PUBLIC INTEREST ADVOCACY CENTRE

RESPONSE TO

"TREATMENT OF EFFICIENCIES IN THE *COMPETITION ACT*"

DECEMBER 8, 2004

INTRODUCTION

The Public Interest Advocacy Centre (PIAC) welcomes this opportunity to submit comments in response to the Competition Bureau's Consultation Paper, "Treatment of Efficiencies in the *Competition Act*". PIAC has been representing consumer interests before various regulatory and administrative tribunals for over twenty-five years, in particular as concerns questions of economic regulation. As a result, PIAC can bring a consumer perspective to bear on the questions raised by the Consultation Paper.

Consumers generally benefit greatly from competition. Lower prices, greater product and service innovation, and expanded variety and choice are all benefits of properly working competitive markets. PIAC strongly supports measures to block the prevention or substantial lessening of competition, through mergers and other structural reorganizations.

PIAC recognizes that in some circumstances competition may need to be subordinated to other factors. One such instance may be the potential of significant efficiency gains arising from a merger. However, such situations should be exceptional. Further, "efficiency gains" must be considered in the context of the other objectives stated in s. 1.1 of the *Competition Act*, and of the welfare of Canadian society in general.

Although the "efficiency defence" is available under provisions of the Act other than s. 96, it has never been invoked there, and, in PIAC's view, it likely never will be. Accordingly, in what follows, PIAC addresses the "efficiency defence" as it applies to mergers under s. 96.

CHANGES IN THE CANADIAN ECONOMY

As the Competition Bureau's Consultation Paper states, the present *Competition Act* was enacted some 17 years ago, when Canada's economy was very different. It was still making the transition from resource-based to a much more broadly diversified mix that is overwhelmingly services and manufacturing. The Canadian economy was small relative to other national economies, and tariff barriers to exports were high, as were transport and communications costs. As a result, it was believed, Canadian companies were largely limited to a small domestic market and faced a significant challenge in achieving economies of scale. This would hurt the domestic economy. More importantly at the time, it was also expected to keep Canadian companies uncompetitive on the world stage; in turn, this would harm job creation at home.

The "efficiencies defence" in s. 96 was in large part designed to help Canadian companies overcome this disadvantage. Mergers would be allowed if they would likely bring about gains in efficiency that would be greater than, and would offset, anti-competitive effects. Given the relatively small size of the domestic market, and the difficulties of exporting, this was a key measure to help the Canadian economy achieve economies of scale.

Meeting foreign competition was emphasized in s. 96(2). Particular attention was to be paid to efficiency gains that would result in a significant increase in exports or a significant substitution of domestic products for imports. The mergers provisions of the Competition Act were to be consistent with an active trade policy for Canada, in a world of protectionism and significant trade barriers.

In PIAC's view, the Canadian economy has changed since the mid-1980s. Lower transport and communications costs have redefined geographic markets. Decreases in tariffs and non-tariff trade barriers, through bilateral agreements such as NAFTA and multilateral agreements such as the Uruguay Round, have also contributed. As a result, where they were once local and national, markets are now continental and global in scope.

Technological and institutional change has also broadened the definition of product markets. For example, convergence in telecommunications is resulting in the breakdown of the distinction between telephony and cable television. In the financial services sector, consumers in 1987 were obliged to have separate bank accounts, brokerage accounts, and insurance accounts. Increasingly, all of these functions can be supplied by any one of these accounts.

As a result, Canadian firms are in a better position, relative to firms in other countries, to obtain economies of scale and scope without restricting the level of competition in the

Canadian economy. As well, encouraging exports and import substitution should have a lower priority than at the time the *Act* was passed. This has important consequences for the interpretation of the “efficiencies defence”.

THE OBJECTIVES OF THE ACT

S. 1.1 of the *Competition Act* lists a number of objectives, without however prioritizing them or relating them to each other. The purpose of the Act is “to maintain and encourage competition in Canada”, in order to

- promote the efficiency and adaptability of the Canadian economy
- expand export opportunities while at the same time recognizing the role of foreign competition in Canada
- ensure that small and medium-sized enterprises “have an equitable opportunity to participate in the Canadian economy”
- provide consumers with competitive prices and product choices.

The first objective, promoting the efficiency and adaptability of the Canadian economy, while laudable, cannot be an end in itself. Rather, it is a means to an end.[1] More precisely, efficiency gains are desirable because they allow for a higher level of consumption, now or in the future; or because they make possible more leisure or a more agreeable environment; or because they lead to a higher level of employment in Canada. Thus, “efficiency” must be read in conjunction with the other objectives, and as a means of better attaining them.

The second objective is to improve Canada’s trade balance, encouraging exports and discouraging imports. In the area of mergers, it is reflected explicitly in s. 96(2), which contemplates allowing reductions in competitiveness so that Canadian companies could attain critical size relative to world markets. However, as noted in the previous section, with the dramatic expansion of geographic and product markets over the last twenty years, concerns as to market size have abated. It is also interesting that, to PIAC’s knowledge, s. 96(2) has never been used as a defense to allow a merger that would otherwise substantially lessen competition.[2]

In PIAC’s view, the objective in s. 1.1 of increasing exports and decreasing imports, through favorable treatment of mergers that would otherwise reduce significantly competition, are no longer consonant with Canada’s economic position, and should be reviewed. It is PIAC’s understanding that, in practice, the provisions of s. 96(2) do not

[1] Considering efficiency as a goal in itself is analogous to accumulating gold and other forms of money for their own sake, as the seventeenth-century French mercantilists advocated. We no longer believe money is intrinsically desirable; what is desirable is the goods and services the money will buy.

[2] In addition, it is not clear whether or not s. 96(2) runs counter to Canada’s obligations under the WTO.

guide the Competition Bureau or the Competition Tribunal's review of a merger. This should continue.

The third objective of the *Act* is to give small and medium-size businesses "an equitable opportunity to participate in the Canadian economy". This objective would seem to be grounded in a historic desire to preserve small independent firms, for political and social reasons, and to protect them from "trusts" and large companies.[3]

PIAC supports the principle of providing equitable opportunities to all businesses, large and small. However, there should be no bias in favour of smaller businesses when considering mergers and the efficiencies defence. Larger firms should not be impeded from realizing economies of scale and other efficiencies, through mergers or otherwise, just to protect smaller firms. Accordingly, the third objective of the Act should not come into play when considering mergers.

The fourth objective, to provide consumers with competitive prices and product choices, is directly linked to a higher standard of living and a better quality of life.[4] At the end of the day, the purpose of efficiency gains, a better balance of trade, and higher employment, is to allow individual members of our society to consume more, to enjoy more leisure, to live a healthy life in a sound environment, and to build worthwhile social institutions.

While there are other, more important goals than material consumption, the *Competition Act* was not designed to address them. Rather, the focus of the *Competition Act* is on the well-being of members of society as consumers. Lower prices and greater variety should be the first priority of the *Competition Act* in today's economy. Increasing efficiency should be seen as a means of attaining this priority objective.[5]

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[3] This thrust was especially strong in the United States. See for example Richard A. Posner, *Antitrust Law*, 2nd Ed. (Chicago: University of Chicago Press, 2001) at 25. Protection of smaller firms seems to have played a much lesser role, if any, in enforcement of competition laws in Canada, which is as it should be.

[4] Following the usage of the Consultation Paper, PIAC uses the term "price" to include non-price attributes of a product, such as quality.

[5] Many economists hold that increasing efficiency should be the only goal of competition policy. Other goals, according to them, should be pursued through other policy instruments. See for example Michael Trebilcock et. al., *The Law and Economics of Canadian Competition Policy* (Toronto: University of Toronto Press, 2002) at 39. However, these other policy instruments are not always available, or may be very costly to use. In a second-best world, it is important that competition policy, even if it should not be the primary tool to resolve problems such as income redistribution, at least should not aggravate them.

MERGERS AND THE EFFICIENCIES DEFENCE: TOTAL SURPLUS STANDARD

Mergers may prevent or substantially lessen competition in a market. S. 92 of the *Competition Act* gives the Competition Tribunal the power to take appropriate steps to prevent this harm. However, the Act recognizes that mergers may also lead to efficiency gains. S. 96(1) provides that a merger will be allowed if it is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that is likely to result.

The Consultation Paper makes clear that efficiency gains may include allocative, productive, and dynamic efficiency gains. In practice, efficiency gains from a merger may include productive efficiency gains, due to larger production runs and increased economies of scale. Dynamic efficiency gains from a merger, such as innovation and improved use of technologies and information, may also be important, but they are typically extremely hard to quantify.[6] As to allocative effects, typically a substantial lessening of competition would be expected to lead to a reduction of efficiency as output is reduced below competitive levels, leading to "dead-weight" losses. Such losses are to be netted out against productive and dynamic efficiency gains.

According to the "total surplus standard", advocated by many economists, as long as the efficiency gains (usually productive and dynamic efficiencies) from a merger outweigh the efficiency losses from any resulting significant lessening of competition (usually allocative efficiency losses), the merger should be permitted.[7]

But the total surplus standard ignores income redistribution consequences of the merger. A substantial lessening of competition is normally accompanied by a significant non-transitory price increase: indeed, this is the measure used by the Competition Bureau and many others. This redistributes income from consumers of the merged firm's products to the firm itself.[8] The total surplus standard assumes that, if efficiency gains are positive, the "winners" of the redistribution could compensate the "losers" and still be better off.[9]

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[6] All of the efficiency gains expected from a merger are very hard to quantify. Indeed, some observers believe that the uncertainty in measuring efficiency gains and losses is so massive that "there should be no general defense of efficiency": Posner, *op. cit.*, at 133

[7] Significant lessening of competition may also result in reduced incentives for productive and dynamic efficiency gains.

[8] In turn, the increased revenues will be passed on, in part to employees through higher salaries and benefits, and in part to shareholders through an increase in earnings that is translated into increased share prices. The magnitude of the final incidence is an empirical matter. To simplify the discussion, we refer to shareholder effects and do not discuss employee effects. This has no impact on the arguments advanced.

[9] This is the well-known Kaldor-Hicks criterion for welfare maximization. See Richard A. Posner, *op. cit.*, at 23.

This is consistent with the view that the only objective of competition policy should be maximization of efficiency. However, it is not necessarily consistent with the objectives in the *Competition Act*.[10]

Some observers suggest targeting the *Competition Act* just to efficiency objectives, leaving to other policy instruments the task of correcting any unwanted side effects such as redistribution of income:

> The use of competition policy to achieve not merely efficiency but an equitable distribution of wealth would result in an excessively complex and non-transparent set of legal rules that would be both uncertain and arbitrary – being determined by the opinions or values of whoever was sitting on the tribunal in a particular case. Government instruments such as taxes and social insurance are much better suited for the goal of distributing income equitably.[11]

However, these other instruments may be very costly, and often may not be politically feasible. As a result, the negative non-efficiency impacts of a merger may never be corrected through taxation, social insurance, and other such measures.[12] Indeed, there is a long tradition in the economics literature that claims that adjusting relative prices is one of the more effective means of income redistribution.[13]

In any event, s. 96(1) says that efficiency gains are to be greater than, and offset, "the effects of any prevention or lessening of competition". While these effects include efficiency losses (typically allocative efficiency losses), the wording does not limit "effects" to these. In particular, a merged firm with increased market power would generally be expected to raise its prices, inter alia redistributing income from purchasers of its products to the merged firm. It is PIAC's view that this redistribution is an effect of the substantial lessening of competition, and should be included when balancing efficiency gains against anti-competitive effects.

Indeed, it is not possible to separate the efficiency effects of a merger from the redistributive effects, without making strong assumptions as to interpersonal comparisons of individuals' income utility. For example, the total surplus approach implicitly assumes that redistribution does not affect overall utility, i.e. that one person's losses can simply be netted out against another's gains. But that is true only if their marginal utilities of income are equal. This is a questionable assumption.

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[10] "The purely legal arguments for total surplus as a criterion to be read directly in section 96 of the Competition Act are not persuasive… Section 96 of the Act is ambiguous." Trebilcock et. al., *op. cit.*, at 149.

[11] Trebilcock et. al., *op. cit.*, at 40.

[12] For example, it is difficult to imagine a tax limited to producers of propane, and tax credits or subsidies targeted just to consumers of propane.

[13] For example, see J de V. Graaff, *Theoretical Welfare Economics* (Cambridge: Cambridge University Press, 1957) at 155 and 171: "By far the simplest way of securing the distribution of wealth we desire is through the price system… [T]inkering with the price system is one of the more feasible and generally satisfactory ways of securing whatever division of wealth is desired."

As an illustration, consider a merger that results in a net efficiency gain of $1 million, accompanied by an increase in prices that transfers $100 million from consumers to the merged firm. While the final incidence of that $100 million may be different from the initial incidence, for simplicity assume that the entire $100 million goes to the firm's shareholders.[14] The net result is that shareholders as a group are better off by $101 million, while consumers are worse off by $100 million. If a dollar in shareholders hands were valued by consumers at $1.02 or more, society as a whole would be worse off. Approving the merger would be welfare-reducing, even though the "total surplus" test is met.

The standard assumption in the economics literature is that an extra dollar has more value to a person with a lower level of income. It is reasonable to suppose that, on average, shareholders are better off financially than consumers.[15] If so, evaluation of any measure, that redistributes income from consumers to shareholders, must take into account the loss in aggregate welfare it causes. The "total surplus" test in mergers analysis does not. It is incomplete and should not be used.

Three other factors reinforce the proposition that redistribution from consumers to firms and their shareholders is welfare reducing. First, in the typical case, a firm has many more consumers than shareholders. Thus the redistribution concentrates wealth, inflicting a (smaller) loss on the many, and a (larger) gain on the few. Even if consumers and shareholders started at identical income levels, this redistribution would lead to a loss in welfare (due to declining marginal utility of income).

Second, results in the behavioural economics literature systematically suggest that persons feel a loss twice as keenly as they do gain of the same size.[16] This suggests that the weight to be attached to a monetary loss should be about twice that to be attached to a monetary gain.

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[14] As pointed out above, some of the $100 million will likely also be captured by employees, depending on various elasticities of substitution and the demand for and supply of the kind of labour used by the firm.

[15] Some economists question this assumption. They point to the increasingly broad ownership of common stock, both directly and through mutual funds and pension plans (Posner, op. cit., at 24). In cases of luxury goods , such as the Whistler Mountain ski resort, the consumers may be wealthier than the shareholders (Trebilcock et. al., *op. cit*., at 150). However, recent statistics show that dividend income is heavily concentrated in the upper income levels of Canadians. Thus, for returns reporting income of less than $20,000, 9.6% reported receiving dividends, while for returns reporting income of more than $100,000, 52.3% reported receiving dividends. Put another way, grossed-up dividends made up 0.6% of the income of those with income below $20,000, but 6.8% of the income of those with income above $100,000. Put yet a third way, of the total amount of dividends reported, 0.9% were reported by taxpayers with incomes of less than $20,000, while 56.8% were reported by taxpayers with income of more than $100,000. (Calculated from Canada Revenue Agency, *Income Statistics 2002* – 2000 tax year, Final Basic Table 2). This calculation does not reflect dividends received within RRSPs or pension plans. Nevertheless, using receipt of dividends as a proxy for share ownership, clearly share ownership is concentrated at upper income levels, where the marginal utility of money is less.

[16] Tversky, A. and D. Kahneman (1992), "Advances in prospect theory: cumulative representation of uncertainty", 5 J. *Risk and Uncertainty* 297. See also Barberis, N. and R. Thaler, "A Survey of Behavioral Finance", Chapter 18 in Constantinides, G.M., M. Harris and R. Stultz, eds., *Handbook of the Economics of Finance* (Elsevier Science, 2003) at 1080.

Third, the total surplus standard assumes that the decrease in consumer surplus (other than the deadweight loss) results in a corresponding increase in producer surplus: the result is a pecuniary transfer from consumers to producers with no consequences for resources and hence no consequences for social welfare. But the merging firms will likely expend significant resources in getting their merger approved, and in defending their increased market power, through collusion with other producers or otherwise. As a result, much of the increased producer surplus may be dissipated in rent-seeking that is wasteful from the point of view of society.[17] These are efficiency losses that are not counted in the total surplus standard.

In PIAC's view, in light of the above discussion, the "total surplus" approach described in the Consultation Paper is flawed and should be rejected.

MERGERS AND THE EFFICIENCIES DEFENCE: BALANCING WEIGHTS STANDARD

Currently, the Canadian approach to the efficiencies defence in mergers uses "balancing weights", as required by the Federal Court of Appeal.[18] Essentially, income redistribution effects will be considered in the efficiencies defence. The weight to be given to a dollar of income distribution, relative to a dollar of efficiency gain, is to be determined on the circumstances of the situation, and may depend on the different socio-economic status of customers and shareholders. Indeed, it is possible that different weights should apply to different classes of customers.

Attempts to attach different weights to impacts on different socio-economic groups have a long history. For example, the issue has long been debated in performing developmental project appraisals in developing countries.[19] In theory, this approach is attractive, allowing the flexibility and discretion to take into consideration the

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[17] See Herbert Hovenkamp, *Federal Antitrust Policy: The Law of Competition and its Practice*, 2nd Ed. (St. Paul, Minn: West Publishers, 1999) at 502: "A profit-maximizing firm will be willing to spend substantial resources in an effort to acquire or retain a certain amount of monopoly power." See also Posner, *op. cit.*, at 13: "[A]n opportunity to obtain a lucrative transfer payment in the form of monopoly profits will attract real resources into efforts by sellers to monopolize and by consumers to avoid being charged monopoly prices."

[18] *Commissioner of Competition* v. *Superior Propane Inc.* (2001), 11 C.P.R. (4th) 289 (April 4, 2001)

[19] "The use of variable weights on gains and losses to different income groups has been the most controversial issue in cost-benefit analysis in recent years. Many considerations have been raised in discussions of this issue, ranging from practical and procedural questions to moral values and political process." Anandarup Ray, *Cost-Benefit Analysis: Issues and Methodologies* (Baltimore: Johns Hopkins Press for the World Bank, 1984) at 22.

circumstances of each case. In practice, however, this very flexibility and discretion leads to significant disadvantages.[20]

First, how are the different classes of affected customers and shareholders to be determined? If weights are to vary according to income levels or socio-economic status, how many categories should there be, and what are the cut-off levels? Should other factors, such as geographic location, be important, e.g. if the losses are to customers in Canada but the gains largely to shareholders in another country? To the degree that some of the costs or benefits flow to employees, rather than to customers or shareholders, should these be identified and weighted separately?

Second, should losses and gains be weighted differently? This suggestion follows from the finding in behavioural economics that on average people are more concerned by a loss than by a gain of equal magnitude.

Third, once the categories are chosen, how are the weights to be selected? Should benefits to one category receive one and a half times the weight of those to another category? twice the weight? three times the weight? Is there a risk that the process to choose weights would become highly politicized?

Fourth, before the weights can be applied, gains and losses must be measured by category. Presumably it is the final incidence of these gains and losses that is important. But such measurements require large quantities of information that might be very difficult to obtain.

These considerations lead PIAC to conclude that, while the balancing weights approach has many attractive features in theory, in practice it would be extremely difficult and controversial to implement. Further, it would cause considerable uncertainty among parties contemplating a merger. Since the weights might vary from case to case, the case law would be of limited use in reducing this uncertainty.

Over and above the practical difficulties of implementation, PIAC has some reservations about the moral justification for the balancing weights approach. Essentially, its underpinning is a utilitarian one, whereby it is acceptable for certain members of society to lose, as long as others gain enough to be able to more than make them whole.[21] Note however that the approach does not require the winners to actually compensate the losers, only to have the potential to do so. The losers remain losers.

It is not clear to PIAC why, in the context of a merger that prevents or substantially lessens competition, it is acceptable for shareholders to obtain benefits that exceed the magnitude of the efficiency gains generated, where the surplus comes at the expense of losses to customers.

[20] Trebilcock et. al., *op. cit.*, at 150; Posner, *op. cit.*, at 24
[21] This is the Hicks-Kaldor criterion for welfare-enhancing changes.

In this context, PIAC notes that the present wording of s. 96(1) requires efficiency gains that **will be greater than, and will offset**, anticompetitive effects. PIAC reads these words to mean that the offset must actually occur; it is not good enough to demonstrate a hypothetical offset that *could* happen.

MERGERS AND THE EFFICIENCIES DEFENCE: CONSUMER SURPLUS STANDARD

A third approach would require that, for the efficiencies defence to succeed, customers should not lose because of the merger. In particular, prices should not substantially increase, relative to what they would be, absent the merger.[22] Equivalently, consumer surplus should not decrease.[23]

This approach has the advantage of limiting the efficiency defence to mergers that are Pareto-improving: nobody in society is worse off, and at least some (presumably the shareholders) are better off.

PIAC finds this approach attractive.[24] Shareholders would be free to enjoy the efficiency gains generated by their firms through the merger. At the same time, customers would be no worse off, and may be better off, in terms of the prices they pay. There would be no uncompensated transfer of wealth from one group to the other.

This approach is also relatively simple to implement. The focus, from the customer end, is on the level of prices. For ease of administration, a price index for the firm could be constructed, as a weighted average for all the products sold by the pre-merger firms. For the efficiencies defence to be successful, a requirement might be that it be likely that this price index not increase for a given period of time post-merger.[25]

A critique of the consumer surplus standard is that it is too stringent: relatively few mergers would be saved under it. The difficulty is that, absent a combination of high

[22] The reader is reminded that here "price" is intended to include non-price attributes, such as quality.
[23] The Federal Court of Appeals has rejected this approach in *Commissioner of Competition* v. *Superior Propane Inc*., [2003] F.C.A. 53. Thus, a legislative amendment may be required to implement it.
[24] As do many observers. See, e.g., Hovenkamp, *op. cit*., at 503. Furthermore, the consumer surplus standard is more consistent than the total surplus standard with the objectives of the *Competition Act*.
[25] The details of constructing such a price index have been explored in depth in a number of industries in Canada, such as telecommunications and energy, that are subject to price cap regulation. A number of industries in Canada, such as telecommunications and energy, are subject to price caps regulation. Simplifying greatly, an average price index is calculated each year for firms that have market power. The firms must obey the constraint that this index cannot exceed a cap determined by the rate of inflation and by the productivity gains that can reasonably be expected in that industry.

price elasticity of demand and low incremental costs, it is commercially rational for a merged firm with newly increased market power to raise prices.

In such a case, the merger might nevertheless be permitted to take place if the merged firm were to commit not to increase prices, as measured by a price index, for a given period, say three to five years. Such a commitment could easily be monitored by the Bureau or an independent third party, with civil liability for breach.

Ongoing monitoring would run counter to the traditional approach found in competition policy, and resembles some elements of price cap regulation.[26] However, the *Competition Act* now contains provisions for the continuing monitoring of a specific industry, air transport, e.g. ss. 4.1 and 104.1.[27] Monitoring of an undertaking not to raise prices for a well-defined period of time after a merger would be much less intrusive and much easier to carry out than the air transport provisions in the Act. Indeed, such monitoring could be left to an independent third party.

Finally, PIAC notes that, as reported in the Consultation Paper, the consumer surplus standard is used in the four other jurisdictions surveyed at page 30: the United States, European Union, United Kingdom, and Australia.[28] Adoption of a consumer surplus standard by Canada would be a step toward harmonization with these countries.

CONCLUSION

PIAC concludes that the efficiency defence found in s. 96 should be retained. However, to justify a merger, efficiency gains must satisfy the "consumer surplus" standard, i.e. they must not result, or be likely to result, in significantly higher prices to customers.

Some parties might consider this standard to be too stringent, in that it might block mergers that would otherwise generate efficiency gains large enough to more than compensate customers for redistributive losses. PIAC recommends that, in such

[26] Competition law authorities have traditionally been reluctant to take on ongoing surveillance of a firm or an industry. See for example Posner, *op. cit.*, at footnote one on page 2: "It might be possible to have one's cake and eat it by limiting the price charged by the efficient monopolist. That is the premise of public utility regulation, but, as I believe all competent students of antitrust agree, it is not a feasible project for antitrust law." However, there have been counterexamples in the U.S., the best known being Mr. Justice Harold Greene's ongoing oversight of the Bell System divestiture and accompanying constraints in the 1980s and early 1990s.

[27] Bill C-19 proposes removing industry-specific measures from the *Act*.

[28] According to Massimo Motta, *Competition Policy: Theory and Practice* (New York: Cambridge University Press, 2004) at 274: "So far, the EC in its decisions has not explicitly ruled out the possibility of using an efficiency defence, but it has not showed much sympathy for this argument either. Whenever cost reductions have been claimed by the merging parties, the EC has dismissed those claims on various grounds."

situations, the merged firm undertake to not increase its average price for a reasonable period of time, say three to five years. In this way, society will benefit from the efficiency gains, shareholders will profit and hence be motivated to seek out such efficiency gains, and customers will not be made worse off.

APPENDIX

In its Consultation Paper, the Competition Bureau invites parties to comment on a set of specific questions. The following are PIAC's observations.

1. At present efficiencies gains constitute a defence under s. 96. The Consultation Paper suggests that instead of a defence, efficiency gains could be one of a list of factors, found at s. 93, that inform the Competition Tribunal whether or not a merger is likely to substantially lessen competition.

   In PIAC's view, the presence or absence of efficiency gains does not affect any lessening of competition. Rather, it is a balancing factor in deciding whether a merger should be allowed, despite its anti-competitive effects. Thus, efficiency gains are not a factor on a par with the other factors in s. 93, and should not be confounded with them.

2. As explained above, PIAC favours the continuation of an efficiencies defence. However, the defence should employ a "consumer surplus" standard, i.e. it should be available only if the merged firm undertakes not to increase prices for a reasonable period of time.

3. The principal lesson to be learned from other jurisdictions, in PIAC's opinion, is the desirability of a consumer surplus standard in the efficiencies defence.

4. Savings from a reduction in output and gains that are redistributive in nature should never be counted as part of efficiency gains. Redistributive effects do enter the consumer surplus standard, however, in that redistribution from customers to shareholders as a result of a merger would not be permitted. Efficiency gains that are likely to be attained by another means should, in principle, also be excluded. However, if there are extra costs associated with "another means", avoidance of those extra costs could be counted as an efficiency gain attributable to the merger.

5. If efficiencies were to be treated as a factor in determining whether a merger significantly lessens competition, it is not clear what weight should be given to it. If efficiencies are a defence, either the standard is met or it is not. There may be some comfort in larger efficiencies gains, in that measurement is imprecise and a larger measured gain is less likely to reflect a true gain that is zero or negative, but otherwise the size of the gain should not matter. By contrast, if efficiency gains are one factor to be balanced against others, the size of the efficiency gains do matter. Thus, in the face of relatively modest efficiency gains, a merger may nevertheless be blocked.
6. PIAC agrees that any assessment of efficiencies is highly complex and requires elaborate evidence. PIAC notes that use of a balancing-weights standard would

make this burden even heavier, whereas use of a consumer surplus standard would not. Incorporation of efficiency gains as a factor under s. 93 would require the complexity of developing appropriate weights, explicitly or implicitly, for that factor.

7. In today's economy, increases in exports and in import substitution are no longer relevant and should not be the subject of special attention. S. 96(2) should be repealed.

8. Efficiency gains in all markets, whether the one in which the merger is taking place or another, should be counted. It is total welfare of society that should be maximized. PIAC recognizes, however, that evidence on efficiency gains in other markets may be difficult to obtain.