

THE COMPETITION TRIBUNAL

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

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

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

BETWEEN:

THE COMMISSIONER OF COMPETITION

AND

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

Applicant

Respondents

OTTAWA, ONT.	Andree Bernier for / pour REGISTRAR / REGISTRAIRE	COMPETITION TRIBUNAL TRIBUNAL DE LA CONCURRENCE FILED / PRODUIT Date: January 19, 2017 CT-2017-002
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NOTICE OF APPLICATION

TAKE NOTICE that the Commissioner of Competition (the “**Commissioner**”) will make an application to the Competition Tribunal (the “**Tribunal**”), on a day and place to be determined by the Tribunal, for an order pursuant to subsection 90.1(1) of the *Competition Act* (the “**Act**”):

- (a) prohibiting the Respondents from doing anything under the Arrangement (as defined below in paragraph 1 of the Statement of Grounds and Material Facts) for a period of 10 years, including, but not limited to:

- i. in respect of existing agency contracts, agreements or arrangements, using or enforcing:
 - a. most-favoured-nation clauses with respect to the sale of E-books in Canada; and
 - b. provisions which directly or indirectly restrict, limit, or impede the ability of an E-book retailer to set, alter, or reduce the retail price of an E-book in Canada; and
 - ii. entering into contracts, agreements or arrangements which contain:
 - a. most-favoured-nation clauses with respect to the sale of E-books in Canada; and
 - b. provisions which directly or indirectly restrict, limit, or impede the ability of an E-book retailer to set, alter, or reduce the retail price of an E-book in Canada; and
- (b) directing the Respondents to pay the costs of this proceeding; and
- (c) such further and other relief as the Commissioner may request and this Tribunal may consider appropriate.

THE ADDRESSES FOR SERVICE ARE:

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Danielle Royal

For Commissioner of Competition:

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Attention: John Syme
Alex Gay
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Katherine Johnson

The Applicant proposes that the hearing of this matter be held in the City of Ottawa, Ontario and be heard in English. The Applicant proposes that documents be filed electronically.

OVERVIEW

1. In 2010, HarperCollins Publishers L.L.C. (“**HarperCollins**”), along with other major publishers and a retailer entered into an anti-competitive arrangement (the “**Arrangement**”) to collectively alter the business model and raise retail prices in respect of the sale of E-books to consumers. Pursuant to the Arrangement, HarperCollins coordinated with its competitors to bring about a collective switch from the existing wholesale model for sales between E-book publishers and E-book retailers to the Agency Model (defined below), underpinned by a most favoured nation (“**MFN**”) provision. Switching the business model to agency allowed the publishers to take control of E-book pricing and eliminate retail price competition for E-books.
2. The Arrangement was formed in the United States between HarperCollins, Hachette Book Group Inc., Verlagsgruppe Georg von Holtzbrinck GMBH, Holtzbrinck Publishers, LLC d/b/a Macmillan, Simon & Schuster Inc. and Apple Inc. It was implemented, first in the United States and then in Canada, by way of agency agreements entered into by publishers, including HarperCollins and its Canadian subsidiary, HarperCollins Canada Limited (“**HarperCollins Canada**”), with E-book retailers. The effect of the Arrangement and the agency agreements is to deprive consumers of retail price competition for E-books and force Canadians to pay substantially more for E-books than they would have but for the anti-competitive conduct of HarperCollins and others.
3. The Arrangement, and the agency agreements through which it was implemented, specifically targeted and continues to target vigorous competition and low prices in the retail market for E-books only. Prior to 2010, both E-books *and* print books were sold by publishers under a wholesale model, which gave E-book retailers the ability to set retail prices and compete as they saw fit, including by offering consumers price discounts. Print books continue to be sold by publishers under wholesale agreements and there continues to be vigorous price competition in the market for print books.
4. For HarperCollins, the Arrangement was a success. However, success came at the expense of Canadian consumers. The implementation of the Arrangement resulted in Canadian

consumers being forced to pay substantially more for E-books than they did under the wholesale model, including at least 18% or more for HarperCollins Canada's E-books.

5. With the inclusion of an MFN provision in the agency agreements, HarperCollins and the other parties to the Arrangement knew that there would be a powerful incentive to transform business relationships with all retailers. The parties to the Arrangement knew that once the market was transformed, it would remain in their collective interest to maintain the Agency Model. This understanding helped to ensure that the Arrangement would endure over time, without need for further communication.
6. The Arrangement to this day remains embodied in agency agreements that HarperCollins Canada and other publishers have with all major Canadian E-book retailers, including Apple Canada Inc. ("**Apple Canada**") and Rakuten Kobo Inc. ("**Kobo**"). The Arrangement's effects continue to be felt by Canadian consumers, who continue to be deprived of competitively priced E-books in Canada.

STATEMENT OF GROUNDS AND MATERIAL FACTS

BACKGROUND

The Parties

Commissioner of Competition

7. The Applicant, the Commissioner of Competition, administers and enforces the *Competition Act*.

HarperCollins Publishers L.L.C and HarperCollins Canada Limited

8. HarperCollins is a US print and E-book publisher incorporated under the laws of the State of Delaware. HarperCollins is a subsidiary of News Corporation, a global diversified media and information services company.
9. HarperCollins is the second largest consumer book publisher in the world. During fiscal 2016, HarperCollins had 239 titles on the *New York Times* bestseller lists, with 30 titles

hitting number one. HarperCollins describes itself as consisting of a number of entities, including HarperCollins Canada.

10. HarperCollins Canada is a Canadian corporation and is also a wholly-owned subsidiary of News Corporation. In addition to being responsible for the HarperCollins' Canadian publishing program, HarperCollins Canada is responsible for the sales, marketing and publicity of HarperCollins' titles in Canada.

Other Market Participants

11. HarperCollins competes with other publishers in supplying print books and E-books to retailers, who subsequently sell them to consumers. In the United States, HarperCollins' major competitors include:

- a. Hachette Book Group Inc. ("**Hachette**"), a US print and E-book publisher incorporated under the laws of the State of Delaware and a wholly-owned subsidiary of Lagardère SCA, a French partnership limited by shares;
- b. Hachette Digital Inc. ("**Hachette Digital**"), a Delaware company and an affiliate of Hachette, and a wholly-owned subsidiary of Lagardère SCA;
- c. Holtzbrinck Publishers, LLC dba Macmillan ("**Macmillan**"), a wholly-owned subsidiary of Verlagsgruppe Georg Von Holtzbrinck GmbH, a Germany-based publishing company, incorporated under the laws of Baden-Württemberg, Germany;
- d. Simon & Schuster, Inc. ("**S&S**"), a US print and E-book publisher incorporated under the laws of the State of New York and a wholly-owned subsidiary of CBS Corporation; and
- e. Penguin Random House LLC ("**PRH**"), a US print and E-book publisher incorporated under the laws of the State of Delaware created on July 1, 2013, as a joint venture between Pearson plc and Random House LLC. Prior to that date, Penguin Group (USA) Inc. ("**Penguin**"), an indirectly-owned subsidiary of Pearson plc, operated as an independent competitor to HarperCollins.

(Hachette, Macmillan, S&S and Penguin collectively, the “Other US Publishers” and, with HarperCollins, the “US Publishers”).

12. In Canada, HarperCollins’ affiliate, HarperCollins Canada, competes in supplying print books and E-books to retailers with, among others:
- a. Simon & Schuster Canada, a Division of CBS Holdings Co. (“**S&S Canada**”), a Canadian corporation and wholly-owned subsidiary of CBS International Inc., a sister company of S&S;
 - b. Hachette Book Group Canada Ltd. (“**Hachette Canada**”), a Canadian corporation and also a wholly-owned subsidiary of Lagardère SCA;
 - c. Macmillan, which operates in Canada directly as opposed to through a wholly-owned subsidiary; and
 - d. Penguin Random House Canada Limited (“**PRH Canada**”), a subsidiary of PRH responsible for the distribution of E-books in Canada formerly published by, among others, Penguin Canada Books Limited (“**Penguin Canada**”), Penguin Group (USA) Inc. and Random House Canada Limited.

The Wholesale Model

13. In the United States today, HarperCollins and the Other US Publishers sell print books to retailers under a wholesale model, as they have for over 100 years. In Canada, they do likewise, either directly in the case of Macmillan or through their affiliates, in the case of HarperCollins, Hachette and S&S. Until 2010, E-books were also sold by HarperCollins and the Other US Publishers to retailers under the wholesale model.
14. Under the wholesale model, a retailer purchases books from a publisher for the wholesale price set by a publisher. The retailer is then free to set the retail price of the books it sells to consumers. That freedom drives rivalry at the retail level and encourages retailers to compete by offering discounts or other pricing inducements to consumers. The print book markets in the United States and Canada are characterized by vigorous price discounting by retailers

which include straight discounts, periodic or seasonal or special event sales or promotions, as well as a variety of innovative offerings and price promotions.

15. As described below, the terms of the agency agreements entered into by HarperCollins and the Other US Publishers, either directly or through their Canadian affiliates, prohibit retailers in Canada from offering discounts and promotions on E-books.

ELEMENTS OF SECTION 90.1 OF THE ACT

The Relevant Product Market Is the Retail Sale of Trade E-books

16. E-books are electronic versions of books (“**E-books**”). The relevant product market is the retail sale of trade E-books, which includes general interest fiction and non-fiction E-books, but excludes self-published E-books. E-books are distributed to consumers by online stores and read on hand-held electronic devices like dedicated e-readers, tablets and mobile phones (“**E-book Devices**”).
17. Media files with audio and video material and audio books are technologically distinct and are not direct substitutes for E-books.
18. Print books are also not direct substitutes for E-books. E-books have a number of features that differentiate them substantially from traditional print books, including:
 - a. Storage and portability – E-book Devices, which are required to operate an E-book, can store an entire library of E-books and are easily transported;
 - b. Ease of purchase – E-books are available for immediate download after online purchase. They do not require a consumer to attend a bricks and mortar location or to wait for, or pay for, delivery after online purchase; and
 - c. Functional optionality – E-book Devices have optional functions that can make reading E-books attractive to consumers, including the ability to adjust font size or lighting, access online dictionaries, bookmark, annotate, highlight text, and access social networking functions to connect to other readers, where desired.

The Relevant Geographic Market is Canada

19. The relevant geographic market is Canada.
20. A Canadian geographic market is consistent with the fact that E-book distribution rights are region-specific, making it difficult for Canadian consumers to substitute to E-books sold by non-Canadian E-book retailers.

HarperCollins is a Party to an Existing Arrangement that Substantially Lessens Competition in respect of the Retail Sale of E-books in Canada

21. In or about early 2010, HarperCollins, certain other publishers and Apple Inc. (“**Apple**”) entered into the Arrangement in respect of the sale of E-books. The Arrangement successfully led to the fundamental transformation of the retail markets for E-books in the United States and Canada. The Arrangement provided for a shift from wholesale agreements, where retailers control retail prices and have the ability to offer consumers discounts, to agency agreements, where publishers control the retail price and have the ability to bar price discounting. The Arrangement also provided for an MFN clause and pricing tiers in the agreements, as further described below.
22. The Arrangement was formed in the United States through a series of communications among the US Publishers either directly or indirectly through Apple. The Arrangement was implemented, first in the United States and then in Canada, by way of agency agreements entered into by publishers and E-book retailers.
23. The US Publishers collectively hold significant market power in the relevant market in Canada, either directly or through their affiliates. The impact of the Arrangement was to increase the publishers’ market power by giving them control over retail E-book pricing and removing the ability for retailers to set E-books prices, including by offering discounts. The publishers took control of E-book pricing in order to increase prices at the expense of Canadian consumers who have been paying significantly higher prices for E-books since 2010.
24. The Arrangement, and its resulting higher prices, continues to this day in Canada.

E-book Competition before Apple's iBookstore

25. In 2007, Amazon.com Inc. (“**Amazon**”) sold its first Kindle e-reader in the United States. At that time, Amazon bought E-books from HarperCollins and the Other US Publishers under wholesale agreements.
26. By 2009, Amazon accounted for almost 90% of all E-book sales in the United States. Amazon used a discount pricing strategy, pursuant to which it priced many best-selling E-books and the E-book versions of newly released hardcover books at \$9.99 USD. To compete with Amazon, other American E-book retailers also adopted a \$9.99 USD retail price for many E-book titles.

The US Publishers and “that wretched \$9.99 price point”

27. HarperCollins and the Other US Publishers despised Amazon’s \$9.99 USD low pricing strategy. They worried that, among other things, \$9.99 USD would become *the* accepted price for E-books in consumers’ minds and their ability to command higher prices for E-books and to maintain their sales of print books in the future would be hampered.
28. An August 14, 2009 email between two senior executives at one of the Other US Publishers noted that the Wall Street Journal was reporting that a hardcover book sold for \$25 to \$35, while the corresponding E-book sold for less than \$10. The email went on to state: “There is that wretched \$9.99 price point becoming a *de facto* standard.” As discussed in greater detail below, in that same email, the executives contemplated cutting off Amazon’s supply of certain E-books as a means of pressuring it to abandon its discount policy. The email concluded by stating that “it would be prudent for you to double delete this from your email files when you return to your office.”
29. HarperCollins and the Other US Publishers wanted Amazon to abandon its pricing strategy, though they did not think they could take Amazon on individually. They recognized that collective action among publishers would be required.
30. On December 1, 2008, a senior executive at a second of the Other US Publishers sent an internal email that indicated that he had agreed with an executive at a competitor “to

exchange information and cooperate very tightly on all issues around e-books and the Kindle.” The email encouraged a colleague to continue discussions with the competitor directly.

31. In an internal email of one of the Other US Publishers dated January 19, 2009, a commitment was made to raise with competitors the options to confront the threat posed by Amazon “in order to control their strategy and pricing.”
32. Another internal email dated July 29, 2009 from the same publisher indicated that “at the heart of our strategy” are discussions among “top publishers” in the United States with the goal to “force [Amazon] to accept a price level higher than \$9.99.” The next day, while expressing continued concern that Amazon’s pricing would lead to “selling content at 7\$. . . [l]ike it works in the music business,” to another executive of the same company, it was noted that he was reassured to know that “none of our competitors” want this to happen either.
33. In 2009, one approach that the US Publishers collectively used to try to move Amazon off its pricing strategy was “windowing”; which involved delaying the release of the E-book versions of new release print books. The US Publishers reasoned that windowing would prevent Amazon from selling the E-book versions of new hardcover books at \$9.99 USD at a time when interest would be greatest.
34. For example, the email dated August 14, 2009 (referenced above), advised that the company’s decision to “window” Senator Edward Kennedy’s biography for 3 months had been communicated “[c]ompletely confidentially...” to a competitor and that the competitor had said that they “... are delaying the new Stephen King ...”
35. In respect of the windowing of the Stephen King book, an email between top executives at the competitor stated that “unless other publishers follow us, there's no chance of success in getting Amazon to change its pricing practices.” The email noted a need to be more confident of “how our fellow publishers will react if we make a move like this” and that “[w]hile I am fairly sure that at least two of them would quickly follow us, our conversation made me feel that I need to shore up that confidence.” The email concluded:

We will keep thinking of how to attack the problem (as we perceive it) of current eBook pricing; as you realize, we think it's too important to ignore. But clearly we need to "gather more troops" and ammunition first!

36. On September 29, 2009, HarperCollins announced that it would “window” Sarah Palin’s book Going Rogue. On the same day, a competitor wrote to Brian Murray, HarperCollins’ CEO, that he was pleased to see that HarperCollins was windowing the E-book. Brian Murray responded that HarperCollins had used the windowing of Senator Kennedy’s biography as its model.

37. On December 10, Brian Murray, CEO of HarperCollins, wrote to others at HarperCollins:

We need to think about how we release the 5-10 delayed e-books. One idea I been (sic) thinking about is that we set up a release schedule (maybe the first and third Monday of each month) where we make these e-books available. Maybe then we get S&S and Hachette to do the same. This would only apply to those e-books that are not published at the same time as the print edition. (emphasis added)

38. By the end of 2009, HarperCollins and certain of the Other US Publishers had announced or implemented a policy of windowing some of their most popular E-books. However, Apple and certain of the US Publishers viewed windowing as an unsustainable practice and wanted to find another way to address the Amazon pricing issue.

The US Publishers take Control of Retail Pricing for E-books with Agency

39. In late 2009, Apple was preparing to unveil the iPad. Apple had planned to launch its E-book retail store, which would compete with Amazon’s E-book retail operations, when it launched the iPad on January 27, 2010. Apple wanted to make sure that its E-book business would be profitable while also avoiding having its pricing undercut by other retailers. The US Publishers’ interest in seeing higher retail prices for E-books aligned with Apple’s desire to have a profitable E-book business.

40. In anticipation of the iPad’s launch, Apple set up back-to-back meetings in New York with, among others, HarperCollins and the Other US Publishers to be held on December 15 and 16, 2009.

41. On December 10, 2009, senior executives at HarperCollins and a competitor spoke to each other regarding Apple's anticipated entry into the E-books market. They also discussed a new business model for the sale of E-books – agency – whereby publishers would set the retail price of E-books and retailers' commissions would be set at 30% of the retail sale price. The executives agreed to confer internally at their respective companies and then circle back to continue their discussion. At HarperCollins, a number of senior executives, including CEO Brian Murray, were made aware of the discussion the company was engaged in with a direct competitor.
42. On December 10, 2009, having spoken with Apple, HarperCollins began work on a proposal for Apple. Aware that Apple also was going to speak to Random House, Brian Murray wrote in an internal email that HarperCollins's proposal to Apple should "bring RH in if possible." Five minutes later, Brian Murray emailed the Random House CEO and requested that the two meet the next day. They did not meet the next day, but they did speak by phone. Ultimately, Random House elected not to be part of the Arrangement; HarperCollins, Apple and the Other US Publishers continued their discussions without them.
43. For its meeting with Apple, HarperCollins prepared a presentation proposing the Agency Model and containing its "keys to winning" the E-books market, which set out criteria for dealing with Amazon. The presentation suggested that Apple consider entering into agreements under the Agency Model not just with HarperCollins, but with publishers generally.
44. On December 15 and 16, 2009, the CEOs of HarperCollins and the Other US Publishers met separately in New York with Apple.
45. In these meetings with Apple, the US Publishers expressed their discontent with Amazon's pricing and also discussed windowing as a way of addressing the problem. Apple expressed the view that windowing was not a good solution.
46. In their meetings with Apple, HarperCollins and one of the Other US Publishers made essentially the same Agency Model proposal. Rather than selling E-books under the wholesale model, HarperCollins and its competitor proposed that Apple enter the E-books

market using what would become referred to as the “**Agency Model**”. Under the Agency Model, E-book retailers would continue to sell E-books to consumers, but they would no longer have control over the retail price. Instead, E-book prices would be set by publishers and E-book retailers would earn a commission on each sale.

47. While Apple was initially resistant to the Agency Model, it quickly determined that the Agency Model provided a means to deal with the Amazon pricing issue in a way that would benefit Apple, as well as the publishers.

The Move to the Agency Model

48. Having decided to pursue the Agency Model, Apple became a hub of communications in moving the competing US Publishers toward the Arrangement.
49. On January 5, 2010, Apple sent substantially the same email to HarperCollins and the Other US Publishers. The e-mail to HarperCollins (CEO Brian Murray) stated:

After talking to all the other publishers and seeing the overall book environment, here is what I think is the best approach for ebooks.

Just like the App Store, we are proposing a principal-agency model with you, (...) In exchange for acting as your agent iTunes would get a 30% commission for each transaction. (...)

So that we could efficiently manage our agency role, we propose a corresponding range of prices for books at various stages in a book's publication and distribution evolution. (...)

There are several things we have to accomplish in order to sell ebooks at realistic prices -

- books need to be cheaper to buy than physical
- you should make less per book since significant costs have been eliminated but still have a healthy, profitable sale
- all resellers of new titles need to be in agency model

We think these agency terms accomplishes all the goals we both have.

50. On January 11, 2010, Apple emailed, among others, each of HarperCollins and the Other US Publishers, enclosing substantially identical draft agency agreements. The draft agreements provided for the Agency Model as Apple had described it: the publishers would set the retail

price of the E-books and Apple would get a 30% commission of each sale. However, rather than including a term requiring that all retailers be on the Agency Model, Apple included an MFN provision. The drafts also included proposed price ranges called “pricing tiers”.

The MFN Provision

51. The MFN provision provided a powerful incentive for the publishers to move all retailers to the Agency Model.
52. The MFN provision required the publishers to reduce Apple’s retail price for any given title to match another retailer’s price, if that title was available for sale, by a different retailer, for less while maintaining Apple’s commission to 30% of the retail price. In short, it guaranteed Apple that the E-books in its iBookstore would always be sold for the lowest retail price available in the market, even if the publishers were not able to sign other retailers, including Amazon, to an agency agreement.
53. The MFN provision therefore incited all the publishers who were part of the Arrangement to switch their agreements with all E-book retailers to the Agency Model. Without the pricing control that agency afforded, an E-book retailer operating under the wholesale model would be able to set retail prices and could offer consumers a discount on any given E-book and the publisher would then have to adjust Apple’s agency price downward to match that discount.
54. The MFN provision virtually guaranteed the transformation of the business model for E-books to agency and helped to ensure that once that transformation took place, the Agency Model, which had at its heart the goals of increasing E-book prices and eliminating retail price competition, would endure.

Pricing Tiers

55. Another feature of the agency agreements circulated to the US Publishers was pricing tiers which applied to the E-book versions of newly released hardcover books. The pricing tiers established maximum E-book prices based on list price ranges for the corresponding new release hardcover books. For example:

Hardcover List Price (USD)	E-book price (USD)
\$25.01-27.50	\$12.99
\$27.51-\$30.00	\$14.99
\$30.01-\$35.00	\$16.99

56. The pricing tiers Apple proposed were identical for all of the US Publishers and contemplated higher prices for the vast majority of E-books that were at that time being sold by Amazon for \$9.99 in the United States.

Apple and the US Publishers Conclude Agency Agreements

57. Over the two-week period following January 11, 2010, Apple and the US Publishers engaged in negotiations regarding certain aspects of the draft agreements. Importantly, these negotiations did not include discussions regarding whether the agreements should reflect the wholesale model as opposed to the Agency Model.

58. Over this same period, Apple kept each of the US Publishers informed as to the progress of its publisher competitors in moving toward the finalization of the agency agreements. In addition, the US Publishers had a number of discussions with each other, including at the CEO level, regarding the move from wholesale to agency. Among other things, individual publishers wanted to ensure that the other publishers would be proceeding with agency.

59. The implications of the shift from wholesale to agency were clear. On January 22, 2010, Michael Serbinis, then Kobo's CEO, reported from New York to Heather Reisman, CEO of

Indigo Books & Music Inc., a leading Canadian print book retailer with a more than 50% ownership interest in Kobo, that the entire industry model was changing. In terms of agency, Michael Serbinis reported:

Pubs want it; they set the price, we get a commission of 30%. Prices will vary from 16.99 / 14.99 / 12.99 – this will make us far more profitable; but take away price control from us / everyone – They are not there yet, but working hard down to the wire over the weekend – They will ‘use’ Apple as a catalyst to change their model – Apple was here working to make it happen – Amazon was here working to fight it as the change in terms will apply to everyone selling ebooks ... If enough Publishers get there, we’ll see an announcement. If not, we won’t.

60. In the three-day period from January 24 to 26, 2010, HarperCollins and the Other US Publishers each entered into substantively identical agency agreements (the “**US Agency Agreements**”) with Apple, all of which contained an MFN provision and pricing tiers.
61. The execution of the US Agency Agreements coincided with Apple’s launch of the iPad on January 27, 2010. The iBookstore went live in the US on March 31, 2010.

Amazon is Forced onto Agency

62. Having signed agency agreements with Apple, HarperCollins and the Other US Publishers moved quickly to force Amazon into agency agreements. On January 27, 2010, Brian Murray (HarperCollins) circulated an internal email with the subject line “Apple Cheat Sheet: Highly Confidential”. Brian Murray wrote:

Windowing

We will make new releases (defined as at least the first 7 months) available to retailers on an agency model.

Implications: If Amazon, B&N, and Sony want our books as new releases, they must adopt our agency model and terms. We have just begun conversations with these partners.

63. The first US Publisher to engage with Amazon did so with the knowledge that HarperCollins and the Other US Publishers would follow its lead. Amazon resisted the move to agency. After its January 28, 2010 meeting with Amazon, the US Publisher wrote in a letter to its authors and the literary community more generally:

This past Thursday I met with Amazon in Seattle. I gave them our proposal for new terms of sale for e books under the agency model which will become effective in early March. In addition, I told them they could stay with their old terms of sale, but that this would involve extensive and deep windowing of titles. By the time I arrived back in New York late yesterday afternoon they informed me that they were taking all our books off the Kindle site, and off Amazon.

64. In a February 2, 2010 email to an executive at Amazon, the US Publisher that had engaged with Amazon made it clear that the purpose of the Arrangement was to re-gain control of pricing at the retail level. He wrote:

(...) [w]e cannot budge on the final price that the consumers pay for our books
(...) That is the very heart of the agency model, and it is why we are doing this
(...) [W]e cannot give up control of price. If we do we are much worse off than we were before.

65. Facing a united publisher front and the threat of losing access to E-books, Amazon capitulated and in February and March 2010 signed agency agreements with HarperCollins and the Other US Publishers.

66. After securing Amazon's move to agency, HarperCollins and the Other US Publishers quickly moved other E-book retailers to substantially similar agency agreements. Between January and June 2010, the US Publishers and Apple transformed the retail E-books market in the United States from a market characterized by aggressive price competition and innovative promotions to effectively eliminating any retail price competition on E-books.

HarperCollins, the Other US Publishers, and Apple either Directly or through an Affiliate, Implement the Arrangement in Canada

67. Amazon made the Kindle available in Canada in fall 2009. However, at that time, Amazon sold E-books to Canadian consumers only through amazon.com, its American online store.

68. The leading E-book retailer in Canada in 2009 was Kobo. Despite its leading market position in Canada, Kobo responded to Amazon's discount pricing and began discounting certain best-selling and new release E-books.

69. As early as 2009, E-book pricing and Amazon's pricing strategy as it related to Canada had also been a concern for HarperCollins and the Other US Publishers. On November 10, 2009, David Kent, CEO of HarperCollins Canada, emailed Brian Murray (HarperCollins), stating in part as follows:

Yes, I do want to review [e-book pricing] with you, now that Canada has (finally) worked out how we can have the Kindle (...) I've been following the whole pricing situation, which sometimes seems surreal, so we'll need your guidance on our pricing policies to parallel yours in the US.

70. Apple, too, wanted to adopt a single business strategy for E-books and E-book pricing across North America and never contemplated anything other than the Agency Model for Canada.

71. From the outset of the discussions between Apple and HarperCollins and the Other US Publishers in December 2009, it was contemplated that the move from wholesale to agency for E-books would apply to both the United States and Canada.

72. An internal HarperCollins email circulated among senior executives at the company following its meeting with Apple on December 16, 2009 referenced Apple's coming iPad/iBook launch and, in terms of sequencing, indicated:

Phase I launch will be in the US and Canada; Phase II will be in 23 other countries including the UK and ANZ.

73. To similar effect, minutes from a HarperCollins Executive Committee Meeting held on December 21, 2009, state in respect of Apple's planned entry into the E-book market:

- Apple
 - Met with all publishers confidentially. "Entering eBook business." Will accommodate enhanced ebooks, \$15.99 price. Providing terms this week.
...
 - US and Canada immediately, Europe slightly later. ...

74. Canada's inclusion as part of the Arrangement was reflected in the draft agreements circulated by Apple to the US Publishers on January 11, 2010, as well as in the US Agency

Agreements executed by HarperCollins and the Other US Publishers in late January 2010, which included Canada as forming part of the “Territory” covered by those agreements.

75. On March 5, 2010, Leslie Hulse, HarperCollins’ SVP, Digital Business Development, in an email to David Kent and Steve Osgoode, then HarperCollins Canada’s CEO and SVP Digital respectively with the subject “Agency Roll-Out in Canada” wrote:

FYI: We heard this week from both Amazon and Apple that they won’t be ready to roll out agency in Canada at the same time that they roll out in the US, so we’ve adjusted our contracts with all agents ... to address the sales of the HC-US catalog into the US only.

We’re assuming we can roll out agency in Canada once the legal due diligence has been done and Apple is ready to lead the charge.

76. On March 24, 2010, Apple sent essentially the same email to HarperCollins and the Other US Publishers:

Like me, I’m sure you’re focused intently on the US launch right now. However, I was wondering if you have time (...) to spend 15 minutes talking about pricing and other issues re: Canada. I want to be able to move quickly after the US launch to follow with Canada.

77. On April 22, 2010, Apple sent draft agency agreements for Canada to the US Publishers. On May 11, 2010, Apple sent another round of draft agency agreements for Canada to, among others, HarperCollins, Macmillan and S&S, with the message: “you spoke and we listened. Here’s the new version of the Canada deal.” By May 17, 2010, Apple had also sent terms of the proposed Canadian agency agreement to Hachette.

78. Apple’s draft agreements were prepared as amendments to the US Agency Agreements and incorporated by reference the key substantive terms of those agreements, including the MFN provision.

79. HarperCollins Canada, Hachette Digital Inc. and S&S Canada signed agency agreements with Apple Canada in June 2010, just prior to Apple’s launch of the iPad in Canada and the launch of iBookstore.ca on July 1, 2010. Macmillan signed an agency agreement with Apple Canada in November 2011.

80. The Arrangement was operationalized in the United States by HarperCollins and the Other US Publishers through the US Agency Agreements. In Canada, the Arrangement was operationalized by HarperCollins and the Other US Publishers entering into, either directly or through their affiliates, agency agreements with Apple Canada, Amazon and Kobo, as well as other E-book retailers doing business in Canada in the period from June 2010 to November 2011.
81. Though the time it took to transform the market from wholesale to agency was longer in Canada than the United States, HarperCollins, Apple and the Other US Publishers did not waver from their decision to bring about that transformation. They could never have done so without the Arrangement and the collective action required to, among other things, force Amazon over to agency.
82. The Arrangement with respect to Canada continues to exist, as reflected in the agency agreements of each of HarperCollins Canada, S&S Canada, Hachette Digital Inc. and Macmillan with Apple Canada, Kobo and Amazon.

The Arrangement Substantially Lessens Competition in the Relevant Market for the Retail Sale of E-books in Canada

83. The Arrangement, as implemented by way of agency agreements in Canada between each of HarperCollins Canada, Simon & Schuster Canada, Hachette Digital Inc. and Macmillan with each of Apple Canada, Kobo and Amazon, enhances the collective market power of those publishers and prevents and lessens competition substantially in the relevant market. The market power of those publishers is derived in part from their collective market share in the E-books market in Canada and is demonstrated by, among other things, their collective ability to successfully alter the pricing model for the retail sale of E-books. But for the Arrangement, the relevant market for the sale of E-books in Canada would be substantially more competitive.

The Arrangement Provides for a Market Structure which is Inherently Anti-Competitive

84. The terms of the Arrangement included a shift to the Agency Model which included uniform pricing across all retailers for any given E-book covered by the relevant agency agreements

and a prohibition against retailer discounting. Whereas, prior to the implementation of the Arrangement in Canada, the retail E-books market had been marked by vigorous competition among retailers; after implementation, retail price competition was and remains thwarted. Collective action by market participants aimed at eliminating the most significant form of rivalry and differentiation among retailers is inherently anti-competitive and undermines market forces.

85. But for the Arrangement, E-books would have continued to have been sold in Canada under the wholesale model (as print books are to this day) and price competition in the relevant market for E-books in Canada would have continued and would exist today.
86. Neither Random House LLC nor Random House of Canada Limited (collectively, “**Random House**”) were parties to the Arrangement. However, following the implementation of the Arrangement in Canada through agency agreements entered into by its largest competitors, Random House of Canada Limited converted its Canadian E-book distribution business to the Agency Model. In 2015, after Penguin and Penguin Canada’s Canadian agency distribution agreements were terminated, sales of Penguins’ E-books were either incorporated into Random House of Canada Limited’s existing agency agreements or replaced by new agency agreements entered into by PRH Canada.
87. The fact that other publishers who were not party to the Arrangement adopted the Agency Model after the Arrangement was implemented does not imply that the E-books market was inevitably going to move to agency. While Random House eventually moved its business to the Agency Model, it did so well after the Arrangement forced a shift in the rest of the E-books market. Given that, when first presented with the opportunity to join the Arrangement and move to agency along with its competitors, Random House elected to remain on the wholesale model, it stands to reason that Random House would not have later changed business models but for the Arrangement.
88. The Arrangement, which exists as a result of the collective action by HarperCollins and others, and the resulting prohibition against retail price competition which it engendered, is inherently anti-competitive and, by itself, results in a substantial lessening of competition in the relevant market for E-books in Canada. The Arrangement’s impact on competition is

exacerbated by the fact that other publishers who were not party to the Arrangement eventually converted to the Agency Model as well.

E-book Prices in Canada Increased Substantially Following Agency Implementation

89. Following the shift from wholesale to agency in Canada, retail prices for E-books sold by HarperCollins Canada, S&S Canada, Macmillan and Hachette/Hachette Digital increased substantially over what they had been under the wholesale model. These average increases measure from 6% to 33%, on a quantity weighted basis. In respect of HarperCollins Canada, in particular, the move from wholesale to agency in Canada led to average increases in the Canadian retail prices of its E-books that measure from 18% to 32%, on a quantity weighted basis.
90. Though prices of HarperCollins' and the Other US Publishers' E-books sold in Canada varied over time since the implementation of the Agency Model in Canada, they have never reverted to their pre-agency levels and remain substantially higher today than would have been the case but for the Arrangement and the resulting shift from wholesale to agency.
91. Prior to the implementation of the Agency Model in respect of E-books in Canada by HarperCollins and the Other US Publishers, whether directly or through their affiliates, Amazon aggressively discounted both print books and E-books. Through its amazon.ca website, Amazon has continued to this day to offer Canadian consumers significant discounts on print books to attract consumers from rival retailers.
92. By contrast, for those E-books published by HarperCollins, Hachette, S&S and Macmillan, as well as E-books published by certain other publishers, there is an absence of retail price competition. Had HarperCollins and the Other US Publishers not entered into the Arrangement and forced Amazon to abandon its discount pricing policy, Amazon would have undoubtedly continued to offer discounts on E-books and that, as in the print book market, the E-book market would have continued to be marked by vigorous price competition among a broad variety of sellers.

93. Instead, since the adoption of agency in Canada, HarperCollins Canada, Hachette Canada, S&S Canada and Macmillan's retail prices for any of their respective E-books have in large measure been uniform across all retail channels.

94. By way of illustration, on or around June 19, 2010, after agency had been implemented in the United States but before it was implemented in Canada by HarperCollins and the Other US Publishers, their books on the Globe & Mail Best Seller list were priced differently by various retailers, as illustrated below:

Retail Price Comparison of Globe & Mail Best Sellers On or Around June 19, 2010 (CAD)				
Publisher	Title	Kobo Price	Amazon Price	List Price
Random House	The Passage	\$14.99	\$16.85	\$27.00
Macmillan	Heart of the Matter	\$10.69	\$10.11	\$26.99
Hachette	Robert Ludlum's TM The Bourne Objective	\$14.99	12.99*	\$14.99
Hachette	The Lion	\$14.99	12.99*	\$12.99
Harper Collins	The Carrie Diaries	\$10.59	\$9.52	\$14.99
Hachette	Innocent	\$14.99	\$12.99	\$12.99
Harper Collins	Sh*t My Dad Says	\$9.21	\$8.54	\$11.99
Random House	Nomad	\$10.99	\$10.99	\$27.95
Penguin International	Savor the Moment	\$10.69	\$9.99	\$16.00
Penguin USA	The Spy	10.69*	\$12.99	\$27.95
WW Norton	The Big Short Inside the Doomsday Machine	\$9.93	\$10.35	\$27.95
Harper Collins	Medium Raw A Bloody Valentine to the World of Food and the People Who Cook	\$10.20	\$11.99	\$20.99
Random House	I Shall Not Hate	\$10.32	\$10.67	\$27.95
Random House	Hitch22	15.69*	\$16.84	\$26.99
Harper Collins	A Funny Thing Happened on the Way to the Future Twists and Turns and Lessons Learned	10.69*	\$9.52	\$17.99

* These books were not sold by Kobo or Amazon on June 19, 2010. These prices reflects prices for a previous day.

95. By contrast, on December 21, 2016, the pricing for HarperCollins and the Other US Publishers' Globe & Mail Best Selling E-books were uniform as illustrated below:

Retail Price Comparison of Globe & Mail Best Sellers On December 21, 2016 (CAD)				
Publisher	Title	Kobo Price	Apple Price	Amazon Price
Penguin Random House	Island Of Glāgs: Book Three Of The Guardians Trilogy	\$13.99	\$13.99	\$13.99
Penguin Random House	The Whistler	\$15.99	\$15.99	\$15.99
Penguin Random House Canada	Do Not Say We Have Nothing	\$14.99	\$14.99	\$14.99
Simon & Schuster	The German Girl	\$11.99	\$11.99	\$11.99
HarperCollins Canada	The Nest	\$13.99	\$13.99	\$13.99
House Of Anansi*	The Best Kind Of People	\$14.59	\$11.99	\$9.66
Hachette Book Group	Two By Two	\$17.99	\$17.99	\$17.99
Simon & Schuster	Secret Path	\$13.99	\$13.99	\$13.99
Penguin Random House	99: Stories Of The Game	\$16.99	\$16.99	\$16.99
Simon & Schuster	Born To Run	\$14.99	\$14.99	\$14.99
Penguin Random House Canada	Born A Crime	\$15.99	\$15.99	\$15.99
Simon & Schuster	The Girl With The Lower Back Tattoo	\$14.99	\$14.99	\$14.99
Simon & Schuster	Bleeding Blue: Giving My All For The Game	\$14.99	\$14.99	\$14.99
Simon & Schuster	Scrappy Little Nobody	\$13.99	\$13.99	\$13.99
Greystone*	The Hidden Life Of Trees: What They Feel, How They Communicate	\$19.29	\$16.99	\$14.25

*Independent publishing companies

96. Regardless of the time period considered post-agency implementation in Canada, the result is the same: uniform pricing for E-books at substantially higher price levels than would have been the case but for the Arrangement as illustrated in the foregoing table. Moreover, notwithstanding the fact that Random House Canada was not a party to the Arrangement and that the agreements that Penguin entered into pursuant to the Arrangement have been terminated, PRH Canada E-books tend to be priced at levels which are comparable to, or aligned with, the elevated prices of E-books of the parties to the Arrangement.

Subsection 90.1(2) Factors

(a) Foreign Competitors

97. The US Publishers are four of the largest trade E-book publishers in the world, which operate globally. There are no foreign competitors who provide or are likely to provide effective competition to HarperCollins Canada, Hachette Canada, S&S Canada and Macmillan. As noted above, PRH already sells E-books in Canada under the Agency Model. In this regard,

it is noteworthy that those firms have been able to sustain the prices of their E-books at substantially elevated levels for years after their transformation of the Canadian market to agency.

(b) Product Substitutes

98. There are no acceptable substitutes for E-books. Consumers choose E-books for many reasons, including price, portability or functional optionality. Print books are not acceptable substitutes. The fact that HarperCollins Canada, Hachette Canada, S&S Canada and Macmillan have been able to sustain the prices of their E-books at substantially elevated levels for years after their transformation of the Canadian market to agency is apposite in respect of this factor as well.

(c) Barriers to Entry

99. There are high barriers to entry as an effective and sustainable E-book publisher or retailer.

100. Entry as a publisher requires, among other things, access to content in the form of saleable written works. Competition for saleable authors among publishers is fierce. Leading authors typically choose publishers that are able to provide them with the various services including editing, book design, sales and market support, as well as distribution capability to reach reading audiences through a variety of channels, including bricks and mortar and online; in a variety of forms, including print and E-book.

101. Entry as a retailer depends on building a large catalogue of book titles and the ability to license E-book apps on electronic devices. Establishing an E-book catalogue depends on establishing distribution relationships with most or all of the largest trade E-book publishers in the world.

102. Kobo, Amazon and Apple all have E-book apps that are distributed to consumers through their own electronic devices. A new entrant has two options for bringing E-book apps to market. One, develop their own device, or, two, develop their own application to license on electronic devices. Both options involve very significant lead-times, risk, research and development and marketing costs.

(d) Remaining Competition

103. Currently, every major publisher and every major retailer in Canada operates on an Agency Model in respect of E-books.

RELIEF SOUGHT

104. The Commissioner therefore seeks an Order from the Tribunal pursuant to subsection 90.1(1) of the Act:

- (a) prohibiting the Respondents from doing anything under the Arrangement (as defined below in paragraph 1 of the Statement of Grounds and Material Facts) for a period of 10 years, including, but not limited to:
 - i. in respect of existing agency contracts, agreements or arrangements, using or enforcing:
 - a. most-favoured-nation clauses in with respect to the sale of E-books in Canada; and
 - b. provisions which directly or indirectly restrict, limit, or impede the ability of an E-book retailer to set, alter, or reduce the retail price of an E-book in Canada; and
 - ii. entering into contracts, agreements or arrangements which contain:
 - a. most-favoured-nation clauses in with respect to the sale of E-books in Canada; and
 - b. provisions which directly or indirectly restrict, limit, or impede the ability of an E-book retailer to set, alter, or reduce the retail price of an E-book in Canada; and
- (b) directing the Respondents to pay the costs of this proceeding; and

(c) such further and other relief as the Commissioner may request and this Tribunal may consider appropriate.

DATED AT Gatineau, Quebec, this 19th day of January, 2017



John Pecman
Commissioner of Competition

SCHEDULE "A"
CONCISE STATEMENT OF ECONOMIC THEORY

CONCISE STATEMENT OF ECONOMIC THEORY

1. Hachette Book Group Inc., Hachette Digital Inc. , HarperCollins Publishers L.L.C., Holtzbrinck Publishers, LLC dba Macmillan (“Macmillan”), Simon & Schuster Inc. and Penguin Group (USA) Inc. are publishers of electronic trade books (“E-books”) in the United States. In 2010, those E-book publishers entered into an arrangement to switch their business model from wholesale to agency in the United States and Canada. The arrangement was implemented in Canada by their respective affiliates: Hachette Book Group Canada Ltd., HarperCollins Canada Limited, Simon & Schuster Canada, a division of CBS Corporation and Penguin Canada Books Limited or directly in the case of Macmillan (collectively “E-book Publishers”).
2. Apple Canada Inc. (“Apple”) is an e-book retailer. It makes E-books available to Canadian consumers through its E-book retail store. Apple is a subsidiary of Apple Inc., which is a party to the arrangement and was instrumental to its creation.
3. E-books are electronic versions of books. Trade books are general interest works of fiction and non-fiction (e.g., fiction, biography, business). Retailers distribute E-books to consumers via a website. Consumers can access this website and make purchases using a personal computer, E-reading device or a hand-held device such as a tablet or smartphone.
4. The relevant product market is the retail sale of trade E-books excluding self-published E-books.
5. E-books are in a separate market from print books. E-books have a number of distinguishing attributes: many E-books can be stored on one electronic device making them easily portable; E-books are immediately available after purchase; and E-books provide readers with the ability to adjust font sizes and lighting, use a built-in dictionary and add annotations, highlights or bookmarks. Print trade books typically sell for higher prices. In light of these facts, a hypothetical monopolist in the retail sale of trade E-books would profitably impose a small but significant and non-transitory price increase. In fact, evidence shows that the arrangement increased prices of E-books substantially in Canada.
6. The relevant geographic market is Canada. The E-book Publishers and Apple do business throughout Canada. E-book distribution rights are region-specific, making it difficult for Canadian consumers to substitute E-books sold by non-Canadian E-book retailers for E-books sold by Canadian E-book retailers.
7. E-books have typically been sold either under the wholesale model or the agency model. Under the wholesale model, an E-book publisher sells the E-book to the retailer and the retailer then re-sells the E-book to the final consumer. The choice of the final selling price to the consumer is determined by the E-book retailer. Under the agency model, the retail price of an E-book is

determined by the publisher and the retailer acts as the publisher's agent in facilitating the sale to consumers. A percentage of the selling price is paid to the E-book retailer as a commission for facilitating the sale. With the agency model, publishers have full control over retail prices.

8. Collectively the E-book Publishers have market power in the relevant market.
9. Over the years 2010 and 2011, E-book Publishers entered into agency contracts with Apple that contained a "most favoured nation" ("MFN") clause. This clause provided a guarantee to Apple that the price of an E-book offered for sale by any of the E-book Publishers on Apple's E-book store would not be priced higher than the same E-book on a rival retailer's website or platform. If the price of an E-book sold through a rival retailer was lower than the price on Apple's E-book store, that publisher would have to reduce its price on Apple's E-book store to match the lower price.
10. The MFN clause re-enforced the understanding that the E-book Publishers would switch all E-book retailers to the agency model. If, for example, HarperCollins allowed a retailer to determine retail E-book prices by remaining on the wholesale model, it risked that retailer undercutting Apple's E-book prices. In this circumstance, the MFN clause would require HarperCollins to reduce its prices on the Apple site to match the low retailer determined price. The revenue that HarperCollins would lose from having to match low prices set by a retailer provided it with a strong incentive to maintain control of setting E-book retail prices across all retailers.
11. Apple also benefited from the MFN clause because it guaranteed that Apple's E-book prices would never be greater than those of other retailers including those that may have had a reputation of being a "low-price" retailer. By maintaining high prices, the MFN also allowed Apple to enjoy high margins on E-book sales. Taken together, the agency model combined with the MFN eliminated an important dimension of competition – competition among E-book retailers on setting prices for all E-books offered by the E-book Publishers.
12. One E-book publisher acting individually would not have been able to impose the agency model on a retailer who had a large volume of its sales. Specifically, the value of that retailer's sales to the publisher would provide the retailer with the leverage to resist a change from the wholesale model to the agency model if that retailer felt that the wholesale model was more in its interest.
13. E-book Publishers could more easily defeat retailer resistance from transitioning from the wholesale to the agency model by working collaboratively. Specifically, while a retailer which objected to the switch to the agency model might be able to take steps to punish one publisher acting alone, it would be significantly more costly and difficult for that retailer to punish several publishers at once.

14. Entry by competitors is unlikely to occur in a timely and sufficient manner due to, among other things, barriers to entry into the market for the retail sale of trade E-books in Canada. To become an effective E-book publisher requires, among other things, a strong reputation in providing editing, book design and other services so as to be able to attract authors who produce saleable written work. To become an effective E-book retailer requires establishing distribution relationships with all large E-book publishers and the ability to widely distribute E-books through various electronic devices.

15. Based on the above, it is likely that the arrangement provided HarperCollins and other E-book Publishers with an increased ability to exercise market power that would likely result in a substantial prevention or lessening of competition. The arrangement was implemented by Apple and E-book Publishers and led to substantial increases in prices for E-books in Canada. With agency contracts through which the arrangement was implemented remaining in place to this day, E-book prices in Canada would be expected to be above levels that would have existed but for the switch from wholesale to agency.