ARTICLES

TOWARDS AN EFFICIENCIES STANDARD THAT BENEFITS CANADIANS

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This commentary offers an alternative economics-based rationale for the adoption of a consumer welfare standard for the assessment of mergers under Section 96 of the Competition Act that is not based on 'fairness' considerations, or any of the other objections recently voiced by the Competition Bureau in response to Senator Howard Wetston's consultation. Our main conclusion is that if the purpose of the merger provisions of Canadian competition law is to regulate mergers to the benefit of Canadians, and if Canada's national treatment obligations under international treaties prevent the differential treatment of Canadian and foreign shareholders in the efficiencies trade-off, then the consumer welfare standard may offer advantages over the current total welfare standard. Our observations are based on an economic analysis that demonstrates the extent to which Canadians benefit from merger efficiencies (and wealth transfers) generally depends almost exclusively on the extent to which merging firm profits flow to Canadian shareholders and does not depend on whether or not a merger reduces costs at operations located in Canada. This economic analysis is consistent with the Competition Tribunal's fourth efficiencies filter in Tervita. In its earlier Superior Propane Redetermination decision, however, the Competition Tribunal concluded that the Competition Act mandates that merger efficiencies should be included as a benefit in the efficiencies trade-off only if they reduce costs at operations located in Canada regardless of shareholder nationality, which would preclude the application of the fourth filter in Tervita. We show that if future transactions subject to Canadian merger law are expected to involve firms with substantial non-Canadian shareholdings—as has historically been the case—and if discrimination against foreign shareholders is not feasible, then a consumer welfare standard may maximize benefits to Canadians. If discrimination against foreign shareholders is feasible, as implied in Tervita, then a total surplus standard that includes efficiencies (and wealth transfers) as a benefit only to the extent that merging firms' profits flow to Canadians, maximizes benefits to Canadians. Given the ambiguity in Tribunal decisions regarding the treatment of efficiencies that flow to foreigners, future amendments to the Act should clarify the efficiencies exception to better reflect its intent.

Ce commentaire présente une autre justification fondée sur l'économie pour l'adoption d'une norme de bien-être des consommateurs pour l'évaluation des fusions en vertu de l'article 96 de la Loi sur la concurrence qui n'est pas fondée sur des considérations d'« équité » ou sur toute autre objection récemment formulée par le Bureau de la concurrence en réponse à la consultation du sénateur Howard Wetston. Notre conclusion principale est que si les dispositions du droit canadien de la concurrence sur la fusion visent à réglementer les fusions au profit de la population, et si les obligations nationales du Canada en matière de traitement en vertu des traités internationaux empêchent le traitement différentiel des actionnaires canadiens et étrangers dans le compromis en matière d'efficacité, alors la norme sur le bien-être des consommateurs pourrait offrir des avantages par rapport à la norme actuelle sur le bien-être total. Nos observations sont fondées sur une analyse économique qui démontre que la mesure dans laquelle les Canadiens et les Canadiennes tirent profit des gains en efficience des fusions (et des transferts de richesse) dépend en général presque exclusivement de la mesure dans laquelle les profits des entreprises fusionnées sont versés aux actionnaires canadiens et ne dépend pas de la réduction ou non des coûts des activités situées au Canada. Cette analyse économique est conforme au quatrième filtre d'efficience du Tribunal de la concurrence dans l'affaire Tervita. Toutefois, dans sa décision antérieure dans l'affaire Superior Propane Redetermination, le Tribunal de la concurrence a conclu que la Loi sur la concurrence exige que les gains en efficience des fusions soient inclus comme un avantage dans le compromis en matière d'efficience seulement s'ils réduisent les coûts des activités situées au Canada, peu importe la nationalité des actionnaires, ce qui empêcherait l'application du quatrième filtre dans Tervita. Nous démontrons que si l'on s'attend à ce que les transactions futures assujetties aux lois canadiennes sur les fusions impliquent des entreprises ayant des participations non canadiennes importantes, comme cela a toujours été le cas, et si la discrimination à l'égard des actionnaires étrangers n'est pas possible, une norme de bien-être des consommateurs pourrait maximiser les avantages pour la population du Canada. Si la discrimination à l'égard des actionnaires étrangers est possible, comme l'indique l'arrêt Tervita, alors une norme d'excédent total qui inclut les gains d'efficience (et les transferts de richesse) comme avantage seulement dans la mesure où les profits des entreprises fusionnées sont versés à la population du Canada maximise les avantages pour les Canadiennes et les Canadiens. Compte tenu de l'ambiguïté des décisions du Tribunal concernant le traitement des gains en efficience qui sont versés aux étrangers, les modifications futures à la Loi devraient clarifier l'exception dans les cas de gains en efficience afin de mieux refléter son intention.

Introduction

It seems obvious that the *Competition Act* (the "*Act*"), in conjunction with all laws within Canada, should seek to enhance the wellbeing of Canadians. In fact, the 1996 Economic Council of Canada report on competition policy, which the federal government requested to begin the process of reforming Canadian competition law, states, "[e]ssentially, we are advocating the adoption of a single objective for competition policy: the improvement of economic efficiency and the avoidance of economic waste, with a view to enhancing the *wellbeing of Canadians*" (emphasis added).[2] The Competition Bureau (the "Bureau") prominently echoes this sentiment on its website: "[t]he Competition Bureau is an independent law enforcement agency that protects and promotes competition *for the benefit of Canadian consumers and businesses*" (emphasis added).[3] Yet, the expressed purpose of the *Act*, which is to "maintain and encourage competition in Canada in order to promote the efficiency and adaptability of the Canadian economy,"[4] tells only half the story.

Nowhere does the *Act* explicitly mandate that the purpose of promoting "the efficiency and adaptability of the Canadian economy" is to benefit Canadians or enhance the wellbeing of Canadians. By defining the purpose of the *Act* to be the promotion of the efficiency of the Canadian economy without explicitly tying it as a path for benefitting Canadians, Parliament has created a tension: what if the efficiency of the Canadian economy comes at the expense of the wellbeing of Canadians?

Some economists may argue that there is no tension: an economy that is operating efficiently is also the economy that can serve Canadians best. The core of this argument is that efficient economies maximize the total gains from trade available in the economy (often referred to as 'total surplus' or the economic 'pie') but it is agnostic about which agents in the economy reap those benefits of the gains from trade. If the distribution of surplus is, in some way, deemed less than socially optimal, then policy tools (like taxes and subsidies) can be used to redistribute the *pie* in ways that maximize social objectives. But the purpose of *efficiency* is to make the *pie* as big as possible, and the distribution of that *pie* is not something with which economists should meddle. That is a job for politicians.

Still, as currently interpreted by the Competition Tribunal (the "Tribunal") in some cases,[5] and possibly the Bureau, the *Act* may blindly seek to enhance the efficiency of the Canadian economy even if the result is to shift welfare from Canadians to non-Canadians. When assessing a merger (or

any economic policy), 'effects on the Canadian economy' is not synonymous with 'effects on Canadians' because there are many non-Canadians participating in the economy. Permitting a merger in the name of improving the efficiency of 'the Canadian economy' can result in net harm to Canadians. The current application of the efficiencies defence illustrates this thesis. After the Commissioner of Competition (the "Commissioner") has established that a merger has or will likely result in a substantial lessening or prevention of competition ("SLPC") to the detriment of Canadians (e.g., by identifying material price increases to Canadian buyers of the merging firms' products), the parties may prevail notwithstanding the SLPC by adducing evidence that the transaction creates efficiencies that are greater than and offset the anticompetitive effects that result from the merger. That is, that the transaction makes the *pie* bigger, even if the distribution of the new larger *pie* is unfavorable for consumers. If all the agents capturing slices of this new bigger *pie* are Canadians (e.g., Canadian consumers, Canadian businesses, etc.) then there is no tension between 'effects on Canadians' and 'effects on the Canadian economy': the enhanced efficiency of the Canadian economy supports the welfare of Canadians. But if some of the agents capturing the *pie* are not Canadians (e.g., if some are foreign shareholders of the merging firms), it is not immediately apparent that the enhanced efficiency of the Canadian economy does support the welfare of Canadians. In fact, quite the opposite may be true. The harms of the SLPC are likely to accrue primarily to Canadians, while many of the benefits of the efficiency may be accruing to non-Canadians, even if they enhance the efficiency of the Canadian economy. Maximizing the size of the Canadian economic *pie* doesn't necessarily maximize how much *pie Canadians* get to eat.

Amendments to the Competition Act

In his response to Professor Edward Iacobucci's discussion paper[6] for Senator Howard Wetston's consultation on possible amendments to the *Act*, the Commissioner recommended that the current efficiencies exception in Section 96 of the *Act* be eliminated and that efficiencies instead should be considered as a factor in assessing the effects of mergers.[7] Among the Commissioner's other rationales for the elimination of the efficiencies exception are that the current efficiencies exception permits mergers that are harmful to Canadians and "suffers from a misguided original policy intent."[8] While these rationales are related to our discussion, they are based on a distinction between the harms to consumers and businesses that purchase the relevant product and the 'private' benefits from efficiencies that accrue to producers. We instead focus on the distinction between the effects of mergers on Canadians and non-Canadians, regardless of whether they are consumers

or producers. Nonetheless, both arguments suggest that the current total welfare standard does not sufficiently address concerns about the distribution of economic surplus.

One of the Commissioner's other reasons for suggesting an elimination of the efficiencies defence in its current form is that it is an 'international outlier.' Under the current efficiencies exception, mergers are generally only blocked if consumer harms are outweighed by producer benefits. The Commissioner, in contrast, cites with approval the US Horizonal Merger Guidelines, which state that merging firms will generally be required to show that efficiencies are of such a sufficient extent that they would "reverse the merger's potential to harm customers … *e.g.*, by preventing price increases …"[9] That is, he points to the consumer welfare standard for consideration as it is an internationally accepted alternative approach to Canada's current efficiencies exception.[10]

The Commissioner concludes that efficiencies should be a factor in the analysis, not an exception to the *Act*, moving Canada in line with international best practice. While he arrives at this conclusion without explicit recommendation of how this would manifest, he quotes the US consumer welfare standard as consistent with international practice. [11] If the US approach is adopted in Canada, then when assessing efficiencies, only variable cost reductions likely to be passed through to consumers would be considered. Not only would this create a more aggressive approach to merger review in Canada, it may also serve to support the objective of directly benefiting Canadians, not just the Canadian economy. While this may not be the intent behind the Commissioner's endorsement of treating efficiencies as a factor, as we discuss below, it may be an additional reason to consider this amendment.

In *Tervita*, the Tribunal[12] and the Supreme Court of Canada[13] both adopted the total surplus standard for the efficiencies trade-off.[14] Under a total surplus standard a merger is allowed if and only if the net economic effects of the merger on both consumers and producers is positive; that is if total economic surplus increases (i.e., the *pie* gets bigger). A common objection to a total surplus standard (like that voiced by the Commissioner above) is that the wealth transfer from consumers to producers is treated as neutral; so long as total surplus increases, who wins and who loses is irrelevant to the analysis. Absent other interventions, an increase in total surplus does not mean that everyone is better off. Often, efficiency is maximized only when some welfare is transferred from losers to winners. Public interest may not be in favour of this exchange.

At times, total surplus can be maximized *only* when socially adverse outcomes are present. Consumers are generally, but certainly not always, economically worse off than the shareholders of the merging firms. Yet it is often the consumers who bear the harm of a merger and the shareholders who are the beneficiaries of the increase in total surplus. This consideration has led the Tribunal to consider the 'balancing weights' standard in some cases,[15] under which some or all of the wealth transfer counts as a negative in the efficiencies trade-off. A consumer welfare standard goes even further than a 'balancing weights' approach because it always treats all of the wealth transfer from consumers to producers as a social cost of the merger. The 'balancing weights' approach is intended to promote *fairness*. But 'balancing weights', or in the extreme, a consumer welfare standard, can address a separate, but related issue. It can be used as a tool when seeking to ensure that efficiency is not being prioritized over the welfare of Canadians.

Many of the mergers that have been reviewed by the Bureau involve firms that have significant non-Canadian shareholdings, and there is no reason to believe future mergers will be any different. Efficiencies from the rationalization of operations based in Canada may make the Canadian economy more efficient if the resources released by the efficiencies remain in Canada and are used to produce additional economic output in other industries.[16] However, the direct benefits from these efficiencies accrue to the merging firms' shareholders in the form of higher profits,[17] and if some of these shareholders are foreigners, then a corresponding portion of the benefits of efficiencies flow to non-Canadians.[18] If the ultimate goal of Canadian merger enforcement is to maximize benefits to Canadians, and not to promote the efficiency of 'the Canadian economy' when these objectives conflict, then the efficiencies considerations in merger review should recognize the nature of these flows.[19] To do otherwise by focusing on promoting the efficiency of 'the Canadian economy' whether or not efficiencies benefit Canadians implies that some mergers that harm Canadians to the benefit of non-Canadians will be allowed.[20]

If the goal were for the *Act* to independently promote the welfare of Canadians, the total surplus standard would *only* count the surplus accruing to and lost by Canadians. Only producer harms and benefits from efficiencies and wealth transfers that flow to Canadian shareholders, regardless of the location of rationalized operations,[21] and consumer harms from price increases and wealth transfers that flow from Canadian consumers, should be considered. Under this 'total Canadian welfare' standard, mergers would be blocked if and only if total harms to Canadians outweigh total benefits to Canadians.

However, the Tribunal has indicated that national treatment obligations under Canada's trade and investment agreements may prevent the Tribunal from fully discriminating between Canadian and non-Canadian shareholders in the application of the merger provisions.[22] If this is the case, and if future mergers are expected to involve firms with significant non-Canadian shareholdings, continued use of a non-discriminatory total surplus standard will allow some mergers that increase total surplus and make the Canadian economy more efficient, even if they harm Canadians. This is because some efficiency benefits that accrue to non-Canadians (e.g., foreign shareholders) would be used to offset harms to Canadians (e.g., consumers) in the trade-off.

If formal discrimination, whereby efficiency benefits accruing to foreign shareholders are discounted relative to benefits to Canadian shareholders,[23] is not feasible in the form of a 'total Canadian welfare' standard, the consumer welfare standard may, instead, better achieve the goal of maximizing the benefits of mergers to Canadians compared to the current total surplus standard. A consumer welfare standard is a blunt instrument that may be the best option to maximize benefits to Canadians given international treaty constraints. This standard disregards all producer benefits entirely in favour of consumers. The consumers are Canadians.[24] The producers *may not* be. A consumer welfare standard that applies to all mergers would therefore be a way to in effect discriminate against non-Canadian shareholders if discrimination is not feasible on a case-by-case basis because of Canada's international treaty obligations.

The remainder of this commentary begins with a detailed discussion of the relationship between merger efficiencies and economic surplus in merger review, including how Canadians are affected depending on their shareholdings of the merging firms. We then discuss Tribunal decisions in *Superior Propane Redetermination* and *Tervita,* which, along with a limited discussion in *Parrish & Heimbecker,* are the only merger decisions that deal directly with the treatment of efficiency benefits that flow to foreign shareholders. We then explain how a consumer welfare standard may maximize benefits to Canadians if merging firms in the future are expected to have substantial non-Canadian shareholdings and Canadian national treatment obligations prevent discrimination against foreign shareholders. We also briefly comment on the appropriate treatment of efficiencies if discrimination against foreign shareholders *is* feasible. This is followed by a section that provides some statistics on the extent of foreign ownership of firms involved in mergers recently reviewed by the Bureau and of firms that operate in Canada more generally. This analysis shows that most recent

complex mergers reviewed by the Bureau involve firms that appear to have significant foreign shareholdings.

The Effects of a Merger on Economic Efficiency

Allocative efficiency is achieved when every customer who is willing to pay more for a good than it costs to produce buys that good. That is, the total amount of available gains from trade are realized (i.e., the *pie* is as big as possible). A merger that results in higher prices, and thus lower output, because it increases the merged firms' market power reduces allocative efficiency. Some consumers whose value for the product was higher than the pre-merger price but lower than the post-merger price will no longer purchase the product. Consequently, some mutually beneficial gains from trade that were realized before the merger are not realized after the merger, and this results in a reduction in total economic surplus. This is the nature of the allocative inefficiency from post-merger price increases.[25]

If the merged firm can produce the same level of output at a lower overall resource cost compared to the pre-merger cost, or if it can produce more output at the same resource cost, then the merger is said to generate efficiencies.[26] Changes to cost structures that reduce the amount of resources used to produce the same amount of output are said to generate efficiencies because the released inputs will be employed elsewhere to produce some other output.[27] As such, the total output that can be produced with available inputs grows.[28] For example, if a merger allows the merged entity to use fewer tons of steel without reducing output, that unused steel is redeployed elsewhere in the economy to make some other goods. The economy expands and becomes more efficient because it can now produce more output from the same amount of resources. If the released resources were used originally in operations located in Canada and are redeployed to produce output in operations located elsewhere in Canada, then the Canadian economy expands. That is, the Canadian economy becomes more efficient. If the released resources are redeployed in another country, whether they were used in Canadian or foreign operations pre-merger, then the other country's economy expands.

Quantification of Merger Effects

When a policy or regulation simultaneously generates both inefficiencies and efficiencies the overall economic effect of the policy is generally assessed through a cost-benefit analysis ("CBA"). CBA is widely used by economists and governments to evaluate the overall impacts of policy proposals. The Canadian government requires that "regulatory proposals and

decisions are based on evidence, robust analysis of costs and benefits, and the assessment of risk, while being open to public scrutiny."[29] The Treasury Board requires all regulatory proposals that are expected to impose annual costs of $1 million or more are to be quantified and monetized though a CBA.[30] They are not alone; governments around the world mandate CBA for policy proposals.[31]

CBA is a decision standard that is used to guide decisions as to whether a policy or regulation should be implemented from an economic-efficiency point of view. If overall benefits to individuals exceed the costs to individuals, then the proposal is deemed to be economically efficient.[32] The gains and losses in a CBA are not necessarily monetary, but they do need to be monetized, or quantified, to make them commensurable. Economists have developed a wide variety of tools to quantify the effects of various policies, which often involve estimating non-monetary effects in monetary terms. For example, environmental effects and loss of life have been quantified be economists and used by governments in cost-benefit analyses.[33]

The total surplus standard applied to evaluate whether efficiencies outweigh the anticompetitive effects of a merger is a CBA. In the context of mergers and first proposed by Oliver Williamson,[34] a total surplus approach to evaluating the overall economic effects of a merger involves first quantifying the anti-competitive effects resulting from post-merger price increases (and/or non-price effects) and merger-specific efficiencies, and then assessing whether the efficiencies are larger, in monetized terms, than the anti-competitive effects. If the inefficiencies from the anti-competitive effects are lower than the merger-specific efficiencies, then total surplus increases if the merger is consummated, which means that the winners from the merger could hypothetically fully compensate the losers for their losses and still be better off. If total surplus increases, then the merger is deemed to be economically efficient.[35]

Who is Harmed and who Benefits from a Merger?

The largest source of harm to consumers from a merger that allows the merged firm to increase prices is generally the transfer of wealth from consumers to the merged firm though increased prices. Consumers who continue to purchase the product because their subjective value for the product exceeds the post-merger price now pay a higher price and thereby receive a lower consumer surplus. For example, if the price increases from $10 per unit to $11 per unit, some consumers will no longer purchase the good because of the price increase while some other consumers continue

to purchase at the new higher price. If the amount that continues to be purchased is 100 units, the consumers who buy these goods pay a total of $100 dollars more for the output they continue to consume than they would have at the old price, and thus have lost $100 in consumer surplus. Although this represents a harm to consumers, it is also a benefit to the producers of $100. This benefit to producers takes the form of higher revenues, and therefore higher profits. Since the increase in profits directly accrues to the shareholders of the merging firms,[36] this wealth transfer is a benefit to the shareholders of the merging firms.[37] A transfer of wealth from consumers to shareholders is not an allocative inefficiency, it is just a redistribution of the *pie*.

As discussed above, mergers that result in fewer units of output being produced, and subsequently consumed, create allocative inefficiency, which results in economic harms that are borne by consumers and producers of the relevant product.[38] In a CBA, the harm from allocative inefficiency is measured as the deadweight loss ("DWL") from lost consumer surplus and DWL from lost producer surplus, respectively. The reduction in the production and consumption of output is economically inefficient because consumers value the output more than it costs the economy to produce, so that a mutually beneficial trade goes unrealized, and the combined producer and consumer DWL measures the economic value of these unrealized gains from trade.

The harm to consumers from the foregone consumption—the DWL from lost consumer surplus—can be measured as the difference between the subjective value that consumers place on the product and the pre-merger price multiplied by the number of foregone units.[39] The total harm to consumers is calculated as this DWL from the consumers who cease to purchase the output combined with the wealth transfer from the consumers who continue to buy the product at the higher post-merger price.

If producers were earning a positive variable margin on the foregone output that is no longer produced and sold because of price increases resulting from the merger, then they too suffer some harm. The loss of the margin on the foregone output is the producer DWL. The producer DWL is typically calculated as the difference between the pre-merger price and the marginal production cost multiplied by the number of foregone units. This harm to producers takes the form of lower profits to the shareholders of the merging firms.[40] Still, firms typically would only choose to merge if this harm to producers was dwarfed by cost savings and the wealth transfer from increased prices in consummated mergers—otherwise, there would be no incentive to merge in the first place.

The economic benefits of a merger are the merger-induced reductions in the use of economic resources to produce output, which release resources for deployment in other sectors of the economy. These benefits are generally captured by the merging firms in the form of lower production and other costs.[41] Reductions in production costs increase the profits of the merging firm, and these profits are ultimately distributed to the firms' shareholders.[42]

For example, suppose that because of a merger, the newly joined entity will require one fewer worker to achieve the same level of output.[43] Suppose that a released worker's compensation was $50,000 per year before the firms merged and implemented the efficiencies that made her employment by the firm unnecessary. Upon release of this worker, the merged firm's costs are reduced by $50,000 per year, and its profits correspondingly increase by $50,000.

The value of the released worker to the rest of the economy is her value in her next best alternative employment, which is presumably where she will be redeployed. While not necessary, it is often assumed that labour markets are competitive and there is no lack of demand for labour, such that the worker's value in her post-merger employment will be equal to her value in her pre-merger employment. Practically speaking, this assumption is akin to assuming her next job will also pay her a wage of $50,000. Fundamentally, though, this assumption is that the value of the worker's output has been unchanged by her place of employment: her labour created $50,000 worth of value before the merger and $50,000 worth of value after the merger.

'Value' to the economy should not be confused with the surplus created by the deployment to a new use. The key point here is that if the worker is re-employed in competitive labour and product markets—which is the assumption that is usually adopted in CBA unless there is reason to believe otherwise—the $50,000 in value created by the redeployment of the worker is not economic *surplus*. The distinction between the value of the resource in an alternative use and the surplus created by the release of the resource is important to understand. The value of the resource in its alternative use is the amount that the employer is willing to pay, which is, in a competitive market, the marginal value product of the resource in its new employment and as such no new surplus is created for the employer. Furthermore, if the resource is re-employed to produce output in a competitive market, then consumers of the output receive no new surplus.[44] Finally, since the worker receives the same compensation in her new employment, her surplus does not change. The redeployment of the worker therefore does not create any new economic surplus in her new deployment.[45]

Despite this critical distinction, measuring new economic surplus for an efficiencies analysis requires us to measure this worker's value at her next best alternative employer. In the example we have described until now, where the value of her output is the same regardless of her employer, the cognizable efficiencies are simply the cost savings at the merged firm: the $50,000 they are no longer paying the worker. But if there were reasons to believe that in the next best alternative, the released worker would only have a value (and therefore compensation) of $40,000,[46] then the cognizable efficiencies would be only $40,000 as well—although total efficiencies would be calculated as the $50,000 in cost savings at the merged firm less the $10,000 reduction in the value of the worker in the alternative use.[47] Regardless of the worker's value in her next best alternative employment, the party that has captured the economic surplus from the release of the worker consists of the shareholders of the merging firm.

As explained above, if the efficiencies result from a reduction in the use of resources in Canadian operations, and the released resources are redeployed elsewhere in the Canadian economy, the Canadian economy expands. In this sense, the Canadian economy becomes more efficient, since it can now produce more output with the same amount of resources.[48] As aligned with Section 1.1 of the *Act*, this hypothetical merger has promoted the efficiency of the Canadian economy.

However, to the extent that the shareholders of the merging firms are non-Canadians, the beneficiaries of this expansion of the Canadian economy are also non-Canadians. If all of the shareholders of the merging firms are non-Canadians, the expansion of the Canadian economy through merger efficiencies provides no direct benefits to Canadians. Similarly, if the merging firms are entirely owned by Canadians and the merger reduces the costs of operations in Argentina and released resources are redeployed elsewhere in Argentina, then the efficiencies expand the Argentinian economy but the direct benefits of this economic expansion accrue entirely to Canadians in the form of higher profits. The extent to which Canadians benefit from merger efficiencies therefore depends on the extent to which Canadian shareholders benefit from efficiencies and does not depend at all on the location of the rationalized facilities.[49]

Consider another simple example. Two firms that are 100% owned by Argentinians merge and expect to combine their two operations in Winnipeg and thereby reduce their Canadian plant maintenance workforce by ten. We assume that there are no output reductions for the merging firms resulting from the reduced workforce. The released maintenance workers earned

wages totaling $1 million annually, and if they are immediately redeployed to other plants in Canada at the same wage they will produce incremental output worth $1 million. The efficiencies from the merger after the integration of Canadian operations are therefore $1 million per year. The following are all of the direct effects of the direct merger efficiencies: 1) the Argentinian shareholders of the merging firms gain $1 million dollars; 2) the released workers change jobs, and; 3) the Canadian economy increases its output by $1 million dollars. The only individuals directly affected by the merger are the Argentinian shareholders of the merging firms, and the released maintenance workers who are unlikely to receive any benefits from the rationalization (and in fact may suffer harms associated with dislocation). The firm that employs the released workers and the consumers of the product produced by the workers in their new employment do not gain any surplus for the reasons discussed above regarding the nature of competitive markets.

There may be circumstances under which only some of the benefits of efficiencies are captured by the merging firms' shareholders, and the rest may accrue to Canadians. For example, if released resources are redeployed in an area in Canada that has excess production capacity or excess unemployment, this may result in 'multiplier' effects from redeployment that increase production and surplus beyond the direct contribution of the released resources. And if a large number of resources are released and redeployed elsewhere in Canada, or are redeployed in uncompetitive labour or product markets in Canada, then they may increase Canadian surplus in the markets in which they are redeployed since their effects may be more than 'marginal'. Furthermore, the increased profits accruing to foreign shareholders may be reinvested in Canada and provide surplus benefits to Canadians. If such benefits do exist, however, they are likely to be second-order effects and in any case they should be included in the efficiencies trade-off—they are not additional benefits that are normally excluded from a properly conducted cost-benefit (or efficiencies) analysis.[50]

Treatment of Foreign Shareholders in Tribunal Decisions

The appropriate treatment of foreign shareholders in relation to efficiencies under the *Act* is unclear. In *Rogers-Shaw*,[51] the Commissioner and his experts argued that the portion of the wealth transfer that benefits certain shareholders, including affluent and foreign shareholders, is socially adverse and therefore should not offset the wealth transfer from Canadian consumers.[52] In Rogers' Closing Submission, it noted that it is not clear whether the Commissioner intended to claim that cost savings from operations

in Canada that would flow through to foreign shareholders are not cognizable.[53] In anticipation of such a claim, Rogers cited *Superior Propane I* and *Superior Propane Redetermination* as the legal authorities relating to the treatment of foreign shareholders in an efficiencies analysis. Rogers claimed that "no decision by the Tribunal or a Court has ever discounted the merging parties' efficiencies based on the proportion of their shareholders who are foreign. The focus when considering efficiencies from a merger is the real resource savings to the Canadian *economy*—not the transfer of wealth to shareholders" (cite to *Superior Propane I* omitted).[54] It also asserted that in *Superior Propane Redetermination*, the Tribunal found that "excluding efficiencies based on the nationality of shareholders constitutes discrimination under Canada's international obligations/trade and investment treaties and would be inconsistent with Canada's treaty obligations (including the obligation under USCMA to provide "national treatment" to investors from the United States and certain other countries)." [55] Finally, "as it concerns balancing weights, there is no case in which the Tribunal has treated a 'transfer' to foreign shareholders differently from a transfer to domestic shareholder[s] and no support in the Act."[56] The Tribunal did not opine on this issue because it concluded that the merger would not likely result in a substantial prevention or lessening of competition and it therefore did not need to address the efficiencies trade-off.[57]

In *Superior Propane Redetermination*, the Commissioner had similarly argued that the wealth transfer from consumers to producers should be a mitigating factor in the efficiencies trade-off.[58] In other words, the impact of price increases borne by consumers who continue to buy the good is socially adverse even if it does not result in allocative inefficiency (i.e., even if it creates no DWL). The caveat to this argument was the Commissioner's suggestion that this socially negative effect need only be considered insofar as it is a harm to *Canadian* consumers.[59] That is, the adverse impact on foreign consumers should have no weight in the analysis.

In this case, the Tribunal also appeared to hold that the application of the *Act* as it relates to efficiencies should be the same regardless of the nationality of ownership of the merging firms; that is, in applying the efficiencies trade-off, the Tribunal is bound by Canada's international treaty obligations to treat foreign shareholders equally to Canadian shareholders.[60] This is the implication cited by Rogers in *Rogers-Shaw*. It further found that efficiencies should count as a benefit of a merger only if they are cost savings on Canadian operations, and efficiencies on operations located outside of Canada should not be included:

> "[I]n the Tribunal's view, efficiency gains and deadweight loss (i.e. losses in efficiency) in foreign markets resulting from an anti-competitive merger in Canada are to be excluded in the application of section 96. This is clearly stated in the statute and is not a discretionary matter for the Tribunal. Accordingly, if the deadweight loss in foreign markets is an excluded effect, so are all other effects in foreign markets."[61]

In *Tervita*, however, which was decided after *Superior Propane*, the Tribunal's fourth screen for cognizable efficiencies "filters out claimed efficiency gains that would be achieved outside Canada and would not flow back to shareholders in Canada as well as any savings from operations in Canada that would flow through to foreign shareholders."[62] This screen implies that efficiencies are considered in the total surplus trade-off only to the extent that they benefit Canadian shareholders, regardless of where rationalized operations are located.[63] As such, the view of the Tribunal in this case is based on the understanding that efficiencies should be considered only to the extent that they provide benefits to Canadians, not 'the Canadian economy', which implies that Canada's national treatment obligations are not a barrier to discriminating against foreign shareholders. However, the treatment of foreign shareholders in relation to efficiency was *obiter dictum* in *Tervita*, and since the Tribunal did not explicitly acknowledge in that decision that the fourth filter is inconsistent with its prior reasoning in *Superior Propane Redetermination*, the legal status of efficiency benefits that accrue to foreign shareholder remains unclear.

How the Adoption of a Consumer Welfare Standard Could Benefit Canadians

Assuming that all of the consumer harms from post-merger price increases are borne by Canadians,[64] if some positive portion of the efficiencies and wealth transfer accrue to non-Canadian shareholders, then the net benefit (benefits less costs) of the merger to Canadians will be less than the change in total surplus, because some portion of the economic benefits of the merger accrue to non-Canadians. This is true even if the merger efficiencies are cost reductions in operations located in Canada. This implies that a total surplus standard that does not discriminate between Canadian and non-Canadian shareholders may allow some mergers that harm Canadians overall.

Consider a merger in a market with the following features:

1) The pre-merger price is $100 per unit;

2) Consumers purchase 1 million units (and all consumers are Canadians);

3) The variable margin of producers of the relevant product is 30% of revenues; and

4) The market demand elasticity is -1.

Suppose that because of a merger:

1) There are efficiencies of $4 million per year as a result of merger-induced resource cost savings; and;

2) The merger increases the price of the relevant product by 10%.

Under a total surplus standard, efficiencies outweigh anticompetitive effects, because the sum of DWL from lost consumer surplus ($0.5 million) and DWL from lost producer surplus ($3 million) is less than the $4 million in efficiencies. The wealth transfer from consumers to producers of $9 million is neutral and does not affect the trade-off.[65] Total harm to consumers is $9.5 million (DWL of $0.5 million, wealth transfer of $9 million) and the total net benefit to producers is $10 million (efficiencies of $4 million and wealth transfer of $9 million, less DWL from lost producer surplus of $3 million). This is just another way of showing that total surplus increases, because producer benefits are greater than consumer harms, by $1 million.

Now suppose that 25% of the merging firms' profits accrue to foreign shareholders. Then Canadian shareholders receive 75% of the $10 million in producer benefits, or $7.5 million. Again, assuming that all consumer harms are borne by Canadians, harms to Canadians would now exceed benefits to Canadians by $2 million. If 50% of shareholder benefits accrue to non-Canadians, producer benefits to Canadians are only $5 million, and consumer harms would exceed Canadian benefits by $4.5 million.

If a total surplus standard is applied to assess the efficiencies trade-off and the purpose of the trade-off is to allow only mergers that benefit Canadians (and not 'the Canadian economy'), then then portion of efficiency gains accruing to non-Canadians would be given zero weight and wealth transfers from Canadians to non-Canadians should not be considered neutral (that is, it should be treated as a harm to consumers without an offsetting benefit to producers).[66] This would ensure that only mergers where the benefits to Canadian shareholders exceed to harms to Canadian consumers are allowed.[67]

However, if Canada's international treaty obligations prevent differential treatment of Canadian and non-Canadian shareholders, and since lending any weight to producers' capture of wealth through efficiencies or transfers puts Canadian welfare at risk, then one option is to discount producer effects altogether–regardless of the nationality of the producers. This is a consumer welfare standard, under which only the effects of a merger on consumers are considered in a determination of whether to allow a merger, and efficiencies are considered only to the extent they are passed through to consumers in the form of lower prices. So long as the consumer welfare standard would be applied in all merger cases regardless of foreign ownership, rather than selectively in mergers of firms with large foreign shareholdings, it would not violate Canada's international treaty obligations.

If foreign shareholders cannot be discriminated against because of Canada's national treatment obligations, a consumer welfare standard may maximize the benefits of merger enforcement to Canadians if it is expected that non-Canadians will continue to have a substantial ownership interest in firms involved in mergers that are reviewable under Canadian merger law. Below, we provide some statistics that demonstrate that non-Canadians own a substantial financial interest in many, if not most, firms that were historically involved in complex mergers reviewed by the Bureau. Non-Canadians also own a significant proportion of large firms with operations Canada, which are more likely to be involved in mergers. These facts suggest that continued application of the current total surplus approach, which is in some cases modified by a balancing weights standard, could sometimes result in allowing mergers that harm Canadians. For the reasons discussed above, this is the case even if only efficiencies on Canadian operations 'count' in the trade-off.[68]

Treatment of Efficiencies if Discrimination Against Foreign Shareholders is Feasible

If it is feasible, notwithstanding Canada's national treatment obligations, for the Tribunal to discriminate between efficiency benefits that flow to Canadians and non-Canadians, then, for the reasons discussed above, the preferrable approach to the efficiencies trade-off *if* the objective of merger policy is to maximize benefits to Canadians is to apply the Tribunal's fourth screen in *Tervita*. This approach is agnostic about the location of rationalized operations: efficiencies on Canadian operations should be included as a benefit in the trade-off only to the extent that the financial benefits of merger cost reductions flow through to Canadian shareholders, and efficiencies on non-Canadian operations should also 'count', but again only to

the extent that the transfer flows to Canadian shareholders. Similarly, if the wealth transfer is considered to be neutral, then this neutrality should only be applied to the extent that the shareholders of the merging firms are Canadians, since otherwise the transfer would benefit foreigners at the expense of Canadians. This would also be consistent with *Superior Propane Redetermination* where the Tribunal, relying on the fact that the purpose of the *Act* is to "maintain and encourage competition in Canada … to promote the efficiency and adaptability of the Canadian economy",[69] found that efficiency gains in foreign markets are to be excluded from the trade-off. Perhaps future amendments to the *Act* can eliminate uncertainty regarding the treatment of foreign ownership while also ensuring that the *Act* provides maximum benefits to Canadians should that be its purpose.

Foreign Ownership of Firms in Mergers Reviewed by the Bureau

Whether or not a consumer welfare standard is justified on the basis of promoting the welfare of Canadians exclusively depends on whether the non-Canadian shareholders can be treated differently from Canadian shareholders under Section 96, and also on whether it is expected that a significant proportion of producer benefits in future mergers would accrue to non-Canadians. In other words, are the issues identified here relevant in practice? It is obviously impossible to forecast how much of future merger benefits will flow to non-Canadians because we cannot know what the shareholder composition by nationality of future mergers will be. We can, however, consider the ownership of firms involved in previous mergers reviewed by the Bureau and the current ownership of Canadian firms by non-Canadians.

Statistics on Foreign Ownership of Canadian Firms

According to a Statistics Canada publication,[70] in 2016, although 99.2% of enterprises in Canada were domestic, the remaining 0.8% of enterprises that were multinational enterprises ("MNEs") held 67% of the assets in the Canadian economy. Half of MNEs were majority Canadian-owned with foreign affiliates ("MOFAs") and these entities held 49% of assets in the Canadian economy. Non-Canadians are likely to have significant ownership interests in MNEs that are majority Canadian-owned. Foreign-majority owned MNEs with Canadian affiliates ("FMOCAs") held 18% of assets in the economy. According to another Statistics Canada report,[71] in 2019, 14.8% of assets in Canada were owned by foreign-controlled firms, and 27% of total operating revenues were earned by foreign-controlled firms.

We are not aware of research that estimates the foreign shareholdings of firms with operations in Canada. This would be a very complex task. Even most large firms that are majority Canadian-owned or Canadian-controlled are likely have significant foreign shareholding such that when these firms are involved in mergers a significant proportion of efficiency (and wealth transfer) benefits to the firms accrue to non-Canadians. For example, an expert for the Commissioner in *Rogers-Shaw* estimated that foreign shareholders would own 25.5% of a merged Rogers-Shaw firm,[72] even though both companies are Canadian-controlled and majority Canadian-owned.

Previous Merger Reviews by the Bureau

Many, and perhaps most, of the mergers recently reviewed by the Bureau have involved firms that are either majority-owned by foreign investors or have significant non-Canadian shareholdings. Between May 2018 and the end of 2021, the Bureau published Position Statements for nineteen mergers.[73] In thirteen of these mergers, both merging firms appeared to be majority-owned by foreign entities. Five mergers (MacEwen/Quickie, Federated Cooperatives/Blair's, CN/H&R, Metro/Jean Coutu, and TMR/AIM) involved firms that appeared to be primarily owned by Canadians, and one (La Coop Fédérée/Cargill) involved a largely Canadian-owned firm and a foreign-owned firm. Several of the merging firms that appear to be primarily Canadian owned also have substantial foreign ownership. For example, CN has significant non-Canadian ownership. The four largest shareholders of CN, including the Bill & Melinda Gates Foundation and three investment funds based in the US, combined own approximately 20% of CN, and other non-Canadian firms and institutions also had significant shareholdings.[74]

Superior Plus' proposed acquisition of Canexus in 2016 was cleared by the Bureau because it concluded that "efficiency gains would be clearly greater than the likely significant anticompetitive effects of the transaction".[75] In its response to Senator Wetston's consultation, the Bureau cited this case as an example of contrasting treatment of efficiencies in Canada and other countries, as the Bureau cleared this merger and yet the merger was challenged by the US agencies (and was ultimately abandoned because of the US challenge). Although Superior Plus and Canexus were Canadian companies, they appear to have had significant non-Canadian shareholdings at the time of the proposed merger. In 2016, at least 25% of the shares of Superior Plus were owned by investment funds and similar entities that were based outside of Canada, and therefore presumably had mainly non-Canadian investors.[76] The funds included The Vanguard Group, Norges Bank Investment Management, Dimensional Fund Advisors LP, and Grantham Mayo

Van Otterloo & Co. LLC. Canexus appears also to have been about 25% non-Canadian owned in 2016, with significant foreign shareholdings by CM-CIC Asset Management Société anonyme of France and Dimensional Fund Advisors LP among others.[77] It is not clear if the Bureau discounted the merger efficiencies that would accrue to foreign shareholders when assessing whether efficiencies outweighed the anti-competitive effects of the merger.

If history is a guide and future mergers are expected to continue to involve firms with significant non-Canadian shareholdings—and there is no reason to think otherwise—and if discrimination against foreign shareholders in not feasible, a consumer welfare standard may better achieve the goal of maximizing the benefit of Canadians assuming some of the producer efficiencies from mergers will be captured by foreign shareholders of the merging firms.

Conclusions

Merger efficiencies that reduce the costs of operations located in Canada may benefit 'the Canadian economy', but they generally only provide net benefits to Canadians if the increase in firm profits that result from cost reductions flow to Canadians through their claims on the profits of merging firms. Efficiencies from a merger of foreign-owned firms that results in the redeployment of now-redundant resources to another sector of the Canadian economy increase the output of the Canadian economy but do not necessarily increase surplus that flows to Canadians. A merger of firms with substantial foreign ownership that results in substantial efficiencies but increases prices to Canadians therefore transfers wealth from Canadians to non-Canadians. This harm to Canadians to the benefit of non-Canadians is an inevitable outcome of the non-discrimination rule in *Superior Propane Redetermination* if a merger between firms with significant foreign shareholdings is allowed because of the efficiencies defence. If Canadian merger law is to maximize the benefits of mergers to Canadians, then it should discriminate against foreign shareholders in favour of Canadians. If Canada's national treatment obligations prevent discrimination on a case-by-case basis, then a potential approach is a blanket consumer welfare standard which discounts producer benefits regardless of nationality so long as future mergers are expected to involve firms with significant foreign shareholdings. If discrimination against foreign shareholders on a case-by-case basis is feasible, then the fourth filter in *Tervita*, which counts only merger cost reductions that flow to Canadians through their shareholdings of the merging firms, whether or not rationalized facilities are located in Canada,

could instead be applied. Future amendments present an opportunity to amend and clarify the *Act* to resolve the current ambiguity with respect to the treatment of foreign shareholders and ensure that the enforcement of the merger provisions benefit Canadians.

ENDNOTES

[1] Andy Baziliauskas, Principal, and Lisa Stockley, Associate Principal, are both PhD economists specializing in matters of antitrust and competition at Charles River Associates. The opinions and conclusions expressed in this article are solely those of the authors and should not be attributed in any way to any other individual or organization. The authors would like to thank Margaret Sanderson, Frank Mathewson, and the referees of the CCLR—Dimitri Dimitropoulos and Ian Cass—for their valuable comments, as well as Rahim Lila and Matthew Cormier for their assistance in editing draft proofs. Any remaining mistakes are our own.

[2] Economic Council of Canada, *Interim Report on Competition Policy* (Ottawa: The Queen's Printer, July 1969) at 19, online: *Government of Canada* <publications.gc.ca/collections/collection_2018/ecc/EC22-12-1969-eng.pdf>.

[3] Government of Canada, "Competition Bureau Canada" (last modified 16 March 2023), online: *Innovation, Science and Economic Development Canada*, online: <ised-isde.canada.ca/site/competition-bureau-canada/en>.

[4] *Competition Act*, RSC 1985, c C-34, s 1.1.

[5] As we explain below, the treatment of efficiencies benefits that accrue to foreign shareholders in *Superior Propane* differs from treatments in more recent cases where the issue was *obiter*, so the ultimate resolution of this issue is unclear.

[6] Edward M Iacobucci, "Examining the Canadian *Competition Act* in the Digital Era" (27 September 2021), online: *Senate of Canada* <sencanada.ca/media/368377/examining-the-canadian-competition-act-in-the-digital-era-en-pdf.pdf>.

[7] Competition Bureau, "Examining the Canadian *Competition Act* in the Digital Era, Submission by the Competition Bureau" (8 February 2022), online: *Innovation, Science and Economic Development Canada* <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04621.html>.

[8] *Ibid.*

[9] US Department of Justice and US Federal Trade Commission, *Horizontal Merger Guidelines*, (Guidelines), (2010), 30-31, online: *US Department of Justice* <http://www.justice.gov/sites/default/files/atr/legacy/2010/08/19/hmg-2010.pdf>.

[10] It is worth noting that the heads of the US agencies under the Biden administration have indicated that focus on the consumer welfare standard (and the narrow technical exercise involved in its application) may be misguided given the purpose of antitrust is to protect "competition". See e.g. Department of Justice, "Antitrust Enforcement: The Road to Recovery", (Remarks delivered by Assistant Attorney General Jonathan Kanter), (University of Chicago Stigler Center, 21 April 2022), online: *US Department of Justice* <http://www.justice.gov/opa/

speech/assistant-attorney-general-jonathan-kanter-delivers-keynote-university-chicago-stigler>.

[11] For a robust defence of the consumer surplus standard in the US, see Russell Pittman, "Consumer Surplus as the Appropriate Standard for Antitrust Enforcement" (2007) US Department of Justice, Antitrust Division, Economic Analysis Group Discussion Paper No EAG 07-9.

[12] *The Commissioner of Competition v CCS Corporation et al*, 2012 Comp Trib 14 [*Tervita CT*].

[13] *Tervita Corp v Canada (Commissioner of Competition)*, 2015 SCC 3 [*Tervita*].

[14] The Bureau's Merger Enforcement Guidelines, since the first version in 1991, also adopt a total welfare standard. See Director of Investigation and Research, Information Bulletin No 5, "Merger Enforcement Guidelines" (March 1991) 49-50, online: *Innovation, Science and Economic Development Canada* <publications.gc.ca/collections/collection_2021/isde-ised/RG54-2-5-1991-eng.pdf>.

[15] For an explanation of the balancing weights standard, see Roger Ware and Ralph A Winter, "Merger Efficiencies in Canada: Lessons for the Integration of Economics into Antitrust Law" (2016) 61:3 The Antitrust Bulletin 365.

[16] If there are delays in or transition costs associated with the redeployment of released resources in Canada, the benefits of efficiencies to the Canadian economy are less than the direct cost reductions.

[17] Some share of profits of foreign shareholders that is subject to Canadian corporate income taxes will be re-captured by Canadians. See e.g. *Canada (Commissioner of Competition) v Rogers Communications Inc and Shaw Communications Inc*, 2023 Comp Trib 1 at para 83, aff'd 2023 FCA 16, (Expert Report of Roger Ware). Additionally, some profits may be reinvested in ways that can, in theory, benefit Canadians as well.

[18] Conversely, if efficiencies are reductions in costs of operations located in another country, then they may make the other country's economy more efficient if released resourced are redeployed in that country, but if the firm has Canadian shareholders some of the benefits of these efficiencies flow to Canadians.

[19] When merging firms have a mix of Canadian and non-Canadian shareholders, it can be extremely difficult not only to sort shareholders into Canadian and non-Canadian, but also to identify which firm's shareholders benefit from efficiencies. This commentary does not discuss this complication in any detail. It is sufficient for the purposes of the argument to assume that a significant proportion of increased profits from merger efficiencies and wealth transfers flow to non-Canadians and the harm to consumers from merger price increases is borne mainly by Canadians.

[20] Below we provide a simple example in which foreign-owned merging firms release workers at Canadian operations. The merging firms produce the same amount of output with fewer workers, and the workers are redeployed elsewhere in the Canadian economy. The redeployment of these workers expands the output of the Canadian economy, thereby making it more efficient, but the benefits of

this redeployment accrue to foreign shareholders in the form of lower costs, and therefore higher profits.

[21] This would be consistent with the Tribunal's fourth filter in *Tervita CT*, which "filters out claimed efficiency gains that would be achieved outside Canada and would not flow back to shareholders in Canada as well as any savings from operations in Canada that would flow through to foreign shareholders": *Tervita CT*, *supra* note 12 at para 262). Other Tribunal decisions have questioned whether such discrimination is possible under Canada's international treaty obligations. We discuss this in more detail below.

[22] For example, as discussed below, *Canada (Commissioner of Competition) v Superior Propane Inc*, 2002 Comp Trib 16, 18 CPR (4th) 417, aff'd 2003 CAF 53 [*Superior Propane Redetermination*].

[23] For example, through a balancing weights approach that partially or fully discounts harms and benefits that accrue to non-Canadians.

[24] In this commentary we ignore the fact that in many mergers reviewed by the Bureau, some of the consumer harms may be borne by non-Canadians. Such harms should be discounted as anti-competitive effects if a total surplus standard is applied. The Commissioner argued, and the Tribunal agreed, that the portion of the transfer to foreign consumers should be excluded from the section 96 analysis in *Superior Propane Redetermination*, *supra* note 22 at paras 192 and 198.

[25] A merger may also result in other inefficiencies, such as productive inefficiencies, reductions in product quality, or dynamic inefficiencies through a reduction in (or slowing down of) innovation. For further discussion of such other inefficiencies, see e.g. Matthew Chiasson and Paul A Johnson, "Canada's (In)Efficiency Defence: Why Section 96 May Do More Harm than Good for Economic Efficiency and Innovation" (2019) 32:1 CCLR 1.

[26] Efficiencies may also take the form of an increase in the quality of goods and services supplied to consumers at the same production cost, as well as dynamic efficiencies through increased investment in innovation. For further discussion of such other efficiencies, see e.g. Brian Facey and David Dueck, "Canada's Efficiency Defence: Why Ignoring Section 96 Does More Harm than Good for Economic Efficiency and Innovation" (2019) 32:1 CCLR 33.

[27] Cost reductions that release resources that are not redeployed elsewhere in the economy are not cognizable efficiencies because they do not result in an increase in economic output. For example, if a firm releases workers who are unlikely to be employed elsewhere in the economy, then the reductions in labour cost are not cognizable efficiencies. If the workers are likely to remain unemployed for, say, one year, then one year's worth of labour costs are not cognizable efficiencies.

[28] Note that cost reductions that are not the result of a reduction in the use of resources in production are not recognized as efficiencies. For example, cost reductions from increased bargaining power with input suppliers are simply a transfer from input suppliers to the merging firms, and do not reduce the use of resources. These types of costs are synergies, and partly explain why in some cases the synergies announced by merging firms exceed claimed efficiencies.

[29] Government of Canada, "Canada's Cost-Benefit Analysis Guide for Regulatory

Proposals" (last modified 29 March 2022), s 1, online: *Government of Canada* <http://www.canada.ca/en/government/system/laws/developing-improving-federal-regulations/requirements-developing-managing-reviewing-regulations/guidelines-tools/cost-benefit-analysis-guide-regulatory-proposals.html>.

[30] Government of Canada, "Policy on Cost-Benefit Analysis" (last modified 29 March 2022), s 6.1.3, online: *Government of Canada* <www.canada.ca/en/government/system/laws/developing-improving-federal-regulations/requirements-developing-managing-reviewing-regulations/guidelines-tools/policy-cost-benefit-analysis.html#toc6>.

[31] See e.g. Congressional Research Service, *Cost Benefit Analysis in Federal Rulemaking*, (8 March 2022), online: *Congressional Research Service* <crsreports.congress.gov/product/pdf/IF/IF12058#:~:text=Cost-benefit%20analysis%20involves%20describing,and%20otherwise%20in%20qualitative%20terms>:"Since the 1970s, federal agencies have been required to consider the costs and benefits of certain regulations that are expected to have large economic effects. Under current requirements, most agencies are to design regulations in a cost-effective manner and ensure that the benefits of their regulations justify the costs."

[32] Under the Kaldor-Hicks criterion that underlies cost-benefit analysis, a decision is economically efficient if the winners from a policy change could hypothetically compensate the losers and still be better off from the change. This criterion does not require the winners to actually compensate the losers, only that the amount that winners gain exceeds the amount of harm to the losers, such that overall gains exceed overall losses. In principle, the government could undertake such compensation through wealth transfers *via* income taxation.

[33] Economists typically estimate non-monetary gains and losses to individuals by estimating either compensating variation ("CV") or equivalent variation ("EV"). CV measures the amount of dollars that would have to be given to (or taken from) an individual to allow her to be as well off with the project under consideration as she was in the status quo. The EV is the amount that a consumer would pay to avoid a change. CV and EV often only differ only by a relatively small 'income effect'.

[34] Oliver Williamson, "Economies as an Antitrust Defense: The Welfare Tradeoffs" (1968) 58:1 Am Economic Rev 18.

[35] There are some effects that are more difficult to quantify. This does not mean they are unquantifiable. We leave aside the question of how to deal with difficult-to-quantify effects in this commentary.

[36] Some portion of higher profits may be captured by taxes transferred to the Canadian governments or investments that may benefit Canadians.

[37] The shareholders of non-merging firms also benefit if their prices also increase.

[38] If the direct buyers of the relevant product use the product as an input into the production of products that are sold in downstream markets and direct buyers pass-through post-merger prices to downstream consumers, then some of the harm is borne by these downstream consumers.

[39] This value need not be constant as is implied by the simplified equation in this

sentence. Economists have tools for estimating the size of this deadweight loss when the subjective value of the good is differentiated across consumers.

[40] Again, for the purposes of this commentary we ignore other forms of inefficiencies and efficiencies, such as those described in footnotes 25 and 26, that could result from a merger.

[41] As noted above, some profits accruing to foreign shareholders will be captured by Canadians through corporate taxes.

[42] As noted above, identifying which firm's shareholders benefit from efficiencies and wealth transfers can be very complex. We ignore this complexity in our commentary. It is sufficient for our claim that a substantial proportion of merger efficiencies in the future accrue to non-Canadian shareholders.

[43] The in-line hypothetical addresses efficiencies that may be considered 'marginal' in so far as the change in the use of the redeployed input is not substantial enough to change the overall market conditions of any other industry. This may not always be the case. In some mergers, the volume of redeployed resources may be substantial enough to, say, impact the market dynamics in another industry which can create additional efficiencies or inefficiencies to be taken into account in a well-defined trade-off analysis.

[44] In competitive markets there is no consumer surplus on the last unit of the good sold. In fact, this is a defining feature of allocative efficiency. Adding an additional resource to a competitive output market, such as the single redeployed worker in our example, would have such a small impact on the total market size that the output price would not adjust and the consumer expected to purchase the incremental output would also receive zero surplus (i.e., he is indifferent between buying and not buying the product).

[45] Adding the $50,000 in value created by the worker in her new employment to the $50,000 in cost savings achieved by the merging firm would amount to double counting. If the redeployment of the worker does create some new economic surplus in her new employment, this surplus should be included in the efficiencies calculation. To our knowledge, such incremental surplus has never been added in an efficiencies analysis.

[46] As noted above, redeployment delays and transition costs may further reduce the economic surplus resulting from cost reductions.

[47] In this case, the worker's surplus is reduced by $10,000 because her compensation is now lower. Before the merger, she traded her labour for $50,000 and received some amount of gains from that trade (i.e., surplus). After the merger, she trades her labour for $40,000 and thus receives $10,000 fewer gains from that trade, making her surplus from selling her labour $10,000 lower. The net overall surplus change from the merger is the $50,000 in cost savings to the merging firm (which is new producer surplus) less the worker's surplus loss of $10,000.

[48] We note again, however, that any delays and transition costs associated with redeploying resources in Canada should be netted out of any reductions at the firms' operations.

[49] As noted above, even cost reductions on Canadian operations do not

necessarily expand the output of the Canadian economy. For example, if Canadian head office cost reductions involve the release of senior executives and these executives go on to work in other countries, they expand the output in other countries, not Canada.

[50] If these multiplier benefits exist and are included in the trade-off, then any negative multiplier effects from reducing resource deployment in the operations of the merging firms must also be considered.

[51] *Canada (Commissioner of Competition) v Rogers Communications Inc and Shaw Communications Inc*, 2023 Comp Trib 1, aff'd 2023 FCA 16 [*Rogers-Shaw*].

[52] *Ibid*, (Final Written Argument of the Commissioner of Competition) at para 154.

[53] *Rogers-Shaw*, *supra* note 51 (Respondent's Final Arguments) at Appendix 2, Response to Question 6.

[54] *Ibid.*

[55] *Ibid*.

[56] *Ibid*.

[57] *Rogers-Shaw*, *supra* note 51, at para 410.

[58] *Superior Propane Redetermination*, *supra* note 22 at para 192.

[59] *Ibid*.

[60] "A "total Canadian welfare standard" as defined by Professor Ross may or may not be discriminatory under Canada's international obligations, but the Act is not. In the Tribunal's understanding, those obligations require "national treatment" in the application of Canadian laws." See *Superior Propane Redetermination*, *supra* note 22 at para 197).

[61] *Ibid* at para 196.

[62] *Tervita CT*, *supra* note 12 at para 262.

[63] In *Parrish & Heimbecker*, the Tribunal stated the screen in *Tervita* somewhat differently, as "[t]he claimed gains in efficiency must not be achieved outside Canada and must instead flow back to Canadian shareholders. Under this fourth screen, savings from operations in Canada that would flow through to foreign shareholders are eliminated." See *Canada (Commissioner of Competition) v Parrish & Heimbecker, Limited*, 2022 Comp Trib 18 at para 657. While the Tribunal's statement in Tervita appears to clearly allow for the inclusion of efficiencies on foreign operations that flow back to Canadian shareholders, the Parrish & Heimbecker statement appears to be more ambiguous in that it says that 'claimed efficiency must not be achieved outside Canada', although the 'must instead flow back to Canadian shareholders' (emphasis added) language creates some ambiguity.

[64] As discussed above, although the Bureau assesses whether a merger is likely to result in an SLPC based on whether final consumers are Canadians or firms who purchase the relevant products are based in Canada, any harms from price increases may be borne by non-Canadians to the extent that buying firms based in Canada are owned by non-Canadians or the buying firms pass through price increases to their downstream customers. We assume for the purposes of this commentary that all harms are borne by Canadians, or at least that the proportion

of harms that are borne by Canadians exceeds the proportion of producer benefits that accrue to Canadians.

[65] Given a demand elasticity of 1, a 10% increase in price leads to a 10% decrease in quantity. Thus, firms produce and consumers purchase 100,000 fewer units (10% of 1,000,000). The post-merger price is $10 per unit higher than the pre-merger price and, assuming a linear downward sloping demand curve, the consumer DWL is calculated as (100,000 x $10)/2 = $500,000. The pre-merger variable margin was assumed to be a constant $30 per unit (30% of each $100 unit) and as such, the producer DWL is calculated as (100,000 x $30) = $3,000,000. There would also be a wealth transfer from the remaining consumers to the producers as a result of the increased price of (900,000 x $10) = $9,000,000.

[66] The portion of the producer DWL borne by non-Canadian shareholders would also be given zero weight.

[67] There is no publicly available evidence indicating that the Bureau has argued that efficiencies should be discounted in the trade-off because some of the benefits of efficiencies would flow to non-Canadian shareholders. As noted above, in *Superior Propane* the Bureau did argue that in some circumstances the wealth transfer could be discounted if the merging firms are owned by foreigners, but to our knowledge the Bureau has never explicitly argued that the portion of increased profits from merger efficiencies that flows to non-Canadian shareholders should be discounted in any way. In *Rogers-Shaw*, the Bureau also argued that the portion of the wealth transfer that accrues to foreign shareholders is socially adverse (see *Rogers-Shaw*, *supra* note 51, (Final Written Argument of the Commissioner of Competition) at para 154) but did not claim that the portion of efficiencies that accrues to foreign shareholders should be discounted.

[68] As discussed above, in *Superior Propane Redetermination*, the Tribunal found that only efficiencies on Canadian operations can be counted as a benefit of a merger.

[69] *Superior Propane Redetermination*, *supra* note 22 at para 196.

[70] Statistics Canada, *Multinational Enterprises in Canada*, (1 April 2019), online: *Statistics Canada* <www150.statcan.gc.ca/n1/pub/11-621-m/11-621-m2019001-eng.htm#a2>.

[71] Statistics Canada, *Foreign-controlled enterprises in Canada, by financial characteristics and selected country of control*, (31 January 2022), online: *Statistics Canada* <www150.statcan.gc.ca/t1/tbl1/en/cv.action?pid=3310008401>.

[72] *Rogers-Shaw*, *supra* note 51 (Expert Report of Lars Osberg) at para 11.

[73] Government of Canada, "Position statements regarding concluded merger reviews" (last modified 20 January 2022), online: *Competition Bureau* <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/h_04449.html>.

[74] CNN Business, "Canadian National Railway Co", online: *CNN Business* <money.cnn.com/quote/shareholders/shareholders.html?symb=CNI&subView=institutional>.

[75] Competition Bureau, "Examining the Canadian Competition Act in the Digital Era, Submission by the Competition Bureau" (8 February, 2022), online:

Competition Bureau <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04621.html>.

[76] S&P Capital IQ via S&P Global Market Intelligence.

[77] *Ibid.*