Litigation - Canada

Class action trilogy clarifies certification test, increases anti-competitive exposure

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Introduction

The Supreme Court of Canada's recent decisions in *Pro-Sys Consultants Ltd v Microsoft Corporation*,(1) *Sun-Rype Products Ltd v Archer Daniels Midland Company*(2) and *Infineon Technologies AG v Option consommateurs*(3) constitute a watershed moment in competition law in particular, and in class proceedings in general.

This trilogy of decisions established that indirect purchasers – that is, consumers who did not purchase products directly from the price fixer, but who purchased them indirectly from a reseller or other intermediary – have a right of action against the alleged price fixer at the top of the distribution chain. The Supreme Court recognised indirect purchasers' "offensive" use of passing on, notwithstanding its rejection of the passing-on defence. However, the Supreme Court also established important limitations – namely that:

- the plaintiffs must be able to 'self-identify' as a purchaser of the product subject to price-fixing; and
- the plaintiffs must demonstrate, likely through expert evidence, that damages can be proven on a class-wide basis.

In addition, the Supreme Court also settled the question of the evidentiary burden on plaintiffs at the certification stage in class proceedings. The Supreme Court rejected a higher threshold based on an assessment of the merits of the claim in favour of a consideration of whether there is some basis in fact for the relevant elements of the certification test.

Background

In *Pro-Sys* the representative plaintiffs brought a class action against Microsoft Corporation and some of its affiliates claiming that the defendant unlawfully overcharged consumers for its Intel-compatible PC operating systems and related software. The proposed class consisted entirely of indirect purchasers. The British Columbia Supreme Court certified the action as a class proceeding, but a majority of the British Columbia Court of Appeal set aside the certification order and dismissed the claim on the basis that indirect purchasers had no cause of action.

In *Sun-Rype* the proposed class members included both indirect and direct purchasers. The claim involved allegations that Archer Daniels Midland Company had participated in an illegal conspiracy to fix the price of high-fructose corn syrup (HFCS) – a common sweetener used in soft drinks and baked goods. The British Columbia Supreme Court certified the action by direct and indirect purchasers as a class proceeding. The British Columbia Court of Appeal upheld the certification order in respect of direct purchasers, but overturned the order in respect of the indirect purchasers, holding that their pleadings did not disclose a valid cause of action.

In *Infineon* the class members consisted of both indirect and direct purchasers. The plaintiffs brought an action against the respondent manufacturers based on allegations that they had engaged in a global anti-competitive conspiracy to inflate the price of the dynamic random-access memory chip used in a variety of electronic devices (eg, computers, mobile phones and digital cameras). The Quebec Superior Court dismissed the motion for authorisation to institute a class action. The Quebec Court of Appeal overturned the decision of the motion judge and authorised the class action to

proceed to trial.

Analysis

Rejection of passing-on defence

The key question in each of the Supreme Court's decisions was whether the passing-on defence prohibited indirect purchasers from asserting claims. In price-fixing cases, the passing-on defence is often asserted by the defendant at the top of the distribution chain. As the Supreme Court noted in *Pro-Sys*:

> "*it was invoked under the proposition that if the direct purchaser who sustained the original overcharge then passed that overcharge on to its own consumers, the gain conferred on the overcharger was not at the expense of the direct purchaser because the direct purchaser suffered no loss*."(4)

Therefore, the defendants to indirect purchaser claims argued that if the overcharge was simply passed on to subsequent consumers, the direct purchaser had no claim against the party responsible for the initial overcharge.

The passing-on defence was rejected by the US Supreme Court in *Hanover Shoe, Inc v United Shoe Machinery Corp*.(5) That decision precluded parties who were responsible for illegal overcharges from relying on the passing-on defence as a method of escaping liability in lawsuits commenced against them by direct purchasers.

The Supreme Court of Canada also rejected the passing-on defence in *Kingstreet Investments Ltd v New Brunswick (Finance)*,(6) which involved a claim for the recovery of *ultra vires* taxes charged on alcohol levied by the provincial government against the corporate operators of several nightclubs. In that case, the Supreme Court held that the province of New Brunswick could not reduce its liability for the illegal overcharge by demonstrating that the overcharge had been passed on to the corporate taxpayers' customers. The Supreme Court underscored three problems with the passing-on defence:

> "*first, that it is inconsistent with the basic premise of restitution law; second, that it is economically misconceived; and third, that the task of determining the ultimate location of the burden of a tax is exceedingly difficult and constitutes an inappropriate basis for denying relief*".(7)

In *Pro-Sys* the Supreme Court confirmed that the passing-on defence was rejected in the context of all restitutionary cases and was not limited to the facts in *Kingstreet*.(8)

Offensive use of passing on

In *Pro-Sys* Microsoft argued that the indirect purchasers' use of passing on as the basis for their claim should be precluded as a "necessary corollary" of the rejection of the passing on defence.(9) In this regard, Microsoft relied on the decision of the US Supreme Court in *Illinois Brick Co v Illinois* .(10) In that case, the US Supreme Court prohibited the offensive use of passing on since "whatever rule [was] to be adopted regarding pass-on in antitrust damages actions, it must apply equally to plaintiffs and defendants".(11)

The Supreme Court of Canada did not consider this argument to be persuasive. The Supreme Court concluded that although passing on as a defence is unavailable because of the policy objectives of restitution law, it does not follow that, for the purposes of symmetry, indirect purchasers are prohibited from claiming losses passed on to the chain of distribution.(12) The Supreme Court summarised its reasons as follows:

> "*(1) The risks of multiple recovery and the concerns of complexity and remoteness are insufficient bases for precluding indirect purchasers from bringing actions against the defendants responsible for overcharges that may have been passed on to them.*
>
> *(2) The deterrence function of the competition law in Canada is not likely to be impaired by indirect purchaser actions.*
>
> *(3) While the passing-on defence is contrary to basic restitutionary principles, those same principles are promoted by allowing passing on to be used offensively.*
>
> *(4) Although the rule in* Illinois Brick *remains good law at the federal level in the United States, its subsequent repeal at the state level in many jurisdictions and the report to Congress recommending its reversal demonstrate that its rationale is under question.*
>
> *(5) Despite some initial support, the recent doctrinal commentary favours overturning the rule in* Illinois Brick."(13)

Thus, in the trilogy of decisions, the Supreme Court recognised that indirect purchasers have a claim against the price fixer that effectuated an overcharge even if the overcharge

was passed on through the channels of distribution.

Certification of class action

The Supreme Court also took the opportunity to re-affirm important evidentiary principles at the certification stage of a class action.

For the most part, the Canadian class actions regime is governed by provincial class proceedings legislation.(14) In recent years, the certification stage has generally become the most critical part of a class proceeding. This is where battle is squarely joined between the parties. Despite minor variations between some of the provinces, the courts will certify a class proceeding where:

- the pleadings disclose a cause of action;
- there is an identifiable class of two or more persons;
- the claims of the class members raise common issues;
- a class action is the preferable procedure for resolution of the dispute; and
- there is a valid representative plaintiff.(15)

Once the pleadings disclose a valid cause of action, the remaining certification requirements set out above are subject to the standard of proof articulated by the Supreme Court in *Hollick v Toronto (City)*(16) – that is, there must be "some basis in fact" for each element of the test.(17) This inquiry does not require determination of conflicting factual and evidentiary issues and does not involve consideration of the merits of the action.

In *Pro-Sys* Microsoft argued that plaintiffs must establish that the proposed class action raises common issues and is the preferable procedure on a balance of probabilities standard. Microsoft also argued that the Supreme Court should adopt the US approach of making factual determinations at the certification stage on a preponderance of the evidence and should require judges to weigh the evidence, even if this overlaps with a determination of the merits. However, the Supreme Court re-affirmed that "Canadian courts have resisted the U.S. approach of engaging in a robust analysis of the merits at the certification stage".(18) In Canada, certification is a screening device to ensure that there are sufficient facts to persuade the applications judge that the claim should continue on a class basis.(19)

In the context of indirect purchaser class actions, assessing whether the commonality issues meet the requisite standard can be a challenging endeavour, which often involves the use of expert evidence. At the certification stage, the *Pro-Sys* decision confirmed that the "expert methodology must be sufficiently credible or plausible" to offer

> "*a realistic prospect of establishing loss on a class-wide basis so that, if the overcharge is eventually established at the trial of the common issues, there is a means by which to demonstrate that it is common to the class*".(20)

In both *Pro-Sys* and *Infineon* the Supreme Court permitted the actions by the indirect purchasers to continue as class proceedings.

However, the Supreme Court refused to certify the class proceeding in *Sun-Rype* on the basis that an identifiable class of two or more persons could not be established. A majority of the Supreme Court determined that "there is insufficient evidence to show some basis in fact that two or more persons will be able to determine if they are in fact a member of the class".(21) The proposed class definition was inadequate because it was impossible to confirm whether the indirect purchasers acquired products containing HFCS as opposed to liquid sugar. Prominent direct purchasers, including The Coca-Cola Company and Pepsico, use both HFCS and liquid sugar interchangeably. Yet, the labels on the products sold by these direct purchasers often did not indicate which sweetener was used.(22) As the majority indicated, "[t]he problem in this case lies in the fact that indirect purchasers, even knowing the names of the products affected, will not be able to know whether the particular item that they purchased did in fact contain HFCS."(23) Thus, the Supreme Court established an important limitation on competition class actions by requiring plaintiffs to self-identify as purchasers of the actual product that has been subjected to price fixing.

Comment

In its trilogy of decisions, the Supreme Court confirmed that indirect purchasers have a cause of action against parties that engage in price-fixing schemes provided that they can self-identify as purchasers of the relevant product. Parties that engage in anti-competitive conduct now face potential class proceedings from both direct and indirect purchasers, thereby expanding the scope of their liability. In addition, the Supreme

Court confirmed that the evidentiary burden on plaintiffs at the certification stage remains relatively low. The cases therefore represent a victory for consumers and plaintiff-side class action lawyers.

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Endnotes

(1) *Pro-Sys Consultants Ltd v Microsoft Corporation*, 2013 SCC 57.

(2) *Sun-Rype Products Ltd v Archer Daniels Midland Company*, 2013 SCC 58.

(3) *Infineon Technologies AG v Option consommateurs*, 2013 SCC 59.

(4) *Pro-Sys*, *supra* note 1 at paragraph 18.

(5) *Hanover Shoe, Inc v United Shoe Machinery Corp*, 392 US 481 (1968).

(6) *Kingstreet Investments Ltd v New Brunswick (Finance)*, 2007 SCC 1, [2007] 1 SCR 3.

(7) *Ibid* at paragraph 44.

(8) *Pro-Sys*, *supra* note 1 at paragraph 29.

(9) *Ibid* at paragraph 30.

(10) *Illinois Brick Co v Illinois*, 431 US 720 (1977).

(11) *Ibid* at 728.

(12) *Pro-Sys*, *supra* note 1 at paragraph 60.

(13) *Ibid*.

(14) See British Columbia Class Proceedings Act, RSBC 1996, c 50; Alberta Class Proceedings Act, SA 2003, c C-16.5; Manitoba Class Proceedings Act, CCSM c C130; Ontario Class Proceedings Act, 1992, SO 1992, c 6; Quebec Code of Civil Procedure, RSQ, c C-25; New Brunswick Class Proceedings Act, RSNB 2011, c 125; Nova Scotia Class Proceedings Act, SNS 2007, c 28.

(15) See for example, Ontario Class Proceedings Act, *supra* note 14, s 5(1); British Columbia Class Proceedings Act, *supra* note 14, s 4(1); and Quebec Code of Civil Procedure, *supra* note 14, art 1003.

(16) *Hollick v Toronto (City)*, 2001 SCC 68, [2001] 3 SCR 158.

(17) *Ibid* at paragraph 25.

(18) *Pro-Sys*, *supra* note 1 at paragraph 105.

(19) *Ibid* at paragraph 104.

(20) *Ibid* at paragraph 118. The evidentiary standard, however, appears to be less burdensome in Quebec. As the Supreme Court noted in *Infineon* at paragraph 128, the

> "*presentation of expert evidence is not the norm at the authorization stage in Québec. A requirement that applicants adduce such evidence and advance a sophisticated methodology capable of demonstrating an aggregate loss and how that loss was passed on through complex distribution channels would be more onerous than the threshold requirement* [provided in the *Code of Civil Procedure*]."

(21) *Sun-Rype*, *supra* note 2 at paragraph 58.

(22) *Ibid* at paragraph 55.

(23) *Ibid* at paragraph 65.

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