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Is Your Exclusive Justified? The Competition Bureau's Concern with Property Controls

In a prior *News ReLease* (*Are Exclusive Covenants About to Become Extinct?*, from November 29, 2023), we discussed the Competition Bureau's Retail Grocery Market Study Report and the resulting Bill C-56, which proposed changes to the *Competition Act*. On December 15, 2024, the federal government passed legislation that brought any agreement which "lessens competition" within the purview of the Competition Tribunal's authority, including exclusive use covenants and restrictive covenants that curtail competition. The Competition Bureau refers to these covenants as "competitor property controls". In another prior *News ReLease* (*Exclusives Under Attack!*, from October 4, 2024), we discussed the guidelines published by the Competition Bureau that outline its preliminary enforcement approach.

Since then: (1) Sobeys' parent company agreed to remove its restrictive covenant over a small municipality in Alberta (as according to the Competition Bureau, the restrictive covenant ensured that there could be no other grocer in the area); (2) Loblaws said it would eliminate all existing exclusives if other grocers agreed to do the same; (3) Walmart announced that it would "unilaterally waive any competitive retail restrictions", and sent letters to many landlords to that effect; and (4) Manitoba passed legislation that renders void essentially all new exclusives or restrictives that "directly or indirectly restrict the sale, ownership, development or use of land as a grocery store". Under Manitoba's new legislation, existing grocery-related property controls may only be saved if they are registered on title before November 3, 2025, but even then, they may be struck down or altered if held to be contrary to public interest.

Updated Enforcement Guidelines

Recently, the Competition Bureau published updated guidelines that elaborate on its enforcement approach. The stated aim of the publication is to provide guidance to businesses to help them comply with the changes to the *Competition Act*.

While the updated guidelines shed some additional light on how the Competition Bureau views the matter, they do not provide much in the way of practical guidance for landlords and tenants when considering whether, and to what extent, an exclusive ought to form part of a new lease, and the practical risks of including one.

Under the *Competition Act*, there are two regimes pursuant to which exclusives and restrictive covenants that lessen competition can come under scrutiny by the Competition Bureau. They are: (1) the abuse of dominance regime; and (2) the anti-competitive collaboration regime. A condition of utilizing the abuse of dominance regime is that the party benefitting from the anti-competitive property control has a dominant market position (at a local or regional level, or in a given industry). But regardless of market position, exclusives and anti-competitive restrictive covenants can yield the same sanctions under both regimes. This arises because the Competition Bureau considers all competitor property controls to inherently restrict competition. So whether the exclusive or restrictive covenant benefits a dominant firm, such as a major grocer, or a 'ma and pa' retailer, the Competition Bureau's enforcement approach and the provisions of the *Competition Act* point towards the same menu of sanctions, being: nullifying the covenant, monetary penalties, and "additional measures to restore competition".

Are Exclusives Ever Justified?

According to the Competition Bureau exclusives and anti-competitive restrictive covenants are justified where they create a "credible pro-competitive rationale" or they "increase competition overall". The only example that the Competition Bureau offers is that the exclusive or restrictive covenant is needed to incentivize a retailer to enter a particular market. According to the Competition Bureau, this justification is evident where no other retailer would otherwise agree to make the necessary investment to open the store. The Competition Bureau states that where a landlord receives interest in a location from several comparably suitable tenants, if one or more do not demand an exclusive, then that is evidence that the exclusive is not necessary to incentivize the investment, and therefore the pro-competitive justification would not be available.

A test like this may work in the abstract, but it is uncertain how it will be applied in the context of real-time deal making. Given this uncertainty, landlords may want to put safeguards in place, such as obtaining an indemnity from the tenant for proceedings under the *Competition Act* (including for any monetary penalties to which the landlord is exposed).

The pro-competitive justification is not, however, without restriction itself. The Competition Bureau says that the justification is only a legitimate reason for including a competitive property control if it limits competition no more than is necessary. The Competition Bureau instructs parties to consider whether the duration of the property control could be truncated, whether its geographic area could be shrunk, or whether the products and services that are the subject to the covenant could be narrowed. Since the justification is based on incentivizing a tenant to make the capital investment in the store, perhaps the covenant is only legitimate for so long as the tenant is amortizing its initial capital investment? Does that mean all exclusives ought to expire after the initial term of the lease? In the UK, certain large grocery retailers are prohibited from entering into exclusives that last for more than 5 years from the date the store initially opens.

It can be gleaned from the guidelines that the Competition Bureau considers restrictive covenants to reflect circumstances where large swaths of land, held by dominant retailers, are prohibited from being used for competitive purposes for decades. While that may be true in some cases, it is not true in all cases. The mandate of the Competition Bureau may be better achieved by assessing the impact of the competitive property control, rather than its form.

Exclusive Use Clauses Going Forward

For the time being, outside of Manitoba, parties can, and still do, include exclusives in new lease deals. But it's not just tenants that ought to be aware of the risks, landlords are exposed as well. Landlords may face monetary penalties and get roped into expensive litigation before the Tribunal. Depending on their market position, the abuse of dominance regime could potentially be used against a landlord too.

An indemnity from a tenant for all loss and cost arising from the exclusive is a good start, but an indemnity is only as good as the financial covenant that supports it. Perhaps the parties will want to capture their consideration of the factors for justification of the exclusive in the lease by including a tenant representation that it would not have signed the lease (or made the investment in the premises) without the exclusive. The parties could go further by adding that the landlord and tenant carefully assessed the geographic area, duration, and variety of goods or services restricted, and have conscientiously narrowed the covenant to the minimum scope. A statement to this effect in the lease may help stave off liability down the road.

Notably, existing exclusives and restrictive covenants are not exempt from the new provisions of the *Competition Act*. While the political aim of the changes to the *Competition Act* is apparently to lower grocery prices, the new law is broad enough to capture all types of businesses. Whether any industries other than grocery will be a target remains to be seen.

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