of the view, however, that the limited evidence provided on this point does not prove that there were such effects.

(3) Conclusion

We are of the view that even with subscriber listings available to independent publishers on reasonable terms, significant entry barriers in the form of the reputation effects and sunk costs reviewed above will remain. The condition of easy entry required to overcome the presumption of market power arising from Tele-Direct's extremely large market share is not satisfied.

B. DIRECT APPROACH: OTHER EVIDENCE OF MARKET POWER

As other evidence of market power the Director relies on the high profits earned by Tele-Direct, its lack of responsiveness to customer needs, and an allegation that it has lagged behind other media in supporting agents, in promoting the product and in using technology to process advertisements received from agents. We are of the view that there is insufficient evidence on the record, and that the question was not explored in sufficient depth, for us to draw a conclusion one way or the other regarding the allegation of lagging behind other media. The evidence regarding profitability and customer dissatisfaction, however, is extensive.

(1) Profits

The respondents acknowledge at paragraph 41 of their response that Tele-Direct earns very large accounting profits. It is also undisputed that Tele-Direct pays 40 percent of its collected revenues directly to Bell Canada and a similar percentage to the other telcos with which it contracts to publish a directory. This payment is said to be in return for access to subscriber lists and for services. The evidence revealed that the only service provided by the telcos is billing.

Where the respondents and their expert, Professor Willig, differ from the Director is with respect to the significance of Tele-Direct's admitted profitability as an indicator of market power. The respondents' argument first points out the well-known concerns about trying to convert accounting to economic profit. While we recognize the validity of those concerns in general, we do not consider that they apply with much force to the most compelling evidence of profitability, the payment by Tele-Direct to Bell Canada. That payment is a set percentage of collected revenues. It is not an accounting "profit" figure or a "bottom line" amount produced by the application of accounting conventions. Therefore, we are of the view that an examination of the payment to Bell Canada and its possible implications for market power is not clouded by accounting conventions at the outset. The presence of such a payment indicates that Tele-Direct has revenues of at least 40 percent over its recorded costs.

Professor Willig took the position that the profits which allow Tele-Direct to make the payment to Bell Canada reflect a return on intangible capital which is a necessary investment in the creation of the profits. In his rebuttal affidavit he stated:

> 46. . . . It is well known that there are many reasons why accounting measures of profits can deviate both randomly and systematically from being an indicator of the theoretical notion of economic profits. One reason for systematic deviation is of general significance in businesses where intangible assets are important. Here, the value of the intangible assets does not appear on the accounting books. Then, when operating margins are expressed as a percent of

> the book value of assets, the resulting percent is systematically too large, relative to economic meaning, simply because the book's list of assets misses the intangible ones. This effect is likely to be of specially great quantitative significance where trade-marks, brand-names, product or service reputation, proprietary technology, and organizational capital are important to the business.
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> 47. Of course, service industries typically contain leading instances of businesses where intangible assets are important. For example, the business of any successful magazine is unlikely to rest on significant tangible assets, and instead to depend on intangible assets that include the name and design of the magazine, and perhaps the organizational capital embedded in the editorial and advertising sales teams. The rate of return on tangible assets earned by such a business will turn sensitively on whether the books include ownership of the business office and a fleet of trucks or autos, or whether the business leases such properties. In either event, the assets that really drive the success of the business will not be valued on the books, and so the rate of return on assets will indicate nothing about the economic profitability of the enterprise, and certainly nothing about market power.
>
> 48. It goes without saying that the directory publishing business is a prime example of the effects just discussed. For all the conventional reasons alluded to, the rate of return on assets, or other accounting measures of profits, are not reliable indicators of market power. . . .[124]

In other words, Tele-Direct is only earning the requisite return on its intangible assets to remain in business and not any kind of economic rents. Professor Willig returned in his oral testimony to the example of a magazine and its intangible assets which create a loyal readership. We have some difficulty seeing the same effect at work with a directory which has no editorial content, unlike a magazine. There may be creativity in the way the directory is assembled so it is of maximum utility to consumers but the evidence was that Tele-Direct lagged behind new entrants like White and DSP in this respect.

When asked specifically about the intangible assets or activities of Tele-Direct, Professor Willig responded:

[124] Expert rebuttal affidavit of R. Willig (30 August 1995): exhibit R-181 at 13, paras. 46-48.

> Evidently . . . there is some value to having, and having had, the "utility" franchise in a given area. If one tries to translate that into what it means today or next year, the operative word really is "reputation", and the reputation is of significance both to advertisers and also to consumers who have to decide whether to pick the book up or not and, if so, which book to pick up. Somehow that reputation attaches to that book because of its heritage, its history, evidently, and also to its identification with the current telco.

. . .

I agree . . . that it is hard to reach out and grab that reputation. But if we think about the character of the directory business . . . the notion that, if you are an advertiser and you are being asked to pay for an ad in advance of the completion of the book and in advance of evidence about what consumers are going to do in terms of using it, then you have to reach, as an advertiser, an expectation, an anticipation of how good the book is going to be.

You have to form an image in your mind before you commit yourself to your advertising expenditure: Is everybody going to use this and will the other advertisers take ads in it? If they don't, then consumers won't use the book and, if consumers don't use the book, then my ad which I am being asked to pay for today won't have its exposure.

The key to the underlying value proposition of the advertiser is the anticipation that 18 months later or 12 months later the book is going to be out and it is going to be a really good book and people are really going to use it.

It is unusual that you can't really tell the value of what it is you are buying until it is done and many months have passed. . . .[125]

There are several difficulties with this hypothesis. First, on a factual level, there is evidence that Tele-Direct's advertisers (except the small group using agencies) do not pay for their advertising 12 to 18 months in advance. Monthly billing commences once the directory is published. Advertisers pay in instalments (interest free) after publication.

Second, Professor Willig emphasized that the key to the value of Tele-Direct's reputation asset was the anticipation that advertisers have that the directory is going to come out and will be a "good" directory that people are actually going to use. Surely all local media, which the respondents postulate are close substitutes for telephone directory advertising, face the same challenge in selling time or space to advertisers. Rather than paying Tele-Direct at a level that

[125] Transcript at 56:11663, 11667-68 (23 January 1996).

allows Tele-Direct to earn a 40 percent premium, would not advertisers simply switch to one of the other alleged close substitutes? Tele-Direct's premium would soon disappear in that scenario.

If, on the other hand, telephone directory advertising is somehow unique because of the close link between a critical mass of advertising in the directory and use of the directory by consumers, then this uniqueness argues against other media being close enough substitutes to provide competitive discipline. Tele-Direct's ability to exploit its association with the telco to earn returns well above its costs would then indicate market power in the market for telephone directory advertising. This latter scenario is more in accordance with the other evidence on the record which reveals that as between the telco directory and other *directory* publishers, the fact of association makes a significant difference. As was already discussed above, one cannot attribute the premium to Tele-Direct having a "superior product" to other telephone directory publishers in terms of the features of the directory. If it had a superior product, Tele-Direct would not concern itself with competing directories, which it does, and the only evidence before us was that the entrants like White and DSP were initially the superior product, until Tele-Direct responded to their enhancements.

Further, Professor Willig's theory of profits as a return on intangible assets cannot co-exist with the respondents' pleading that Tele-Direct's profits go to cross-subsidize Bell Canada's local telephone service as set out in their second amended response:

> 20. . . . What was initially conceived as an essential but costly feature of telephone service has become a lucrative revenue source for the telcos. . . .

> 21. In Ontario, for example, T-D Pubs pays each of the independent telcos with which it contracts 43% of the gross revenue collected from subscribers of the telco who advertise in the telephone directories. In the case of T-D Pubs, this revenue source, as well as the entire net income of T-D Pubs, are included by the CRTC in Bell Canada's revenues to reduce the cost of local service. Each residential telco subscriber in Ontario and Quebec receives a subsidy of over $2 per month as a result of the revenues captured through telephone directory advertising.

Bernard Courtois, Vice-president, Law and Regulatory Matters for Bell Canada, explained:

> . . . So, both the commission revenues from Tele-Direct [the 40 percent] and all the net income of Tele-Direct, that is equivalent to adding $284 million to the revenues of Bell Canada in 1994 for regulatory purposes. Divide that by the number of residential subscribers and it amounts to $3.38 per month on the average residence telephone bill.
>
> I should say that the average residence basic telephone bill in Bell Canada with Touchtone is about $12.75. So, if you didn't have the Tele-Direct activities going on, that bill would have to be more than $16.00. Of course, if Tele-Direct were a completely arm's length company, we would still get some of that commission revenue.
>
> . . .
>
> Q. I think you did point out that in any telco basically they always collect some of this profit through the 40 percent. I mean every telco seems to collect that so they all get subsidized in that way by publishers. Is that what you were saying?
>
> A. That's correct, and I should point out that it's a very large part. I guess the commission revenues might be two-thirds and the net income one-third of that subsidy. . . .[126]

George Anderson, who was previously with NYNEX, described a similar situation in the United States. He testified that the utility directory publisher has to "impute" a substantial portion of its income, over and above the cost for subscriber listing information which has been widely available for some time in that country, back to the telco to help defer the cost of telephone service. In his words:

[126] Transcript at 32:6559-61 (3 November 1995).

> The [AT & T] consent decrees . . . took an unregulated business, which was Yellow Pages, and at the ninety-ninth hour put it in with the regulated segment of the business to serve as a cash cow, not my words, to serve as a funding business that would help defray, defer, hold down the rate of return and hold down the cost of telephone service.[127]

James Logan, currently President of YPPA and formerly with US West, confirmed this view.

We observe that if all Tele-Direct and other telco directory publishers were earning was a competitive return on all assets, including intangibles, the telcos would not have "profits" available to use for a completely different purpose, namely cross-subsidization of local telephone service. Unless intangibles are to be treated as a *deus ex machina* to explain away high economic profits, they must be identifiable, as must be the activities resulting in their creation. Otherwise, simply asserting "intangibles" would always preclude high profits from demonstrating market power. We cannot accept an approach leading to such a conclusion. Intangibles that can account for *apparent* high economic profit are the result of activities that are extraordinarily successful, such as those creating new products or ways of doing things better than others. In contrast to the example of successful magazines cited by Professor Willig, there is no evidence of this in the case of Tele-Direct or the other Yellow Pages publishers. Moreover, the fact that there is such widespread subsidization of telephone services by Yellow Pages publishers associated with telcos strongly suggests that the source of the subsidies is not any outstanding effort on the part of individual publishers.

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[127] Transcript at 41:8556-57 (17 November 1995).

The Director also argues that the fact that new entrants view the market as potentially profitable, even given the large price discounts off Tele-Direct's prices that they must offer and the other expenses they must incur to establish their own credibility or reputation, is an objective measure of Tele-Direct's profitability. We agree that market participants are responding to economic profit rather than to accounting profit.

We conclude, therefore, that the payment to the telcos by Tele-Direct is a form of "economic rent" whose value depends on the surplus that can be earned from publishing a directory associated with a telco. The cost to the telcos of providing the subscriber listings and doing the billing is minimal. The listings are a by-product of supplying telephone service and the billing for advertising is incorporated into the subscriber's monthly telephone bill. While it is true that it would be more costly for Tele-Direct to do the billing itself, it is unlikely that it would cost, at most, more than a few percent of revenue.[128]

In the face of competition from other media the amount that Tele-Direct could afford to pay, and that the telcos could demand, would be considerably less. With sufficient competition the payments to the telcos would disappear entirely. Even if Tele-Direct earns no economic profit on its operations beyond what it pays out to Bell Canada, its price to average cost margin is extraordinarily high. While no benchmark was placed in evidence, merger guidelines, both in the United States and Canada, place products in separate markets if their existence would not

[128] All the work relating to contract verification and dealing with complaints is already done by Tele-Direct. What is performed by Bell Canada are simply the mechanical steps of bill preparation and mailing.

prevent a hypothetical monopolist, post-merger, from increasing prices by five percent. Even allowing as much as two percent for mailing costs, one is left with a margin of 38 percent. We are of the view that the evidence of economic rents provides a direct indication of Tele-Direct's market power.

(2) Dissatisfied Customers

The Director submits that the respondents' actions towards the advertisers, their customers, display market power. Reference is made to Tele-Direct's requirement that advertisers give up copyright in their advertisement, its restrictions on group advertising and evidence of low customer satisfaction in general. There is evidence, in the form of studies like the Elliott reports and the presence of consultants, that a significant percentage of Tele-Direct customers are less than happy with the service provided by Tele-Direct. We reviewed the evidence to this effect in the section on Market Definition when dealing with the arguments of the respondents which emphasized the low degree of customer satisfaction. As a direct indicator of market power, however, we are reluctant to rely on customer dissatisfaction because of the practical difficulties in applying such a subjective test.

(3) Other: Pricing Policies

In addition to the evidence of profitability advanced by the Director, the Tribunal is of the view that Tele-Direct's approach to setting prices supports the conclusion that Tele-Direct is behaving more like a firm with a comfortable margin of market power than a firm facing close substitutes. We note Professor Willig's point that evidence of price discrimination, in isolation, would not reliably indicate market power. In combination with the other evidence it is, however, compelling. Two aspects of Tele-Direct's price-setting policy are important: the premiums charged for colour and larger size (price discrimination) and the effort to equalize price per thousand across geographic markets (circulation alignment).

(a) Price Discrimination

As we reviewed in the section on market definition, colour and increased size are more valuable to advertisers who rely more heavily on the Yellow Pages. In broad terms, these are advertisers whose business involves infrequently purchased or emergency services (e.g., plumber, exterminator, mover, auto repairs, lawyer), infrequently purchased, expensive durables where comparison shopping is likely (e.g., cars, major appliances), services used by travellers (e.g., car rental) or which encourage orders by telephone (e.g., pizza, lumber yard with telephone order business). They need to attract attention in the Yellow Pages so that a consumer is drawn to their Yellow Pages advertisement as opposed to the Yellow Pages advertisement of their competitor. In our view, Tele-Direct systematically price discriminates against advertisers who are heavily reliant on the Yellow Pages through its pricing of colour and size and its ability to do so is direct evidence of market power.

Tele-Direct charges a 50 percent premium to add red to an advertisement. This premium is unrelated to costs of production. The representative of one of the independent publishers testified that at a 50 percent premium, a publisher would be realizing a very high profit margin. In other words, the additional printing and production costs are well below the price charged.

Ms. McIlroy explained that the object of Tele-Direct's pricing of colour at a premium is to control its penetration to ensure that it will be sufficiently uncommon so that the coloured advertisements "stand out" on the page. The price is set high enough that everyone will not buy it. In the same vein, Tele-Direct introduced multi-colour in those markets where there was already a lot of red in the directories as an alternative way of allowing advertisers to "stand out". This is not the kind of pricing policy that can be pursued by a firm under competitive pressure because its competitors would simply charge a lower price to take advantage of the profit opportunity and compete away the premium.

Further, the premium for red is largely invariant across local markets. It is difficult to see how there could be such uniform pricing in the face of "competition" from other local media, which would vary from market to market. Tele-Direct's pricing of red can hardly be seen as a response to these prices but is much more consistent with a company concerned only about its own, unique environment.

Based on the evidence before us, there is similar uniformity and lack of relationship to cost in Tele-Direct's pricing of larger advertisements. A comprehensive Tele-Direct rate card was not placed in evidence. In the 33 local markets included on the excerpt from the YPPA rates that was tendered as an exhibit, the price increases by about 90 percent for each doubling of advertisement size from a quarter column (1/16 page) to a double quarter column (1/8 page) and from a double quarter column to a double half column (1/4 page).[129] As in the case of colour, the evidence revealed that the additional costs of producing larger advertisements do not appear to justify the increase in price. Based on cost, one would expect a discount greater than ten percent for an advertisement twice as large.

The respondents do not dispute that Tele-Direct's premiums for red and for size cannot be explained by additional costs. Counsel conceded in argument that those were the facts but argued that Tele-Direct was engaging in "value pricing". He hypothesized that an advertiser buying a larger advertisement might get ten times the results that would have been obtained with a smaller advertisement and, therefore, paying almost twice as much for the larger advertisement is actually a bargain. The larger advertiser, the argument goes, is getting more value out of the medium. Value pricing is not a phenomenon readily associated with a competitive market, the hallmark of which is pricing which is ultimately cost-driven.[130] Value pricing is more likely to be associated with a regulated monopolist and is more an indication of the presence of market power than of its absence.

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[129] YPPA Rates and Data Information for the period 1992-95: exhibit A-111 at 9.

[130] Leaving aside dynamic, innovation-driven industries, to which telephone directories do not belong.

The ability of Tele-Direct to discriminate against customers who spend *more* on advertising by way of larger or coloured advertisements is of particular importance in assessing whether Tele-Direct lacks market power *because* other local media provide close substitutes for Yellow Pages, as argued by the respondents. Larger Yellow Pages advertisers have greater choice among the allegedly competitive media since, by definition, they have more dollars in Yellow Pages that they can switch to any other media. Smaller advertisers are less likely to be able to afford the full range of other media. While it may be true, as Professor Willig pointed out, that certain vehicles, such as community newspapers or church calendars might be more acceptable to smaller advertisers, there is no denying that, from a budget point of view, larger advertisers have more options. Thus, larger Yellow Pages advertisers should have the more elastic demand if there are, as the respondents argue, close substitutes to Yellow Pages. The fact that Tele-Direct's margin over cost increases with enhanced expenditures on colour and size indicates the opposite. The anomaly of Tele-Direct being able to price discriminate against advertisers who at first blush have the greatest range of options underscores its market power.

The two broadly-scoped independent publishers, White and DSP, also charge some premiums for colour or size, although neither charges a premium as high or as consistent across the board as Tele-Direct's.[131] Certainly, no one has suggested that either White or DSP has market power. Yet, Mr. Campbell provided the same explanation of DSP's pricing of red, for

[131] In Sault Ste. Marie, DSP charges a premium for red ranging from 36 to 50 percent for full page, half page, double half column (1/4 page), double quarter column (1/8 page) and quarter column (1/16 page). For each doubling in size, however, DSP price increases are 56 percent to 76 percent, considerably lower than Tele-Direct's size premium. In Niagara Falls, White charges only between eight and nine percent premium for red, with one exception, a quarter column advertisement, which reflects a 28 percent increase. For each doubling in size, White charges from 74 to 91 percent more.

example, as Ms. McIlroy did -- that it is priced above incremental costs to ensure its scarcity. Does the independents' use of some premiums for colour or size imply that Tele-Direct has no market power? We think not. The presence of two publishers in Sault Ste. Marie and Niagara certainly does not indicate a "competitive" market.

The evidence regarding the independent publishers does not detract from our view that Tele-Direct's ability to price discriminate is evidence of market power. Although the independents can, to a much more limited extent, implement some of the same pricing policies, this is not surprising. Tele-Direct prices in each local market create an "umbrella" beneath which the new entrants can shelter which underlines that Tele-Direct has market power sufficient to create the umbrella.

(b) Circulation Alignment

Since 1987 (or for 1989 prices onwards), Tele-Direct has actively pursued a policy of "circulation alignment" in calculating its annual price increases. The only exception was in 1992 (for 1994 prices) when poor economic conditions resulted in a zero price increase across the board. The objective of this policy was to bring about consistency in cost per thousand or CPM between directories. Some directories had experienced rapid growth in circulation but since they were subject to the same general price increases as other directories which had not grown as much in circulation, their CPM or price relative to circulation was substantially lower. Ms. McIlroy referred to the Mississauga directory as one in which the rates were seen as too low given the circulation of the directory. A program was therefore instituted to bring the CPMs in all markets into line over a number of years by imposing additional price increases (but not price decreases) in particular local markets.

In applying the alignment policy absolutely no allowance was made, or is made, for differentials in the intensity of competition from other media in each local market. The entire process can be described as a very bureaucratic one and certainly not what one would expect if Tele-Direct was forced to respond to varying degrees of competitive pressure in the numerous (approximately 100) local markets where it operates.

Professor Willig conceded that this "bureaucratic" approach to pricing and apparent indifference to local market conditions was puzzling but theorized that it could result from Tele-Direct's connection to a utility company. Utilities come from a culture of regulation where pricing flexibility is frowned upon. Further, if individual sales people were given latitude to discount to individual customers, the result for a large organization like Tele-Direct would be chaos.

Pricing individually by customer goes well beyond responding to the supposedly competitive media in a local market and thus does not directly address the point. The regulatory "culture" of utilities, is, of course, undeniable. What is more pertinent is how Tele-Direct could maintain such a culture in the form of its approach to pricing in the presence of the alleged close substitutes. If its bureaucratic price-setting led Tele-Direct to set a price too high in a particular market, surely it would see a dramatic revenue loss to other media and would quickly change its approach. There is no evidence that this has happened.

(4) Conclusion

The other direct evidence of market power advanced by the Director along with Tele-Direct's pricing policies affirm our previous conclusion based on the indirect approach that Tele-Direct has market power in telephone directory advertising.

VIII. TIED SELLING

A. INTRODUCTION

Tying or "tied selling" is dealt with in section 77 of the *Competition Act*. The relevant parts of section 77 are:

> (1) . . . "tied selling" means
> (*a*) any practice whereby a supplier of a product, as a condition of supplying the product (the "tying" product) to a customer, requires that customer to
> (i) acquire any other product from the supplier or the supplier's nominee, or
> (ii) refrain from using or distributing, in conjunction with the tying product, another product that is not of a brand or manufacture designated by the supplier or the nominee, and
> (*b*) any practice whereby a supplier of a product induces a customer to meet a condition set out in subparagraph (*a*)(i) or (ii) by offering to supply the tying product to the customer on more favourable terms or conditions if the customer agrees to meet the condition set out in either of those subparagraphs.

> (2) Where, on application by the Director, the Tribunal finds that . . . tied selling, because it is engaged in by a major supplier of a product in a market or because it is widespread in a market, is likely to
> (*a*) impede entry into or expansion of a firm in the market,
> (*b*) impede introduction of a product into or expansion of sales of a product in the market, or
> (*c*) have any other exclusionary effect in the market,
> with the result that competition is or is likely to be lessened substantially, the Tribunal may make an order directed to all or any of the suppliers against whom an order is sought prohibiting them from continuing to engage in . . . tied selling and containing any other requirement that, in its opinion, is necessary to overcome the effects thereof in the market or to restore or stimulate competition in the market.

A tie is the supply of one product *on the condition that* the buyer takes a second product as well *or* on terms that *induce* the buyer to take the second product as well. Such an arrangement may be prohibited by the Tribunal under section 77 if it meets all the other requirements of that section, namely that the tying is a practice engaged in by a major supplier and results in a substantial lessening of competition. The requirement that Tele-Direct must be a major supplier is satisfied by our earlier finding of market power in the telephone directory advertising market. The other requirements of the section are still to be resolved.

The Director alleges that the respondents have engaged in a practice of requiring or inducing customers for advertising space in telephone directories (the tying product) to acquire another product, telephone directory advertising services (the tied product), from the respondents. The Director further alleges that the practice of tied selling has impeded entry into or expansion of firms in the market resulting in a substantial lessening of competition.

The advertising space or publishing business is described at paragraph 9 of the application as including:

> . . . all matters relevant to the provision of advertising space in a directory, including access to a subscriber data base (including information relating to new subscribers) upon which the books are based, compilation, physical creation of hard copy, printing, promotion and distribution.

The advertising services business refers to:

> . . . the provision of services relating to the sale of advertising space in a telephone directory, including establishing new customers, calling on customers, and providing advice, information and other services relating to the design, cost, content, location, creation and placing of the advertisements.

The Director further states that the purchaser of an advertisement in a telephone directory obtains two products related to the two businesses: advertising space and advertising services.

B. FACTS

Before we proceed further, it is necessary to review some facts relevant to the supply of advertising services to Yellow Pages advertisers.

(1) Tele-Direct's Internal Sales Force

Tele-Direct sells telephone directory advertising through its internal sales force. This group is sub-divided into those representatives who deal with customers over the telephone ("tel-sell") and those who attend at the customers' places of business ("premise"), together called the general sales force or "GSF". The premise sales representatives travel from place to place during the year to canvass advertisers for a particular area or directory within a confined time frame. In

1994, premise sales accounted for about 60 percent of the revenues generated by Tele-Direct's internal sales force, while tel-sell generated less than 30 percent of revenues.

A further category of sales representatives, sometimes included as part of the GSF and sometimes considered apart from it by Tele-Direct, is that which services so-called "national accounts". These representatives are called national account managers ("NAMs") or national account representatives ("NARs"). This group accounts for the remaining approximately 10 percent of revenues.

There are no hard and fast rules governing which accounts are handled by the NAM/NAR group as opposed to the remainder of the GSF. Some large accounts are serviced by the GSF. The Tele-Direct witnesses indicated that, in general, accounts that require a great deal of servicing, for example, multiple visits over a year, are likely to be assigned to the NAM/NAR unit. Because of the canvass-based sales approach used by the GSF, often the GSF is involved in a canvass in another area and is unavailable to service a particular account repeatedly. The NAMs and NARs are located in certain centres all year long and can service these accounts more easily. A further factor is the account's complexity, including number of headings, the number of markets, and the amount of change required each year. If the account requires a lot of attention to ensure accuracy (for example, that no directories are missed) and perhaps clerical-type support, it will end up in the national group. There was also evidence that accounts which had little future growth potential or which had simply proven to be problem accounts in the past are handled by the NAM/NAR unit.

Tele-Direct (Publications) Inc. is divided into two geographic regions, eastern and western. The eastern region is comprised of the province of Quebec, with parts of Ontario such as Ottawa, Kingston, Sault Ste. Marie and Sudbury. The western region covers the remainder of Ontario. The structure and organization of the company in both regions is broadly similar, although the eastern region is smaller both in terms of revenue serviced and number of sales representatives.

The facts regarding (a) remuneration, (b) evaluation and (c) account assignment and continuity for Tele-Direct's internal sales force are relevant because one of the Director's arguments regarding Tele-Direct's motivation to engage in the alleged tied selling is that its internal sales force can be more effectively motivated to sell more Yellow Pages advertising than agents.

(a) Remuneration

The remuneration of the Tele-Direct representatives is highly dependent on the revenues generated by each individual as they are paid through a combination of salary and commission. Both the tel-sell and premise representatives earn a base salary (which is higher for premise) and in addition are eligible for a number of commissions and incentives.

The amount of commission paid to a sales representative is determined by the nature of the advertising which is sold. If the sales representative manages to generate new business (an increase over the previous year's advertising expenditure), an annual commission of 13 percent is paid on the total new business. If the advertiser is renewing the advertising which was purchased in the previous year, the sales representative is paid a 2.4 percent commission on the renewal amount. Renewal commission is paid on any portion of an account which is renewed, even if the total amount of advertising purchased is less than the previous year. The renewal commission was first introduced in the early 1980s, prior to which the representatives were paid only salary and new business commission. The final basis upon which a commission is paid to a sales representative reflects rate increases. This applies in a situation where an advertiser renews exactly the same advertising program as it had in the previous year but there has been a rate increase which is applicable to that advertising program. The sales representative receives renewal commission on the amount spent the previous year and rate increase commission on the difference between the two account totals because of the rate increase. The rate increase commission is six percent.

Since 1993, a premise representative also has the potential of earning a yearly bonus in the amount of $2,000. The bonus is based on factors such as the number of complaints made against the representative by advertisers, the representative's score in Tele-Direct's internal evaluation, the number of "lates" (advertising submitted after a directory closing date) and mistakes and the representative's overall work flow. Apart from the bonus, there are a number of other incentives offered to premise sales representatives, for example, awards and trips.

The NAM/NAR group also earn base salary plus commission but with a much larger proportion of their income accounted for by salary. Their new business commission is nine percent, with a renewal commission of 0.5 percent and a rate increase commission of 1.2 percent. They may qualify for a bonus equal to seven percent of their income for maximizing net sales or a bonus of three percent for maximizing retained revenue. An average NAM earns less than an average premise representative.

Sales representatives are supervised by salaried sales managers. Sales managers also qualify for various incentives and bonuses, which may vary in nature from year to year, based on the results of the sales representatives that they supervise.

(b) Evaluation

In the western region Tele-Direct has a formal assessment program for its sales representatives called Total Performance Assessment ("TPA"). Each representative is assessed using the TPA every six months.

The TPA is comprised of three categories: sales results (worth 60 percent), customer satisfaction (worth 20 percent) and job administration (worth 20 percent). The sales results score is largely based on the representative's incremental revenues in relation to other representatives (25 points of 60). Customer satisfaction is broken down into customer disputes and an overall customer survey. Customer disputes refer to the number of times customers of the representative have called in with a complaint or a concern. The customer survey component is a Gallup survey.[132] The final aspect is job administration which includes work flow (success in meeting benchmark requirements for servicing a certain percentage of revenue during a canvass by a certain date), number of internal queries and lates.

The TPA is not used in the eastern region which has not had a formal evaluation program since 1994 because of union disputes. Currently, sales representatives in the eastern region are evaluated by an internal management review in which their supervisors conduct follow-up interviews with clients. It is Tele-Direct's intention to replace this less formal evaluation process in the future.

(c) Account Assignment and Continuity

Tele-Direct uses a canvass approach to sell advertising. Each directory has a canvass period, the length of which depends on the size of the directory, during which the GSF focuses its attention on selling advertising for the next issue of that directory. The GSF is under time constraints to complete its sales and solicitations prior to the deadline, or the closing date, for the directory. Once one canvass is complete, the GSF moves on to the next one.

[132] Each year 25 customers of each sales representatives are asked questions relating to the quality of the service provided by the representative.

For each canvass, Tele-Direct canvass coordinators assign accounts to the sales representatives to ensure as much as possible that each salesperson ends up with a bundle of accounts which is balanced in revenue and in growth potential. Accounts are assigned based on a complex system of "markets" and "grades". For example, "Market 1" accounts are dealt with by premise representatives while "Market 2" accounts are dealt with by tel-sell. As well as being divided by market, accounts are also graded; the lower the grade assigned to an account the higher the potential that type of business will buy Yellow Pages. Grades are based on the type of business as represented by the heading under which it would appear in the directory.

For each canvass the grades and markets for the accounts are analyzed to determine whether, based on factors like time, the size of the cities or towns included and the number of sales representatives available, the premise representatives will cover all of the grades in Market 1, or whether, perhaps, some of the higher grades in that market should be assigned to tel-sell. For the same reasons, for a given canvass, not all accounts are assigned; those with lower potential or that are inactive may be dropped.

For both the premise and the tel-sell group, account assignment has traditionally been random. With a few minor exceptions, accounts were divided up at the beginning of each canvass with no intention of returning individual accounts to the same representative who serviced them in the previous year. In 1993, a test was conducted in a northern market whereby there was 100 percent continuity of tel-sell accounts. Ms. McIlroy's impression of the results was that they were positive in general; however, we have no information about whether tel-sell continuity has been adopted more generally. For premise sales, Tele-Direct adopted the Very Important Advertiser ("VIA") program in the late 1980s which provided a form of continuity: advertisers spending a certain amount per month were assigned the same representative every year. By 1992-93, there was a more general continuity policy in place whereby 30 percent of all premise accounts were assigned back to the sales representative for three years if $500 or more was being spent or a pricing incentive was involved. Currently, about 55 percent of the accounts of a typical premise representative (about 85 percent of revenue) are subject to continuity.

(2) Tele-Direct's Commissionability Rules

Prior to 1958, a 15 percent commission was available on "national" advertising. The definition of "national" was, however, unclear. In 1958, Bell Canada adopted a new policy, developed in consultation with and endorsed by the Canadian Association of Advertising Agencies. To be commissionable at 15 percent, the advertising had to appear in two or more directories serving two or more "calling areas" with no more than 80 percent of the total advertising in one directory. No particular association membership was required of the agency; if the agency's ability to pay was in doubt, its credit was investigated.

Tele-Direct's definition of a commissionable account underwent a further change effective January 1, 1976. The amended definition of commissionability became known as the "eight-market rule". To qualify as a commissionable account under this rule, the advertiser had to purchase advertising with a minimum value of a trade-mark in eight "markets", as defined by

Tele-Direct. Canada was divided into 19 markets, with six in Quebec and seven in Ontario. The entire United States constituted a single 20th market. If the account qualified and the agency provided completed artwork, Tele-Direct would pay a 15 percent commission on the account. Again, no particular membership in an industry association was required.

The commissionability rule was next changed effective July 1, 1993 to create the so-called "national definition" which is the current rule. Under this rule, to be commissionable an account must advertise, at a minimum, in directories in two provinces. Advertising must be placed in at least 20 directories and in each directory the value of the advertising must be a minimum of a trade-mark. Finally, 20 percent of the total value of the advertising must be placed in directories outside Tele-Direct's territory.

In order to receive 25 percent commission on "national accounts" the agency has to be a CMR and a member of YPPA. In addition, to be eligible for the 25 percent commission, the CMR must transmit its order to Tele-Direct via the Value-Added Network ("VAN") run by the YPPA. This facility provides for electronic transmission of account data and other information to a publisher. In order to access VAN, the CMR must be a member of the YPPA and must acquire the necessary computer hardware and software.

All accounts which met the eight-market rule as of July 1993 have been "grandfathered"; Tele-Direct still pays 15 percent commission on those accounts. Once an account ceases to qualify under the eight-market rule, it cannot be re-qualified. New accounts, those which reached eight-market status after July 1993, cannot be "grandfathered". Tele-Direct has made no commitment to how long the "grandfathering" of eight-market accounts will remain in place. It could be discontinued at any time.

C. ALTERNATE THEORIES OF THE CASE

As elaborated in the opening statement, the Director's theory of the case for tying is that the respondents, as a condition of supplying space, have required or induced customers to acquire the tied product, services, from them. We have already reviewed the structure of the market. The respondents offer a commission on accounts meeting their "national" definition and on grandfathered eight-market accounts. They service the remainder of the accounts themselves and do not offer a commission, or price space and services separately, for those "local" accounts, amounting to over 90 percent of Tele-Direct's revenue.

In accordance with his theory, the Director alleges that the respondents by refusing to sell either the space or the services in an unbundled fashion have violated section 77. Counsel for the Director described the Director's case in opening in alternative terms by referring to the respondents' refusal to pay commission except to the limited extent that they now do as a violation of section 77 because commission would be a means of recognizing or effecting an unbundling for the services that non-commissionable customers seek. The Director says that as matters now stand, non-commissionable customers have a choice of either obtaining services from respondents as part of the "package" price that they pay for their advertising or paying twice for the services -- once as part of the package price charged by the respondents and once directly to the service provider.

The respondents say that the Director's concept of tying is misconceived. They submit that there is no product known as "advertising services" separate from a product known as "advertising space". They focus on the *selling* portion of the services referred to by the Director and argue that the sales advice provided by Tele-Direct's internal sales force forms an inseparable package with the space which Tele-Direct supplies in its directories. Indeed, they emphasize, there is no advertising space without a sale. They argue that how advertisements in their directories are sold is a business decision to be made solely by Tele-Direct and is not justiciable. Tele-Direct determines when it is more appropriate to sell its product through its internal sales force and when it will "employ" and pay a commission to agents to sell its product.

In other words, the respondents argue that they have chosen a "hybrid" system. As their primary sales channel, they maintain an internal sales force. They have also chosen to employ agents to sell to a limited group of large advertisers who have distinct needs. Among the reasons given for primary use of the internal sales force were: efficiency, that the average cost of revenues serviced internally was lower than for revenues serviced by outside agents; revenue growth, that the internal sales force is more effective in growing revenue; and servicing, to ensure attention to small advertisers and non-advertisers that Tele-Direct considers important but external agents might not.

The respondents take the position that the Director's application regarding tied selling is an attack on vertical integration. They characterize Tele-Direct's decision regarding commissionability as a choice in some instances to buy services from agents and in others to make the services in-house. They refer to the words of Posner J. in *Jack Walters & Sons Corp. v. Morton Buildings, Inc.* for guidance:

> The end that Walters [a terminated dealer] alleges is that Morton [the manufacturer] wanted to take over the retail function; in the terminology of industrial organization, it wanted to integrate forward. But vertical integration is not an unlawful or even a suspect category under the antitrust laws: "Firms constantly face `make-or-buy' decisions -- that is, decisions whether to purchase a good or service in the market or to produce it internally -- and ordinarily the decision, whichever way it goes, raises no antitrust question." . . . Vertical integration is a universal feature of economic life and it would be absurd to make it a suspect category under the antitrust laws just because it may hurt suppliers of the service that has been brought within the firm.
>
> A common type of vertical integration is for a manufacturer to take over the distribution of his product. . . .
>
> We just said that vertical integration is not an improper objective. But this puts the matter too tepidly; vertical integration usually is procompetitive. If there are cost savings from bringing into the firm a function formerly performed outside it, the firm will be made a more effective competitor.[133] (references omitted)

The respondents urge us to take from the words of Posner J. that their narrowing of the commissionability criteria is simply taking over the distribution function internally and Tele-Direct's decision about how to run its business, which it does not have to "justify" to anyone.

The Director underlines that he is not opposed to vertical integration in principle. He cautions, however, that if the method chosen for the vertical integration violates a section of the

[133] 1984-2 Trade Cas. (CCH) ¶ 66,080 at 66,024-25 (7th Cir. 1984).

Act, with particular reference to sections 75, 77 and 79, then it is subject to challenge and the respondents cannot achieve immunity by "waving the flag of vertical integration". We agree that simply affixing the label of "vertical integration" does not conclusively decide anything. It does not preclude the Director from attempting to convince the Tribunal that what is going on in the case before it meets the requirements of a section of the Act. This view is not inconsistent with the *dicta* of Posner J. in the *Jack Walters* case, who indicates that the presence of market power may cast vertical integration in a different light and points out that market power was not present on the facts before him:

> . . . some economists believe that monopolistic firms might integrate vertically in order to deny supplies or outlets to competitors, or to make it more costly for new firms to enter the market (because they would have to enter at more than one level of production or distribution), or to facilitate price fixing with their competitors. But nothing of this kind is suggested here. Walters does allege that Morton has a big name in the prefabricated farm buildings market, but there is no indication that this is a meaningful economic market that might be worth monopolizing, or that Morton's purpose in integrating into retail distribution was to make life harder for *its* competitors. Its object was to make more money by reducing the cost of retail distribution, not by coercing or excluding (or for that matter colluding with) its own competitors, whoever they may be, or discouraging potential competitors. *Indeed Walters' tie-in claim is premised on the ready availability, from other manufacturers, of the building parts that Morton sells in kits from which Morton Buildings are put together. This shows that Morton has no monopoly*.[134] (emphasis added; references omitted)

The recognition that vertical integration is generally pro-competitive on efficiency grounds raises another issue. The Director says there is no provision in section 77 for an efficiency "defence". We agree that there is no such explicit reference to an efficiency defence. However, many forced "package sales" are the product of efficiency and even a supplier with market power may sell items in combination for efficiency reasons.

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[134] *Ibid*. at 66,025.

A fundamental requirement of tying is the existence of two products, the tied product and the tying product. It is implicit in the determination of whether there are one or two products that efficiency considerations must be taken into account. We consider that demand for separate products and efficiency of bundling are the two "flip sides" of the question of separate products. Assuming demand for separate products, if efficiency is proven to be the reason for bundling, there is one product. If not, there are two products. As we will review below, this approach is consistent with the American jurisprudence regarding the test for separate products relied on by the Director.

The Director is of the view that, assuming that the necessary elements of the section have been met -- major supplier, two products, tying, and the exclusion of competitors resulting in a substantial lessening of competition -- it is not necessary for him to provide a plausible explanation of *why* or *how* the firm benefits from the tie. This is a valid position. The Tribunal would not impose such a requirement on the Director. It cannot be denied, however, that there is always more comfort in drawing conclusions the greater the depth of understanding.

In this case, the Director has in fact provided explanations as to why Tele-Direct might be engaged in tied selling. The Director submits that Tele-Direct is leveraging its market power in the sale of space into the market for advertising services through tying. One explanation of this is that Tele-Direct's policy of bundling advertising space and services allows Tele-Direct to exploit better an alleged information asymmetry it enjoys *vis-à-vis* its customers, the advertisers. As with any advertising medium, it is not possible to evaluate effectiveness of Yellow Pages advertising with any degree of precision. To the extent that data on effectiveness of the medium is available, it is in the control of Tele-Direct not the advertisers. In light of this, the Director argues that Tele-Direct prefers to keep advertising services in-house as much as possible because its representatives can be more effectively motivated to "oversell" than independent service providers. We will deal with this reasoning in due course.

The Director also says that the "usual" assumption of profit maximization used in determining whether a firm stands to gain from a tie does not apply in the instant case and the economic literature on the subject that relies on this assumption to analyze the possible effects of a tie is not a useful source. He says it is futile to seek a "rational" or "profit-maximizing" explanation for Tele-Direct's behaviour since Tele-Direct, because of its unique situation and relationship to Bell Canada, is not subject to the constraints of profit-maximization and its corollary, cost-minimization.

In support of the premise that Tele-Direct is not profit-maximizing, Thomas Wilson,[135] an economist expert witness for the Director, draws on the fact that the profits of Tele-Direct are included for regulatory purposes when decisions are made about Bell Canada's prices. He is of the view that the pressure to minimize costs is reduced and that there may also be systematic distortions such as the use of more capital than an unregulated firm would use in order to boost the capital base of the regulated firm (the "Averch-Johnson effect"). However, this particular

[135] Professor of Economics and Director of the Policy and Economic Analysis Program at the University of Toronto.

hypothesis is not supported by the evidence which, in fact, points in the other direction insofar as Tele-Direct has chosen to subcontract capital intensive operations such as printing.

Professors Wilson and Slade, for the Director, are also of the view that management's decisions with respect to the commissionability of various accounts are motivated by a concern to maximize *sales* rather than to minimize *costs*. Professor Wilson sees the reduced pressure on regulated firms to minimize costs as allowing Tele-Direct's management to pursue personal interests, such as operating a larger enterprise, thereby garnering personal satisfaction and monetary rewards. Professor Slade is of the view that the ownership structure of Tele-Direct, whereby there is no threat of a takeover, contributes to allow management to pursue its hypothesized desire for larger size.

Even though there are several occasions when we have difficulty understanding the decisions of Tele-Direct's management if they really are pursuing cost-minimization, we are far from convinced that Tele-Direct's management is not generally constrained to follow a profit-maximizing course. The fact that Tele-Direct is a wholly-owned subsidiary should be sufficient to ensure that there is adequate ownership control. It is obvious from the evidence of Mr. Courtois, the Bell Canada representative on Tele-Direct's Board of Directors, that Bell does not practice micro-management. The main instrument of control appears to be the requirement that Tele-Direct pay Bell the same percentage of revenues as Tele-Direct is required to pay other telcos when it contracts to perform their directory functions. This requirement was introduced precisely to impose market discipline on Tele-Direct. In addition to the forty percent of revenue that Tele-Direct remits to Bell, it also makes a substantial contribution to Bell's profits in the form of dividends. The evidence does not support the conclusion that Bell has been cavalier about allowing Tele-Direct's management to pursue other than profit-maximizing goals. Moreover, in recent years Bell's earnings have been well below its regulated allowed rate of return, a situation not conducive to permissiveness. Even when Bell earnings were not below the allowed rate of return, higher profits from Tele-Direct would still benefit Bell between applications for rate increases.

While we do not rule out that Tele-Direct's management may be under less than the usual amount of pressure to perform, we are reluctant to discard the usual working assumption of profit-maximization in the absence of some compelling evidence that is consistent with the assumption that Tele-Direct is pursuing other goals. The only specific evidence cited in support of the premise that Tele-Direct's management pushes revenue growth beyond the point of profit-maximization is the stress that they place on canvassing businesses that do not advertise in the Yellow Pages, the non-advertisers. The success rate from this effort is low and Professor Slade concludes that the fact that the effort is made can be explained by management's greater concern with growth of revenue than with profits. On the whole, however, the evidence on the canvass of non-advertisers is that moderate resources are devoted to this task. We are not convinced that the canvass of non-advertisers is not profit-maximizing.

We note here that there is another possible theory of the case. For reasons of clarity and coherence, however, it is more convenient to deal with it at a much later point in these reasons. We return to it below as an "Addendum" to our conclusion regarding the separate products issue.

We therefore do not accept that we should approach this case with a view to treating Tele-Direct as other than a profit-maximizing firm, albeit a firm with market power. Nor do we accept that efficiency considerations are not relevant to our section 77 analysis. Efficiency and demand, together, form the basis of the consideration of one or two products, to which we now proceed.

D. SEPARATE PRODUCTS

(1) Approach to Determining Separate Products or Single Product

The first element of section 77 to be considered is whether advertising space and advertising services are separate products. The Director takes the position that advertising services constitute a distinct product separate from advertising space. The respondents argue that advertising services are in fact an "input" into Yellow Pages advertising, not a separate product.

Merely labelling advertising services and advertising space as either two "products" or as "inputs" into a single product does not assist. As Areeda, Hovenkamp and Elhauge state:

> . . . just about any product could be described as a tie of its components. And just about any two products could be described as mere parts in a more encompassing single product. . . .[136]

There must be some rationale for distinguishing between situations where there are two products involved, and thus at least the possibility of an illegal tie that should be prohibited, and those where there is a single product and no question of tying.

The parties are in agreement that the Canadian jurisprudence does not provide much guidance on the test to be applied. Both parties referred to the 1984 decision of the Supreme Court of the United States in *Jefferson Parish Hospital District No. 2 v. Hyde*[137] for guidance, although they emphasize different portions of the decision.

In *Jefferson Parish* the Court provided its most extensive discussion of the "single product" test. At issue in the case was the validity of an exclusive contract between the hospital and a firm of anaesthesiologists. Any patient who chose to have an operation performed at that hospital was required to use an anaesthesiologist employed by the firm in question (Roux & Associates). The Court had to decide if this constituted an illegal tying arrangement. In making that inquiry, the Court considered two questions, whether the hospital was selling two separate products that might be tied together and, if so, whether the hospital used market power to force its patients to accept the tying arrangement. The majority answered the first question in the affirmative but the second question in the negative (the hospital was found not to have

[136] P.E. Areeda, H. Hovenkamp & E. Elhauge, *Antitrust Law*, vol. 10 (Boston: Little, Brown, 1996) at 175.

[137] 466 U.S. 2.

market power), so in the result it found no illegal tying arrangement. The minority found only one product and concluded for that reason that there was no illegal tying arrangement.[138]

In discussing the question of separate products, the majority noted that the answer to the question of one or two products turns not on the functional relationship between them but rather on the character of the demand for the two items. The majority then stated:

> . . . Thus, in this case no tying arrangement can exist unless there is a sufficient demand for the purchase of anesthesiological services separate from hospital services to identify a distinct product market in which it is efficient to offer anesthesiological services separately from hospital services.[139] (reference omitted)

We adopt this statement of the majority as the applicable test for separate products. We believe that this test effectively captures both the demand and the efficiency elements necessary for us to distinguish between cases when a tie that is injurious to consumer welfare is possible and those in which the tie, although imposed by a major supplier, is efficient and should not be condemned. Demand is, of course, critical. If there is no demand, it would be pointless to require that the two products be offered separately. Efficiency is also critical as the existence of separate demand should not govern if providing the products separately would result in higher costs that would outweigh the benefits to those who want them separately.

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[138] The majority consisted of Stevens, Brennan, White, Marshall and Blackmun JJ. The minority included O'Connor, Powell, Rehnquist JJ. and Burger C.J.

[139] *Supra* note 137 at 21-22.

Our approach will be to examine first the evidence pertaining to the demand side of the equation, to determine whether the Director has proven buyer, in this case advertiser, interest in acquiring space and service separately. By this we mean an answer to the question: "Is there a significant set of advertisers who actually want the items separated?" If this question is answered in the affirmative, then we will turn to the evidence relating to whether it is efficient to separate the products.

The respondents rely on a portion of the minority judgment in *Jefferson Parish*. The minority wrote:

> . . . there is no sound economic reason for treating surgery and anesthesia as separate services. Patients are interested in purchasing anesthesia only in conjunction with hospital services, so the hospital can acquire no *additional* market power by selling the two services together. . . . In these circumstances, anesthesia and surgical services should probably not be characterized as distinct products for tying purposes.[140]

In conclusion, they reiterated:

> . . . Since anesthesia is a service useful to consumers only when purchased in conjunction with hospital services, the arrangement is not properly characterized as a tie between distinct products. It threatens no additional economic harm to consumers beyond that already made possible by any market power that the hospital may possess. *The fact that anesthesia is used only together with other hospital services is sufficient, standing alone, to insulate from attack the hospital's decision to tie the two types of services.*[141] (emphasis added)

[140] *Ibid*. at 43.

[141] *Ibid*. at 46.

The respondents did not provide us with any reason to adopt the minority judgment over the majority. In fact, the majority opinion explicitly rejected tests based on functional relationships, including the "useless without" test. In a footnote the majority noted:

> The fact that anesthesiological services are functionally linked to the other services provided by the hospital is not in itself sufficient to remove the Roux contract from the realm of tying arrangements. We have often found arrangements involving functionally linked products at least one of which is useless without the other to be prohibited tying devices. . . .[142]

There are also sound economic reasons to reject such a test. As pointed out in the Areeda text, it may perversely save the most dangerous ties and call for review when there is little likelihood of adverse effects. The authors of that text use the example of a manufacturer with a monopoly over can-closing machinery who requires all purchasers of the machinery to buy cans from it to point out that:

> . . . [s]uch a tie would bring the [manufacturer] a complete monopoly over cans, for presumably no one would buy empty cans without the machinery to close them. Yet the useless-without test would immunize this tying arrangement. Moreover, while short-run profit maximization is *generally* not enhanced when the tied product has no other use, monopoly in the tied market can impair competition severely in the long-run. . . .[143]

(2) Other Case Law

The respondents have also advanced a plethora of other American cases with respect to the question of separate products. In general, the respondents rely on these cases to urge us to view the facts before us solely from the supplier's (Tele-Direct's) perspective and to ignore

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[142] *Ibid*. at 19 n. 30.

[143] *Supra* note 136 at 269.

demand considerations. Their fundamental premise appears to be that Tele-Direct's choice to "market" its product in a certain fashion is determinative and negates the possibility of any tying claim. We did not accept the Director's argument that considerations of demand govern; likewise we reject the respondents' argument that a supplier's choice is paramount. Both elements of demand and efficiency will be taken into account, as set out above. In any event, it is clear that the case before us is unique and does not "fit" exactly into any of the precedents cited to us. A more detailed treatment of the case law follows.

(a) Single Product

One tying case was referred to, *Souza v. Estate of Bishop*,[144] a case against a lessor of land in Hawaii based on the refusal of the lessor, like most other landowners in Hawaii, to sell the land. The tying product was argued to be the residences plaintiffs owned on the land while the tied product was the leasehold. The claim was dismissed on a motion for summary judgment, affirmed by the Court of Appeal.

From this decision, the respondents ask us to conclude that if a supplier presents two products as a package or, in other words, if they are being marketed together, that is the end of the matter and the Tribunal must conclude that there is a single product. The Court found that the plaintiffs' argument defied reason because the product being marketed was a house plus leased land and not a house purchasable separately from the land on which it stood. The Court also

[144] 1987-1 Trade Cas. (CCH) ¶ 67,628 (9th Cir. 1987).

found that the plaintiffs presented no evidence that the house and the leased land constituted separate products. We have already set out the test we intend to apply, which takes into account both demand and supply. We do not accept that simply because a producer or a supplier bundles products together that they are, *ipso facto*, one product.

Four cases are relied on by the respondents because they involve the Yellow Pages industry or an analogous industry. The respondents argue that these cases indicate that the United States courts have uniformly rejected any concept of an antitrust violation because of a publisher's refusal to pay commission or its decision to change the accounts on which it will pay commission. Thus, they conclude that the courts "in effect" have treated directory advertising as one product. They make this argument despite the fact that none of these cases was based on a claim of tied selling and therefore the issue of separate products in the sense with which we are dealing here was not before the court. The respondents claim, however, that these cases indicate that there is only one product *because* the tying argument was not raised in any of them.

We do not accept that the absence of a tying claim makes the cases dispositive of the issues before us in a tying case. In general, we do not see how the results in these cases can be directly transferred to the case before us. We will, however, review the decisions in order to see what, if any, assistance we can draw from the findings in resolving the issue of separate products on the facts before us.

In *Selten Agency, Inc. v. Pacific Telephone and Telegraph Co.*,[145] a specialized advertising agency brought an antitrust action involving numerous allegations against a number of telcos and telephone directory publishers that were members of the National Yellow Pages Service Association ("NYPSA") (the predecessor to YPPA). All of the allegations involved joint action by the NYPSA members. The only issue with any possible, although remote, relevance to this case was the claim by the agency that the NYPSA members *agreed* not to pay commissions on local advertising to agencies, constituting an illegal horizontal division of markets.

The Court concluded there was no evidence of an illegal agreement. The evidence was that the NYPSA agreement covered only national advertising; there was no prohibition on commissions for local advertising. Publishers were free to offer commission on local accounts and, the Court notes, some, in fact, did so. The Court also noted that those who did not offer commission on local accounts had their own sales force and therefore did not require the services of advertising agencies. The respondents rely heavily on the next sentence of the judgment, that "[i]t is not a violation of the antitrust laws for a publisher to refuse to buy a service that is not worth buying"[146] to argue that publishers do not have to buy services from agents or, in other words, provide a commission for any accounts they do not want to. As we have already stated, we do not accept that the supplier's choice is the sole governing factor in a tying case. Due consideration must be given to the supply side of the equation but we cannot ignore demand considerations.

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[145] No. CV 77-3450-FW (Dist. Ct. C.D. Cal. 8 June 1981).

[146] *Ibid*. at 17.

In *O'Connor Agency v. General Telephone Co.*,[147] an advertising agency alleged that a Yellow Pages publisher conspired with other publishers to change the definition of local or "B" accounts so that commission would no longer be paid on those accounts. The defendants brought a motion for summary judgment which was granted.

In granting the motion, the Court found an "agreement" to change the criteria based on adherence to the YPPA guidelines. Using a rule of reason approach, the Court then proceeded to consider and weigh both the anti- and pro-competitive effects of the change in the relevant market. The Court found that the plaintiff had provided no admissible evidence that the relevant product market was Yellow Pages and also provided insufficient admissible evidence of actual anti-competitive effect arising from the change. The Court also found that the publisher had a legitimate business reason for adhering to YPPA standards, namely the uncontroverted evidence that the defendant changed the commission criteria to increase its national Yellow Pages advertising which was not performing up to expectation.

The respondents rely on this case for the very broad proposition that "the U.S. jurisprudence directly involving Yellow Pages has rejected any concept of any antitrust violation because of the refusal of a publisher to pay commission to a CMR or as a result of the publisher changing the accounts on which it will pay a CMR" and that "[i]n effect the courts have said there is only one product that we're selling and we can sell it through whatever channel we

[147] No. CV-93-3650 LGB (U.S. Dist. Ct. C.D. Cal. 2 August 1994), appeal pending.

want".[148] The case certainly does not support those broad generalizations. It was a conspiracy case resolved on a motion for summary judgment because of failure to prove either a relevant market or actual anti-competitive effect.

The respondents submit that the case of *Thompson Everett, Inc. v. National Cable Advertising, L.P.*[149] is analogous to the case at bar. In that case an independent cable television advertiser representative brought action against exclusive contracts between the cable company and their spot advertising sales agents on the basis that the "traditional" cable representatives or sales agents were engaged in a concerted effort to exclude the independent from the business. The Court of Appeal affirmed the decision of the lower court to grant summary judgment.

The Court found that the exclusive contracts were not being enforced through an illegal conspiracy. It also found that the independent did not have access to the exclusive contracts because it was not willing to compete with the exclusive agents for them and was simply seeking to substitute its own method of serving the cable company for that selected by the cable company. The Court also found that there was no unlawful monopoly in the cable representative market because cable companies are part of a larger market.

Once again, the respondents rely on this case to argue that the Court endorsed the cable company's choice of using exclusive representatives simply because that was the way the cable

[148] Transcript at 66:13762-63 (26 February 1996).

[149] 57 F.3d 1317 (4th Cir. 1995).

company chose to do it. We have already indicated that the supplier's choice will not be the only consideration in a tying case. Indeed, the case itself does not go that far.

The most interesting decision referred to by the respondents is *Ad-Vantage Telephone Directory Consultants, Inc. v. GTE Directories Corp.*[150] The case involved a claim by an "authorized selling representative" ("ASR") for the placement of national advertising in telephone directories that the publisher had monopolized or attempted to monopolize the sale of Yellow Pages advertising. Because of problems in collecting payment for advertising placed by the ASR, the publisher started billing the advertisers directly. The ASR claimed that the publisher's direct contact with its customers resulted in a loss of accounts to it and its eventual failure.

The monopolization case failed because the ASR could not define any relevant market in which it and the publisher competed. The ASR had originally based its claim on the national advertising market where the publisher competed for the sale of national advertising as an ASR itself but could not show any market power on the part of the publisher in that market. The claim was then amended to allege that the relevant market was the sale of advertising space in a specific directory, shifting the focus to local advertising. Based on evidence that the ASR had received commission for the placement of advertisements for two local advertisers, apparently by accident, the ASR argued that it competed with the publisher's sales force for local advertising. The argument of the ASR was that the lawful power to publish the exclusive directory for a

[150] 1987-2 Trade Cas. (CCH) ¶ 67,683 (11th Cir. 1987).

specific geographic area did not give the publisher the right to be the exclusive seller of advertising space within that directory as publication and sale were separate activities.

The Court commented that the ASR's market theory had a certain "superficial" appeal based on its similarity to a typical wholesale/retail monopolization case where a vertically integrated manufacturer uses its dominant position at one level of activity (manufacturing) to eliminate competition at another level (retailing). The Court noted that for the ASR's theory to work, the publisher must be viewed as a wholesaler or manufacturer of advertising space and the ASR as a retailer of this space. If not a retailer, the ASR could not be considered a competitor of the publisher at the retail level.

The Court concluded that, to the extent that the sale of Yellow Pages advertising is an activity separable from the publishing of the advertising, the sales made by independent ASRs were in the nature of an agency and not retail sales. Agents, the Court noted, do not compete with those whom they represent. The wholesale/retail analogy failed, in part, because there *could* be no "resale" of Yellow Pages:

> . . . Yellow pages is not a product that is produced and distributed. The blank yellow pages do not exist prior to the sale of an advertisement, somehow awaiting distribution on a resale market. Each advertisement, that is, the space of the ad, is "created" when the advertisement is sold to the advertiser. . . . ASRs do not maintain an inventory of ad space to be sold. An ASR cannot purchase a page in the yellow pages and then distribute it to advertisers as it sees fit.[151]

[151] *Ibid*. at 58,482.

The agency characterization was preferred, in part, because the Court considered the relationship between the publisher and the ASR in the case before it to be analogous to the relationship between an airline and a travel agent:

> . . . The publisher lawfully establishes the price for its advertising and announces it to the public. It determines when it is going to publish directories, and has the ultimate say on how many advertisements it will accept. An advertiser may deal directly with the publisher, or may use an Authorized Sales Representative. However, should it use an ASR, the ASR must submit a request for advertising to the publisher, analogous to a reservation in the forthcoming publication. The ASR does not purchase an inventory of yellow pages space. The service which the advertiser has paid for is performed by the publisher, not the ASR. Further, should the advertisement fail to appear as requested in the appropriate directory, the publisher is under an obligation to refund the advertiser's money. Finally, should a publisher not receive enough advertisements to make a directory profitable, it must still publish the directory; the publisher retains the "risk" that not enough yellow pages advertisements will be "distributed" -- not the ASRs.[152]

The Court found ample evidence in the record that the ASR functioned as an agent, including the NYPSA guidelines which provided that ASRs represented the publisher "when selling National Yellow Pages advertising to national advertisers or their advertising agencies, or when negotiating disputes with such national advertisers or their advertising agencies".[153] The Court noted that there was also evidence that the ASR acted as an agent of the advertiser, including liability to the publisher for payment, but concluded that "[e]ither way, an ASR functions as an agent, not an `independent contractor,' and not, in any case, as a retailer of yellow pages advertising space."[154] Thus, the leveraging argument failed as there was no "second activity" to be monopolized by using the publisher's market power to publish directories as leverage.

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152 *Ibid*. at 58,483.

153 *Ibid*.

154 *Ibid*. at 58,484.

One element of this decision is the Court's insistence that the ASRs had to be considered retailers in order to be in competition with the publisher. A finding that the ASRs were merely agents of the publishers or, perhaps, agents of the customers, in the sense of having no independent existence from either or both of those two entities seems to preclude competition between the ASRs and the publisher. We do not believe, however, that the inapplicability of a strict retail model is conclusive. The Court did mention in passing, for example, independent contractors. The fundamental question is whether the publisher is in competition with the ASR or other person alleged to be excluded by the activity in question, which we agree is a question that should also be addressed in the context of a tying claim.

A second important element of the Court's conclusion concerned the functions performed by ASRs, that were apparently viewed as simple "order takers" insofar as the commission from the publisher was concerned. The Court indicated its assumption that the ASR was paid separately by the advertiser for other services such as layout[155] when it distinguished the case before it from a successful monopolization claim by an advertising agency against a television station. The television station had expanded its in-house advertising agency services by starting to produce commercials (for a fee) as well as selling air time. In *Ad-Vantage*, the Court stated:

[155] Or these might have been provided by the advertiser's "advertising agency" and not the ASR.

> Thus, in *Six Twenty-Nine Productions*, a leveraging argument was possible. The production of [Yellow Pages] advertisements is a related activity separate from the sale of advertising space. Each is a separate source of revenue. In the context of this case, no evidence was presented indicating that ASRs receive no separate compensation from their clients when the ASRs engage in the production -- the lay out -- of the advertisements. In fact, testimony of a former NYPSA official indicated that *most* of the national yellow pages advertising is purchased through ASRs by advertising agencies on behalf of national advertisers, supporting the notion that ad agencies perform a separate function. Thus, the leveraging argument made in *Six Twenty-Nine Productions* is not available here.[156]

What we take from this case is that it is important to examine the actual services performed by the agents for advertisers and the relationship between Tele-Direct and the agents, with a view to determining if they do, in fact, "compete" with Tele-Direct in any relevant sense.

(b) Relationship between Agents, Advertisers and Tele-Direct

The respondents say that, as in the *Ad-Vantage* case, agents in the case before us function as either representatives of Tele-Direct or, on occasion, as agents of the advertisers. In the first case, Tele-Direct does not compete with itself or its own representatives and in the second, it cannot be considered to compete with its customers. Based on the evidence of Charles Mitchell, Tele-Direct's Director of Marketing Sales Support, they submit that, in fact, Tele-Direct has not competed for agency accounts since 1992. The Director argues that, unlike in *Ad-Vantage*, the Canadian CMRs are not agents of Tele-Direct. The Director submits that the evidence supports the proposition that Tele-Direct has consistently considered, and still does consider, the agencies as its competitors.

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[156] *Supra* note 150 at 58,484.

The initial point at issue is the exact contractual relationship between agents and Tele-Direct. In 1988, Tele-Direct required the agencies to sign new contracts with it. Under those contracts, the agent warrants that it is duly authorized to enter into the agreement on behalf of the advertiser. Further, the agency agrees that "it is not acting and does not purport to act as agent for Tele-Direct."[157] This is exemplified by the provisions that the agent agrees to pay for the advertising; to indemnify and hold harmless Tele-Direct from claims by the advertiser; and to warrant on behalf of the advertiser the truth of all assertions in the advertising. Tele-Direct's Corporate Secretary and legal counsel, Patrick Crawford, confirmed that these contracts have not been revoked and that the agencies were not agents for or of Tele-Direct.

The respondents argue that the 1993 YPPA agreements entered into by the agencies in order to be accredited as CMRs supersede the earlier contracts although no steps have been taken to repudiate or amend the earlier contracts. In the application to be accredited as a CMR, the agency agrees to "represent" the publisher in the same terms as quoted in *Ad-Vantage* from the NYPSA guidelines.[158] The YPPA guidelines, however, describe a CMR as a member of YPPA which:

> a. Represents to the users the Publishers' product, services and policies, while representing to the Publishers the customers' needs, desires and concerns.
>
> b. Develops a comprehensive national Yellow Pages advertising program for prospects and/or advertisers.

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[157] Confidential exhibit CJ-16 (blue vol. 7), tab 214 (public), art. 10.

[158] Exhibit J-5 (green vol. 3), tab 154 at 32277.

c. Compiles and provides current information pertaining to all Publishers' practices affecting an advertiser's national Yellow Pages program.

d. Develops market research and cost studies for the advertiser or its agency as a basis for making advertising proposals.

e. Provides Publishers on a timely basis with the authorized list of dealers for solicitation under Advertiser's Trade Item.

f. Pays Publishers' invoices without recourse within the time period set forth in the individual Publishers' credit terms, notwithstanding its own collection status with that advertiser or its agency, unless any individual Publisher provides otherwise.

g. Absorbs all adjustment amounts incurred as a result of its own acts, errors, or omissions which including (*sic*) among other things, failure to notify Publishers of cancellations of orders, unless any individual Publisher provides otherwise.[159]

What comes out of this somewhat contradictory documentation of the relationship is that agents are not agents or representatives of Tele-Direct in any sense that would preclude a finding that the two are in competition. The agents are not so allied with Tele-Direct as a publisher that they have no independent existence. Their relationship has elements of both co-operation and competition.

The agents rely on the Yellow Pages industry, as represented by YPPA, and Tele-Direct specifically, to provide information on the effectiveness of Yellow Pages advertising. They are

[159] Exhibit J-4 (green vol. 2), tab 99 at 28021-22.

accredited based on industry standards. With respect to accreditation and the promotion of the medium, the relationship between Tele-Direct and the agents is undoubtedly cooperative.

However, the thrust of the Tele-Direct internal documentary evidence is that Tele-Direct treated the agents as competitors of its internal sales force. Prior to the 1990s, Tele-Direct sought to protect its client base from the agents by selling advertisers on using its services instead, stressing the advantages that dealing directly with Tele-Direct offered, including monthly billing and later closing dates, as well as considering more positive initiatives like assigning representatives to large accounts for a longer period of time. During the early 1990s, when Mr. Mitchell was head of the national accounts group, Tele-Direct actively competed for agents' clients. Mr. Mitchell testified that as of 1992, the approach changed to one of protecting internal accounts and revenue only but the documentation does not bear this out. Certainly, one of the reasons for the creation of Tele-Direct (Media) Inc. in 1994 was to combat the loss by Tele-Direct of national accounts to CMRs. The only "contradictory" evidence on this point is a somewhat unclear statement by Wayne Fulcher of DAC that prior to the formation of its CMR, Tele-Direct did not "normally" try to take away agency "headquartered" accounts. However, Mr. Fulcher does think that Tele-Direct's CMR is in competition with his agency.

Perhaps the most telling point is that Tele-Direct requires that agencies pay at the time of issue of a directory for advertising placed on behalf of their clients. If agents were only agents of Tele-Direct, they would not be financially responsible for the obligation of third parties -- the advertisers. This is compelling evidence that the agencies do not act as agents of Tele-Direct.

The evidence is that Tele-Direct has always considered agents to be, and has reacted to them, as competitors.

Nor can the agents be considered to have no independent existence apart from the advertisers themselves that they also "represent" in the sense of placing orders for advertising on their behalf. Yellow Pages advertising is not a simple product to buy and advertisers desire assistance in making the purchase. Agents, however, are not *mere* "order placers" for advertisers or other advertising agencies employed by advertisers. The evidence before us, which is reviewed in more detail below, is that agents provide a range of services, including advice, layout, design and administration, for which they do not receive additional compensation beyond the commission paid by Tele-Direct.[160] Further, we have no evidence that much of the agents' business consists of simply placing orders for another advertising agency employed by the customer to do the remaining work involved in producing the advertising. Advertisers want these other services in relation to their Yellow Pages advertising from agents. Thus, for advertisers, agents have a separate existence from Tele-Direct.

The relationship between Tele-Direct and agents is complex. Tele-Direct treats the agents as independent businesses with which they cooperate to advance their own objectives but with which they also compete. While Tele-Direct apparently recognizes that agents can service certain accounts better than its internal sales force, by reason of its creation of a class of commissionable

[160] The evidence is that agents charged separately for artwork when the commission rate was 15 percent but do not do so at the 25 percent commission rate.

accounts, it is also its goal, or at least the goal of certain groups within the corporation such as the national accounts group, to keep as much revenue as possible in-house and reduce its dependence on agencies to the absolute minimum possible. We conclude that the business relationship between Tele-Direct and agents is not inconsistent with Tele-Direct and agents treating each other as competitors.

(c) Additional Economic Benefit

The respondents argue that there is an "exception" to tying recognized in the American jurisprudence where the seller of the alleged tying product does not receive an "additional economic benefit" from the sale of the tied product. They say that Tele-Direct gets no additional economic benefit from the sale of services in this case because there is no "separate charge" for services.

The respondents cite two cases on this point. The first is *Directory Sales Management Corp. v. Ohio Bell*,[161] a decision affirming summary judgment granted against the plaintiff in an antitrust suit by an independent directory publisher against the telco and its directory publisher. The two defendants were wholly-owned subsidiaries of the same parent. One of the allegations was that the defendants tied business telephone service (tying product) to a free Yellow Pages listing (tied product) by refusing to reduce the price of the telephone service if the subscriber chose not to be listed.

[161] 833 F.2d 606 (6th Cir. 1987).

The Court noted that an illegal tying arrangement might exist if the telco in some way charged for the "free" listing indirectly in the bill for telephone service, even though it did not charge for the listing directly. The evidence was that there was no hidden charge for the listing as the telco did not pay the publisher for the expenses incurred in publishing the listing. The Court stated that if the telco did not receive a "financial benefit" from the tied product, there could be no tying arrangement.

The second case is *Beard v. Parkview Hospital.*[162] Dr. Beard, an osteopathic radiologist, was employed by a group of doctors that was the exclusive provider of radiological services to Parkview Hospital. Dr. Beard resigned from the group with the intention of providing radiological services on his own to patients at Parkview Hospital. The hospital did not permit him to do so and Dr. Beard sued, alleging that the exclusive contract for radiological services was an illegal tie of radiological services to other hospital services. Under the terms of the contract between the hospital and the group providing the radiological services, the group billed patients directly for its services and the hospital did not share in the fee. The lower court granted summary judgment for the hospital.

In affirming the dismissal, the appeal court approved the lower court's reliance on the requirement that the seller of the tying product must benefit directly from the sale of the tied product. The Court held that the requirement was also consistent with *Jefferson Parish*, which stated that an illegal tying arrangement is one where a firm with market power attempts to

[162] 1990-2 Trade Cas. (CCH) ¶ 69,154 (6th Cir. 1990).

impose restraints on competition in the market for the tied product, because the seller who "derives no economic benefit from sales of an alleged tied product or service is not attempting to invade the alleged tied product or service market in a manner proscribed by section 1 of the Sherman Act."[163]

Areeda explains the purpose of this rule in American case law and its relationship to tying as a *per se* offence:

> . . . a tie-in, though affecting a substantial volume of commerce in the tied product, is not per se unlawful when it does not foreclose any rival supplier or, perhaps, when any such foreclosure is inherently minor. . . .
>
> One convenient and frequent way to capture the concept of a relevant foreclosure is to ask whether the defendant has a financial interest in the tied product. In most courts, ties do not cross the threshold of potential power or effect when the defendant lacks an economic interest in the tied product, primarily because such a tie does not ordinarily enhance the defendant's power in the tied market or bring about any other consequences of the kind that the per se rule against tying seeks to prevent. "Foreclosure" there may be but not a relevant one.[164] (reference omitted)

Further, using the example of a defendant firm accused of providing its product *A* only to buyers who purchase *B* from a second, separate firm *T*, thus "foreclosing" other suppliers of product *B*, he explains:

> The defendant who gains not a penny, directly or indirectly, from firm *T*'s sales of product *B* is no "competitor" in the market for the tied product *B*. This much is clear, although there are difficulties ahead in deciding what type and magnitude of financial connection with firm *T* makes the defendant a "competitor" of those foreclosed suppliers.[165]

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163 *Ibid*. at 64,348.

164 P.E. Areeda, *Antitrust Law*, vol. 9 (Boston: Little, Brown, 1991) at 330-31.

165 *Ibid*. at 333.

Therefore, where there is no financial interest in sales of the tied product or in the tied market, the alleged tie-in does not cross the threshold for *per se* illegality, although the alleged tie does remain subject to review under the rule of reason.[166]

There are three points to be made regarding this argument of the respondents. First, the test of lack of any financial interest in the tied market or economic benefit from the sale of the tied product, however worded, is closely linked in American law to the *per se* nature of tying, which makes us reluctant to adopt it directly because Canadian law is based on a different standard, that of "substantial lessening of competition".

Second, there is some validity to the Director's argument that the question of economic benefit from the tied product, or of participation by the firm with market power in the tied market, only arises when two separate corporate entities are involved in the supply of the tying and the tied products. That was the case in both decisions cited and is not the case on our facts.

Further, in the *Beard* case it was abundantly clear that the hospital itself, the supplier of the alleged tying product, was not a participant in the radiological services, or tied product, market in any way as it did not receive any part of the fee for those services, which went directly from the patient to the unrelated doctors' group. In *Ohio Bell*, the situation was less clear as the two corporate entities were related but, in any event, the Court was definitive that there was no evidence of a "hidden" or "indirect" charge for the Yellow Pages listing in the telco's bill for

166 *Ibid*. at 347.

telephone service. The telco, the firm with market power, was not attempting to, in the words from *Beard*, "invade" the market for the supply of directory listings.

In contrast, on the facts before us, Tele-Direct itself supplies both space and services to all advertisers, both commissionable and non-commissionable. We also have evidence that it considers both consultants (detailed elsewhere) and agencies, the alternate service suppliers, to be its competitors. Since Tele-Direct provides services, it must be compensated for them. As a rational firm it would not provide something for nothing. Therefore, it cannot be concluded that it receives "no additional benefit" from its own sales of the alleged tied product. The precise form of that compensation or "benefit" is not at issue here.[167] Whether Tele-Direct has succeeded in foreclosing any alternate suppliers in the services market is evidently a relevant question but that is not what this argument of the respondents focuses on. This argument is that Tele-Direct gets no additional economic benefit from the provision of services and that, therefore, any exclusionary effects in that market are irrelevant because of the lack of linkage to the firm with market power over the tying product. The facts do not support this hypothesis.

(d) Separate Billing/Separate Payment

The respondents argue that if a producer pays for the "components" of a "product" directly and then sells the "product" complete with "necessary inputs" at a specified price, there

[167] The element of no separate charge, or separate billing, for services, which the respondents appear to allude to as part of this argument, is another issue which is dealt with in the next section.

is no tying. They state that the concept of tying *only* applies where the customer pays *separately* for the alleged tied and tying products. In oral argument, this was expressed as the proposition that it is not a tie to bundle something because as long as there is only one "cost" to the buyer, what is being sold is the supplier's single "product".

A distinction was drawn between the case at bar and the facts in *Jefferson Parish*, in which the respondents submit the items found by the Court to be separate products were not "bundled" but were in "two pieces" because there were two bills. They argue that the patient in *Jefferson Parish* paid for both "parts", presumably hospital services and anaesthesiological services, and that if a buyer pays for two different things on two bills, there cannot be one product. Reference was also made to the case of *Collins v. Associated Pathologists, Ltd.*[168]

Turning to *Jefferson Parish*, the distinction drawn by the respondents between that case and the instant case on the facts relating to billing is not as apparent as argued. In *Jefferson Parish*, the hospital and Roux & Associates had a contract which provided that all anaesthesiological services required by the hospital's patients would be performed by Roux. The hospital agreed with Roux to provide an anaesthesia department, including space, equipment, maintenance and other services, drugs and supplies, and nursing personnel (subject to approval by Roux). The use of the anaesthesia department was restricted to physicians employed by Roux. As the Court said:

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[168] 1988-1 Trade Cas. (CCH) ¶ 67,971 (7th Cir. 1988).

> The hospital has provided its patients with a package that includes the range of facilities and services required for a variety of surgical operations. At East Jefferson Hospital the package includes the services of the anesthesiologist.[169] (reference omitted)

The Court describes the billing arrangement as follows:

> . . . The fees for *anesthesiological services* are billed separately to the patients by the hospital. They cover the hospital's costs *and* the professional services provided by Roux. After a deduction of eight percent to provide a reserve for uncollectible accounts, the fees are divided equally between Roux and the hospital.[170] (emphasis added)

The majority of the Supreme Court did consider the "separate billing" of anesthesiological services" as a factor that entered into its determination of whether there were separate products. Yet, the actual billing arrangement, as described by the Court, looks very much like a combined bill for the tied product (professional anaesthesiological services) and part of the tying product (hospital services), much like Tele-Direct's bills for Yellow Pages advertising. Specifically, the amount billed included both a professional services portion for anaesthesiological services and a hospital-supplied anaesthesia equipment, facilities, support personnel and drugs portion. The fee is simply divided equally between the two, irrespective of the actual extent of professional services required in the particular case. It is not explicit separate billing of professional services.

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[169] *Supra* note 137 at 18.

[170] *Ibid*. at 6 n. 4.

In any event, there is no indication in the Court's decision that the factor of "separate billing" is essential or even critical. The most that can be said is that it is one factor to examine. We agree with the Director that if the entire resolution of the one or two products issue could be determined simply by the pricing or billing arrangements, this would allow suppliers to immunize all activity from tying claims simply by refusing to quote separate prices for items provided as a package.

Further, the Director submits that the mechanism or the route by which the money ends up in the hands of the separate service supplier is not relevant. In the commissionable market, the separate service supplier is paid by commission. A payment by commission may be somewhat more circuitous than, for example, direct billing by the hour by agents for their services (allied with a discounted price for space provided by Tele-Direct to persons who did not use its services) but the end result is the same -- the advertiser pays for the services, the advertiser receives the services of an agent, the agency receives payment for the services provided. Payment to agencies by way of commission was historically, and to a large degree still is, a fact of life in all advertising media.

The significance of the reference to *Collins* in this context escapes us. The Court in that case found that there was no distinct demand for pathology services as a product separate from hospital services. The Court did not refer to billing arrangements at all in making its findings. It based its conclusion solely on the lack of consumer or patient requests for specific pathologists or perception of pathology services as separate from other hospital services.

In summary, none of the cases referred to convinces us that the approach we have adopted to the separate product question is inappropriate. Several were largely irrelevant because they dealt with completely different facts or different, non-tying, antitrust issues. To the extent issues were raised which we considered relevant, particularly in the other Yellow Pages cases, we dealt with them in that context. We will now proceed with the basic approach we outlined at the outset and consider the evidence and arguments relating to demand and efficiency.

(3) Demand by Advertisers

Are advertisers that fall in that portion of the market which Tele-Direct currently defines as non-commissionable interested in purchasing the services associated with creating and placing a Yellow Pages advertisement from a source other than Tele-Direct? In other words, does Tele-Direct's practice of bundling space and services for a single price "force" them to buy a product that they would rather not buy from Tele-Direct? Or, do they regard the two components as a package that they would rather not acquire separately in any event?

The Director called 19 advertiser witnesses; the respondents called two. All of the witnesses except the two called by the respondents expressed a desire to obtain the services associated with developing and placing Yellow Pages advertising from someone other than Tele-Direct. Seven of the 19 advertisers called by the Director are current agency clients; [171] the remainder of the advertisers are serviced directly by Tele-Direct representatives. Of those, eight

[171] One advertiser (Turpin Group Inc.) participates in a trade-mark advertisement for General Motors dealers for which General Motors, a national advertiser, uses DAC. Turpin's own advertising is treated as local and it deals with Tele-Direct's internal sales force.

use or have used a consultant. Three would like to use an agent but cannot qualify for commission.

Fourteen witnesses represent multi-outlet (whether franchised, licensed or corporate-owned), multi-directory advertisers. The geographic dispersion of the outlets ranges from a metropolitan area to country-wide. Three are single outlet but multi-directory advertisers because of the wide territory from which they draw business. The remaining four advertisers are single outlet, single directory advertisers. All of the witnesses called are spending above-average amounts in the Yellow Pages. Two were spending close to the average of $1,700 (at about $2,000 annually each); the remainder ranged from $7,000 to $300,000.

The respondents have not attempted to rebut the specific evidence of the advertisers who indicate that they would prefer to obtain advertising services from someone other than Tele-Direct. They called two witnesses to show that some advertisers prefer Tele-Direct's services, although one of those witnesses stated that advertisers should have the choice of dealing with Tele-Direct or using an agent. Counsel admitted in oral argument that in the "top end" of the market, some advertisers find the bundling of services and space by Tele-Direct problematic. He argues, however, that these advertisers constitute a "statistically insubstantial sample" and that there will always be a number of people "who would like to get something for nothing" and "as long as they aren't paying for it".

It is true that the customers called to give evidence constitute a very small proportion of total advertisers. They were not randomly selected and we do not treat them as a statistically significant sample. However, coupled with their anecdotal evidence of why they prefer to use agents is the evidence that in the current commissionable market, which includes grandfathered eight-market accounts, agents enjoy the lion's share of the business. When advertisers have the choice, the vast majority choose an agent, rather than Tele-Direct, for services. There is clearly separate demand beyond what Tele-Direct considers a "national" account (the 1993 definition) with respect to eight-market accounts, currently grandfathered. Moreover, there is no reason to believe that the line drawn by Tele-Direct between commissionable and non-commissionable accounts accurately reflects the boundary of demand; that those accounts that are commissionable prefer to use an alternate service provider while those who are not commissionable do not. Given the strength of demand for agents' services in the current commissionable market, we think it is reasonable to infer that the preference shown by the large majority of commissionable accounts for the use of agents extends down into the current non-commissionable market, at least to some extent. We are satisfied there is sufficient evidence before us to conclude that there is demand for separate advertising services below the existing commissionable market and that the advertisers called by the Director can tell us something about the nature of that demand.

Common amongst the Director's witnesses, whether single or multi-directory advertisers, was a preference for the advice or consultative services provided by an agent or a consultant over those of Tele-Direct. A recurring theme was that the agent or consultant provides an "overall" picture, reviewing all of the client's Yellow Pages advertising, including white pages listings, which headings were being used and which should be used, all the directories involved, what the client's competitors are doing and the nature of the business's markets. These service providers help plan the Yellow Pages advertising, including recommending headings and, in some cases where the level of expenditure is higher, budgeting. In the case of agents, a representative is assigned to the account for a long period of time and the clients have the perception that the agency "understands" its particular business. That these service providers tend to pay attention to the overall picture is suggested by the testimony of two advertisers, one the client of an agent and one of a consultant, that the agency or the consultant was the one to bring to its attention duplicative advertisements in its Yellow Pages program.

The advertisers using agents also mentioned creative services as one of the elements of the service provided. For the clients of consultants, creative services are at least equally important since by re-designing an advertisement and by substituting other design techniques, like, for example, screening, for the more expensive size and colour, the consultants are able to reduce the cost of advertising.

In the case of both agents and consultants, advertisers generally perceive that these "independent" service providers are more interested in helping them get more out of their Yellow Pages advertising dollar than is the typical Tele-Direct representative. Frequently, according to the advertisers, the Tele-Direct representative does not have time to sit down and consult with the advertiser. The advertiser has to accommodate itself to the schedule of the representative faced with a full schedule and deadlines in a particular canvass. Another recurring complaint is that the Tele-Direct representative is more interested in selling more colour or a larger size than in arriving at the level and type of advertising that is right for that client; representatives are perceived as quite aggressive and prone to "upsell". Most of the advertisers also recognize that these problems result from the way in which Tele-Direct operates its canvasses and compensates its representatives; their comments were not directed at the representatives as individuals. While the agencies are also paid commission, individual representatives are paid straight salary for servicing the agency's existing client base.[172]

The multi-directory advertisers also prefer the services of third parties because they provide "co-ordination" or "administrative" services. These multi-directory advertisers are primarily the clients of agents rather than consultants.[173] They testified extensively about the advantages of using an agency which will keep track of publication dates for the various directories, control the uniformity of the advertisements, company image and message across directories and, where applicable, organize the contact between head office and franchisees or licensees for approval of advertisements and billing. Promoting a uniform message and image is particularly important to franchisers whose franchisees may be quite independent of head office

[172] The evidence is that the agencies generally keep servicing existing clients and prospecting for new clients separate; adding new clients is usually the primary responsibility of one or more designated persons. Out of the five CMRs that testified, two pay commission for new clients; only one of those offers that incentive to all employees, the other has a vice-president who is responsible for new business.

[173] Only two of the multi-directory (leaving aside the one who is in only two directories) advertisers were clients of consultants and only one of those talked about uniformity of advertisements and co-ordinating dates and deadlines.

and also to those which had enrolled businesses to their network which operate the franchised business as only a part of their overall business.[174]

It might be argued that the administrative services provided by agents are not supplied at all by Tele-Direct.[175] On that reasoning, administrative services would not be a component of the advertising services at issue in the tying case. The argument would be that since Tele-Direct does not supply administrative services, it is not in competition with agents because it is supplying different services and customers who want administrative services are free to purchase them separately.

It appears that, in fact, Tele-Direct has made some effort to provide the administrative services emphasized by the advertiser witnesses who appeared before us (uniformity and co-ordination) through its national accounts group and with its efforts regarding continuity. Further, while it is possible that such administrative services could *conceivably* be purchased separately, there is no reason to believe that it would be efficient to do so. There is no evidence of agents providing these services to advertisers who use Tele-Direct for the remaining services, even

[174] E.g., the "Autopro" line of automobile parts is offered by licensed Autopro mechanics and service stations across the country; the franchisees of Location Pelletier offer short-term vehicle rentals under that banner but usually operate another business as well.

[175] A similar conclusion was reached in the United Kingdom by the Office of Fair Trading ("OFT") in its 1984 report on the Yellow Pages industry: exhibit J-6 (green vol. 4), tab 282. When British Telecom withdrew all commission and internalized services through an exclusive sales contractor, the advertising agencies argued that they were placed at a disadvantage in competing to offer services to advertisers as the advertiser had to pay for the sales contractor's services, included in the rate card price, and then pay again to use the services of an agent. The OFT concluded that the "administration of the account" on the advertiser's behalf, by which they meant the day-to-day running of the account (negotiating claims, authorizations, proof-checking, paying bills) could not be carried out by the sales contractor and would either be done by the advertiser using its own resources or an agent. In respect of those services, therefore, the agencies were not competing with the sales contractor but rather with the advertiser's own resources.

though there is clearly a demand for them. The fact that Tele-Direct provides administrative services in some cases but not in others simply means that Tele-Direct and the agents are not providing precisely the same product. Indeed, one would not expect to find homogeneous packages of services. Otherwise, there would be no reason for customers to choose one service provider over the other. Therefore, we are satisfied that administrative services are a relevant and important aspect of advertiser demand for advertising services.

We now turn to the respondents' argument that advertisers only prefer agents because they are getting something for nothing or they are not paying for the agents. We do not accept this argument. The advertiser is paying for the advertising services whether provided by Tele-Direct or, if the account is commissionable, by an agent. With respect to the use of consultants, advertisers pay to use consultants as Tele-Direct's price remains the same but the consultant charges the advertiser a portion of the amount the advertiser saves by use of the consultant. Those savings would otherwise be for the advertiser to either spend on more Yellow Pages advertising or to pocket.

Even if we were to accept that the cost to advertisers of obtaining services is the same whether they choose Tele-Direct or an agent, we think it is still evidence of separate demand that where advertisers have the choice, the advertisers prefer to use agents. However, the evidence is, as will be explained, that when advertisers use agents, they bear costs additional to what they would have to bear if they placed their advertising through the Tele-Direct representative. Thus, it is apparent that customers prefer agents even if it is more costly to use an agent than to deal directly with Tele-Direct. This is strong evidence of demand for the services of agents by advertisers when they have the possibility of using them.

One source of higher cost derives from the billing practices of Tele-Direct. When advertising is placed through Tele-Direct's representative, the cost of advertising is divided into twelve equal parts and included in the Bell Canada telephone bill commencing upon issue of the directory. Advertisers who use agents are required to pay for their advertising on an issue basis, that is, to pay the full amount upon issue of the directory. When this occurs the advertisers' additional cost of using an agent is roughly one-half the annual cost of funds or, in other words, one-half of the commercial interest rate.[176] Given interest rates over the past 20 years, this has, depending upon the time, constituted approximately three to six percent of the advertising bill, a cost the advertiser does not pay if it uses Tele-Direct's services. In the words of Mr. Kitchen of Lansing Buildall, these advertisers are "paying a premium in terms of the payment schedule." While it is true that some advertisers that used agencies have arranged for periodic payments, no arrangement disclosed in the evidence is as favourable to them as the Tele-Direct monthly billing practice.

Another cost borne by some advertisers in order to use an agent is the placing of "extra" advertising in directories outside the areas from which the advertiser draws its customers so that

[176] Counsel for the respondents appeared to take the position that advertisers did not incur higher costs of using agents in those cases where the advertisers placed advertisements in a number of directories that were issued throughout the year. Although this argument has a superficial appeal because it appears that advertisers are paying on a periodic basis either way, it is not valid. Advertisers who use an agent must pay in advance for each directory as opposed to over a 12 month period if they use Tele-Direct.

the criteria for the eight-market rule (grandfathered accounts) are met. Five advertiser witnesses buy "extra" advertising. In one case, the cost of the additional advertisements is paid by the agent; in another the agent pays 15 percent of the cost of the additional advertisements. The other advertisers bear the full cost of the "extra" advertising.

How far down does the demand for separate services extend? We have evidence from a number of advertisers, both agency clients and clients of consultants, probably best described as large local or regional advertisers. Despite the amounts they are spending in Yellow Pages, these advertisers would not qualify even under the eight-market rule if they only advertised in the areas where they have locations or from where they draw business.[177] Since there are only seven market areas in Ontario and six in Quebec, that rule requires advertising outside the boundaries of each province.[178]

However, we did not hear from any truly "small" advertisers. Although two of the advertiser witnesses spend about average amounts in the Yellow Pages, they are the outlying examples. Most of the remaining witnesses, even those using consultants, spend at least $10,000

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[177] Of the seven agency clients, five, to all appearances, would not meet the eight-market criteria; the sixth apparently does but does not meet the 20-directory requirement for the 1993 rule. The seventh may meet the 1993 definition but as a group advertisement which is problematic for other reasons (see chapter "IX. Abuse of Dominant Position" under "D. Market for Advertising Services", *infra*). The three advertisers who currently use Tele-Direct but would like to use an agent are similar: a franchiser, a large regional advertiser and a company with three offices in two provinces.

[178] Among the agency clients, HOJ Car and Truck Rentals, for example, spends $125,000 annually and has 36 franchises, all located in southwestern Ontario. Location Pelletier spends $120,000 to $160,000 annually but its 60 licensees are all within the province of Quebec. Stephensons' Rent-all Inc., as Mr. Day of Day Advertising Group, Inc. testified, became non-commissionable when the eight-market rule came in and that was when it began to do the "extra" advertising. Stephensons has 38 retail outlets in southern Ontario and spends $140,000 on Yellow Pages advertising. Among the consultant clients, Canac-Marquis Grenier has 10 outlets across Quebec and spends $50,000 on its advertising; Tiremag Corp. spends $20,000 although it has only one outlet.

and most spend considerably more than that. Advertisers spending more than $10,000 annually represent only two percent of Tele-Direct's total advertisers by number and about one-third of its advertising revenues. There are, therefore, a vast number of advertisers representing a significant amount of revenue about which we know little regarding the character of their demand for separate advertising services.

The Director refers us to documentary evidence dating from 1975 when Tele-Direct changed to the eight-market commission rule to show that approximately 20 percent of the pre-1976 agency customers purchased less than $1,000 per year of Yellow Pages advertising. Many purchased as little as $500 worth of advertising annually. We have no reason to doubt the accuracy of these statements. We are reluctant, however, to reach conclusions about "small" advertisers based only on documentary evidence that is some 20 years old.

On the other hand, we have the views of Michael Trebilcock, the respondents' economist expert witness,[179] regarding "smaller" advertisers, which imply that these advertisers do not demand advertising services from a source other than the publisher. Based on the data provided in the report of the Office of Fair Trading,[180] he notes that for smaller advertisers, the cost of providing advertising services overwhelmingly comprises space and selling effort rather than advisory services. The reasoning behind these statements is sound and there has not been any evidence or argument to the contrary. It is certainly plausible that the lowest-cost

[179] Professor of Law and Director of the Law and Economics Programme at the University of Toronto.

[180] *Supra* note 175.

"advertisements", for example a bold listing, do not contain much, if any, creative content. We therefore accept that the general thrust of this argument is valid and that, for "smaller" advertisers, it is highly doubtful that a separate demand for advertising services exists.[181]

The evidence supports the view that there is buyer interest in obtaining advertising services from suppliers other than Tele-Direct over at least part of the spectrum of advertisers. While it is difficult to know where exactly to draw the line, we can conclude at this point that there is no evidence that would satisfy this threshold test of separate demand from "smaller", including new, advertisers. It is apparent that the larger advertisers would have the greater need for the services of agents or consultants based on the complexity of their advertising. Smaller, including new, advertisers whose advertising is relatively more simple likely would not have such need.

However, based on the evidence before us, we are not prepared to draw a firm line below which we could confidently say there is no evidence of buyer demand for services of independent advertising service providers. Therefore, at this point, we only conclude that there is evidence of buyer demand for advertising services for suppliers other than Tele-Direct for "larger" advertisers.

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[181] We note from Tele-Direct's 1994 Corporate Post Canvass Analysis Report that "new" advertisers, those using Yellow Pages for the first time or new businesses, are certainly among the smaller Tele-Direct advertisers. Selling effort is especially important with respect to new advertisers. The average *annual* expenditure by a new advertiser is $839, less than half the average for all advertisers. Less than one-half of one percent of new advertisers spend $1,000 or more *per month* where the corresponding percentage among established advertisers is about 3.5 times greater. Apparently, the typical new Yellow Pages advertiser starts with a small advertisement, in which case it is the value of the medium and the "sales pitch" which are important and not other advertising services.

(4) Respondents' "Efficiency" Arguments

Given the evidence of demand for services from suppliers other than Tele-Direct, is there evidence that efficiency considerations would dictate a single product? Based on the historical practices of Tele-Direct, the Director has ample evidence that the products can and were, in fact, sold separately. Pre-1975, a large percentage of advertisers could acquire services from a source other than Tele-Direct. Under the eight-market rule and the 1993 rule, any advertiser that qualifies or can make itself qualify by some extra advertising can acquire services separately from an agent. The respondents have put forward a number of efficiency arguments which, if valid, they say would lead to the conclusion that there is a single product and therefore, no tie. These arguments are largely based on the analysis and evidence of Professor Trebilcock, their expert witness. There were also profitability studies entered in evidence by the respondents and they will be dealt with in the next section.

(a) Impossibility of Leveraging: Fixed Proportions

Professor Trebilcock, for the respondents, is of the view that the Director's theory that Tele-Direct is attempting to leverage its market power (assuming it has market power) over space into the services market by bundling space and services is not valid. He states that such leveraging cannot occur because advertising space and advertising services are complements which are consumed in fixed proportions. There is agreement between the experts on both sides that complementary goods used in fixed proportions imply that the only profit-maximizing motive to bundle the two products is in order to minimize costs; all opportunities to exploit market power could be accomplished with control over either product. This implies that the bundling is socially efficient and it should be concluded that there is only one product.[182]

Professor Slade, for the Director, argues that space and services are at least partially substitutable. Professor Slade is of the view that:

> . . . it is possible to achieve the same impact by using a large ad or one that is cleverly designed. In addition, astute targeting of the "right" directories can substitute for purchasing space in a larger group of directories. More generally, an agency that provides service can often advise on ways to cut expenditure on space while maintaining the same level of advertising impact. In addition, it might even suggest ways of obtaining a higher impact from lower expenditure by, for example, substituting white knockout for colour.[183]

Because of the failure of the assumption of complementarity, she argues, leveraging is possible. Certainly the possibility of an extension of market power over a substitute, even if only a partial substitute, is one which causes concern and should be examined further.

The evidence supports variable rather than fixed proportions. To the extent that agents tend, compared to Tele-Direct representatives, to be less likely to promote increased expenditures on space, the additional expenditures on advertising services by agency clients (through the purchase of extra advertising, foregoing monthly billing) lead to the substitution of

182 We should note here that while the Director refers to space and services, Professor Trebilcock refers to three elements: space, consulting advice (design, graphics, layout, etc.) and selling effort (or pure promotion of the value of the medium). He recognizes that selling effort is clearly variable in relation to space. That is the genesis of the principal-agent problem dealt with later in this section.

183 Expert rebuttal affidavit of M.E. Slade (28 August 1995): exhibit A-119 at 11.

advertising services for advertising space. Furthermore, once it is recognized that there is an issue of the quality and content of advertising services, as indicated by the evidence of advertisers and their willingness to pay more for agents than it would cost them to use Tele-Direct's representatives, even assuming the same expenditure on space using an agent or Tele-Direct, it is difficult to see how advertising services are being consumed in fixed proportions with advertising space.

The evidence regarding the activities of consultants also suggests that advertising services and advertising space are not used in fixed proportions, and that they are partial substitutes. The purchase of services from a supplier other than Tele-Direct results in reduced expenditures on space. An example provided by a consultant concerned a very large and apparently inappropriate existing advertisement for a taxi company in the Hamilton area. The existing full page advertisement included a large picture of an airplane and reference to airport service. The consultant (Serge Brouillet of Ad-Vice Communications) determined from his marketing needs analysis for the client that he actually did very little airport business. The changes proposed by the consultant were both less costly and appeared to be more effective.

We conclude that advertising space and service are not consumed in fixed proportions and it cannot therefore be assumed, as argued by the respondents, that only efficiency explains why they are bundled by Tele-Direct.

(b) Widespread Industry Reliance on Internal Sales Force

As part of his expert evidence on behalf of the respondents, Professor Trebilcock stated that any theory of the tying allegations in this case must explain four central facts. One of those facts is stated as:

> Almost all yellow pages directory publishers organize their selling functions in a similar way to TD i.e. by heavy reliance on an internal sales force.[184]

It is not in dispute that all North American publishers, whether telco-affiliated or independent, rely heavily on their internal sales force. The Director has, however, brought forward evidence indicating that where the line is drawn between accounts that are open to agency competition because they qualify for commission and those which are exclusive to the internal sales force differs from publisher to publisher. The Director further argues that Tele-Direct's current commissionability rule is one of the strictest in North America.

The respondents submit that Tele-Direct's national account definition simply represents the transposition of the YPPA national account definition (also referred to as the YPPA "A" account definition) into the Canadian context. The YPPA by-laws provide that, as a minimum standard, an advertising program involving two or more publishers, 20 or more directories, and at least three states with 30 percent of the advertising revenue outside the primary state is considered national Yellow Pages advertising. Publisher members must accept advertising

[184] Expert affidavit of M. Trebilcock (18 August 1995): exhibit R-174(b) at para. 27.

meeting those criteria as national. They are not precluded from accepting advertising meeting less stringent criteria as national. Each publisher decides on the level of compensation for advertising it defines as national.

While the *terms* of the YPPA definition are similar to those used by Tele-Direct in its definition, the evidence was that the effect of applying the definition in Canada is very different. Where there are about 6,000 directories in the United States, there are only about 350 in Canada. Tele-Direct is one of only seven or eight publishers in Canada and controls 70 percent of Canadian Yellow Pages publishing revenue. Tele-Direct's definition incorporates a minimum of two provinces instead of three states. Tele-Direct requires 20 percent of the published revenue outside the primary *publisher's territory*; the YPPA definition requires 30 percent of the revenue but outside the primary *state*. Under the YPPA definition, as long as two publishers are involved, there could be minimum revenue in the second publisher's territory. According to the agency witnesses, the 20 percent requirement is especially onerous given that Tele-Direct's territory includes the two most populous provinces. Overall, commission is currently paid on 13 to 14 percent of total directory advertising revenues in the United States as opposed to seven to eight percent of total revenues in Canada.

Although it is true that an account wholly within a large state such as California (with a larger population than all of Canada) might not be commissionable under the "A" account definition, according to the President of the YPPA, most publishers, including telco affiliates (RBOCs) pay commission on regional accounts, called "B" accounts. For example, the evidence was that Pacific Bell has a commissionable account which could include accounts wholly within the state of California.

In Canada, with one exception, all the telco publishers require advertising to be placed in two publishers' territories to qualify for commission at 25 percent,[185] usually with a minimum of 20 percent of revenues required outside the dominant publisher's territory. Effectively, this generally means that two provinces will also be required.[186] Since the other publishers have much smaller territories than Tele-Direct, their "two publishers" requirement is easier to meet.

Professor Trebilcock places great stress on the fact that independent publishers also rely heavily on an internal sales force because "many of these directories do not remotely possess any market power (however measured) in many of the directory markets in which they operate."[187] Therefore, he concludes

> *The stark and enormously significant implication of this fact is that the decision to vertically integrate advertising selling functions clearly has nothing to do with market power*. It must be explained entirely by the kind of efficiency considerations . . . outlined earlier in this opinion.[188]

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[185] AGT Directory Limited only pays 25 percent on foreign numbers (as do all publishers) but pays 15 percent on *any other* advertising, including local accounts.

[186] Except for Edmonton Tel: advertising in Calgary and Edmonton would qualify under its rule.

[187] *Supra* note 184 at para. 27.

[188] *Ibid*.

Based on the evidence from White and DSP, we know that, in Canada at least, despite the fact that they offer commission on all accounts brought to them by CMRs,[189] the independents rely heavily on their internal sales force. The evidence that we have is that an internal sales force is a *necessity* for their survival rather than a choice based on efficiency considerations. Despite the liberal commission rules, they receive a small proportion of their overall revenues from agents and must rely on their own sales force for the bulk of their revenues.[190] In fact, recruiting an effective sales force is one of the hurdles a new publisher has to overcome.

While we agree that the independent publishers are unlikely to have market power, we are reluctant to conclude solely on the basis of the fact that they rely on an internal sales force that the "bundling" of sales and service by a publisher with market power is competitively benign.[191] We would likely be willing to draw that conclusion if we had evidence that the markets in which independents are operating, particularly in the United States, are competitive. If they were, yet most sales by publishers were on a bundled basis, that would be a very strong indication that efficiency was dictating the bundling and that there was only one product at issue.

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[189] The evidence of Mr. Lewis of White was that White pays commission (in the United States and presumably also in Canada) on any account submitted by a CMR without restriction. The commission rate is 23 percent for established directories and 30 percent for newer directories. Likewise, DSP pays CMRs commission on any account.

[190] E.g., for White: eight percent of revenues in U.S. placed by agents; in Canada, one-half of one percent of revenues placed by agents.

[191] In circumstances where the dominant players are telco publishers and those publishers only pay commission on national and regional accounts, it follows that agents are active mainly in those sectors. They are not set up to service local accounts even if independents pay commission on those. Thus, because the dominant players do not want to use agents for local accounts, independents *cannot*, even if they wanted to, rely solely on agents but must use an internal sales force. Professor Slade is of the view that agents would tend to serve this market over time if the major publishers changed their policies and provided a broader market. Further, as the independent is usually the newcomer into a market dominated by the telco publisher, agents are reluctant to recommend a new directory, even for national and regional accounts where at least some of the major players pay commission, until it has proven itself.

The only evidence we have, however, is that those markets, like Tele-Direct's market, are dominated by the telco publisher. It was pointed out to us by the respondents that most RBOCs' prices are even higher than Tele-Direct's. We also referred in the section dealing with Tele-Direct's market power to testimony that indicates that American telco publishers also have sufficient profits to subsidize local telephone service. We are, therefore, not satisfied that widespread reliance on an internal sales force across publishers, including independents, dictates a single product on efficiency grounds because it may be a function of telco dominance in all markets.

(c) Agents' Views

The implication of finding and prohibiting the tied selling alleged by the Director is that agents would, one way or another, be permitted to offer their services to a wider range of accounts below the level of "national" accounts currently considered by Tele-Direct as commissionable. Professor Trebilcock is of the view that agents are not interested in servicing smaller accounts.

In interviews with agents that the Director's staff undertook in investigations prior to filing the application, the agents stated that they were not interested in the smaller accounts. As reported by Professor Trebilcock, who had access to the summary of the interviews prepared by the Director's counsel, the smallest accounts that any of the agents expressed an interest in ranged from those spending from $10,000 to $50,000 per year on Yellow Pages. A lower limit of

$10,000 excludes almost 98 percent of all customers and approximately 70 percent of total revenue but would represent a substantial increase over the amount of revenue currently commissionable.

When giving evidence the agents took a different position and stated that they would be interested in all customers but would handle the business differently. The only reasonable interpretation is that the early answers reflected the agents views given their current method of operation. Their answers when giving evidence, in contrast, reflected the willingness of businesspeople to consider any reasonable opportunity to turn a profit, including considering the possibilities of paddling into uncharted waters. On the whole, we regard their views during the interviews as the more reliable. Because the agents apparently have little or no interest in servicing smaller accounts, we infer that they regard themselves, at least in their current setup, as at a cost disadvantage *vis-à-vis* Tele-Direct in dealing with these smaller customers.

Therefore, we agree with Professor Trebilcock that agents are not interested in servicing smaller accounts, although neither he in his evidence nor the Tribunal at this stage can be more explicit than having regard to the $10,000 to $50,000 range about what constitutes "smaller" accounts.

(d) Justification for Tele-Direct's Practice of Bundling

Professor Trebilcock attempted the most complete explanation and justification of Tele-Direct's practice of bundling space and services over most advertiser accounts. Initially, he divides what the Director has alleged to be advertising services into selling effort and consulting advice regarding the advertisement (artwork, placement, etc.). He states that selling effort cannot be priced on its own as customers will not pay for a "sales pitch"; it must be bundled with either space or consulting advice. The overall problem facing Tele-Direct (and other publishers) is to exercise control over those selling its product and to motivate agents or internal staff, as the case may be, to provide an optimal mix of selling effort and consulting advice *from Tele-Direct's viewpoint*. The Tribunal agrees that there is what is known as a "principal/agent" problem at work here. The issue is the nature of the problem and whether Tele-Direct's viewpoint is the only relevant one or should be the operative one.

Professor Trebilcock divides his explanation concerning Tele-Direct's approach to commissionability into three categories: small advertisers, larger local advertisers (which presumably includes regional advertisers) and currently commissionable advertisers (larger national or regional accounts involving multiple publishers). We have accepted that it is likely that small advertisers have no separate demand for advertising services. New advertisers, with few exceptions, coincide with small advertisers. For the sake of completeness we continue with the "efficiency" or cost-side evidence for all advertisers including small advertisers.

Professor Trebilcock's primary explanation of why Tele-Direct prefers to rely on its own resources for servicing small customers is that it is highly likely that it is cheaper for Tele-Direct to service small customers internally. His view is that the most effective method of selling advertising to these customers, probably because of significant economies of scale, appears to entail "`blanketing' directory territories in concentrated time blocks on a sequential basis" as Tele-Direct currently does. It is, however, not self-evident that this approach results in lower per unit costs than using smaller numbers of representatives who take a longer time to do a canvass. There is simply no evidence.

Another factor cited by Professor Trebilcock that is likely to lead to attenuated efforts by CMRs regarding small advertisers is the possibility that advertisers would engage in opportunistic conduct. The difficulty Professor Trebilcock foresees is that once the successful selling effort has been made, which the customer is unwilling to pay for, the customer is in a position to ask for, and other sellers are in a position to offer, a discount because they need only provide the consulting advice and not the selling effort, for which the first seller will be uncompensated. He believes that this problem is most acute for small advertisers, including first-time buyers. For large advertisers, selling effort constitutes a smaller percentage of overall advertising services. In addition, larger customers might have more difficulty engaging in opportunistic conduct because they are more likely to become known to agents. Tele-Direct can avoid this "free riding" by small advertisers by bundling space and selling effort. This is a version of the free riding argument often made in defence of vertical arrangements such as resale price maintenance which may be valid in some circumstances. There is, however, absolutely no evidence that it applies on the facts in the instant case.

Professor Trebilcock also points to a divergence of interest between Tele-Direct and agents which leads to an incentive compatibility problem should Tele-Direct use agents to service small advertisers, otherwise referred to as the "completeness externality". This externality, compounded by advertiser opportunism as explained above, is also the principal explanation advanced for why Tele-Direct prefers to provide services internally for "larger local" advertisers. As Professor Trebilcock recognizes, a simple cost difference cannot explain the reluctance of Tele-Direct to offer a commission on these accounts as the agents would not service them, even if commission were offered, if they were at a cost disadvantage to Tele-Direct.

According to Professor Trebilcock, there is a positive correlation between the "completeness" of a directory and the value that users place on it. Advertisers are willing to spend on a directory to the extent that the users find it valuable. But since each individual advertiser benefits only minimally from their own contribution to completeness, they are unwilling to pay for this effect. Tele-Direct, as the publisher, is able to internalize this externality over the longer term (the more "complete" and useful the directory, the more valuable the advertising space and the higher rates it can charge).

While there is no doubt that publishers value "completeness" for the reasons stated, it is largely an undefined term. There is no explanation in Professor Trebilcock's evidence, for example, of why a directory is in any sense more complete when there are paid bold listings rather than unpaid listings in ordinary type. Nor is there any adequate explanation of why users would value more advertisements in colour or larger advertisements unless they provide more information. There were also indications from the evidence that there can be *too much* advertising from the viewpoint of users. In large centres such as Montreal and Toronto, it has been necessary to split directories because of their size. Thus, while it is indisputable that directories must have sufficient representation by advertisers so that the directory is considered to be a useful reference, it is far from clear that *all* increases in advertising contribute to this objective. This point is critical because if Tele-Direct is encouraging increased selling effort beyond the range where further advertising contributes to completeness in any meaningful positive way, then the ability of Tele-Direct to sell additional advertising through its own sales force cannot be assumed to be socially beneficial in providing users with additional value.

Professor Trebilcock is of the view that the completeness externality leads to two results. First, Tele-Direct has a stronger incentive than CMRs to recruit new accounts; CMRs will focus most of their efforts on attracting existing advertisers from Tele-Direct or other CMRs. Second, while Tele-Direct is interested in retaining customers over the long term in order to enhance completeness, CMRs will be more concerned with immediate returns. Thus, when Tele-Direct recommends the, in Professor Trebilcock's words, "optimal" advertising package, the CMR will have an incentive to convince the advertiser that a less expensive or "sub-optimal" package is equally useful in order to recruit the customer. The risk of dissatisfaction on the part of the customer is increased; the customer may stop using Yellow Pages because of informational imperfections which make it difficult to distinguish between weakness in the medium and bad advice.

Further, Professor Trebilcock is of the view that it would be difficult for Tele-Direct to structure incentives to CMRs to induce them to sell a "socially optimal" quantity and quality of advertising by way of contract because of significant transactions costs. On the other hand, Tele-Direct can and does motivate its internal sales force "to sell and advise clients to purchase optimal packages by offering training, encouragement, screening of advertising sales by managers, internal promotions, awards, a team ethic, etc."[192]

The Tribunal is inclined to agree with Professor Trebilcock that it is probably easier for Tele-Direct to create incentives that motivate its own representatives to sell more than agents. The more important question is whether leaving Tele-Direct the unfettered choice of when to use agents and when to service internally leads to a truly "socially optimal" result. We have already indicated some doubts that the unrestricted pursuit of completeness, while it may be in Tele-Direct's interest, is wholly in the public interest or "socially optimal".

The Director argues that Tele-Direct chooses to retain services in-house because this allows it to motivate its sales force to exploit better the "information asymmetry" it enjoys *vis-à-vis* its customers or, in other words, to "oversell". He submits that Tele-Direct's incentive structure results in its sales representatives convincing advertisers to buy more than they would if they were provided with balanced information or the possibility of obtaining an alternative viewpoint from another service supplier. Witnesses stated that they did not regard the advice from Tele-Direct's representatives as objective. We have acknowledged that, as a general matter,

[192] *Supra* note 184 at para. 22.

the effectiveness of marginal dollars spent on advertising is difficult to determine. This leaves customers somewhat vulnerable to the advice they receive. The incentive structure for Tele-Direct's representatives makes the Director's argument that they are motivated to "oversell" at least plausible. To the extent that the Tele-Direct representatives succeed in selling "too much" advertising to one advertiser, the effect would multiply throughout a heading, since, as the evidence revealed, many firms base their Yellow Pages expenditures on that of their competitors (the "prisoner's dilemma"). We, therefore, cannot accept Professor Trebilcock's critical assumption that the advertising a Tele-Direct representative sells is necessarily socially optimal.

With regard to recruiting new customers, we accept that a publisher would want to ensure that there was a thorough and efficient canvass of potential new customers, in the sense that all were approached and there was no duplication of effort. Since the prospective new Yellow Pages advertisers are easily identifiable from business telephone subscriber information in the hands of the publisher, it makes sense to assign them to specific persons rather than creating a "free for all". This can be done on an individual basis, by territory, or any other method that avoids multiple contact of the same prospect by different persons. The assignment is key; if customers are assigned it makes little difference whether the persons making the contact are employees or outside agents.

Professor Trebilcock also believes that a reason why Tele-Direct does not make larger local customers commissionable is that agents would curry favour with customers by recommending less than the "optimal" amount of advertising (or the amount that a Tele-Direct representative would recommend), with long-term detrimental effects, because they are primarily interested in immediate returns. While Tele-Direct may worry about the advice being given by agents, it is far from clear that the quality of their advice is a cause for concern with respect to satisfying the needs of consumers. The facts before us do not support Professor Trebilcock's view that agents tend to take a short-term view. When the actual relationships between customers and agents and customers and the internal sales force are considered, it is the former who have the long-term relationship. Until recently most Tele-Direct representatives, *unlike* agents, predominantly had a short-run relationship with customers. Professor Trebilcock also acknowledged that agents might be reluctant to be perceived as pushing current sales because customers might be inclined to switch agents. Tele-Direct's representatives do not have this concern because customers do not have freedom of choice. Much of the representatives' livelihood depends on increased sales to existing customers whereas the employees of the agents are on salary and receive no additional compensation for increased sales to existing clients.[193] Moreover, there is no evidence that agents' clients have tended to cancel advertising for any reason.

In Professor Trebilcock's view, the fact that Tele-Direct chooses to pay commission on multiple publisher accounts is evidence that Tele-Direct is motivated by efficiency considerations with respect to all its decisions regarding commissionability. Otherwise why would Tele-Direct choose to make any part of its sales commissionable? Professor Trebilcock

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[193] Based on the evidence of the representatives of CMRs who testified; together those CMRs account for a large portion of commissionable sales.

interprets the fact that Tele-Direct pays commission on national accounts and that the bulk of sales to this segment is made by agents as proof that agents can more efficiently service this segment. While Professor Trebilcock believes that the tendency of agents to undersell and focus on existing advertisers and the possibility of opportunism are still present, the cost advantages of agents compensate for these weaknesses. These sophisticated advertisers are also better able to monitor whether they are being sold the "optimal" amount of advertising and the possibility of losing such a client effectively polices the agent. While the Director accepts that the agents are more efficient in servicing the commissionable segment, he disputes, as noted above, that agents in any circumstances sell "sub-optimal" amounts of advertising as defined by Tele-Direct's perspective. The Director takes issue with the view that Tele-Direct is more efficient in dealing with the rest of its customers. Detailed evidence on relative efficiency was placed before us and is the focus of the next section.

In summary, as indicated in the section on advertiser demand, we have accepted Professor Trebilcock's view that there is no separate demand for advertising services for "small" customers. With respect to those advertisers for which separate demand has been proven, called "larger local" advertisers by Professor Trebilcock, the Tribunal does not accept that either the completeness externality or the possibility of advertiser opportunism is supported on the evidence before us and, therefore, does not dictate that space and services are a single product with respect to those customers. The question of relative efficiency or cost advantages on the part of Tele-Direct with respect to servicing those advertisers will be addressed in detail in the next section.

(5) Comparative Profitability Studies: Agents/Internal Sales Force

The respondents have introduced evidence bearing on the comparative efficiency of Tele-Direct's representatives and agents to argue that the commissionability rules are, and always have been, efficiency based. The primary evidence is a comparative cost study dated 1995 created for these proceedings and entered through Michel Beauséjour, Tele-Direct's Vice-president of Finance. In addition, there are two other internal contribution-to-profit studies from 1974 and 1985, along with the descriptive evidence of Donald Richmond, Director of Manufacturing and Contract Administration for Tele-Direct, and Jan Rogers, Director of Corporate Methods and Support.

Before turning to a detailed discussion of the evidence it is necessary to consider its import with respect to the respondents' claim that its policies with respect to the payment of commission and the utilization of agents are dictated by efficiency considerations. While the studies referred to are relevant to the respondents' position, there are very important caveats that seriously weaken the conclusions that can be drawn from the evidence. Firstly, in an ordinary "make or buy" decision what is being compared is only the *cost* of producing a particular product in-house or buying it. This basic requirement (of looking only at cost) is violated when a comparison is made between the *contribution to Tele-Direct's profit* by the internal sales force and agents, i.e., revenue considerations enter.

More importantly, the products (i.e., the provision of services to commissionable and non-commissionable accounts) being compared in the Raheja study from 1974 and the 1995 study are very different. In fact, these studies are well described by the comparison of "apples and bananas". It is difficult to see what can be derived from the exercise of comparing the contribution to profit of agents and Tele-Direct's representatives who each deal with an entirely different set of customers. A significant percentage of the non-commissionable accounts are dealt with entirely over the telephone. Where representatives meet with customers, the customers' needs, for the most part, cannot be compared with the large multi-directory customers who rely on agents. What is the point of comparing the contribution to profit of agents, who are acknowledged to be relatively effective in serving complex "national" customers, with the contribution to profit of Tele-Direct's representatives in serving customers, many of whose requirements are relatively simple? While the comparison in 1985 between NAMs/NARs and agents might be considered to be a close, although not an exact comparison, the data are not current and not particularly detailed.

Overall, we have found these profitability studies not to be supportive of the respondents' position. The early studies are out-of-date (and Raheja is of limited relevance because of the difference in products being compared and an error in it), a critical point when considering current efficiency. At numerous points in the 1995 study, the differences in costs can be traced to differences in the characteristics of the customers being served rather than to any possible difference in the relative costs of agents and Tele-Direct's personnel. It also suffers from bias in favour of Tele-Direct because of its time frame and from methodological weaknesses.

For completeness, we will comment on the studies to further explain why, in our opinion, they are not reliable for the purpose advanced by the respondents, that is, to demonstrate that Tele-Direct's internal sales force is more efficient than agents.

(a) Raheja Study (1974) [194]

This study was prepared as part of a review of Tele-Direct's policy towards advertising agencies, including agencies specializing in Yellow Pages, which were a relatively recent phenomenon at the time, with a view to determining a commission payment. The study itself notes that the system of classifying accounts at Tele-Direct made it difficult to calculate profitability of the various components. Nevertheless, Mr. Bourke was of the view that management at the time placed sufficient confidence in the results of the study to make decisions on the basis of it. The study showed that in the "local market", defined as all sales within Tele-Direct's own directories, agency sales were less profitable. Although there is no evidence of the weight that the study played in the decision, in 1976 Tele-Direct sharply restricted the commissionable market by moving to the eight-market rule.

The odd thing about the exercise is that, taken on its own terms, there is an obvious error in the study: the commission to agents is counted both as a reduction from revenue *and* as an expense. When the error is corrected the comparative ratio is somewhat better for the agents than it is for Tele-Direct's own representatives. The respondents take the position that the existence of

[194] Confidential exhibit CJ-32 (black vol. 11), tab 83 at 132667ff.

the error is irrelevant; management acted on the information, proving that Tele-Direct was motivated by efficiency considerations and not by any other motive. While the study may suggest that Tele-Direct was at least *interested* in efficiency at the time, it is peculiar that so simple an error was not easily immediately detected by those supposedly basing decisions on it. In the circumstances, and having regard to the many qualifications in the study, the existence and results of the study are not of assistance.

(b) Profitability Study: National Accounts - Selling (1985) [195]

This study deals with the contribution to profit of national accounts serviced by agencies and NAMs in 1983 and 1984. Agencies included specialized and regular agencies while the NAMs included one Tele-Direct sales representative who dealt with high revenue potential customers and another who dealt with low revenue potential customers.

The study was entered in the record during the cross-examination of Mr. Beauséjour. Although the bottom line contributions to profit were noted, there was no examination of the study with the witness other than to establish that the then prevailing methodology regarding the payment to Bell Canada was employed. Based on the description in the document the only costs that were specifically attributed to the agents and NAMs were agency commissions and so-called sales expenses. The latter included the salaries of sales personnel in the national accounts group

[195] Exhibit J-1 (red vol. 1), tab 61.

but also the personnel who processed orders submitted by agents.[196] All other costs were allocated on the basis of the net revenues generated by each of the two channels.

For the combined eastern and western regions, the contribution to profit as a percentage of total revenues generated for the agents and NAMs in 1983 was 18.7 percent and 17 percent respectively. In 1984 the contribution was 20 percent for both. While there are caveats,[197] the important point that emerges from the study is that Tele-Direct had no reason to believe at that time that it was less costly to rely on its own representatives who dealt with customers with the same or similar characteristics as those served by agents. The respondents did not bring to our attention any further study or any evidence whatsoever of internal consideration of relative efficiency leading up to the 1993 change in the commissionability rules. The only documentation on the record, and the evidence of Mr. Mitchell who was intimately involved in the preparation leading up to the change, focuses on effects on number of accounts and revenues that would be available to agents or the internal sales force under various scenarios.

(c) Profitability Study (1995) [198]

Towards the end of the hearing counsel for the respondents introduced through Mr. Beauséjour a document comparing the relative contribution to profit in 1994 of agents and

[196] Total salaries were allocated to CANYPS, agencies, NAMs and GSF.

[197] To anticipate questions that might arise as a result of the discussion of Tele-Direct's latest contribution to profit study, the same percentage cost of customer service (the payment to Bell Canada) and "melt" is used for both agents and NAMs. There is some tipping of the scales in favour of agents with respect to the cost of customer service since it is applied net of commission in the case of agents. On the other hand, no account is taken of the fact that agents pay up-front and the customers of NAMs pay over a year.

[198] Confidential exhibit CR-185.

the internal sales force, including the national accounts group. The document was admitted over the strenuous objections of counsel for the Director. During discovery, Tele-Direct provided a cost of sales figure for its internal sales force of 12.3 percent of revenue. The basis for that figure was explored through detailed follow-up questions and further explanation. There was no indication from the respondents that a second study was being undertaken by Tele-Direct, and that it contained results that were different from those that had been given on oral discovery and in follow-up answers. On December 4, 1995, counsel for the respondents produced the second study to counsel for the Director.

While we found the timing of the production and, in fact, counsel for the respondents' conduct of this whole matter of the new study to be, to say the least, unfortunate, we admitted the document while allowing the Director further discovery and preparation time. Despite the inappropriate timing, we were of the view that the Tribunal should not forego receiving information that could have an important bearing on the case and which apparently went to the heart of the respondents' position that the bundling of space and services by Tele-Direct was dictated by efficiency considerations.

(i) Unrepresentative Timing of Study

Apart from the general difficulty, already highlighted, of comparisons being made between the servicing of very different types of accounts, there is another serious defect in the recent study. The period for which the study is done almost certainly creates a bias in favour of the internal sales force *vis-à-vis* the agents because of the state of progress of certain improvements Tele-Direct was making to its process. The study fails to take account of the fact that the application of technology is in a period of transition. While improvements favouring the internal sales force have been put in place, those favouring agents are on the immediate horizon. Despite this, the latter have been ignored in the study.

The system that Tele-Direct was putting in place in 1994 with respect to the publishing process was much more efficient for the internal sales force than the system that it replaced. More specifically, a computer system was introduced that allowed the electronic storage of advertisements, including finished artwork. This means that advertisements that renew without change, about 70 percent of all advertisements, are already in the computer. This is contrasted by Mr. Richmond with the previous system:

> . . . In the old system, when we used an outside supplier [for pre-press functions, e.g., layout, paste-up], if we got an ad from last year, we may or may not have found that artwork because it was kept in a filing cabinet somewhere. It meant that the next year we had to have an artist redraw the artwork to match what was in the book before. This was very inefficient. We had to store logos all over the place so that everybody could get hold of it.[199]

There are also savings when there are changes to the advertisement. Under the new system, minor changes can easily be made on the electronic version of the advertisement.

Although agents submit their advertisements "camera ready" (as "veloxes"), they must be scanned into its system by Tele-Direct. If there is no change in an advertisement from the

[199] Transcript at 34:7026 (7 November 1995).

previous year then it follows that it should be possible to avoid re-scanning the advertisement, as it is already in the system, so some savings should be possible. Mr. Richmond did not know the percentage of agents' advertisements that are repeated without change but he did state that *all* CMR advertisements are scanned, implying they are scanned even if there is no change. It is not clear why Tele-Direct does this.

Thus, until recently and certainly when commission was further restricted in 1993, the costs that Tele-Direct would have experienced for the internal sales force were those that existed prior to the introduction of the new system. Under the old system the fact that agents were submitting complete advertisements meant that the cost comparison in the publishing part of creating a directory was far more favourable to agents than is presently the case. According to Mr. Richmond the cost of implementing the new system is $26 million and the annual savings are of the order of $12 million, which would have made previous publishing costs for internally-generated advertisements almost twice as high as they were in 1994.

Using current data disadvantages the agents with respect to the near future. There would be no need to scan agents' advertisements if the advertisements could be transmitted electronically. Currently, newspapers and magazines have systems in place for this purpose. The Yellow Pages publishers are moving in this direction, according to Mr. Logan, the President of the YPPA. He foresees this capability on the VAN system, the electronic YPPA order system, in two to three years. The pay-off would be a smoother flow with lower costs for publishers and CMRs and a reduction in errors.

The other area within publishing where change can be anticipated is in how Tele-Direct receives orders over the VAN. Currently a clerk in Montreal and one in Toronto take the information off the VAN as hard copy. After the order has been dealt with in this form, it is eventually re-entered into Tele-Direct's system. Ms. Rogers stated that Tele-Direct had hoped to be able to transfer all orders received through VAN directly into the contract data base without re-keying but this did not happen. According to Mr. Logan of the YPPA, "[t]he bigger publishers, both independents and utilities, now are developing and I think probably most of them -- not everybody, most of them -- can take the information directly off the VAN and run it into their systems without re-keying".[200] For some reason Tele-Direct is lagging behind other North American publishers in taking advantage of the VAN, the system for which agents made significant investments and for which, in part, Tele-Direct agreed to raise commission rates from 15 to 25 percent over a two-year period. While there have been reductions in cost in processing agents' orders since the movement to VAN, according to Ms. Rogers these appear to be less related to the VAN than to internal reorganization and, therefore, this confirms that Tele-Direct has not taken full advantage of the VAN.

For all these reasons, we conclude that the study does not recognize the technological transition in publishing Yellow Pages and that failure to do so favours the internal sales force over the agents.

[200] Transcript at 36:7370 (9 November 1995).

(ii) Methodological Weaknesses

There are significant methodological problems with this study. The study is based on a "causal model". Costs were analyzed by Tele-Direct personnel to determine whether particular costs would be experienced in the absence of either agents or the internal sales force. If the answer was in the affirmative those costs were assigned to the group that caused the costs in question. Costs that could not be identified as caused by one or the other channel were treated as common costs and allocated to the two channels on the basis of relative revenue. This overall methodology was submitted to Tele-Direct's auditing firm for confirmation that the approach was sound. All cost assignments and allocations were performed by Tele-Direct personnel and the results were not audited by an outside firm. The testing of the results was done only through discovery and cross-examination during the hearing.

In the final result, the internal sales force's contribution to profit is shown to be approximately 13.5 percentage points higher than that of the agents. If we ignore for the moment the complications created by the difference in types of accounts serviced by each, this result would mean that in order for the agents to be competitive with the internal sales force the commission rate paid to them would have to be nine percent rather than the average of 22.5 percent that in fact is paid to them (22.5 less 13.5).

We turn first to the method used to allocate common costs. It is, in our view, valid to allocate these costs on the basis of revenue where the common costs can be considered to be related to the level of sales. This is true for an area such as manufacturing the directories, where the costs depend on the volume of advertisements and it may make little difference whether the advertisements are generated by the internal sales force or agents. This approach to allocating common costs is far less justifiable when the costs in question relate to personnel, e.g., the personnel department itself. This is important because sales representatives and all their support personnel are internal to Tele-Direct while the agents and their support personnel are not. In areas like these it would be more appropriate to allocate costs based on the relative proportion of employees identified as devoted to servicing the internal sales force and agents. Mr. Beauséjour admitted that this was an equally valid approach as using relative sales and that either method could have been used.

An analysis of each of the common cost areas to see whether it was more appropriate to use one or the other weighting procedure would have produced a more objective and defensible result. We note that Tele-Direct did depart from its approach to allocating common costs on the basis of revenue in at least one instance, which also happened to work in its favour.[201]

In the study Tele-Direct has violated its own methodology for attributing costs on a causal basis in a way that increases the costs of dealing with agents. As noted earlier, the current system of storing advertisements in a computer is in the process of being introduced. The cost of duplication between the old and new systems which would, on the stated approach, be attributed

[201] Depreciation of the scanner (a common cost since it is caused neither by internal sales force or CMRs) is divided equally between internal sales force and agents based on relative volume of items by number scanned from these sources. Based on the revenue methodology otherwise employed most of the depreciation would be allocated to internal sales force.

to the internal sales force, was treated in the study as a "transition" cost and was subtracted from the total internal costs. Similar costs related to moving to the VAN system were, however, attributed to the agents. To be even-handed, they too should have been considered "transition" costs and subtracted from the agents' costs. Further, it is questionable that the large investment in the new system for dealing with internal orders should simply be ignored, as was done in the study, rather than amortized over several years. The effect of not doing so is also to understate internal costs.

Counsel for the Director questioned the validity of the cost attribution in the study in several areas where a relatively small percentage of costs was taken to be caused by internal sales force even though the internal sales force and its direct support account for 61 percent of total employees. With respect to the costs of the Personnel and Benefits department, Tele-Direct concluded that there would only be a saving of about 16 percent from eliminating the internal sales force and thus only 16 percent of the total cost was attributed to the internal sales force. Similarly, in the Labour Relations department the saving assumed was only 30 percent. In defence of these decisions, Mr. Beauséjour explained that there were certain basic requirements that would have to be maintained to service the remaining personnel even if 61 percent of the personnel were eliminated. In effect, this approach treats the present organizational chart as inviolate. We question whether Tele-Direct would approach such a massive change on an "avoidable cost" basis.

The Director's principal challenge to this study relates to the method of dealing with the "cost of customer service" ("CCS"), the 40 percent of net sales revenue that is paid to Bell Canada. In all past studies of profitability, CCS was treated as a cost. It was also so treated throughout the many months when there were successive drafts and refinements of the 1995 study, almost until the moment that the study was entered in these proceedings. As a result of the penultimate amendment to the figure for CCS, the contribution to profit of the agents changed from being slightly less than the internal sales force to almost five percent *more* than the internal sales force.[202] Subsequent to that, Mr. Beauséjour decided that there was no reason to treat CCS as a cost since Tele-Direct and Bell were part of the same corporate entity and it makes little difference whether Tele-Direct made payments to Bell in the form of CCS or as dividends. Despite the apparently fortuitous timing of this realization, we accept that the point is valid. It is one thing for Bell to insist that CCS be included as a cost in order to impose market discipline on Tele-Direct but it is another matter when a study of the relative costs of using agents and internal staff is being performed. It then makes better sense to treat Bell and Tele-Direct on a consolidated basis. This in itself is not a methodological weakness.

However, the same reasoning means that the Tele-Direct study should have taken into account the benefits accruing to Tele-Direct/Bell from the fact that agents pay up-front for advertisements whereas customers of the internal sales force pay monthly. Mr. Beauséjour recognized this benefit in cross-examination but it does not appear in the study. As discussed

[202] The reason why CCS has such a large impact is that under Tele-Direct's contract with Bell Canada the revenue from agents who are billed by Tele-Direct rather than Bell are not subject to the payment of CCS. Thus the average payment of CCS is much lower in the case of agents than of internal sales force.

earlier, the difference in timing of payment amounts to interest for about half a year, an appreciable difference of three to six percent per year.

(iii) Particular Examples of Problems Arising from the Difference in Products

The respondents advance this study as evidence which they say proves the different, and greater, "interface" costs that they incur when processing orders originating with external agents as compared to the costs of processing orders originating internally. As we indicated at the outset, it is extremely difficult, in conducting a study of this nature, to distinguish the genuine interface costs, costs that arise because Tele-Direct is dealing with agents rather than the internal sales force, from costs that arise from the nature of the advertising, and thus are not clearly related to the channel submitting the order and are not true interface costs. This problem permeates the study and, thus, it cannot prove relative interface costs in its present form as the respondents maintain it can.

That is not to say that we think the problems arising from the difference in the products, unlike the unrepresentative timing and methodological weaknesses already identified, consistently operate in the respondents' favour by lowering internal costs and raising agents' costs. As detailed below, this is sometimes the case; sometimes the reverse is true.

We turn to some examples. One relates to the interpretation and treatment of credits to customers as a result of Tele-Direct's errors. Customers using the internal sales force were reimbursed 1.3 percent of gross revenues as a result of errors made by sales representatives or during the publishing process. The rate of reimbursement to agents as a result of publishing error was 3.5 percent. This difference in the rate of Tele-Direct's errors is a factor in the overall lower contribution to profit of agents.

In the notes to the study it is stated that the difference is due to the fact that orders from agents are handled by more people, that is, CMR personnel and the national accounts publishing group of Tele-Direct. It is, however, irrelevant how many people in the CMR handle orders because only errors attributable *to Tele-Direct* are reimbursed. One possibility that may explain part of the difference in error rates is the greater knowledge and, perhaps, incentive that agents have to discover and complain about errors compared with the customers of the internal sales force. Mr. Beauséjour admitted this was a possibility. While this explanation would probably not change Tele-Direct's view that the higher reimbursement is a "cost", it would hardly be a reflection of lower efficiency in the use of agents compared to the internal sales force.

On the other hand, Ms. Rogers stated that the higher error rate in processing agents' orders was due to the larger, more complex advertising programmes submitted by agents. This suggests that the error rates are related to the nature of the advertising programmes rather than the channel through which they flow. To the extent that the principal reason for the difference is the difference in the type of accounts serviced by each channel, it cannot be concluded that the difference in error rate is a cost of dealing with agents.

The comparatively large error rate in dealing with agents' advertisements also shows up in other costs attributed to dealing with agents. A Tele-Direct employee checks the advertisements after the directories have been printed, a duplication of effort since the agents also verify their advertisements. In addition, there are the resources expended in error negotiations with the agents.

Apart from the difference in the size of advertising programmes mentioned by Ms. Rogers, we also know about one other respect in which there is a significant difference in the content of advertisements submitted by the internal sales force and agents. Approximately 80 percent of "trade-mark" advertisements are handled by agents. Three Tele-Direct clerks within the department which processes agents' orders are assigned to checking a proposed trade-mark advertisement to ensure it has been authorized by the owner of the trade-mark. This is a cost assigned totally to agents that depends on the nature of the advertisement rather than on the channel dealing with the advertisement.

In a related area, that of bad debts, the study may, in fact, underestimate the comparative cost of dealing with agents as opposed to the internal sales force. Over the years there is a regular, although fluctuating, percentage of unpaid bills to customers serviced internally. Until recently Tele-Direct has not had the same experience with agents. Mr. Beauséjour noted that Tele-Direct is currently owed money by an agent but no figure for non-collection from agents was included in the study. The area of "melt", bad debts along with discontinuance of phone service, which negatively affect the internal sales force contribution to profit, are probably due to the character of the clients served by the internal sales force rather than having anything to do with who is servicing them. This is consistent with the more "volatile" nature of smaller accounts commented on in internal Tele-Direct documents.

(d) Conclusion

The numerous points on which the various studies are subject to challenge confirm that they cannot be used for the purpose of comparing the relative efficiency of Tele-Direct's internal sales force and agents.

(6) Conclusion on Separate Products

The Director has alleged that tying is present over the entire demand spectrum, although counsel for the Director has, in effect, recognized that there may not be tying for "small" customers.[203] According to the respondents, there is no tying for any of their customers. The parties' positions represent the two extremes. The Director would have us order the respondents to offer space and services separately (whether by separate prices or expanded commission) to all their customers. The respondents would have us make no order, thus allowing them to offer the two separately only to those customers that they choose.

[203] By proposing the further alternative remedy of reverting to the pre-1975 commission rule.

We are of the view that neither extreme is supported by the evidence. What we see is that customers or advertisers are not homogeneous in terms of their need for services, or demand, or in terms of the costs involved in servicing them, or efficiency considerations. On the contrary, they are very heterogeneous, ranging from an individual running a small business from home and spending a minimal amount on a simple advertisement in the Yellow Pages to large corporations advertising in a multitude of directories. Our view is that we cannot decide whether there is one product or two products for all these different customers in a blanket fashion. We must engage in an exercise of "line drawing".

We are of the view that the evidence on demand for separately supplied advertising services and the evidence and arguments relating to efficiency of supply indicate that advertising space and advertising services are separate products with respect to "large local" and regional advertisers. They are a single product for "small" advertisers. The difficulty is in knowing how reasonably or workably to distinguish regional and, more problematic "large local", advertisers from "small" advertisers, whether in terms of number of markets (as in the eight-market rule) or dollars spent on Yellow Pages. In approaching this task we have been mindful that the Director bears a burden in this regard of justifying any remedy granted. To the extent that the evidence and argument have left the matter unresolved, it behooves us to be cautious in our conclusions.

We know that in the current commissionable market, including grandfathered accounts, where advertisers have a choice, they overwhelmingly choose agents. We have found that demand extends well below the 1993 "national" definition and below the eight-market definition of commissionability.

The differences in the constituents of demand between the relatively smaller advertisers that employ the services of a consultant and those of larger, multi-directory advertisers that use agents or would use them if their accounts were commissionable are notable. The needs of the latter are more complex. In addition to advice and creative services, most require help in administration and in assuring uniformity of message. We infer that the intensity of demand, as measured by their willingness to pay, year after year, for these services by way of extra advertising or issue billing, is greater for larger customers that have multi-dimensional needs.

We turn to cost considerations to focus further on the appropriate dividing line. We have concluded that agents' interest, presumably driven by their view of their comparative efficiency *vis-à-vis* Tele-Direct, is primarily in customers with a minimum size ranging from $10,000 to $50,000 in annual expenditures on Yellow Pages advertising. This alone would dictate raising the bar for any unbundling of space and services to a minimum of $10,000.[204]

While the evidence that at least some independent publishers are willing to pay commission on any business brought in by agents could be interpreted to mean that it would be efficient to unbundle across the entire demand spectrum, we are not comfortable going that far. It

[204] We are referring to monetary amounts here because that is the way the evidence came in. Other criteria, such as number of markets, are more informative and other evidence was presented in that form. We attempt to relate the two measures below.

is far from clear that these publishers are guided by the relative efficiency of agents and in-house staff in servicing customers since for the most part their market position requires them to rely heavily on in-house staff despite their liberal commission rules. Their policy on commission could as easily be reflective of their desire to attract additional demand as of the relative efficiency of agents and in-house staff.

The approach of the large American publishers associated with telcos is to bundle space and services for all accounts smaller than those classified as national accounts or, for those who use a "B" account definition, for accounts smaller than regional accounts. We are not satisfied, however, that the publishers in question operate in competitive markets and that their choice of a dividing line is necessarily efficiency driven. As a result, we conclude that while unbundling of national and "B" accounts by them is probably efficiency driven, we cannot say that bundling for the balance of their accounts is motivated by efficiency and is conclusive on the dividing line for one versus two products.

Tele-Direct's studies are not helpful in drawing conclusions with respect to relative efficiencies of agents and Tele-Direct's employees along the demand spectrum. What we do know is that the eight-market rule was created by Tele-Direct primarily to capture more accurately "national" accounts than did the original 1958 definition and, at the time, Tele-Direct apparently considered this rule to be in its interest. Further, it is also clear that Tele-Direct did no studies and had no internal discussion of relative efficiencies when it further restricted commissionability in 1993. In doing so it ignored demand from existing eight-market customers (including those that were forced to buy unneeded advertising to qualify for eight-market status). Given that agents had served these types of customers over many years, that other publishers have "B" accounts, and that Tele-Direct at no time addressed the comparative efficiency of agents and the internal sales force for these accounts, there is no evidence of any efficiency offset which would lead us to conclude that space and services were not separate products for all the accounts within reach of the eight-market rule.

The eight-market rule was not specifically designed to deal with the needs of regional advertisers. This is obvious from the fact that there are seven markets in Ontario and six in Quebec. By almost any definition an advertiser covering all the markets in a province would be considered "regional" although such an advertiser would not be commissionable under the eight-market rule. Many of them likely managed to bring themselves within the rule with extra advertising. At a minimum, a firm that covers an entire province the size of Quebec or Ontario should qualify without more. We have no reason to doubt that the strong demand for advertising services from agents displayed by currently grandfathered eight-market accounts extends to advertisers that cover six markets, which would mean, for example, the entire province of Quebec. It is difficult to see that the efficiency implications for separately supplied advertising services at the six-market level are significantly different than for eight markets.

There is a rough relationship between the number of markets served and the amounts spent on Yellow Pages advertising. According to Tele-Direct's internal studies, the average amount spent on Yellow Pages advertising among customers served by Tele-Direct representatives but that were in the commissionable category under the eight-market rule was $54,000.[205] The comparable figures for accounts that would qualify under a seven-market and six-market rule, respectively, are $44,000 and $26,000. While some agents might find six-market accounts below their threshold of interest, the evidence is that they are within the range that some agents are willing to service, perhaps in anticipation of future growth.

We are cognizant that looking only on the demand side a case might be made for unbundling well below the six-market level. The evidence with regard to efficiency, principally the agents' views on accounts that they would like to service, does not support this conclusion. The Director suggests that there is no harm in unbundling across the board -- the market can be allowed to decide. If agents are more efficient, they will end up servicing the accounts. If Tele-Direct's internal sales force is more efficient, especially for smaller accounts, it will end up servicing those accounts. This implies a simple solution to a complex problem. In large measure, Tele-Direct is "the market" since the pricing of advertising services is inevitably its responsibility, whether it chooses to set commission rates for various types of accounts or to charge separately for the services of its internal sales force. Given widespread unbundling, Tele-Direct might well decide to set several different prices (or commission rates) for advertising services depending on the relative costs of servicing various categories of accounts. As the study on relative profitability showed, this would likely be a difficult task. It is not one that should be imposed without some greater certainty that there will be a significant overall benefit from the

[205] While the document is not explicit, the data were gathered in 1993 so we infer these are 1993 figures: confidential exhibit CJ-31 (black vol. 10), tab 69 at 131635.

change. Therefore, we find that space and services constitute two products down to the six-market level and a single product below that level.

Addendum on Tying

At the outset of our discussion on tying, we indicated that another theory of the tying case was possible and we address that now. While some of the respondents' arguments and evidence are related, they did not adopt the precise approach which we outline hereunder.

One interpretation of the evidence is that advertising space and services are not demanded nor provided separately even in the existing commissionable market. Rather, larger advertisers either wish to purchase the bundle of space and services from Tele-Direct or from agents, in either case they are purchasing bundled space and services. Tele-Direct insists that the agents it deals with be accredited. The Director acknowledges that the placing of advertising in telephone directories is complex and accepts accreditation of agents by Tele-Direct. Indeed we do not necessarily envision advertisers purchasing space from Tele-Direct and providing their own services (except perhaps in the case of advertisers with accredited in-house advertising departments).

Following from the fact that accreditation means that only accredited services providers (including Tele-Direct's internal sales force) can place orders for space and they do so along with providing other services, it could be concluded that space and services must be bundled to be sold and that, therefore, they constitute a single product. Another way of viewing the matter would be that advertising space and services could be considered a single finished product on the basis that the real complaint respecting tying is not that advertisers are precluded from purchasing space and services separately, but that Tele-Direct has simply refused to supply unbundled space (i.e., at a discount) to agents which prevents them from selling to advertisers the same bundle of advertising space and services that is sold by Tele-Direct.

The evidence does not support this interpretation for the following reasons. First, we are satisfied that agents are not resellers of Tele-Direct's advertising space such that advertisers are purchasing the space *from agents* along with services. Agents do not carry an inventory of advertising space which they purchase from Tele-Direct for resale to advertisers. They assume no risks with respect to advertising space. Rather, when the agent's customer decides to purchase Yellow Pages advertising, the agent submits an order to Tele-Direct together with all other necessary information and Tele-Direct processes the order. The fact that Tele-Direct contracts with and bills the agents for the space, and treats the agents as the "buyer" in that sense, is not determinative of the relationship between the agent and the advertiser. We think that the fact that the agent does not have an inventory of space for resale is more consistent with the agent acting as an agent for the advertiser for the acquisition of space from Tele-Direct.[206] On this view of the evidence, the purchaser is not purchasing a bundle of space and services from the agent.

[206] Agents are agents for or "represent" advertisers in the sense that they place advertising on the advertisers' behalf but, as indicated earlier, agents have an independent interest and existence apart from advertisers in other aspects of service provision.

Second, the evidence does not indicate that advertisers wish to purchase advertising space from an agent as opposed to Tele-Direct. We think, all other things being equal, they are probably indifferent. However, there was evidence that they would prefer to pay Tele-Direct for space through monthly billing on their telephone bill rather than purchasing the space through agents on an issue billing basis. It is Tele-Direct that requires the latter arrangement, not the customer who demands it. This is not evidence that advertisers demand Yellow Pages space from agents as part of a service and space bundle. Nor have we been presented with evidence suggesting that efficiency would be adversely affected if Tele-Direct was to contract with and bill advertisers directly for space.

Finally, a purpose of the *Competition Act* is to encourage competition in order to provide consumers with competitive prices and product choice. There is evidence of demand for services from agents as opposed to Tele-Direct and efficiency considerations at the six-market level and above do not preclude facilitating such choice. For these reasons we have rejected this alternative interpretation of the evidence and have accepted that advertising space and advertising services constitute separate products.

E. TYING CONDITION

Having determined that there are separate products over at least part of the spectrum of Yellow Pages advertisers, we must now determine if those advertisers falling within that range were somehow "forced" to buy the products together rather than from separate sources. Since we have not found separate products below six markets, any references to the "local" market in this section refer only to that portion of the market from the current "national" definition down to six markets. In that range, where we have found separate products, we must establish that the two products were "tied" together as set out in subsection 77(1).

Paragraph 77(1)(a) provides one definition of tied selling. In essence, it is described as a practice whereby a supplier, as a "condition of" supplying the tying product to a customer, requires that customer to acquire another product from the supplier. Paragraph 77(1)(b) provides an alternative definition, the operative portion of which is that tied selling is a practice whereby a supplier "induces" a customer to meet the condition of acquiring another product from the supplier by offering to supply the tying product on more favourable terms and conditions if the customer agrees to acquire the second product.

The Director pleaded both the "requirement" or "condition" and the "inducement" in the application. The Director submits that, on non-commissionable accounts, the respondents require the customer to acquire their advertising services as a condition of supplying the space at a bundled price "and/or" the respondents induce customers to acquire their services by offering to supply space at no additional cost for the additional value if the customer also acquires their services.

It is undisputed that Tele-Direct does not segregate the charges for space and services in the non-commissionable market segment and that those "local" customers who get their services elsewhere than from Tele-Direct (for example, by using a consultant) or do not need any or some of the services, do not pay less or get a discount off the total price of their advertising. The Director submits that the effect of this is that "local" customers must buy space and services together from Tele-Direct; it is only economically viable to purchase services separately from an independent provider in the commissionable market. To do so in the non-commissionable market would require the customer to pay twice for services, once to Tele-Direct as part of the bundled price and once to the independent service provider that would actually provide the services. The Director argues that the effect of this is that it is either a "requirement" that both space and services be acquired from Tele-Direct or, perhaps the better fit on the facts, a compelling "inducement" to do so.

The Director points to evidence of the advertisers that recognize that if they use an independent service provider when commission is not available they will, in effect, be paying twice for services and this is why they stay with Tele-Direct despite dissatisfaction with the quality of service. Further, the Director emphasizes that Tele-Direct itself knew the value of this economic inducement and used claims that its services were "free" or included in the cost of the space to convince customers to choose its services.

The respondents advance a number of arguments relevant to the question of whether space and services are indeed tied together on the facts of this case. They argue that there is no "condition" involved because there is no contractual obligation to purchase services from Tele-Direct as local customers are free to acquire services from a CMR; however, Tele-Direct will not pay a commission on the account. They rely on the case of *Ortho Diagnostic Systems, Inc. v. Abbott Laboratories, Inc.*[207] for the proposition that it is not an antitrust violation to sell components as a package where the same items can be purchased separately but at greater cost. They argue that there are no *more favourable* terms and conditions offered to customers that take Tele-Direct's services over those that do not because there is only one set of terms and conditions in the local market -- the bundle.

We see no reason to conclude that the references in the section to "conditions" or even "terms and conditions" require that these be embodied in an explicit contractual document. As we understand this requirement, it is to determine that customers are effectively forced or coerced to take the two products, which have been determined to be separate products, from the supplier of the tying product rather than acquiring only the tying product from that source and getting the tied product from someone else. This obviously can occur where there is an explicit contractual requirement to that effect. It may, however, also be equally present where there is a discount or other advantage that constitutes an inducement to acquire the two from the same source. The "conditions" or coercion referred to in the section mean more than contractual terms; they may be economic conditions which have the effect of precluding choice of supplier. Whether customers actually do have an effective choice or not is a question of fact to be determined on the evidence before us, not of the legal nature of the purchase arrangement.

[207] 1993-1 Trade Cas. (CCH) ¶ 70,266 (S.D.N.Y. 1993).

The *Ortho* case is of no assistance to the respondents. The case involved an application for a preliminary injunction by Ortho to prevent the implementation of a contract between the Council of Community Blood Centers and Abbott for a number of blood tests. Ortho alleged both monopoly leveraging and tying based on the theory that Abbott's pricing of various "packages" of blood tests forced any rational buyer to purchase all five tests from Abbott rather than buying one or more tests from competing suppliers like Ortho. The preliminary injunction was denied on the basis that Ortho had shown no irreparable harm.

The passages quoted to us by the respondents were simply the Court's summary of Abbott's arguments and authorities on the monopoly leveraging point.[208] The Court stated that Abbott's arguments gave it "pause" but all that it concluded in the end was that Ortho had shown that there were sufficiently serious questions on the merits to warrant litigation. On the tying claim, the Court, in fact, noted:

> There is some case law to support the position that a tie does not have to be explicit but can instead be inferred from the pricing structure of two products and the market power which the party has. . . .
>
> Absent an explicit condition in the contract, there is a question of fact for the fact-finder regarding the existence of the tie, and we are unable on this state of the record to determine if plaintiff is likely to prevail on the merits of the tying claims. What is evident however is that there are sufficiently serious questions going to the merits of the tying claim to make them a fair ground for litigation.[209]

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[208] *Ibid* at 70,333.

[209] *Ibid*. at 70,334.

Therefore, the relevant question for us is whether, on the facts before us, the customers of Tele-Direct were "forced" to acquire services from it or did they have the option of acquiring space alone from Tele-Direct. We conclude that the evidence of the advertiser witnesses and Tele-Direct's own behaviour amply support the position of the Director that the lack of commission in the "local" market operated as a powerful inducement to acquire both space and services from Tele-Direct.

F. SUBSTANTIAL LESSENING OF COMPETITION

Has the extent of the exclusion resulting from Tele-Direct's limitation of commission to "national accounts" as defined in the 1993 rule resulted in, or is it likely to result in, a substantial lessening of competition? It is first necessary to establish the relevant comparator that should be employed in evaluating the magnitude of the lessening involved. There is no purpose in comparing the six to eight-market accounts with all other accounts that are currently bundled and that we have decided may remain that way because demand characteristics and likely efficiency comparisons dictate a single product. The most relevant comparator is the size of the existing commissionable market under the 1993 definition because we are considering expanding that market. Eight-market accounts are currently commissionable but this could be discontinued at any moment without an order of the Tribunal so we include eight-market accounts as part of the tied portion of the market to evaluate substantiality. Further, grandfathering currently prevents accounts from "growing into" eight-market status.

In a word, it is clear that six to eight-market accounts constitute an appreciable volume of business that, without the tying practice, would be available for agents to service. The largest constituent is currently grandfathered eight-market accounts. In addition, there are the six and seven-market accounts now serviced exclusively by Tele-Direct. Based on the Tele-Direct documentation prepared in anticipation of the 1993 rule change and the evidence of Mr. Mitchell, both of which are far from being completely clear, we find that a fair approximation of the value of accounts which are now commissionable under the 1993 definition (thus, excluding grandfathered accounts and including "national" accounts serviced both by Tele-Direct and agents) is about $30 million. Our best estimate of the accounts which have been found to be tied, namely six, seven and eight-market accounts, and would be added to the commissionable market is about $19 million. Thus, the combined total of the accounts found to be tied adds up to well in excess of 50 percent of the current commissionable market. Both in relative and absolute dollar terms, the amount of revenue affected by the tie is undoubtedly sufficient to conclude that there is a substantial lessening of competition.

A final issue arises with respect to substantial lessening. The respondents advance in their written argument a "technical" argument based on the use of definite and indefinite articles in subsection 77(2). They submit that the substantial lessening of competition must be assessed in the market for the tying product, here the market for the supply of advertising space: has the tying of space and services impeded entry into or expansion of a firm or had any other exclusionary effect in the space market? This argument was not referred to orally.

While the definite and indefinite articles can be read in different ways, the section should be read in a way that makes sense. Since tying generally, and certainly in this case, involves "leveraging" from the tying product market to the tied product market, it is only sensible to assess the effects of the practice, or the substantial lessening of competition, in the target or tied product market.

G. REMEDY

Section 77 of the Act provides that upon a finding by the Tribunal of tied selling by the supplier of the tying product (Tele-Direct), the Tribunal may make an order "prohibiting [the supplier] from continuing to engage in . . . tied selling. . . ."

Prohibiting Tele-Direct from continuing to engage in tied selling means that the tying product, advertising space, and the tied product, advertising services for six, seven and eight-market accounts, must be unbundled by Tele-Direct. The "unbundling" may take the form of separate prices: Tele-Direct could quote separate rates for space and services. It may also take the form of an expanded definition of commissionable accounts to allow six, seven and eight-market customers to use the services of an agent, who would earn commission at an appropriate rate.

While we do not rule out the possibility of advertisers acquiring space from Tele-Direct (at the separately quoted space price) and then paying a separate fee for services to Tele-Direct or to an agent, we think this scenario is unlikely. There are practical implications arising from Tele-Direct's predominance in the publishing market and the accreditation of agents that suggest that the marketplace in an "unbundled" environment after our order will work largely the same as it does today except that the commissionable market will be expanded to cover six, seven and eight-market accounts. Advertisers that wish to utilize Tele-Direct's services would continue to buy space and services from Tele-Direct at one price.

Because of the specialized nature of the Yellow Pages industry, the respondents regard accreditation as important and the Director and his witnesses, for example, Ms. McIlroy and Professor Slade, support it. Thus, Tele-Direct would be justified in requiring that services, including the placement of orders, be provided by accredited service providers only. Unbundling does not require that advertisers be given the opportunity to interface directly with Tele-Direct to place their orders, if they do not wish to utilize Tele-Direct's services. Advertisers would either deal with Tele-Direct for space and services or with an agent for services and, through an agent, with Tele-Direct for space. This contributes to our view that in all likelihood, the structural arrangement that exists today would likely continue, changed only to permit agents to compete with Tele-Direct to provide services to six, seven and eight-market accounts.

The prohibition on tying, however, does not carry with it a requirement that Tele-Direct pay a specified commission to agents. It will be up to Tele-Direct to pay such commission as it chooses. Commission rates could be identical for all accounts or might be variable. However, the prohibition on tying implies that the price charged by Tele-Direct for its space and services together cannot, in relation to the price at which it offers space to customers using agents (i.e., its price for both space and services together less the commission to the agent) be an inducement to customers' using Tele-Direct's services rather than agents, thus continuing the tie. In other words, the price for space to customers of agents cannot be artificially inflated (or the commission paid to agents artificially reduced) so that space is not realistically available separately. Tele-Direct cannot make it economically non-viable for customers to purchase space from Tele-Direct and use an agent's services because in those circumstances the space effectively costs more than if the customer were to use Tele-Direct's services.

The intervenor agents (and the Director in the alternative) submit that the Tribunal should order Tele-Direct to pay a minimum 15 percent commission to agents. Although this proposition was advanced in the context of the Tribunal finding a tie across the entire market for Yellow Pages advertising in Tele-Direct's directories, in the context of our finding that there is only tying down to the six-market level, the minimum 15 percent commission would apply in respect of six, seven or eight-market customers serviced by agents. We have no difficulty with Tele-Direct voluntarily complying with our order prohibiting tying by paying a minimum 15 percent commission. A 15 percent commission rate has historical precedent and is well accepted in the advertising industry. It appears to be a workable "average" that would be simpler to administer than variable commission rates for each of the six, seven and eight-market accounts, should Tele-Direct choose to use it.

However, the setting of a commission rate by the Tribunal is not, in our opinion, envisioned in the powers given to it under section 77 of the Act regarding tying or in the general jurisdiction given to the Tribunal under section 8 of the *Competition Tribunal Act*.[210] The Tribunal is not a rate-setting body. The implication of rate-setting is an ongoing regulatory oversight which is the antithesis of the objectives of competition policy. To grant this remedy, the Tribunal would be required to hold itself open to revision to the 15 percent rate. We could not saddle Tele-Direct or the agents with a rate cast in stone forever and the alternative of ongoing rate regulation is, in our view, simply not part of the mandate of the Tribunal. It is true that the Tribunal issued the Consent Order providing for a 25 percent commission on national accounts, but that order was for a limited time and was on consent. It provides no justification for a gearing up of a general regulatory process implied by setting a rate for an indefinite period in this contested proceeding.

The Tribunal's order will therefore provide that Tele-Direct is prohibited from tying its advertising services to advertising space for six, seven and eight-market accounts. Should Tele-Direct choose to comply with the order by a commission arrangement with accredited agents at a minimum rate of 15 percent, the Tribunal would find such an arrangement acceptable compliance. Otherwise, Tele-Direct can price space and services separately or implement a commission arrangement for six, seven and eight-market accounts at an appropriate level or levels. The price Tele-Direct charges for its bundle of space and services, if it continues to offer them as a package, in relation to the price that it charges for space separately cannot be such that

[210] R.S.C. 1985 (2d Supp.), c. 19.

it continues to tie space to services by way of an inducement offered to customers that take Tele-Direct's services. The order will specify that the parties may apply to the Tribunal for interpretation of the order or directions if they consider it necessary to ensure compliance.

IX. ABUSE OF DOMINANT POSITION

A. INTRODUCTION

For ease of reference, we set out again subsection 79 (1) of the Act, which deals with abuse of dominant position:

> Where, on application by the Director, the Tribunal finds that
> (*a*) one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,
> (*b*) that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and
> (*c*) the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market,
> the Tribunal may make an order prohibiting all or any of those persons from engaging in that practice.

Unlike previous abuse of dominance applications that have come before the Tribunal, where only one market was at issue, the Director here is putting forward two abuse of dominance cases, one involving the alleged market for the supply of advertising space and the second, the alleged market for the supply of advertising services.

One case is that the respondents have market power in the market for the supply of telephone directory advertising space, or publishing, and have engaged in a practice of anti-competitive acts which has resulted in a substantial lessening of competition in that market. This case involves the responses of the respondents to the instances of new entry by competing broadly-scoped publishers in local markets, most significantly the entry of White in the Niagara region and the entry of DSP in Sault Ste. Marie.

The second case is that the respondents have market power in the market for the supply of telephone directory advertising services or, in the alternative, that they are leveraging their market power in the space market into the services market, and have engaged in a practice of anti-competitive acts which have resulted in a substantial lessening of competition in the services market. Among the anti-competitive acts alleged to form a practice affecting this market are both acts directed at agents and acts directed at consultants. For example, one of the alleged anti-competitive acts is the bundling of space and services (restricted commissionability rules for agents) which forms the basis of the tying portion of the Director's application. Another is the alleged refusal by Tele-Direct to deal with consultants.

B. APPROACH TO SECTION 79 ANALYSIS

In dealing with the particular allegations in this case, the purpose of section 79 must be kept in mind. Neither party disputed that section 79 is not intended to condemn a firm merely for having market power. Instead, it is directed at ensuring that dominant firms compete with other firms on merit and not through abusing their market power.[211] Such abuse includes, as pointed out by the Director, entrenchment and extension of market power.[212] It would not be in the public interest to prevent or hamper even dominant firms in an effort to compete on the merits. Competition, even "tough" competition, is not to be enjoined by the Tribunal but rather only anti-competitive conduct. Unfortunately, distinguishing between competition on the merits and anti-competitive conduct, as the Tribunal has noted in the past, is not an easy task.[213]

The Tribunal established in *NutraSweet* that the list of anti-competitive acts set out in section 78 is not exhaustive. The Tribunal held that the common feature of the acts included in section 78 is that they are all performed for a "purpose", namely "an intended negative effect on a competitor that is predatory, exclusionary or disciplinary."[214] The Tribunal's approach to assessing whether acts are anti-competitive was set out most recently in *D & B*:

> . . . in evaluating whether allegedly anti-competitive acts fall within section 78, the Tribunal must determine the "nature and purpose of the acts which are alleged to be anti-competitive and the effect that they have or may have on the relevant market". The required analysis will take into account the commercial interests of both parties to the conduct in question and the resulting restriction on competition. The decision in *Laidlaw* makes it clear that, although such proof may be possible in a particular case, it is not necessary for the Director to prove subjective intent to restrict competition in the relevant market on the part of a respondent. The respondent will be deemed to intend the effects of its actions.[215] (references omitted)

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[211] Consumer and Corporate Affairs Canada, *Competition Law Amendments: A Guide* (Supply and Services Canada, December 1985).

[212] *NutraSweet, supra* note 4 at 47.

[213] *Laidlaw, supra* note 33 at 333.

[214] *NutraSweet, supra* note 4 at 34.

[215] *D & B, supra* note 31 at 257.

The Tribunal must determine the "purpose" of the act that is alleged to be anti-competitive. "Purpose" is used in this context in a broader sense than merely subjective intent on the part of the respondent. As counsel for the Director pointed out, it might be more apt to speak of the overall character of the act in question.

What the Tribunal must decide is whether, once all relevant factors have been taken into account and weighed, the act in question is, on balance, "exclusionary, predatory or disciplinary". Relevant factors include evidence of the effects of the act, of any business justification and of subjective intent which, while not necessary, may be informative in assessing the totality of the evidence. A "business justification" must be a "credible efficiency or pro-competitive" business justification for the act in issue.[216] Further, the business justification must be weighed "in light of any anti-competitive effects to establish the overriding purpose"[217] of the challenged act:

> . . . The mere proof of *some* legitimate business purpose would be, however, hardly sufficient to support a finding that there is no anti-competitive act. All known factors must be taken into account in assessing the nature and purpose of the acts alleged to be anti-competitive.[218]

In their argument, the respondents advance several propositions regarding the nature of an anti-competitive act that they submit the Tribunal must determine as a matter of law in this case. One of these propositions is particularly relevant to the case relating to the publishing

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[216] *Ibid.* at 261.

[217] *Ibid.* at 262.

[218] *Ibid.* at 265.

market. They state that certain acts constitute "competition on the merits" and cannot ever be anti-competitive acts. In another formulation, they state that objectively competitive conduct cannot constitute an anti-competitive act. They would define "objectively competitive" conduct as conduct which a non-dominant firm would have undertaken in similar circumstances.[219] Applying this argument to the specific case of the allegations involving the publishing market, the respondents say that the Director cannot allege, for example, that "zero price increases" are an anti-competitive act because competitive firms sometimes use zero price increases or even price decreases to compete.

We do not take issue with the proposition that section 79 is not intended to prevent dominant firms from competing on the merits. We do, however, doubt that it is possible to define, in the abstract, a list of acts that are "objectively competitive" and that could never, therefore, engage section 79. Competition on price is surely one of the hallmarks of a competitive market. Yet even the act of "price cutting" cannot be given absolute immunity from review under section 79 because of the possibility of predation. In our view, a case-by-case, factual analysis will always be necessary to determine if, in the particular circumstances, an act is anti-competitive. All the relevant factors must be weighed in deciding whether a particular act is, in the circumstances, competition on the merits or an anti-competitive act. That question cannot be answered as a matter of law in a vacuum.

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219 They rely mainly on *Clear Communications Ltd. v. Telecom Corp. of New Zealand* (1994), 174 N.R. 266 (P.C.).

C. MARKET FOR ADVERTISING SPACE - PUBLISHING

(1) Facts

The independent publishers DSP and White have already been discussed at various places in these reasons, largely in chapter "VII. Control: Market Power". We summarize here and add some further relevant facts.

Since 1993, DSP has produced a white pages and classified directory covering Sault Ste. Marie, Elliot Lake and Wawa in northwestern Ontario. Since January 1994, it has been a division of Southam Inc. but is still operated largely independently from the Southam newspapers in the area in question. Tele-Direct publishes three separate directories for the areas covered by the DSP directory.

The DSP Canadian directory is combined with a corresponding directory for the Sault Ste. Marie, Michigan area. The American portion is published by Noverr Publishing Inc. ("Noverr") which publishes several directories in the state of Michigan.

White publishes competing directories (Niagara Falls, St. Catharines and Fort Erie) to Tele-Direct's in the Niagara region in Canada. White also entered Canada in 1993. White is a wholly-owned subsidiary of the American company White Directory Publishers, Inc. which is a private company controlled by the Lewis family. The American company began operations in

1968 with a classified directory (yellow pages only) in the Buffalo area. A white pages directory was later added and then in the second half of the 1980s and early 1990s additional directories containing both classified and white pages were started in other areas of New York state and Pennsylvania. White's entry into Canada was followed by further expansion in the United States in 1994 and 1995, into Florida and North Carolina.

Both DSP and White first published "prototype" directories in Canada, DSP in January 1993 and White in November and December 1993.[220] DSP published its first revenue directory in November 1993. White began its canvass for its first revenue directory in late 1993 and continued in 1994. Its first revenue directory was published in late 1994.

In order to produce their directories, White and DSP had to generate subscriber listings for their white and yellow pages. As discussed earlier, despite the 1992 ruling of the CRTC, at the time of their entry DSP and White did not have commercially viable direct access to subscriber listings. They had to use the most recent Tele-Direct directories, re-key the data, verify and update each listing.

Included in the directories of White and DSP were features which were not present in the existing directories of Tele-Direct in either region, including audiotext, community pages, larger

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[220] Advertising in a prototype directory is provided free to businesses. A prototype serves to lend credibility to a new publisher's claim that it will, in fact, produce a directory and affords the publisher an opportunity to prove to advertisers the value of advertising in its directory.

size print, three-column format, postal codes and additional colour plus a free smaller size copy in addition to the regular size directory (a "mini").[221]

Less detail was provided on the other two competitive markets referred to by the Director. In October 1994, a competing directory was published in Joliette, Quebec by Les Pages Soleil, a joint venture involving the company which publishes the Locator directories in Ontario. Les Pages Soleil also feature enhancements like community pages, postal codes and only three columns per page.

In Newfoundland, a company called Unifone Files Inc. ("Unifone") intended to publish a province-wide directory called "The Big Phone Book", apparently some time in 1993 or 1994. Tele-Direct (Services) Inc. publishes seven directories in Newfoundland for Newfoundland Tel (St. John's, eastern Newfoundland (four), western Newfoundland and central Newfoundland). In addition to its broader scope, the Unifone directory was to feature larger print, community pages and a "mini" directory. As of February 1994, however, Unifone was no longer in existence and it never did publish a directory.

The two entrants for which we had evidence on this point (White and DSP) priced advertising in their directories 30 to 40 percent below Tele-Direct's rates.

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[221] DSP also included a "reverse" directory -- listings by phone number first.

Tele-Direct responded to these various entrants using a number of initiatives, including price freezes, advertiser incentive programs, advertising and promotional expenditures, and directory enhancements. Tele-Direct was also involved in litigation or threatened litigation against the entrants in Sault Ste. Marie and Niagara. Further details on these responses follow.

Tele-Direct adopted a zero percent price increase or price freeze in Sault Ste. Marie in 1993. Except for 1994, when there was a general price freeze across all of Tele-Direct's territory, prices were increased annually in the vast majority of Tele-Direct's directories outside of the competitive markets.[222] In 1995, there were zero price increases in Sault Ste. Marie, Joliette and the Niagara region. The information on the record regarding 1996 prices is that all markets were subject to a price increase, including the competitive markets.

Tele-Direct has offered advertiser incentive programs of various kinds throughout its territory at different times. The critical distinction between the programs offered in the competitive markets and those offered in other markets is that in the competitive markets the incentives were available to advertisers who *renewed or increased* their advertising whereas in the other markets only those advertisers who *increased* their level of spending were eligible.

The advertiser incentive program in Sault Ste. Marie was first offered in 1993. While originally intended as a one-year program it was extended to three years, ending in 1995.[223] In

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[222] The exceptions for Tele-Direct's directories were the neighbourhood directories and areas subject to rescoping or splitting of directories. At the request of other telcos, like Newfoundland Tel and Northern Tel, prices were also frozen in those directories in 1995.

[223] In the first year (1993), all existing advertisers renewing or purchasing advertising received the next size up or colour, if applicable, at no extra charge. In 1994, all advertisers who participated in the program in 1993 were offered the next size up free,

Niagara, a program similar to the Sault Ste. Marie advertiser incentive program was offered in 1994 and 1995. As of the hearing, no decision had been taken about proceeding to offer the program in Niagara for a third year. In Joliette, a program was offered in 1995 which provided that advertisers renewing or purchasing advertising would receive the next largest size advertisement or colour if applicable. In Newfoundland, the same program was offered in four directories in 1994. Mr. Beauséjour, Tele-Direct's Vice-president of Finance, confirmed that the program was instituted in response to the presence of Unifone.[224]

In each competitive market, Tele-Direct added a number of features to its directories that were introduced first by the entrant. Most of these features tend to be fairly standard in many American markets. For example, the enhancements used by White in its Canadian prototype are almost all standard features for it in its American markets. The features added by Tele-Direct in response are not generally used by it in its directories in other markets.

We have limited information about the Joliette and Newfoundland situations in this respect. Tele-Direct did add a community pages section to its Joliette directory. Mr. Renwicke thought that postal codes had also been added. A memorandum dated October 1993 records a

free colour or a 15 percent rebate if they renewed or increased their advertising. Those who had not participated in 1993 and new advertisers were given a 15 percent rebate. In the third and final year, the program became even more complex with different choices available to 1994 participants who were renewing depending on which option they had chosen (rebate/free size up or colour) in 1994. Non-advertisers and non-participants were again offered a 15 percent rebate as were 1994 participants who were increasing their advertising.

[224] In 1995, when Unifone was no longer present, advertisers were offered a 15 percent rebate if they increased their advertising but participants in the 1994 program could receive the rebate if they renewed their upsized or colour item.

recommendation by Tele-Direct (Services) Inc. that the Newfoundland directories contain "some enhancements starting with the central Newfoundland 1994 directory."[225]

In Sault Ste. Marie, Tele-Direct added enhancements to its directories similar to those offered by DSP, including four-colour format, postal codes, community pages and its own audiotext system (Talking Yellow Pages or "TYP"). Likewise, in Niagara Tele-Direct reacted to the entrance of White by adding enhancements similar to those of White to the Tele-Direct directories in that area. Tele-Direct did not introduce all of the enhancements included by the entrants. For example, it did not adopt larger type or distribute "mini" directories.

Some further detail is required about the audiotext system or TYP in order to understand the allegations advanced by the Director in this respect. Audiotext is an electronic technology which allows consumers with Touch-Tone phones to obtain access to audio messages which are stored on a computer. The directory publisher provides in its directory codes which can be used by consumers to gain access to the messages on topics of interest to the consumer. The provision of an audiotext service is comprised of both hardware components, the computer and satellite dish, for example, and the information lines which are fed to the satellite dish from a supplier. Depending on the information being offered, the lines are updated at regular intervals during the day, on a daily basis or on a monthly basis.

[225] Confidential exhibit CJ-87 (black vol. 14), tab 104 at 134481.

Tele-Direct introduced its first TYP in Kitchener in 1988 followed by Toronto and Quebec City that same year. Unlike the audiotext involving the provision of general information on various topics to consumers, the Kitchener and Quebec City services involved advertiser-specific information. The code was provided in the advertisement; the interested consumer could call for more detailed information regarding that supplier, for example, prices. These services were later abandoned for lack of advertiser interest; the Toronto service, which is of the general information type, is still offered. Since it first offered TYP, Tele-Direct's supplier of the information lines required has been a company called Perception Electronic Publishing ("Perception").[226] As of November 1993, Perception is owned by Brite Voice Systems.

When it entered the Sault Ste. Marie market with its prototype directory in January 1993, DSP provided an audiotext service. This was the first time such a service was offered in Sault Ste. Marie. The information supplier for DSP was Perception. During the first two months that it was offered, the DSP audiotext service was heavily used.

Tele-Direct introduced its TYP in Sault Ste. Marie in April 1993 in advance of its June 1993 directory, some three months after DSP published its prototype directory, also using Perception for its information feed. Tele-Direct used flyers to distribute the relevant codes to consumers. It was roughly at the same time as the Tele-Direct TYP were introduced that DSP began to experience deterioration in its audiotext service because the information was no longer being updated in a timely manner. DSP was in constant contact with Perception in order to get

[226] Formerly called BDR Audio Network.

the lines updated within an acceptable time frame, but with no success. The quality of DSP information feed from Perception remained poor until November 1993, which was essentially the same time that Perception was acquired by Brite Voice Systems.

Tele-Direct also engaged in large advertising campaigns in Sault Ste. Marie and Niagara. No detailed information was provided in this respect regarding the other two competitive markets. Compared with pre-entry levels virtually all of the advertising and promotional expenditures were new. In Sault Ste. Marie, Tele-Direct spent only about $50,000 on advertising in 1992 as compared to $215,000 in 1993. By 1994, expenditures had dropped back to $22,000. In Niagara, Tele-Direct spent $43,000 in 1992, $71,000 in 1993 and $28,000 in 1994.[227] In 1993, advertising expenditures in Sault Ste. Marie constituted approximately 11 percent of published revenues for that city; in 1993 in the Niagara area, advertising expenses amounted to less than one percent of published revenues.

Another circumstance relevant to the Director's allegations respecting publishers is that Tele-Direct initiated a suit against DSP in May 1993 for infringing the "walking fingers" trade-mark and Tele-Direct's copyright in the advertisements in the Tele-Direct directory with its prototype directory. In the spring of 1995, Tele-Direct notified DSP that it would also be challenging the 1994 and 1995 DSP directories. At the time of the hearing, the lawsuit had reached the stage of discoveries. A representative for Tele-Direct had been discovered and the discovery of the representative for DSP was scheduled for November 1995.

[227] Exhibit R-152.

Although no suit has been launched in relation to White, Tele-Direct made it abundantly clear to White early in 1993 that it would vigorously defend its trade-marks and its interpretation of its copyright interests arising from the advertisements in the Tele-Direct directories. In particular, Tele-Direct informed White that it could not make use of an advertiser's copy, layout or graphics as they existed in the current Tele-Direct directory in creating the first White directory.

(2) Control of a Class or Species of Business in Canada

The Tribunal has already found that the supply of telephone directory advertising constitutes a relevant product market and that the relevant geographic markets are local in nature. We have also found that Tele-Direct possesses market power in those markets. We are satisfied, therefore, that Tele-Direct has market power in the market for the supply of advertising space or the telephone directory publishing market and therefore controls the business in the relevant geographic markets.

(3) Practice of Anti-competitive Acts

(a) Allegations - Pleadings

The Director's application, as amended, says at paragraph 65 that the following acts together constitute a practice of anti-competitive acts affecting the market for advertising space, or the publishing market, which leads to a substantial lessening of competition in that market:

> . . .
>
> (g) targeting price reductions and other discounts to those markets in which entry by competing publishers has occurred or is occurring; and
>
> (h) causing, directly or indirectly, advertising agencies to refuse to place advertising in telephone directories published by competing publishers or otherwise discriminating against or causing independent advertising agencies to discriminate against competing publishers; and
> (i) making disparaging statements in regard to new market entrants.

In argument, the Director did not refer to the act set out in (i). Under the heading in the written argument, "Otherwise Discriminating between Publishers", the Director gathers evidence relating to the respondents' policy of not allowing the directories of competing publishers to count towards the 20 directory requirement of Tele-Direct's national account definition. Under the heading in the written argument, "Targeting/Raising Rivals' Costs", the Director refers to various actions by the respondents in response to entry by competing publishers in the local markets of Joliette (Quebec), Newfoundland, Niagara and Sault Ste. Marie which are alleged to constitute anti-competitive acts because of their targeted nature and intent and the degree or intensity of the response. The particular responses listed are zero price increases, incentive programs, advertising and promotional spending, directory enhancements, interfering with the DSP audiotext feed and litigation or threats of litigation.

The respondents say that the allegations involving directory enhancements, promotional spending and litigation or threats of litigation are not encompassed by the pleadings and cannot be relied on by the Director.

It is not in dispute that the evidence and the argument put forward by the Director on this issue must be supported by the pleadings, either by the specific words in the application or by reasonable inference therefrom. It is trite to say that the pleadings are intended to define the issues in dispute between the parties, to give fair notice to each party as to the case that it will have to meet and to assist the decision maker in considering and deciding the allegations that have been made. Where, as here, an argument about the scope of the application is only raised at the stage of final argument, we agree with the Director that regard may be had to interlocutory proceedings, discovery and the conduct of the hearing itself to determine what the *parties* considered were the issues raised by those pleadings. We need not restrict ourselves to the pleadings in a vacuum.

(i) Enhancements

Directory enhancements were not explicitly mentioned in the application. However, in its request for leave to intervene, White specified, in paragraph 9 of the request, those matters in issue which affected it. Item (e) reads:

> offering directory enhancements (community pages, an audio text system and postal codes) targeted to areas where competition or the threat of competition exists. . . .

As stated in the reasons of the Tribunal for granting leave to intervene, the respondents did not oppose the intervention. The respondents only objected to White being given leave to make representations with respect to certain issues which, the respondents argued, were outside the scope of the Director's application. The respondents submitted that the representations of an intervenor must be relevant to the proceedings and that relevance is defined by the parties' pleadings. The Tribunal agreed. The issues in White's intervention challenged by the respondents as being outside the scope of the application did not include item (e) "enhancements" but rather focused on six other items. The Tribunal accepted that four of the disputed six items were not supported by the application and excluded them from the purview of White's intervention.

If the respondents were genuinely of the view that the question of directory enhancements was outside the scope of the application as defined by the pleadings, then they would have challenged that part of White's intervention request. The question of what was and what was not supported by the pleadings regarding the alleged anti-competitive acts in relation to independent publishers was squarely in issue at the intervention hearing. The clear implication of the respondents' failure to challenge item (e) is that they considered that enhancements were within the pleadings.

Nothing occurred after the intervention hearing that would have led to any other conclusion. The Director requested the production of documents and conducted discovery on the question of enhancements. Eventually the relevant documents were produced, without objection.[228] The Director submits that Tele-Direct has taken this "about face" on the question of enhancements in order to provide an after-the-fact explanation for its belated production of a

[228] For a more complete discussion of this issue, see *infra* in this section on abuse of dominance in publishing under "(b) Alleged Anti-competitive Acts", "(ii) Targeting/Raising Rivals' Costs".

boxful of relevant documents relating to its responses in competitive markets. The Director called evidence at the hearing on enhancements, without objection. The respondents themselves led evidence on the question of enhancements. Tele-Direct cannot now change a position that it took on an interlocutory proceeding and maintained throughout discovery, the hearing and up until the commencement of its final argument. The entire case has been conducted on the basis that directory enhancements are fairly in issue. Enhancements are properly before the Tribunal.

(ii) Advertising and Promotional Expenditures

Unlike directory enhancements, advertising and promotional expenditures were not specifically addressed at White's intervention hearing. If we looked only at the words of the pleadings, it might be arguable whether those words would support the allegation. Again, however, we have a course of conduct that sheds considerable light on whether the parties themselves thought promotional expenditures were at issue as part of the allegation of anti-competitive acts. It is clear that they did. Oral and documentary discovery was conducted by the Director on this issue. Counsel for the Director referred to it in his opening address. The Director called evidence in chief on the issue and the respondents called responding evidence. Advertising and promotional expenditures are properly before the Tribunal.

(iii) Litigation and Threatened Litigation

Counsel for the respondents pointed out that the Director was not seeking any remedy specifically relating to litigation. Counsel for the Director did not address the respondents' argument that litigation or threatened litigation falls outside the pleadings. In argument on the merits, however, the Director took the position that litigation or threats of litigation contribute to the anti-competitive act of "targeting" or "raising rivals' costs".

The words of the pleadings do not obviously incorporate such a concept. The original application, at paragraph 65(h), contained a specific allegation of an anti-competitive act of "threatening or taking legal action to restrict competing suppliers of advertising space from gaining access to, or from utilizing, subscriber listing information". This allegation was later withdrawn. However, as with promotional expenditures, litigation was dealt with in the evidence and argument. In view of the specific withdrawal by the Director of the reference in the pleadings to litigation or threatened litigation, the respondents' position is somewhat stronger on this point than on the others. But, it is not necessary to decide the issue on procedural grounds. As will become apparent, we are not satisfied on the merits of the argument that litigation or threatened litigation constitute anti-competitive conduct in this case.

(b) Alleged Anti-competitive Acts

(i) Causing Agencies to Refuse to Place Advertising with Independents

The independent publishers' directories do not count towards the 20-directory requirement that forms part of the 1993 definition of a Tele-Direct commissionable account. The Director argues that the effect of the Tele-Direct policy in this regard is that CMRs do not recommend independent directories to advertisers when they would do so if those directories counted towards qualification as a commissionable account. Thus, it is submitted, this excludes independents from revenues that they would otherwise obtain.

The Director relies on the evidence of Mr. Lewis of White comparing the situation in Canada with respect to advertising placed in his directories by CMRs to that in the United States. In distinction to Tele-Direct's policy, in the United States publishers include the directory of any other YPPA member in determining whether an account qualifies for commission. White is a YPPA member and therefore its directories count towards the minimum directory requirement in the United States. Mr. Lewis testified that in that country eight percent of White's advertising revenues are placed by CMRs while in Canada less than one-half of one percent comes from CMRs.

The respondents respond that this testimony alone does not constitute proof of the requisite exclusionary effect. Because White has been operating in the United States for a lot longer, and is therefore more established than it is in Canada, they question the validity of the comparison being made. Further, they rely on the evidence of Stephanie Crammond of Media Nexus, a specialized Yellow Pages advertising agency, that if she had confidence in the distribution figures cited by the various independents, she would consider them. Likewise, Richard Clark of DAC stated that his position on independent directories was to "wait and see" if they were going to stay around and then base a decision on which directory had greater usage. He did point out that typically the telco directory has the greater usage and, therefore, if a competing directory is used, generally it is on a secondary basis, with the primary advertising dollars allocated to the telco directory.

On balance, we are not persuaded by the Director's argument. While we recognize that monetary incentives are bound to enter into an agency's recommendation to a client, the Director's argument implies that agencies are entirely driven by earning commission and will compromise the quality of the advice they give by omitting to recommend a good, independent directory merely because it would not help the account qualify for a Tele-Direct commission. The burden of the remainder of the Director's case, as it involves agencies, is that they are, among other things, independent suppliers of advice to advertisers and therefore provide a valuable alternative to Tele-Direct's captive salesforce. For the Director to suggest now that agencies would not provide good advice seems to be somewhat inconsistent with that position. But apart from this, the independents, of course, pay their own commission on advertising placed in their directories.

There are factors at play other than Tele-Direct's criteria in agents' decisions when recommending directories to their clients. As Mr. Clark's testimony indicates, an important reason why independent publishers in Canada may not receive a high volume of business from agencies is that, because Tele-Direct is the established publisher, it is rarely a choice *between* Tele-Direct's directory and the independent directory for a particular area. Rather, the agency will generally recommend the Tele-Direct directory as the primary directory for advertising because of widespread usage and then, if additional money is available, recommend the independent *also*.

In summary, we do not accept that Tele-Direct's policy regarding the 20-directory requirement discourages agency recommendations of independent directories.

One final observation in this area arises from the respondents' written argument at paragraph 590, that as a matter of law "[i]t cannot be an anti-competitive act for a dominant firm to decline to assist or give aid to a competitor." We agree with the general proposition that a firm is not, and should not be, required to "assist" its competitors. The respondents, however, add an additional element to the proposition when they submit that:

> Each of the anti-competitive acts listed in section 78 require the dominant firm to *actively initiate* some action. . . . None of the listed acts are triggered simply by the dominant firm *not doing something or refusing to assist*. . . . (emphasis added)

While the respondents did not advance this argument in relation to the specific allegation we are dealing with here (or, in fact, in relation to any specific allegation), it certainly seems relevant to the question of whether Tele-Direct should be obliged to recognize advertising in independent directories as counting towards Tele-Direct's commissionability requirement of a minimum of 20 directories. As stated above, as a general proposition, competitors should not be required to assist one another. But, this general proposition may be shown to be inapplicable in a given section 79 case by the Director proving that the "act" of the respondent meets the elements of that section and is an anti-competitive act leading to a substantial lessening of competition.

Then, any order of the Tribunal which may issue is, by definition, not an order to "assist" a competitor but rather, in the case of subsection 79(1), an order to cease and desist from anti-competitive conduct.

It is, therefore, not sufficient, in circumstances such as these, to argue the general proposition. Nothing can be determined by simply labelling the alleged anti-competitive "act" as "doing something" (active) or "not doing something" (passive). The anti-competitive effect of the conduct of the respondents, whether "active" or "passive", must be weighed against any business justification in order to conclude whether there has or has not been a substantial lessening of competition. That can only be done by reference to the evidence. On this point, Tele-Direct only argued the general proposition.

(ii) Targeting/Raising Rivals' Costs

Reaction of Tele-Direct

Before turning to the evidence it is necessary to consider what the Director means when he alleges that "targeting/raising rivals' costs" is an anti-competitive act. There is a growing body of literature dealing with "raising rivals' costs" ("RRC"). The theory was proposed as a similar but more credible route to market power than predatory pricing because it does not depend on short-term price cutting beyond what is profit-maximizing followed by later recoupment. With RRC, it is not necessary to cause the rivals to exit, no "deep pockets" are necessary and the additional profits are gained immediately.[229] Typically, an RRC strategy involves increasing rivals' costs by raising the price of some scarce input which in turn results in the rival reducing its output.[230] In other words, there is a relatively immediate output reduction in the market concerned. Only two elements of the act alleged by the Director seem to bear any resemblance to this conception of RRC -- the audiotext affair and litigation and threats of litigation. As we shall see, the remaining actions of Tele-Direct relating to pricing, incentives and advertising did not result in output reduction in the markets in question. The considerations involved in RRC can provide little assistance in evaluating the allegations relating to those reactions of Tele-Direct in competitive markets or the "targeting" aspect of this act.

The Director has not attempted to explain what is meant by targeting in any detail, perhaps regarding the term as largely self-explanatory. It is, however, far from being a household word in competition law. While we have no reason to discourage novel approaches to discerning potentially anti-competitive conduct that might fall within section 79, we do see considerable difficulty in applying the targeting concept. It is always difficult to distinguish between anti-competitive practices and normal competition. The conduct in question may be generally benign and it is only in certain contexts that it is anti-competitive. The difficulty is even more pronounced in this case, given the actions on the part of Tele-Direct that the Director would have the Tribunal, if not prohibit completely, certainly restrict.

[229] T.G. Krattenmaker & S.C. Salop, "Competition and Cooperation in the Market for Exclusionary Rights" (1986) 76:2 Amer. Econ. Rev. 109.

[230] D.T. Scheffman, "The Application of Raising Rivals' Costs Theory to Antitrust" (1992) 37 Antitrust Bulletin 187.

In argument counsel for the Director described the nature of targeting as follows:

> The reason that acts of predation or near-predation can be anti-competitive is because the firm is dominant in a larger market. The danger is that, rather than bringing the public the benefit of competition in a limited area, what is happening is that in the long-term analysis the dominant firm is leveraging its market power from its broadly-dominated market into specific targeted areas where competition enters, with a view to either eliminate that competition entirely or, as in the situation here where the expressed intent fell a bit short of that, to ensure that the competition didn't move into any other markets and to raise their costs so that those companies would know that it was not going to be a profitable enterprise to continue their expansion.
>
> What we are suggesting is that this is really a test of degree, that we have in at least one of the markets evidence which is very close to predation. What we have is such a tightly focused and overwhelming marshalling of the dominant resources of the company to these targeted areas that there is a need for a remedy.
>
> . . .
>
> . . . While one may formulate various tests that would have different requirements in terms of the super-normal targeted response, this is probably the clearest case imaginable in terms of the absolutely overwhelmingly aggressive nature of the response to these targeted markets.[231]

Counsel clarified that "leveraging" in this context means the use of monopoly rents from other markets to subsidize near-predatory behaviour in the markets in question.[232]

One of the ordinary meanings of the word "target" is

> anything that is fired at or made an objective of warlike operations . . . [233]

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[231] Transcript at 64:13167-68, 13170 (16 February 1996).

[232] *Ibid.* at 13169.

[233] *The Concise Oxford Dictionary*, 7th ed. (Oxford: Clarendon Press) at 1094.

In one obvious sense, therefore, "targeting" simply refers to focused or aimed rather than general responses. The facts show that Tele-Direct behaved differently in the competitive markets. If the Director is arguing that the actions of Tele-Direct constitute the anti-competitive act of targeting merely because its actions in markets in which broadly-scoped entry was occurring were different from those in markets where no such entry had occurred, we do not accept the argument. Targeting cannot be distinguished as an anti-competitive act merely by the fact that there is a differentiated response. Targeting, in the sense of a differentiated response to competitors, is a decidedly normal competitive reaction. An incumbent can be expected to behave differently where it faces entry than where it does not. One competes where there is competition. Similarly there may be gradations of reaction depending on the nature of the competitive threats.

The earlier discussion regarding market power established that, whereas the broadly-scoped directories published by entrants in the "targeted" markets were considered by Tele-Direct as competition for its own directories, the same was not true of other publishers who sought market niches defined by geography or other specific characteristics of their intended audience (e.g., ethnic, religious, easy to read directories). Furthermore, both White and DSP introduced features into their directories such as postal codes, information about cultural events, coupons, etc., that provide value to users that could affect whether the Tele-Direct directories would be retained by telephone subscribers in those markets if Tele-Direct did nothing.

If "targeting" does not depend solely on differentiated responses, how is it to be distinguished from competition on the merits? We do not take the Director to be proposing that an incumbent, even one with a dominant market position, is precluded from responding to entry. Entry would obviously be *encouraged* if the incumbent accommodated the entrant. It is, however, doubtful that anyone would suggest that this is a desirable competitive outcome. Anything short of accommodation is likely to make the post-entry prospects of an entrant less attractive than the pre-entry benefits enjoyed by the incumbent. It is, therefore, not enough for us to find that Tele-Direct's responses made entry less attractive.

Indeed, the Director's position seems to be that a firm is free to act to discourage entry but that there is a limit to what it may do. This is reflected in the Director's proposed remedy, which would allow Tele-Direct to use two out of three of price reductions or discounts, enhancements and an advertising campaign in individual markets.[234] Once the incumbent passes this critical threshold, it is submitted that it has moved into the realm of anti-competitive conduct. The reasoning behind this, as we understand it, is that while what has been done in the particular markets may not be particularly harmful, the long-term harm caused by discouraging future entry outweighs any immediate benefit. In other words, the response in the markets where entry occurs is part of an effort to discourage entry into other markets by behaving in a fashion which is nearly, but not necessarily, predatory in the strict sense in which that word is usually used.

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[234] Tele-Direct would be unrestricted in its responses if it implemented those responses throughout its territory.

In support of the position that Tele-Direct's response went beyond what is "normal", the Director relies on its expressions of corporate intent, the number, variety and degree of its responses and the intensity of those responses. As a standard for assessing how far Tele-Direct went the Director submits that we can look to the evidence that its response in Sault Ste. Marie caused Tele-Direct to incur losses, a comparison to the experience of independent entrants in American markets, and the difference between White's and DSP's expectations and their actual results and their future plans.

Counsel for the Director also suggests that Tele-Direct is using its monopoly rents from other markets to cross-subsidize its responses in competitive markets. This possible meaning of targeting would only apply, however, where the dominant firm is incurring losses in the targeted market. However, the Director does not appear to be suggesting that this is a necessary condition for the Tribunal to find that "targeting" is an anti-competitive act in this case.

First, we will examine the question whether what Tele-Direct did in the competitive markets was generally of benefit to consumers (advertisers) in those markets, largely neutral or, in fact, harmful. While Tele-Direct's actions clearly made it more expensive for the entrants than if it had accommodated them, seizing market share from a rival by offering a better product or lower prices is not, in general, exclusionary since consumers in the markets concerned are made better off. The Director has not attempted to argue that Tele-Direct's responses caused harm to advertisers in the particular markets in which entry occurred. The Director did, however, submit that at least some of Tele-Direct's actions were of negligible or temporary benefit to those advertisers.

With respect to the zero price increases, there is no question that advertisers benefitted from this initiative. The evidence indicates that the advertiser incentive program in competitive markets was carefully designed to absorb customers' directory advertising budgets so that little would be left for the new entrants when they canvassed for paid advertising. Yet, it is difficult to conclude that these programs did not benefit advertisers, particularly when rebates were involved. Making its directories more attractive by adding enhancements and increased advertising by Tele-Direct would both tend to increase usage of telephone directories and, thus, benefit advertisers in those markets. There was evidence that some of the enhancements to Tele-Direct's directories were viewed by the company as temporary expedients. For example, the postal code feature in Niagara was designed to be easily removable.[235] Nevertheless, as no evidence was brought to our attention indicating actual removal of the postal code section, we can only conclude it has been maintained by Tele-Direct. Further, although the Director argued that much of Tele-Direct's advertising was "negative" advertising which only disparaged its competitors, we do not have enough information on the advertising campaign to be in a position to identify which portions were "negative" and if the negative outweighed the positive. Overall, the inescapable conclusion is that Tele-Direct's responses to entry resulted in an improvement for advertisers in the "targeted" markets.

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[235] Mr. Bourke wrote to Mr. Renwicke stating that postal codes should be left as a section rather than integrated as part of the listing (as White had done), otherwise "we'll [n]ever get rid of it": confidential exhibit CJ-86 (black vol. 13), tab 101 at 134297.

What, then, about the likelihood of harm in Tele-Direct's territory as a whole because of the effect of these responses on future entry or expansion? There is evidence that Tele-Direct was not solely concerned with "meeting" competition in Sault Ste. Marie and Niagara. Tele-Direct also feared further entry into other areas, particularly from DSP which was associated with Southam and had the advantage of having local connections and organization through the publisher's newspapers. This is clear from the evidence of Ms. McIlroy, who was in a key position as Vice-president of Marketing at that time.

Ms. McIlroy testified that Tele-Direct designed its strategies first around the Sault Ste. Marie situation and then replicated them in Niagara when White appeared. She confirmed that one of her objectives in Sault Ste. Marie, as set out in document recording her notes for a presentation, was to "limit Southam motivation to continue Yellow Pages roll-out in Ontario".[236] She further explained that as a "counter-strategy", if Southam's intention to enter directory publishing was a long-term, well-funded strategy, then her second objective was to "make the cost of carrying on business against [Tele-Direct] market-by-market exceptionally high."[237]

But those were not the sole objectives. Ms. McIlroy also described Tele-Direct's strategy in the following terms:

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[236] Confidential exhibit CJ-33 (black vol. 12), tab 88 at 133221A.

[237] Transcript at 21:4088-89 (17 October 1995).

> . . . the basic premise was to make it expensive for the competitor to compete with us and to focus on doing everything and doing it right in the Sault, putting whatever investments or resources that was necessary to avoid unnecessary market share [loss] and to protect our interest in that market.[238]

Similarly, in a presentation that she made to her fellow officers she set out the following points as constituting Tele-Direct's "challenge":

> • Protect usage and awareness - promotion
>
> • Add value to advertiser - incentive
>
> • Add value to user - product enhancements
> - size and colour
>
> • Sustain leadership profile
>
> • Compete on value vs. cost
>
> • *Make competition an expensive proposition*[239] (emphasis added)

Mr. Renwicke disputed whether the last point was ever accepted as corporate policy, but in matters of dispute between Ms. McIlroy and her fellow officers we accept her evidence. She left Tele-Direct on good terms and she has no discernible reason for colouring her evidence, particularly as she was the officer responsible for preparing tactics that the Director would have us label as anti-competitive.

It is only the reference to making competition "expensive" as part of Tele-Direct's strategy that raises any question of anti-competitive motivation. It is doubtful that Tele-Direct could make competition expensive without negatively affecting its own profitability. According

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238 Transcript at 20:3918-19 (16 October 1995).

239 Confidential exhibit CJ-33 (black vol. 12), tab 88 at 133316.

to Ms. McIlroy the participants at the officers' meeting were taken aback at the cost to the company of making it expensive for the competition. They agreed to "spend what it took" with the proviso that the expenditures would be selective and the officers would be kept current on what was transpiring, even as frequently as on a weekly basis. The fact that Ms. McIlroy convinced her fellow officers to adopt a policy of making competition expensive even when doing so would be detrimental to current profits provides some indication that Tele-Direct was trying to influence its competitors' future conduct to some extent.

There is as well another consideration. The documents relating to Tele-Direct's responses in Sault Ste. Marie and Niagara were not provided during documentary discovery within the time frame ordered. They did not make their appearance until after Tele-Direct apparently learned that the Director had contacted Ms. McIlroy and that she would appear as a witness in these proceedings for the Director. Counsel for Tele-Direct attempted to blame the delay in the production of these documents on inadvertence. He said that the relevant box of documents got lost but that no one seemed to know where or why. If the documents were lost, a detailed explanation is in order especially given the controversial issue to which they pertain and that the content of some of the documents is clearly adverse to Tele-Direct's position. A vague explanation carries little weight. The belated production and inadequate explanation cause the Tribunal to make an adverse inference with respect to Tele-Direct's intentions on this issue. Tele-Direct apparently considered that it might have "gone too far" in its responses in those markets. This, along with the statements of corporate policy, provides support for the view that Tele-

Direct intended, in a subjective sense, to convey a warning about future entry as well as protecting its position in the individual markets subject to entry.

Nonetheless, the critical question is whether there is a reasonable likelihood that future entry will be discouraged by Tele-Direct's actions. If so, is that possible negative effect more compelling than the proven benefits in the individual markets from Tele-Direct's improving its product, freezing prices and increasing advertising expenditures, all of which contributed in some measure to increasing usage of telephone directories, which is generally seen as pro-competitive. A reasonable likelihood of significant long-run detriment must exist if these tactics are to be discouraged.

The Director relies to some extent on the evidence given by White and DSP, which will be canvassed below, regarding their intentions about future expansion, which he says shows that future entry and expansion *have been* deterred by Tele-Direct's behaviour. That evidence is, however, a small portion of the evidence put forward by the Director in support of his case. In effect, the Director asks us to *infer* from the "overwhelming intensity" of Tele-Direct's response in the markets where it faced entry that potential entry into other markets *will* be deterred.

Before we proceed to consider the more detailed arguments, we should indicate at the outset that we have serious reservations with respect to the overwhelming intensity approach adopted by the Director. The Director has not advanced any "objective" criteria by which the

Tribunal is to assess whether Tele-Direct's responses in the competitive markets have the overall anti-competitive character or "purpose" required for section 79.

Although the Director is not arguing that Tele-Direct's conduct was predatory, predation is certainly the closest analogy to what is put forward here. The essence of an allegation of predatory pricing is that the firm foregoes short-run revenues by cutting prices, driving out rivals and thus providing itself with the opportunity to recoup more than its short-term losses through higher profits earned in the longer term in the absence of competition. A predatory pricing allegation is difficult because, at least in the short-run, consumers apparently benefit from lower prices. In addition, predation can only succeed if the predator has greater staying power than its rivals and a reasonable prospect of recouping its losses. In order to distinguish competitive pricing action from predation, therefore, the "Areeda-Turner test" for predatory pricing[240] was developed and has been adopted by the courts.

Our difficulty here is that, unlike the predatory pricing case, no "test" or criteria of any kind were even proposed by the Director or his experts. Indeed, we acknowledge that the likelihood of being able to establish objective criteria to distinguish between harmful and beneficial conduct of the type in issue is remote. In effect, because of the absence of any criteria, the Tribunal is being asked by the Director to place itself in the shoes of a potential entrant with a view to assessing the credibility of the alleged "threat" being issued by Tele-Direct by its

[240] In brief, the essence of the test is that a price below reasonably anticipated short-run marginal costs is predatory while a price above short-run marginal costs is not. Because marginal cost data are often unavailable, average variable cost is generally used as a proxy. For a summary of the conclusions of Areeda and Turner on this topic, see *Antitrust Law*, vol. 3 (Toronto: Little, Brown, 1978) at para. 711d.

responses to entry. The Tribunal must determine whether the response in the initial markets in which entry occurred was so "overwhelmingly intense" that an entrant would be intimidated and future entry or expansion deterred.[241] What may seem to be a response of "overwhelming intensity" to one person may not to another. It is inevitably a highly subjective exercise. Decisions by the Tribunal restricting competitive action on the grounds that the action is of overwhelming intensity would send a chilling message about competition that is, in our view, not consistent with the purpose of the Act, as set forth in section 1.1. We are concerned that, in the absence of some objective test, firms can have no idea what constitutes a "competitive" versus an "anti-competitive" response when responses like those used by Tele-Direct in this case are involved (e.g., price freezing or cutting, incentives, product improvements, increased advertising).

While Tele-Direct certainly made very strong responses to entry in Niagara and Sault Ste. Marie, there is no certain way for the Tribunal to judge what magnitude of response Tele-Direct would have employed had it not been concerned, among other things, with discouraging further entry. To say that the response was greater than it otherwise would have been assumes that we can judge how much Tele-Direct would have done had it been acting competitively and that, therefore, we can determine, with reasonable assurance, to what degree the observed responses went beyond that and became anti-competitive. In trying to make this comparison urged upon us by the Director, it must be recognized that Tele-Direct was facing pretty stiff competition from

[241] There would evidently be little point in the incumbent pursuing an aggressive course of responses in every market subject to entry solely to make an impression or deliver a threat since that strategy would have already been defeated. If there was widespread response by the incumbent in all markets in which entry occurred or was threatened, consumers would benefit in the short-term with no discernible long-term negative effects.

the new entrants. The entrants' publications were initially superior with respect to features and they were priced up to 40 percent below Tele-Direct. While Tele-Direct's expenditures on advertising and promotion constituted a sea change from its previous expenditures, DSP spent more over the three years from 1992 to 1994 than Tele-Direct did, including large amounts in the local Southam newspaper.

The Director makes two broad arguments in support of the position that Tele-Direct's actions went beyond "normal" competition and, taken together, constitute anti-competitive acts. The first is that Tele-Direct's "bottom line" results in Sault Ste. Marie in 1993 reveal that Tele-Direct barely broke even in that market when the cost of introducing the improvements to the directory and the advertising and promotional expenditures are taken into account. This conclusion was not disputed by Mr. Beauséjour who agreed that the results shown were "very close to breakeven".

The analysis presented to the witness, however, included the payment to Bell Canada (CCS) as an "expense" deducted from revenue. When Bell and Tele-Direct are treated on an integrated basis, as we earlier found in the tying context to be appropriate when considering Tele-Direct's profitability study, it would be inaccurate to refer to Tele-Direct's results in Sault Ste. Marie as a "marginal profit" or "loss" situation. The pro-rated share of the payment to Bell would have to be added back to the Tele-Direct's results in Sault Ste. Marie. Given that the Bell payment is mostly contribution to profit and it is a substantial amount, this would move the Sault Ste. Marie results well above the breakeven point, even with the extra expenditures on enhancements and advertising. Indeed, it would appear that the payment to Bell constitutes the largest portion of the "profit" that attracts independent publishers to attempt to enter Tele-Direct's markets and which allows them to contemplate profitably pricing 30 or 40 percent below Tele-Direct. In the Niagara region, Tele-Direct earned a profit in 1993 even when the payment to Bell is treated as an expense.

The Director's second argument is that experience in the industry also demonstrates that Tele-Direct went beyond "normal" competitive responses. This includes the evidence regarding expectations of White and DSP versus their experience and their future intentions as well as evidence about how American telco publishers have responded to entry in their markets.

With respect to the experience of an American telco publisher responding to entry, Mr. Anderson, who was with NYNEX, testified in chief that when NYNEX perceived independent directory publishers as significant competition, it would make its sales force aware of their presence, possibly do more advertising, and consider the scoping of its directories and their features. He also pointed out that it had not been his experience that features would be introduced only in a competitive market. After a trial run, if the feature proved successful, it would be implemented "across the product line." In cross-examination, he admitted that NYNEX had never, at least to his knowledge, offered an incentive program similar to that used by Tele-Direct in its competitive markets in response to entry of a competing publisher. He gave the same response when asked about a specific market where, in response to entry, NYNEX might have frozen prices in specific markets in response to entry for two years, without rescoping. With respect to the remaining possibilities put to him by counsel for the Director, Mr. Anderson either had no knowledge (e.g., advertising as a separate budget item) or commented on the lack of applicability in the American context (e.g., telco publishers cannot offer audiotext, no trade-mark to protect through legal action). Without any knowledge about the marketplace in which NYNEX operates, we are unable to draw any conclusions about this evidence.

With respect to White, Mr. Lewis stated that his experience in entering markets in the United States had led him to believe that White would have larger sales in Niagara than turned out to be the case. In its first revenue year, White expected to capture between 30 and 40 percent of Tele-Direct's revenue.[242] In fact, White's revenue for its second directory (the first revenue-generating directory), published in 1994, was 17 percent of Tele-Direct's revenue. Revenue for the third directory (the 1995 directory) represented a nine percent increase from the previous year for a total of about 19 percent of Tele-Direct's revenue.

Mr. Lewis stated that his initial plans for expansion beyond the Niagara region in Canada had been put on hold indefinitely due to Tele-Direct's conduct *and* the inability to obtain complete subscriber listing information. At the time of the hearing, this matter of subscriber listings was on appeal to the federal Cabinet. Mr. Lewis also said that upon a favourable Cabinet decision on the privacy issue, he would anticipate starting a number of additional directories in the Toronto and Niagara region. Any conclusion that White was deterred from future expansion

[242] Anticipated sales are expressed as a percentage of estimated revenue of the existing directory. This does not mean that all sales are drawn from the incumbent as the demand for directory advertising is expected to increase when a second publication is introduced.

by Tele-Direct's conduct and that, therefore, that conduct passes an anti-competitive threshold would be difficult in light of this evidence and the subsequent Cabinet decision overruling the CRTC decision that was to the effect that consumers should be able to opt out of having their listing information released to independent publishers.[243]

In formulating its entry strategy, DSP factored into its business plan both the risk of legal action by Tele-Direct and the possibility of a Tele-Direct competitive reaction. DSP, erroneously as it turns out, anticipated little response from Tele-Direct based on that company virtually ignoring the entry of the Locator directories in a large number of communities. As we have discussed, the Locator directories are simply not close substitutes for Tele-Direct's directories. DSP's expectation for its first revenue-generating directory was to capture about 50 percent of Tele-Direct's revenue. In developing this estimate, DSP reviewed the American experience and consulted extensively with its joint venture partner, Noverr. Instead, the directory generated about half of the expected revenue in dollar terms. The revenues for the second revenue-generating directory, published in 1994, were once again considerably lower than expected. It was, however, anticipated that the revenues for the 1995 directory would be higher and marginally profitable.

DSP has also decided not to expand in Ontario even though that was the original plan. While Tele-Direct's conduct was said to have been the reason for that decision, the evidence

[243] For further explanation of this matter, see chapter "VII. Control: Market Power" under "A. Indirect Approach: Market Structure", "(2) Barriers to Entry", "(c) (i) Subscriber Listing Information", *supra*.

suggests that there were other reasons as well. In particular, it would appear that DSP's expectations were quite aggressive for a new business and, to some extent (in relying on the Locator experience), in error. The Director says that the Sault Ste. Marie, Michigan part of the DSP joint directory, which did not experience a response like Tele-Direct's, had been far more successful than its Ontario counterpart. However, that side of the publication also fell well short of what had been anticipated as a "normal" first year revenue, further suggesting that the DSP's expectations may not have been realistic.

We do not have enough evidence to arrive at any conclusion about the effect of Tele-Direct's actions on deterring entry or expansion in the Newfoundland and Joliette situations.

The remedy suggested by the Director changed from the application to final argument. In our view, the remedy, as currently formulated, illustrates the difficulty of dealing with "targeting" as an anti-competitive act. The notice of application, at paragraph 1(b)(xiii), requested that:

> the Respondents be prohibited from targeting price reductions and other discounts for advertising space to those markets in which entry by competing publishers has occurred or is occurring.

In oral argument, counsel for the Director explained that the remedy ultimately being requested by the Director would read as follows:

> that the respondents be prohibited for a period of five years from: (i) targeting a price, a price reduction, or other discount including any advertiser incentive program offering free colour, free size up, or a first time placement discount where there is no annual increase in advertiser spending; *and* (ii) targeting any

> directory enhancement, including audio-text service; *and* (iii) targeting any advertising campaign; to a market where entry by a competing directory publisher has occurred, is occurring, or is reasonably anticipated to occur unless such listed item is offered or applied uniformly and simultaneously by the respondents in the majority of their directory markets.

The "and" between the listed items is critical. The Director proposes that Tele-Direct be permitted to do any *one* or *two* of the three enumerated actions in any market where entry has occurred. However, if all three should be undertaken then they would have to be followed in a majority of Tele-Direct's local markets.

We recognize that the Director is likely attempting, by this compromise remedy, to recognize that Tele-Direct's responses are of benefit to consumers in the market in which they occur. This effectively highlights the difficulty of the "targeting" allegation. First, the number of competitive responses (one or two) that Tele-Direct is allowed is completely arbitrary. The Director has not provided the Tribunal with any rationale as to why one or two (but not three) responses would not be anti-competitive. Further, there is no suggestion that the Tribunal should limit the extent to which Tele-Direct could invoke the competitive responses to which it would be entitled. Yet, the Director alleges that Tele-Direct's responses in the competitive markets were anti-competitive in part *because of* their intensity and ferocity.

Considering the difficulty in circumscribing "targeting" so that it does not result in discouraging desirable competitive activity, we do not find that Tele-Direct's conduct with regard to pricing, promotion and changes to its directories in the competitive markets, in particular in the Sault Ste. Marie and Niagara areas, is anti-competitive.

Litigation or Threatened Litigation

Finally, we turn to the Director's argument that litigation or threatened litigation by Tele-Direct, when taken together with the other actions of Tele-Direct, contribute to targeting/raising rivals' costs.

The Director argues that Tele-Direct's use of litigation or threatened litigation "goes into the mix" to show intent and the excessive degree of the overall response to entry in the competitive markets. The Director does not rely on the nature of the litigation on its own. The Director does not argue, for instance, that the litigation was a "sham". "Sham" litigation, or litigation which the plaintiff knows is without foundation but uses to stifle or impair competition, can be a technique of predation.[244] In the words of Robert Bork: "As a technique for predation, sham litigation is theoretically one of the most promising."[245]

Since no argument is being made that the litigation started by Tele-Direct against DSP was "without foundation",[246] we need some other means to determine whether the litigation in question crossed the line to anti-competitive conduct. We do not consider that it is sufficient to look at the litigation only in combination with the other responses. There must be some evidence

[244] Sham litigation could include a claim with no reasonable cause of action which might be struck out at an early stage of proceedings or a claim based on facts that were untrue or otherwise not supportive of the claim, in which case, the litigation could be extensive.

[245] R.H. Bork, *The Antitrust Paradox* (New York: Basic Books, 1978) at 347.

[246] Some mention was made that the copyright claim might be a "broad" interpretation of the existing American law but that is hardly definitive.

specific to the bringing or the conduct of the litigation itself that would lead us to conclude that the purpose was to contribute to the impairment of competition over the protection of property rights.

The Director points out that while Mr. Crawford, Tele-Direct's Corporate Secretary and legal counsel, originally testified that Tele-Direct defended any unauthorized use of its trade-marks and copyrights, it became apparent on cross-examination that this was not true. Tele-Direct overlooked unauthorized use on a number of occasions. Perhaps the difficulty with this witness's credibility on this issue and the fact that litigation seems only to be taken against specific competitors do lead to the view that Tele-Direct focused on those competitors. However, that alone is not enough if the litigation is not a sham.

On the facts of this case, we cannot conclude that Tele-Direct brought, conducted or gave warnings regarding otherwise apparently valid litigation in such a manner that its purpose was clearly to contribute to the impairment of competition in those markets where entry occurred rather than the protection of its intellectual property rights. There is no evidence, for instance, of undue delay. As of the date of the hearing, DSP had not yet been discovered but a major factor in this delay was the illness of Mr. McCarthy, the intended representative for DSP. Discovery of DSP was, however, scheduled for November 1995 with Mr. Campbell for DSP. Discoveries of Tele-Direct had been completed by the date of the hearing. There is no evidence that the litigation is following any other than the "normal" course. Unlike the *Laidlaw* case, there is no evidence of responding to an apparently minor matter in a "wildly overly aggressive manner" with multiple claims or of pointed threats to put a competitor "out of business" using, in part, the pursuit of legal action for which, as the Laidlaw representative informed the competitor, a large sum of money had been reserved.[247] While Tele-Direct did not proceed against White after its warning regarding possible litigation, it is certainly plausible that it did not do so because of the similarity of the issues to the DSP case. That litigation would seem likely to settle at least the copyright question once and for all, by establishing a precedent for Tele-Direct's dealings with other publishers.

The Tribunal, therefore, cannot accept the Director's submission that litigation or threatened litigation in this case can contribute to a finding of anti-competitive acts by Tele-Direct.

Audiotext in Sault Ste. Marie

The Director alleges that Tele-Direct used its power as a major buyer to influence the supplier of audiotext information in Sault Ste. Marie, Perception, resulting in a degradation of the feed to DSP. The respondents acknowledge in their written argument that the allegation could be an anti-competitive act, if proven, but dispute that it is supported by the evidence. The critical questions are whether Tele-Direct was merely asserting its contractual rights and what responsibility, if any, can be assigned to Tele-Direct for the quality of service delivered by Perception to DSP.

[247] *Laidlaw*, *supra* note 33 at 298.

Did Tele-Direct have a contractual right to exclusivity?

The respondents state in their written argument, at paragraph 930, that "Perception recognized that Tele-Direct was entitled to the exclusive right to its only feed . . . ." This statement is not supported by the evidence. Up until January 1994, the only contract between Tele-Direct and Perception was for the Toronto area and it provided Tele-Direct with exclusive access to Perception's feed in the Toronto local calling area only. Perception had in fact refused to grant Tele-Direct exclusivity for other areas because of the limitation on its ability to market its service.

In the fall of 1992, when Tele-Direct became aware of the proposed entry into Sault Ste. Marie by DSP, including offering audiotext, Tele-Direct entered into negotiations with Perception to supply its TYP in that market. One of Tele-Direct's concerns was that the feed in Sault Ste. Marie be exclusive to it, that DSP not have access to the same feed. The evidence reveals that the parties did not, in fact, come to an agreement on exclusivity until much later. While exclusivity is mentioned in a letter in March 1993,[248] the draft contract sent by Perception to Tele-Direct in May 1993 is instructive. The letter enclosing the contract states that with "all the excitement of getting `the Soo' up and talking" Perception had neglected to send Tele-Direct the contract for Sault Ste. Marie. The contract clearly states that it is a "non-exclusive" licence to receive and store information.[249]

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[248] Confidential exhibit CJ-86 (black vol. 13), tab 96 at 134118.

[249] Draft contract and covering letter: confidential exhibit CJ-87 (black vol. 14), tab 114 at 134825-27.

The contract was never signed by Tele-Direct but nonetheless provides proof that Perception, at least, did not consider at that time that Tele-Direct had exclusive rights to its feed. They were certainly not *ad idem* in that respect. The final contract covering Sault Ste. Marie, which does provide for exclusivity, was not signed until January 1994.[250] A letter in September 1993 provides that upon acceptance of a new agreement by Tele-Direct, the "BDR Audio Network will be made available to only directory publishers in Canada and exclusively to Tele-Direct within Ontario and Quebec."[251] Peter Dolan, Director of Sales at Tele-Direct (Services) Inc., admitted, however, that Tele-Direct had to go "back and forth" with Perception a couple of times in order to get the wording regarding exclusivity re-inserted into the final contract. Tele-Direct does not appear to have had, until November 1993 at the earliest, a right to exclusivity with Perception and, therefore, had no right to insist or attempt to insist on exclusive service from Perception prior to that date.

Did Tele-Direct influence the delivery of service by Perception to DSP?

Upon becoming aware in late 1992 that Perception was supplying an information feed to DSP and that it had the same content as Tele-Direct's feed, Tele-Direct, through Mr. Dolan, expressed its displeasure to Perception. Perception agreed to remedy the situation prior to publication of the DSP directory. Mr. Dolan said that he thought Perception would acquire an

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[250] Confidential exhibit CJ-31 (black vol. 10), tab 68 at 131548-54.

[251] *Ibid.* at 131555.

alternate feed for DSP as a remedy. At the same time, Tele-Direct was pushing for exclusivity with Perception.

Tele-Direct's TYP were launched in mid-February 1993. Tele-Direct was not satisfied with Perception's response to its complaint regarding the feed to DSP, including an effort in early February whereby Perception started sending slightly re-arranged or reworded content to DSP. In cross-examination, Mr. Dolan indicated that Tele-Direct wanted a "superior feed" to that provided to DSP.[252]

A meeting was scheduled for February 23, 1993 with Perception. The agenda, which was provided to Perception, states that what Perception was doing with respect to the DSP feed was "not satisfactory" to Tele-Direct. Mr. Dolan explained that Perception was simply re-voicing the network and again stated that Tele-Direct was not satisfied because it wanted a "superior" feed. This concern was communicated to Perception at the meeting.

In re-examination, taking Mr. Dolan to clause 8 of the January 1994 contract with Perception which uses the word "superior", counsel for the respondents elicited a response that "superior" meant "of high quality" and that was the way in which Mr. Dolan had used the word in his cross-examination. Clause 8 of the contract reads:

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[252] Transcript at 42:8856 (20 November 1995).

> . . . Brite does commit that the BDR Audio Network will continue to be of the same exceptional quality as the affiliate has enjoyed. BDR will continue to be of superior quality and utilize its own personnel for the creation and dissemination of information.[253]

Clause 11.6, which was later brought to the witness's attention, is instructive:

> . . . Brite will continue to supply the superior level of programming that the Affiliate has come to expect. Other audio networks offered by Brite Voice Systems or any Brite subsidiary or related company, will not exceed the BDR Audio Network in measurable deliverables including, but not limited to, frequency of reports, quantity of content, program choice and diversity as well as voice quality. Brite will make every effort to avoid American colloquialism. . . .[254]

Even in the contract, therefore, it is apparent that the word "superior" is used in a comparative, rather than an absolute, sense.[255] When questioned by the panel about clause 11.6 of the contract, Mr. Dolan agreed that what the clause was meant to ensure was that nobody had anything *better* than Tele-Direct. We conclude, therefore, that, despite the later attempt at qualification, Mr. Dolan was using the word "superior" in its comparative sense throughout his testimony. Tele-Direct was pressing Perception for a better feed than Perception was giving DSP.

Of most significance, on January 25, 1993, Tele-Direct held out what can only be regarded as a major "carrot" to Perception. Mr. Dolan, on behalf of Tele-Direct, wrote asking Perception for its "advice and recommendations" on the most efficient way to provide a TYP

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[253] Confidential exhibit CJ-31 (black vol. 10), tab 68 at 131550.

[254] *Ibid.* at 131551.

[255] The September 1993 letter also uses the word "superior" and essentially the same language about "measurable deliverables" (confidential exhibit CJ-31 (black vol. 10), tab 68 at 131555) as later appeared in the January 1994 contract.

service throughout Tele-Direct's territory.[256] There is evidence that by March of 1993, consequent upon a February 25, 1993 officers' meeting, these plans were scaled down dramatically. TYP installation was to begin only in markets currently or potentially threatened by a competitor, some ten markets. TYP were treated as a strategic tool against competition rather than a widespread innovation. In fact, after Sault Ste. Marie TYP were introduced only in Niagara Falls, in response to White, and in Windsor, where Tele-Direct was concerned both about potential entry by White and the fact that the Windsor Star is owned by Southam. It is difficult to escape the conclusion that Tele-Direct was using the promise of the roll-out of TYP service throughout its territory in order to gain the cooperation of Perception when it introduced its TYP service in Sault Ste. Marie in February 1993.

That the promised roll-out of the TYP service was a factor in the relationship between Tele-Direct and Perception is clear from the letter Perception wrote Tele-Direct on March 1, 1993, following the February meeting. In it Perception informed Tele-Direct that an "alternative audio source" for DSP would be provided by March 29, 1993. The letter concludes ". . . you are a very important client to us and we want to work with you as you roll out audiotex *(sic)* throughout your territory."[257]

The deterioration to DSP feed was coincident with its first revenue canvass in the spring and summer of 1993. (Its first revenue directory was published in November 1993.) Because of

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[256] Confidential exhibit CJ-86 (black vol. 13), tab 95 at 134080.

[257] *Ibid.* at 134107.

the poor quality of the feed, the audiotext lines were not used to nearly the same extent as in the first two months of operation. Because of the reduced volume, DSP could not use the record of the number of calls to its audiotext service as evidence of widespread use of its directory by consumers. As a result, the audiotext service was not as positive a factor as it might have been in selling its directory to advertisers.

Mr. Campbell said that it would have been virtually impossible for DSP to change its information supplier when it experienced problems. Despite what Mr. Dolan said, there was little reason for Tele-Direct to think that Perception was able, even if willing, to produce an alternative high quality feed for DSP. As matters turned out, the feed to DSP only became acceptable again once the merger of Perception and Brite resulted in another source of feed becoming available in about November 1993.

We are of the view that Tele-Direct used its bargaining power, stemming from its dominant position in the market for the supply of telephone directory advertising, to pressure Perception to, in effect, withhold supply from DSP for the purpose of frustrating or, at least, negatively impacting, the DSP attempt at entry in Sault Ste. Marie.[258] Unlike the other responses used by Tele-Direct in the competitive markets, the only perceptible effect on consumers and advertisers was a negative one. It would appear to us that the kind of conduct engaged in by

[258] Entry meaning the attempt by DSP to establish itself in the Sault Ste Marie market on an economic basis with a revenue directory; that is, not the publication of a prototype directory alone.

Tele-Direct regarding audiotext in Sault Ste. Marie unequivocally falls within the class of anti-competitive acts against which sections 79 is meant to guard.

Did Tele-Direct engage in a practice of anti-competitive acts in relation to audiotext in Sault Ste. Marie? Based on the standard set out in *Nutrasweet*,[259] an "isolated act" does not constitute a practice. In the instant case the deterioration in the audiotext feed to DSP resulted from intensive and repeated efforts on the part of Tele-Direct that hardly qualify as an "isolated act". Nor do we find that the reasonably anticipated duration and seriousness of the consequences of the efforts by Tele-Direct suggest that they should be treated as "isolated" and thus outside the reach of section 79. We therefore consider that Tele-Direct's actions regarding the DSP feed for its audiotext service in Sault Ste. Marie constitute a practice of anti-competitive acts.

Further, we find no difficulty in concluding that the effects of the deterioration in the quality of the audiotext feed resulted in a substantial lessening of competition in the Sault Ste Marie market. In conducting its first revenue canvass, DSP was denied the anticipated marketing advantage of using its audiotext call volumes to prove usage of its directory to potential advertisers because the feed deteriorated just as the canvass started. Achieving credibility with advertisers is one of the biggest hurdles that an entrant publisher must overcome.[260] The audiotext problem was a serious setback for DSP in its initial effort to attract paid advertising. However, as the Director has not requested a remedy specific to the audiotext problem or, more

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[259] *Supra* note 4 at 34-35.

[260] See further discussion, *supra* at 123.

generally, governing Tele-Direct's relationship with the suppliers, no remedy follows from this finding.

D. MARKET FOR ADVERTISING SERVICES

1) Class or Species of Business in Canada (Relevant Market): Agents

The Director alleges a number of anti-competitive acts which form a practice resulting in a substantial prevention or lessening of competition in the market for the supply of advertising services. These alleged anti-competitive acts affect agents and consultants or, in some cases, one or the other. The Director takes the position that when determining whether there is a substantial prevention or lessening of competition the effects of all of the listed acts found to be anti-competitive should be combined because they all affect the advertising services market. Further, one of the alleged anti-competitive acts is the tying of the provision of advertising services to advertising space, the same allegation we have already dealt with in the tying portion of this decision. Another alleged anti-competitive act which bears a striking resemblance to an allegation of tying is also included under the heading "Squeezing", namely, "further restricting the availability of commission [to other service providers] over time".

The respondents submit that, to the extent a separate "services" market exists, consultants and agents are in different services markets and acts affecting more than one market cannot be combined to form a practice and, thus, to determine whether there has been a substantial prevention or lessening of competition. A prevention or lessening of competition must take place *in a market* in the words of section 79. They also argue that Tele-Direct does not have market power in either services market.

As we have found that there is an anti-competitive tie covering only part of the alleged advertising services market, we cannot agree with the Director that there is one advertising services market in which both agents and consultants operate that encompasses *all* of Tele-Direct's customers. Customers meeting the 1993 commissionability rule are evidently included in the services market. The customer segment that we have determined is anti-competitively tied under section 77 -- namely regional customers -- is also included. (We will return below to the question of whether the tying practice should also form part of the section 79 case.) Agents are operating in this services market. And, Tele-Direct competes with the agents in providing services to those customers. Consultants do not.

It is difficult to see how acts taking place in different markets could be logically combined to determine if competition is substantially lessened or prevented in a particular market. Thus, only the acts affecting agents can be combined for the purpose of determining whether there has been a substantial lessening of competition in the services market.

Correspondingly, only acts affecting consultants can be combined to determine whether there has been a substantial lessening of competition in the relevant market in which they operate. It is a separate section 79 case. The details of the allegations against consultants will be dealt with below under the heading "Consultants".

Further, not all the alleged practices of anti-competitive acts respecting agents are of a sufficiently similar character so that they can be combined when assessing whether there has been a substantial prevention or lessening of competition in the services market. In particular, tying (and its restatement "restricting commission over time") differs significantly from the other alleged anti-competitive acts. The Director has brought the allegation of tying under both sections 77 and 79. The analysis and result are the same under both sections. Having found that tying results in a substantial lessening of competition by impeding entry of or expansion of agents into or excluding them from the part of the demand spectrum between six and eight markets, should this substantial lessening of competition be combined with the effects resulting from any other practice of anti-competitive acts that the Director succeeds in proving? If so, all anti-competitive acts so found would automatically lead to a finding of substantial prevention or lessening of competition by reason of our finding respecting tying.

In our view, it is not appropriate to combine the effects of tying with the effects of the practice of other anti-competitive acts. The other alleged anti-competitive acts (save for group advertising) relate to a specific historical market, the commissionable market including the eight-market grandfathered accounts. It is possible to evaluate the effects of the alleged anti-competitive acts in this well-defined context. The issue is whether there has been a substantial lessening of competition where agents have historically been competing. In the case of tying, the allegation is that the extent of the market itself has been limited.

In this case, there is a distinct difference between the nature and effect of tying and the other alleged anti-competitive acts, save for group advertising which we return to below. We note that this might not be true in other cases where there might be some interaction or a less distinct dividing line between the section 77 and section 79 claims. A finding that the respondents have engaged in tying does not act as a spring-board for a finding of substantial lessening in the market segment where the agents have been competing. Prohibiting tying should permit the agents to compete in the enlarged market as they have in the historically commissionable market. A finding of substantial lessening of competition in the historically commissionable market should therefore be based on a practice of acts with respect to that market.

Therefore, we need not deal with tying further under section 79. We will now turn to the allegations relating to the commissionable market and then the allegation regarding the prohibition on group advertising which is distinct.

(2) Control of the Existing Commissionable Market

It is evident that, despite the Director's submission to this effect, Tele-Direct does not have *direct* control or market power in the currently commissionable advertising services market.

It has a modest market share of approximately 25 percent in that market.[261] The Director also advances an alternative position that is not based on direct control by Tele-Direct but rather on the hypothesis that it is leveraging its control in the publishing market into the services market. We have found that Tele-Direct has control in the telephone directory advertising market which gives it market power in the publishing of advertising space. The Director argues that Tele-Direct is using this market power as a lever to obtain market power in advertising services through its alleged anti-competitive acts. We agree that this is an arguable theory that could, if proven, fall within the parameters of section 79. Whether Tele-Direct has, in fact, leveraged its existing market power must now be determined.

(3) Analysis Respecting the Existing Commissionable Market

The alleged anti-competitive acts are set out in full at paragraph 65 of the application. We paraphrase them here (not necessarily in the order set out in paragraph 65) as they relate to agents and alleged abuse of dominance only:

(1) "squeezing" the return available to agents by transferring functions to, withholding services from and making terms of supply to agents more onerous;

(2) discriminating against agents by providing space to them on less favourable terms than available to Tele-Direct's internal sales force, including:

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[261] See further discussion of market share below under "Analysis Respecting the Existing Commissionable Market".

- *group advertising* - prohibiting advertisements containing the name of more than one local advertiser, e.g., franchisees;

- *issue billing* - requiring agents to pay for advertising on behalf of their clients at the time of issue as opposed to payment on a monthly basis which is the payment method employed when sales of advertising are made through Tele-Direct's own sales personnel;

- *closing dates* - requiring that agents submit advertising for publication earlier than the date applicable to Tele-Direct's sales personnel;

- *tear sheets, etc.* - refusing or delaying to provide tear sheets and other information and material to agents; and

- *promotional programs* - delaying to inform agents of or refusing to make certain promotional programs available to agents' clients, including:

    - a program whereby an advertiser using Tele-Direct's sales personnel could obtain a subsidy towards the cost of Yellow Pages advertising if Yellow Pages are mentioned in advertising in other media;

    - cooperative advertising programmes whereby a supplier contributes to the cost of advertising of its customer or distributor;

    - keyed advertising in which a new advertisement with a new telephone number is placed in the Yellow Pages and the calls to that number are monitored to assess the effectiveness of the advertisement; and

    - other trial and test programs.

The Director submits that these acts have had adverse effects on agents and that there is no business justification that would exempt the acts from being found to be anti-competitive. The Tribunal would observe that some of these acts appear to have created some difficulty for agents and, in some cases, there does not seem to be an acceptable business justification. However, it is not necessary to embark upon a detailed act-by-act analysis to weigh their effects on agents against their business justification because of our conclusion that the Director has not demonstrated that the acts have or are likely to prevent or lessen competition substantially in the relevant advertising services market.

Both parties referred us to the statement set out in the Tribunal's decision in *NutraSweet* that:

> [i]n essence, the question to be decided is whether the anti-competitive acts engaged in ... preserve or add to ... market power.[262]

The Director's operative theory is that Tele-Direct is extending its market power from the space market to the services market through the alleged practice of anti-competitive acts. This means that the Director must demonstrate that Tele-Direct has or is establishing, or is likely to achieve, market power in the services market.

In order to assess whether Tele-Direct now controls the services market, we first look to market shares in the currently commissionable market. There is disagreement between the Director and Tele-Direct on the respective market shares of Tele-Direct and the agents. The parties rely on a variety of data that most supports their positions. Market share estimates range from 65 to 87 percent for agents and from 13 to 35 percent for Tele-Direct. We reject the extreme numbers put forward by the Director and Tele-Direct as not supportable on the evidence and, indeed, they were not seriously advanced by either side. While there are weaknesses in the

[262] *Supra* note 4 at 47.

data, we are satisfied that a market share of about 75 percent for agents and 25 percent for Tele-Direct is reasonably accurate.[263]

A high market share for agents and a correspondingly low market share for Tele-Direct would suggest that, even if Tele-Direct has engaged in anti-competitive acts, it has not been successful in obtaining market power in the advertising services market. Indeed, the fact that Tele-Direct's market share is as high as it is may well be attributable to factors unique to Tele-Direct but which are not anti-competitive, such as the desire of some advertisers to deal directly with the publisher. From the available data, it is apparent that, even on an individual basis, Tele-Direct does not have as high a market share as DAC/NDAP, which has about a 40 percent share. Based on all these considerations, we are satisfied that Tele-Direct's 25 percent share falls well short of a level that might be considered to indicate market power.

We must also consider whether there is any evidence of a trend towards a material increase in Tele-Direct's market share, which might indicate that it is in the process or is likely in the future to acquire market power as a result of the acts which the Director alleges to be anti-competitive. Certainly, there is anecdotal evidence of individual advertisers switching from an agent to Tele-Direct for some of the reasons which constitute acts which the Director submits are anti-competitive, for example, issue billing. We have no evidence, however, of any declining trend in market share for agents or increasing trend in market share for Tele-Direct over any

[263] Both sides agreed that the agents' market share in 1993 was about 80 percent: confidential exhibit CJ-31 (black vol. 10), tab 69 at 131680. Adjusting to exclude sales into Tele-Direct's directories by agents based outside of Tele-Direct's territory, we arrive at approximately 75 percent for agents and 25 percent for Tele-Direct.

period of time. Further, it would not seem that the agency business is unattractive or that agents are in any way systematically going out of business. On the contrary, we have had evidence of additional agents being accredited in recent years and others who are still seeking accreditation.

Is there any reason to believe that in the future the alleged anti-competitive acts will have any *greater* deleterious effect on the agents than they may have had in the past? We recognize that a new element has been added to the interactions in the marketplace by the relatively recent creation of Tele-Direct's CMR. Could it be that, in combination with Tele-Direct (Media) Inc. which provides an additional vehicle for Tele-Direct to use practices like the alleged anti-competitive acts, the alleged anti-competitive acts will likely cause competition to be prevented or lessened substantially in the future?

We are unable to arrive at such a conclusion. We have no evidence of the competitive impact of the advent of Tele-Direct's CMR into the market. It has been competing since 1994 but we were provided with no evidence whatsoever from which to infer that the combination of its presence and Tele-Direct's alleged anti-competitive acts have resulted or will result in a materially lower market share to agents and a correspondingly higher share for Tele-Direct. One would have expected that if this was an important factor, we would have seen some significant movement of accounts from the independent agents to Tele-Direct's CMR. There was no such evidence. It is true that Tele-Direct's CMR is in its early years and it may not be as effective now as it will be later. To be valid, however, inferences about the future must be based on evidence.

Given the record before us, any conclusion about the future effect of Tele-Direct's CMR in combination with the alleged anti-competitive acts would be speculative.

The Director has the burden of proving a substantial lessening of competition. We conclude that while some of the disadvantages which form part of the Director's abuse of dominance case and were imposed on agents by Tele-Direct may have had some adverse effect on them, that effect could not have been and is not likely to be substantial or the agents would not hold 75 percent of the market or there would be evidence of a decline over time in the share held by agents.

(4) Group Advertising

Group advertising is display advertising consisting of the individual business names of a number of franchisees or distributors under a common logo or trade-mark.[264] This type of advertisement is now prohibited by Tele-Direct and to all intents and purposes is not sold by agents or Tele-Direct.[265] The revenues that might potentially be converted into group advertising are currently non-commissionable and are serviced by the internal sales force as local or individual business accounts.

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[264] The difficulty here is that some franchisees or licensees carry on a number of businesses besides the licensed or franchised one and they do not operate their business under a "corporate" name. They wish to be listed in the advertisement under their own name, which often has high recognition value in their community, while still participating in the group advertising to promote the licence or franchise. An example is the Autopro dealers: the licensed Autopro garages or service stations do not carry the "Autopro" name. Tele-Direct does not permit them to be listed under their individual names.

[265] There was evidence of an occasional advertisement that appears to be a group advertisement or something resembling a group advertisement but we are satisfied that it is Tele-Direct's policy not to permit group advertising.

The effect of the alleged practice of anti-competitive acts regarding group advertising is to prevent competition by limiting the size of the commissionable market available to agents, rather than limiting their ability to compete for existing commissionable accounts. Because of the difference in the nature of the allegations, whether there is a likely substantial prevention of competition as a result of Tele-Direct's practice regarding group advertising must be evaluated separately from the alleged practices of anti-competitive acts respecting the existing commissionable market.

We believe that Tele-Direct's policy on group advertising is dictated by its concern with a net revenue loss should advertisers abandon or reduce individual advertising in favour of group advertising. The incidental effect is to deny a type of advertising that would primarily be of interest to larger advertisers, for example, franchisers, some of whose accounts are likely targets for agencies. Although we heard anecdotal evidence of how certain advertisers would prefer to participate in group advertising, we were not presented with evidence as to the magnitude of the effect of this restriction. In the circumstances relating to agents we are of the opinion that such information should have been provided. Without such evidence, we cannot conclude that the prohibition against group advertising constitutes a substantial prevention of competition.

(5) Conclusion

We are unable to conclude that the evidence demonstrates that the acts alleged to be anti-competitive in the existing commissionable market and in respect of group advertising have had, are having or are likely to have the effect of preventing or lessening competition substantially. As a result, the Tribunal is without jurisdiction to grant a remedy under section 79 of the Act. It is, therefore, not necessary to consider in detail whether the individual acts complained of are anti-competitive and whether separately or in combination they amount to a practice.

We are not unmindful that some of Tele-Direct's actions in respect of agents seemed wilful and senseless. However, the Competition Tribunal does not exist to regulate industry practices generally. Rather, it has jurisdiction only to remedy the substantial prevention or lessening of competition and where this has not been proved, no remedy can be ordered.

E. CONSULTANTS

(1) Introduction

At paragraph 65(b) of the application, the Director alleges that Tele-Direct engaged in anti-competitive acts by refusing to deal directly with consultants as agents for advertisers purchasing space from Tele-Direct. The paragraph continues:

> The Respondents have issued guidelines to their advertising space sales staff which provide that the customer must deal with the Respondent's salespersons and no consultant can deal with the salespersons as a customer's agent.

The following, more specific, aspects of refusing to deal directly with consultants were provided in the written argument at paragraph 297:

> **[I.]**
> (a) written instructions: refusal to act upon written instructions received from consultants on behalf of advertisers;
>
> (b) oral instructions: refusal to act upon oral instructions received from consultants on behalf of advertisers or meet consultants or the advertiser in the presence of consultants to receive same;
>
> (c) follow-up: refusal to deal with consultants on subsequent errors or problems.

In paragraph 65(c)(v) of the application, the Director alleges that Tele-Direct also engaged in anti-competitive acts by providing advertising space to consultants on less favourable terms than to its own sales staff, including rejecting or delaying orders based on alleged errors or other problems which would not result in delay or rejection of orders from Tele-Direct's own sales representatives. As set out in paragraph 296 of the written argument, the specific aspects of these acts are:

> **[II.]**
> (a) delivery and processing problems: refusal to acknowledge or accept delivery of orders involving consultants or denial of delivery resulting in the delay or rejection of same, refusal to process such orders or the return of such orders to the advertiser or consultant;
>
> (b) alleged errors: the identification of errors or problems in such orders which would not result in the delay or rejection of orders handled by the Respondents' own sales staff;
>
> (c) oral instructions: refusal to meet with the advertiser to take instructions originating in advice from consultants;
>
> (d) consequential acts: rejecting or delaying the processing of consultant orders, permitting or facilitating the following consequential actions:
>
> > (i) informing advertisers that their orders may or may not be processed if prepared by consultants or that consultants are "scam artists", have committed errors or similar threats or derogatory comments;
> >
> > (ii) inducing breach of the contract between advertisers and consultants.

The final alleged anti-competitive acts of relevance to consultants are found at paragraph 65(e) of the application. The Director maintains that Tele-Direct is engaging in anti-competitive acts by refusing to supply specifications to consultants for the placing of advertisements in its directories.

We will deal with the alleged anti-competitive acts under the headings (a) refusal to deal directly with consultants, (b) discriminatory acts and (c) specifications, starting in "(5) Anti-competitive Acts", below.

(2) Allegations - Pleadings

The respondents argue that the "consequential acts" listed under II. (d) above do not fall within paragraph 65(c)(v) of the application and should not, therefore, be considered by the Tribunal. They also submit that one of the remedies requested by the Director, pertaining to copyright in advertisements, was not pleaded. The Director conceded that the case for including the remedy is not strong and we will not deal with it further.

On the question of the construction of the pleadings and what may be considered as fairly within them, once we have reached the stage of final argument we have indicated that what is determinative is what the parties considered to be in issue, looking at the proceeding as a whole. We will use the same general approach to the arguments here.

Counsel for the respondents admitted that aspects II.(a) and II.(b) were clearly in the application and II.(c) might be reasonably inferred from the application but II.(d) was outside the pleadings. The elements of (d) which were emphasized in oral argument by the respondents regarding their objection related to the question of inducing breach of contract and what was termed the "bad mouthing" claim or the making of disparaging remarks about consultants. In reply, counsel for the Director stated that the Director was not seeking a remedy with respect to the consequential acts and that there was little point in addressing whether they were part of the case. We have some difficulty with this position. The Director is clearly seeking a remedy for the alleged anti-competitive acts of providing advertising space to consultants on less favourable terms than to its own sales staff, including rejecting or delaying orders based on alleged errors or other problems, of which II.(d)(i), at least, is a subset. The Director also accepted, however, and we agree that any issue of counselling breach of contract is a matter for the civil courts so we will not deal with it further. The remaining acts listed in II.(d) were addressed by *both* parties through evidence and argument. Based on their conduct of the proceedings, the respondents were aware that these acts were in issue and there is, therefore, no prejudice to them by the Tribunal dealing with them on the merits.

(3) Competition Between Consultants and Tele-Direct

For the Director to succeed in any of the allegations, it must first be shown that Tele-Direct and the consultants are competitors. The respondents submit that consultants do not "sell" anything; they merely "unsell". They describe consultants as being in the business of providing independent (or non-partisan) advice to disgruntled, local Yellow Pages advertisers. They say that Tele-Direct does not operate in this market since advertisers recognize that Tele-Direct's advice is partisan and not independent.

The Tribunal accepts that while the relationship between Tele-Direct and the consultants is not that seen in the more usual competitive context, they are nonetheless competitors. It is true that consultants exist by downselling, while it is highly unlikely that Tele-Direct representatives would offer the same type of advice. It is also true that consultants' advice is independent while Tele-Direct representatives are, by definition, partisan. Further, consultants normally do not have an ongoing relationship with an advertiser and their remuneration arrangement takes a different form than that for Tele-Direct. There may be other differences of detail.

At bottom, however, both consultants and Tele-Direct representatives provide services which a customer can use to achieve the final result of an advertisement in the Yellow Pages. As we have seen from the evidence put forward in this case, a customer may choose to use either a consultant or the Tele-Direct representative to obtain these services. In this sense, they are substitutes for one another and compete to serve the advertising customers. There was substantial evidence put before us that Tele-Direct, in fact, views consultants as significant competitors, monitors their progress and takes action to attempt to limit their inroads on its revenues.

This is not to say that consultants (and Tele-Direct) operate in the "separate" services market, an argument which we have already rejected. Both consultants and Tele-Direct are participants in the broad telephone directory advertising market. Tele-Direct controls that market, as set out in the chapter entitled "VII. Control: Market Power", above.

(4) Facts

(a) Consultants and their Method of Operation

Three directory advertising consultants testified before the Tribunal. Jim Harrison of Tel-Ad Advisors Ltd. ("Tel-Ad") has serviced the Ontario market from an office in the Toronto area since June 1984. Prior to that time, Mr. Harrison was an employee of Dominion Directory. Serge Brouillet, previously in sales and also training and promotion with Tele-Direct, started Ad-Vice Communications ("Ad-Vice") in mid-1989 in Sudbury to service northern Ontario. In the fall of 1990, he sold the northern Ontario operation to Charles Blais to be run as Ad-Vice North and moved into the Toronto market. Mr. Blais also appeared as a witness. Mr. Blais operated the Ad-Vice franchise in Sudbury from November 1990 to December 1992 when he sold it back to Mr. Brouillet who ran it in 1993.

A summary of the *modus operandi* of consultants in general will provide context for the relations between consultants and Tele-Direct and for the Director's allegations. Consultants operate on the basis that many Yellow Pages advertisers can reduce their Yellow Pages spending without reducing the effectiveness of the advertising. In other words, they target customers who are dissatisfied with the amount that they are spending with Tele-Direct and are willing to pay a fee to lower it. Consultants recruit customers by going through the Yellow Pages and identifying likely candidates for their services, those for whom they can save money. Two of the major factors are the size of the advertisement and the use of colour; number of headings and number of directories are also reviewed.

After contacting the client by telephone to determine interest, the consultant or an employee of the consultant meets with the client and makes a presentation showing the client various options for changing the advertising. The potential for conflict with Tele-Direct and its commissioned sales representatives is obvious from the outset. The consultants' income depends on reducing customers' expenditures on Yellow Pages. Thus, they attempt to convince the customer that the extra amount spent for options like larger size and colour is not worth paying. To do this, they might bring to the attention of the customer how much more those options cost and question their effectiveness for the customer. Tele-Direct's representatives, of course, emphasize the value and effectiveness of colour, size and the like by drawing on arguments and evidence put together by Tele-Direct to show that they are worth the cost.

With respect to submitting customers' orders to Tele-Direct for processing, when it first commenced operations Tel-Ad sent orders to Tele-Direct on behalf of customers. These were rejected by Tele-Direct. Then Tel-Ad sent in the orders on a generic order form with no identifiers; these were also rejected and returned either to Tel-Ad or the customer. Attempts to submit orders with a letter of power of attorney from the customer also failed. Eventually, Tel-Ad simply left the orders with the customers to be submitted to Tele-Direct. In July 1984, Tel-Ad started legal action against Tele-Direct for refusing to accept advertising orders directly from Tel-Ad. Tel-Ad also sought an interlocutory injunction requiring Tele-Direct to accept orders submitted by Tel-Ad on behalf of advertisers. The injunction application was denied on the basis of no irreparable harm and the action was later abandoned. Tel-Ad's activities led to the first version of Tele-Direct's guidelines for dealing with consultants, drafted in 1986. Tele-Direct's guidelines are reviewed in some detail below.

(b) Tele-Direct Reaction - General

The existence and activity of consultants strike at the trustworthiness of advice provided by Tele-Direct's sales representatives and place highly profitable revenues in jeopardy. Tele-Direct does all within its power to eliminate any possibility of consultants gaining the ear of its customers. It has taken out advertisements warning customers to beware of consultants. The same message is conveyed by the representatives and by letters to customers telling them to call Tele-Direct if contacted by consultants.

According to the 1986 Tele-Direct guidelines for dealing with consultants, the "official" line on consultants to be conveyed by representatives is that their objective is to reduce Yellow Pages advertising which will reduce the effectiveness of the advertising and likely adversely affect the customer's business, based on studies conducted by Tele-Direct. Emphasis is placed on the fact that consultants are only paid if the customer reduces Yellow Pages spending, implying that consultants are likely to give biased advice, and that Tele-Direct will perform the "same" service as the consultant (advice and artwork) and "not charge a fee".[266] Tele-Direct also encouraged its representatives to point out to the customer that while Tele-Direct was concerned with the long-term, consultants do not have a continuing relationship with the customer and therefore have no incentive to take into account the possible negative repercussions on the customer's business if their advice is followed.

There is evidence that at least some sales representatives went considerably further in their efforts to discredit consultants, calling them "scam" artists and other epithets, saying they were unfamiliar with Tele-Direct's specifications and showing poor photocopies of artwork done by consultants to customers in an attempt to cast doubt on the ethics and professionalism of the consultants.

Tele-Direct has also taken other, positive steps to combat consultants by improving elements of its service to its customers. For example, Tele-Direct has attempted to create a better working relationship with customers through "consultative" selling and by assigning representatives to customers for up to three years rather than changing each year. While the changes made by Tele-Direct were not in response to consultants alone, they were rooted in customer dissatisfaction with Tele-Direct's service.

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[266] These assertions ignore the fact that Tele-Direct representatives would rarely, if ever, give advice on how to reduce spending.

(c) Tele-Direct's Consultant Guidelines

The guidelines set out Tele-Direct's procedures and directives to its sales force for dealing with orders for advertising originating with consultants and for handling customer contact once involvement of a consultant has been detected or suspected. This stage of the relationship between consultants, customers and Tele-Direct forms the focus of the Director's allegations of anti-competitive conduct. While the application of the various guidelines has been somewhat erratic and interpretation of their terms varied, it is clear that Tele-Direct has at no time dealt directly with a consultant acting *on behalf of* or in a representative capacity for an advertiser. Tele-Direct has always insisted on visiting a customer suspected of using a consultant even after an order was received from the customer and obtaining the customer's signature on its own documents. The package provided by Mr. Brouillet of Ad-Vice to his clients, following futile attempts on his part to avert the visit of the Tele-Direct representative by providing Tele-Direct's contract or a similar document to his clients himself,[267] advises the client that the Tele-Direct representative will be in contact to transfer the advertising program onto the Tele-Direct forms.

(i) 1986 Guidelines and Their Application

As general rules, the 1986 guidelines provided that:

[267] Tele-Direct threatened him with legal action, apparently for breach of copyright in its contractual terms and conditions.

> (c) Tele-Direct will not accept insertion orders directly from directory consultants who have not been granted accredited agency status by Tele-Direct.
>
> (d) Tele-Direct sales representatives should continue to contact their customers directly and request that the customers actually sign the Tele-Direct contracts and layout sheets so as to ensure the accuracy of the Yellow Pages advertising proposal prepared by a directory consultant.[268]

While the Tele-Direct policy of refusing to accept orders directly from consultants may have been followed in Tele-Direct's western region, it was not followed in the eastern region, in particular in Montreal, Sudbury and Ottawa. Letters sent in 1989 by Tele-Direct to Consultant en publicité annuaire et communication (CEPAC 2000) Inc. (" CEPAC 2000 ") in Montreal and Ad-Vice in Sudbury and in 1990 to Steven White of Tel-Ad in Ottawa[269] outlined for the consultants in question the procedure to follow in submitting orders to Tele-Direct.[270] The orders had to be delivered to named Tele-Direct managers in the relevant offices, accompanied by proper authorization by the advertiser on the advertiser's company letterhead.

Paul de Sève, Tele-Direct's Vice-president of Sales for the eastern region, confirmed that, although Tele-Direct's policy was not to deal directly with the consultant on the advertiser's behalf, in the eastern region at least, it was accepting orders from consultants. Orders were not automatically rejected and returned to the consultant even though Tele-Direct was aware of consultant involvement. The orders were taken as an indication that the customer wanted to

[268] Confidential exhibit CJ-10 (blue vol. 1), tab 5 (public).

[269] Not affiliated with Mr. Harrison.

[270] Initially, Tele-Direct refused to accept orders from Mr. Brouillet, until he obtained a copy of the letter sent to CEPAC 2000.

change its advertising and a Tele-Direct representative would visit the advertiser and deal with him or her directly. In Tele-Direct's own words,

> . . . Regardless of whether the "cut agent" or the customer was directing insertion/change/cancellation of Yellow Pages advertising through letter or order form, we would accept this information as notification that the customer wished to renegotiate his Yellow Pages advertising. The Tele-Direct representative would deal directly with our customer, using our forms and contracts in the setting up of Yellow Pages advertising.[271]

(ii) 1990 Policy and Application

Tele-Direct implemented new consultant guidelines in December 1990. The opening words of the revised guidelines state that:

> We changed our operating procedures on dealing with "cut agents" effective December, 1990, to further strengthen and reinforce our direct servicing philosophy with our customers.
>
> These changes were made to ensure that we did not act on "cut agent" instructions, for the insertion/change/cancellation of our customers' Yellow Pages advertising. Furthermore, these changes were intended to leave no doubt in the minds of our customers that we do not do business with "cut agents".[272]

The "general procedures" established by these guidelines were as follows:

> • we will always accept letters/packages sent or given to us by customers and act in accordance with their wishes.

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[271] Operating procedures prior to December 1990: confidential exhibit CJ-11 (blue vol. 2), tab 58 at 107788 (public).

[272] Operating procedures, December 1990: *ibid.* at 107792 (public).

> • to the best of our knowledge, we will not accept, nor act upon, information sent or given to us by "cut agents" on behalf of our customers, nor accept or act upon information sent or given to us by customers containing directives from "cut agents."
>
> Instead, our procedure will be to not accept packages from "cut agents" or from customers for "cut agents" and in the event that a package is accepted in error, its contents will be returned to the "cut agent" with a covering letter designed for this purpose.[273]

The guidelines then provide more detail on the procedure to be followed in particular situations. The gist is that if, upon external examination of a letter or package, it became apparent that it was from a consultant or from a customer working with a consultant, the letter or package would be returned to the consultant. If the letter or package was apparently from a customer, with no external indication of consultant involvement, the letter or package would be opened but if further examination of the contents revealed the involvement of or a directive from a consultant, the letter or package would be returned to the consultant. Even when the letter or package appeared to come from or was, in fact, dropped off by the customer, if it was rejected because of consultant involvement, the customer would not be informed that the order had been returned to the consultant.

Mr. de Sève admitted that the procedures set out above represented a dramatic change from the 1986 guidelines, at least with respect to how the Montreal, Sudbury and Ottawa offices had been operating.[274] It is also clear from his testimony that the principal reason for the change was that Tele-Direct was having second thoughts about having "legitimized" the consultants to

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[273] *Ibid.*

[274] There is some question as to whether the consultants affected were notified specifically of the change in policy or of the exact terms of the new policy. Messrs. Brouillet and Blais said that they were not.

the extent they had by writing the letters referred to above in 1989 and 1990. The 1990 strike by Tele-Direct's sales representatives meant that the consultants were particularly active in the fall of that year.

The 1990 guidelines were adhered to strictly in one respect. At no time did Tele-Direct accept orders that were not submitted on the customer's letterhead. Other aspects of the guidelines appear to have been unevenly applied. Despite the statement that Tele-Direct would *always* accept orders from its customers and "act in accordance with their wishes", there was evidently considerable uncertainty within Tele-Direct as to how the guidelines were to be applied with respect to rejecting customers' orders for consultant involvement. Some orders containing indications of consultant involvement or where a consultant was known to be involved were accepted without incident or accepted after an initial rejection. Yet, Mr. de Sève's evidence, which as Vice-president of Sales for the eastern region we take to be an "official" application of the guidelines, was that where there was doubt, it was *assumed* that the documents came from a consultant and they were returned to the consultant without advising the customer.

This is what happened in the summer of 1991 in the case of a package containing 23 orders under customers' signatures which were, in fact, prepared by Ad-Vice North (Mr. Blais). An internal Tele-Direct document dealing with how it should respond to a complaint by Mr. Blais about this incident indicates that packages were being returned to Ad-Vice North by the Sudbury office *even though* Ad-Vice North was not mentioned in any of the correspondence and *regardless of* the fact that the letter of direction was from the customer because the employees recognized the Ad-Vice "format". Mr. de Sève stated that consultant involvement was probably assumed because of the number of orders in one envelope.

Mr. de Sève also confirmed that in 1991 Tele-Direct adopted a further policy of not processing orders received at the closing date according to the customer's instructions if they originated with a consultant even though it would do so for orders coming from its own sales force. Tele-Direct would instead rely on its last year's contract with the customer or the latest contract signed by the customer.

(iii) 1992 Policy and Application

The difficulties with and the inconsistency in application of the 1990 guidelines led to the most recent Tele-Direct guidelines for dealing with consultants, dated February 1992. These guidelines are currently in force. The operating procedures in those guidelines state that they are designed to "formalize our existing policy of dealing directly with customers." Two important aspects of that policy are:

> . . . Tele-Direct will not accept a customer's appointment of a consultant to act on his/her behalf in dealings with Tele-Direct; and, Tele-Direct will not knowingly take instructions from a consultant acting on behalf of a customer.[275]

The detailed procedures provide that when correspondence is received from a consultant, whether by mail, courier, delivery, etc., it is opened and the contents examined to determine what action (from a list of A to D) should be taken. According to the procedures, any correspondence

275 Confidential exhibit CJ-12 (blue vol. 3), tab 105 at 109796 (public).

from a customer appointing a consultant to act on his/her behalf is to be returned to the customer with a form letter indicating that Tele-Direct will only deal with its customers directly (B). Any "directive" from a consultant is to be returned to the consultant with a form letter which simply states that the material was received "in error" (C). A second form letter is to be sent to the customer explaining that the material has been returned to the consultant without being processed and stating Tele-Direct's policy of only dealing with the customer directly. The guidelines also state that any correspondence from a consultant regarding problems with or errors in published advertising are to be ignored altogether and the matter resolved directly with the customer (D).

Most importantly, if the correspondence contains instructions from a customer regarding his/her advertising, the procedures provide that the instructions should be accepted and handled "in the normal fashion, i.e., deal directly with the customer" (A). The evidence of Messrs. Renwicke and de Sève regarding when correspondence will be considered by Tele-Direct to contain instructions "from a customer" and will be accepted and handled in the "normal fashion" reveals that the guidelines are still open to interpretation. Mr. de Sève testified that even if the instructions are from the customer, on the customer's letterhead, if they include any reference to consultant involvement, the order will not be accepted. He was of the view that such a case fell within B or C set out above. Mr. Renwicke, on the other hand, first stated that such an order would be accepted. He then qualified this by saying that it depended on the "tonal quality" of the letter and of any references to a consultant. According to him, the defining criteria is whether it was perceived that the consultant "is going to be seen to or is actually playing a leadership role for that account".[276]

Assuming that the order is accepted, the guidelines also set out a "protocol" for customer contact by sales representatives when dealing "directly" with customers which reveals that little weight is given to the order already received from the customer. The representatives are to conduct themselves throughout in a "business-like and professional manner" but are expected to "only provide Yellow Pages selling services *directly to a customer*." While Tele-Direct's representatives are permitted (but not required) to meet with a customer when a consultant is present, they must decline to take *any* instructions from a consultant even if the customer insists. The protocol provides that all instructions must come directly from the customer. If the customer refuses to deal with the Tele-Direct representative directly, the representative is to review with the customer the customer's legal obligations under the existing Tele-Direct contract, i.e., that the previous year's advertising will simply be renewed. If this approach fails, the sales representatives are advised to try again later to re-convene the meeting but if the customer still refuses to deal directly, then advise the customer that the contract will remain in force in accordance with its terms.

Mr. de Sève admitted that under this protocol, where a customer handed the Tele-Direct representative a package containing instructions prepared by a consultant and asked the

[276] Testimony of P. de Sève: transcript at 44:9123-27 (22 November 1995); testimony of D. Renwicke: transcript at 46:9630-34 (27 November 1995).

representative to follow them, that would lead to a termination of the interview and the instructions would not be followed. He also admitted that, in fact, Tele-Direct representatives would refuse to meet with the customer in the presence of the consultant because they would not be able to discuss with the client "one-on-one" the merits of the change in the advertising program.

(d) Specific Incidents

The Director relies on numerous specific incidents involving consultants and their customers as evidence in support of his allegations. The respondents dispute that some of those occurrences took place or if they took place, took place as related by the Director's witnesses.

We accept that there were times when Tele-Direct went beyond simply rejecting or returning orders from customers where consultant involvement was suspected and treated these in an extremely cavalier fashion. On one occasion in 1989, a package of customer orders prepared by Mr. Brouillet, including one from Ad-Vice's law firm, was left with a secretary who threw it out of the Tele-Direct office and into the hallway. The lawyer was able to confirm after a number of phone calls that his order had been retrieved and was processed. He inquired about the remaining orders but Tele-Direct refused to inform him of the fate of the other orders in the package.

On another occasion in 1990, when the manager designated to receive orders from Ad-Vice in Sudbury was not in the office, the process server left the package on the counter and the receptionist threw it in the garbage. Apparently the order was not processed in accordance with those instructions, according to the respondents, because the advice was delivered late. The only evidence brought to our attention on this point was a recently written note by the Tele-Direct representative that stated "delivered past deadline - did not use their material".[277] The affidavit of service sworn contemporaneously, however, indicates that the package was delivered on August 16, 1990. Mr. de Sève's evidence was that the closing date for Sudbury was in November. We therefore do not accept that the package was delivered late.

We accept the evidence of incidents in which orders from customers who had used a consultant were subject to "errors" in processing by Tele-Direct. In three cases Tele-Direct acknowledged to the customers that errors had been made and provided a credit. These included Todd Optical Ltd. (mistake in telephone number and location), Adler Moving Systems (advertisement in the Elliot Lake directory omitted), Forest Products and Builders (advertisement did not appear), all customers of Mr. Brouillet. The owner of Todd Optical Ltd. had written a letter of support for Ad-Vice. We note that these errors all had potentially serious adverse consequences for the businesses involved.

Another customer of Ad-Vice, Lockerby Taxi Inc., whose owner appeared as a witness, experienced an odd error when an unpaid "filler" advertisement was published featuring

[277] Confidential exhibit CJ-27 (black vol. 6), tab 33 at 128522.

Lockerby's name with the query "Sales Down?" in the background. Mr. Flinn was never provided an explanation or apology for the error. His attempt to obtain compensation was denied by Tele-Direct because he could not prove damage to his business.

The Director also called evidence that Tele-Direct informed customers that advertising prepared by a consultant did not comply with its specifications on the slimmest of pretexts.[278] Several of the examples related to clients of Mr. Brouillet, who testified that to his knowledge the advertisements were in accordance with existing specifications. The respondents called no evidence that the advertising did not meet specifications. In one case, the respondents admitted that the advertisement prepared by CEPAC 2000 did, in fact, comply with specifications.[279] We conclude that Tele-Direct would not have objected to these advertisements had it not been for the involvement of a consultant in each case.

As noted above, Tele-Direct's admitted practice is not to act on a customer's order, where a consultant is believed to be involved, until the customer has been visited by a Tele-Direct representative. Instead, Tele-Direct treats the order from the customer merely as an "indication" that the customer wants to change his or her advertising. Thus, in every case of suspected consultant involvement, the customer will be visited by a Tele-Direct representative. At the point of a meeting between the Tele-Direct representative and the customer, usually the customer

[278] E.g., Postime Distributors (wrong paper, wrong size), Paul's Quality Woodcraft (non-compliance with specifications in general), M & L Service (wrong paper) and Canac-Marquis Grenier (borderless advertisement not allowed).

[279] The advertisement was for Canac-Marquis Grenier.

would have already signed a contract with the consultant approving the changes recommended by the consultant and agreeing to pay the consultant's fee. The respondents deny that there was any tendency within Tele-Direct to delay visiting a customer who was known or suspected to have used a consultant until the last minute and to use the visit as the occasion to make disparaging remarks implying that the customer had been "taken advantage of" by the consultant or to use other tactics to pressure the customer into changing his or her mind about the program recommended by the consultant.

We accept that these types of tactics were fairly widely used by Tele-Direct's representatives. Last minute contact resulting in pressure on the customer and some confusion as to what the customer had to do to ensure the advertising would run as originally ordered occurred in several examples put before us. Mr. Harrison recounted the example of Mr. Kantor of Tiremag Corp. Mr. Kantor's order was delivered by registered mail to Tele-Direct in April 1993. Mr. Kantor was contacted by the Tele-Direct representative six months later, close to the closing date for the Brampton directory, and informed that no order for that directory had been received and that unless something was done, his advertising for the previous year would have to be used. Mr. Kantor insisted that he had already given them his instructions but Tele-Direct never located the package. The previous year's advertisement was run, then Tele-Direct located the package and admitted it had made a mistake. Similar problems occurred for Pat's Party Rentals, a client of

Mr. Brouillet.[280] Other examples are the Britannia Restaurant & Banquet Hall, again a client of Mr. Brouillet, and the Muskoka Riverside Inn, a client of Mr. Blais.[281]

Eric Beesley of Georgetown Quik-Lube Ltd., who appeared in person, testified that, having submitted his order much earlier, he was contacted by the Tele-Direct representative the day before the closing date to attempt to persuade him to stay with his existing program. Then on the final day, he was called again and advised that he had to attend at the Tele-Direct office in person to make the changes. Mr. Beesley, however, was aware of the contractual clause allowing him to make changes in writing by a certain date, pointed out that he had complied with it and the advertising was processed as he had ordered.

There is only one documented case in the evidence in which a Tele-Direct representative counselled a customer *outright* not to honour a contract with a consultant.[282] Tele-Direct's guidelines explicitly warn Tele-Direct representatives not to provide advice with respect to customers' legal obligations. There is, however, abundant evidence of instances where customers

[280] The order was sent in under her signature on July 15, 1991. On September 30, 1991, the client received a form letter from Tele-Direct stating that the material had been returned to the consultant without processing. (As of that date, Ad-Vice had not received anything back.) The customer panicked, thinking her advertising would not appear. Mr. Brouillet was unable to obtain confirmation that the advertising would appear as ordered. The client ended up dealing directly with Tele-Direct and Mr. Brouillet had to sue to recover his fee.

[281] The Britannia Restaurant & Banquet Hall order was sent in on August 2, 1991. On September 25, 1991, shortly before the closing date, Tele-Direct faxed the client its contract documents, which described the previous year's program. The client simply signed the documents, thinking they represented the new order. The old program appeared, the client protested, Tele-Direct insisted on full payment, the client refused to pay and was eventually barred from placing further advertising in Tele-Direct's directories. A Tele-Direct notation on a document relating to this customer indicates some concern even on its part about what transpired. The Muskoka Riverside Inn submitted its order prior to the deadline for making changes. The order was returned to the consultant and the client notified he had to send the order himself. The client missed the deadline for changing artwork and Tele-Direct ran the old advertising.

[282] L.J. Sunshine Hardwood Flooring. Ad-Vice has sued the customer for breach of contract. In his defence, the customer claims that the Tele-Direct representative advised him that he had been "misrepresented" and should stop payment on his cheque.

refused to pay consultants following a meeting with the Tele-Direct representative. If the customer refuses to pay, the consultant is obliged to take legal action to recover the fees owed.[283] In general, where the consultants have gone to court, they have been successful in having the contract honoured. While it might be argued that the persistent refusals to pay by customers indicates dissatisfaction with the consultants' services rather than reflecting any tactics employed by Tele-Direct's representatives, on the evidence we accept that there is a link between the visit by the representative and the instances of refusal to pay the consultants' fees.

The issue in many of these incidents is whether Tele-Direct made innocent errors, or whether the climate in Tele-Direct towards consultants resulted in what was, in effect, sabotage of the consultants and their customers. An important reason for concluding that there was more than innocent errors at work is the evidence that Tele-Direct was willing to sacrifice the interests of customers by putting them in the middle of Tele-Direct's struggle against consultants. There is more than a hint of malevolence in the formal and explicit decision in the 1990 guidelines not to inform customers when orders submitted on their behalf were being refused (although this was changed in the 1992 guidelines).

(5) Anti-competitive Acts

The Director alleges a number of anti-competitive acts by Tele-Direct involving consultants relating to Tele-Direct's refusal to deal directly with consultants on behalf of advertisers, its discriminatory treatment of customers and customers' orders originating with

[283] Or, evidently, write off the account or accept a reduced fee in settlement, as Mr. Blais did on one occasion.

consultants and its refusal to supply specifications to consultants. None are specifically listed in section 78 of the Act. As the list is not exhaustive, there is no reason not to assess the actions characterized by the Director as anti-competitive acts by Tele-Direct to see if they have the requisite exclusionary, predatory or disciplinary purpose.

The respondents argue that the challenged conduct cannot be anti-competitive because it was generally in accordance with the Tele-Direct guidelines for dealing with consultants, which they say were not intended to and do not prevent the consultants from doing business but rather render Tele-Direct's dealings with consultants "fair and consistent". They further submit that they have valid business reasons for their policy. These "business justifications" will be dealt with in detail for each alleged anti-competitive act.

In a related argument, the respondents submit that, to the extent that the Director is able to prove that Tele-Direct engaged in any of the alleged acts, those acts ceased in 1992 with the implementation of the most recent guidelines for dealing with consultants which have been consistently applied, unlike prior versions. They submit that any practice cannot be caught by section 79 as more than three years have elapsed since it ceased. We do not see validity in the argument. The 1992 guidelines are obviously still in force. The Director has not alleged that it is only the failure to follow the guidelines that is anti-competitive but that certain actions of Tele-Direct, which may not be contrary to the guidelines (refusal to deal directly with consultants on behalf of advertisers) or are simply not dealt with in the guidelines (some discriminatory acts, refusal to supply specifications), are anti-competitive. To the extent that the guidelines sanction conduct that the Director is alleging is anti-competitive, then the Director is, in effect, challenging the guidelines and their application also. The guidelines certainly do not prohibit (and may actually encourage) the particular conduct by Tele-Direct that is the subject of the allegations.

(a) Refusal to Deal Directly with Consultants

The respondents here repeat the argument that we dealt with earlier under the section concerning the abuse of dominant position with respect to publishers and the 20-directory requirement. They argue that a refusal *cannot* be an anti-competitive act and that they are not required to assist their "detractors" by dealing with consultants as that would be akin to placing a positive duty to act on the respondents. As we stated in that section, semantic arguments about whether the act in question is active or passive do little to advance the real issues in dispute. We will therefore proceed to analyze the more substantive arguments without further comment.

The evidence is clear that Tele-Direct has engaged, since the advent of Mr. Harrison and Tel-Ad in 1984, in the specific aspects of refusing to deal directly with consultants on behalf of customers set out under I. in the introduction above. Tele-Direct has refused to act on written instructions received from consultants on behalf of advertisers; refused to act upon oral instructions received from consultants on behalf of advertisers or meet consultants or the advertiser in the presence of consultants to receive same; and refused to deal with consultants on subsequent errors or problems.

In the eastern region between 1986 and 1990, Tele-Direct acted in contravention of its own 1986 guidelines by *accepting* orders from, at least, CEPAC 2000, Ad-Vice and Tel-Ad, as evidenced by the letters. Even those letters, however, make it clear that the order must be accompanied by a letter *from the customer on the customer's letterhead*.

There is also evidence that Tele-Direct refuses to accept oral instructions from consultants. The 1992 guidelines are clear that the Tele-Direct representative must not accept instructions, even indirectly, from anyone other than the customer. While the current guidelines allow the representative to meet with the customer with the consultant present, the representative is not required to do so. The evidence was that most of the time the representative refuses to meet with the customer with the consultant present. Likewise, Tele-Direct would not deal with consultants on follow-up matters on behalf of customers.

We must weigh the anti-competitive effects of the acts against the business justifications put forward by the respondents. There is no doubt that Tele-Direct was trying to make life difficult for the consultants by refusing to deal with them directly on behalf of advertisers. Tele-Direct did not want the consultants to have any legitimacy in their dealings with its customers. The 1990 guidelines were brought in to eliminate the slight leniency that had developed under the 1986 guidelines, which had placed letters from Tele-Direct in the hands of various eastern region consultants confirming that orders coming from them would be accepted and processed by Tele-Direct.

There are two possible types of adverse effects that might arise from Tele-Direct's refusal to deal with consultants acting on behalf of customers. The first is the possible increase in costs to the consultants that would result from having to do business in a somewhat roundabout way, rather than submitting orders directly. The second, and more important, effect is the effect on the consultants' credibility with customers when they have to explain to customers that they are not permitted by Tele-Direct to submit orders directly on their behalf but must use an indirect procedure. This might put the consultants in a negative light in the eyes of the customer, particularly if the customer is already generally aware of the background of acrimonious relations between Tele-Direct and consultants. Against that backdrop, the indirect procedure that the consultants must use for submitting orders to Tele-Direct might appear as a form of subterfuge.

The evidence does not indicate that cost increases to consultants from Tele-Direct's refusal have been a real issue. The consultants' businesses have experienced ups and downs. While Mr. Harrison was unable to grow his business between 1986 and 1992, servicing an average of 60 new accounts a year, in the last few years he has expanded and is now handling 200 to 250 new accounts a year. Mr. Brouillet testified that Ad-Vice revenues from Yellow Pages consulting were at a high between 1992 and 1994 but dropped roughly to 50 percent of that amount in the last two years. He has also diversified into other businesses in recent years. Mr. Blais eventually gave up and left the business.

Although all three of the mentioned consultants testified at the hearing, none of them expressly linked whatever difficulties that they might have experienced to an *increase in costs*.

Even Mr. Blais did not do so. Undoubtedly, the consultants would like to have the advantage of being able to deal directly with Tele-Direct on behalf of advertisers. We find it instructive that Mr. Harrison has been operating since the mid-1980's, and still operates, in spite of Tele-Direct's refusal to deal directly with him in a representative capacity. Evidently, he, and other consultants no doubt, have managed to find an alternative to direct submission of orders that does not impose significant increased costs, or any increased costs at all, on their businesses. We cannot, therefore, identify any adverse cost effects on consultants resulting from Tele-Direct's refusal to deal with them acting on behalf of advertisers.

The question of possible negative reputational effects or damage to consultants' credibility arising from Tele-Direct's refusal to deal with them acting for customers is complex. To the extent that consultants lose reputation or credibility, customers will be less likely to demand their services. We do have evidence from the consultants that they have suffered negative reputational effects. For example, Mr. Brouillet testified that he could not keep sales help because of the negative environment; sales personnel felt they were regarded by advertisers as not legitimate, as "scam" or "con" artists.

Unfortunately, it is difficult to determine whether these effects result from the refusal by Tele-Direct to deal directly or from other actions of Tele-Direct that are not alleged to be anti-competitive. The Director has not challenged as anti-competitive Tele-Direct's general hostility towards consultants, as manifested by the placing of advertising warning customers about consultants, writing letters to customers and sending out its representatives to their premises with messages to the same effect. In our view, the negative reputational effects on consultants are due largely to the general environment created by Tele-Direct rather than the specific refusal to deal directly with consultants acting for advertisers. Any connection between the negative reputational effect or loss of credibility on the part of consultants and the refusal to deal directly is very weak.

We turn to Tele-Direct's business justifications for its consultant guidelines and, thus, for its refusal to accept written or oral instructions from consultants or deal with them on follow-up matters. The respondents' general position is that their refusal to deal with consultants "is clearly an efficient response to the damaging effect of the consultants on their business". They point out that the objective of the consultants is to decrease directory advertising which is exactly the opposite of the respondents' objective, which is, in their words, to sell directory advertising "in order to increase the usage of their directories and produce a more complete directory." Because the consultants generally serve customers on a one-time basis, the respondents take the position that consultants have a "perverse" incentive to "undersell", which detracts from the completeness of the directories.

We have already dealt with the "completeness" argument as part of the analysis of tied selling. As we concluded there, it is far from clear that all increases in advertising (especially size and colour which are targeted by consultants for reduction) contribute to completeness. Therefore, the "upselling" of size and colour by Tele-Direct representatives cannot be assumed to be socially beneficial, nor can the "downselling" of those attributes by consultants be assumed to be socially detrimental. The optimal situation is one in which both points of view are freely available to advertisers so that the advertisers themselves can make the choice.

At paragraph 840 of their written argument, the respondents have also provided the following more detailed justifications for issuing and following their consultant guidelines:

> (i) the consultants do not accept responsibility for payment for the advertising;
>
> (ii) to ensure that the customer is fully informed with respect to the advertising they are purchasing and their available options;
>
> (iii) to ensure customers understand with whom they are dealing;
>
> (iv) to prevent the conflicts that may occur if the Respondents' sales representatives were to take instructions directly from the consultants;
>
> (v) to ensure that advertisers are aware of new programs and initiatives.

We need only deal with the first point. The Director has in effect admitted the validity of the respondents' first business justification, that consultants do not accept financial responsibility for the advertising, by the remedies he seeks. At paragraph 69(b)(iii) of the application, the proposed remedy was:

> . . . that the Respondents accept orders for advertising space on behalf of any party that can satisfy the Respondents' reasonable requirements of evidence of authority to act on behalf of an advertiser and *capacity to pay for the space requested*. (emphasis added)

At paragraph 391 of the written argument, the following further remedy was added:

> . . . that the Respondents be prohibited from requiring that customers who choose to utilize the services of a third party to place advertising be required to enter into a contract directly with the Respondents where the third party who has satisfied the Respondents' reasonable requirements of evidence of authority to

> act on behalf of the advertiser and *where the third party has guaranteed payment on behalf of the principal.* (emphasis added)

These proposed remedies imply that in the Director's view it is reasonable for Tele-Direct to insist on financial guarantees if Tele-Direct is to deal with consultants as representatives of the customer. The consultants do not currently accept any financial responsibility. What the Director has done is to suggest an alternative method of operations for Tele-Direct in its dealings with consultants. He is proposing, in effect, that Tele-Direct begin to deal directly with consultants acting for advertisers by creating a new third sales channel (in addition to the internal sales force and agents).

There is evidence that dealing directly with the consultants would require Tele-Direct to set up an additional interface to deal with them. As described by Mr. Logan of the YPPA, this was the experience of US West, which set up a group of specially trained employees to deal with consultants to avoid problems with its sales force when it dealt directly with consultants. Such direct dealing, therefore, would obviously entail an additional cost to Tele-Direct. Further, Tele-Direct does not currently deal with guarantees in the sense proposed by the Director. Agents, of course, simply pay up front. A system would have to be set up to accommodate this new procedure.

In the circumstances, we think that the additional costs that Tele-Direct would incur if it were forced to deal with consultants directly on behalf of advertisers is a valid justification for not doing so, given that no adverse cost effects on agents were proven and that any negative reputational effects that are attributable to the refusal to deal directly are, at best, weak. We conclude, therefore, that, overall, Tele-Direct is not engaging in anti-competitive acts by refusing to deal directly with consultants on behalf of advertisers and, in particular, by refusing to accept written or oral instructions from, or engage in follow-up communication with consultants acting on behalf of advertisers.

(b) Discriminatory Acts

The discriminatory acts involve Tele-Direct's actions after the customer has submitted an order based on a consultant's advice and the effects that flow therefrom. Notwithstanding Tele-Direct's stated policy, orders submitted by a customer are sometimes returned because Tele-Direct believes a consultant was involved in the preparation of the order. There is no justification for Tele-Direct precluding an advertiser from seeking the advice of a consultant if the advertiser so chooses. Indeed, that is what one part of Tele-Direct's written guidelines states. Yet, the guidelines, even the 1992 guidelines, also mandate the return of certain customer orders. The fact that Mr. De Sève, a senior executive of Tele-Direct, is aware, and apparently condones, the return of customer orders for suspicion of consultant involvement proves that these were not merely isolated instances or errors.

Further, the history of the 1990 guidelines underlines the fact that Tele-Direct was fully aware of and, in fact, sanctioned the foreseen negative consequences of those guidelines for its advertisers. The advertisers' interests were sacrificed in order to hamper the consultants. The effect of the 1990 guidelines, as Tele-Direct itself recognized when they were first drafted, was to place the advertiser in the middle of the battle between Tele-Direct and the consultants, to the detriment of the advertiser.

A document attached to the guidelines identifies "perceived weaknesses" in the guidelines which were to be reviewed with the legal advisors. The first related to the fact that Tele-Direct would be rejecting any package delivered by a consultant or bearing any external indication of consultant involvement even if delivered by the customer or also bearing customer information on its face. Packages would therefore be rejected even though they might contain instructions from the customer on the customer's letterhead. A second concern was whether it was a reasonable business approach not to notify customers that the letter/package delivered to Tele-Direct had been rejected and returned to the consultant. In spite of these misgivings, the new policy was put in place.

The internal document dealing with the incident where 23 orders prepared by Mr. Blais were rejected even though they were under customers' signatures states that legal counsel, in fact, recommended against the procedure in the guidelines which permitted this type of rejection. Counsel, as reported in the letter, was of the view that the customers had the right to deal with whomever they wished in designing their advertising and further had the right to send Tele-Direct their instructions on their letterhead and expect that they would be acted on as coming from them, provided that Tele-Direct was not required to deal directly with the consultant and the correspondence did not carry any consultant identification.

The respondents did not attempt to provide a business justification for rejecting or returning customer orders where there was no evidence of non-compliance with specifications or of late delivery. In the circumstances, we find that the rejection, return, denial of receipt or refusal to process customer orders involving consultants constitute anti-competitive acts.

As noted earlier, the Director is not of the view that Tele-Direct's insistence on visiting a customer after the customer has signed a contract with a consultant and submitted an order to Tele-Direct is by itself an anti-competitive act. He says that the issue relates to what the representative tells the customer and how the order received from the customer is treated. We agree that this is the crux of the difficulty. The anti-competitive acts are those that lead the customers to believe that they will be disadvantaged or that actually harm them because they have used a consultant. These include suspicious errors, last minute contact resulting in confusion for the advertiser about what must be done to have the new advertising run or resulting in missed deadlines, identifying errors or problems in the advertising that would not otherwise be a problem and informing customers that their orders might not be processed. We accept that such incidents occurred and that there is no assurance that they will not be repeated whenever consultants are seen as a threat.

The respondents argue that they were trying in all cases to ensure that their business operated efficiently by requiring consultants to meet deadlines and specifications. We have found that non-compliance with specifications and deadlines were largely pretexts for an attempt to pressure customers into changing their minds about a consultant's recommendations. Most of the incidents in evidence are more accurately characterized as highly disruptive because of the negative impact on customers rather than ensuring the smooth operation of Tele-Direct's business as argued. We have no hesitation in finding that statements or actions by Tele-Direct to discourage advertisers from dealing with consultants by expressly or implicitly indicating that advertisers will thereby be disadvantaged by Tele-Direct constitute anti-competitive acts.

The Director alleges that the respondents discriminate against consultants by refusing to meet with customers to take instructions originating in advice from consultants. On its face this looks very much like the allegation listed in I.(b) and forming part of the refusal by Tele-Direct to deal directly with consultants on behalf of advertisers. Presumably, the discriminatory act being alleged here is a refusal to accept oral instructions from customers using consultants while oral orders from customers not using consultants are accepted and acted on. As has already been noted, Tele-Direct requires that customers using consultants sign Tele-Direct's documents. In and of itself, this is not an anti-competitive act. It might, however, be a discriminatory act if customers not using consultants are not required to sign a contract in like circumstances.

However, the evidence of Mr. Giddings is that, by and large, all of Tele-Direct's customers sign its documents. In fact, Mr. Giddings testified that the only contracts which do not require signing are those contracts renewing advertising worth less than $100. Further, Mr. Giddings indicated that for those contracts which are not signed, if there is a conflict between the customer and the representative as to what advertising was actually ordered, which results in a "write-off", the representative is financially responsible for the write-off. This policy does not seem unreasonable on an operational basis. With respect to orders which Tele-Direct will accept orally from customers dealing with its representatives (that is, those under $100), there is no evidence that consultants deal with or are interested in obtaining clients whose orders are so small. We do not find this allegation to constitute an anti-competitive act.

There is no doubt that those discriminatory acts of Tele-Direct which we have found to be anti-competitive constitute a practice. They are not "isolated acts".

(c) Specifications

The Director submits that Tele-Direct's refusal to supply specifications to consultants is an anti-competitive act. He argues that consultants cannot adequately advise the customers who choose to use their services without up-to-date access to basic technical information. The Director points to evidence of Tele-Direct using alleged non-compliance with specifications to delay orders or discredit consultants in customers' eyes.

(i) Majority View (Rothstein J. and C. Lloyd)

The majority of the Tribunal are unable to agree with the Director for the following reasons. We see the refusal by Tele-Direct to provide specifications to consultants as another manifestation of Tele-Direct's general aversion to having any relationship with consultants. Looking at the experience of consultants and Tele-Direct's refusal to supply specifications to them, the evidence is that this has not adversely affected their ability to compete. Consultants have been in business since 1984 and we have heard of no difficulty experienced by them because Tele-Direct refused to provide them with specifications.[284] In one way or another, they were aware of what Tele-Direct's specifications required.

As to whether Tele-Direct not providing specifications to consultants would cause a problem in the future, Mr. Brouillet stated:

> . . . If there were changes in their specifications and we were not informed about it, then obviously, there would be a problem. If there was really a problem, the client only had to call us within 24 hours, we could fix what was wrong and forward that to Tele-Direct.[285]

There is no evidence before us that suggests that Tele-Direct's specifications change frequently. If anything we are left with the contrary impression from the absence of evidence from consultants that frequent changes were a problem. Mr. Brouillet stated that once a problem is pointed out it can be quickly fixed. On the basis of this evidence, we are satisfied that any

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[284] This is not to say that Tele-Direct did not reject some orders based on non-compliance with specifications. This may have been the fault of the consultant not to conform to the specifications of which he was aware or because Tele-Direct, without justification, wished to create difficulty for a consultant. But Tele-Direct's rejection of orders was not attributable to consultants not being aware of what Tele-Direct's specifications required.

[285] Transcript at 15:2762 (6 October 1995).

changes to specifications will become known by consultants quickly. We, therefore, have no basis upon which to infer that refusal to provide specifications to consultants will, in any material way, adversely affect their ability to compete in the future.

The respondents did not argue the business justification "that customers understand with whom they are dealing" to justify the refusal to supply specifications to consultants, although this was raised as a justification for other acts. However, we are of the view, based on the evidence, that this business justification is applicable here. There is evidence before us of a number of instances in which there was confusion on the part of advertisers as to the exact relationship of a consultant with Tele-Direct.[286]

We infer from the way in which some consultants operate that this confusion could be exacerbated if a consultant, on visiting a proposed customer, is armed with up-to-date specifications obtained from Tele-Direct. There are indications in the evidence that in their initial contact with advertisers, consultants do not go out of their way to distinguish themselves from Tele-Direct. In some cases, the evidence is that the customer remains confused as to the exact relationship between the consultant and Tele-Direct.[287] In other cases, it is apparent that while an advertiser may initially be confused, the fact that the consultant does not represent Tele-Direct

[286] Evidence of Mr. Lee of M & L Service, Mr. and Mrs. Jovandin of L.J. Sunshine Hardwood Flooring, Mr. Fox of Fox & Partners Limited, Mr. Harmic of Dominion Springs Corporation, Mr. McMaster of H.R. Home Renovations. Of course, the consultants blamed Tele-Direct for the confusion and Tele-Direct blamed the consultants. We cannot say for certain how the confusion about the relationship between Tele-Direct and consultants arose in each case but it does appear there was confusion in the minds of some customers.

[287] E.g., Mr. Lee of M & L Service.

eventually becomes apparent. It may become apparent in conversation between the advertiser and consultant or when the advertiser is requested to pay the consultant separate from Tele-Direct. In the case of Ad-Vice, a follow-up letter makes this clear.[288]

However, in our view, it is the initial confusion that creates the difficulty. We do not think consultants should be "getting their foot in the door" of advertisers because of such initial confusion. Being provided with specifications by Tele-Direct could be used by them as a form of "calling card" signifying a relationship with Tele-Direct that does not really exist. Notwithstanding that in many cases the confusion is eventually cleared up, we do think customers are best served when they know from the outset precisely with whom they are dealing and in this case, the relationship or lack of relationship between Tele-Direct and a consultant. We therefore think that Tele-Direct is justified in refusing to provide specifications to consultants and conclude that such refusal is not an anti-competitive act.

While we are not satisfied that the Director has made a case that the refusal to provide specifications to consultants is an anti-competitive act, we are not unmindful that ultimately it is the advertisers that might encounter difficulty if they retain the services of consultants who use incorrect specifications. It is for this reason that we have, in providing for a remedy for discriminatory acts against advertisers, required Tele-Direct, at its option, to take positive steps to revise a customer's order that is not submitted in compliance with its specifications so that the

[288] The package provided by Mr. Brouillet to his clients advises the client that the Tele-Direct representative will be in contact to transfer the advertising program to the Tele-Direct forms.

order complies or advise the customer what is wrong and how the customer may revise the order in accordance with its specifications.

(ii) Minority View (F. Roseman)

In my view, the refusal to supply specifications is an anti-competitive act. While differing from the majority in their conclusion, I accept that there is little evidence of past harm to consultants from the refusal. Nevertheless, consultants may suffer adverse effects in the future should Tele-Direct change its specifications. The consultants will eventually learn of the changes through trial and error but this leaves a considerable degree of uncertainty during an indeterminate transitional period. Therefore, there is the likelihood that the consultants will be significantly hampered so that the refusal to supply specifications should be considered an anti-competitive act given the complete absence of any sound business justification for the refusal.

The respondents have not advanced any valid business justification. They argue that the refusal is justified by the uniqueness and complexity of Tele-Direct's business and its desire to maintain the value and quality of its product. It is difficult to see how avoidable errors in orders prepared by consultants (and submitted by customers) contribute to quality.

I do not accept the majority's view that the evidence supports the conclusion that the availability of specifications to consultants would result in increased confusion on the part of customers as to the consultants' identity and purpose. I agree with the majority that it is impossible to identify the source of the confusion that apparently arose for some customers.[289] However, it is noteworthy that none of the incidents of confusion referred to by the majority was linked to Mr. Harrison[290] but only to Mr. Brouillet. Yet, it is Mr. Harrison who has been able to obtain ongoing access to Tele-Direct's specifications from YPPA through an affiliate in the United States. Because I am of the view that refusal to supply specifications will likely significantly hamper the consultants' ability to compete and that there is no valid business justification for the refusal, I conclude that the refusal constitutes an anti-competitive act.

(6) Substantial Lessening of Competition

The competitive effectiveness of consultants has been reduced as a result of Tele-Direct's practice of discriminatory acts. Consultants incur higher costs as a result of being forced to defend themselves before customers and by having to seek the aid of the courts in enforcing their contracts. These activities require time and expense that could otherwise be spent in attracting and serving customers.

In addition, the consultants' ability to attract new business is negatively affected when their customers are inconvenienced or harmed by Tele-Direct's discriminatory acts. Customers so

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[289] *Supra* note 287.

[290] *Ibid*. All of the incidents cited related to clients of Ad-Vice except for Mr. Fox of Fox & Partners Limited, who was not linked to a specific consultant.

affected are unlikely to be repeat customers or to recommend the services of consultants to other Yellow Pages advertisers.

Although consultants currently service a small portion of the total telephone directory advertising revenue, they are competitively significant. Tele-Direct was forced to respond positively to the presence of consultants by improving its servicing of its customers. Thus, consultants have had and can continue to have a significant positive influence on Tele-Direct's level of service to its customers as Tele-Direct legitimately strives to offset the inroads that consultants make into its sale of Yellow Pages advertising.

It is difficult to arrive at a numerical determination of the effect on consultants of the practice of discriminatory acts we have found to be anti-competitive because the acts are intermingled with other forces that hamper consultants. What we know, however, is that the consultants' ability to compete is limited and fragile as compared to Tele-Direct's virtual monopoly through its control of publishing. Consultants, by the nature of their services, have little ongoing business and must convince advertisers to pay for their services when these advertisers could place advertising in directories without incurring such expense, i.e., the market for their services is necessarily a "thin" one.

Where a firm with a high degree of market power is found to have engaged in anti-competitive conduct, smaller impacts on competition resulting from that conduct will meet the test of being "substantial" than where the market situation was less uncompetitive to begin with.[291] In these circumstances, particularly Tele-Direct's overwhelming market power, even a small impact on the volume of consultants' business, of which there is some evidence, by the anti-competitive acts must be considered substantial. Of course, in the future, in the absence of any order by the Tribunal, there would be no constraint on Tele-Direct intensifying discriminatory acts against consultants and exacerbating an already substantial effect on them. We have no difficulty concluding that Tele-Direct's proven practice of anti-competitive acts has had, is having or is likely to have the effect of lessening competition substantially in the market.

(7) Remedies

The Tribunal recognizes that consultants' interests are antithetical to Tele-Direct's and that Tele-Direct should not be forced to assist consultants. However, consultants must be able to compete with Tele-Direct to provide services to advertisers. Tele-Direct cannot use its market power to impede consultants' activities and to disadvantage customers who wish to retain the services of consultants. On the other hand, Tele-Direct must not be restrained from competing fairly with consultants.

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[291] The approach we adopt is implicit in *Director of Investigation and Research v. Imperial Oil Ltd.* (26 January 1990), CT8903/390, Reasons and Decision at 16, [1990] C.C.T.D. No. 1 (QL) (Comp. Trib.) and in U.S. Dept. of Justice/Federal Trade Comm'n, *Horizontal Merger Guidelines*, (2 April 1992) at 1.51. Although dealing with a consent order, *Imperial* in effect addresses the issue of what constitutes a substantial lessening of competition when there are varying initial degrees of market power by evaluating what is required to cure the alleged substantial lessening of competition. Similarly, the Guidelines view any numerical increase in concentration more severely the higher the initial market share of the acquiring firm.

We have concluded that Tele-Direct's refusal to deal with the consultants directly on behalf of advertisers is not an anti-competitive act. No remedy is provided in this respect. Nor is any remedy provided for Tele-Direct's refusal to provide specifications to consultants.

We have found that Tele-Direct engaged in a practice of discriminatory acts against consultants and customers who use consultants resulting in a substantial lessening of competition. While many of the acts in evidence occurred more than three years before the filing of the Director's application, the practice continues. The practice of these acts is prohibited. Customers using consultants must be treated by Tele-Direct no differently than customers who do not use consultants.

For greater certainty, we elaborate on this remedy. Where a customer uses a consultant and the customer submits an order for advertising in the Yellow Pages, Tele-Direct is prohibited from rejecting the order. Tele-Direct may accept the customer's order without revisiting or contacting the customer to attempt to change the customer's mind. It will be open to Tele-Direct to act on the documents submitted by the customer or, if it considers it necessary, require the customer to sign a Tele-Direct document. If Tele-Direct decides to accept the order as it is, Tele-Direct is prohibited from not processing it or unduly delaying its processing and from refusing to confirm to the customer that the order will be processed as submitted. If the order is accepted and it turns out there is non-compliance with Tele-Direct's specifications, then the order must be processed in accordance with a revision made by Tele-Direct that complies with the specifications or the customer must be advised promptly that the order does not comply with specifications and informed of the exact problem and how to rectify it.

Alternatively, Tele-Direct has the option of providing further advice to the customer to try to convince the customer to change the order submitted. It may do so, including visiting the customer, but it is prohibited from employing the techniques that we have condemned as anti-competitive when doing so. For example, Tele-Direct may not delay until close to the closing date for submitting orders for a directory to contact the customer about alleged problems in the order. Tele-Direct may not advise the customer who used a consultant that the order does not conform to Tele-Direct's specifications or is otherwise unacceptable unless there is a material problem, in which case, Tele-Direct must provide the necessary information so the customer can cure the problem. Tele-Direct cannot use problems with the order in such a way as to leave the customer only with the option of reverting to the prior year's advertisement or having no advertisement appear. Nor may Tele-Direct delay until close to the closing date so that if the Tele-Direct's representative is able to convince the customer to change the order from that recommended by the consultant, that the customer does not have the opportunity of contacting the consultant if the customer wishes further advice from that source.

Subsequent efforts by Tele-Direct to resell the advertisers should be restricted to the merits of the advertising recommended by the consultant. Tele-Direct is prohibited from having its representatives discuss the role of or advisability of using a consultant at this time. We recognize that it may be difficult to distinguish between legitimate "puffing" of Tele-Direct's service and disparaging comments or inferences about the consultant's service. In view of the instances of disparaging comments by Tele-Direct that have occurred, we caution Tele-Direct to ensure that its instructions to its representatives are clear that in their follow-up meetings they are not to disparage consultants. What would be of concern would be evidence of systematic continuous representations that are untrue or that disparage consultants in these follow-up meetings.

For example, it is simply untrue that customers would receive the same advice from Tele-Direct for no cost as from a consultant who charges a fee because Tele-Direct representatives will rarely if ever recommend a reduction in advertising, which is the essence of the consultants' advice. The fact that consultants have a short-term relationship with a customer may be true but comments to this effect are disparaging if made with a view to causing a customer to lose confidence in a consultant's advice, not based on the merits of that advice. Tele-Direct should ensure that in these meetings its representatives restrict their selling effort to the merits of the advertising.

Observation by C. Lloyd and F. Roseman

We would have preferred to see a prohibition on attempted reselling by Tele-Direct's representative after an order was received from a customer. In our view, Tele-Direct has ample opportunity to establish a situation of trust and confidence between its customers and its representatives. If it fails to use its opportunities and customers choose to take the advice of a consultant because they perceive that they have not received quality service from Tele-Direct, then, ideally, that would be the end of the matter for that directory year. We have chosen, however, not to dispute the Director's concession that Tele-Direct should not be precluded from visiting advertisers after they have submitted an order.

X. ORDER

FOR THESE REASONS, THE TRIBUNAL ORDERS THAT:

Definitions

1. In this order,

(a) "market" shall mean a market as defined by Tele-Direct for purposes of its commissionability rules prior to the filing of the application in this matter, and, for greater certainty, there shall in future be no fewer than six markets in Quebec and seven markets in Ontario;

(b) "consultants" shall mean firms which advise telephone directory advertisers on how to increase the effectiveness of and reduce expenditures on telephone directory advertising, primarily in the Yellow Pages, and which assist advertisers in the placement of orders for telephone directory advertising, but does not include firms which are accredited advertising agencies.

Tied Selling

2. The respondents are prohibited from continuing to engage in tied selling, namely tying the supply of advertising space by them to the acquisition of advertising services from them, for customers advertising in six, seven and eight markets.

Abuse of Dominant Position

3. The respondents are prohibited from engaging in the practice of discriminatory acts relating to consultants and customers of consultants.

Remaining Allegations

4. The remainder of the application of the Director is dismissed.

Interpretation

5. The Director or the respondents may apply to the Tribunal for directions or an order interpreting any of the provisions of this order.

Confidentiality

6. As required by paragraph 11(1) of the Confidentiality (Protective) Order issued by the Tribunal on March 30, 1995, the panel determines that a "reasonable period" for the retention, in a secure and organized manner, by the respondents of those protected documents returned to them by the Director upon completion or final disposition of this proceeding and any appeals relating thereto, shall be five years.

DATED at Ottawa, this 26th day of February, 1997.

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

(s) Marshall Rothstein
Marshall Rothstein