EFFICIENCIES IN MERGER REVIEW

THE EFFICIENCY DEFENCE IN THE *COMPETITION ACT*: A CASE FOR THE FACTORS APPROACH

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Background and Introduction

On January 31, 2003, the Federal Court of Appeal issued the final ruling on the proposed merger between Superior Propane and ICG Propane. Despite the creation of virtual monopolies in numerous local markets (including many in Atlantic Canada), the Court upheld the Competition Tribunal's earlier decision to allow the merger. The case marked the first instance where section 96 of the *Competition Act* (the efficiency defence) was successfully invoked to allow an otherwise anticompetitive merger.[1] Section 96(1) reads as follows:

> The Tribunal shall not make an order under section 92 [prohibits mergers which prevent or lessen competition] if it finds that the merger or proposed merger ... is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.

The *Superior Propane* decision sparked considerable debate on the treatment of efficiencies under the *Competition Act* and gave rise to private member Bill C-249 which would have repealed the efficiencies exception of section 96(1) and made efficiencies a factor to be considered along with the other factors (listed under section 93) considered in the review of mergers. The bill was adopted by the House of Commons; however, after receiving first and second readings in the Senate, it died with the dissolution of Parliament on May 23, 2004.

Later in 2004, the Competition Bureau launched a national consultation process on the role of efficiencies under the *Competition Act*. This process, which included input from interested Canadian parties as well as from international antitrust jurisdictions, culminated in the submission of the "Report of the Advisory Panel on Efficiencies" to the Commissioner of Competition in August 2005 (Côté, Bennett and Gibbins, 2005). The Report concludes that, given Canada's lagging productivity growth, competition policy should continue to promote efficiency. Since mergers can lead to enhanced efficiency and productivity, the Report recommends the regular and explicit consideration of efficiency as part of the merger review process. For those cases where competition fails to result in optimal efficiency, the Report recommends the retention of the efficiency defence, which the authors believe would apply only rarely. The authors, however, believe that monopoly inevitably results in long-run inefficiency; therefore, the Report recommends that the efficiency defence not be used in merger-to-monopoly situations.

Since there can be no denial that efficiency is an important policy objective and that mergers can enhance efficiency, the Report is correct to recommend that efficiency considerations be an explicit part of merger review. However, there are other important objectives of competition policy against which the goal of efficiency must be balanced. Furthermore, it is debatable whether an efficiency defence is the most effective way to promote efficiency. Therefore, this article argues that, not only should the Report have recommended the elimination of the efficiency defence for merger-to-monopoly cases, it should have gone a step further and eliminated it altogether. Section 96 should be dropped in favour of including the evaluation of efficiencies as one factor among others that are included in the assessment of the anticompetitive effects of proposed mergers (the factors approach).

The Importance of International Harmonization

In an era of global markets, Canadian firms seeking to establish transnational mergers must often receive approval from numerous merger control regimes. Divergent regulations and procedures increase the costs associated with this process. These costs, outlined in Marfels and Sawler (2004), include the following:

- Divergent regulations and procedures increase the administrative costs of filing in numerous jurisdictions. These costs include fees for lawyers, economists and translators.

- Divergent merger regulations reduce the timeliness associated with the review process. A merger is a strategic investment decision that is a response to the merging parties' economic and competitive environment (Weston, 2001). Market conditions can change rapidly, requiring a quick strategic response. However, in dealing with the complexities of divergent merger regimes, firms have to wait months for an authority's decision. By this time, even if the merger is approved, the strategic opportunity may be lost. If the merger is not approved, firms face the opportunity cost associated with not being able to pursue alternative strategies while the merger is under review.

- Divergent merger regulations raise the uncertainty associated with multijurisdictional merger review. Before making the decision to pursue a merger, the merging parties must assess the likelihood that they will gain approval. Numerous merger control regimes, each applying divergent regulations, make predicting the ultimate outcome of the review process much more difficult. This creates uncertainty among the merging parties which increases the opportunity cost of pursuing multijurisdictional mergers.

As previously discussed in Marfels and Sawler (2004), the extra costs arising from divergent merger regulations impose significant impediments on Canadian firms pursuing mergers which cross multiple jurisdictions. These costs may prevent firms from pursuing mergers which could otherwise enhance consumer welfare or improve Canadian competitiveness in international markets.

Despite the recognition of the need for greater international harmonization, with the efficiency defence, Canadian merger review deviates from that of almost all of its major trading partners, including the U.S. and the European Union. The EU's approach to evaluating efficiencies is summarized in the Competition Bureau's "Report of the International Roundtable on Efficiencies" (2005):

> The EC will consider any substantiated claims of efficiency as part of the overall analysis of the merger to determine whether the merger will significantly impede effective competition in the common market. To the extent that the efficiencies may counteract the effects on competition – and in particular the harm to consumers – that the merger otherwise might have, those efficiencies may be taken into account as a factor pleading in favour of the merger being approved. [4]

The Report summarizes the U.S. approach as follows:

> ...the authority evaluates whether the claimed efficiencies are likely to be sufficient to reverse the merger's potential to harm consumers in the relevant market. ... In that context, extraordinarily great cognizable efficiencies would be necessary to prevent a merger to monopoly from being anticompetitive. When analyzing efficiencies the authority does not simply balance the raw magnitude of cognizable efficiencies generated by the merger with the likely anticompetitive effects of the transaction to determine whether the former outweighs the latter. Nor does it access efficiency claims in isolation; rather, it evaluates such claims simultaneously with market definition, concentration, competitive effects, entry, and failing firm issues (the other Horizontal Guidelines factors). [9]

The U.S. and the EU's approaches to evaluating efficiencies deviate from the Canadian approach in two principal ways. First, while the U.S. and EU consider efficiencies in the context of their potential to reverse the proposed merger's harm to consumers, Canada applies a balanced weights approach developed by Townley (1999, 2004). Second, while both the EU and the U.S. evaluate efficiencies as one factor among many to be considered when assessing the overall anticompetitive effects of the merger, Canada does not evaluate efficiencies along with other factors relevant to assessing overall anticompetitiveness. Rather, once the anticompetitive effects have been established, it is determined whether there are enough efficiencies generated by the merger to outweigh the anticompetitive effects.

Given that the U.S. and the EU treat efficiencies as one factor among many to be considered, it does not make sense for Canada to stand alone with an efficiency defence. Harmonizing merger control with that of our major trading partners will reduce impediments to Canadian firms seeking mergers that might otherwise improve consumer welfare or enhance competitiveness in international markets. This opinion is shared by the Norwegian Competition Authority. In their submission on behalf of the Norwegian Authority to the Competition Bureau's consultation on the treatment of efficiencies, Eckbo and Voldon (2005) write:

> The NCA notes that one of the objectives of the Canadian *Competition Act* section 1.1, is to foster international trade. To promote that, one should seek to harmonize the regulations that enterprises meet under different jurisdictions. As most other developed countries use a factor approach, it could thus be regarded as an advantage for enterprises operating in different countries if Canada did the same. [3]

The views of the Norwegian Authority are especially relevant for Canada given Norway's position as a relatively small, resource-based economy adjacent to a much larger common market.

Canada's divergent merger regulations raise the costs and uncertainty for firms seeking to establish transnational mergers which could enhance consumer welfare and increase Canadian competitiveness. Thus, Canada should seek to harmonize its regulations with those of its major trading partners; section 96 should be dropped, and the evaluation of efficiencies should be included as one factor among many that are considered in the assessment of the anticompetitive effects of proposed mergers.

Efficiency and International Competitiveness

It is sometimes argued that the relatively small size of its markets makes Canada a special case which requires an efficiency defence. It is claimed that mergers which create market power are justified when they allow firms to achieve the economies of scale required to compete internationally.[2] The correct definition of the relevant geographic market makes this argument irrelevant. If a firm is competing internationally, then its relevant geographic market is international, not national or regional. Even if a merger creates a single Canadian competitor, the resulting increase in market power is likely to be negligible as the Canadian firm controls only a small share of the international market. The efficiency defence is not required for such mergers to be approved, as they raise no anticompetitive concerns in the first place. This is the view held by the Norwegian Competition Authority, expressed in its submission to the Competition Bureau's consultation on the treatment of efficiencies (Eckbo and Volden, 2005):

> One of the advantages put forward in the consultation paper is that in a small economy such as the Canadian, greater concentration is required to realise economies of scale. However, Canada is also an open economy, and the relevant markets will often go beyond Canada's borders. Therefore, an efficiency defence that is stronger than Canada's trading partners should not be necessary. [2]

Thus, given that Canada is part of much larger North American and global markets, an efficiency defence is not required for Canadian firms to compete internationally.

The Objectives of the *Competition Act*

As set out in section 1.1, the objectives of the Act are as follows:

> The purpose of this Act is to maintain and encourage competition in Canada in order to promote the efficiency and adaptability of the Canadian economy, in order to expand opportunities for Canadian participation in world markets while at the same time recognizing the role of foreign competition in Canada, in order to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy and in order to provide consumers with competitive prices and product choices.

Thus, the principal objective of the *Competition Act* is to maintain and encourage competition in Canada. Preserving competition helps to achieve other stated objectives, including the promotion of efficiency, equality of opportunity for small businesses, the protection of consumer choice, and the protection of consumer welfare. Clearly, efficiency is not the single objective of the *Competition Act*. However, the efficiency defence allows the

objective of efficiency to override all of the other objectives of competition policy; it, therefore, contradicts the overall objectives of the Act. This is the view held by Létourneau J.A. in his dissent in part in the final decision in *Superior Propane*.[3] In his decision, he writes:

> I was of the view that efficiency of the economy expressed in the defence of efficiency was not meant to and could not override and eliminate competition in an Act designed to maintain and promote competition. Economic efficiency was not, in my opinion, the paramount objective of the Act as found by the Tribunal. [para. 72]

He then quotes from his reasons in the first Federal Court of Appeal decision in the case:

> The Act maintains and promotes competition. It assumes that economic efficiency will generally and primarily develop through competition. ... In my respectful view, however, section 96 was not meant to authorize the creation of monopolies since it would defeat the purpose of section 1.1. The section was not intended to authorize mergers resulting in monopolies whereby, contrary to section 1.1, competition is eliminated, small and medium-sized enterprises are not able to enter or survive in the market and consumers are deprived of competitive prices. [para. 72]

This is strong support for the belief that the primary objective of the Act is not the promotion of efficiency, but the preservation and promotion of competition. In turn, competition helps realise the other stated objectives of the Act. Because efficiency is not the only objective of merger policy, the efficiency defence should not be used to justify otherwise anticompetitive mergers. Merger review should seek to promote all of the objectives (finding a balance when they are in conflict); typically, this can be achieved by promoting and preserving effective competition. The efficiency defence, therefore, should be dropped in favour of the factors approach, as this is best suited for preserving competition first and then finding a balance among the other stated objectives of the Act.

Preserving Competition: the Appropriate Objective for Merger Review

As discussed above, the primary objective of the Act is the preservation and promotion of competition. Critics may argue that, regardless of the stated objective of section 1.1, the primary focus of merger review should be efficiency rather than competition. The remainder of this article argues that preserving competition (best accomplished through the factors approach) is the appropriate objective for Canadian merger review. This is because competition promotes numerous policy objectives, including equality of distribution, freedom of choice and equality of opportunity. Somewhat ironically, preserving competition is also an effective way to promote efficiency: not only allocative efficiency, but cost efficiency and dynamic efficiency as well.

Equality of Wealth and Income

Market power results in a redistribution of wealth from consumers to owners. Typically, owners come from wealthier segments of society. Thus, the elimination of competition will generally result in a less equitable wealth distribution. The overall effect of monopoly profits can be significant. Using conservative assumptions, Comanor and Smiley (1975) estimate the impact of past monopoly profits on the distribution of household wealth in the U.S. In 1962, those households with wealth exceeding $100,000 accounted for roughly 2.4% of

the total households and slightly more than 40% of the household wealth. Comanor and Smiley estimate that in the absence of monopoly, their share of aggregate wealth would lie somewhere between 16% and 27.5%, which would represent a decline of nearly 50% of their household wealth. Monopoly profits benefit only the wealthiest segments; the study estimates that the relative wealth position of 93.3% of the total households would be improved in the absence of monopoly.

Under current Canadian merger policy, the problem of the effects of income distribution has been addressed by the application of Townley's balanced weights approach to the efficiency defence.[4] Nevertheless, the successful application of the efficiency defence to a merger which reduces competition will likely result in a redistribution of wealth from poorer to wealthier segments of society.

Freedom of Choice

Consumers value choice, as indicated by their willingness to pay higher prices for preferred products in differentiated markets. Consumers who see their preferred product eliminated following an acquisition suffer a loss of surplus based on the extra amount they were willing to pay for their preferred product. This loss of surplus is not included in the analysis of the anticompetitive effects of a proposed merger where products are treated as homogeneous under a single market. Granted, given the appropriate definition of the relevant product market, the magnitude of this loss in welfare is relatively small. Nevertheless, excluding the value of choice could tip the scales in favour of a merger which reduces total surplus.

Furthermore, from a practical perspective, the exercise of individual freedom requires choice. Competition preserves consumers' choices and, therefore, protects the practical exercise of freedom.[5] In contrast, an efficiency defence which can limit competition and choice limits consumer freedom.

Equality of Opportunity

Competition helps to ensure that all individuals have an equal opportunity to participate in the Canadian economy. Under Becker's (1971) classic analysis, employer discrimination raises a firm's costs, thereby reducing its competitiveness. In competitive markets, discrimination cannot persist, as those firms practising discrimination will be driven from the market. It is only in the presence of market power that economic profits provide firms' agents with a buffer from the rigours of competition which allows them to exercise their preference for discrimination. Numerous studies have identified the link between market power and both racial[6] and gender[7] discrimination.

Uncertainty in the Evaluation of Efficiencies

The wording of section 96 raises efficiency to a level of importance where it is allowed to override the other objectives of competition policy. However, there is considerable difficulty and uncertainty involved in predicting post-merger efficiencies. Even the merging firms themselves seem to have difficulty predicting post-merger efficiencies. Consider the principal finding of an exhaustive survey conducted by Tichy (2001) of about 80 empirical merger studies:

> The empirical results unveiled the myth that mergers increase efficiency and improve the competitive positions of countries. About half of mergers did not attain even the business goal of improving profits; about a quarter increased profits by market-power induced price rises, and only one quarter at best augmented consumer welfare. [385]

Unless these merging firms are irrational, they must believe that (in the absence of gains in market power) their merger will produce efficiency gains that will ultimately lead to greater profits. That roughly half of all mergers did not even attain the goal of improving profits shows that firms are not particularly adept at predicting post-merger efficiency gains. This is not to suggest that authorities should block mergers because they have a tendency to destroy value: mergers are an important strategic vehicle for responding to changes in business conditions. Rather, given merging firms' poor record of realising post-merger efficiency gains, claims of post-merger efficiencies should be treated with a great deal of scepticism. This view is echoed in the U.S. *Horizontal Merger Guidelines*:

> Efficiencies are difficult to verify and quantify, in part because much of the information relating to efficiencies is uniquely in the possession of the merging firms. Moreover, efficiencies projected reasonably and in good faith by the merging firms may not be realized. Therefore, the merging firms must substantiate efficiency claims so that the Agency can verify by reasonable means the likelihood and magnitude of each asserted efficiency, how and when each would be achieved (and any costs in doing so), how each would enhance the merged firm's ability and incentive to compete, and why each would be merger-specific. Efficiency claims will not be considered if they are vague or speculative or otherwise cannot be verified by reasonable means.[8]

This lingering suspicion can be traced back to earlier merger guidelines, as far back as 1968, predating the *Competition Act*.[9] Note that this high level of scepticism towards claims of post-merger efficiencies exists even though, under U.S. legislation, efficiencies are evaluated as one factor (among many) that is considered in the evaluation of whether a proposed merger would lead to a substantial lessening of competition.

The uncertainty associated with predicting post-merger efficiencies makes the application of section 96 difficult and vague. Emberger (2003), an official of the EU's Competition Directorate on exchange at the Competition Bureau in 2002, echoes this view in regards to section 96:

> ...it is a well-known fact that merger-related claimed efficiencies are often debatable and realised efficiencies post-merger are often less than predicted. ... It is recognized that the attainment of dynamic efficiencies is crucial to both the general evolution of competition and the international competitiveness of Canadian industries. However, claims that a merger will lead to dynamic efficiencies are ordinarily extremely difficult to measure. Accordingly, the weight given to such claims will generally be qualitative in nature. [45]

Further on, she writes:

> Applying the balanced weight standard requires a very difficult and complex socio-economic welfare analysis, which is probably beyond the capabilities of any competition watchdog, including the Canadian Competition authorities. What is more, such an analysis cannot take

> sufficient account of qualitative effects a merger may generate (such as a reduction in service level or innovation), which are not quantifiable like a price increase. [46]

Clearly, there are considerable difficulties and uncertainty associated with predicting post-merger efficiencies and applying section 96. In Canada, there is a degree of scepticism – efficiencies are only accepted if they can be substantiated and if the gains could not be obtained by other means.[10] Nevertheless, with the efficiency defence, an entire merger case can hinge on efficiency claims. Given the poor record of merging firms in predicting their own post-merger efficiencies, even with their intimate knowledge of their operations, it is reasonable to suggest that what may appear to competition authorities to be the most reasonable efficiency claims may never be realized.

Competition and Cost Efficiency

"The best of all monopoly profits is a quiet life."[11]

Given the uncertainty associated with predicting post-merger efficiency gains, the best way to promote efficiency is not an efficiency defence which can lead to a reduction in competition. Rather, the best way to promote efficiency is to preserve competition. Competitive rivalry encourages continuous productivity improvements as firms strive to gain an advantage over their rivals. In the absence of competition, firms may not always pursue cost-efficiency.

There are several reasons why a lack of competition may lead to a reduction in cost-efficiency. First, market power may generate profits which allow managers to pursue a "quiet life" where they do not have to work too hard to keep costs under control but still provide owners with economic rents. Second, market power may allow managers to pursue objectives other than firm profits or managerial leisure. Examples include expansion of market share and managerial influence and the reduction of risk below profit-maximizing levels. Third, managers may expend resources to obtain and maintain market power. This practice may be profit-maximizing for the firm, but it is not cost-efficient. Fourth, the existence of market-power-induced profits may allow inefficient managers to persist. In the absence of competitive rivalry, there is a lack of signals for owners to determine whether managers are efficient. Profits from market power may make managers appear to be efficient when they are not (Berger and Hannan, 1998). The magnitude of the loss of cost efficiency resulting from market power can be quite significant. In an empirical study on the U.S. banking industry, Federal Reserve Board Governors Berger and Hannan find "the estimated efficiency cost of concentration to be several times larger than the social cost of mispricing as traditionally measured by the welfare triangle." (Berger and Hannan, 1998)[12] Estimates of cost efficiency losses resulting from the "quiet life" are not included in the analysis of the anticompetitive effects of a proposed merger. Paradoxically, mergers which raise market power but are permitted under the efficiency defence may lead to a reduction, not only in consumer welfare, but in cost efficiency as well.

Competition and Dynamic Efficiency

The efficiency defence may also lead to a reduction in dynamic efficiency. Not only does competitive rivalry encourage firms to seek cost advantages over their competitors, it also provides the incentive to seek technological

advantages. In a recent study of the principal influences on the growth and innovation of the market economies, Baumol (2004) writes:

> Free competition ... has arguably played a critical role in the growth of the capitalist economies. Of particular significance here is rivalry among oligopolistic firms – those large firms in markets dominated by a small number of sellers. And crucial here is the fact that in today's economy many rival oligopolistic firms use innovation as their main battle weapon in which they protect themselves from competitors and with which they seek to beat those competitors out. [10]

Monopolists making the decision to invest in innovation, in a sense, are competing with their existing products. A new product can jeopardize the on-going profits from existing technology. This replacement effect reduces the incentive for monopolies to invest in research and development and retards their introduction of innovative products. In contrast, when there is competitive rivalry, the potential payoff from innovation can be substantial. A successful new technology may allow an innovator to jump ahead of its competitors to earn monopoly profits. Furthermore, competitors who fail to innovate may be cut out of the market altogether. Thus, competition creates a greater incentive to innovate.

While large firms tend to be effective at producing incremental improvements to existing technologies, small firms typically produce more revolutionary innovative breakthroughs. Consider the principal findings of a recent study sponsored by the U.S. Small Business Administration (CHI Research, 2003):

- Small firm innovation is twice as closely linked to scientific research as large firm innovation on average, and so is substantially more high-tech or leading edge.

- Small firms produce more highly cited patents than large firms on average. Small firm patents are twice as likely as large firm patents to be among the 1% most cited patents. That is, small firm patents are on average more technically important than large firm patents.

- Small patenting firms produce 13-14 times more patents per employee as large patenting firms.

These small innovative firms often rely on large firms to market and distribute their innovations (through licensing or strategic alliances, for example). Reduced competition among potential partners gives the large firms more bargaining power when negotiating terms with the small innovators (Acs, Morck and Yeung, 2000). This, in turn, reduces the payoff accruing to small innovators and, thus, their incentive to innovate. Therefore, an efficiency defence which reduces or eliminates competition may limit small firm innovation, reducing dynamic efficiency.

Conclusion

This article has argued that section 96 of the Act should be dropped in favour of including efficiencies as a factor among the others considered in the evaluation of whether a merger will lead to a substantial lessening of competition. There are two primary reasons this change should be adopted. First, it will bring Canadian merger policy in line with that of our major trading partners. Such harmonization will reduce the barriers to Canadian

firms seeking to establish transnational mergers which could increase consumer welfare or enhance Canadian firms' competitiveness in international markets. Second, Canada should adopt the factors approach to the evaluation of efficiencies because this would change the primary focus of merger policy from efficiency to the preservation of competition. Competition helps markets achieve a number of policy objectives, including equality of opportunity, freedom of choice, a more equitable wealth distribution, allocative efficiency, cost efficiency and dynamic efficiency. Without a doubt, efficiency is an important objective of merger review policy, but so are the other objectives. Given the uncertainty associated with predicting post-merger efficiencies and the benefits of competition towards promoting cost-efficiency and dynamic efficiency, it is not clear that an efficiency defence is even the best way to promote efficiency. For these reasons, a better option for the treatment of efficiencies is to include the analysis of efficiencies with the other factors considered in the analysis of the anticompetitive effects of the merger.

Notes

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[1] This article does not intend to assess the merits or shortcomings of the *Superior Propane* decision. *Superior Propane* is relevant to this article in that the case raised awareness of the problems associated with section 96.

[2] "The Treatment of Efficiencies under the *Competition Act*: Summary of Stakeholders' Written Comments" (prepared by The Intersol Group and InfoLink, conference publishers, January 2005) at 2-3.

[3] *The Commissioner of Competition v. Superior Propane Inc. and ICG Propane Inc.*, 2003 FCA 53.

[4] See Townley (1999, 2004).

[5] Economists such as Hayek (1944) and Friedman (1962) have discussed the value of competition as a means of preserving freedom of choice.

[6] See, for example, Cavalluzzo and Cavalluzzo (1998) and Berkovec et al. (1998).

[7] See, for example, Brainerd and Black (2002) and Ashenfelter and Hannan (1986).

[8] Revised Section 4, *Horizontal Merger Guidelines*, U.S. Department of Justice and the Federal Trade Commission, April 8, 1997.

[9] *Merger Guidelines, Abridged Version,* Antitrust Division of the U.S. Department of Justice, May 1968.

[10] *Merger Enforcement Guidelines*, Competition Bureau, at paras. 8.7 – 8.10.

[11] John R. Hicks, "Annual Survey of Economic Theory: The Theory of Monopoly" (1935) 3:1 Econometrica.

[12] Berger and Hannan's estimates range from two times to 200 times. Their best, though still conservative, estimate is 20 times.

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CANADIAN COMPETITION RECORD

EFFICIENCIES IN MERGER REVIEW: WHAT IS THE BEST APPROACH FOR CANADA?

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Part I – Introduction

In 1986, the *Competition Act* was amended to include what many at the time described as a "state-of-the art" efficiencies defence, in what is now section 96. It was proclaimed into force with much fanfare and hope that efficiencies would play a significant role in the administration and enforcement of the new merger provisions in the Act.[1] Unfortunately, the experience over the first 20 years has been a profound disappointment. Apart from one litigated case, *Commissioner of Competition v. Superior Propane* ("*Superior Propane ICG*"),[2] in which the elements of the defence were found to have been met, section 96 has not played any meaningful role in merger review.[3] Indeed, a number of economists have pointed out that had the anti-competitive effects of the merger been properly calculated by the Commissioner of Competition, the efficiencies defence probably would not have been met even in that single case.[4]

Of course, since at least some aspects of how section 96 ought to be interpreted and applied have now been clarified after two decisions of the Competition Tribunal and another two of the Federal Court of Appeal (the "FCA"), the prospects for the efficiencies defence could get better. However, as discussed in Part IV below, there are good reasons to remain sceptical.

Some might argue that efficiencies have played, and will continue to play, a meaningful role in merger review outside the context of the section 96 defence, namely, (i) in the exercise of the Commissioner's discretion not to challenge mergers in "close" cases, and (ii) when the Competition Bureau is assessing whether a merger is likely to prevent or lessen competition substantially.

As to the exercise of discretion in favour of efficiencies in close cases, the public record reflects that there were a few such cases in the late 1980s,[5] but since then the paucity of press releases and backgrounders issued in connection with the Bureau's merger reviews makes it difficult to make this argument. In any event, it is highly likely that the average number of such cases has been less than one or two every five years since 1986, particularly given (a) the complete absence of anecdotal or other evidence suggesting that there have been more than a small handful of such cases since 1986, (b) the Bureau's support for Bill C-249,[6] together with the positions it took throughout the *Superior Propane ICG* case, reflect a certain animosity towards efficiencies in recent years, and (c) that certain Commissioners over the years have taken the position that any case in which the section 96 defence is invoked ought to be put before the Competition Tribunal.[7]

As to whether the Bureau gives appropriate consideration to efficiencies in determining the likely competitive effects of mergers, questions have been raised in recent years. In the author's experience, the Bureau historically has indeed considered efficiencies at the stage of assessing likely competitive effects. This practice was orally confirmed by Gaston Jorré, Senior Deputy Commissioner (Mergers), during the recent public consultation

process on efficiencies. However, others appear to have had a different experience.[8] On at least one occasion, a senior Bureau official has publicly stated that efficiencies are not considered at the competitive effects stage of the Bureau's analysis.[9] Moreover, the Tribunal observed in its redetermination decision in *Superior Propane ICG* (the "Redetermination Decision") that "efficiencies are to be considered only under s. 96 and not under s. 92".[10] While this statement was made in the context of explaining that efficiencies do not have to be so great as to "cleanse" the anti-competitive effects of mergers, as is the case in the U.S., it was quoted in the consultation paper (the "Consultation Paper") that reinvigorated the current debate, as providing support for the position that "[c]urrently, there is relatively little scope for consideration of merger efficiencies at the stage of determining whether a merger substantially lessens competition" [11]

The bottom line is that, no matter how one looks at the record, it is clear that efficiencies have not played a meaningful role in merger review in this country over the last 20 years. The situation is such that the House of Commons Standing Committee on Industry, Science and Technology recommended, following an in-depth review of the Act, that "the Government of Canada immediately establish an independent task force of experts to study the role that efficiencies should play in all civilly reviewable sections of the Competition Act".[12]

Those experts, who served on the Commissioner's Advisory Panel on Efficiencies (the "Advisory Panel"), have subsequently concluded that "the efficiency defence has had very little public policy relevance"; that "it has not lived up to the hopes and expectations of the members of the Economic Council of Canada"; that "while efficiencies have not been entirely ignored ...they have not been a regular or explicit consideration in merger review either"; and that "the current standard for weighing efficiency gains against competition effects is not satisfactory" [13]

These and other findings led the Advisory Panel to recommend, among other things, that:[14]

- competition policy in Canada should encourage efficiency;
- merger review should involve regular and explicit consideration of the efficiency gains generated by a merger;
- the efficiencies defence in merger review should be retained;
- the circumstances in which the defence may apply, and the applicable standards, should be more clearly defined, transparent and consistent;
- the defence should not be permitted in the case of a merger to monopoly;
- the Act should be amended to make it explicit that efficiency gains also should be considered in the analysis of whether a merger substantially prevents or lessens competition;
- the current practice of conducting a qualitative assessment of claims of dynamic efficiency is appropriate and consistent with international practice, although measurement problems preclude such claims from being given special weight in merger review;

- the existence of a major productivity gap relative to the U.S. and other OECD countries is an objective reason for giving efficiency gains relatively more weight in Canadian merger law than they are given in the laws of the U.S. and many other jurisdictions; and

- the Bureau should take into account the strength of merging parties' efficiency claims and the likelihood that a trade-off is justified when deciding whether to challenge a merger before the Tribunal, i.e., it should not routinely refer to the Tribunal cases in which the efficiencies defence is invoked.

With the noteworthy exception of the suggestion that the efficiency defence not be available in the case of a merger to monopoly, the foregoing recommendations make good sense.

A modified version of the total surplus test would best respond to the Advisory Panel's recommendation for a test that is transparent, predictable and certain for the business community and the public at large. However, the recent record suggests that it is unlikely that either Parliament or the Bureau would support amendments to the Act which would resurrect the total surplus approach. In any event, the experience to date with section 96 suggests that the total surplus test, and anything resembling it, including the current test, is not politically sustainable. Moreover, there are good grounds for having substantial reservations about the practical utility of, and the costs that would be associated with invoking and administering, the total surplus test or any other test that is based on a quantitatively-oriented trade-off framework.

For the reasons explained in this article, it will not likely be possible to give efficiencies a more meaningful role in merger review unless an alternative approach that has not yet been tried or proposed in the Consultation Paper is adopted. After setting out the criteria against which alternative tests should be assessed, this article evaluates the various approaches that have been tried or proposed and ultimately proposes an alternative approach and refinements to the existing wording of the Act if the proposed alternative approach is not embraced.

Part II – The Criteria Against which Alternative Tests Should be Assessed

Transparent and Predictable

The Advisory Panel underscored the importance of a revised efficiency defence being transparent and predictable. This is certainly a very important criteria. All other things being equal, business persons are more likely to make use of a defence that is transparent and predictable than one that is associated with significant uncertainty. Of course, transparency and predictability can only take a test so far. It would be difficult to craft a defence that is more transparent and predictable than the total surplus test that was set forth in the Commissioner's 1991 *Merger Enforcement Guidelines* ("MEGs")[15] and endorsed by the Tribunal in its initial decision (the "Initial Decision") in *Superior Propane/ICG*.[16] Unfortunately, as discussed in Part V below, that test played virtually no role in merger review in the decade or so that it was used by the Bureau.

Meaningful Role to Efficiencies in Merger Review

Given the Advisory Panel's conclusions that competition policy should encourage efficiency and that "efficiency gains should be a *regular* and *explicit* consideration in merger review",[17] and the overall tenor of its report, it

is reasonable to infer that the Advisory Panel believed that the efficiencies defence should play a meaningful role in merger review. In any event, at the very least, it should play a more meaningful role than it has played to date. This criterion likely would exclude all of the specific approaches that the Bureau has advocated or supported to date.

Practical and Workable

The Advisory Panel also emphasized the importance of efficiency claims being "accessible". An amended efficiencies defence is not likely to play a meaningful, if any, role in merger review under the Act unless it is practical and workable. Business persons, their legal counsel and Bureau staff must be able to work with the defence at a practical level. To a certain extent, this criterion is consistent with the criterion of transparency and predictability. However, as a test becomes increasingly complicated due to the nature of the economic calculations, assumptions, and perhaps even value judgments that must be made, it becomes less understandable and therefore less practical and workable for business persons. Except in the rarest of cases, business persons are not likely to risk the very large sums of money that typically would be at stake in a case in which reliance would have to be placed on the efficiencies defence, unless the defence were readily understandable, practical and workable.

Politically Sustainable

It is particularly remarkable that the current debate regarding the role of efficiencies in merger review has been conducted virtually without explicit consideration of the need for any revised or refined efficiencies defence to be politically sustainable. The one noteworthy exception is the Advisory Panel, which observed that Parliament is the appropriate body to define the appropriate standard for any trade-off that should be made between efficiency gains and anti-competitive effects, and which recommended that any revised efficiencies defence should be "politically acceptable".[18]

The simple fact is that any amended efficiencies defence that is not developed with appropriate consideration being given to political realities is not likely to be sustainable in the long run, at least not if the revised approach resembles anything that (i) has been discussed to date, and (ii) would not virtually vitiate the defence.[19] If one simply had to be concerned about the fact that an otherwise appealing approach might be repealed at some point in the future, one might be inclined to go ahead with it and hope that it is retained for as long as possible. Unfortunately, past experience[20] and common sense suggests that it would be prudent to be very wary of how Parliament, the Commissioner and even the public at large might react if a high profile merger is permitted to proceed on the basis of a test that cannot readily be understood or cannot withstand scrutiny by the layperson. In the type of emotionally charged political environment that might prevail after such a merger is permitted to proceed on the basis of efficiencies and in the face of substantial political and public opposition, the Act might be amended in a way that vitiates the defence or worse (e.g., a political override may be inserted into the merger review provisions).

Promotion of Economic Welfare

It is easy for those in the competition community to take for granted that an important criterion for assessing alternative potential efficiency defences that may be proposed is the extent to which the alternatives focus solely on the promotion of economic welfare and are not susceptible to being interpreted in a way that advances other socio-political objectives at the expense of economic welfare.

Cost

Another factor that should be kept in mind in evaluating alternative approaches to efficiencies is the cost that those approaches are likely to impose on business persons, the Bureau, and the public at large (who will indirectly pay the costs of the Bureau's assessment and of any subsequent Tribunal and appellate proceedings, to the extent that they are not paid by the merging parties and interveners).

Convergence with Foreign Approaches?

In his remarks to the Standing Committee on Industry, Science and Technology, the immediate past Commissioner defended Bill C-249 in part because, as amended prior to the time of his appearance before the Committee, it contemplated an approach that he believed is "consistent with the treatment of efficiencies in other jurisdictions".[21]

All other things being equal, convergence with the approach taken by one's principal trading partners, particularly those with whom one shares a free trade zone, is a worthy goal. This is provided that there are not good reasons why a different approach would be better and provided that the benefits of a unique or tailored approach do not outweigh the benefits of convergence.

In the case of how efficiencies are treated in merger review, the benefits of converging towards the approach adopted in the U.S., the E.U. and the U.K. would appear to be very slight, at best. Business persons would know with a high degree of certainty that efficiencies would rarely, if ever, play a meaningful role in merger review. By contrast, an approach tailored to recognize unique characteristics of Canada's economy, such as the greater probability of the existence of non-captured scale and other economies,[22] and our reduced ability to withstand Type I errors (e.g., having pro-competitive mergers blocked), would seem to make good sense. Such an approach would offer the prospect of capturing those efficiencies, increasing overall economic welfare, and bridging the "major productivity cap" that the Advisory Panel cited as being "an objective reason for giving efficiency gains relatively more weight in Canadian merger law than they are given in the laws of the United States and many other jurisdictions".[23]

Parenthetically, to the extent that other jurisdictions have been increasing the role given to efficiencies over the last decade, it would be ironic if Canada were to adopt, in the name of convergence, an approach that went in the opposite direction.

Part III – Efficiencies as a Factor, Defence or Both?

During the consultation process that preceded the Advisory Panel's appointment, participants in a roundtable held on January 26, 2005 in Toronto were asked whether efficiencies should be treated as (i) a factor in the initial determination of whether a merger is likely to prevent or lessen competition substantially, or (ii) a defence to a finding that a merger is likely to have such anti-competitive effects. The author submitted that the optimal approach should be to treat efficiencies as <u>both</u> a factor and a defence, given our experience and the questions that evidently have been raised regarding whether the Bureau gives appropriate consideration to efficiencies during the competitive effects stage of its assessment.

Many advocates of the "factor approach" believe that the Bureau would more frequently consider efficiencies at the initial stage of its assessment if efficiencies were explicitly listed together with the various other assessment criteria set forth in section 93 of the Act.[24] They further believe that amending the Act in this way would help to overcome the reluctance that some people appear to have to make submissions on efficiencies, because that "might be seen as an acknowledgement that [their] merger contravenes section 92."[25] They also believe that few parties are willing to invest the substantial resources required to develop a full defence under section 96.

There are at least three fundamental problems with relying solely on a factor approach. First, efficiencies wouldn't help in the very situation in which they might make a difference. In short, greater efficiencies would be required than under any other approach when a balancing of the other assessment criteria would lead to the conclusion that the merger is likely to prevent or lessen competition substantially. This is because such a conclusion would be based upon a finding that the merger is likely to result in the merged entity having the ability to exercise materially greater market power, alone or interdependently with other firms in the relevant market, than it would be able to exercise in the absence of the merger. Accordingly, the only way that efficiencies could save the merger at that point would be if they were so great as to "cleanse" the merger of its anti-competitive effects, i.e., by reducing the merged entity's profit-maximizing level of output to a point that corresponds to a price that is at or below the price that likely would have prevailed in the absence of the merger. In other words, efficiencies would have to pass what the Tribunal has referred to as the "modified price standard" in order to make a difference.[26] As has been explained elsewhere,[27] this would be an exceptionally difficult test to meet. As the Tribunal has noted, this is confirmed by the U.S. experience.[28] In the Canadian context, it is doubtful that this test would ever be met.

The second fundamental problem with relying solely on the factor approach is that it is conceptually inconsistent with viewing competition as a rivalrous process to believe that efficiencies could be relied upon to justify a conclusion that a merger is not likely to prevent or lessen competition substantially when all other factors point towards the opposite conclusion. If a merger is likely to create or increase market power, or to maintain it at a greater level than it would be in the absence of the merger, it is axiomatic that the process of competition likely will be lessened or prevented. If this effect on market power is likely to be material or significant, then it is axiomatic that the process of competition likely will be lessened or prevented substantially. This is because the Lerner Index will have increased to a level that indicates that there has been a substantial lessening or prevention of the intensity of competition, as reflected in an increase in market power that can only be attributed to a substantial weakening of the constraints imposed on the merging parties' behaviour by the collective forces of

actual and potential competition. As the Tribunal has pointed out, "s. 92 [is] about market power, the ability to influence price, rather than about whether price would, or would likely, rise or fall as a result of the merger"[29] Accordingly, the only way that efficiencies could save a merger that otherwise would be found to be likely to prevent or lessen competition substantially, would be if the fundamental concept of competition currently contemplated by section 92 were changed.

The third problem that would be associated with relying solely on the factor approach is that it would likely result in fixed-cost savings being discounted or completely ignored.[30]

It follows that the only way that efficiencies can have any realistic prospect of making a meaningful difference when a balancing of other factors would lead to a conclusion that a merger is likely to prevent or lessen competition substantially is if they can be considered as part of an appropriately defined defence.

To address the genuine concerns that apparently are held by some regarding the role that efficiencies should have (but apparently have not always had) during the initial stage of the Bureau's merger review process, it would make good sense also to amend the Act to include efficiencies among the factors to be considered by the Tribunal (and, implicitly, by the Bureau) at that stage, i.e., in determining whether a merger is likely to prevent or lessen competition substantially. Indeed, such an amendment would in any event be appropriate given the Tribunal's observation that "efficiencies are to be considered only under s. 96 and not under s. 92".[31]

At the competitive effects (i.e., section 92) stage of the assessment, it would be appropriate to consider, among other things, the extent to which: (i) the overall rationale for the merger is based on a desire to achieve cost savings or synergies; and (ii) those efficiencies are likely to have a positive effect on rivalry, for example by (a) assisting two smaller firms to better compete with the market leader, (b) increasing the merged entity's incentive to expand production and reduce prices, thereby reducing its incentive to coordinate with other firms in the market post-merger, or (c) leading to the introduction of new or better products or processes.[32]

Part IV – The Current Approach (Weighted Surplus)

The Advisory Panel expressed dissatisfaction with the current approach and characterized it as being "highly complex" and "lacking basic predictability"[33] It also observed that many consider it to be "cumbersome and unpredictable"[34] Professor Tom Ross has further observed that "many informed people believe it is unclear"[35]

This approach performs poorly against virtually all of the assessment criteria discussed in Part II above. It is highly unlikely that business persons would understand the approach or have any confidence in how it would be applied in the context of a transaction that they may be considering. As a result, it is difficult to believe that they would risk proceeding with any transaction that stands a reasonable chance of being found to be likely to prevent or lessen competition substantially, in reliance on the efficiency defence as currently interpreted by the Bureau, the Tribunal and the Federal Court of Appeal ("FCA").

Caution must be exercised when describing the "current approach" because technically there is no single approach. In its first decision in *Superior Propane/ICG*, the FCA specifically stated that "the same standard may not be equally apposite for all mergers".[36] It then endorsed the balancing weights "approach" (described below) as meeting its generic requirements that, whatever approach is selected, it "must be more reflective than the total surplus approach of the different objectives of the Competition Act", and it must be "sufficiently flexible in its application to enable the Tribunal to fully assess the particular fact situation before it."[37] In its Redetermination Decision, the Tribunal stated that it would have adopted the balancing weights approach had there been "sufficient information in evidence to come to an assessment of whether the estimated balancing weight of 1.6 is reasonable given the socio-economic differences between and among consumers and shareholders".[38] In the end, it adopted what has been characterized by the FCA and the Bureau as the "socially adverse effects" approach.[39] (The 2004 MEGs state that "[o]ther approaches to the wealth transfer may be appropriate, depending on the circumstances of a particular case".[40]) Ross and Winter have described the "socially adverse effects" approach as the "weighted surplus approach".[41] That is the term that will be used in this article.

The weighted surplus approach is a hybrid between what is now being called the consumer surplus approach and the total surplus approach that was described in the Bureau's 1991 MEGs[42] and endorsed by the Tribunal in its Initial Decision.[43] Those approaches are briefly summarized in Parts V and VI below. The weighted surplus approach is a hybrid because it requires some of the wealth transfer likely to result from the merger to be considered in the section 96 trade-off assessment if, and only if, a part of that wealth transfer (or, in extreme cases, all of the wealth transfer) would involve a socially adverse transfer of income from an identified lower income group to higher income shareholders.[44]

In the weighted surplus approach, the total surplus approach is the general starting point. Accordingly, if a merger is found to be likely to prevent or lessen competition substantially and the efficiency defence in section 96 is invoked, an assessment of the merging parties' various efficiency claims must be made. Among other things, this will involve an assessment of whether any of the claims should be excluded or reduced on the basis that: (i) the likelihood of their attainment has not been established on the balance of probabilities; (ii) they likely would be attained in alternative ways if the order sought by the Commissioner were made; and (iii) they will not result solely from a redistribution of income between two or more persons within the meaning of subsection 96(3).[45] In addition, the costs of achieving claimed efficiencies must be calculated and deducted from the aggregate amount claimed. Moreover, an assessment may be made of the extent to which the claimed gains are likely to accrue to foreign shareholders, as the Tribunal appeared to take the position that any portion of the claimed efficiency gains that flows through to foreign shareholders should not be included in the trade-off assessment.[46] Furthermore, to account for differences between the points in time when quantifiable anti-competitive effects are likely to occur and when quantifiable efficiency gains are likely to be realized, the present value of the former (and ultimately the latter) must be calculated. This will involve making an assumption as to the appropriate discount rate, which can have a substantial impact on the overall assessment.

Once the present value of the "cognizable" efficiency gains is calculated, the "effects of any prevention or lessening of competition that will result or is likely to result from the merger" must then be calculated. This

begins with an estimate of the price elasticity of demand. This is necessary in order to estimate the magnitude of the likely price increase and reduction in output likely to result from the merger. It is prudent to prepare a sensitivity analysis based on a range of plausible demand elasticities.

Next, an assessment must be made of the pre-existing market power exercised by the merging parties pre-merger.[47] A range of estimates of this can be derived from the above-mentioned estimates of the market elasticity of demand as well as from the firm elasticity of demand.[48]

Based on the FCA's initial decision in *Superior Propane/ICG*, one must then determine how to treat the wealth transfer from customers to producers, (represented by area C in Appendix 1).[49] As observed by the Tribunal, this will require "a value judgment and will depend on the characteristics of [the affected] consumers and shareholders",[50] and it will "rarely [be] so clear where or how the redistributive effects are experienced".[51] In general, the exercise "will involve multiple social decisions",[52] and "[f]airness and equity [will] require complete data on socio-economic profiles on consumers and shareholders of producers to know whether the redistributive effects are socially neutral, positive or adverse".[53]

If it is found that the merger likely will result in a socially adverse transfer of wealth from one or more identified lower income group(s) to higher income shareholders, a decision must then be made as to how to weigh the relevant part(s) of the wealth transfer. (If the entire wealth transfer will involve a socially adverse transfer, then it would be necessary to decide how to weigh the full transfer.) If the income effect on some purchaser groups would be more severe than on others, different weightings among the groups presumably would be required.

At this point, the balancing weights approach can be of some assistance. As proposed by Professor Peter Townley, one of the Commissioner's experts in *Superior Propane/ICG*, this simply involves determining the weight that would have to be given to the aggregate reduction in consumer surplus (i.e., the sum of the deadweight loss, including any deadweight loss attributable to pre-existing market power, plus the wealth transfer) in order for it to equal the increased producer surplus that would result from the merger (i.e., the sum of the efficiency gains and the wealth transfer), if the value of the producer surplus is multiplied by 1.[54] For example, in *Superior Propane/ICG*, the aggregate reduction in consumer surplus was $43.5 million, i.e., the estimated $40.5 million wealth transfer plus the estimated $3 million deadweight loss. By comparison, the aggregate increase in producer surplus was $69.7 million, i.e., the sum of the efficiency gains accepted by the Tribunal, namely $29.2 million, plus the wealth transfer of $40.5 million. The balancing weight was therefore represented by w in the following formula: $1(69.7) - w\ (\$43.5) = 0$. Solving for w yielded a value of 1.6, which was the weight at which the consumer losses and the producer gains just balanced.[55] Accordingly, for consumer losses to outweigh producer gains, they would have had to be given a weight of greater than 1.6.

Professor Townley's helpful insight was that members of the Tribunal often would be in a position to determine, even in the absence of complete information, whether there was any reasonable basis for believing that a weighting greater than the balancing weight ought to be applied to the socially adverse portion(s) of the wealth transfer. If not, then notwithstanding an insufficiency of the information required to accurately calculate a full set of distributional weights, it could be concluded that the efficiencies likely to result from the merger would outweigh

the adverse effects on consumer surplus. As is apparent, this is more of a tool to be used within the weighted surplus approach than a full-blown approach in its own right. It would appear that the FCA misunderstood this fundamental fact, as what it characterized as the balancing weights approach does not resemble what Professor Townley proposed.[56]

In its Redetermination Decision, the Tribunal observed that Professor Townley had assigned the same weight to all consumers only because "information on individual consumers is lacking" [57] The Tribunal then looked to the tax system for guidance on "social attitudes toward equity among different income classes" and observed that "if the proper weight is to be inferred from the tax system alone, then it is unlikely to be as high as 1.6 given the general proportionality of effective tax rates" [58] Later in its decision, the Tribunal stated that the balancing weights approach would have been adopted if there had been "sufficient information in evidence to [enable it to] come to an assessment of whether the estimated balancing weight of 1.6 is reasonable given the socio-economic differences between and among consumers and shareholders".[59]

Although the balancing weights tool did not turn out to be particularly helpful in *Superior Propane/ICG*, it has the potential to make a more useful contribution where additional information on socio-economic differences between and among consumers and shareholders is available. Particularly in cases where the efficiencies are substantial and much of the wealth transfer should be considered to be neutral, which Ross & Winter suggest will usually be the case,[60] the balancing weights tool can help to demonstrate that the weights given to socially adverse effects would have to be unreasonably and unrealistically high in order for the adverse impact on consumer surplus to outweigh the likely increase in producer surplus.

After determining that there was not sufficient information in evidence to make use of Professor Townley's balancing weights proposal, the Tribunal proceeded to attempt to estimate the adverse redistributive effect of the merger at issue based on the evidence. Ultimately, it drew upon statistical information in Professor Townley's expert report that he obtained from Statistics Canada's report entitled *Family Expenditure in Canada, 1996*. That information suggested that only 4.7% of purchasers of bottled propane were from the lowest-income quintile, while 29.1% were from the highest-income quintile. After recognizing that not necessarily all of the other household purchasers were in the higher income groups, the Tribunal ultimately focused on the lowest-income quintile and held that it could not "avoid the conclusion that the redistributive effect of the merger on low-income households that purchase propane will be socially adverse".[61] While it also appeared to recognize that lower income groups might use propane for "non-essential" uses,[62] such as barbeques, the Tribunal was not able to draw any firm conclusions based on the evidence. It also was not able to draw any conclusions regarding the extent to which business purchasers such as farm businesses which use propane to dry grain might be owned by less well-off persons or might be unable to pass on the price increase resulting from the merger.

Accordingly, the Tribunal confined the adverse effects on consumer surplus to the $3 million in quantifiable deadweight loss that it had found in its Initial Decision would likely result from the merger at issue, plus the $3 million reduction in deadweight loss that it attributed to changes in the merged company's product line, plus an estimate of $2.6 million to reflect the adverse redistributive effect on the lowest-income quintile of bottled propane purchasers.[63] After observing that it had no basis upon which to determine whether the deadweight loss

should be weighted equally with adverse redistribution effects, the Tribunal ultimately concluded that, even if the $2.6 million in adverse distribution effects were weighted twice as heavily as the $6 million reduction in deadweight loss, the combined adverse impact on consumer surplus would not exceed $11.2 million.[64] Since this estimate was still far below the recognized efficiency gains of $29.2 million, it concluded that the defence in section 96 had been met.

On appeal, the FCA held that the Tribunal had basically followed the directions it had given to the Tribunal in its first decision. Among other things, it also confirmed that the Commissioner bears the burden of proving the extent of the anti-competitive effects of a merger, including any adverse redistributive effects.[65]

Where does all of this leave us?

As the Advisory Panel has recognized, the collective impact of the FCA's decisions and the Tribunal's Redetermination Decision has left us in a position in which "the efficiency defence may be less accessible today than it was when it was first enacted".[66]

Business persons who are considering pursuing an efficiency-enhancing merger that may raise significant *prima facie* competition issues and that therefore requires the benefit of the efficiency defence, would have to consider a host of complicated factors that collectively would give rise to substantial uncertainty as to whether the merger would be found to meet the requirements of the defence. Broadly speaking,[67] these include:

- The extent to which their efficiency claims are likely to be rejected or reduced on the ground that: (i) they have not been demonstrated on the balance of probabilities – in the absence of extensive substantiation, past experience suggests that claimed gains are likely to be significantly discounted by the Bureau; (ii) they likely would be achieved in alternative ways if the order that likely would be sought by the Bureau were granted by the Tribunal – once again it would be prudent to expect that Bureau staff will enthusiastically and exhaustively explore this issue to the point that there is some significant discounting of claimed gains; and (iii) they represent mere distributions of income between two or more persons within the meaning of subsection 96(3).[68] The latter filter can involve complicated and subjective decisions, for example, relating to the value placed on human resources that are likely to be laid off and therefore freed-up for other uses after the merger.

- The extent to which the aggregate gains that survive the filtering described in (i) – (iii) of the preceding paragraph are likely to be further reduced on the ground that some or all of them flow through to foreign shareholders[69] – this will require an assessment of the nationality of shareholders, something that can be very difficult for a large publicly traded company.

- The extent to which the remaining gains are likely to be even further reduced to account for the costs required to achieve the gains.

- The weight that likely will be given to qualitative dynamic efficiencies, such as any R&D synergies or product improvements that are likely to result from the merger.

- The weight likely to be given to any reduction in non-price competition, such as quality, service, variety and innovation. This is something that is very subjective, and therefore uncertain, in nature.

- The extent to which the Bureau and the Tribunal likely will discount efficiencies likely to arise in the future – prudence will dictate using a range of conservative discount rates to perform a sensitivity analysis. The outcome of the overall trade-off could be highly dependent on the rate used to discount the efficiencies and the adverse "effects" against which the efficiencies will be weighed. If so, this will be another source of substantial uncertainty, as it will not be possible to accurately predict in advance the discount rate that will be used by the Bureau and the Tribunal.

- The price elasticity of demand that is likely to be used to calculate the price increase, output reduction and deadweight loss that the Bureau and the Tribunal may conclude are likely to result from the merger. Once again, it would be prudent to use a range of conservative elasticities, and the outcome of the overall trade-off could hinge on the elasticity that ultimately will be adopted.

- The firm elasticity of demand that is likely to be used to calculate the pre-existing market power exercised by the merging parties – business persons and their advisors are likely to find this step to be exceptionally difficult, if at all possible. (The experience in *Superior Propane/ICG* suggests that the additional deadweight loss, represented by area E in Appendix 1 hereto, that may be brought into the trade-off assessment after taking account of pre-existing market power could have an enormous impact on the over all assessment.)[70]

- How much of the wealth transfer is likely to be included in the trade-off assessment. As discussed earlier in this Part, this stage of the analysis is particularly complicated and highly dependent on subjective value judgments. In short, it involves:

  - making an initial assessment of the socio-economic profiles of the merged entity's customers and shareholders – this includes the profiles of the shareholders of business customers;

  - making judgments about whether the redistributive effects of the merger likely to be identified by the Bureau, and ultimately by the Tribunal, will be considered to be neutral, positive or adverse for each distinct income group of customers;

  - making value judgments about the weights that will be placed on such transfers;

  - making judgments about the extent to which alternative uses of the product by socially advantaged groups of customers are "essential", versus non-essential;[71] and

  - making judgments about the extent to which business customers can pass-on any part of the wealth transfer (i.e., price increase) and, if so, how that is likely to impact upon their downstream customers.[72]

- The weight that likely will be placed on the deadweight loss, relative to the weights placed on the socially adverse portions of the wealth transfer.[73]

- The balancing weight that would have to be given to the aggregate reduction in consumer surplus in order for it to equal the increased producer surplus that would result from the merger – as discussed above, this can be a useful tool in the overall analysis.

It is highly unlikely that business persons would fully understand all of the foregoing or, in any event, have any confidence in how the various elements of the current approach would be applied in the context of their particular transaction. As a result, it is difficult to believe that anyone would risk proceeding with any transaction that stands a reasonable chance of being found to be likely to prevent or lessen competition substantially, in reliance on the efficiency defence as currently interpreted by the Bureau, the Tribunal and the FCA.

Part V – The Total Surplus Approach

Unfortunately, the Advisory Panel does not appear to have been given a mandate to assess the total surplus approach, or indeed, any other specific approach to efficiencies in merger review.[74] Its only implicit reference to the total surplus approach is its statement that "the efficiency defence has had very little public policy relevance".[75]

The total surplus approach contemplates a trade-off of: (i) the efficiencies likely to be attained through a merger after applying the filters and adjustments described in the first six bullet points at the end of the preceding section; and (ii) the deadweight loss that likely will result from the merger, including any deadweight loss that may be related to the merged entity's pre-existing market power. No part of the wealth transfer is included in the trade-off assessment under the total surplus approach. As is well known, this is the approach that was described in the 1991 MEGs and applied by the Tribunal in its first decision in *Superior Propane ICG* (although pre-existing market power was not properly accounted for). Although it was embraced for approximately eleven years (1988-1999)[76] by the Bureau, the *Superior Propane/ICG* merger is the only one that was officially found to have met its requirements, albeit in a controversial decision.[77]

A principal reason why the section 96 defence played virtually no role in merger review during the first decade of its existence was that the evidentiary burden on the merging parties was set too high.[78] In addition, the likelihood of the Bureau referring to the Tribunal any case in which section 96 was invoked probably also had an impact, by exercising a chilling effect on business persons' willingness to pursue efficiency enhancing mergers that raised *prima facie* issues under section 92. This would have been particularly the case after the questions raised in *Hillsdown* regarding the total surplus approach.[79]

It is typically very difficult to prove, on the balance of probabilities, that efficiencies are more likely than not to be achieved. CEOs and other senior executives often pursue a merger on the basis of a high level assessment of, or even just a "gut feel" for, the cost savings and synergies likely to be achieved and of the "fit" between the two firms in question. They and their investment bankers seldom conduct the type of detailed analysis required to substantiate claims as being more probable than not before the Bureau and the Tribunal. As reflected in a recent report on the efficiencies that have been achieved from the acquisition of Famous Players Inc. by Cineplex Entertainment Ltd., sometimes the efficiencies that result from a merger substantially exceed projections made at the time of the merger.[80]

If a policy is intended to maximize total surplus, it is inappropriate to require that efficiencies be strictly proved, on the balance of probabilities, to be more probable than not. This is because: (i) efficiencies are ordinarily the

principal source of any increase in total surplus that may be brought about by a merger; (ii) they are inherently uncertain in nature, and, most importantly, (iii) over time they are likely to dwarf any static losses in consumer surplus that may result from the merger, particularly where the merger is likely to result in dynamic efficiencies. Accordingly, the more appropriate evidentiary burden for a policy intended to maximize total surplus would be something like the standard that has been adopted in New Zealand. There, all that has to be established (on the balance of probabilities) is "a tendency or real probability", rather than it being "more probable than not" that claimed public benefits will materialize.[81] The "reasonably likely" standard that appeared in section 100 of the Act prior to its amendment in 1999 would also serve this purpose, if it were made clear that this does not mean "more probable than not".[82]

By comparison, having to prove, on the balance of probabilities that claimed efficiencies are "more likely than not" to be achieved, would be an appropriate approach for a policy designed to maximize consumer surplus, because such a policy should be biased in favour of preventing mergers that would reduce consumer surplus.

Based on the foregoing, it is submitted that one modification which might help to give the total surplus approach more of a role than it played prior to its rejection by the FCA would be to replace the words "is likely to bring about" in section 96 with words such as "is reasonably likely to bring about", or "has a tendency or real probability to bring about". It would also be advisable to add a new provision in subsection 96(4) to make it clear that it is not necessary to establish that the gains in efficiency are more likely than not to be brought about.

Of course, to resurrect the total surplus approach, it would be necessary to address the FCA's interpretation of the words the "effects of any prevention or lessening of competition that will result or is likely to result from the merger,"[83] by further amending section 96 to make it clear that those words should be interpreted to exclude any portion of the wealth transfer or other effects not reflected in the deadweight loss.

As a practical matter, the modifications suggested above probably wouldn't give the total surplus approach much more of a role in merger review than it had prior to the FCA's rejection of that approach. McFetridge and Bian have calculated that, properly applied to address the FCA's misconception that the deadweight loss declines as elasticity decreases,[84] the total surplus approach "will be impossible to satisfy for the typical merger to monopoly or dominance with inelastic demand", and that the same is true in "tight oligopoly situations ... [involving] a three to two merger".[85] According to their calculations, it is only "in the case of four-to-three mergers that the total surplus approach becomes easier to satisfy" than the consumer surplus approach.[86] Given that challenges of four-to-three mergers are very rare in Canada, it appears that the scope for the total surplus approach to play a meaningful role in merger review is extremely limited. This would appear to be confirmed by experience.

Moreover, the prospects of the above-suggested amendments being made to section 96 cannot be considered to be high, particularly given (i) the support expressed for Bill C-249 by the Commissioner and the House of Commons,[87] and (ii) the absence of the total surplus approach from the possible options discussed in the Consultation Paper.[88]

Even if the Advisory Panel's views regarding transparency, predictability and efficiencies having a greater role to play in merger review were to have the surprising result of making the Commissioner and Parliament more receptive to the total surplus approach, experience suggests that the approach would not likely be sustainable. Not long after the Tribunal's Initial Decision, in which it permitted the merger of the last two significant suppliers of propane in Canada to proceed based on its "total surplus" interpretation of the efficiency defence, Bill C-248 was introduced to Parliament.[89] As is widely recognized, the amendment contemplated by that Bill would have written the defence out of the Act for all practical intents and purposes.[90] It is reasonable to expect that if section 96 were amended in the near future to resurrect the total surplus approach, politicians would react in a similar fashion the first time a high profile, publicly sensitive, anti-competitive merger were permitted to proceed on the basis of the amended section 96.[91]

Accordingly, it is better to take the present opportunity to develop an approach that is more politically sustainable than the total surplus approach, and that in any event is likely to have a more meaningful role in merger review than the total surplus approach had prior to its rejection by the FCA, or would likely have even if amended as suggested above.

Part VI – The Consumer Surplus and Price Standard Approaches

Since abandoning the total surplus approach in favour of the weighted surplus standard in the initial Tribunal hearing[92] and the lead-up thereto,[93] the Commissioner has advocated both the consumer surplus standard, as currently understood, and the price standard.[94]

A policy designed to maximize consumer surplus would not permit any merger to proceed if it is likely to result in any reduction in consumer surplus.[95] This condition would be met by what has become known as the price standard approach. Pursuant to that approach, which also is sometimes referred to as the consumer surplus approach,[96] to save an otherwise anti-competitive merger, efficiencies must be so great that the profit-maximizing level of output for the merged entity would correspond to a price that is at or below the pre-merger level. In other words, the efficiencies would have to "cleanse" the merger of its anti-competitive effects.[97] This is more or less the approach that has been embraced in the U.S.[98] and the E.U.[99] Any test, including the one contemplated by Bill C-249,[100] that would require efficiencies to be "passed on" to consumers would be a type of price standard approach.[101]

As the FCA recognized, the price standard "is the most difficult standard for the parties to a merger to satisfy".[102] This is confirmed by the U.S. experience, as almost no mergers in that jurisdiction have ever been found to meet this standard, although a very small number may have been permitted to proceed based on a somewhat less strict approach.[103] Given the substantially smaller number of mergers that occur in Canada and the disappointing experience with the substantially more lenient total surplus approach over the period 1988-1999, it is reasonable to expect that the prospects for the price standard to play any meaningful role in Canadian merger review are remote, at best.[104] Accordingly, notwithstanding its virtues, in terms of being very transparent and predictable, and perhaps having lower administration costs, its shortcomings are fatal if one is truly interested in an approach that would give a more meaningful role to efficiencies in merger review than they have had to date.

The same is true of what the Tribunal and the FCA have called the consumer surplus approach.[105] Pursuant to that approach, efficiencies can only save an anti-competitive merger if they outweigh the sum of the deadweight loss and the wealth transfer likely to result from the merger.[106] In contrast to the price standard, mergers leading to a price increase may be permitted, so long as the efficiency gains are greater than the loss in consumer surplus. As the Tribunal has observed, this standard also would be virtually impossible to satisfy, and would therefore "vitiate" section 96.[107] While the FCA recognized that this standard would be difficult to meet,[108] it did not expressly reject that standard on the basis that it would vitiate section 96, because there was no evidence on the record to support that conclusion. (However, in its second decision, the FCA appeared to uphold the Tribunal's rejection of the consumer surplus standard on the ground that it does not provide discretion to deal with the impact of a merger on different socio-economic groups of consumers and shareholders of the merged entity.)[109]

In any event, in the absence of any evidence, anecdotal or otherwise, to suggest that there has ever been a merger in Canada that would have satisfied the consumer surplus approach, it is reasonable to expect that this approach would not give efficiencies a meaningful role in merger review. Accordingly, notwithstanding that it might be more transparent, predictable and cost-effective than the current approach or the approach suggested in Part IX below, it should not be embraced.

Part VII – The Merger Outcomes Approach

One of the options offered for consideration in the Consultation Paper was what was described as the "Merger Outcomes" approach. Pursuant to that approach, section 96 would be amended to allow "the case to be re-opened" if "the predicted efficiencies were not achieved" by the merger in question.[110] To determine whether the efficiencies had been achieved, the Bureau would closely monitor the situation.

The two benefits of this approach identified in the Consultation Paper are that it would: (i) provide greater incentive to the merged entity to achieve the efficiencies; and (ii) perhaps make it easier for merging parties to convince the Bureau and/or the Tribunal to accept their efficiencies claims, because "the relevant decision maker ...[would have] the comfort of knowing that it will be able to assess the achievement of the projected efficiencies post-merger" [111] The Consultation Paper recognized that this "would create post-merger uncertainty for merging parties, who might not achieve their efficiencies for a whole host of reasons that were beyond the scope of contemplation at the time when they made their efficiencies" claims.[112] It further recognized that this approach would create a substantial administrative burden on the Bureau and/or the Tribunal due to the need to monitor mergers that had been permitted to proceed on the basis of claimed efficiencies.

An additional problem with this approach is that it may be very difficult to "unscramble the eggs" or to craft other effective relief in the event that the claimed efficiencies were not realized. Furthermore, it would be fundamentally unfair to allow for the possibility of re-opening a case on the basis that claimed efficiencies had not been achieved, when it would not be possible to re-visit the determination of whether the merger had actually prevented or lessened competition substantially. It would also be difficult to maintain fairness over time because, as a practical matter, the Commissioner likely would not re-open a case when the substantial majority of the

efficiencies had been achieved. Unfortunately, different Commissioners would have different views about the appropriate threshold for re-opening a case.

Most fundamentally, there is nothing in the Consultation Paper's discussion of this approach that addresses the appropriate standard to apply to efficiencies, for example, total surplus, weighted surplus, consumer surplus, price standard, etc. Accordingly, it would seem that this option, like the "Merger to Monopoly" option discussed in Part VIII below, would only be an add-on to a broader approach.

In any event, in aggregate, the other problems associated with the "Merger Outcomes" approach are such that it would likely be vigorously opposed by the business and legal communities. It is difficult to believe that business persons would be prepared to assume the considerable risk and uncertainty associated with proceeding with a merger that could be re-opened if projected efficiencies were not largely realized, unless they believed that they could integrate the merging firms' respective operations to the point that the Bureau would be left with no effective remedy. In other words, the only situation in which efficiencies may have a role to play in merger review under the Merger Outcomes approach is the situation in which the principal advantage of that approach would not be available.

Part VIII – Merger to Monopoly

In *Superior Propane/ICG*, the Commissioner took the position that, "as a matter of law ... section 96 does not apply in the circumstances of a merger-to-monopoly."[113] This position was rejected by the Tribunal in its Initial Decision on the ground that "[s]ection 96 does not make any distinction between the 'elimination' and the 'substantially lessening' of competition".[114] In its Redetermination Decision, the Tribunal observed that "the creation of monopoly is irrelevant to its task under the merger provisions of the Act".[115] The majority of the FCA concurred, in holding that "[i]f monopoly is to be taken into account for purposes of s. 96(1), it is the effects of the monopoly that must be considered, not the existence of monopoly *per se*" [116]

Shortly after the Tribunal's Initial Decision, Bill C-248 was introduced to Parliament. Among other things, it would have amended section 96 by adding a new provision that stated:[117]

> (5) This section does not apply where, after the transaction has been completed, the merger or proposed merger, will result or is likely to result in the creation or strengthening of a dominant position.

That Bill died on the order paper when Parliament was prorogued in September 2002. It subsequently came back as Bill C-249, which also died on the order paper (after being amended) following the dissolution of Parliament on May 23, 2004. When that Bill was being considered by the Standing Committee on Industry, Science and Technology, the then Commissioner proposed amendments to the Bill which would have prevented efficiencies from saving a merger where the merger would likely result in (i) "the elimination or near elimination of competition" or (ii) "an increase in prices of products of the merging parties from the prices that existed or would likely have existed before the merger or proposed merger".[118]

In the Consultation Paper, the option of retaining the current approach but adding "an explicit exception that would bar the successful application of the defence when a merger created a monopoly or near monopoly" was offered for consideration.[119] Although the Advisory Panel did not endorse any specific proposal, it stated that "it would be inappropriate to allow efficiency gains to justify a merger when competitive pressure was all but removed".[120] It added that it did not believe that the difficulties that many commentators had suggested would be associated with attempting to appropriately define "monopoly" would be insurmountable.[121] In this regard, it observed that "some of the competition law bills debated in the 1970s (C-42 and C-13, 1977) contained language that would have prevented the efficiency defence from applying in situations in which a merger would have led the merging parties to enjoy 'virtually complete control ... in respect of a product in a market'."[122]

What the Advisory Panel failed to recognize is that this wording is similar to the wording in the abuse of dominance provisions in paragraph 79(1)(a) of the Act, which apply to persons who "substantially or completely control, throughout Canada or any area thereof, a class or species of business".[123] The Bureau's *Enforcement Guidelines on the Abuse of Dominance Provisions* imply that firms with a market share as low as 35% may meet this test.[124] By contrast, in *Superior Propane/ICG*, the Tribunal defined monopoly as "an entity with a high degree of market power",[125] which would suggest a firm with a much higher market share.

In the U.S., "monopoly power", which must be demonstrated for the purposes of § 2 of the Sherman Act, is considered to connote the ability to "profitably raise prices substantially above the competitive level"[126] or "to control prices or exclude competition."[127] The jurisprudence suggests that firms with market shares in excess of 60-70% face realistic exposure to being found to have such power,[128] and there are cases in which firms with significantly lower market shares have been found to have such power.[129]

This experience confirms that any attempt to define monopoly in terms of the degree of market power held by a firm would likely capture firms with market shares far below 100%. Any such definition also would be subject to the Advisory Panel's criticism of the current test as one which "lacks basic predictability".[130]

Alternatively, defining monopoly as a firm having a particular share of the market would be very problematic for several reasons, including that any particular market share would be completely arbitrary and unlikely to find significant support. Those in favour of precluding the efficiency defence in cases involving merger to "monopoly" would not likely be satisfied with defining monopoly in terms of an entity having a market share of less than 100%. By contrast, the business and legal communities likely would fiercely oppose any definition below 80-85%. Any proposal to define a "monopoly" as an entity having a market share between 85% and 100% would be very difficult to defend on any principled basis.

More fundamentally, at a conceptual level, precluding the application of the efficiency defence in cases involving merger to "monopoly" would risk sacrificing efficiency enhancing mergers. The only possible legitimate reason for making such a sacrifice would be political in nature, namely, to prevent the type of political backlash that occurred in response to the Tribunal's Initial Decision in *Superior Propane/ICG* – or indeed an even greater backlash that could result in either a "political override" being inserted into the merger provisions of the Act, or proposals to amend the Act in undesirable ways.

As it turns out, at a practical level, an exception for mergers to monopoly is not needed because such mergers virtually never generate sufficient efficiencies to offset even the deadweight loss likely to result from the merger.[131]

In passing, it may also be noted that preventing the application of the efficiencies defence in cases involving merger to monopoly would be inconsistent with the spirit of subsection 92(2), which prevents the Tribunal from finding that "a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially solely on the basis of evidence of concentration or market share" [132] It also would be inconsistent with the Government's intention in 1985 when it proposed the amendments to the Act that included what is now section 96. After discussing the efficiencies defence and the substantial lessening test, the Guide that was released with those amendments stated: "Consequently, an appropriate merger law for Canada should focus on the economic effects stemming from the merger itself as opposed to establishing a minimum standard of competition remaining in a market after a merger has been completed" [133]

Part IX – An Alternative Approach

Based on the foregoing, it is highly unlikely that efficiencies are going to have any meaningful role in merger review unless an alternative approach that has not yet been tried or proposed in the Consultation Paper is adopted. To briefly recapitulate, as the Advisory Panel has found, the current (weighted surplus) approach is "not satisfactory", in part because it is "highly complex" and "lacking basic predictability" [134] It is also more difficult to meet than the more transparent, certain, predictable and objective total surplus approach that was employed from 1988 to 1999.[135] Given that the latter approach did not yield a meaningful role for efficiencies in the decade or so that it was employed, there is no reason to expect any more from the current approach. Indeed, there is every reason to believe the contrary. For the reasons explained above, the same is true for the other approaches that have been proposed.

An alternative approach that may have more potential to (i) give a more meaningful role to efficiencies and (ii) be politically sustainable, would be to abandon the quantitative focus that is inherent in the approaches discussed above, in favour of a qualitative orientation. The most obvious shortcoming associated with such a shift in focus is that it would offer less transparency, certainty and predictability than those other approaches. Given that those approaches have not given, or would not give, a meaningful role to efficiencies in merger review, this sacrifice would not have much practical downside. In short, it does not appear possible to achieve a meaningful and politically sustainable role for efficiencies while maintaining the degree of transparency, predictability and certainty afforded by the total surplus, consumer surplus, price standard and, to a lesser degree, the weighted surplus approaches.

A more qualitative and subjectively oriented approach that may respond to the principal shortcomings of the approaches discussed above would be to replace the current defence in section 96 with: (i) a defence that would prohibit the Tribunal from making an order in respect of a merger if it finds that the merger is reasonably likely to result in substantial dynamic efficiencies that would not likely be attained if the order that would be sought to address any prevention or lessening of competition likely to result from the merger were made; and (ii) an

exception to this defence where the merger would likely result in dynamic efficiency losses that would be clearly and substantially disproportionate to the dynamic efficiency gains likely to be brought about by the merger.[136] Quantitative efficiencies would only be relevant under this defence to the extent that they relate to dynamic efficiencies. However, they would also be relevant at the section 92 stage of the analysis.[137] In the interest of convergence, a second defence should be added to section 96 to prohibit the Tribunal from making an order where the efficiencies likely to result from a merger will ensure that prices will not be higher than they would have been in the absence of the merger. While it would be very surprising if this defence were ever met, inserting it into section 96 would ensure that any international merger allowed to proceed on this basis in the U.S. and the E.U. would be allowed to proceed in Canada, even if it was not likely to result in substantial dynamic efficiencies.

While being quite subjective in nature, this approach would appear to have a number of virtues. First, it would dispense with the complex calculations associated with the other approaches discussed above. Second, it would focus on dynamic gains and losses, which have far more potential than static gains and losses to impact upon economic welfare over the medium and long term. Third, it would give a more meaningful role to efficiencies for those mergers reasonably likely to result in substantial dynamic efficiencies. Upon a demonstration of a reasonable likelihood of such efficiencies being attained, the defence would be met, and no order could be made by the Tribunal unless the Commissioner demonstrated that the merger likely would result in dynamic efficiency losses that were clearly and substantially disproportionate to the dynamic efficiency gains. Thus, in "close" cases and other cases in which the Commissioner could not meet this significant burden, parties to mergers likely to result in substantial dynamic efficiencies would prevail. Fourth, there would be no need for a trade off assessment to be performed except where a merger is likely to result in very substantial losses in dynamic efficiencies. Fifth, the approach would be more politically sustainable than an approach which would allow a merger to proceed on the basis of the static gains likely to be achieved by the merging parties alone. This is because the Commissioner (if she did not refer the matter to the Tribunal) or the Tribunal would be able to defend the decision to allow the merger on the basis of substantial dynamic efficiencies with which consumers and politicians would be able to more easily identify than the "mere" static efficiencies that would accrue largely to the merging parties and their shareholders.

It bears emphasizing that as a practical matter, the discretion inherent in this alternative approach may not be materially greater than the discretion that exists under the current approach. While it is unlikely, given the significant uncertainty inherent in this approach, that merging parties would ever proceed with a merger that raises *prima facie* competition issues solely in reliance on efficiencies, this approach holds more potential than the other approaches discussed above to tip the balance in favour of proceeding with a merger where substantial dynamic efficiencies are likely to be achieved, particularly in "close" cases.

The following wording would achieve the proposed approach outlined above:

> Exception
>
> 96 (1) The Tribunal shall not make an order under section 92 if it finds that the merger has brought about or is reasonably likely to bring about substantial gains in dynamic efficiency that would not likely be attained if the order were made.

> (2) For the purposes of this section, the Tribunal shall not find that a merger is reasonably likely to bring about gains in efficiency described in subsection (1) by reason only of a redistribution of income between two or more persons.
>
> (3) Subsection (1) does not apply if the merger is likely to bring about losses in dynamic efficiency that are clearly and substantially disproportionate to the dynamic efficiencies likely to result from the merger.
>
> (4) The Tribunal shall not make an order under section 92 if it finds that the merger has brought about or is reasonably likely to bring about sufficient gains in efficiency to ensure that prices of the products in respect of which a substantial prevention or lessening of competition has occurred or is likely to occur will not be higher than they would have been in the absence of the merger.

Part X – Conclusion

Unfortunately, efficiencies have not played a meaningful role in merger review under the Act. It is hoped that the Advisory Panel's recognition of this reality will help to prompt much needed change.

At a minimum, regardless of the approach that ultimately is adopted, the evidentiary burden on the merging parties should be reduced. Instead of having to demonstrate (on the balance of probabilities) that cognizable efficiencies are likely to be achieved, merging parties should simply have to demonstrate (on the balance of probabilities) that efficiencies are reasonably likely to be achieved. It should be made clear in the Act that to establish a reasonable likelihood, all that must be demonstrated is a "substantial probability", rather than it being "more likely than not", that the claimed efficiencies will be achieved.

Given the unsatisfactory experience with the total surplus approach and the substantial shortcomings associated with the current (weighted surplus) approach, efficiencies are not likely to play a meaningful role in merger review unless a new approach is adopted. In any event, it does not appear to be realistic to expect that Parliament and the Bureau would support the total surplus approach, or that the total surplus approach would be politically sustainable even if they did support that approach after reflecting upon the Advisory Panel's findings and recommendations (e.g., regarding the shortcomings of the current approach and the desirability of a more transparent and predictable approach).

To the extent that other quantitatively-oriented approaches, such as the consumer surplus approach and the price standard, would be much more difficult to satisfy than either the total surplus approach or the weighted surplus approach, they have even less potential to give efficiencies a more meaningful role in merger review. The fact that the price standard approach is more or less the approach that is embraced in the U.S. and the E.U. is not a sufficient reason for adopting and relying solely upon that approach, if it will not help to achieve the paramount objective of giving efficiencies a more meaningful role in merger review.

Accordingly, it appears to be necessary to sacrifice some certainty and predictability – to the extent the current approach can be said to have either of those things, in order to give efficiencies a more meaningful role in merger

review. To achieve this objective, it is submitted that section 96 be amended to replace the current defence with: (i) a defence that would prohibit the Tribunal from making an order in respect of a merger if it finds that the merger is reasonably likely to result in substantial dynamic efficiencies that would not likely be attained if the order that would be sought to address any prevention or lessening of competition likely to result from the merger were made; and (ii) an exception to this defence where the merger would likely result in dynamic efficiency losses that would be clearly and substantially disproportionate to the dynamic efficiency gains likely to be brought about by the merger.

This article also recommends that:

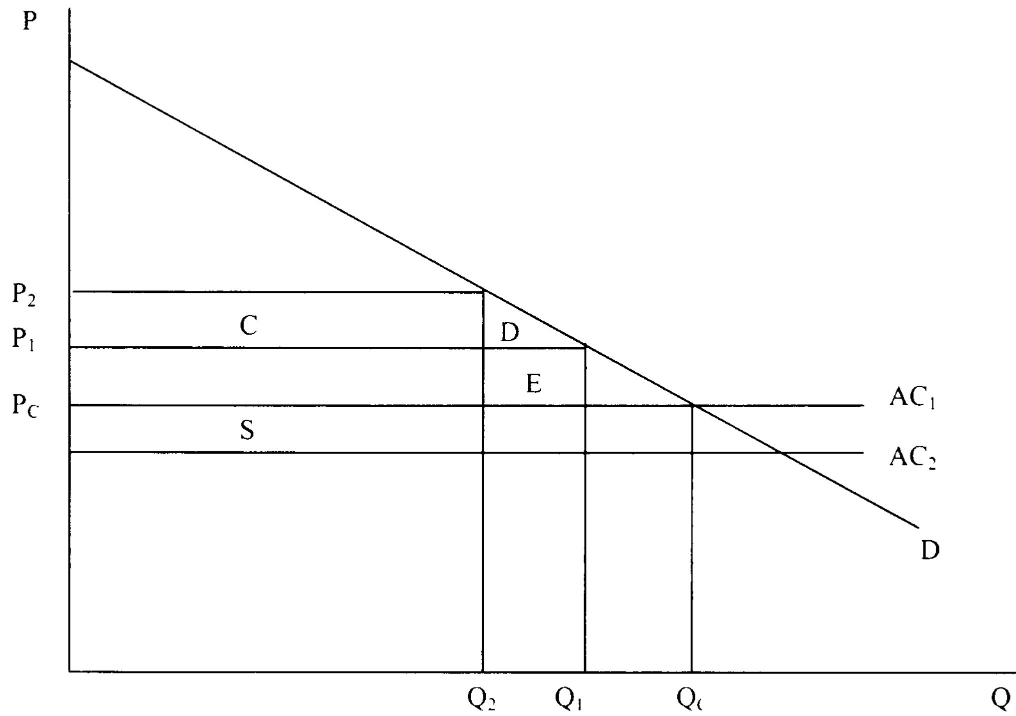
- section 93 be amended to make it clear that efficiencies should be considered in determining whether competition is likely to be prevented or lessened substantially (i.e., in determining whether the process of competition, as reflected in the extent to which current and potential competition are able to constrain the exercise of market power by a merged entity, is likely to be adversely impacted to a substantial degree – this recommendation is not intended to effect any change, but simply to clarify that efficiencies are relevant at the section 92 stage of the analysis);

- in the interest of convergence, a second defence should be inserted into section 96 to prohibit the Tribunal from making an order where the efficiencies likely to result from the merger will ensure that prices will not likely be higher than they would have been in the absence of the merger – (it would be surprising if this second defence were ever met – however, this would ensure that any merger allowed to proceed on this basis in the U.S. or E.U. would be allowed to proceed in Canada, even if it was not likely to result in substantial dynamic efficiencies);

- the Commissioner ought to make it clear that she will not routinely refer to the Tribunal cases in which the efficiencies defence is invoked; and

- the Advisory Panel's recommendation that the efficiencies defence not be available in cases involving merger to "monopoly" should be rejected.

APPENDIX 1



C = wealth transfer
D = dead weight loss
E = dead weight loss related to pre-existing market power
S = cost savings from the merger
P_1 = pre-merger price
Q_1 = pre-merger quantity
P_2 = post-merger price
Q_2 = post-merger quantity
Pc = competitive price
Qc = competitive quantity
AC_1 = average costs before the merger
AC_2 = average costs after the merger

Notes

* Partner, Osler, Hoskin & Harcourt LLP, Toronto. Comments received from Janet Bolton and Paul Winton are gratefully acknowledged.

1 See, for example, Consumer and Corporate Affairs Canada, *Competition Law Amendments: A Guide* (1985) at 17; Calvin S. Goldman, *Notes for an Address to the Grocery Products Manufacturers Association*, Toronto, October 2, 1986, at 2 (S-86-47); and Calvin S. Goldman, *Corporate Concentration and Canada's New Competition Act*, Notes for an Address to the National Conference on Mergers, Corporate Concentration, and Corporate Power in Canada, Montreal, March 24, 1987, at 5 and 13-15 (S-87-9).

2 (2000), 7 C.P.R. (4th) 385 (Comp. Trib.); *rev'd in part* (2001) 11 C.P.R. (4th) 289 (FCA); *redetermination*, (2002), 18 C.P.R. (4th) 417 at § 137 (Comp. Trib.); *aff'd*, (2003) 23 C.P.R. (4th) 316 (FCA).

3 This is confirmed by a former senior official who left the Bureau in 2004. See Richard Annan, *Submission on the Competition Act Consultations* at 2 (available at http://www.primestrategies.ca/bureau/submissions/Goodmans_LLP.pdf, and listed under "Goodmans").

4 Tom Ross and Ralph Winter, "Canadian Merger Policy Following Superior Propane", (2003) 21:3 Can. Comp. Rec. 7 at 20; and Margaret Sanderson, *Public Consultation on Treatment of Efficiencies in the Competition Act* (available at http://www.primestrategies.ca/bureau/index.html) at 7. See also Don McFetridge "Efficiencies Standards: Take Your Pick" (2002) 21:1 Can. Comp. Rec. at 55; and Frank Mathewson and Ralph Winter, "The Analysis of Efficiencies in Superior Propane: Correct Criterion Incorrectly Applied" (2000) 20:2 Can. Comp. Rec. 88 at 92.

5 See Calvin S. Goldman, *The Impact of the Competition Act of 1986*, Notes for an Address to the National Conference on the Centenary of Competition Law in Canada, Toronto, October 24, 1989 at 17 (S-10266): ("Cases in which efficiency gains played a role have included the acquisition by Fleetcher Challenge of B.C. Forest Products Limited; the acquisition of Freuhauf Canada Inc. by the Trailmobile Group of Companies Ltd; the acquisition by Dofasco Inc. of the Algoma Steel Corporation; and the recent acquisition by Consumers Packaging of Domglas where anticipated efficiency gains were confirmed by an independent expert to be in the order of $53.9 million a year.").

6 *Bill C-249, An Act to amend the Competition Act* (available at http://www.parl.gc.ca/37/3/parlbus/chambus/ house/bills/private/ C-249/C-249_3). That Bill was passed by the House of Commons on February 2, 2004, but died on the Order Paper in the Senate before the dissolution of Parliament on May 23, 2004. Before the Standing Committee on Industry, Science and Technology, the Commissioner of the day expressed strong support for the Bill. See Konrad von Finckenstein, *Bill C-249 An act to amend the Competition Act*, March 31, 2003 (available at http://cb-bc.gc.ca/epic/internet/incb.nsf/vwGenerated InterE/ct02543e.html). The current Commissioner subsequently appeared before the Standing Senate Committee on Banking, Trade and Commerce to express support for the Bill. See Sheridan Scott, *Bill C-249: An Act to amend the Competition Act* (available at http://competition.ic.gc.ca/epic/internet/incb-bc.nsf/en/ct2846e.html). See also *infra*, notes 20, 87, 89 and 117.

7 See, for example, Gwillym Allen, *Treatment of Efficiencies in Merger Analysis*, May 3, 1999 (available at http://www.competitionbureau.gc.ca/internet/index.cfm?itemID=882&lg=e) at 5 ("In these cases, the Bureau feels that it is more appropriate for the Competition Tribunal to determine whether the merger increases aggregate welfare or not"). This was not the first time a Bureau official had communicated this position.

8 The Report of the Advisory Panel on Efficiencies (August 2005), at 23-24, noted the "varying perceptions of the Bureau's willingness to consider efficiency claims in detail"; the fact that the Bureau's practice in this regard "seems to have changed over time"; and the fact that the situation is such that the business community is reluctant to make strong submissions on efficiencies. (Available online at http://www.competitionbureau.gc.ca/internet/index.cfm?itemID= 1954&lg=e.)

9 Allen, *supra* note 7 at 1 ("efficiencies only become relevant once a prevention or a substantial lessening of competition has been established").

10 *Commissioner of Competition v. Superior Propane et al.* (2002), 18 C.P.R. (4th) 417 at § 137 (Comp. Trib.).

11 Competition Bureau, *Treatment of Efficiencies in the Competition Act, Consultation Paper*, September 2004, at 33 (available at http://www.competitionbureau.gc.ca/internet/index.cfm?itemID=1602&lg=e).

12 *A Plan to Modernize Canada's Competition Regime* (April 2002), (available at http://www.parl.gc.ca/InfoComDoc/ 37/1/ INST/Studies/Reports/indurp06-e.htm) at Recommendation 28. In making this recommendation, the Committee took note of the fact that "[t]he Commissioner has not even once found the efficiency gains to a merger proposal sufficient to offset any lessening of substantial competition", and observed that the situation following the Tribunal's Redetermination Decision, *supra* note 10, is "confusing to say the least"

13 *Supra* note 8 at 5 and 24-25.

[14] *Ibid.* at 4-6 and 50-57.

[15] Director of Investigation and Research, *Merger Enforcement Guidelines* (1991), at part 5 (available online at http://www.competitionbureau.gc.ca/internet/index.cfm?itemID=1673&lg=e). In the interest of transparency, it should be disclosed that the author was the principal draftsperson of the MEGs and a strong advocate of the total surplus test. See generally, Paul Crampton, *Mergers and the Competition Act* (Carswell: 1990), at 520 *et seq.*, and Paul Crampton, "The Efficiency Exception for Mergers: An Assessment of Early Signals from the Competition Tribunal" (1992) 21 Can. Bus. L.J. 371.

[16] *Supra* note 8.

[17] *Supra* note 8 at 50 and 51.

[18] *Supra* note 8 at 54.

[19] It is recognized that an approach that virtually vitiates the defence could be politically sustainable.

[20] Bill C-248, which became Bill C-249, was introduced for first reading on February 7, 2001, shortly after the release of the Initial Decision in *Superior Propane/ICG, infra*, note 43. As initially proposed, it would have precluded the defence in section 96(1) from being satisfied "unless the majority of the benefits derived or to be derived from such gains in efficiency are being or are likely to be passed on to customers within a reasonable period of time in the form of lower prices". Bill C-248 also would have precluded the defence "where, after the transaction has been completed, the merger or proposed merger, will result or is likely to result in the creation or strengthening of a dominant market position". As passed by the House of Commons on February 2, 2004, Bill C-249, *supra* note 6, would have repealed the efficiencies defence in section 96 and made efficiencies a factor to be considered along with other factors in section 93, in determining whether a merger is likely to prevent or lessen competition substantially.

[21] Von Finckenstein, *supra* note 6 at 3.

[22] This was recognized by the Tribunal in its Redetermination Decision, *supra* note 10 at § 142. The Tribunal then observed: "Given the size of the American economy and the historic purpose of American antitrust laws, it is not surprising that the potential for losing scale economies was not a significant concern…" *Ibid.*

[23] *Supra* note 8 at 52.

[24] Consultation Paper, *supra* note 11 at 33.

[25] *Ibid.*

[26] Redetermination Decision, *supra* note 10 at § 88. The Tribunal distinguishes this from a "pure Price Standard", pursuant to which "a merger can only be approved if it does not lead to an increase in market power". *Ibid.*

[27] See generally P. Crampton (1990), *supra* note 15.

[28] Redetermination Decision, *supra* note 10 at §§ 114-129.

[29] *Ibid.* at § 136.

[30] See Sanderson, *supra* note 4. See also Advisory Panel Report, *supra* note 8 at 33-34. For a more detailed discussion of the differences in how efficiencies should be treated under alternative approaches, see Paul Crampton, "Alternative Approaches to Competition Law – Consumers' Surplus, Total Surplus, Total Welfare and Non-Efficiency Goals" (1994) 17 World Competition 55.

[31] Redetermination Decision, *supra* note 10 at § 137.

[32] Cf. *Department of Justice and Federal Trade Commission Horizontal Merger Guidelines* ("U.S. Horizontal Merger Guidelines") at Section 4 (available at http://www.usdoj.gov/atr/public/guidelines/horiz_book/4.html). In fairness to the Bureau, the Advisory Panel's Report recognized that "[t]he Bureau does take efficiency claims into account when assessing the motives for a merger, and efficiencies may be one of a number of factors that the Bureau considers when deciding not to challenge a merger in a close case" *Supra* note 8 at 24. In the author's experience, the Bureau has also generally considered the extent to which efficiencies are likely to lead to the types of pro-competitive results mentioned above. This experience is shared by other practitioners. See National Competition Law Section, Canadian Bar Association, *Treatment of Efficiencies in the Competition Act*, December 2004, at 9 (available online at http://www.prime strategies.ca/bureau/index.htm).

[33] *Supra* note 8 at 54 and 57.

[34] *Ibid.* at 54.

[35] Thomas W. Ross, *Efficiencies in Merger Review and Other Matters under the Competition Act, Submission to the Consultations on the Treatment of Efficiencies under the Competition Act being conducted by the Intersol Group*, December 20, 2004, at § 44 (available at http://www.primestrategies.ca/bureau/submissions/Ross_Submission.pdf).

[36] *Commissioner of Competition v. Superior Propane Inc.* (2001), 11 C.P.R. (4th) 289, at § 140 (FCA).

[37] *Ibid.*

[38] *Supra* note 10 at § 338

[39] *Commissioner of Competition v. Superior Propane Inc. et al.*, (2003) 23 C.P.R. (4th) 316 at § 63 (FCA); and *Competition Bureau, Merger Enforcement Guidelines* (2004), at § 8.26 (available at http: www.competitionbureau.gc.ca internet index. cfm?itemID=1245&lg=e).
[40] *Ibid.* at § 8.27.
[41] *Supra* note 4 at 9.
[42] *Supra* note 15.
[43] *Commissioner of Competition v. Superior Propane Inc. et al.*, (2000) 7 C.P.R. (4th) 385 at § 20 *et seq* (Comp. Trib.).
[44] The Tribunal has recognized that the wealth transfer, or part of it, can in some cases have socially positive income effects, such as where the product is a luxury item purchased by wealthy buyers and sold by a producer the shareholders of which are "less wealthy than the buyers". Redetermination Decision, *supra* note 10 at § 331.
[45] Examples of such redistributive gains include gains solely attributable to increased buying power, most types of tax savings, and savings that flow from a reduction in output, service, quality or variety. See generally § 8.17 of the 2004 MEGs, *supra* note 39 This topic is dealt with in greater detail in the 1991 MEGs, *supra* note 15 at § 5.3.
[46] Redetermination Decision, *supra* note 10 at § 194-198. Although the Tribunal was focusing on redistributions to foreigners (in the form of part of the wealth transfer), it can be taken to have implied that efficiency gains flowing outside the country also should be excluded from the balancing process. *Cf.* Crampton (1990), *supra* note 15 at 531-532, where this point is discussed in greater detail.
[47] Redetermination Decision, *supra* note 10 at §§ 165-169.
[48] See Mathewson & Winter, *supra* note 4 at 91; and Margaret Sanderson, "Competition Tribunal's Redetermination Decision in *Superior Propane*: Continued Lessons on the Value of the Total Surplus Standard", (2002) 21:1 Can. Comp. Rec. 1 at 4.
[49] *Supra* note 36 at §§ 109 and 139-141; Redetermination Decision, *supra* note 10 at § 325.
[50] Redetermination Decision, *supra* note 10 at § 329.
[51] *Ibid.*
[52] *Ibid.*
[53] *Ibid.* at § 333. Earlier in its decision, the Tribunal accepted the following definition of socially adverse suggested by Professor Townley: "If shareholders are uniformly better off than consumers, then the redistribution of income arising from the merger may be unfair to the less well-off group, and hence be socially adverse" The Tribunal then observed that "if the consumer and shareholder groups were each characterized by variability of income and wealth of their members, it might be difficult to characterize the redistribution of income arising from a merger as being unfair to one group or the other." *Ibid.* at § 100.
[54] See the Affidavit of Peter G.C. Townley, submitted in *Commissioner of Competition v. Superior Propane Inc.* et al., at 33 (available at http://www.ct-tc.gc.ca/english/CaseDetails.asp?x=68&CaseID=202#274).
[55] See the Redetermination Decision, *supra* note 10 at §§ 102-104. It is not clear why the Tribunal did not include in this calculation the further $3 million that it estimated to represent the qualitative anti-competitive effects of the merger.
[56] *Supra* note 36 at § 23. This is discussed in greater detail in Roger Ware, "Is Competition Economics 'Beyond the Ken of Judges'? The Federal Court of Appeal Ruling in Superior Propane" (2001) 20:3 Can. Comp. Rec. 1 at 5-6.
[57] *Ibid.* at § 108.
[58] *Ibid.* at § 112.
[59] *Ibid.* at § 337.
[60] *Supra* note 4 at 20. Note also that the Tribunal observed that "demonstrating significant adverse redistributional effects in merger review will, in most instances, not be an easy task". *Supra* note 10 at § 372.
[61] *Supra* note 10 at § 356.
[62] *Ibid.* at §§ 353 and 368.
[63] *Ibid.* at §§ 368-371.
[64] *Ibid.* at § 371.
[65] *Supra* note 39 at § 60-64.
[66] *Supra* note 8 at 23.
[67] The typical analysis usually winds up being much more complicated than suggested by the following points.
[68] Note that in *Superior Propane/ICG*, the Commissioner submitted that only $21.2 million of the $38.51 million claimed annual savings should be accepted. Ultimately, the Tribunal accepted $29.2 million. See *supra* note 43 at §§ 326 and 383.
[69] Redetermination Decision, *supra* note 10 at §§ 194-198. Cf. note 46 above.
[70] Mathewson and Winter calculated that had pre-existing market power been properly accounted for in that case the deadweight loss would have been approximately 8.5 times the value reported by the Commissioner's expert. *Supra* note 4 at 91. The $3

million in quantifiable deadweight loss that was recognized in that case was predicated on an average price increase of 8%. The estimates of additional deadweight loss associated with pre-existing market power that the Commissioner unsuccessfully attempted to introduce in final argument ranged from $23.44 million (calculated on an assumed price increase of 4%) to $54.89 million (calculated on an assumed price increase of 9%). Redetermination Decision, *supra* note 10 at §§ 167-168. By comparison, the accepted efficiencies in that case amounted to $29.2 million.

71 As discussed above, the Tribunal appears to have suggested that only expenditures for essential purposes should be included in the assessment. *Supra* note 10 at §§ 352-357 and 368.

72 In its Redetermination Decision, the Tribunal spent a significant amount of time assessing this issue but ultimately was unable to arrive at any particular conclusion. What cannot be ignored is its observation that "[h]ow the burden of the price increase is ultimately shared across business owners in interrelated markets and by households is an important question" *Supra* note 10 at § 362.

73 As mentioned above, in its Redetermination Decision the Tribunal observed that there is no statutory basis for assuming equal weighting for redistributive effects and the deadweight loss, and suggested that, "since efficiency concerns are paramount in merger review, perhaps adverse redistributive effects should be weighted half as much as dead weight losses" *Supra* note 10 at § 371.

74 *Supra* note 8 at 7-8.

75 *Ibid.* at 25.

76 Cf. Calvin S. Goldman, *Mergers Efficiency and the Competition Act*, Notes for an address to the Commercial and Consumer Law Workshop, Faculty of Law, McGill University, October 15, 1988 (S-10170), (confirming use of the total surplus approach as far back as 1988); Allen, *supra* note 7 (revealing a shift away from this approach in 1999); and Gwillym Allen, *The Enforcement of the Efficiency Exception in Canadian Merger Cases, Speaking notes for a meeting with the Competition Law Group, Stikeman Elliott, Toronto, June 5, 1999* (available at http://www.competitionbureau.gc.ca/internet/index.cfm?itemID=888&lg=e). In an electronic *Information Notice* dated May 16, 2001, the Bureau ultimately announced that the approach set forth in Part 5 of the MEGs "no longer applies"

77 *Supra* note 43. Cf. *supra* note 2 for the cites to subsequent decisions of the FCA and the Tribunal in this matter; and *supra* note 4 for some of the commentary that the decision generated.

78 See Paul Crampton, "The Treatment of Efficiency Gains in Canadian Merger Analysis", in OECD, *Competition Policy and Efficiency Claims in Horizontal Agreements*, (1996), OCDE/GD(96)5, at 59 (available online at http://www.oecd.org/document/38/0,2340,en_2649_34685_2474918_1_1_1_1,00.html).

79 *Canada (Director of Investigation and Research v. Hillsdown Holdings (Canada) Ltd.* (1992), 41 C.P.R. (3d) 289 at 337 *et seq* (Comp. Trib.).

80 See Shirley Won, "Cineplex Sees More Savings from Merger", *The Globe and Mail*, Thursday, April 13, 2006, at B7 (discussing how efficiencies initially projected to be approximately $20 million at the time of the merger were now being projected to $30 million).

81 *Re Weddel Crown Corporation Ltd. and Ors* (1987), 1 NZBLC 104,200 at 104,213 (Com). More recently, the High Court of New Zealand observed, in *Air New Zealand And Anor v. Commerce Commission and Ors*, HC AK CIV 2003 404 6590 [17 September 2004], at § 36:

> "The public benefit test also requires an examination of likely results. In this context, likely refers to probable outcomes rather than possible or speculative effects: Air New Zealand v. Commerce Commission [1985] 2 NZLR 338, 341-342 citing Re Queensland Cooperative Milling Association Limited v Defiance Holdings (1976) 1 ATPR para 40-012,p 17, 223 at p 17,243. The degree of probability is:
>
> > '... above mere possibility but not so high as more likely than not and is best expressed as a real and substantial risk that the stated consequence will happen.'
> >
> > Port Nelson Limited v Commerce Commission [1996] 3 NZLR 554 at 562 (CA)"

See also *Fisher and Paykel Ltd. v. Commerce Commission*, [1990] 2 NZLR 731 at 767 (H.Ct.).

82 Unfortunately, the words "reasonably likely" were not the subject of material discussion by the Tribunal and the Federal Court of Appeal before they were removed from section 100. In *Canada (Director of Investigation and Research v. Superior Propane Inc.* (1998), 85 C.P.R. (3d) 192 (Comp. Trib.) the Tribunal (per Rothstein J.) simply noted that the Commissioner's burden "is less than applicable after a full hearing of an application under section 92, but higher than that required under section 104" In this latter regard, the Tribunal observed: "It is insufficient for the Tribunal to simply be satisfied that there is a serious issue or that the matter is not frivolous or vexatious as in the case of ordinary interlocutory or injunctive relief..."

[83] *Supra* note 36 at §§ 92 and 139-141.
[84] *Ibid.* at §§ 103-106. This "elasticity gaffe" is also discussed in the various articles cited at note 4 above, and in the Tribunal's Redetermination Decision, *supra* note 10 at §§ 394-398.
[85] *Supra* note 4 at 47-48.
[86] *Ibid.* at 48-49.
[87] Bill C-249 was passed by a majority vote of 175 to 29 on February 2, 2004, before dying on the order paper in the Senate. See also *supra* note 6.
[88] *Supra* note 11 at Part 2.
[89] Cf, *supra* note 6. Bill C-248 which received First Reading on February 7, 2001 and Second Reading on February 25, 2002, was reintroduced as C-249 on October 25, 2002, after Parliament was prorogued on September 18, 2002.
[90] See *supra* note 20.
[91] The adverse reactions of the some members of the Tribunal (in *Hillsdown* and *Superior Propane ICG*) and of the FCA to the total surplus approach are a further indication that this approach does not resonate widely with people outside the competition law community.
[92] See Initial Decision, *supra* note 43 at § 420.
[93] See Allen, *supra* note 7 at 3-5 (discussing the Compensating Variation and Equivalent Variation tests); and Allen, *supra* note 76 at 3 (describing the circumstances in which "the Bureau would attempt to determine whether the anti-competitive effects include adverse distributional effects") (available at http://www.competitionbureau.gc.ca/ internet/index.cfm? itemID=888&lg=e). In an electronic Information Notice dated May 16, 2001, the Bureau then announced that the approach set forth in Part 5 of the MEGs "no longer applies".) See also *supra* note 76.
[94] See the Redetermination Decision, *supra* note 10 at §§ 307 and 335; and *supra* note 6 (regarding the Commissioner's support for Bill C-249).
[95] See Crampton, *supra* note 30 at 85-86.
[96] See, for example, the Consultation Paper, *supra* note 11 at 46.
[97] In its Redetermination Decision, the Tribunal distinguished between a "pure" price standard, which it suggested would not permit a merger to proceed if it were likely to lead to any increase in market power, and a "modified" price standard, which is what is described in the preceding paragraph. *Supra* note 10 at §§ 86-89. The "pure" approach therefore would not assist parties to any merger likely to prevent or lessen competition substantially. The approach discussed below is what the Tribunal characterized as the modified price standard.
[98] See, for example, the U.S. *Horizontal Merger Guidelines*, *supra* note 32, at Part 4; William Kolasky and Andrew Dick, "The Merger Guidelines and the Integration of Efficiencies into Antitrust Review of Horizontal Mergers" (2003) 71 Antitrust L.J. 207; the Redetermination Decision, *supra* note 10 at § 1.4 *et seq.*; and the Advisory Panel's Report, *supra* note 8 at 45.
[99] See, for example, the Advisory Panel's Report, *supra* note 8 at 45.
[100] See also *supra* notes 6 and 20, and the discussion in Part III above.
[101] Indeed, if the efficiencies had to be passed on in the form of <u>lower</u> prices, the approach would be more strict than the price standard approach. Cf, *supra* note 97.
[102] *Supra* note 36 at § 21.
[103] See Kolasky and Dick, *supra* note 98 at 232-235; and United States Federal Trade Commission and United States Department of Justice, *Commentary on the Horizontal Merger Guidelines*, March 27, 2006 at 55 – 59 (available at http://www.ftc.gov/bc/ bcmergacq.htm). As noted in Part III above, part of the reason why this approach is so difficult to meet is that it virtually ignores savings in fixed costs.
[104] Cf. discussion in Part III above.
[105] See *supra* note 36 at § 22; and the Tribunal's Redetermination Decision, *supra* note 10 at §§ 90-94. In its Initial Decision, the Tribunal characterized the consumer surplus standard in terms similar to those used above to describe the price standard. See *supra* note 43 at § 428.
[106] Redetermination Decision, *supra* note 10 at §§ 90-94.
[107] *Ibid.* at §§ 187 and 214-215. See also Crampton, *supra* note 15 at 386.
[108] *Supra* note 36 at § 22.
[109] *Supra* note 39 at §§ 32 and 62.
[110] *Supra* note 11 at 35.
[111] *Ibid.* at 35-36.
[112] *Ibid.*

[113] *Supra* note 43 at § 414.
[114] *Ibid.* at § 419.
[115] *Supra* note 10 at § 272.
[116] *Supra* note 39 at § 49.
[117] House of Commons of Canada, *Bill C-248*, First Session, Thirty-seventh Parliament, 49-50 Elizabeth II, 2001 (First Reading, February 7, 2001). *Cf. supra* note 89.
[118] Von Finckenstein, *supra* note 6 at 4-5.
[119] *Supra* note 11 at 34.
[120] *Supra* note 8 at 55.
[121] *Ibid.* at 55-56.
[122] *Ibid.* at 56.
[123] This wording was taken from section 2 of the former *Combines Investigation Act*, R.S., c.C-23.
[124] Competition Bureau, *Enforcement Guidelines on the Abuse of Dominance Provisions*, July 2001, at 15.
[125] Redetermination Decision, *supra* note 10 at § 281.
[126] *United States v. Microsoft Corporation*, 253 F. 3d 34, 51 (D.C. Cir. 2001).
[127] *United States v. Grinnell Corp.*, 384 U.S. 563 at 571. Others have suggested that "the pivotal inquiry is almost always whether the challenged party has substantial market power in its relevant market." Robert Pitofsky, *New Definitions of Relevant Market and the Assault on Antitrust* 90 Colum. L. Rev. 1805, 1807 (1990).
[128] R. Hewitt Pate, *The Common Law Approach and Improving Standards for Analyzing Single Firm Conduct*, Address Before the Thirtieth Annual Conference on International Antitrust Law and Policy, Fordham Corporate Law Institute, New York, New York, October 23, 2003, at 7 available at http://www.usdoj.gov/atr/public speeches 202724.htm. However, in *United States v. Dentsply International Inc.*, 399 F. 3d 181 at 187 (3rd Cir. 2005) it was observed that "a share significantly larger than 55% has been required to establish prima facie market power."
[129] See Brian Facey and Dany Assaf, "Monopolization and Abuse of Dominance in Canada, the United States, and the European Union: A Survey" (2002) 71 Antitrust L.J. 513, 537 n. 100.
[130] *Supra* note 8 at 57.
[131] See McFetridge, *supra* note 4 at 47; and Peter G.C. Townley, *The Treatment of Efficiencies in the Competition Act: Response to the Commissioner of Competition's Consultation Paper* (December 2004) at 13 (available at http://www.primestrategies.ca/bureau/submissions.htm). See also Ross, *supra* note 35 at § 73, and Lay Member Schwartz's concurring opinion in the Tribunal's Redetermination Decision, *supra* note 10 at §§ 393-397.
[132] R.S., 1985, c. C-34, s.92(2).
[133] *Supra* note 1 at 16.
[134] *Supra* note 8 at 5, 54 and 57, respectively.
[135] *Supra* note 76.
[136] This is a modification of an approach suggested in 2001. See Paul Crampton "Beyond Bill C-23: A Competition Law for the New Millennium" [2002] 36 Can. Bus. L.J. 161.
[137] If a two-track approach to horizontal agreements ultimately is adopted, there is no reason why this approach could not be used in the new civil provision. (There arguably would be no need for section 86 – the provisions dealing with specialization agreements.)

EFFICIENCIES ANALYSIS IN CANADIAN MERGER REVIEW: A CASE FOR LEAVING THINGS BE

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Since the Competition Tribunal's original decision and its Redetermination decision in *Superior Propane*,[1] we have collectively engaged in near-continual debate on how best to treat efficiencies in merger review. We have proposed amendments,[2] held cross-country consultations,[3] published a report on international treatment,[4] constituted an Advisory Panel[5] and, remarkably, since critics claim this is impossible to do, continued to review mergers without mishap.

Commentators appear to agree that efficiency is an important policy objective, which should be considered in merger review. This is in fact what exists today. While other authors in this issue advocate reform in order to achieve the proper place for efficiencies in merger review, this article advocates maintaining the *status quo*. I have come to this position not through any tremendous affinity for the balancing weights approach (or weighted surplus approach).[6] Rather, this position is the result of adopting the medical dictum "first do no harm" to policy development. The current situation is not perfect but it is much better than the alternatives that have been proposed. The current situation is one in which the total surplus rule will be a correct guide in all but the rarest cases.

In support of this position, this article describes the alternatives that have been proposed, and for each alternative discusses the potential problems relative to the *status quo*. The three alternatives noted in the consultation process and also the proposal that Paul Crampton discusses in his article in this issue of the *Record* are considered. For purposes of comparison, the next section very briefly describes what we have in place today.

What Do We Have Today?

To start, the law is the same law that has been on the books since 1986. Mergers that are likely to substantially lessen or prevent competition will not be allowed to proceed except if they are likely to bring about gains in efficiency that will be greater than, and will offset, the anticompetitive effects of the merger and such gains in efficiency would not likely be attained if the order sought before the Competition Tribunal were made. Efficiency gains must be real savings in resources, as opposed to redistributions of income between two or more persons, to be considered. In applying the trade-off analysis embodied in section 96 of the *Competition Act*, the Tribunal shall consider whether the efficiency gains will result in a significant increase in the real value of exports or a significant substitution of domestic products for imported goods.

Under the current framework, the Competition Bureau considers variable and fixed cost savings[7] stemming from economies of scale, economies of scope and economies of density, and savings that flow from specialization, the elimination of duplication and the avoidance of capital expenditures that would otherwise have been required.[8] As well, the Bureau considers savings that arise from plant specialization, rationalization of administrative and management functions, and savings relating to distribution, advertising and raising capital.[9] The Bureau also recognizes dynamic efficiency claims, notwithstanding the difficulty in measuring these.[10] This is all good economic policy.

The anti-competitive effects described in the *Merger Enforcement Guidelines* ("MEGs") encompass the deadweight loss, redistributive effects and non-price effects related to reduced service, quality, choice and any loss in productive and dynamic efficiency. The non-price effects will be considered from a qualitative, rather than a quantitative, perspective.

In terms of the trade-off analysis itself, the legal test in Canada today is the one established by the Competition Tribunal in the *Superior Propane Redetermination Decision*. The only part of the Tribunal's original decision in *Superior Propane* that was altered in the *Redetermination Decision* was added consideration to the redistributional effects arising from any anticompetitive merger. Thus, the jurisprudence established by the Tribunal in the original decision in respect of burden of proof[11] and whether certain cost savings may be considered efficiencies under the Act continues to hold. As well, the Tribunal's rejection of the Commissioner's position that section 96 does not apply to a merger to monopoly holds. Section 96 applies as much today to mergers to monopoly as it did prior to the *Superior Propane* case. (As explained below, this is not problematic.)

In the *Redetermination Decision*, the Tribunal rejected the Commissioner's submissions that all of the redistributive effects of the merger should be considered part of the anticompetitive effects arising from the transaction.[12] This was upheld on appeal. As a result, we do not have a consumer surplus standard. The Federal Court of Appeal directed the Tribunal to consider all of the "effects" of the lessening or prevention of competition in light of the statutory purpose of the Act, but it did not specify a trade-off framework. In so doing, the Tribunal adopted the balancing weights standard advocated by the Commissioner in the original hearing. Alternatively, this may be thought of as a relative weights standard, where different weights are assigned to consumer and producer surplus as opposed to the equal weights to each that are embodied in a total surplus standard. The balancing weights approach involves calculating the minimum weight on consumer surplus (relative to the weight assigned to producer surplus) that would be needed to find the merger unacceptable. Having calculated this value, the Tribunal would then ask whether the socio-economic circumstances support weighting consumer surplus (relative to producer surplus) at this minimum weight or higher. If yes, then the anticompetitive effects of the transaction will outweigh the efficiencies and a Tribunal order will be issued.

Generally, the Tribunal noted that:

> [R]edistributional effects can legitimately be considered neutral in some instances, but not in others. Fairness and equity require complete data on socio-economic profiles on consumers and shareholders of producers to know whether the redistributive effects are socially neutral, positive or adverse. While complete data may never be attainable, the Tribunal must be able to establish on the evidence the socially adverse effects of the transfer.[13]

Ultimately, the Tribunal examined the extent to which there were more low-income consumers of propane than high-income consumers. Yet, most propane is used by businesses as an intermediate input to their production process. The Tribunal noted that it would need to know the pass-on effects as well as the income distribution of those along the chain of distribution to properly determine the potential adverse effects of the transaction. With no information on the record in this regard, the Tribunal treated the intermediate purchasers – including small and medium-sized business owners and family-owned agricultural operations – as equivalent to the producers. Thus,

the transfer between these groups was not included in the estimated socially adverse effects of the merger.

As demonstrated in an article by Tom Ross and Ralph Winter,[14] the circumstances under which the Tribunal's approach to relative weights in *Superior Propane* would materially deviate from the total surplus standard are likely to be very rare. This is because the Tribunal did not say that it would automatically weight any consumer with less wealth than shareholders more favourably. Instead, the Tribunal indicated that it would only grant additional weight to those consumers who are "poor or needy" When applying this standard, the Tribunal focused on the consumption of bottled propane by the lowest-income quintile of consumers,[15] finding that while the redistributive effects of the merger on these households was likely to be socially adverse, the number of such households is quite small.[16] Importantly, the Tribunal found that the interests of other households and business owners should be weighted equally with shareholders of the merged firm in this case.[17]

Superior Propane is not unusual in this regard. In mergers where consumers are drawn from across the income distribution, Ross and Winter show that even if the weight on income to poor consumers were 50% greater than that on other consumers and producers, the weight on consumer surplus as a whole would only be 10% greater than that on producers.[18] Ross and Winter conclude from their calculations that:

> the balancing weights approach to implementing the weighted surplus standard would lead to the acceptance of virtually as many typical mergers – that is mergers in markets with average income elasticities of demand – as the total surplus rule.[19]

As a result, the current approach – the *status quo* – is very close to the total surplus rule in practice, but allows for rare exceptions when there are large detrimental impacts on the distribution of wealth that would overwhelm the efficiency effects.[20] As noted by Ross and Winter, the *status quo* is also the principled approach to take, given economic theory.[21]

What Could We Have Instead?

While many competition specialists endorsed the total surplus standard, there is little support for the balancing weights approach.[22] This may be due to a lack of understanding, as it is astonishing that so many prior supporters of the total surplus standard are willing to abandon the *status quo* given how close it is to a total surplus standard. The current approach could hardly be closer to a total surplus standard. The guidance that is provided to counsel is clear: assume the use of total surplus unless there is something very unusual about the merger in that the merging parties' customers are primarily drawn from very low income groups. So if your clients are slum landlords who are going to merge and double prices with cost efficiencies that are modest and would be barely sufficient under the total surplus criterion, then you are unlikely to win a contested Tribunal case.[23] Otherwise, if the merging firms sell intermediate goods to other businesses or sell final goods to a broad cross-section of consumers, the *status quo* will be essentially a total surplus standard.

Three alternatives to the *status quo* were proposed during the consultation process. These are:

1. *Section 93 Factor Approach*, which would involve eliminating section 96 and making efficiencies a factor to be considered in the context of determining whether a merger leads to a substantial lessening of

competition. A variation on the factor approach would limit the efficiencies recognized under section 93 to those passed on in some form to customers, which would lead enforcement authorities to discount or ignore efficiencies that do not produce short-term benefits for customers, such as fixed cost savings.

2. *Merger to Monopoly*, which would retain section 96 but add an explicit exception that would bar the successful application of the defence when a merger created a monopoly or near-monopoly. A variation on this option would give expanded remedial powers to the Tribunal in the case of a merger to monopoly, thereby allowing the Tribunal to impose conditions or other remedies sufficient to address concerns about the monopoly market conditions. It is unclear what these remedies might entail.

3. *Merger Outcomes*, which would involve amending section 96 to allow the Tribunal to re-open a case if the efficiencies realized were significantly less than predicted.

In addition to these three proposals, Paul Crampton is proposing more radical reform. He advocates abandoning the "quantitative focus" that is inherent in the approaches described above (and the *status quo*) in favour of a qualitative analysis that would have efficiencies considered as both a factor and a defence. Under this scheme (the *Crampton Proposal*), the following changes would be made:

(a) section 93 would be amended to indicate that efficiencies should be considered in determining whether competition is likely to be prevented or lessened substantially,

(b) section 96 would be amended to remove the trade-off analysis and instead the merger would be allowed to proceed if it brought about or is reasonably likely to bring about substantial gains in dynamic efficiency that would not likely be attained if the order were made unless the merger would likely result in dynamic efficiency losses that would be clearly and substantially disproportionate to the dynamic efficiency gains likely to be brought about by the merger; and,

(c) section 96 would have an additional defence added to it that prohibits the Tribunal from making an order where the efficiencies likely to result from the merger will ensure that prices will not likely be significantly higher than they would have been in the absence of the merger.

In what follows, each proposal is dealt with in turn. With each, whether there are any net benefits to be achieved relative to the *status quo* is discussed.

Section 93 Factor Approach

A *Section 93 Factor Approach* to efficiencies would have efficiencies considered as part of the substantial lessening of competition analysis. The examples provided in the September 2004 consultation paper to illustrate such analysis are:

- Two small firms merge and are better able to compete with a larger rival;

- The merged entity increases its investment in research and development to improve its product, which enhances rivalry with competitors;
- The merger results in efficiencies that create a maverick firm and undermine conditions for coordinated conduct; and,
- The merger results in cost-reducing efficiencies that are likely to lead to lower (or not significantly higher) prices, increased output or higher quality goods.

But in each of these cases, to my mind adding efficiencies to the section 93 analysis adds nothing. None of these mergers are likely to be found to substantially lessen or prevent competition under the current Act. Adding efficiencies as a factor to the analysis does not change this.

Some argue that including efficiencies as a factor in the analysis will result in the Bureau more routinely considering efficiencies in merger cases. I fail to see how this will make any difference. The Bureau already considers the business rationale for the merger. Merging parties (and their counsel) typically present their business motivation. Whenever synergies are important for the transaction – which is the vast majority of cases – the Bureau considers these in the normal course of its review. Efficiencies are being considered today, and they are being considered routinely because they are the *raison d'être* for the vast majority of merger transactions. They need not be itemized in detail as per a section 96 analysis to be relevant. To claim otherwise is to take an overly restrictive view of what efficiencies are.

This is clear from the Bureau's enforcement record – 98% of the mergers examined by the Bureau are found to raise no issue under the Act. It is important to recall why managers and shareholders pursue mergers. They do so because the merger is expected to increase profits. How? By generating cost savings and synergies, which are efficiencies.

The variation proposed for the *Factor Approach* would restrict the consideration of cost savings to only those that would be passed on to consumers. This approach would remove fixed cost savings from consideration unless the current practice is changed and a much longer time period is used for the review. In such circumstances, the *Factor Approach* becomes a consumer surplus standard.

Why should we care about fixed cost savings? Canada is a small economy with a considerable natural resource and manufacturing industrial base. Many of these industries have large fixed operating and capital costs relative to variable costs. As a result, we would expect competitive prices in these industries would exceed the marginal costs of the more efficient firms within the industry; otherwise, firms cannot earn sufficient revenues to recover their fixed sunk costs of investment.[24] As well, fixed and sunk investment means that entry will only occur at a price that provides some expected return on the fixed investment of entry in addition to marginal cost. Where capacity increments are lumpy and sunk, overcapacity can persist for some time. Mergers represent an efficient means of removing higher-cost excess capacity, and often provide a catalyst for additional efficiency improvements that firms are unable to finance independently.[25] As a result, mergers help improve returns on capital for shareholders.

While all of this is true for mergers everywhere, small economies like Canada need to be more receptive to efficiency claims than larger economies. Simply put, the Canadian economy cannot recover as easily from enforcement efforts that block welfare-enhancing mergers as a bigger economy like the United States or Europe. So, while there may be some welfare-improving mergers blocked in the United States and Europe, these are large economies with many alternative opportunities for shareholders and hence it might be argued that the cost of forgoing an efficient transaction for shareholders is not so great relative to the cost of the opposite error; namely, allowing a merger that may raise prices. Antitrust experts in small economies elsewhere in the world have made the same observation. In particular, I refer to the work of Michal Gal.[26] Small economies with limited domestic demand constrain the development of a critical mass of productive activities that are required to achieve the lowest costs of production. Firms may be characterized by sub-optimal production, the efficiency losses from which filter through to consumers. While free trade opens opportunities for firms to expand and hence improve scale, the capital that has been sunk in the past may not be easily rationalized without mergers.

All fixed cost savings, while relevant to the profitability of the transaction from the parties' perspective, will be irrelevant to efficiency considerations under a consumer surplus standard because fixed costs do not affect firms' pricing decisions.[27] As well, many production efficiencies would likely be irrelevant.[28] Only a limited set of plant-level efficiencies would flow through to variable cost savings, and likely no multi-plant level savings would be relevant. Dynamic efficiencies are also unlikely to flow through to marginal costs.[29] Looking back at some past decisions, this means that the vast majority of savings that were relevant in *Hillsdown*, *Imperial Oil* and *Superior Propane*, to name a few cases, would not be considered.[30]

In the aftermath of a merger, improvements in fixed costs will not be immediately passed on to consumers. However, in the long run, free entry and low transportation costs ensure that efficiency improvements are passed on to customers. But, the Bureau – like other antitrust agencies – does not take a long-term perspective to merger review. As a result, fixed cost savings would be irrelevant under any consumer surplus standard, yet of the total cost savings available for mergers in many of our industries, fixed cost savings are the most material. This raises a second issue for industries that have a strong export orientation – the primary beneficiaries of restricting the relevant cost savings to those that will be passed on to customers may be foreigners. Why would Canadian policy-makers choose to ignore many significant cost savings that ultimately accrue to Canada's benefit through allowing for more efficient production, while only counting savings that may predominantly flow to foreign customers?

Merger to Monopoly Option

The *Merger to Monopoly* would retain section 96 in its current form but add an explicit exception that would bar the successful application of the defence when a merger created a monopoly or near-monopoly. This is better than the *Factor Approach* in that fixed cost savings would continue to be relevant. However, it is unclear what benefit is achieved as the added text is unnecessary given the existing jurisprudence. Instead, adoption of the *Merger to Monopoly* option may perpetuate a misconception that was effectively dispelled by the Tribunal in *Superior Propane*.

Mergers in markets with pre-existing market power can still give rise to a substantial lessening of competition, as the Tribunal's decision in *Superior Propane* clearly indicates.[31] Further, the greater the amount of pre-existing market power, the greater the efficiencies must be in order to offset the resulting welfare loss. As a consequence, the more closely a merger approaches a merger to monopoly, the less likely it is that any efficiency accompanying the merger will offset the resulting welfare loss, even under a total surplus standard. If pre-existing market power is properly measured, it is unnecessary to amend section 96 to explicitly note the difficulties that merging parties moving to monopoly will face in meeting the trade-off standard.

Alternatively, if the language proposed for the *Merger to Monopoly* option is adopted, it begs the question of whether pre-existing market power and its implications have been properly understood and measured. Given the importance of pre-existing market power, and the extent to which the failure to properly measure it ultimately affected the Tribunal's decision in *Superior Propane*, it would be misguided to reduce any emphasis on this important welfare effect from mergers.[32] As well, I would expect such a change to put undue emphasis on market definition, since market definition will ultimately determine whether the efficiency exception is available to merging parties (in addition to the role played by market definition in determining likely competitive effects).

Merger Outcomes

Under the *Merger Outcomes* option, if the Tribunal were to allow a merger under section 96 it could include conditions that would allow for a post-merger assessment of whether the efficiencies were achieved and if not it could re-open the case. This option, like the *Merger to Monopoly* option, has the benefit of continuing to take into account fixed cost savings. However, it does introduce the potential for further delay and uncertainty for merging parties and for the Commissioner when litigating cases.

The vast majority of mergers are reviewed and resolved by the Competition Bureau in an informal review process with minimal levels of public transparency and formal due process. A tiny number of mergers are reviewed and resolved by the Competition Tribunal pursuant to an elaborate and formalized adversarial process. A contested merger review is characterized by substantial financial costs, inordinate delays and protracted uncertainty.[33] Yet most merger transactions are time-sensitive. Often the financial terms of the acquisition are dependent on the stock prices of either the acquiring or acquired company. Protracted delays and uncertainty are also likely to jeopardize supplier and customer relationships and retention of key management and technical personnel. It is difficult to imagine the Tribunal could expeditiously deal with applications to reverse or remedy a completed transaction owing to a failure to achieve expected efficiencies within this procedural environment.[34] Instead, the application would more likely turn into a rehearing of the case.

Finally, I agree with the observation by Paul Crampton that it may be very difficult to "unscramble the eggs" even if it can be established that the merger failed to achieve all of the forecasted cost savings.[35] Yet if the merger is only allowed to proceed on the basis that some component of the business is not fully integrated in order to allow for a possible future divestiture, this would be expected to limit the potential to realize the full efficiencies.

Overall, I find the potential administrative burden from the *Merger Outcomes* option unattractive. We risk turning the Tribunal into a regulator, a role for which it is ill-equipped. The Tribunal has neither the resources

for active monitoring of completed mergers, nor does it have the procedures in place to expeditiously decide matters as is required of a regulator.

The Crampton Proposal

In his article in this issue, Paul Crampton offers an alternative model, one that has efficiencies in two places – as a factor and an explicit defence but without any trade-off when part of section 96. The only trade-off under section 96 is in respect of dynamic efficiency gains and losses. As well, an additional defence under section 96 would be added to confirm that mergers that are unlikely to substantially increase prices would not be blocked. As explained below, this proposal adds unnecessary complications, is far from certain and it risks having fixed cost savings made irrelevant to the analysis relative to the *status quo*.

Before discussing the proposal in detail it is useful to define some terms. Economists distinguish static and dynamic efficiency in the following way. Static allocative efficiency is achieved when the social marginal benefit of the last unit produced equals its social marginal cost. Productive (or cost) efficiency means that output is produced at minimum cost, including opportunity cost. Dynamic efficiency is achieved when the social marginal benefit from the introduction of new products and processes is equal to the social marginal cost from such activity. I assume that the dynamic efficiencies referred to in the *Crampton Proposal* are the improvements made to consumer surplus from the introduction of new products and services and the improvements made to producer surplus from the introduction of new cost-saving technologies. When dynamic efficiency is optimized, the flow of surplus realized through the introduction of new products or processes over time, net of the cost of researching and developing these new products and processes, is at a maximum.

While I agree that the potential benefits from improvements in dynamic efficiency may far outweigh static allocative efficiency benefits from mergers, dynamic efficiencies are inherently uncertain and difficult to measure. The *Crampton Proposal* recognizes this and argues for a move away from quantitative oriented assessments to evaluations that are more qualitative in nature. But this begs the question of how is one to know if the forecasted dynamic efficiencies (and any potential dynamic efficiency losses) are "substantial" or not? When will it be clear that they are reasonably likely to result from the merger?

The gains to be achieved from new products and processes are highly uncertain at the time of the investment. These are products that do not currently exist. While firms may make predictions as to the prospects for success at the time that the innovative activity is occurring, outcomes are highly variable. Consider the research and development activities of pharmaceutical companies. Drug companies must screen an estimated 5,000 chemical compounds for each product approved for commercial sale.[36] Here, failure (in the sense of a compound that does not have any positive clinical benefit) is the rule, rather than the exception. Next consider the time that is taken before the benefits from the innovative activity are realized. It is not uncommon for many years to pass between the research and development ("R&D") stage and bringing a product to market.

Imagine a merger within this setting. How much does the compound failure rate need to change as a result of the merger to be considered substantial? If the merger meant that among 5,000 chemical compounds two instead

of one had the potential for commercial sale, is this substantial? What if the merger only affected the timing that the one possibility might have in coming to market, but it was still uncertain which of the 5,000 compounds would be the right one? These complications with dynamic efficiencies exist today with the *status quo*. But adopting an efficiencies defence that depends on dynamic efficiencies alone will exacerbate these problems, even if dynamic efficiencies are considered in a qualitative way.

My fear is that any competition authority (be it the Bureau or Tribunal) trying to make such predictions prior to the introduction of the new technology which will be the reality at the time of the merger, is likely to view the claims as sufficiently speculative to not consider them "reasonably likely" or "substantial" The end result will be that they are not considered. This would make the revised section 96 exception not operable in practice. In such circumstances the *Crampton Proposal* reverts to including efficiencies as a section 93 factor and for any merger that is not likely to generate dynamic efficiencies, section 96 is unavailable.[37]

In such circumstances it might be argued that having efficiencies as part of the substantial lessening of competition analysis is valuable. While the *Crampton Proposal* does not require efficiencies to be passed on to consumers, if a substantial lessening of competition is defined as the ability to materially increase prices then it is clear that fixed cost savings, which do not enter into firms' short-run pricing decisions, are not relevant.[38] The only efficiencies that would be relevant are those in respect of variable costs. As a result, this component of the test is like that of the U.S. price standard, although under the *Crampton Proposal* prices could rise post-merger just not by an amount that substantially lessens competition.[39] As indicated earlier, any proposal that fails to include fixed cost savings as part of the relevant set of efficiencies is flawed in my opinion.

The section 96 defence does not reintroduce fixed cost savings under the *Crampton Proposal*. Instead, the section 96 analysis is strictly related to dynamic efficiencies: the Tribunal would "not make an order under section 92 if it finds that the merger has brought about or is reasonably likely to bring about substantial gains in dynamic efficiency that would not likely be attained if the order were made".[40] There is a limited exception to this in that if the merger is likely to generate "dynamic efficiency losses that would be clearly and substantially disproportionate to the dynamic efficiency gains likely to be brought about by the merger" the transaction will not proceed. Presumably this exception is designed to capture the merger's potential effect on the introduction of new products and processes. It does not capture the merger's impact on pricing incentives for either the existing set of products and processes in use or the ones that might be introduced. As a result, welfare-reducing mergers may be allowed to proceed.

In putting forward this proposal, Crampton argues that the *status quo* and the total surplus standard previously have failed to provide a meaningful role for efficiencies. But as indicated earlier, efficiencies – viewed in a larger context – are considered today by the Bureau. The fact that the efficiency defence under section 96 is rarely invoked does not equate to a lack of a meaningful role for efficiencies. Cost savings and synergies generally drive mergers. Few are likely to substantially lessen or prevent competition. This is why agencies throughout the world challenge such a small fraction of total merger activity. Moreover, there is no other competition regime in the world (to my knowledge) that has given efficiencies a clearer predominant role in situations where efficiencies and anticompetitive effects arise as is provided by the *status quo* in Canada.

Any Reduction in Blocking Welfare-Enhancing Mergers?

Proponents of reform argue that the current environment is sufficiently uncertain as to dissuade business people from pursuing efficiency-enhancing mergers.[41] But no empirical evidence is offered to support this position.

Tables 1 and 2 provide a break-down of the Bureau's completed merger examinations, and their complexity classifications over time. Today, just as it was the case prior to the *Superior Propane* decision, about 98% of the Bureau's merger examinations give rise to a finding of no issue under the Act. In 1.5% of the cases, the Bureau seeks some form of remedy and in another 0.4% of the cases the parties abandon the merger as a result of the Commissioner's identified competition concerns. There are variations year over year, notably because we are dealing with such small numbers. Thus, if the total number of examinations in any given year is 260, the difference between five and six cases with remedies appears significant relative to the total number of transactions with remedies.[42] Nonetheless, since the *Redetermination* decision through fiscal year 2004/05, about 2% of merger examinations have resulted in remedies, which is comparable to the 1.5% average over the ten year period. If instead a comparison is made between the number of cases with remedies relative to the set of combined complex and very complex transactions, in fiscal 2004/05 the number of cases with agreed remedies was 11% which is the same as the average over fiscal years 1998/99 through 2001/02 prior to the *Redetermination* decision. Fiscal years 2003/04 and 2002/03 are much higher at 30% and 26%, respectively. There is insufficient information to know if these were anomalous years, reflecting the idiosyncratic nature of the set of mergers under review in those two years, or instead indicate a more aggressive enforcement approach.

Now consider the cases where the Bureau has sought remedies not dealt with by international agencies through consent orders since the Tribunal's decision in *Superior Propane*. The products and services involved have been landfills,[43] newsprint,[44] book retailing,[45] radio stations,[46] cement,[47] port terminal grain handling services,[48] food service distribution,[49] bread,[50] whisky,[51] agricultural chemical products,[52] newsprint,[53] motion picture exhibition,[54] whisky,[55] pharmaceutical products used in the treatment of human sexual dysfunction,[56] retailing plus-size ladies apparel,[57] railways,[58] car rental,[59] retailing of home improvement products,[60] and sawmills and log purchases.[61] In all cases the mergers proceeded with some adjustments. Thus, it is not obvious that efficiency-enhancing mergers were prevented. Would any of these transactions have been more likely to proceed without consent orders if the Bureau considered the potential for dynamic efficiencies under a section 96 trade-off? I tend to think not.

While it might be debatable whether a substantial lessening of competition was likely to result in all of these cases, I believe including efficiencies as a section 93 factor would not likely have changed the Bureau's conclusions in these cases. The Bureau believed the transactions were likely to lead to material price increases, which is why it concluded there was likely to be a substantial lessening or prevention of competition. Presumably the Bureau believed this even with the parties presenting whatever evidence they had in respect of variable cost savings (and other savings) in efficiencies submissions. While we might wish to have the merger review process reformed to increase the role of the Tribunal to test the Commissioner's theory of anticompetitive harm in these cases, reforming section 96 is not the answer to this problem.[62]

Unfortunately, there is no list of the mergers that are abandoned due to the Commissioner's competition concerns, but there is no evidence from Table 1 that the number of such transactions has increased post-*Superior Propane* compared to prior to the decision. Across the ten fiscal years, the average percent of concluded examinations abandoned for competition reasons is 0.4%. In fiscal 2002/03 there were no such cases, while in 2003/04 and 2004/05 there was one in each year. This is no different from the years prior to the *Superior Propane* decision.

What about transactions which never materialize? To what extent would the alternative proposals increase the likelihood that efficiency-enhancing mergers that are not pursued under the *status quo* would materialize under another regime? As discussed, any approach that has the effect of not counting fixed cost savings as relevant efficiencies will increase the probability that efficiency-enhancing mergers are not pursued relative to the *status quo*. The *Crampton Proposal* also runs this risk since fixed cost savings will not be relevant under the section 93 analysis or under the section 96 framework. Will the emphasis on dynamic efficiencies compensate for this? I believe not. In markets characterized by heavy investments in R&D and lots of innovative activity, mergers are unlikely to give rise to substantial lessening of competition findings, so the added emphasis given to dynamic efficiencies under the *Crampton Proposal* relative to the *status quo* which also considers dynamic efficiencies (as well as fixed cost savings) will not mean fewer efficiency-enhancing mergers are blocked. Furthermore, putting the proposed framework into effect raises sufficient complications that it offers no tangible improvement over the *status quo* when it comes to preventing efficiency-enhancing mergers from proceeding.

For these reasons, there is no reason to propose amendments to section 96. While some commentators have argued that amendments are inevitable and it is best to proactively reform the section rather than leaving it to the whims of Parliamentarians, there is little to suggest that competition law reform is at the top of our current minority government's legislative agenda. Cracking a vase now because it might later be more badly broken strikes me as highly sub-optimal relative to continuing to own a perfectly functional vase. The current regime is the right one economically, and it is not difficult to administer, as is evident from the several years of merger review post-*Superior Propane*.[63] The imperfect economically efficient world of merger review as we know it has not come to an end.

Table 1: Merger Examinations *

	2004-2005	2003-2004	2002-2003	2001-2002	2000-2001	1999-2000	1998-1999	1997-1998	1996-1997	1995-1996	Total
Total Examinations Concluded	**265**	**215**	**267**	**345**	**389**	**402**	**354**	**412**	**302**	**215**	**3,166**
No Issue Under the Act	259	202	257	338	381	392	346	406	299	210	3,090
Advanced Ruling Certificates Issued	179	138	163	217	215	223	191	238	189	122	1,875
Monitoring Only								2	1	1	4
With Agreed Remedies**	3	6	6	7	6	9	3	4	2	0	46
Consent Orders and Registered Consent Agreements	2	3	3	2	1	1	2	1	1	0	16
Contested Proceedings	0	1	1	0	0	0	2	0	0	0	4
Parties Abandoned Proposed Merger as Direct Result of Commissioner's Position	1	1	0	0	2	1	3	0	0	4	12
Proposed Mergers Abandoned for Other Reasons	2	5	3	0	0	0	0	0	0	0	10
Percent of Concluded Examinations with No Issues*	**98.5%**	**96.2%**	**97.3%**	**98.0%**	**97.9%**	**97.5%**	**97.7%**	**98.5%**	**99.0%**	**97.7%**	**97.9%**
Percent of Concluded Examinations with Agreed Remedies*	**1.1%**	**2.9%**	**2.3%**	**2.0%**	**1.5%**	**2.2%**	**0.8%**	**1.0%**	**0.7%**	**0.0%**	**1.5%**
Percent of Concluded Examinations Abandoned for Competition Reasons*	**0.4%**	**0.5%**	**0.0%**	**0.0%**	**0.5%**	**0.2%**	**0.8%**	**0.0%**	**0.0%**	**1.9%**	**0.4%**

Notes & Sources:

* Annual Report of the Commissioner of Competition 1999-2005, Competition Bureau of Canada.

** Include pre-closing restructuring, post-closing restructuring with undertakings, remedies in other jurisdictions that resolve the Canadian competition issues and consent orders

*** Excludes transactions where the parties abandoned the proposed merger for non-competition reasons

Table 2: Classification by Complexity Level *

Year **		Complexity		
		Non-Complex	*Complex*	*Very Complex*
2004-2005	Number of Transactions	213	19	8
	Percent of Total	88.8%	7.9%	3.3%
2003-2004	Number of Transactions	165	18	2
	Percent of Total	89.2%	9.7%	1.1%
2002-2003	Number of Transactions	215	21	2
	Percent of Total	90.3%	8.8%	0.8%
2001-2002	Number of Transactions	271	41	2
	Percent of Total	86.3%	13.1%	0.6%
2000-2001	Number of Transactions	282	52	14
	Percent of Total	81.0%	14.9%	4.0%
1999-2000	Number of Transactions	232	49	8
	Percent of Total	80.3%	17.0%	2.8%
1998-1999	Number of Transactions	212	56	6
	Percent of Total	77.4%	20.4%	2.2%
Nov 1997-Mar 1998	Number of Transactions	68	8	0
	Percent of Total	89.5%	10.5%	0.0%

Notes & Sources:

* Annual Report of the Commissioner of Competition 1999-2005, Competition Bureau of Canada.

** Fiscal unless stated otherwise

Notes

* I wish to thank Andrew Tepperman for insightful discussions about dynamic efficiency and Ralph Winter for his valuable comments on a draft of this paper. I also wish to thank Paul Crampton for clarifying his proposal to me. Any errors or omissions are my responsibility.

1 *Canada (Commissioner of Competition) v. Superior Propane Inc.* (2000), 7 C.P.R. (4th) 385; reversed (2001), 11 C.P.R. (4th) 289 (F.C.A.); application for leave to appeal to S.C.C. dismissed without reasons, [2001] S.C.C.A. No. 252 (September 13, 2001); reasons for decision on remand, 2000 Comp. Trib. 16 (April 4, 2002), CT 1998002 (Comp. Trib.) [*Superior Propane Redetermination Decision*].

2 A private member's bill, Bill C-249, sought amendments to section 96 of the *Competition Act* that would have repealed the efficiencies exception and replaced it with treating efficiencies as a factor for possible consideration with section 93 factors. As well, Bill C-249 included a consumer benefit requirement whereby the relevant gains to be considered would be those that "will provide benefits to consumers, including competitive prices or product choices" and that would not likely be attained in the absence of the merger.

[3] With Bill C-249's death on the Order Paper in May 2004, the Competition Bureau launched a consultation process in respect of the treatment of efficiencies in September 2004. Submissions on various trade-off options were sought and three roundtable discussions held in late January 2005. A final report of the consultation process was provided in April 2005 but was not released to the public.

[4] The Competition Bureau published a report in late April 2005 following consultations with international competition authorities on the treatment of efficiencies. This report summarizes the treatment of efficiencies in merger review in Australia, the European Union, Mexico, the United Kingdom and the United States.

[5] The Commissioner of Competition also constituted an Advisory Panel to report on the Economic Council's original rationale for recommending that efficiency gains be given specific consideration as an offsetting public benefit to mergers and whether this consideration was still warranted today, and if warranted what should characterize the treatment of efficiency gains under the Act. The Advisory Panel was not asked to comment on the standard for any trade-off analysis should one be recommended. The Advisory Panel's report was submitted to the Commissioner in August 2005 and released to the public in October 2005.

[6] I have been a proponent of the total surplus approach and continue to believe that this is the right public policy for any efficiency trade-off in merger review.

[7] "Both variable and fixed cost savings are relevant to the analysis because both generate producer surplus (even though it is recognized that generally only variable (i.e. marginal) cost savings lead to price reductions)." *Merger Enforcement Guidelines*, September 2004, at 33, n. 98.

[8] *Merger Enforcement Guidelines* at ¶8.14.

[9] *Ibid.*

[10] *Ibid.* at ¶8.15.

[11] The Respondents bear the burden of proof in respect of proving all the elements of section 96 on a balance of probabilities, except for establishing the anticompetitive effects of the merger which must be demonstrated by the Commissioner.

[12] *Superior Propane Redetermination Decision* at ¶335.

[13] *Ibid.* at ¶333.

[14] Thomas W. Ross and Ralph A. Winter (2004) "The Efficiency Defense in Merger Law: Economic Foundations and Recent Canadian Developments" Antitrust Law Journal 72(2) at 241.

[15] *Superior Propane Redetermination Decision* at ¶350.

[16] *Ibid.* at ¶356.

[17] *Ibid.* at ¶367.

[18] Ross and Winter (2004) at 257.

[19] *Ibid.* at 258.

[20] Thomas W. Ross and Ralph A. Winter, "Canadian Merger Policy Following *Superior Propane*" (2003) 21:3 Can. Comp. Rec. 7.

[21] Ross and Winter (2004) discuss the theoretical foundations for the *status quo*, finding that it conforms to welfarism and the Pareto principle that if a merger makes some individuals better off by increasing their surplus as consumers or their profits as shareholders without harming others, the merger should be allowed.

[22] My initial reaction to the balancing weights standard was also very negative. I considered it to present a large number of difficult pass-through problems that would make it difficult for the Bureau to establish socially adverse effects.

[23] I am indebted to Ralph Winter for this illustrative example.

[24] There are different types of firms in an industry, which may be ranked from lowest to highest marginal cost. The sum of the marginal cost curves of these firms trace out the short-run industry supply curve. The marginal firm has sufficiently higher marginal cost relative to other firms (i.e., the infra-marginal firms) that if price equals marginal cost for the marginal firm, the infra-marginal firms will be earning a markup sufficient to compensate for their capital costs. Since the firm owning the marginal facility is not earning a mark-up sufficient to cover its capital costs, one might wonder why the facility was built in the first place. Two possibilities exist. First, the marginal facility may have rising, not constant, marginal cost as it produces full capacity (e.g. decreasing returns) so that pricing at marginal cost is above long-run average cost. This might happen if it has older technology that breaks down more often or requires greater maintenance. Second, the marginal facility may have already recovered its cost of capital many years ago (or at least it was expected that it would when it was built) and as long as price is able to recover short-run average cost the firm will keep operating the facility (i.e., the capital cost is mostly sunk).

[25] When faced with excess production capacity at the industry level, it is most efficient for all the high variable cost facilities to shut down rather than for all firms to run at lower utilization rates. Mergers help facilitate this reorganization of production from time to time when excess capacity is high and or the difference in variable cost between facilities becomes very large. If a

large firm buys a small facility and then shuts it down, the smaller facility's output is at least partially replaced with output from the more efficient larger firm. Other firms may also replace some of the lost output.

[26] See Michal S. Gal, "Size Does Matter: The Effects of Market Size on Optimal Competition Policy" (2001) 74 Southern California Law Review 1451, and Michal S. Gal, *Competition Policy for Small Market Economies* (Cambridge: Harvard University Press, 2003).

[27] While fixed costs become variable costs over the long run, the Bureau does not take a long-run perspective to merger review.

[28] Production efficiencies include product-level, plant-level and multiplant-level operating and fixed cost efficiencies; efficiencies associated with integrating new activities within the firm; and savings attributable to the transfer of superior production techniques and know-how from one of the merging parties to the other. Plant-level savings refer to those that flow from specialization, elimination of duplication, reduced downtime, smaller inventory requirements, or the avoidance of capital expenditures that would otherwise be required. Multiplant-level savings include those associated with plant specialization, rationalization of administrative and management functions and the rationalization of research and development activities. Efficiencies also may be brought about in respect of distribution, advertising and raising capital. A reduction in transaction costs associated with integrating activities that previously were performed by third parties, such as contracting for inputs, distribution and services, also may constitute production efficiencies.

[29] Dynamic efficiencies include gains attained through the optimal introduction of new products, the development of more efficient productive processes and the improvement of product quality and service. Ordinarily it is extremely difficult for both the parties and the Bureau to forecast such savings.

[30] See Margaret Sanderson, "Efficiency Analysis in Canadian Merger Cases" (1997) 65 Antitrust Law Journal at 633 for a discussion of the savings claimed in *Hillsdown* and *Imperial Oil*.

[31] Notwithstanding the Tribunal's mention of the likely existence of pre-existing market power in this industry, it still found that the merger was likely to substantially lessen competition, with prices rising, on the Commissioner's evidence, by 7% to 11% depending upon the product and after taking into account the pass-through of cost savings (at ¶453 of the Tribunal's original decision).

[32] See Margaret F. Sanderson, "Competition Tribunal's Redetermination Decision in *Superior Propane*: Continued Lessons on the Value of the Total Surplus Standard" (2002) 21:1 Can. Comp. Rec. 1.

[33] Margaret Sanderson and Michael Trebilcock discuss these issues in a paper presented to the University of Toronto Law and Economics Programme Roundtable entitled "Process and Politics in Canadian Merger Review," June 16, 2000. For a discussion of potential reforms to the Tribunal process, see Neil Campbell, Hudson Janish and Michael Trebilcock, "Rethinking the Role of the Competition Tribunal" (1997) 76 Canadian Bar Review 297.

[34] Even the consent order process is subject to potential delay as the recent Agricore United application for a section 106 variation demonstrates. Having received ten extensions from the Commissioner to sell the United Grain Growers port terminal in Vancouver, Agricore United then filed a section 106 application when the Commissioner indicated she was unprepared to grant further extensions. Some nine months later, Agricore United sought an adjournment to the proceedings. When the adjournment motion was dismissed, it withdrew its application. While the port terminal sale is now in the hands of a trustee, this has been achieved after considerable delay and expense incurred by the Commissioner and the merging parties. (The author was retained by the Commissioner in this proceeding.)

[35] Paul Crampton, "Efficiencies in Merger Review: What is the Best Approach for Canada?" in this issue of the *Record*.

[36] PhRMA (Pharmaceutical Research and Manufacturers of America), "Why do Prescription Drugs Cost so Much and Other Questions About Your Medicines" June 2000 at 2.

[37] Savings in fixed and variable costs are the predominant efficiency claims made by merging parties in Canada.

[38] In his article, Paul Crampton describes determining whether competition is likely to be prevented or lessened substantially as "determining whether the process of competition, as reflected in the extent to which current and potential competition are able to constrain the exercise of market power by a merged entity, is likely to be adversely impacted to a substantial degree" This language differs from the language in the MEGs and Tribunal jurisprudence. It is not clear from the article what distinction is meant by Mr. Crampton relative to existing jurisprudence under section 92. I interpret Mr. Crampton's language to continue to focus on the exercise of market power as the operative meaning of a substantial lessening or prevention of competition. To this end, because fixed costs do not enter into firms' short-run pricing decisions, savings in fixed costs will not reduce firms' short-run prices. As a result, if post-merger the firm has the ability to increase prices because it has (enhanced) market power, this will be found to result in a substantial lessening of competition. Fixed cost savings will not change this finding when efficiencies are considered as part of determining a substantial lessening of competition.

[39] A merger that lessens competition, but not substantially, would be allowed to proceed.

[40] Crampton, *supra* note 35.

[41] See, for example, Crampton, *ibid.*

[42] If there are 260 cases and 98% are found to have no issue and five cases have remedies, the difference between having six and five remedies is small relative to the 260 cases but sizeable if only the set of cases with remedies is considered – moving from five to six cases with remedies is a 20% increase over the sample of five.

[43] Canadian Waste Services Inc. and Browning-Ferris Industries Ltd. discussed in the Commissioner's Annual Report 2002.

[44] Abitibi-Consolidated Inc. and Donohue Inc. discussed in the Commissioner's Annual Report 2002.

[45] Chapters Inc. and Trilogy Retail Enterprises L.P. discussed in the Commissioner's Annual Report 2002.

[46] Astral Media Inc. and Telemedia Radio Inc. discussed in the Commissioner's Annual Report 2002.

[47] Lafarge S.A. and Blue Circle Industries PLC discussed in the Commissioner's Annual Report 2002.

[48] United Grain Growers Limited and Agricore Cooperative Ltd. discussed in the Commissioner's Annual Report 2002.

[49] SYSCO Corporation and SERCA Foodservice Inc. discussed in the Commissioner's Annual Report 2002.

[50] Canada Bread Company, Limited and Multi-Marques Inc. discussed in the Commissioner's Annual Report 2002.

[51] Diageo PLC, Pernod Ricard S.A. and The Seagram Company Ltd. discussed in the Commissioner's Annual Report 2002.

[52] Bayer AG and Aventis CropScience discussed in the Commissioner's Annual Report 2003.

[53] Abitibi-Consolidated Inc. and Donohue Inc. discussed in the Commissioner's Annual Report 2003.

[54] Famous Players Inc. and Galaxy Entertainment Inc., and Onex Corporation and Loews Cineplex/Cineplex Odeon Corporation discussed in the Commissioner's Annual Report 2003.

[55] Diageo plc, Pernot Ricard SA and The Seagram Company Ltd. discussed in the Commissioner's Annual Report 2003.

[56] Pfizer Inc. and Pharmacia Canada Inc. discussed in the Commissioner's Annual Report 2003.

[57] Reitmans (Canada) Limited and Shirmax Fashions Ltd. discussed in the Commissioner's Annual Report 2003.

[58] Canadian National Railway Company and the Ontario Northland Railway discussed in the Commissioner's Annual Report 2003, and Canadian National Railway Company and the British Columbia Rail Limited discussed in the Commissioner's Annual Report 2005.

[59] Budget Group Inc. and Cendant Corporation discussed in the Commissioner's Annual Report 2003.

[60] RONA Inc. and Réno-Dépôt Inc. discussed in the Commissioner's Annual Report 2004.

[61] Canfor Corporation and Slocan Forest Products Ltd. discussed in the Commissioner's Annual Report 2004 and West Fraser Timber Co. Ltd. and Weldwood of Canada Ltd. discussed in the Commissioner's Annual Report 2005.

[62] Instead reform is needed to the Tribunal procedures as others have advised.

[63] In his article, Paul Crampton offers a long list of considerations that need to be taken into account when undertaking an efficiency trade-off under the *status quo*. While the issues to be addressed are complex, a list of the issues that have to be addressed to determine if there is a substantial lessening of competition is likely to be as long and as complex as the list for efficiencies. Moreover, adopting his proposal will not reduce the number of issues to be addressed. It just changes some of them. The fact that the list is long and the issues complicated does not make mergers beyond business people's reach. They hire legal advisors to assist.