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June 2, 2004

Ms. Lourdes DaCosta  
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Competition Bureau  
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50 Victoria Street  
Gatineau QC K1A 0C9

Dear Ms. DaCosta,

## **RE: Draft *Merger Enforcement Guidelines***

I am writing as Chair of the Canadian Bar Association National Competition Law Section (the CBA Section) concerning the Competition Bureau's March 2004 Draft *Merger Enforcement Guidelines* (the Draft MEGs).

The Draft MEGs appear to go a long way toward updating and clarifying the Bureau's approach to merger analysis and the drafters are to be commended. The purpose of our submission is to provide the Bureau with high-level, conceptual comments on certain aspects of the Draft MEGs. The CBA Section also has a number of technical comments to present to Bureau staff at a meeting currently scheduled for June 14, 2004. We trust the comments in this submission will also be discussed at that meeting.

I hope that the observations and recommendations in our submission will be helpful to the Competition Bureau in its consideration of the Draft MEGs. In the meantime, please do not hesitate to contact either Oliver Borgers (Merger Committee Chair, 416-601-7654) or Jay Holsten (Merger Committee Vice-Chair, 416-865-7523) if you have any questions.

Yours truly,

*(Signed by Trevor M. Rajah on behalf of Susan S. Boughs)*

Susan S. Boughs  
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**Submission on the  
Competition Bureau's Draft  
*Merger Enforcement Guidelines***

**NATIONAL COMPETITION LAW SECTION  
CANADIAN BAR ASSOCIATION**



**May 2004**

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## **PREFACE**

The Canadian Bar Association is a national association representing 38,000 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the National Competition Law Section with assistance from the Legislation and Law Reform Directorate at the National Office. The submission has been reviewed by the Legislation and Law Reform Committee and approved as a public statement of the National Competition Law Section.



# **Submission on the Competition Bureau's Draft *Merger Enforcement Guidelines***

## **I. INTRODUCTION**

The National Competition Law Section of the Canadian Bar Association (the CBA Section) is pleased to provide its comments respecting the Competition Bureau's March 2004 Draft *Merger Enforcement Guidelines* (the Draft MEGs).

The CBA Section welcomes the opportunity provided by the Competition Bureau for interested parties to submit comments on the Draft MEGs, particularly given the central importance of the MEGs to Canadian competition law and policy. The Draft MEGs appear to go a long way toward updating and clarifying the Bureau's approach to merger analysis and the drafters are to be commended.

The purpose of this submission is to provide the Bureau with high-level, conceptual comments on certain aspects of the Draft MEGs. These comments concern issues that the CBA Section believes are of particular importance, and therefore merit careful consideration by the Bureau. The CBA Section also has a number of specific, and in many cases technical, comments to present to Bureau staff at a meeting with the Task Force, currently scheduled for June 14, 2004. We trust the comments in this submission will also be discussed at that meeting.

## II. GENERAL COMMENTS ON THE “PURPOSE” OF THE MERGER PROVISIONS

The *Superior Propane* case, in particular the decision of the Federal Court of Appeal,<sup>1</sup> highlighted the potential for the *Competition Act*'s purpose clause, section 1.1, to influence the interpretation of the Act's various provisions. In *Superior Propane*, section 1.1 was used to assist in the interpretation of the so-called “efficiency defence” in section 96, and in particular to determine the meaning of the word “effects” in the phrase “the effects of any prevention or lessening of competition.” Significantly, the Court did not address section 1.1's interpretive effect on other provisions, and recognized that (unlike section 96) a provision may be sufficiently clear and precise as to override an ambiguous purpose clause.<sup>2</sup> Moreover, the Court did not cast doubt on the substantial jurisprudence interpreting other of the Act's merger provisions, including jurisprudence respecting the anti-competitive threshold in section 92 (*i.e.*, a “substantial prevention or lessening of competition” or “SPLC”) and other similar thresholds (e.g., the “undue prevention or lessening of competition” in section 45).

The Tribunal in *Superior Propane* also reiterated that efficiency is the paramount objective of the merger provisions and the Court found no error in these findings. The CBA Section, therefore, believes it would be desirable for the Draft MEGs to state more clearly what appears to be implied therein, namely that the Bureau's approach to determining whether a merger is, or is likely to, result in a SPLC has not changed from the 1991 MEGs.

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<sup>1</sup> *The Commissioner of Competition v. Superior Propane Inc. and ICG Propane Inc.*, [2001] 3 F.C. 185 (C.A.).

<sup>2</sup> *Ibid.*, at paragraph 106.



On its face, nothing in the Draft MEGs or section 93 suggests that the policy goals in section 1.1 apply directly in the context of a merger analysis other than in respect of the balancing that occurs under section 96. However, a recent Bureau news release referencing language similar to section 1.1 but making no reference to section 96 could suggest that the Bureau does not regard the application of the section 96 factors as being so limited.<sup>3</sup> As such, it would be desirable for the Bureau to confirm in the Draft MEGs that the section 96 factors apply directly to a merger analysis only through section 96 of the Act, forestalling the potential perception that the Act's substantive merger test – whether a merger will, or is likely to, give rise to a SPLC – has become a hybrid SPLC/public interest-type test.<sup>4</sup>

This confirmation is, in our view, vitally important to Canadian competition law and to preserving Canada's influence in the domain of international competition policy. A shift from an SPLC to a hybrid SPLC-public interest test would be widely perceived as a regressive development. A hybrid test would undermine the justiciability of the merger review test and diminish the certainty and predictability of the merger review process. It would run contrary to current international views on the appropriate structure of merger review regimes<sup>5</sup> and create divergence rather than convergence with other jurisdictions'

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3 See Competition Bureau, *Bureau Resolves Competition Issues in Forestry Merger* (1 April 2004), in which the Bureau stated that "[t]he Competition Bureau is committed to ensuring that small and medium sized enterprises have an equitable opportunity to compete and participate in the economy".

4 See, for example, Rowley & Baker, *International Mergers: The Antitrust Process*, Vol. I (London: Sweet & Maxwell, 1996), at 4, which describes SPLC and public interest regimes, as well as market dominance regimes.

5 See, for example, Michal S. Gal, *Competition Policy for Small Market Economies* (Cambridge, MA: Harvard University Press, 2003), at 206, which identifies the SPLC and dominance tests as the two "major tests" for "merger illegality". See also Mario Monti, EU Commissioner for Competition, *Introductory Remarks to Session 2: Analytical Framework for Merger Review*, presented at International Competition Network Inaugural Conference, Naples, 28-29 September 2002, where Mr. Monti spoke of the commonality between the European dominance and U.S. SPLC tests (the former of which has since been modified following substantial debate in Europe on the appropriate merger test for Europe) and noted that, in those "exceptional" cases where "public interest criteria" are used, such criteria "should be very clearly spelt out in the law" (which, we would submit, is not the case for the section 96 factors).

regimes, most significantly in the United States and Europe.<sup>6</sup> Finally, the economic approach to SPLC analysis outlined in the Draft MEGs has been followed in numerous contested mergers by both the Competition Tribunal and the courts. It should be viewed, therefore, as already supporting the objectives of the Act, without need for the introduction of non-economic policy goals directly into the analysis related to SPLC.

For these reasons, we would recommend that the following language be added to paragraph 8.21 of the Draft MEGs:

It should be noted that the examination of anti-competitive effects under section 96 of the *Competition Act* goes beyond the analysis under section 92 of whether a merger will, or is likely to, result in the creation or enhancement of the merged entity's ability, alone or in concert with other firms, to exercise market power.

### III. DEFINITION OF MERGER

The Draft MEGs propose to expand the concept of “control” to include the concept of *de facto* control. This is at odds with the approach in the Act, which provides only two trigger points in merger review: the acquisition of *legal* control;<sup>7</sup> and the acquisition of a significant interest. The acquisition of *de facto* control over a partnership or corporation is not an acquisition of control for purposes of the Act. Moreover, as the members of the CBA Section who have had the opportunity to deal with the concept of *de facto* control under the *Investment Canada Act* know all too well, it is an ambiguous and uncertain concept. Therefore, while it is open to the Bureau to consider the notion of *de*

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<sup>6</sup> We would note in this regard that the Bureau has been a strong advocate of the ICN's objective of achieving “soft convergence” among national competition regimes. See, for example, Konrad von Finckenstein, Q.C., Commissioner of Competition (as he then was), *International Mergers and Acquisitions: Working to Reconcile National Regimes with Global Markets*, Speaker's Notes for remarks made to La Conférence de Montréal, June 28, 2002. It should also be noted that the ICN, while advocating soft convergence of competition laws (which, for reasons noted above, would seem to favour adoption of an SPLC or dominance test for mergers), has recognized that some jurisdictions continue to apply non-competition considerations in merger assessments. To the extent that such factors are taken into consideration, the ICN has recommended that the way in which they interact with competition factors should be made transparent. Such a recommendation, while falling short of recommending against inclusion of non-competition factors, may minimize the potential negative effects arising from the use of non-competition factors in a merger analysis. See the ICN's Recommended Practice for Merger Notification Procedures, in particular Comment 3 of Part B of the Recommended Practice for Transparency.

<sup>7</sup> *Competition Act*, s. 2(4) control is defined only for partnerships and corporations, and the Section acknowledges that it is an open question whether other definitions of control may be drawn upon in the case of other types of entities.

*facto* control in determining whether there has been an acquisition of a significant interest, we fail to see how adding this concept clarifies the determination of whether a “significant interest” has been “acquired”. We would therefore recommend that the Bureau abandon the *de facto* control concept and focus instead on setting out the meaning of “significant interest,” the legal term used in section 91.

While the Bureau’s working definition of “significant interest” in paragraph 1.6 of the Draft MEGs (“the ability to materially influence the economic behaviour”) accurately and succinctly captures the legislative intent behind the use of the word “significant”, it does not grapple with the word “interest”. An “interest” in a business is commonly understood to mean ownership of an economic interest, i.e. an *investment* in a business. A supply contract may well enable the supplier to materially influence the economic behaviour of its customer, without the supplier having an “interest” in the customer’s business as that term is commonly understood. The Bureau’s approach in paragraphs 1.14 and 1.15 therefore results in a degree of uncertainty in the analysis of such situations and should be clarified.

#### **IV. THE ANTI-COMPETITIVE THRESHOLD**

Among the most significant changes in the Draft MEGs is the elimination of the 5 per cent price increase guideline for assessing whether a merger will, or is likely to, result in an SPLC.

We believe that the removal of this reference is unnecessary, unhelpful, and inconsistent with the goals of providing greater guidance and transparency. The reference to the 5 percent price increase guideline in the 1991 MEGs leaves open the possibility that an assessment of a given market may disclose that some amount other than 5 per cent is more appropriate for the purposes of this determination. In practice, however, the 5 per cent threshold is helpful as a general guideline, for example in a preliminary assessment of a merger’s potential impact on competition prior to there having been an opportunity, by the parties, their counsel or the

Bureau, to carry out a more detailed assessment.<sup>8</sup> Unless the Bureau has itself abandoned this approach we would recommend that the Draft MEGs maintain use of the 5 per cent price increase threshold. If the Bureau has abandoned this approach, we would strongly recommend that it reconsider its position.

We further note an inconsistency in the Draft MEGs with respect to abandonment of the 5 per cent price increase guideline for market power assessment purposes while retaining such a threshold for the purposes of application of the hypothetical monopolist test for market definition. In addition, the statement in footnote 22 that “materiality refers to sustainability rather than the magnitude of the price increase” contorts, in our view, the meaning of the word “material”. Competition is substantially constrained when sufficient marginal customers are forced to pay prices that are higher in a degree that – if sufficient choice of supply were preserved – would affect their choice of supply, thus rendering the price increase unprofitable. The sustainability (or, put another way, the time period permitted for such substitution to take place) is a separate issue from the magnitude of a change in price that will affect customers’ choices in a given context. This magnitude of price increase is already identified for purposes of market definition and is similarly appropriate for purposes of assessing a SLPC.

## V. MARKET DEFINITION

The Draft MEGs state “market definition is based on substitutability and focuses on demand responses to changes in relative prices. Supply responses are also important when analyzing market power, but are examined later in the analysis.”

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<sup>8</sup> For a discussion of the importance of including concrete, numerical thresholds in guidelines, see William Blumenthal, *Clear Agency Guidelines: Lessons from 1982* (2000), 68:1 *Antitrust L.J.* 5 at 16 (discussing the reasons underlying the success of the 1982 U.S. Department of Justice merger guidelines, including: “*The Guidelines were fully specified.* Not only did the Guidelines fill in the interstices, but they filled in virtually all of the interstices—and generally not with abstract standards, but with numbers. What degree of substitutability was required for products to be included within the same market? Over what time would market responses be measured? The Guidelines were clear: under the hypothetical monopolist approach, substitutability such that a 5 percent price increase for one year would be unprofitable, with separate six-month and two-year time frames used to measure production flexibility and entry, respectively. Similar detail was provided throughout, as tests were fashioned with specific parameters. One could quarrel with the drafters’ chosen specifications, but the choices were there for all to see and use.”)

As noted by Daniel L. Rubinfeld in *Market Definition with Differentiated Products: The Post/Nabisco Cereal Merger*,<sup>9</sup> “market definition is not an end in itself.” Rather, it provides a foundation on which one can evaluate likely competitive effects. Supply-side responses by “sellers that are not currently supplying the relevant market”,<sup>10</sup> however, can just as effectively prevent a hypothetical monopolist from imposing a significant, non-transitory price increase as will the substitutability of the products.

The purpose of market definition is to identify the set of suppliers who will be in a position to discipline attempts by the merged entity to increase prices in a material degree. That is the meaning of “competition”. As the Supreme Court of Canada noted in the PANS case, “[t]he aim of the market structure inquiry is to ascertain the degree of market power of the parties,” which requires identifying “competitors”.<sup>11</sup> The hypothetical monopolist test is a tool that may be of assistance in this regard, but it should not be adhered to rigidly, since there may be circumstances where a narrow focus on demand considerations is misplaced.<sup>12</sup>

Moreover, exclusion of supply-side responses at the market definition stage may result in an unnecessarily complicated analysis. In many cases, the methodology espoused in the Draft MEGs – identifying product markets according to demand considerations but taking (quick) supply-side responses into account only when calculating market shares and concentration – will lead to the same result.<sup>13</sup> In differentiated product markets, however, it can lead to an indeterminate result. In certain manufacturing industries, such as secondary steel or aluminum manufacturing (where customers may have different demands, e.g. square-shaped versus circle-shaped pieces, but suppliers are generally

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9 (2000), 68 Antitrust L.J. 163, at 177.

10 Draft MEGs, paragraph 4.2.

11 *R. v Nova Scotia Pharmaceutical Society*, [1992] 2 S.C.R. 606 at 653 (“PANS”).

12 Again, in *PANS*, the Supreme Court of Canada noted that “[t]he structure-behaviour framework of analysis remains merely a convenient way of approaching conspiracy problems, and it should not be seen as a rite of passage.” The same is true, the CBA Section would submit, with respect to the market structure component of merger analysis.

13 See Rubinfeld, *supra*.

capable of switching between the manufacture of the different products with relative ease), the two-stage approach would require the Bureau officer to define an inordinate number of different product markets, only to aggregate the capacities and/or production of the producers involved in those “markets” for purposes of assessing market shares and concentration.<sup>14</sup>

The CBA Section notes further that consideration of supply-side substitution need not and should not shift the focus of the analysis from the products to the identity of suppliers.<sup>15</sup>

The confusion the two-step approach generates at a practical level is evidenced by paragraph 4.12, which recognizes that such market shares “may understate the relative market position and competitive influence” of sellers who participate through a supply response.

At the very least, if the two-step approach is maintained, the CBA Section recommends that a paragraph be added, after paragraph 4.12, recognizing that, where supply-side considerations warrant, the practical effect of the market share calculations may be to include suppliers with fungible resources and a common set of products into a more broadly defined product market. Again, however, given the role of the MEGs to guide and clarify the thinking not only of merging parties but of Bureau staff, the CBA Section recommends that the Draft MEGs revert to a more purposive analysis of relevant product markets that serves to identify all relevant competitive conditions (including supply responses) with respect to a product or group of products.

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14 Another example where, taken to its extreme, failure to consider supply-side substitution leads to excessively fragmented market definitions is knowledge-intensive companies, which sell their employees' skills rather than a pre-identified set of products. These firms have been described as “those who organize their business flexibly to respond to demand pressures, where usually most of the labour is integrated into a common pool from which resources are drawn to meet clients' needs just in time ... typically consulting companies and professional service companies (investment banks, insurance companies, etc.).” See Padillo, Dr. Atilano Jorge, *The Role of Supply-Side Substitution in the Definition of the Relevant Market in Merger Control*, National Economic Research Associate, European Commission, Madrid, 2001, at 24.

15 See Draft MEGs, paragraph 3.11.

## VI. ANTI-COMPETITIVE EFFECTS

The new and expanded material in this section of the Draft MEGs is one of the most important improvements in the proposed guidelines. The Bureau quite rightly recognizes that a coherent theory of anti-competitive harm is a necessary pre-requisite for reaching a conclusion that a merger is likely to prevent or lessen competition substantially. With this in mind, the CBA Section has the following comments on Section 5 of the Draft MEGs' treatment of anti-competitive effects.

### A. Unilateral Effects

The discussion of unilateral effects is generally helpful and, in the CBA Section's view, consistent with modern economic theory. However, notably absent is a discussion of the conclusions that the Bureau has arrived at in a number of relatively recent mergers that combined post-merger shares above 45 per cent ("red") are presumptively anti-competitive.<sup>16</sup> By contrast, shares between 35 per cent and 45 per cent ("yellow") are regarded as warranting further analysis, while post-merger shares below 35 per cent ("green") typically are regarded as not leading to a substantial prevention or lessening of competition and therefore not requiring further analysis.

In the CBA Section's view, the so-called "stoplight" system of screening mergers has been one of the most significant enforcement developments in the past few years. However, it continues to be unclear how broadly the stoplight presumptions apply. For example, do they apply outside the retail merger context? Moreover, there are many examples of mergers cleared by the Bureau where the post-merger share was in excess of 45 per cent. There are also examples of mergers that have been successfully challenged by the Bureau before the Competition Tribunal or which have been settled by consent,

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<sup>16</sup> See, for example, Letter from Commissioner to Toronto-Dominion Bank and Canada Trust (28 January 2000) and earlier letters in respect of the proposed mergers of Bank of Montreal and Royal Bank (1998) and of Canadian Imperial Bank of Commerce and Toronto-Dominion Bank (1998). See also the Commissioner's press release in respect of various transactions in the retail grocery industry (e.g., Sobey's/Oshawa Group (1999), Loblaws/Provigo (1999) and Loblaws/Oshawa Group (1999)).

where the *post-divestiture* share was above 50 per cent.<sup>17</sup> In such cases, the Tribunal (and the Bureau where the matter was settled by consent) must have considered that the merger would not give rise to an SPLC even though the post-divestiture share remained in the above 50 per cent range.

Finally, the CBA Section questions how rigidly a system of market share presumptions can be applied in light of section 92(2), which prohibits the Tribunal from finding that there is an SPLC based on measures of concentration or market share alone. Nonetheless, if it is the Bureau's intention to continue to apply market share presumptions such as those outlined in the bank and grocery merger cases, the CBA Section believes that it is critical that this approach to market share be outlined in the new MEGs.

### **B. Coordinated Effects**

The Draft MEGs' treatment of co-ordinated effects is also useful, which is particularly important given the complexity of the subject matter and the fact that it is often not well understood by merging parties. However, the CBA Section also believes that the discussion can be further improved in a number of ways.

First, the CBA Section questions whether it is the Bureau's intention to give coordinated effects greater prominence in its enforcement activity, as is arguably occurring in the United States.<sup>18</sup> We note that in addition to the bank mergers, there have been a number of recent mergers in Canada where challenges appear to have been based, at least in part, on coordinated effects / interdependence theories.<sup>19</sup>

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17 See, for example, Canadian Waste (1998; 51 per cent and 58 per cent post-divestiture shares) and United Grain (2002; 41-52 per cent post-divestiture shares).

18 As highlighted in a speech given by Deborah Platt Majoras at the 2004 Langdon Hall conference, coordinated effects theory has been raised by the U.S. Department of Justice or FTC in several recent cases including *Dairy Farmers of America*, *UPM*, *Arch Coal/ Alcan/Pechiney* and *SGL Carbon*.

19 See, in particular, *Abitibi/Donahue* (CT2001/009), *Lafarge/Blue Circle* (CT 2001/004) and *United Grain* (CT 2002/001).



At a substantive level, the CBA Section believes that the Draft MEGs' discussion of "co-ordinated effects", while a significant improvement over the 1991 MEGs' sparse treatment of the subject, could be further improved. The Draft MEGs, for example, differ from the Bureau's *Merger Enforcement Guidelines as Applied to a Bank Merger* (the "Bank MEGs"), which provided that interdependent behaviour "is more likely in markets in which firms can recognize and reach a co-operative understanding, monitor one another's behaviour, and respond to any deviations from the co-operating behaviour by others."<sup>20</sup> The CBA Section believes this more clearly states the three necessary preconditions for interdependent or co-ordinated behaviour to be a potential concern. Indeed, the first of these prerequisites is missing from paragraph 5.19 altogether. Even the statement in the Bank MEGs, however, could more clearly recognize the central role of these three factors in the analysis.

The CBA Section is also concerned that the lengthy list of potentially relevant factors identified in paragraph 5.22 will give rise to a "laundry list" analytical approach, thereby diverting attention away from the briefer discussions of (i) conditions required for interdependent behaviour to occur and (ii) the requirement for a causal link between a merger and the creation or enhancement of coordinated market power. The potential significance of this danger is evidenced by the *Airtours* case, in which the European Commission received a salutary reminder of the importance of clear evidence and analysis of each of these issues. The CBA Section believes that the Draft MEGs would benefit from a similarly rigorous, and focused, discussion of the necessary conditions for interdependent behaviour. If the Bureau determines to keep its "list" approach, the MEGs should comment on the relative significance of various factors in the list.

### C. Differentiated Products

The Draft MEGs take, in the CBA Section's view, an unwarranted negative posture towards product differentiation. This is evidenced, for example, by the statements in

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<sup>20</sup> Bank MEGs, at paragraph 65.

paragraphs 5.3 and 6.11, respectively, that “product differentiation limits the level of direct competition among firms” and constitutes a barrier to entry in the form of “advantages enjoyed by incumbents” to be overcome by new entrants.

Product differentiation is an important aspect of non-price competition that can contribute substantially to consumer welfare and economic efficiency. While product differentiation may play a role in the finding of an SPLC (*e.g.*, in a unilateral effects analysis where the merging parties' products are particularly close substitutes), there are also cases where product differentiation will support a contrary conclusion (*e.g.*, when the merging parties' products are relatively less close substitutes, and in interdependence analysis, generally). Similarly, it is incorrect to suggest that product differentiation is exclusively a barrier to entry; it can also have an enabling effect by providing opportunities for new entrants.

Accordingly, the CBA Section strongly encourages the Bureau to take a more balanced approach to product differentiation. In particular, the Draft MEGs should recognize that product differentiation is an important feature of our economy and that, for reasons described above, whether product differentiation will be a factor in support of or against a finding of a SPLC will depend on the specific circumstances of the case.

#### **D. Innovation Markets**

The CBA Section is pleased that the Draft MEGs do not follow the U.S. enforcement approach of defining so-called “innovation markets” for the purposes of merger analysis. However, we also note that the language of paragraph 5.9 of the Draft MEGs is somewhat ambiguous, and could be construed as an indication that the Bureau intends to use innovation markets in its merger analysis. Given our understanding that the Bureau was careful to omit innovation markets from its *Intellectual Property Enforcement Guidelines*, the CBA Section believes that it would be desirable for the Bureau to make it clear that paragraph 5.9 does not constitute recognition of innovation markets in Canadian

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merger review under the Act (as distinct from an analysis of likely future competition in respect of the relevant product markets).

## VII. THE EFFICIENCY EXCEPTION

By providing a defence for mergers that give rise to efficiencies that are greater than and offset their anticompetitive effects, Canada deliberately chose to place a greater weight on efficiencies compared to other jurisdictions, such as the United States. This approach reflects Canada's particular economic and national interests, including the small, open and export-oriented nature of the Canadian economy and the important role that efficiencies can play in promoting these interests. As such, section 96 – the “efficiency defence” – is a fundamental feature of Canadian competition law and policy.

The test for weighing efficiency gains against anti-competitive effects was substantially modified as a result of the Federal Court of Appeal's judgment in *Superior Propane*. It is not surprising that the Draft MEGs would be modified to reflect the changes flowing from that decision. At the same time, if amendments along the lines of those proposed in Bill C-249 are enacted, they will substantially modify section 96 by converting efficiencies from a defence to an otherwise anti-competitive merger to one of the many factors to be taken into consideration by the Tribunal when examining the competitive impact of a merger. Any such amendments would require the further revision of Part 8 of the Draft MEGs.

With the above in mind, the CBA Section has the following general comments in respect of the Draft MEGs' treatment of efficiencies.

First, the Draft MEGs appear to reflect an interpretation of some of the judicial guidance provided in the *Superior Propane* decisions that favours the Bureau's preferred approach to the application of section 96. The Federal Court of Appeal, however, did

not say that the approach advocated by the Commissioner in *Superior Propane* is the only approach that meets the requirements of section 96. The Court merely indicated that the balancing weights approach “seems” to meet these requirements, leaving open the possibility that there may be other acceptable approaches as well.<sup>21</sup> Accordingly, a more balanced description of the standards and approaches that may be acceptable under section 96 would be preferable.

Second, the value of the Draft MEGs as “guidelines” is diminished by the use of vague wording regarding the Bureau’s enforcement approach for section 96. In order to clarify the Bureau’s enforcement approach, we would recommend incorporating additional explanatory statements and examples. For example, paragraph 8.8 states a broad requirement for a description of the precise nature, magnitude and likelihood of claimed efficiencies. This statement would benefit from the use of numerous examples (*e.g.*, savings in controllable costs or by elimination of redundancies rather than changing the operating paradigm, complexity of steps needed to obtain synergies, similarity of merging businesses, sufficiency of financial strength to fund necessary restructuring, *etc.*).<sup>22</sup> Similarly, the discussion of redistributive effects in paragraphs 8.25 to 8.27 contains language that is extremely broad, stating that there are different approaches to analyzing wealth transfers and proceeding to identify only two of several such approaches. With respect to the brief discussion of one of the two approaches expressly mentioned, the socially adverse effects approach, it would be helpful to have further detail regarding the methodology the Bureau would use to assess whether a wealth transfer is likely to have socially adverse effects. Such detail could include quantification of how much of the

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21 *Superior Propane*, *supra*, at paragraph 141.

22 See Suzanne Loomer, Stephen R. Cole and John Quinn, *Quantifying Efficiency Gains in a Competition Case: Sustaining a Section 96 Defence* presented at National Conference, Canada's Changing Competition Regime, Toronto (26-27 February 2003), at 15.

transfer would be included in the assessment as well as the type of data that would be examined in order to make such a determination.<sup>23</sup> As for the “other”, unidentified, approaches for analyzing wealth transfer, it would be helpful to identify these other approaches and to indicate the circumstances in which each particular approach might be preferred and the reasons why.

The CBA Section applauds the Bureau for articulating that it will consider efficiencies at the enforcement stage of a merger and not solely before the Tribunal. The CBA Section is concerned however that the Bureau apply settled principles on the law of efficiencies where those principles have been pronounced upon by the Tribunal. In this regard, the Bureau should not be imposing a merger specificity requirement for efficiencies, simply to be in keeping with the US merger guidelines. There are two problems with doing so. First, it is not the law. Both *Superior Propane* and *Hillsdown* make it very clear that the Act does not require that claimed gains in efficiency not be achievable in another, less anti-competitive way. As noted by the Tribunal in *Superior Propane* (no.2):

[147] As stated in the Horizontal Merger Guidelines, claimed efficiency gains must be "merger-specific". Although those Guidelines do not elaborate, this requirement appears to mean that a claimed efficiency gain is not cognizable if it could be achieved in another, presumably less anti-competitive, way.

[148] The Tribunal found that the gains in efficiency in the instant merger would not be achieved absent the merger (i.e. if the order were made) and hence could be included in the test under subsection 96(1) (Reasons, at paragraph 462). This requirement is not the same as the one used by the American enforcement agencies. After satisfying itself that the two approaches were not identical, the Tribunal noted the same distinction was addressed in *Hillsdown*, supra, which supported the view that the Act did not require that claimed gains in efficiency not be achievable in another, less anti-competitive way, although this was the requirement of the Commissioner's Merger Enforcement Guidelines ("MEGs").

While the MEGs are not binding on the Commissioner, the law is and as such should be duly reflected in the MEGs.

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23 This would apply in the determination of the “greater than and offset” portion of the current section 96 efficiencies defense, or in the calculation of efficiencies as one of several factors in the overall analysis of whether a transaction may result in a substantial prevention or lessening of competition should Bill C-249 be passed.

Second, even if the Bureau retains this requirement, it must be made clear that theoretically possible alternative means of achieving efficiencies do not preclude real efficiencies from being properly considered. This is consistent with the CBA Section's submission on Bill C-249.<sup>24</sup> The language from the former MEGs addressing this point should be retained.

Finally, we note that reference is made to the dissenting views of a lay Tribunal member from *Superior Propane* regarding the consideration of anticompetitive effects from a "qualitative" perspective. That position should not be followed by the Bureau nor expressed in the MEGs as it was dissenting obiter comment and was expressly rejected by the Tribunal, whose opinion was upheld by the Federal Court of Appeal.

Anticompetitive effects should be quantified whenever possible, even if only roughly as required by the Tribunal and Federal Court of Appeal.

## **VIII. FAILING FIRM BUSINESS FAILURE AND EXITING ASSETS**

The CBA Section is concerned that the discussion of the so-called "failing firm" defence has omitted language used in the 1991 MEGs. The omitted language made it clear that insolvency was only one circumstance in which the Bureau may find that, with the appropriate focus on comparing the post-merger world to the likely world in the future if the merger does not take place, a transaction which may have caused an SLPC based on the past, might actually have no such effect. There must be a causal link between the diminution of competition and the merger in question. If the assets of one or more of the merging parties can be shown to be likely to exit the market in any event, then the merger is not the cause of the change in competition. "Failing firm" is just one example of why

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<sup>24</sup> Submission on Bill C-249 – Proposed Amendment to the Section 96 of the *Competition Act* (Mergers Efficiency Defence), October 2003.

comparison of the merger outcome with the likely degree of competition without the merger is so important. The Bureau's assessment of the likelihood of retrenchment, or of a "prevent case", are other examples of the same general concept. The past is not always a perfect guide to the future.

As such, the CBA Section is concerned that:

- the "failing firm" analysis is without such analytical background; and
- the draft should require a competitively preferable purchase to offer "net price above liquidation value", otherwise liquidation is in fact the more likely outcome.

## **IX. ENHANCING THE "GUIDANCE" PROVIDED BY THE MEGS**

The Draft MEGs, by definition, are intended to provide guidance to those who consult them as to how the Bureau is likely to analyze a particular transaction. For the most part, we believe that the Draft MEGs would achieve this objective. However, we also believe that there are certain changes that could be made to enhance the Draft MEGs in this regard. A number of these changes have been discussed elsewhere in this submission in the context of comments made in respect of particular substantive sections of the Draft MEGs. The following, however, are comments of a more general nature.

### **A. The Use of Citations**

The Draft MEGs contain citations to jurisprudence and to decisions and/or positions taken by the Commissioner. While such citations can be of assistance in providing guidance to readers, we would offer two observations respecting the use of such citations:

- i) Citations can only provide meaningful guidance if they include a brief description of the analysis underlying the citation. At present, there are numerous citations that provide no indication at all as to the reason for the citation, including some that do not even provide a page reference to assist the reader in identifying the

basis for the citation's inclusion in the Draft MEGs. Indeed, in some cases the CBA Section has been unable to identify the relevance of the case to the point under discussion in the Draft MEGs.

- ii) Where the Commissioner's own conclusions or arguments are cited as the basis for a particular interpretation of the Act (as is done, for example, in footnotes 14 and 17 in relation to the *Seaspan* and *Bayer* cases), it should be made clear that these citations provide examples of the Bureau's enforcement approach in a particular case as distinct from representing authorities for a legal position (as is the case with jurisprudence). This could be done, for example, by including an express reference to these citations in the "Purpose" section of the Draft MEGs.

## **B. Expanded Discussion of Analytical Tools and Methodologies**

The ability of the Draft MEGs to fulfill their guidance function would also be enhanced by the inclusion of additional discussion of significant analytical tools or methodologies that, at present, are mentioned in the Draft MEGs in a relatively cursory manner. In particular, the Draft MEGs make reference to critical loss analysis, cluster theory, spatial competition analysis, raising rivals costs and the Herfindahl-Hirschman Index ("HHI"), but provide little or no information about how they may be applicable to a proposed transaction. In particular:

- i) Footnote 32 states that critical loss analysis "may" be of assistance in defining product or geographic markets, but nothing is said about whether/when the Bureau uses critical loss analysis for this purpose, nor is mention made of the fact that critical loss analysis can also be used to help determine whether a merger will, or will likely, result in an SPLC (i.e., as part of the assessment of whether a firm or group of firms, post-merger, will be able to profitably impose a material price increase);
- ii) Paragraphs 3.18, 3.29 and 5.27 are similarly vague about cluster markets, spatial competition analysis and raising rivals costs, with the first and third of these referred to only indirectly in the Draft MEGs without actually naming the relevant economic concept or providing a reference to more extensive literature on the subject, nor cases in which they have been used; and
- iii) Footnote 53 of the Draft MEGs states that "the Bureau may examine changes in the [HHI] ... to observe the relative change in concentration before and after a merger," but goes on to state that "the Bureau does not use HHI levels as a safe harbour threshold." While it is helpful to know that the Bureau may examine HHI



levels in its examination of a transaction, meaningful guidance would require that the Bureau identify the circumstances in which it will examine HHIs and the criteria that it will use for such examinations. In this latter regard, even if HHIs are not used as a safe harbour threshold, the Bureau must ascribe some importance to different HHI levels, otherwise it would not bother with the exercise of examining pre - and post-merger HHI levels. Thus, the reference to HHIs in the Draft MEGs begs the question, “to what levels does the Bureau refer?”

Accordingly, the CBA Section believes that the Bureau should provide a few sentences of detail about each of these tools and methodologies. This could include a brief description of each of the tools and methodologies, the circumstances under (or an example of a situation in) which they may be useful, the Bureau’s perception of the tools or methodologies as credible bases for merger analysis, the extent to which they are (or are not used) by the Bureau in its merger analysis and, where possible, concrete benchmarks to assist in understanding when and how these tools and methodologies will be applied.

### **C. Commissioner’s Commitment to the MEGs**

The Commissioner’s decision to resile from the MEGs in *Superior Propane* has caused some stakeholders to question the predictive value of the MEGs. As such, it would be appropriate for the Bureau to restate its commitment to the MEGs.

## **X. CONCLUSION**

We hope that the foregoing comments will be of assistance to the Bureau in its consideration of the Draft MEGs. We would be pleased to address any questions that the Bureau has about these comments, and look forward to meeting with Bureau staff in this regard on June 14, 2004.