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EXCLUSIVITY CLAUSES AND FREE TRADE

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The recent Superior Court decision involving two Curves and Énergie Cardio franchisees, [403-9971 *Canada inc c Place Lasalle Property Corporation*, 2014 QCCS 3153, <http://www.canlii.org/en/qc/qccs/doc/2014/2014qccs3153/2014qccs3153.html> (2014-07-02) Peacock J.] reveals the fact that exclusivity clauses, although interpreted restrictively by courts, are generally valid. The question arises, where an exclusivity clause prevents the lessor from renting commercial space to anyone who competes with its existing tenants, could the Canadian *Competition Act*¹ (“Act”) be called to the rescue and used to invalidate the exclusivity clause because it unreasonably restricts commercial freedom?

1. The *Competition Act* and Canadian courts’ approach

Exclusivity clauses such as the one described above are common place and generally valid². They often become the subject of litigation³ but courts usually limit their analysis to interpreting these clauses, thereby upholding, at least implicitly, their validity. A Canadian court has yet to invalidate an exclusivity clause because it unduly limits free trade⁴. In a case dating back to 1996⁵, Wal-Mart, acting as a mis-en-cause, contested an exclusivity clause preventing a shopping center from renting space to a pharmacy, on the basis that it contravened the *Pharmacy Act*⁶. The Superior Court decided that the protection offered by the clause was legitimate and

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¹ RSC 1985, c C-34.

² Jacques Deslauriers, *Vente, louage, contrat d’entreprise ou de service*, Montréal, Wilson et Lafleur, 2013, para. 1177.

³ *Ibid*, para. 1179.

⁴ Joy Goodman, « Stipulations de restriction d’usage, clauses de non-concurrence, d’exclusivité et de «rayon» », *Revue du Barreau*, Tome 59, printemps 1999, p. 300. A case law search on the CanLII database for decisions citing the *Competition Act* and including the key words “exclusivity clause / covenant” or “clause d’exclusivité” does not reveal any Canadian case, from 1999 to August 2014, invalidating an exclusivity clause because it contravened the *Competition Act*.

⁵ *Katiou inc. c. Rossdeutscher*, [1996] A.Q. no 448, J.E. 96-800, C.S. (appeal settled: no 500-09-002282-960); Joy Goodman, « Stipulations de restriction d’usage, clauses de non-concurrence, d’exclusivité et de «rayon» », *supra* note 4, p. 300.

⁶ RQLR c P-10.

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that the *Pharmacy Act*, which was public policy, was not infringed. The *Competition Act* was not however cited by the parties in that case.

Canadian courts have not yet been called to apply the *Competition Act* to exclusivity clauses in commercial leases. A potential explanation comes from the fact that such clauses are, by their very nature, limited in time, usually to the duration of the lease, and in space, to the surface of the shopping center⁷. Even if these clauses constitute an exception to the principle of free trade, they do not have a significant effect on markets. Moreover, the tenant usually gives good consideration in exchange for such covenants, in the form of restriction of use clauses, which limit the tenant's own activities within the leased premises. Finally, exclusivity clauses are interpreted restrictively by Courts, in order to not further limit commercial freedom⁸.

The *Act's* main purpose⁹ is "to maintain and encourage competition in Canada", not as an end in itself but for the benefits that it brings to both businesses and consumers¹⁰. In order to achieve this result, the *Act* regulates the creation, preservation and enhancement of businesses' market power¹¹. According to the Competition Bureau, responsible for the enforcement of the *Act*, exclusivity clauses fall outside its scope because they cannot be regrouped in any of the two main categories of practices sanctioned by the *Act*: abuse of dominant position and conspiracy.

With respect to abuse of dominant position, the *Act*¹² requires that three criteria are met before the Competition Tribunal finds that there is abuse of dominant position:

- a) one or more persons substantially or completely control, throughout Canada, or any area thereof, a class or species of business;
- b) such person or 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 the market.

For an act to be considered anti-competitive within the meaning of the *Act*, it must have an intended purpose that is predatory, exclusionary or disciplinary and has a negative effect on a competitor¹³. Such act will not however constitute abuse of dominant position unless it prevents or substantially lessens competition in a market by preserving or enhancing the market power of a dominant firm¹⁴.

⁷ Goodman, *supra* note 4, p. 300.

⁸ Deslauriers, *supra* note 2, para. 1181.

⁹ Section 1.1, *Competition Act*.

¹⁰ Renaud, Madeleine et Thérien, Dominic, "La Loi sur la concurrence", in *Développements récents en droit de la non-concurrence (2013)*, vol. 377, Cowansville, 2013, Y. Blais, p. 81.

¹¹ *Ibid*, p. 83.

¹² Section 79, *Competition Act*.

¹³ Michael Kilby and Ashley Piotrowski, "Abuse of Dominance", in *Competition Act and Commentary*, Toronto, Lexis Nexis, 2014, p. 121.

¹⁴ *Ibid*, p. 123.

Due to its temporal and spatial limitations, it is difficult to see how an exclusivity clause in a lease agreement may prevent or lessen competition substantially within a market, even where the tenant controls a class of business.

The second class of conduct sanctioned by the *Act* is competitor collaboration for the purpose of lessening competition. Agreements to fix prices, restrict supply or allocate markets are criminally sanctioned¹⁵. Other arrangements between persons two or more of whom are competitors that prevent or lessen competition substantially are also sanctioned under the *Act*¹⁶. However, exclusivity clauses do not fall within this category of conduct either because they apply to businesses that operate in different markets - landlords and tenants - not to competitors.

But before concluding that exclusivity clauses are safe and sheltered from the application of pro-competition laws, two recent foreign developments should be considered.

2. Recent developments in France and South Africa

First, in a decision rendered on July 3, 2013¹⁷ the Paris Court of Appeal reiterated that exclusivity clauses in lease agreements are not anti-competitive *per se*, as long as they do not affect competition to a greater extent than necessary to ensure the business' profitability. The case dealt with exclusivity clauses signed by several famous national chains with the owner of a shopping center where they rented premises. The exclusivity clause restricted the chains from operating facilities in adjacent malls, on a 5km perimeter. A second shopping center claimed that these clauses restricted its choice of tenants and prevented free market entry.

The Paris Court of Appeal analyzed the clauses under the French *Code du commerce*¹⁸, which prohibits all agreements aiming to fix prices, restrict supply or allocate markets, similarly to the Canadian *Act*¹⁹. Unlike the Canadian provision however, which explicitly states that the agreement needs to be between competitors, the French provision does not make this distinction. In order to determine if the clause constituted a barrier to entry, the Court analyzed the scope of the exclusivity protection, the duration of the lease, the conditions for terminating and renewing the lease, the market position of the parties and the surrounding market conditions²⁰. Given that the duration of the exclusivity protection corresponded to the length of the lease, which is limited by law to three years in France, that the

¹⁵ Section 45, *Competition Act*, Shawn C.D. Neylan and Michael Laskey, "Competitor collaboration: Cartels, Bid-Rigging and Other Anti-Competitive Agreements", *Competition Act and Commentary*, Toronto, Lexis Nexis, 2014, p. 44.

¹⁶ Section 90.1, *Competition Act*.

¹⁷ CA Paris, July 3, 2013, *Odysseum c Le Polygone* no. 11/17161; in line https://groupes.renater.fr/sympa/d_read/creda-concurrence/CaP/3juillet2013/Odysseum2.pdf.

¹⁸ Section L 420-1, *Code du commerce*.

¹⁹ Section 45, *Competition Act*.

²⁰ *Odysseum*, *supra* note 17 p. 7

geographical area was limited to 5 km and that the lease allowed for early rescission without an obligation to pay rent for the remaining months, the Court decided that the clause was valid and did not constitute a barrier to entry.

This decision shows that exclusivity clauses are not entirely sheltered from the application of competition laws. Depending on the wording of the relevant provisions, pro-competition legislation could be used to invalidate exclusivity clauses that exceed what is necessary to protect the parties' legitimate business interests.

A second pertinent development comes from South Africa, where the Competition Commission was called to decide whether exclusive lease agreements between supermarkets and landlords raised barriers to entry into grocery retailing²¹. These agreements offered exclusive rights to "anchor tenants" to operate food retail stores, often preventing bakeries, butcheries and other part-line stores from operating in the same center. Although certain supermarkets dominated local markets, there was not sufficient evidence, according to the Commission, to demonstrate the anti-competitive effects of the conduct. Despite this conclusion, the Commission advocated against the use of long term exclusive agreements and recommended that the duration and scope of such agreements are limited and proportional to the investment made by the supermarket in a particular shopping center.

These foreign decisions put a question mark over the use of exclusivity clauses in lease agreements: such clauses are valid only if their scope and duration are reasonable and provided that they are not used as barriers to entry. Although Canadian courts have not yet analyzed such exclusivity clauses in light of the *Competition Act*, these foreign developments should be food for thought, as they are compatible with the general objective of the *Competition Act*, which is to preserve and encourage competition in Canada.



²¹ Lizél Blignaut and Yongama Njisane, *No evidence that supermarket exclusive lease agreements are anti-competitive*, Jan 28, 2014; in line <http://www.lexology.com/library/detail.aspx?g=e08e4aa2-b167-4b3e-887c-133e935ec273>.

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