

**COMMENTS OF THE ABA SECTIONS OF ANTITRUST LAW AND
INTERNATIONAL LAW TO THE CANADA COMPETITION BUREAU'S
DISCUSSION PAPER FOR THE MERGER ENFORCEMENT GUIDELINES
CONSULTATIONS**

December 22, 2010

The views stated in this submission are presented jointly on behalf of these Sections only. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and therefore may not be construed as representing the policy of the American Bar Association.

The Sections of Antitrust Law and International Law (“Sections”) of the American Bar Association (the “ABA”) are pleased to submit these comments to the questions posed by the Canada Competition Bureau (the “Bureau”) in its Discussion Paper for the Merger Enforcement Guidelines Consultations (“Discussion Paper”). The Sections endorse the Bureau’s initiative to explore whether to revise the Merger Enforcement Guidelines (“MEGs”) and applaud its invitation for public comments. The Bureau identifies appropriate potential reasons to update the MEGs: to reflect Bureau merger review practices more accurately; to incorporate developments in the law or economics since the MEGs’ 2004 release; and to implement necessary clarifications or fundamental changes where, if at all, they are needed. The Sections appreciate the opportunity to participate in this process.¹

The current MEGs provide a concise and straightforward explanation of the analytical principles and methods that comprise the Bureau’s framework for review. The Sections recommend that the Bureau retain this concise structure when incorporating any

¹ The Sections submit these comments based on learning and experience developed in numerous prior opportunities to address merger policy initiatives by many international antitrust/competition authorities. For example, in the past thirteen months, the Section of Antitrust Law submitted two rounds of comments to the U.S. Department of Justice and Federal Trade Commission, as part of the process leading up to their joint issuance of the 2010 Horizontal Merger Guidelines. <http://www.abanet.org/antitrust/at-comments/2009/11-09/P092900.shtml>; http://www.abanet.org/antitrust/at-comments/2010/06-10/2010_hmg.shtml. Similarly, in August 2009 and May 2010, the Sections jointly submitted rounds of comments to the U.K. Competition Commission and Office of Fair Trade, in connection with the development of their 2010 Mergers Assessment Guidelines. http://www.abanet.org/antitrust/at-comments/2009/08-09/intl_law-fair_trading.shtml; http://www.abanet.org/antitrust/at-comments/2010/05-10/2010_draft_merger.shtml. The U.S. and U.K. merger policy projects raised many of the same issues of merger analysis also found in the Discussion Paper. As a consequence, the Sections’ comments substantially reflect comments previously provided in the submissions to the U.S. and U.K. authorities.

revisions to the MEGs. The Sections welcome transparency from the Bureau and respectfully submit that further explication of principles and the provision of examples should be accomplished in a way that is consistent with the current MEGs' clarity and concision. The Sections also observe that "backgrounders" and other public statements can serve as useful vehicles for informing the public about the practical application of the framework of principles articulated in the MEGs.

1. The MEGs provide that, typically, the first stage in the Bureau's review of a merger involves defining the relevant market in which the merging parties operate, followed by a determination of market share(s) and concentration, and then a competitive effects analysis. Should the Bureau consider:

a. revising the MEGs to shift emphasis away from the detailed assessment of market definition and more towards a direct assessment of competitive effects?

The MEGs suggest that Bureau merger review usually follows a pre-determined analytical path. This is reflected by statements that "[t]ypically, the first stage" of a review is market definition (§ 3.1), that "the next step" is the identification of market participants followed by market share calculation (§ 4.1), and that competitive effects analysis occurs when the foregoing steps (or other information) suggest that the merger may substantially lessen or prevent competition (§ 5.1). The Sections endorse the inclusion of a statement in the MEGs that Bureau merger review does not need to proceed along this, or any, pre-determined ordering of analytical steps. Rather, the Bureau's review should proceed in a case-specific manner.

For example, in some cases, before all the facts applicable to market definition are discovered and market definition analysis can be completed, the Bureau may have more readily at hand information with which to make a more direct assessment of likely competitive effects. In those situations, market definition need not be the "first stage" of the analysis. By contrast, in other cases, where market definition is simple, relevant facts are readily available, and no structural concerns are evident because of low concentration levels, it may be unnecessary for the Bureau to conduct a competitive effects analysis.

Accordingly, market definition and competitive effects are not analytical substitutes. The Sections do not endorse the view that the Bureau should change the MEGs to "shift emphasis away from a detailed assessment of market definition." To the contrary, the Sections recommend that the Bureau reaffirm in the MEGs that market definition is an indispensable element of any decision to *challenge* a transaction – including in cases for which facts and economic tools are available to enable the Bureau to assess competitive effects more directly.² Rigorous application of the market definition exercise helps to ensure that the Bureau will identify the competitive

² In cases where the Bureau chooses not to challenge a transaction, market definition can still be of utility in structuring a review, but a final finding regarding the appropriate market need not always be made if a transaction has no likelihood of harming competition in any product or geographic market no matter how defined.

alternatives available to consumers and determine the individual and collective importance of those alternatives. A reduced emphasis on market definition would risk a weakening of the Bureau's ability to ascertain these factors, which are critical for any reasoned prediction about a merger's likely effects on consumers.

This holds true whether predicted effects are unilateral or coordinated. The analytical tools that the Bureau uses to evaluate unilateral effects typically require numerous judgments and estimates, such as the selection of the competitive model, estimation of variables, and assessments of issues such as entry and repositioning. A conclusion drawn from a direct assessment of competitive effects that cannot be reconciled with (or is counter-intuitive to) reasonable inferences from a well-defined product and geographic market is less reliable than if these tools are integrated within the contours of a relevant market. Similarly, a determination that the merging parties are the major or even the only competitors in a market should not obviate the need for a distinct unilateral competitive effects analysis.

A policy to continue to require market definition analysis will strengthen the Bureau's ability to make the right decisions. It will also enhance transparency by furthering the ability of counsel and the business community to assess more accurately the Bureau's potential analysis of transactions. Market definition analysis provides structure to the merger review process, enables the Bureau and the merging parties to focus on common issues, and, if the case proceeds to litigation, provides the Competition Tribunal with a necessary concrete frame of reference for determining whether a merger will substantially lessen or prevent competition.

b. revisiting or expanding the use of “next best substitutes” and “smallest market principles” (paragraph 3.5) in the MEGs?

The concepts of “next best substitutes” and “smallest market principle” apply to the hypothetical monopolist test (“HMT”) for market definition articulated in ¶ 3.5 of the MEGs. The HMT locates the relevant product market through a process to identify the smallest collection of products (inclusive of at least one product of the merging parties) over which a hypothetical monopolist would impose and sustain a five percent price increase. If, as applied to the first candidate product grouping, the HMT does not show the existence of a relevant market, then the test is run again after the “next-best substitute” is added to the candidate market. The next-best substitute is “the product that would represent the greatest diversion in demand by buyers in response to the postulated price increase.” (MEGs n. 9.) This process continues iteratively, each time by adding the next-best substitute, until the HMT identifies the smallest set of products over which a hypothetical monopolist would charge and sustain a five percent price increase.

The Sections interpret this question as suggesting a potential departure in the MEGs from the next-best substitutes and smallest market principle paradigm. The Sections believe that these concepts should be retained, because they create a structure to the market definition exercise that facilitates predictability and reduces the risk of uncertainty and ambiguity. The Sections recognize that the 2010 Horizontal Merger Guidelines of the U.S. Department of Justice and Federal Trade Commission (hereinafter

"2010 U.S. Merger Guidelines") incorporate revisions to market definition analysis on these issues,³ and that the Bureau may be considering making similar revisions to the MEGs. If so, then the Sections respectfully suggest that the Bureau accompany any such changes with detailed guidance on how such revisions will change operation of the HMT and the market definition process. Such additional guidance could appropriately be provided in a publication other than the MEGs themselves.

The next-best substitutes concept provides guidance on when and how putative markets subject to the HMT are expanded. The smallest market principle gives guidance on when the expansion process should end. Both are important. Should the Bureau eliminate either from the MEGs, the Sections urge that the MEGs clarify and explain how markets should be defined. Otherwise, it may be difficult to choose between alternative defined markets that may satisfy the HMT yet differ in meaningful ways in regard to each market's participants (and their products).⁴ Ambiguity on this central question diminishes substantially the significance of market shares or concentration figures. Absent a means to select which among different markets is appropriate for a particular merger, the market definition exercise would potentially become less meaningful.

2. Should the Bureau consider revising the MEGs to provide more detail on the types and sources of evidence that Bureau considers in merger reviews, and the relative weight typically assigned to such evidence?

The MEGs refer to the factors that must be taken into account in determining whether a merger is anticompetitive, in accordance with section 93 of the *Competition Act* (the "Act"), but contain limited discussion on the specific types of information from which the Bureau draws inferences or bases conclusions. In this, the MEGs' approach is appropriate. Merger reviews are highly fact-specific, and an exhaustive list of the types of potentially useful evidence in merger reviews is not realistic. An extensive list of potential types of evidence could unintentionally cause some to misinterpret it as a type of evidentiary "checklist" applicable to all investigations.

In the Sections' view, the MEGs can usefully identify each of the types of evidence described in questions 2(a)–2(d) as examples of potentially useful information, but should largely remain focused on the general principles that the Bureau applies when assessing whether evidence obtained from different parties is credible, non-speculative and fact-based. The Sections further suggest that the MEGs clarify that all types of evidence from all types of parties are potentially relevant, and that relevance depends on the evidence's reliability, including the trustworthiness of its source.

³ Compare U.S. Department of Justice and Federal Trade Commission, 1992 Horizontal Merger Guidelines § 1 (1997) with 2010 U.S. Merger Guidelines § 4.

⁴ For example, in a hypothetical merger between two manufacturers of luxury automobiles, "North American luxury automobiles" and "Worldwide automobiles and motorcycles" may both satisfy the five percent test. Those two markets differ substantially in terms of market participants and concentration and may also have meaningful differences on relevant issues such as entry conditions or product repositioning.

The MEGs could usefully note that customers, competitors and other third parties, depending on the circumstances, may not always have incentives to provide full information or the ability to provide accurate information. Similarly, natural experiment evidence will provide value only if it is reliable and relevant to the transaction at issue, and documents may be more or less reliable and probative depending on when they were created, the extent of the authors' knowledge, and other case-specific circumstances.

More detailed and welcome guidance on the issues covered by questions 2(a)–2(d) can be set out in an Appendix to the text of the MEGs (as is currently done with the topic of sunk costs). In addition, the Bureau can elaborate on these issues through complementary publications such as speeches and technical backgrounders that explain the factual foundations for decisions in particular merger cases. With regard to the additional transparency on the specific types of evidence identified in questions 2(a)–2(d), the Sections respectfully submit the following observations:

a. evidence from customers, competitors and other third parties about how they will respond to and be affected by the merger;

Information obtained from customers, competitors and other parties is often important to assessing the likely competitive effects of a merger. Depending on the circumstances, such evidence can also be susceptible to bias and influence from a wide range of factors that are unrelated to the competitive dynamics of the merger. Given the different contexts from which industry participants often provide information, the Bureau could usefully provide guidance on its approach to weighing evidence obtained from these discrete sets of groups.

b. the degree of competition among the merging parties;

The degree of competition between the merging parties can provide useful information for merger analysis, but this is just one element of a broader analysis.⁵ The Sections welcome enhanced transparency on how the Bureau assesses “degree of competition” and applies that evidence, particularly in mergers in dynamic markets. For example, elaboration on the circumstances in which market concentration might be less relevant, such as in bid markets or markets with low entry barriers, would be useful. In addition, the Sections encourage the Bureau to explain how it evaluates evidence of significant competition between the merging parties as part of an overall competitive analysis, and not merely in isolation as direct evidence of anticompetitive effects.

c. documents provided by the parties created prior to and following consideration of the proposed merger;

⁵ Also important, for example, are the likelihood of timely and sufficient entry by other firms, including through expansion or repositioning, as well as the nature and extent of change and innovation in the market, as set out in section 93 of the Act and any likely efficiencies, as set out in section 96 of the Act.

The Sections submit that the Bureau should evaluate all documents that can assist it in analyzing the competitive effects of a merger, no matter when the documents were created. The critical factors should be whether the documents are probative, credible and reliable. The MEGs draw distinctions based on the timing of documents in only a few instances.⁶ To the extent the Bureau bases such distinctions on general principles, a short description of those principles would facilitate transparency. To the extent the Bureau considers documents associated with a consummated merger differently from documents related to a pending merger, this should also be made clear.

d. evidence based on "natural experiments," such as comparisons of current prices in geographic markets where both merging parties are present to current prices in geographic markets where only one of the merging parties is present;

Competition agencies and, increasingly, courts frequently use natural experiments to shed light on the likely competitive effects of a merger. Additional guidance would be welcome in a publication ancillary to the MEGs on how such information is incorporated into a rigorous analysis, particularly in light of the potential for conflicting interpretations of many natural experiments.⁷ The Bureau could include guidance, for example, on how it determines which features of the natural experiment will be used as a proxy for the merger conditions, and on what changes in the market could occur after the merger that would weaken the inferences to be drawn from the comparison.

On the other hand, the subjects raised in questions 2(e) and 2(f) concern economic evidence, regarding which the Sections believe that further explanation in the text of the MEGs itself is warranted.

e. Should the Bureau provide more detail on the types and sources of evidence relating to the role of diversion ratios and price/cost margins in evaluating unilateral effects?

The MEGs contain very limited discussion of diversion ratios or price/cost margins⁸ – topics that are the subject of increased debate among antitrust practitioners regarding their use and value in merger analysis. The Sections encourage the Bureau to state in the MEGs the general conditions under which, in the Bureau's view, diversion

⁶ See MEGs, ¶¶ 3.14, 8.15 and 11.2.

⁷ See, e.g., the dissenting opinion of Pelletier, J.A., in *Commissioner of Competition v. Canada Pipe Company Limited*, 2006 FCA 236, in which Justice Pelletier disagrees with the Competition Tribunal's interpretation of the pricing of a product in different geographic markets.

⁸ The MEGs define diversion ratios (n. 66) and observe that diversion ratios can provide evidence of buyer-switching in response to relative price changes (¶ 5.15), and that diversion ratios can be used to determine whether products are next best substitutes (n. 28).

ratios are more or less likely to provide useful information about the competitive discipline that firms exert on each other.⁹ The MEGs could also be usefully expanded to include a short discussion of the circumstances under which diversion ratios can be estimated by looking at firms' relative market shares, as well as the circumstances under which an assumption of proportionate diversion is likely to under-estimate, or over-estimate, true diversion ratios.

It would also be appropriate for the MEGs to acknowledge that not all diversion ratio information needs to stem from quantitative analyses. Ordinary course of business experience (as may be reflected in the merging firms' internal documents) may speak to whether a firm's lost customers are more likely to switch to any one particular rival.

The Sections would also find it useful for the MEGs to provide additional discussion regarding price/cost margins, an area where the current MEGs are largely silent. Two specific areas merit particular attention. First, many have argued that high margins should not be considered in isolation when evaluating the likely competitive effects of a merger, but should instead be considered along with diversion ratios, fixed costs, and other evidence when assessing the extent to which a merger reduces competitive constraints.¹⁰ The Bureau's position should be clarified with respect to the relative weight (if any) it attaches to margins and the extent to which the Bureau believes that high margins are indicative of significant pre-existing market power.

A second issue relating to price/cost margins where the Sections believe further discussion in the MEGs would be useful relates to what is sometimes referred to as "critical loss analysis" debate. High margins have sometimes been pointed to as evidence that very few sales need to be lost to render a post-merger price increase unprofitable. On the other hand, economists have pointed out that a high pre-merger margin means that a post-merger price increase is unlikely to result in many lost sales.¹¹ It would be useful to know if the Bureau agrees with the U.S. Department of Justice and Federal Trade Commission, which have expressed a limited reliance on "critical loss" analyses.¹²

⁹ For example, diversion ratios are less likely to provide reliable information about competitive discipline when significant post-merger repositioning is likely, or when historical diversion ratios have been driven by something other than price increases (e.g., changes in consumer tastes) that are not properly predictive of future switching behavior in response to changes in relative prices.

¹⁰ See, e.g., Carl Shapiro, "The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years," *77 Antitrust Law Journal*, No. 1, 2010 (forthcoming).

¹¹ See, e.g., Daniel O'Brien and Abraham Wickelgren, "A Critical Analysis of Critical Loss Analysis," *71 Antitrust Law Journal*, 1612 (2003).

¹² See 2010 U.S. Merger Guidelines § 4.1.3 (stating that high pre-merger margins normally indicate a small predicted loss following a price increase, and thus a smaller recapture rate necessary to satisfy the hypothetical monopolist test).

The Sections also note that the MEGs include no discussion of how price/cost margins should be calculated. A discussion of what costs should, and should not, generally be included in these calculations, and the situations in which fixed (or joint) costs might appropriately be included in those calculations, would be helpful.

A separate but related subject that the Sections believe should be discussed either in the MEGs or elsewhere is the usefulness of using firms' commonly reported gross margin calculations as a readily available proxy for the margins that would ideally be used in the merger analyses.

f. Should the Bureau provide more detail on the types and sources of evidence relating to the role of product repositioning?

The MEGs' discussion regarding product repositioning is very limited. The Sections believe that the MEGs should highlight product repositioning as an important example of dynamic competition that is frequently not accounted for in static economic models of competition. This dynamic consideration can dramatically change the predictions of those static models. What may appear to be an anticompetitive merger could, once dynamic considerations such as repositioning are considered, end up posing far fewer (and perhaps no) competitive concerns.

In particular, product repositioning can dramatically affect diversion ratios. Consistent with our comment regarding 2(e), the Sections recommend that the MEGs acknowledge that when product repositioning is likely, historically observed (or estimated) diversion ratios may significantly overstate future diversion ratios, and thus significantly overstate the likely competitive effect of a merger.

Additional guidance would be useful regarding the different types of evidence that the Bureau typically considers in assessing the timing, likelihood, magnitude and likely effect of repositioning. Sometimes, in an industry, there has been little or no significant historical repositioning, but the industry also had not experienced a price increase of the nature that the Bureau is analyzing as a potential effect from a current-day merger. Explication would be welcome on the different inferences the Bureau may draw in such factual situations.

3. Significant and partial interests and interlocking directorships are addressed in various contexts in the MEGs. Should these discussions be consolidated and/or expanded?

The MEGs discuss (i) whether a minority investment or interlocking directorship constitutes a "merger" for the purposes of Part VIII of the *Act*¹³ and (ii) when

¹³ The Bureau will consider the acquisition of a minority interest as a "merger," as defined in section 91 of the Act, when it results in the establishment of "control over or significant interest" in a business. While subsection 2(4) of the *Act* defines "control" as the ability to elect more than 50% of the board of directors of a corporation or the right to more than 50 percent of the profits of a partnership, the term "significant interest" is not defined by the Act. The Bureau interprets the term to mean "the ability to materially

interlocking directorships could pose anticompetitive effects.¹⁴ The Sections recommend that the Bureau consolidate those discussions and dedicate a portion of the MEGs to a concise and more unified discussion of how the Bureau assesses the competitive effects of interlocking directorships and partial interests.

Should the Bureau dedicate a new section in the MEGs to partial interests and interlocking directorships, identification of the factors the Bureau considers when evaluating such investments and interlocks would be appropriate. The Sections recommend that the Bureau incorporate into the MEGS the “three main factors” that the Bureau has elsewhere identified as central to its analysis: (i) an “[a]bility to materially influence the economic behaviour of the business;” (ii) an “[a]bility to seek confidential information;” and (iii) “[c]hange[s] to incentives (or the change in the profit-maximizing function).”¹⁵ The Sections recommend, however, that any further discussion on how the Bureau assesses these factors in practice be placed in an appendix or be discussed in other publications such as “technical backgrounders.”

In addition, the Sections recommend that the Bureau consider including in the MEGs *de minimis* thresholds for interlocking directorates, similar to those found in Section 8 of the U.S. Clayton Act.¹⁶ The Sections also would welcome a brief

influence the economic behaviour of the business (including decisions relating to pricing, purchasing, distribution, marketing, investment, financing or the licensing of intellectual property rights).” MEGs ¶ 1.5. The Bureau defines an acquisition of significant interest with respect to directorships as a “sufficient level of representation on the board of directors of the corporation to materially influence that board.” *Id.* ¶ 1.7.

¹⁴ MEGs ¶¶ 1.5, 5.10. The MEGs state that “[i]n the absence of other relationships, a direct or indirect ownership of less than 10 per cent of the voting interest in a business does not generally constitute ownership of a ‘significant interest.’” MEGs ¶ 1.8 n.3. The Bureau frequently is called upon to consider partial interest investments and interlocking directorates. *See, e.g.*, Competition Bureau, Technical Backgrounder on the Acquisition of Sogides Ltee by Quebecor Media Inc. (2006), available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02032.html>; Competition Bureau, “Competition Bureau Review of Cinema Mergers Opens the Door to Competition” (Apr. 22, 2002), available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/00401.html>. Other notable matters include the Kingdom Hotels International and Colony Capital’s 2006 acquisition of Fairmont Hotels, and Torstar’s 2006 acquisition of a partial interest in Bell Globemedia.

¹⁵ OECD, Policy Roundtables, Minority Shareholdings (2008), at 103-04 (outlining the factors the Bureau considers when assessing the likely competitive effects of partial interest investments and interlocking directors and discussing multiple considerations relevant to assessing the identified factors).

¹⁶ 15. U.S.C. § 19(a)(2).

description in the MEGs about whether the Bureau analyzes partial acquisitions of assets or economic interests any differently from partial acquisitions of voting equity.¹⁷

4. Should the Bureau consider expanding the discussion of unilateral effects in the MEGs to include more detail regarding:

a. bargaining and auction models;

Bargaining and auction models can provide important insights into the likely competitive effects of a merger. Given the complexities associated with the use of such models, however, the MEGs realistically can provide little detailed guidance on the models' use, other than potentially to list them as one source of evidence that may be used in appropriate circumstances. Moreover, these are only two of the many different types of economic models that may be informative in a merger review. In the Sections' view, other than by referring to bargaining and auction models in this limited manner, the MEGs should not place undue emphasis on them. The Bureau could provide important insight into how it applies such models in publications other than the MEGs or in a concise appendix.

The Sections also urge that any discussion of bargaining and auction models, or any other type of economic model or simulation, include the caveat that such models necessarily reflect highly simplified assumptions about likely conduct in a complex world. Generally, such models would be but one element of a larger, more detailed assessment of the potential unilateral effects of a proposed merger.

b. when considering differentiated products whether the products of merging parties should be first and second choices of a significant number of buyers; and/or

The extent to which buyers view the merging parties as their first and second choices determines the diversion ratio between the merging parties. Diversion ratios can be important to understanding how the merging firms provide competitive discipline to each other. As discussed in response to question 2(e), however, diversion ratios are not

¹⁷ For example, the U.S. Antitrust Guidelines for Collaboration Among Competitors explain, with respect to financial interests, that “[t]he potential impact may vary depending on the size and nature of the financial interest (e.g., whether the financial interest is debt or equity). In general, the greater the financial interest in the collaboration, the less likely is the participant to compete with the collaboration [T]he analysis is sensitive to the level of financial interest in the collaboration or in another participant relative to the level of the participant’s investment in its independent business operations in the markets affected by the collaboration.” U.S. Dep’t of Justice and FTC, Antitrust Guidelines for Collaboration Among Competitors ¶ 3.34(c) (2000), *available at* <http://www.ftc.gov/os/2000/04/ftcdojguidelines.pdf>.

always easily estimated. Historical evidence regarding diversion ratios may not be an accurate predictor of post-transaction diversion, particularly in dynamic industries.

The Sections recommend that a revision to the MEGs regarding diversion ratios and, by extension, the extent to which the merging parties' products are first and second choices for buyers, be limited to a brief discussion on whether the Bureau believes a certain proportion of customers must view the merging parties' products to be first and second choices for adverse unilateral effects to be likely. Alternatively, the MEGs might describe the factors (e.g., margins) the Bureau believes may raise (or lower) competitive concerns for a given share of buyers that view the merging parties' products as their first and second choice.

More detailed discussion of these issues is welcome, but the Sections believe it would be most beneficial either in an appendix or in publications ancillary to the MEGs. Such additional discussion would include the possible problems associated with trying to assess the degree to which buyers perceive the products of the merging firms as the first and second choices would be useful. For example, the Sections believe it would be useful for the Bureau to acknowledge that over-reliance on static or backward-looking information (such as win/loss data) when undertaking differentiated product analysis can be misleading, and that it is important to incorporate dynamic, mitigating factors such as repositioning.

The MEGs' recognition (e.g., in paragraph 5.16) that repositioning is an important factor in merger analysis is helpful, and should remain. The Sections would also welcome specific and detailed guidance from the Bureau to supplement the MEGs references to repositioning and perhaps address several other points. For example, the differences among suppliers and their products that make them "differentiated" can take a wide variety of forms. Moreover, the same dynamic in which such differences emerged, i.e., as firms reacted to conditions in the marketplace, may lead to modification of the differences – "repositioning" – in response to a merger. Competitive responses can include new product introductions, modification of existing products, or more effective marketing of differentiating features to particular customers. In addition, customers can prompt repositioning through adjustments in their purchasing preferences or by communicating to suppliers how they can win the customer's business. "Repositioning" in its various forms is ubiquitous, especially in the types of markets to which differentiated products analysis applies. Competitor responses are important reasons why many mergers in such markets do not raise significant competitive.

c. merger simulation that may include demand estimation, upwards pricing pressure or diversion ratio analysis.

The Sections do not believe that the MEGs should suggest that any particular type of quantitative analysis is a necessary element of merger analysis. Rather, the merits of a particular analysis need to be assessed according to the specific facts of the market. The MEGs can help to elucidate the circumstances under which different types of quantitative analyses are more likely to be appropriate.

The Sections recommend expanded discussion in the MEGs regarding the circumstances under which different types of quantitative analyses are most likely to be given significant weight and how the authorities will generally assess the reliability of those models. The U.S. agencies, for example, have indicated that they are much more likely to credit models (and their predictions) that provide generally robust conclusions across a variety of alternative assumptions. Presumably this is also a criterion for the Bureau, and as such, a disinclination to credit non-robust models should be made clear.

It also would be helpful for the Bureau to describe the relative weight it gives to such quantitative analyses, particularly when the model results suggest conclusions different from documents or statements. The Sections recommend that the MEGs emphasize that tension between bodies of evidence does not call for simply choosing one type of evidence over another. Rather, such tensions more likely suggest that evidence is not being correctly developed or interpreted. Tension between documents and quantitative analyses may suggest that the economic models need to be scrutinized to determine if important economic forces are being ignored or incorrect assumptions applied, or that the documents are being misinterpreted or are untrustworthy. Ultimately, economic models and other sources of evidence (including, for example, market definition and concentration statistics) should suggest consistent conclusions about the likely competitive effects of a merger.

It would be useful for the Bureau to acknowledge that most quantitative models incorporate necessary simplifications, a result of which may be that a model fails properly to capture potentially important economic factors such as repositioning, entry, innovation, or cost savings.¹⁸ It would be useful for the Bureau to identify the types of validation tests the Bureau believes such models must pass before being given significant weight.¹⁹

5. Is the discussion of coordinated effects in the MEGs sufficient, or should the Bureau consider providing in the MEGs some further discussion of how the Bureau assesses potential harm from coordinated exercises of market power?

The 2004 update to the MEGs substantially modernized the Bureau's approach to the analysis of coordinated effects, consistent with the approach used in several other jurisdictions, including the United States. The existing discussion of coordinated effects provides a useful analytical framework that engenders predictability.

¹⁸ Models may also fail to capture important economic characteristics such as asymmetric information, switching costs, or reputation considerations. Depending on the industry, such market characteristics can be critical, and can thus significantly affect the reliability of predictions coming from simplified economic models.

¹⁹ Validation tests might include, for example, the requirement that conclusions be relatively robust to a variety of alternative, yet equally plausible, modeling assumptions, or that the model be able accurately to predict key economic values (e.g., prices, margins or market shares) that are observed in the real world.

The Sections believe that it would be helpful for the Bureau to supplement the MEGs' existing discussion of coordinated effects with a discussion of how the likelihood of coordinated effects depends on the interplay of several different factors. This interplay means that no single market characteristic is likely to be dispositive with respect to the likelihood of coordination, and thus a competitive effects analysis should not focus on any single, or limited set of, market characteristics. Similarly, depending on the interplay with other factors, a particular market characteristic might end up being viewed as making coordination either more or less likely.

For example, consider firm cost symmetry. The MEGs assume that symmetry in cost structures or size is a factor facilitating the formation of a coordinated understanding.²⁰ Considering this factor in isolation, however, does not contemplate that the combination of two small firms into a merged entity closer in cost structure and size to one or more larger competitors may result in a move from passive “follower”-type behavior to more aggressive competition. The MEGs could usefully acknowledge that these conditions are not always sufficient to find a likelihood of post-merger coordinated behavior, but rather may enhance competition in certain circumstances.

6. Should the Bureau consider incorporating in the MEGs a discussion of the potential effects that a merger of competing buyers may have on upstream markets?

The MEGs address mergers of competing buyers using the same analytical framework for assessing market power that is applied to mergers of competing sellers – defining market power of buyers as the ability of a single firm or group of firms profitably to depress prices paid to sellers to a level that is below the competitive price for a significant period of time.²¹ The Sections would welcome greater clarity in the MEGs concerning the Bureau’s approach to several issues that arise in the context of such mergers.

One welcome revision would be a statement that the Bureau will generally have competition concerns only with respect to buyer mergers that are likely to result in the power to depress prices below competitive levels, such that output decreases are likely, including a deterioration in the quality of the output.²² There should generally be no competition concerns if a merger results simply in increased bargaining ability such that prices are not reduced below a competitive level. A reduction in prices paid by the

²⁰ MEGs ¶¶ 5.22 and 5.30.

²¹ See MEGs ¶¶ 2.3 – 2.4.

²² Typically (in the case of merger review as opposed to abuse of dominance), increases in market power are determined with reference to pre-merger prices not ideal “competitive” prices. However, assessment of buyer power with reference to competitive prices could be appropriate where pre-existing supplier power has resulted in market distortions and deadweight loss. Provided that any acquired monopsony power as a result of a merger does not drive prices below competitive levels, a strong case exists that the merger does not harm, but may enhance, competition.

merging firm might be significant in assessing the efficiencies associated with the merger and should be analyzed in that context. Guidance in the MEGs on the factors on which the Bureau relies to draw distinctions between bargaining power and monopsony or oligopsony power would be helpful.

It would also be helpful for the Bureau to explain the framework within which it considers welfare effects in this context, as well as its views with respect to mergers that increase buyer power without necessarily affecting output. The Bureau has previously stated that the exercise of monopsony power that reduces price without a concurrent reduction in output “may also give rise to concerns,” but does not elaborate on when or why those possible concerns would likely arise absent output effects.²³

The Sections further recommend that the Bureau explain what, if any, balancing it believes is necessary between upstream and downstream markets when there are upstream output effects.²⁴ Although the Bureau has previously noted that a reduction in upstream input purchases may result in higher downstream prices if output in that downstream market decreases, the Bureau has appropriately recognized that an output market price increase may not always occur.²⁵ In fact, not only might output prices fail to rise following the exercise of monopsony power, they may even fall as a result of lower input costs. It would be helpful for the Bureau to provide guidance on the factors it would consider in this regard, e.g., how it will balance the potential upstream output reduction with possible benefits to consumers that can be attributable to a price reduction to buyers, and more generally, on the merging parties’ burden in showing that reduced buyer prices will be passed on to consumers.

7. Is the discussion regarding prevention of competition (paras 2.10 – 2.12) in the MEGs sufficient, or should the Bureau consider providing further guidance on how the Bureau assesses the theories of "potential competition" and "actual competition"?

Paragraphs 2.10–2.12 in the MEGs provide a helpful explanation of the Bureau’s analysis of potential competition. The MEGs would benefit from a more developed explanation of how the Bureau analyzes the likely competitive discipline that a potential new competitor would have, but for the transaction. Such a discussion would be usefully aligned with entry analysis in part 6 of the MEGs. Factors the Bureau assesses in determining whether a merging party would enter or expand (potential competition) are

²³ See Competition Roundtable on Monopsony and Buyer Power, <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02995.html>.

²⁴ This assumption of at least some output effects seems to be the most important scenario upon which to focus given that at least some output effects will arise except in the unlikely situation that supply is perfectly inelastic.

²⁵ See Competition Roundtable on Monopsony and Buyer Power at 23.

similar to those the Bureau would consider when assessing whether another firm might enter or expand in a market (entry analysis).²⁶

In the pharmaceutical industry, it is not uncommon for mergers to involve parties with potentially competing pipeline products. Because of high development costs, the time involved in obtaining regulatory approval, and the inherent risks in innovation, however, many potential competitors never become actual competitors.²⁷ Similarly, mergers in highly innovative, dynamic industries can involve difficult market definition issues.²⁸ In light of these kinds of uncertainties, the Sections recommend that the Bureau add a safe harbor in the MEGs for mergers between potential competitors. Such a revision would clarify that the Bureau will not decide that a merger between potential competitors poses an undue risk adverse competitive effects, if actual competition between the parties absent the merger is unlikely within a specified number of years (e.g., 3-5 years).²⁹ Alternatively, the Sections urge the Bureau to explain why a time-based approach does not apply in potential competition cases but does apply elsewhere in the MEGs (e.g., the 2-year timeframe for assessing entry).³⁰

The MEGs helpfully discuss the broad factors that the Bureau examines when assessing potential prevention of competition (“type, scope and timing of the potential entry or expansion”) but do not address the types of evidence the Bureau uses in such

²⁶ The Sections believe the Bureau should not depart from its historical reluctance to define "innovation" markets. See MEGs ¶ 5.9 n.64; see also Competition Bureau, Intellectual Property Enforcement Guidelines ¶ 5.1, available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/01286.html>.

²⁷ See, e.g., Ilene Knable Gotts & Richard T. Rapp, *Antitrust Treatment of Mergers Involving Future Goods*, ANTITRUST, Fall 2004, at 100.

²⁸ See, e.g., U.S. Dep’t of Justice, “Statement Of The Department Of Justice Antitrust Division On Its Decision To Close Its Investigation Of XM Satellite Radio Holdings Inc.’s Merger With Sirius Satellite Radio Inc.” (Mar. 24, 2008), available at http://www.justice.gov/atr/public/press_releases/2008/231467.pdf.

²⁹ See, e.g., European Commission, Case No COMP/JV.37 – BSKyB / KirchPayTV (Mar. 21, 2000) (restricting potential competition analysis to whether competitor would enter market in the “short to medium term”), available at http://ec.europa.eu/competition/mergers/cases/decisions/jv37_en.pdf; David J. Teece and Thomas M. Jorde, "Antitrust Policy & Innovation: Taking Account of Performance Competition and Competitor Cooperation," ESSAYS IN TECH. MGMT & POL'Y 301 (2003) (observing with respect to developments in product markets marked by innovation that “because there is significant variation among products, no single number will be appropriate for all cases . . . [but] a four-year period [may] be established as a default time frame, with the option of adjusting the period if strong evidence suggests that would be appropriate in an individual case A fixed four-year rule will not be optimal in all cases. It could provide too broad a market definition in some cases and too narrow a definition for others; however, its unambiguous nature has the advantage of being easily understood.”).

³⁰ MEGs ¶ 6.3 (providing that new entry “normally must occur” within a two-year period).

cases.³¹ It would be helpful to learn more about the types and sources of evidence the Bureau considers in potential competition investigations, such as the entering firm's expected capacity, distributional capabilities and cost competitiveness, and demand factors such as consumer preferences, brand strength, and consumption trends. Recent innovation can drive significant changes to consumer preferences, moreover, that historical data do not reveal. Also beneficial would be insight into how the Bureau ascribes weight to different types of evidence, including patents, research and development spending, business plans, and consumer studies. This additional explanation can be set out in a concise appendix or in ancillary publications, as discussed above with respect to questions 2(a)-(d).

8. The MEGs provide that, when price discrimination is feasible, it may be appropriate to define relevant markets with reference to the characteristics of the classes of buyers or to the particular locations of the targeted buyers. Should the Bureau consider including an expanded discussion of price discrimination in both market definition and the assessment of competitive effects? Should the Bureau consider incorporating a discussion of the conditions when the Bureau, for practical reasons, may define relevant geographic markets based on the location of suppliers, rather than the location of customers?

The Sections recommend an expanded discussion of price discrimination in the MEGs. Currently, the MEGs provide limited discussion of the circumstances under which price discrimination is feasible: (i) sellers must be able to charge different prices to targeted sets of customers, because the customers cannot avoid post-merger price increases by switching to other products or geographic locations; and (ii) the targeted customers are unable to engage in arbitrage.³²

³¹ For example, the U.K. Office of Fair Trade has expressed a need for careful analysis in this area:

When applying theories of harm based on . . . potential competition, the OFT is mindful that it should apply evidentiary checks and balances because loss of potential – as opposed to actual – competition could easily be alleged and might be difficult to rebut in the large range of scenarios in which the parties did not overlap pre-merger. The risk that a non-incumbent firm that is not in fact a potential entrant might be incorrectly judged to be one is serious unless a sufficiently careful approach is taken to the correct evidential standard. Unduly lax evidentiary standards could result in speculative over-intervention.

U.K. Office of Fair Trading, Completed acquisition by Air France Finance S.A.S / City Jet Ltd of VLM Airlines N.V., ME/3535/08, ¶ 108 (2008), *available at* http://www.of.t.gov.uk/shared_of.t/mergers_ea02/2008/AirFrance.pdf;jsessionid=63F6764727FF9FB71B4ED3B9E249266D.

³² *Id.* ¶ 3.9.

It would be useful for the Bureau to explain further how it evaluates the potential for anticompetitive effects where price discrimination is possible and the factors it considers when defining price discrimination markets. In practice, analysis of these two issues often overlap because many of the same factors affect market definition and assessment of competitive effects.

The Sections recommend that the Bureau provide further guidance on the conditions under which it believes it is appropriate to define relevant markets through price discrimination. For example, price discrimination markets are often appropriate where prices are individually negotiated, suppliers have information about buyers that would allow them to distinguish customers who are willing to pay a higher price for the relevant product from those who are not, and arbitrage is difficult because of high transportation costs, informational asymmetries, or other impediments to resale. Likewise, the geographic scope of markets may be more limited in situations where suppliers deliver their products or services to customers' locations, demand or supply conditions differ between those locations, and there are impediments to arbitrage between the locations. These principles could be usefully elucidated in the MEGs.

The Sections also suggest a clarification that not all price discrimination is a competitive concern. A significant amount of economic literature acknowledges that price discrimination can improve consumer welfare by reducing prices and increasing output to certain customers. It would also be useful for the Bureau to state its position regarding the argument that price discrimination does not necessarily imply market power. The Bureau should make clear that a sustainable post-merger price increase to targeted customers is the relevant competitive concern. Similarly, the MEGs should note that differences in margins (or "netbacks") across geographic areas or product or customer types are not necessarily evidence of price discrimination markets, but may be the result of the different costs associated with serving the different customer types.³³

It would be useful for the Bureau to elaborate on how it weighs efficiencies in the context of price discrimination markets. The Sections suggest that the MEGs discuss how the Bureau considers an efficiencies defense that includes benefits to all customers, when evaluating a merger that may harm a more narrowly targeted group of customers. For example, the Sections would welcome clarification that the Bureau will not seek to prevent a merger that may reduce competition to serve a narrow set of customers where the merger will result in efficiencies that will inure to the benefit of all consumers, and where those efficiencies significantly outweigh the potential harm to the targeted customer group.

The Sections further submit that clarification is welcome regarding the conditions under which the Bureau will define relevant geographic markets based on the locations of suppliers rather than the location of customers. Supplier-based geographic markets often apply when customers receive goods or services at suppliers' locations. Additional

³³ See DENNIS W. CARLTON & JEFFREY M. PERLOFF, *MODERN INDUSTRIAL ORGANIZATION* 290, 293, 308 (4th ed. 2005).

guidance regarding the factors which would lead to markets defined by reference to supplier location would be beneficial.

9. When determining, for the purposes of market definition, whether a hypothetical monopolist would find it profitable to impose at least a small but significant and non-transitory increase in price, in most cases, the Bureau considers a five per cent increase to be significant. Should the Bureau consider providing further explanation as to when the Bureau may consider an increase of less than five per cent to be significant?

The goal of market definition is to identify the products that offer the most significant competitive constraints on the products of the merging parties, as a starting point in assessing the competitive effects of the transaction. The hypothetical monopolist approach defines the market as the set of products that must be controlled by the monopolist in order for a price increase of a small but significant amount to be profitable. The U.S. antitrust agencies recently reiterated their adherence to a five percent SSNIP.³⁴ They noted that "the Agencies may ... use a price increase that is larger or smaller than five percent" if appropriate,³⁵ but did not elaborate on the specific circumstances in which they would depart from the five percent test.³⁶

Paragraph 3.4 of the MEGs states that the Bureau "in most cases ... considers a five per cent price increase to be significant" but qualifies this by noting that "market characteristics may sometimes necessitate using a different price increase."³⁷ The Sections recognize that the Bureau departs from the five percent test only in rare cases but believe that a concise explanation in the MEGs of the circumstances in which the Bureau may use a SSNIP other than 5% would be useful.³⁸ It would also be helpful for

³⁴ 2010 U.S. Merger Guidelines § 4.1.2.

³⁵ *Id.*

³⁶ In practice, departure appears limited to mergers involving retail markets where customers are many and diffuse and where small changes in price can have a disproportionate impact on profitability. For example, the FTC argued for a 1% standard in defining the relevant product market in the recent Whole Foods matter. *See* Plaintiff Federal Trade Commission's Corrected Brief on its Motion for Preliminary Injunction 13, *FTC v. Whole Foods Market, Inc.*, available at <http://www.ftc.gov/os/caselist/0710114/080107corbrief.pdf>. The FTC has frequently used a once-cent-per-gallon price increase in defining relevant markets for petroleum mergers. *See Federal Trade Commission, Bureau of Economics, The Petroleum Industry: Mergers, Structural Change, and Antitrust Enforcement* at 12 n.13 (August 2004).

³⁷ MEGs ¶ 3.4 n.27.

³⁸ There can be situations in which a 5% price increase would be unprofitable for a hypothetical monopolist in a candidate market but a larger price increase would be profitable; the MEGs should recognize this possibility and note that if a 5% price increase

the Bureau to note that a smaller SSNIP typically will result in smaller potential anticompetitive effects. The choice of SSNIP is important to (and potentially determinative of) a finding of likely competitive effects. Too high of a SSNIP may result in a broad market where competitive effects are unlikely, but within which there could still be substantial scope for competitive harm from a merger. Too small of a SSNIP may make it difficult to identify, with even modest certainty, likely customer reaction and may be no different than defining the relevant market around the specific products the merging parties offer.³⁹ Commentators have also suggested that low SSNIPs are not appropriate in technology markets.⁴⁰

10. The market concentration thresholds in the Horizontal Merger Guidelines recently issued by the competition authorities in the United States (“U.S. Guidelines”) were updated. These Guidelines now note that changes in the number of competitors may actually be more significant in some contexts. While the U.S. Guidelines differ from the MEGs in their measure for market concentration (Herfindahl-Hirschman Index versus post-merger market shares), are the current thresholds in the MEGs sufficient or should the Bureau consider similar changes?

The 2010 U.S. Horizontal Merger Guidelines were updated in an effort to reflect the U.S. agencies’ actual practices over recent time.⁴¹ Based on their merger enforcement statistics,⁴² the U.S. agencies, in the 2010 U.S. Merger Guidelines, increased the HHI levels at which they invoke presumptions based on market shares and concentration.⁴³ The Section of Antitrust Law applauded the U.S. agencies for increasing the HHI thresholds to reflect actual practice more accurately, but recommended that the U.S. agencies remove the presumptions as a vestige of outdated guidelines and inconsistent with current practice – a view the Sections continue to hold.⁴⁴ The

will be unprofitable, a market may still be defined if a larger price increase would be profitable.

³⁹ See John Morris and Gale Mosteller, "Defining Markets for Merger Analysis," 36 *Antitrust Bull.* 599 (1991) (arguing that the use of a SSNIP below 5% will lead to inappropriately narrow markets and negatively impact consumer welfare).

⁴⁰ J. Gregory Sidak and David J. Teece, Comments on the Horizontal Merger Guidelines Review Project at 15, available at <http://www.ftc.gov/os/comments/horizontalmergerguides/545095-00025.pdf>.

⁴¹ <http://www.ftc.gov/opa/2010/08/hmg.shtm>.

⁴² <http://www.usdoj.gov/atr/public/201898.pdf>.

⁴³ See 2010 U.S. Merger Guidelines § 5.3.

⁴⁴ The Antitrust Section urged the U.S. agencies “to remove the presumption of illegality keyed to the level and increase of the HHI [because t]he presumption does not reflect how the Agencies conduct investigations, is not theoretically warranted, and could be misinterpreted by other countries thereby undercutting international efforts to promulgate

Sections endorse the recognition in the current MEGs that “[i]nformation that demonstrates that market share or concentration is likely to be high does not, in and of itself, provide a sufficient basis to justify a conclusion that a merger is likely to prevent or lessen competition.”⁴⁵ This principle is appropriately aligned with the MEGs’ observation that “the Tribunal cannot find that a merger lessens or prevents competition substantially based solely on evidence of market shares or concentration.”⁴⁶ These core principles are important to retain in the MEGs, consistent with the MEGs’ recognition that concentration information is merely one factor in a multi-factor, integrated, competitive effects analysis.⁴⁷

The Sections encourage the Bureau to revise the MEGs’ concentration thresholds to the extent they do not reflect Bureau practice. Moreover, in the Sections’ view, it would be appropriate to revise the MEGs to reflect – as the 2010 U.S. Horizontal Merger Guidelines reflect – that the number of competitors may be a more significant factor in certain contexts. The Section of Antitrust Law suggested that the U.S. agencies adopt the following language on this point,⁴⁸ and the Sections respectfully offer the same suggestion to the Bureau:

The [Bureau] may measure market concentration using the number of significant competitors in the market. This measure is most useful when there is a significant gap in market share between significant competitors and smaller rivals or when it is difficult to measure revenues in the relevant market, or when each competitor has a similar capability of winning future sales in markets characterized by competitive bidding.

11. Should the Bureau consider incorporating a more expansive discussion of the characteristics that constitute a “maverick” firm?

The MEGs provide a useful discussion of “maverick” firms and their role in the analysis of coordinated effects. The Sections welcome articulation in the MEGs of any additional principles, not already reflected in the MEGs, that the Bureau applies to merger analysis involving this topic. Doing so would facilitate greater transparency and

solid merger analysis principles.” Comments of the ABA Section of Antitrust Law HMG Revision Project (#P0292900) June 4, 2010 (“SAL Comment”) at 4 (http://www.abanet.org/antitrust/at-comments/2010/06-10/2010_hmg.shtml).

⁴⁵ MEGs ¶ 4.11.

⁴⁶ MEGs ¶ 4.11 n.49.

⁴⁷ With regard to mergers that result in market shares or concentration levels that exceed certain analytic thresholds, the MEGs note that “the Bureau examines various factors to determine whether such mergers will likely create, maintain or enhance market power and thereby result in a substantial lessening or prevention of competition.” MEGs ¶ 4.13.

⁴⁸ SAL Comment, *supra* note 47, at 13.

predictability regarding the Bureau's methods for conducting competitive effects analysis. For example, the MEGs could supplement the definition of a "maverick as a firm that has a disproportionate incentive to deviate from coordinated behaviour" by broadly identifying types of empirical evidence that the Bureau uses to identify such a firm and to assess its competitive significance.⁴⁹ The Sections also endorse more elaborate discussion of this topic in the context of actual merger reviews, through "technical backgrounders" and other ancillary publications to the MEGs.

12. Entry and Expansion

a. The current MEGs assess entry based on the likelihood that it will occur within a two-year period (paragraphs 2.14 and 6.3). Should the Bureau revisit this two-year period? (The U.S. Guidelines have eliminated this requirement and provide a simplified discussion of ease of entry and its role in merger analysis.)

The MEGs characterize the two-year period as a "rule of thumb." As noted by the Bureau's question, the 2010 Horizontal Merger Guidelines eliminated the reference to a two-year period. In its place are less concrete concepts; for example, entry must occur "rapidly and easily" enough such that the "the prospect of entry . . . will deter or counteract any competitive effects of concern."⁵⁰

Although no theoretical or empirical support exists for a pre-determined minimum time period within which entry must occur to counteract or deter the anticompetitive effects of a transaction, the Sections believe the specific time benchmarks remain useful. For example, the Bureau could include in the MEGs specific recognition of its case-specific, flexible approach to entry analysis, while also making clear that entry that takes place within certain time periods is more likely to be given more weight. In addition, it would be helpful for the Bureau to explain that the earlier that entry is likely to take place, the greater is the scale of the entry (relative to current market participants, including the merging parties) and the lower are the sunk costs of the entry, the greater the weight that the Bureau will place on the competitive effect of that entry.

⁴⁹ *But see* MEGs ¶ 5.31 n.75 (suggesting at least one means by which a maverick firm might be identified). For example, recent literature suggests a number of empirical approaches by which a maverick firm may be identified. Breunig and Menezes, for instance, suggest that maverick-like behavior might be identified by measuring (1) the extent to which particular suppliers might under-price rivals and (2) the timing of the supplier's responses to systematic cost changes. Robert Breunig and Flavio Menezes, "Empirical Approaches for Identifying Maverick Firms: An Application to Mortgage Providers in Australia," *JOURNAL OF COMPETITION LAW & ECONOMICS* 4(3), 811-836 (2008). Similarly, Jonathan Baker suggests that mavericks can also be identified through what he calls "revealed preferences" and "natural experiments" Jonathan B. Baker, "Mavericks, Mergers and Exclusion: Proving Coordinated Competitive Effects Under the Antitrust Laws," 77 *N.Y.U. L. REV.* 135 (2002).

⁵⁰ 2010 U.S. Merger Guidelines § 9.

b. Should the Bureau consider addressing different kinds of entry and how the Bureau assesses evidence relating to entry? (The U.S. Guidelines now emphasize the importance of actual entry into the relevant market.)

The Sections recommend that the MEGs be adjusted to reflect the dynamic nature of entry analysis. For example, the Sections believe the Bureau should value perceived entry as much (if not more) than actual entry. Perceived potential competitors can act as significant competitive constraints and should be credited as entrants (or market participants), particularly where there is evidence that market participants have adjusted their competitive behavior in reaction to perceived potential competitors in the past (i.e., similar to evidence of actual past entry). In addition, the MEGs should reflect the potential for the merger to induce entry (e.g., by providing an opportunity to take advantage of poor post-merger integration and availability of experienced personnel, particularly sales and customer service staff with existing customer relationships).

The Sections also recommend that the MEGs more clearly recognize that entry sufficient to counter any anticompetitive effects of a transaction can occur through smaller scale entry of multiple firms, which, in the aggregate, can replace any output likely to be lost as a result of the merger. Consistent with this recognition, the MEGs should note that for a firm to be viewed as a credible entrant, that firm need not enter on the scale or strength of one of the merging parties. Likely and timely entry (by one or multiple firms) at a scale large enough to replace the amount of any likely post-merger output reduction should be considered sufficient.

c. Does the discussion in the MEGs relating to firms' participation in relevant markets through a supply response (paragraph 4.2) more appropriately belong in an evaluation of barriers to entry and expansion? How useful is this distinction?

The Sections do not believe that the distinction is a useful one in practice and recommend that the Bureau eliminate it from the MEGs. The Section of Antitrust Law made a similar recommendation to the U.S. antitrust agencies during their recent Guidelines review process, noting that under an integrated approach to merger review, it makes more sense to consolidate the analysis of potential supply responses in a single section.⁵¹ The 2010 Horizontal Merger Guidelines now follow that approach.

13. Should the Bureau consider including in the MEGs illustrative examples of the application of the Bureau's analytical approach to merger review and, if so, which sections of the MEGs would benefit from the inclusion of examples?

⁵¹ See Comments of the ABA Section of Antitrust Law Regarding the Federal Trade Commission and Department of Justice Horizontal Merger Review Project (#P092900) Nov. 9, 2009 at 33.

The Sections have reservations about the use of hypothetical illustrative examples beyond those already contained in the MEGs. In light of the highly fact-specific nature of merger analysis, any stylized fact pattern that could be readily explained within the MEGs would likely be so simple as to be minimally instructive, and could be potentially misleading. On many occasions, conclusions reached by the Bureau will be based on numerous factors, including greater weighting of some evidence over other evidence, based on credibility or other intangible factors. That kind of analysis is not readily clarified through the use of illustrative examples.

More generally, the Section has reservations with respect to the use of real-world examples as appropriate to the purposes of the revised MEGs. Because individual transactions each involve unique facts that influence both the application of the analysis under the MEGs and the manner in which the Bureau applies its enforcement discretion, reference to real-world examples could potentially interfere with the clarity and utility of the MEGs. Certain of the unique facts associated with individual transactions can lose relevance over time as markets change, and many important facts must remain confidential. Thus, there is some question whether real-world examples would provide useful guidance over the life of the MEGs. Moreover, in practice, one would expect that the individual elements of the MEGs analysis will necessarily be weighted differently to fit the varying competitive dynamics of distinct markets that are affected by a given transaction.

More helpful than additional (illustrative or real-world) examples in the MEGs would be additional timely information outside the context of the MEGs about how the Bureau analyzed particular matters. Specifically, in light of the goals of transparency regarding the Bureau's analytical paradigm for mergers, the Sections recommend that the Bureau continue its policy of issuing technical backgrounders⁵² and consider expanding its practice to cover all significant mergers where a consent agreement was negotiated with the Bureau, as well as those mergers where the Bureau concluded that a consent agreement negotiated with a foreign authority will address Canadian concerns.

14. The Countervailing Power section of the MEGs (paragraphs 7.1 – 7.3) contains a discussion of when buyers may be able to credibly constrain the ability of a seller to exercise market power. Should the Bureau consider revising the MEGs to discuss buyers that may have a credible alternative to self-supply or sponsor entry, and what further evidence would be required to establish that such buyers are immune from or mitigate harm owing to the loss of competition arising from the merger? Where some buyers may be protected owing to countervailing power, should the Bureau consider expanding the discussion in the MEGs regarding the protection of smaller buyers from an exercise of market power?

Currently the MEGs recognize that powerful buyers may constrain the ability of merging parties to exercise market power. The MEGs also provide useful guidance

⁵² Competition Bureau, Policy Statement for the Publication of Technical Backgrounders, April 2005, at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/01301.html>.

regarding the significance given by the Bureau to such buyers in assessing the competitive effects of mergers. For example, the MEGs delineate certain conditions under which powerful buyers may constrain the exercise of market power. Additional detailed guidance regarding the Bureau's consideration of powerful buyers in its analysis would be beneficial.

In particular, the Sections believe the MEGs should be updated to reflect the broad spectrum of tools available to powerful buyers who wish to defeat price increases. At present, paragraph 7.2 notes that buyers can constrain the exercise of market power if: (i) they have the ability to switch to other sellers in a reasonable amount of time; (ii) they can vertically integrate; or (iii) they can sponsor new entry or expansion of an existing seller. Powerful buyers may also withdraw or reduce their business in relation to other products produced by the supplier (outside the relevant market), or delay purchases. Similarly, the buyer may threaten to withdraw or reduce their business in relation to future products produced by the supplier. Moreover, multi-national or multi-regional buyers may have the ability to retaliate against the merged entity by taking action in other geographic markets in which either party operates, but in which the competitive conditions may be different.⁵³

Where a market is characterized by buyers with varying amounts of countervailing negotiating power, the Bureau should separately assess the competitive effects of the merger on different categories of buyers, and in particular the extent to which countervailing buyer power may be relied upon to protect less powerful customers. In markets where sellers are unable to discriminate between buyers with varying amounts of power, the presence of one powerful buyer may be sufficient to protect other customers from a price increase as well. This is often the case where there are no bilateral negotiations between buyers and sellers and the market price of the input is transparent to all market participants. As the MEGs acknowledge, where price discrimination is possible countervailing buyer power often cannot offset the potential adverse effects of the merger and less powerful buyers may remain vulnerable to a price increase.⁵⁴

⁵³ The Sections note that even smaller customers may exercise buyer power. This can occur, for example, where the customer's business has unique importance to competing suppliers or where small losses in volume have a significant impact on suppliers' costs because of sensitivity to the level of capacity utilization.

⁵⁴ The Sections do not believe that buyer power should be disregarded simply because it affects only some customers. Buyer power should be considered in assessing the competitive effects of a merger on those customers that have buyer power. Depending upon the circumstances, there may be other factors that inform an analysis of competitive effects relating to customers that do not have buyer power. For example, less powerful customers might not view the merger parties as particularly close substitutes or might have other alternatives available. In particular, smaller customers may be able to buy from fringe suppliers that are not a viable alternative for larger buyers.

The Sections also believe it would be useful for the Bureau to provide additional guidance, whether in the MEGs or in ancillary publications outside the MEGs on the types of evidence the Bureau considers in determining whether powerful buyers can constrain the exercise of market power. For example, where the merging parties argue that powerful buyers may credibly constrain the ability of a seller to exercise market power by switching to other suppliers, the Bureau should assess whether alternative suppliers have sufficient capacity to satisfy the buyers' demand. If the merging parties argue that powerful buyers can retaliate by altering their purchasing behaviour outside of the relevant product or geographic market, the Bureau should examine the existing and potential relationships between the buyer and the merging entities in those markets. The Bureau should also consider the state of competitive conditions in the relevant alternative markets. If the buyer has significant power in the alternative markets, it is more likely that buyers will be immune from or able to mitigate potential harm that otherwise might result from the loss of competition arising from the merger.

The Bureau also should consider historical evidence of price negotiations in assessing whether buyers are likely to possess countervailing power, including a history of being able to extract lower prices, or to demand discounts or other more favourable conditions from sellers. This dynamic is common in markets where interactions between buyers and sellers are long-term in nature, and where buyers have an intimate knowledge and understanding of the seller's business, including its cost structure.

The Bureau should therefore clarify that the presence of powerful buyers is a relevant, but not dispositive, factor in the analysis. In addition, the Sections recommend noting that for countervailing buyer power to prevent an exercise of market power, it is not sufficient that the power merely existed before the merger. Rather, such power must remain effective post-merger.

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The Sections applaud the Bureau for its openness and transparency in commencing this important process. We hope the Bureau finds these joint comments to be useful. Should the Bureau decide to revise the MEGs, the Sections would welcome the opportunity to review and provide comments to any proposed revisions.