

ADVERTISING & MARKETING BULLETIN

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FREEBIES: THEY CAN COST MORE THAN YOU THINK

Offering free products or services to attract customers is a common marketing strategy. E-businesses, in particular, often provide a product free of charge in exchange for an e-mail address. However, in light of the Federal Court of Canada's decision in *Culbane v. ATP Aero Training Products* ("Culbane"), businesses may want to think twice before enticing potential customers with giveaways. This practice may result in more than a larger client base – allegations of anti-competitive behaviour coupled with criminal and civil consequences can also ensue.

THE CASE

Both the plaintiff and defendant authored and published aviation training materials. Each offered examination guides from their respective websites: the plaintiff charged a fee while the defendant company offered the guides for free. The defendant company had originally charged customers for the guides, but several years ago it started to provide the guides in exchange for users' e-mail addresses. The e-mail addresses served as a means of advertising and promoting additional products.

The plaintiff claimed that the defendant's actions amounted to predatory pricing – a criminal offence under the *Competition Act*¹ ("Act"). Predatory pricing can be found to have occurred when a business reduces its prices in the short term to drive competitors out of the market or discourage new competitors from entering the market. Once the level of competition falls, the predator raises its prices and recoups lost profits.

THE ACT

Section 50(1)(c) of the *Act* prohibits predatory pricing, that is, engaging in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have that effect. Conviction of this offence carries a potential two-year term of imprisonment.

Section 36 of the *Act* confers a private right of action on any person who has suffered loss or damage as a result of conduct contrary to any provision of the *Act*'s criminal offences. A private litigant may seek to recover losses that it suffered by reason of the criminal behaviour regardless of whether the defendant has been convicted of a criminal offence. In *Culbane*, there was no prior criminal prosecution for predatory pricing.

THE CIVIL ACTION

In *Culbane*, the principal issue was whether the defendant's giving away products for no charge constituted an unreasonably low price for the purpose of section 50(1)(c) of the *Act*.

Because costs were associated with maintaining the on-line guides and the products were originally sold for a price, the judge found this suggested an unreasonably low price. The indefinite period of time that the guides were being offered, the offensive price-cutting scheme and the lack of evidence that the free exams and guides would provide a long-term economic benefit were additional considerations that led the judge to conclude that the price for the guides was unreasonably low.

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¹ R.S.C. 1985, c. C-34.

However, the judge was not satisfied that the defendant's conduct had the effect or tendency of lessening competition, or that the defendant had such a design. This conclusion was reached without a detailed assessment of relevant product and geographic markets – the emphasis was on the conduct's effect on the plaintiff. The judge found that various causal factors contributed to the decrease in the plaintiff's sales, not simply the defendant's unreasonably low prices. Accordingly, the plaintiff did not establish conduct contrary to s. 50(1)(c) of the *Act*, and the private action based on predatory pricing failed.

IMPLICATIONS

The *Culhane* decision could have far-reaching effects for businesses that promote their products by giving away products for free. Offering free products could be construed as selling at unreasonably low prices, especially if customers were previously charged for the products. If that offering is coupled with evidence that the free products were given with the intention of reducing or eliminating competition, the promoter could be susceptible for a claim that it engages in unlawful predatory pricing.

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The foregoing provides only an overview. Readers are cautioned against making any decisions based on this material alone. Rather, a qualified lawyer should be consulted.

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