COMPETITION POLICY COUNCIL

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The Impact of the Supreme Court's New "Quantitative Evidence" Ruling on Business Mergers

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The recent Supreme Court of Canada decision in *Tervita Corp. v. Canada* raises the evidentiary standard and places a strong onus on the Commissioner of Competition to present all quantitative evidence possible when challenging some proposed mergers that may lessen or prevent competition. The Court's decision elevates the role of empirical analysis, in presenting quantitative arguments, to a hierarchical position that supersedes qualitative arguments, and may make merger challenges less likely than before to succeed. The ultimate implications are uncertain, and will be tested in subsequent cases.

This is the consensus view of the C.D. Howe Institute's Competition Policy Council, which held its ninth meeting on April 22, 2015.

The Competition Policy Council comprises top-ranked academics and practitioners active in the field of competition policy. The Council, chaired by Finn Poschmann, Vice President, Policy Analysis, at the C.D. Howe Institute, provides analysis of emerging competition policy issues. Professor Edward Iacobucci, Dean of the University of Toronto Faculty of Law and Competition Policy Scholar at the Institute, advises the program, along with the Institute's Benjamin Dachis, Senior Policy Analyst, and Aaron Jacobs, Researcher. The Council, whose members participate in their personal capacities, convenes a neutral forum to test competing visions and to share views on competition policy with practitioners, policymakers and the public.

The Council would like to warmly thank Ralph Winter for providing a briefing note to the group, and Ben Dachis, Aaron Jacobs, and Ed Iacobucci for their contributions.

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At Issue: On January 22nd, 2015, the Supreme Court of Canada issued a decision, *Tervita*, with major implications for merger analysis in competition law and policy. The case involved a challenge, from the Commissioner of Competition, to a proposed merger between two waste disposal firms on the grounds it would substantially prevent competition in the region where they operate, Northeastern British Columbia. What are the competition law and policy implication of *Tervita Corp. v. Canada* (Commissioner of Competition) 2015 SCC 3 [*Tervita*]?

Background and Prior State of Law

Section 92(1) of the *Competition Act* empowers the Commissioner of Competition to challenge a merger, at the Competition Tribunal, if it "prevents or lessens, or is likely to prevent or lessen, competition substantially." Among the options available to the merging parties, if challenged, is to invoke an efficiencies defence under the terms of section 96. The *Act* allows for mergers that substantially lessen or prevent competition if the potential gains in efficiency "will be greater than, and will offset, the effects of any prevention or lessening of competition." This is the "efficiencies defence."

The *Act* further specifies that if a merger is likely to bring about gains in efficiency, the Tribunal may not block it "by reason only of a redistribution of income between two or more persons." Section 96 therefore invites empirical analysis of factors such as likely price changes, and estimates of the price elasticity of demand, and of producer and consumer surplus, because gains in producer surplus may offset, in law, losses in consumer surplus (which is an economic term for the gain to consumers when they can buy a product for less than the maximum amount they are willing to pay). Canadian law does not necessarily elevate the economic interests of consumers above those of producers or their shareholders or employees. Finally, the *Act* provides no guidance on the weight the Competition Tribunal might place on such quantitative effects, as opposed to qualitative ones, such as environmental remediation costs in the example at hand.

Interpretation of section 96 of the *Act* was tested in the earlier case of *Superior Propane*, which established that the onus of proving that efficiency gains from the merger will be greater than and will offset the lessening of competition that results from the merger falls on the merging parties. It is "a balancing test that weighs efficiencies on one hand, against anti-competitive effects on the other."[1]

1 *Superior Propane I and II: Canada (Commissioner of Competition) v. Superior Propane Inc.* (2000), 7 C.P.R. (4th) 385; *Canada (Commissioner of Competition) v. Superior Propane Inc.*, 2001 FCA 104, [2001] 3 F.C. 185.

The Facts at Hand

Tervita Corporation is a supplier of disposal services for hazardous waste generated by oil and gas operations. By 2010, four permits for operating secure landfills for such waste had been issued in Northeastern British Columbia. Tervita held two and was operating the associated landfills. A third permit was held by an Aboriginal community, which did not yet operate a landfill under the permit. The fourth permit was held by Babkirk Land Services Inc., a wholly owned subsidiary of Complete Environmental Inc., but Babkirk was not operating in the market in July 2010, when Tervita signed a letter of intent to buy Complete.

The sale was set to close in January 2011, before which the Commissioner of Competition informed the parties that she opposed the transaction on the grounds that it was likely to prevent substantial competition in secure landfill services in Northeastern British Columbia. On the theory that Babkirk likely would have entered the market, absent the acquisition of Complete, the Commissioner asked the Competition Tribunal to order, pursuant to Section 92 of the *Competition Act*,[2] that the merger be dissolved or, in the alternative, that Tervita divest itself of Complete or Babkirk.

The Competition Tribunal found that the Commissioner had failed to establish quantitatively or sufficiently the competitive harms from the proposed merger, but that on balancing the potential quantitative and qualitative issues in the case, the proposed merger should indeed be rejected. In reaching this decision, the Tribunal concluded that existing plans to operate the Babkirk site as a bioremediation site would not have been successful, and Babkirk would therefore have competed, but for the merger, in landfill services. The Federal Court of Appeal reached substantially the same conclusion. The Court rejected the efficiencies defence on balance, concluding that "negligible" or "insignificant" efficiencies were insufficient to offset the anti-competitive harms of the merger.

In *Tervita*, the Supreme Court of Canada overturned the Federal Court of Appeal, dismissing the Competition Bureau's opposition to the merger, owing to the Commissioner's failure to meet the burden of proof the Court felt appropriate to the language of the *Competition Act*. The Supreme Court argued that the Bureau must quantify all elements that can be quantified in assessing the validity of a section 96 efficiencies defense for a merger that is challenged under section 92.[3]

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2 *Competition Act* (R.S.C., 1985, c. C-34); http://laws-lois.justice.gc.ca/eng/acts/c-34/page-59.html#h-40.

3 For more details on the case at hand, see summaries at: http://www.dwpv.com/~/media/Files/PDF_EN/2015/2015-01-23-SCC-Allows-Challenged-Merger-3.ashx http://www.osler.com/NewsResources/Supreme-Court-of-Canadas-Tervita-decision-provides-important-guidance-on-Canadas-merger-laws/ http://www.blakes.com/English/Resources/Bulletins/Pages/Details.aspx?BulletinID=2056 or http://www.goodmans.ca/files/file/docs/01.26.2015%20Comp%20Update.pdf

> It is the Commissioner's burden to quantify all quantifiable anti-competitive effects. Effects that can be quantified should be quantified, even as estimates, provided such estimates are grounded in evidence that can be challenged and weighed. If effects are realistically measurable, failure to at least estimate the quantification of those effects will not result in the effects being assessed on a qualitative basis. Effects will only be considered qualitatively if they cannot be quantitatively estimated. This approach minimizes the degree of subjective judgment necessary in the analysis and enables the Tribunal to make the most objective assessment possible in the circumstances.[4]

The Court thus created a new two-part test. It held that if the Commissioner does not present all quantifiable and estimable quantitative evidence of the anti-competitive effects resulting from a merger, then the Tribunal must give zero weight to the Commissioner's proffered quantitative anti-competitive effects, after which qualitative evidence may or may not come to bear.

A Hierarchy of Evidence: The Council's View

The Court's segmentation of quantitative and qualitative evidence apparently creates a hierarchy where none had existed before.

Many on the Council felt that *Tervita*'s categorical distinction between quantitative and qualitative evidence was philosophically troublesome, and that the distinction is more accurately one of degree. Further, the examples provided by the court – identifying price elasticity as clearly quantitative and product quality as qualitative – did not illuminate the distinction. One member pointed out that quality differences can be quantifiable as well. The dissent in *Tervita* observed that:

> [T]he need for "reasonable objectivity" does not justify a hierarchical approach to quantitative and qualitative aspects under the efficiencies defence; nor should qualitative effects be of lesser importance than quantitative effects. The statutory language of the Act does not distinguish between quantitative and qualitative efficiencies, and many of the wide-ranging purposes of the Act set out in s.1.1 may not be quantifiable … It is neither helpful nor necessary to predetermine their relative role and importance in the s.96 defence [12].

4 *Tervita*: https://scc-csc.lexum.com/scc-csc/scc-csc/en/14603/1/document.do.

A number of Council members voiced concern about what they felt was an unwarranted faith in quantitative evidence. Analyses of economic efficiency rely on estimating price changes, responsiveness of consumer demand, and the cost of production – all of which require data to be readily available. Moreover, the methods and assumptions employed are inherently imprecise, and will over- or under-estimate a lessening or prevention of competition.

It may not be possible to quantify anticompetitive effects, owing to inadequate data, but that would not mean a merger was necessarily benign. Some members indicated that the current adversarial system already creates the incentives for parties to bring credible evidence and to be tested on their precision, under cross-examination, and the requirement for quantification went too far. Many noted that it was odd for the Court to put such importance on objective verifiable quantitative evidence when, following *Superior Propane*, a decision with respect to section 96 ultimately relies on the judgement of Tribunal members, who have to weigh different kinds of anticompetitive effects.

The Consequences of the Ruling

The Council turned to addressing the potential consequences of the ruling, which affects Canadian business, the Bureau, and potentially the federal government.

Consequences for Canadian Business

The immediate consequence of *Tervita* is that the Commissioner may request significantly more information from parties seeking to merge, to satisfy the new quantitative evidence burden. In addition, some merging parties may be more inclined than otherwise to employ the efficiencies defence, especially if they believe the Bureau will not be able to present quantitative estimates of competitive harm. The parties to a challenge will further elevate economic analysis's role in litigation, and may make quantifiability an issue for litigation, were merger parties to claim that the Bureau could have quantified an effect and failed to do so, while the Bureau argued that the effect was not quantifiable.

There was also some disagreement among Council members about how wide-reaching might be the effect of the case. On one hand, some Council members felt the ruling simply requires the Commissioner to prove its case with empirical evidence, not speculation and, moreover, there are only a small number of cases where the efficiencies defence is likely to arise. On the other hand, other members were concerned that the number of cases involving debates over empirical data and the relevance thereof will expand, potentially beyond section 96 cases, and that in any event no matter the number of cases to which the law applies, the law should strive to make sense from a policy perspective.

Some also expressed concern that the emphasis on quantifying effects could have consequences elsewhere in competition policy, such as in vertical restraint cases, abuse of dominance and in competitor agreements that potentially prevent or lessen competition, and hence would have bearing on many arrangements that businesses might contemplate.

Consequences for the Competition Bureau

It is clear that Bureau now must do more to prove its case in merger reviews: the onus on the Bureau and the evidentiary burden have each increased. Some on the Council felt that the Bureau may be hesitant in future to bring merger review cases, given the new burden placed on it, or that it may seek to know earlier in the process whether the parties in question would employ the efficiencies defence. A few members expressed the view that the decision may inspire better and more rigorous quantitative work on the part of the Bureau, and perhaps explicit discussion of its ability to assemble it.

Many Council members felt that it was now incumbent on the Bureau to revise its merger enforcement guidelines and its competitor collaboration guidelines to reflect the new guidance from the Court on the efficiencies defence.[5]

Consequences for the Government

Does the Bureau's loss in *Tervita* mean that the government should amend the *Act*, for instance to qualify, in section 96, the Court's insistence that the Bureau quantify "all quantifiable anti-competitive effects" that might attach to a merger? After all, what is relevant in an economic sense, and whether a factor is "realistically measurable," are themselves subjective judgements to be reached in pursuit of an objective conclusion. Both quantitative and qualitative evidence may be probative if relied on thoughtfully.

Few Council members had appetite for immediate legislative change. Most Council members felt that the best course was to evaluate *Tervita*'s impact on behaviour, and respond as appropriate. There was disagreement about whether the *Tervita* decision would in principle allow the Commissioner to introduce qualitative evidence where quantitative data were hard to obtain. If the case law developed

5 At http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03420.html and http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03177.html.

a flexible approach to the quantification requirement, one that would reflect the inherent limitations of empirical methods, the decision may not prove problematic over time. On the other hand, if future cases inflexibly require quantification in all cases of effects that are quantifiable in principle, then *Tervita* will predictably make the efficiencies defence too easily available.

Some on the Council felt that the case showed the need for a change in judicial process and oversight of the Bureau. Many Council members questioned the initial decision even to bring the case, given the costs of enforcement versus the small scale of the merger. Many also questioned the decision of the Tribunal to substitute its own business judgement, for that of the principals, about the likely profitability of bioremediation at the Babkirk site. Given the importance of timeliness in mergers review, there is some concern that the Bureau has considerable power to exercise discretion to hinder mergers, and that this power is subject to little effective oversight.

Conclusions

The decision in *Tervita* invited mixed reactions from the Council. The majority view was that the Court ascribed a spurious precision to quantitative empirical methods, which risks introducing significant problems to the section 96 test, including an expansion in the number of parties invoking the efficiencies defence, which at the least would raise enforcement costs.

On the other hand, some on the Council also expressed the view that this approach may not matter much in practice, given the small number of cases in which the section 96 test is a pivotal factor, and that, in any event, insisting that the Commissioner prove a case was not objectionable. There was consensus that much will be revealed in time, depending on the manner in which future cases rely on *Tervita*. For that reason, there was consensus that little need be done about *Tervita* in the short run, but that the matter may require revisiting in the future.

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Members of the Council participate in their personal capacities, and the views collectively expressed do not represent those of any institution or client.

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