File No. CT 2005-006

COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34, as amended;

IN THE MATTER OF an application by B-Filer Inc, B. Filer Inc. doing business as GPAY GuaranteedPayment and NPay Inc. for an order pursuant to section 103.1 granting leave to make application under sections 75 and 77 of the *Competition Act*;

AND IN THE MATTER OF an application by B-Filer Inc., B-Filer Inc. doing business as GPAY GuaranteedPayment and NPay Inc. for an interim order pursuant to section 104 of the **Competition Act**.

BETWEEN:

B-FILER INC., B-FILER INC. doing business as GPAY GUARANTEEDPAYMENT and NPAY INC.

Applicants

\- and -

THE BANK OF NOVA SCOTIA

Respondent

AFFIDAVIT OF FRANK MATHEWSON

I, **FRANK MATHEWSON**, of the City of the Toronto, in the Province of Ontario, **MAKE OATH AND SAY**:

1. I am a Professor of Economics and Director of the Institute for Policy Analysis at the University of Toronto.

2. I have been asked by counsel to the Respondent, The Bank of Nova Scotia, to provide an expert opinion relating to economic issues arising from B-Filer's Application under Section 75 of the *Competition Act*.

3. I attach my report setting out my opinion on these issues as Exhibit "A" to this my Affidavit.

4. I attach a copy of my curriculum vitae as Exhibit "B" to this my Affidavit.

SWORN BEFORE ME at the City of Toronto, on Monday, July 31, 2006.	
"Yasmin Nizami" Commissioner for Taking Affidavits	"Frank Mathewson" **FRANK MATHEWSON**

File No. CT 2005-006

COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34, as amended;

IN THE MATTER OF an application by B-Filer Inc., B-Filer Inc. doing business as GPAY GuaranteedPayment and Npay Inc. for an order pursuant to section 75;

BETWEEN:

B-FILER INC., B-FILER INC. doing business as GPAY GUARANTEEDPAYMENT and NPAY INC.

Applicants

-and-

THE BANK OF NOVA SCOTIA

Respondent

REPORT OF PROFESSOR FRANK MATHEWSON

A. MANDATE

1. I have been asked by counsel to The Bank of Nova Scotia ("Scotiabank") to provide an opinion on two economic issues concerning this case. The first economic issue is product market definition for the purposes of Section 75(1)(a) and 75(1)(b). I have been asked to provide an opinion on the boundaries of the product market, and I have also been asked to provide an opinion on whether the product market claimed by the Applicants is appropriate. The second economic issue that I have been asked by counsel to address is the effect on downstream competition of Scotiabank's termination of its banking relationship with the Applicants. Counsel has also asked me to provide comments on the Affidavit of the Applicants' economic expert, Dr. Lawrence P. Schwartz.

2. My curriculum vitae is attached as Appendix A to this Report.

B. DOCUMENTS RELIED UPON

3. In preparing this Report, I have relied on documents produced by Scotiabank and Applicants in this proceeding, on the transcripts for the discovery of the Applicants and the Respondent, on information provided to me by Scotiabank, and on publicly available data and information. The documents that I have relied on to prepare my Report are listed in Appendix B to this Report.

C. SUMMARY OF CASE

4. This case involves the decision by Scotiabank to terminate its banking relationship with the Applicants. The Applicants are B-Filer Inc., B-Filer Inc. doing business as GPAY GuaranteedPayment, and NPay Inc. This Report refers to the Applicants collectively as either "the Applicants" or "GPay". GPay, in conjunction with its joint venture partner UseMyBank, supplies what it calls an "internet bank card debit payment service". This service facilitates online payments from consumers to merchants. In this Report, this service is labelled "the GPay service". To provide its service, GPay makes use of the online bill payee functions of several Canadian banks, the E-mail Money Transfer ("EMT") service provided by Canadian banks, and a number of **[CONFIDENTIAL]** deposit accounts at Canadian banks.

5. From the inception of the GPay service until September 2005, Scotiabank provided GPay with bill payee status on Scotiabank's online banking service and supplied a number of deposit accounts to GPay that GPay used to provide its service. Scotiabank terminated its banking relationship with GPay as of September 2005, and thereafter GPay had neither bill payee status nor deposits accounts at Scotiabank.

6. This termination by Scotiabank is the subject of this proceeding. Applicants claim that 'Scotiabank Biller Services', which refers to online bill payee status, is a product market; that 'EMT **[CONFIDENTIAL]** Deposit Accounts' comprise a product market; and that Scotiabank's termination of its relationship will have an adverse effect on competition in the market for online debit payments. Scotiabank offers the Interac Online debit payment service to its banking customers, and Applicants and their economic expert claim that GPay competes with Interac Online but not with other online payments methods, such as credit cards.

D. SUMMARY OF ECONOMIC OPINION

7. My economic opinion is that Scotiabank Biller Services and EMT Business Deposit Accounts, are not, as claimed by Applicants, properly defined product markets for the purposes of this case. Consistent with previous refusal to deal cases decided by the Tribunal, the product market analysis presented in this Report focuses on the products that the Respondent allegedly refuses to supply (that is, for the purposes of Section 75(1)(a) and 75(1)(b)) and considers whether there are alternative products which Applicants could use without being substantially affected by the substitution. In this regard, the conclusions are as follows:

1) **[CONFIDENTIAL]**, and perhaps other products, are in the same product market with 'EMT **[CONFIDENTIAL]** Deposit Accounts'. Applicants currently use **[CONFIDENTIAL]**

deposit accounts at Royal Bank, Bank of Montreal, and CIBC to receive EMTs.[1] Applicants use these accounts in the same way that they used **[CONFIDENTIAL]** deposit accounts at Scotiabank before termination and in the same way that they currently use **[CONFIDENTIAL]** deposit accounts at Royal Bank. These products are identical in all their relevant features, including their limits for receiving EMTs. There appears to be no evidence on the record that **[CONFIDENTIAL]** deposit accounts are not substitutable for **[CONFIDENTIAL]** deposit accounts for receiving EMTs;

2) Scotiabank Biller Services is not a product market; the market that includes Biller Services also includes EMT deposit accounts (**[CONFIDENTIAL]**). The primary differences between processing payments via Biller Services compared to using EMTs are that (i) payers (not GPay) pay an additional fee (currently $1.50 per transaction) to their bank – half of which is then remitted to Certapay,[2] the Company responsible for the EMT product – when GPay processes a payment using EMTs; and (ii) there is a $1,000 per day limit on sending EMTs, while the maximum bill payment permitted on Scotiabank's online bill payment system is $49,999.[3] Although GPay claims that substitution of EMTs for Biller Services for processing payments has caused some inconvenience for GPay (this remains to be established), and the data indicate that payments processed by GPay from Scotiabank accounts fell immediately after termination, these effects on GPay's business cannot be said to be 'substantial'. Scotiabank customers account for only about **[CONFIDENTIAL]** percent of day-to-day banking in Canada,[4] and payments from Scotiabank accounts represented about 20 percent of GPay's volumes processed and 20 percent of the number of GPay transactions in the year before Scotiabank's termination of GPay's Biller Services (September 2004 to August 2005, inclusive).[5]

However, it is not necessary to speculate whether GPay could substitute towards other products without being substantially affected, because there is evidence with respect to the

---

[1] BFI001581 ("**[CONFIDENTIAL]** accounts where GPay can deposit EMT's"), and Discovery of Raymond Grace, July 28, 2006.

[2] Certapay is a division of Acxsys Corporation (https://www.certapay.com/en/newsEvents/factSheet.html). The shareholders of Acxsys Corporation are Bank of Montreal, CIBC, Royal Bank, Scotiabank, TD Canada Trust, National Bank of Canada, Desjardins Group and Credit Union Central of Canada (http://www.acxsys.ca/about.php).

[3] Information provided by Scotiabank. The limit maximum payment to a bill payee at the Bank of Montreal is $10,000, and the maximum at Royal Bank is $100,000. Discovery of Raymond Grace, July 28, 2006.

[4] Internal confidential data from Scotiabank.

[5] BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

products GPay substituted towards after termination and how this substitution affected GPay's business. As claimed by Applicants and noted above, the Scotiabank volumes processed by GPay fell after termination in September 2005. However, as of June 2006, GPay's payment volumes from Scotiabank accounts are now approximately at the levels that they reached prior to Scotiabank's termination, despite the fact that GPay has had to substitute away from Scotiabank bill payee status and business deposit accounts.[6]

With respect to the effect of Scotiabank's termination on downstream competition, the conclusion is as follows:

3) Scotiabank's termination of its relationship with GPay will have a minimal, if any, effect on competition. In the analysis of the competitive effects, consideration is given to whether Scotiabank's termination would enhance or preserve any Interac Online market power. The Applicants' service and the service with which Scotiabank is associated, Interac Online, appear not to be close substitutes, and consequently the Applicants' service would not constrain any hypothetical attempt by Scotiabank to exercise any supposed market power with respect to Interac Online. Approximately 98 percent of current payments processed by GPay are made to online offshore casinos,[7] while none of Interac Online's merchants are online offshore casinos.[8] Scotiabank has also indicated that Interac Online will not allow online offshore casinos or their management companies to receive payments through the Interac Online system.[9] Furthermore, there are many other forms of payment for online purchases, such as credit cards and e-wallets that are likely to be closer substitutes for Interac Online than GPay, so that these closer substitutes would impose greater discipline on any hypothetical market power accruing to Interac Online. Absent GPay, the products remaining in the market are sufficiently close substitutes for Interac Online that Scotiabank could not exercise any market power.

4) Existing Scotiabank consumers who wish to use GPay have alternatives to meet their needs, including credit cards. If the demand for online offshore gambling is relatively price inelastic, as seems likely, then these consumers facing any incremental cost of using GPay

---

[6] BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

[7] Answers to Undertakings of Ray Grace.

[8] See the list of 'Participating Merchants' of Interac Online are listed at http://www.interaconline.com/merchants_merchants.php?page=2. None of these merchants are online casinos.

[9] Affidavit Evidence of Robert Rosatelli.

without its previous Scotiabank banking relationship will suffer a relatively small loss of consumer surplus. With respect to future consumers, there is no evidence presented by the applicants that GPay will develop into a viable and sustainable payment mechanism as a substitute for instruments such as debit and credit cards and other online payment instruments. GPay's current business portfolio may be the best indicator of its viable future business portfolio, a business that Scotiabank does not wish to serve.

5) Scotiabank terminated its banking relationship with GPay for a number of reasons including the fact that GPay's manner of conducting business requires banking customers to disclose their online banking password. Scotiabank also sought to minimize the legal, reputational, and regulatory risks associated with continuing to do business with GPay.

8. Thus, Scotiabank's termination of GPay's banking services was not driven by a strategic attempt to disadvantage a competitor, or to dampen competition for current or future merchants or consumers.

E. KEY FACTS AND OVERVIEW OF APPLICANTS' SERVICE

9. This section of the Report describes how the GPay service works, describes in detail the banking services that were supplied by Scotiabank to GPay, and provides a timeline of the GPay service.

I. The GPay Service

10. The GPay service appears to work as follows:

Step 1: GPay receives a request from a payer to transfer funds to an online merchant.

Step 2: The payer transmits his/her online banking information (including username and password) to GPay. GPay uses this information to access the payer's account and transfer funds from the payer's account to GPay's own account. The means by which GPay effects the transfer of funds to its own account depends on whether the payer wishes to transfer funds located at a financial institution where GPay has bill payee status.

As a general matter, if the payer wishes to make a payment from an account held at a bank with which GPay has bill payee status, GPay obtains, from the payer, the information required to access the payer's account, including the account number and internet banking password. GPay uses the bill payment feature on the bank's internet banking service to transfer funds from the payer's account to its own biller suspense account at the same bank.[10]

If the payer wishes to transfer funds from an account with a bank with which GPay does *not* have biller payee status, GPay transfers the funds from the payer's account using the EMT feature of the account holder's account. GPay obtains the payer's bank account number and password for online banking access, and uses the EMT service to transfer funds from the payer's account to its own deposit account.[11]

Step 3: Payments made *via* online bill payment are released from GPay's suspension account each evening, at a time designated for the release of all bill payment funds on the day that the bill payment is made.

Step 4: GPay transfers funds among its various accounts and then transfers some of these funds (i.e. payment values net of merchant discounts) from its current accounts at the Bank of Montreal to the payee. Funds are transferred to payees via electronic means.

II. Overview of Banking Services Supplied by GPay

Scotiabank Biller Services

11. The Scotiabank bill payment service is offered as a convenience to its banking customers, to allow Scotiabank customers to pay for bills using internet banking or telephone banking. The system was intended to allow banking customers to pay such things as their tax, water, and utility bills. The system was not intended for use by a company such as GPay to transfer large sums of money out of banking customers' accounts to GPay's accounts as a flow-through, and then eventually out to merchants.[12]

12. Money directed to a particular bill payee, in this case, GPay, would be held in the bank's suspension account and then released to the bill payee on the evening of the day on which the money was directed to a particular bill payee. In the case of Scotiabank, bill payments made before 8:30 p.m. are held in a Scotiabank suspension account and are released to the bill payee to whom the funds were directed at 8:30 p.m. each evening. Bill payments made after 8:30 p.m. are directed to the bill payee the following day.

---

[10] Amended Notice of Application Pursuant to Sections 75 and 77 of the Competition Act, 8.6(i).

[11] Amended Notice of Application Pursuant to Sections 75 and 77 of the Competition Act, 8.6(i).

[12] Affidavit Evidence of Robert Rosatelli.

13. Bill payments can be cancelled. If a customer has made a bill payment, he or she can reverse that bill payment at any time prior to the funds being released from the suspension account at 8:30 p.m.[13]

E-mail Money Transfers

14. E-mail Money Transfers allow deposit account holders at participating financial institutions to 'send' funds electronically from their own accounts to account holders at participating banks. Currently, EMTs can =be used to transfer funds from accounts at Bank of Montreal, Scotiabank, CIBC, TD Canada Trust, and Royal Bank.[14] Recipients of EMTs with accounts at Bank of Montreal, Scotiabank, CIBC, TD Canada Trust, or Royal Bank, who have registered for online banking can deposit the received funds into their accounts after receiving an e-mail notification. Funds are deposited to the recipient's account after the recipient enters the answer to a security question provided by the sender and selects an account to which the funds are to be deposited. Since May 2005, there has been a thirty minute hold on all EMTs,[15] which allows the sender to cancel the payment within this time.

15. CIBC, TD Canada Trust, and Bank of Montreal allow EMTs to be received only into **[CONFIDENTIAL]** accounts, while Scotiabank and Royal Bank allow EMTs to be received into either **[CONFIDENTIAL]** accounts.[16] However, none of these banks allow business customers to receive EMTs in circumstances where the business customer no longer qualifies as a small business, but instead has volumes which cause it to be classified as a commercial banking customer.[17] The limits on sending of funds *via* EMT for an individual banking customer per profile are $1,000 per day, $3,000 per week, and $7,000 per month. The limits on receiving EMTs into **[CONFIDENTIAL]** profiles are $10,000 per day, $70,000 per seven day period, and $300,000 per thirty day period.[18] Each profile may be associated with multiple accounts, but the limits on the dollar value of funds that can be deposited *via* EMT are imposed on the profile, rather than on the account. Banks typically limit the number of profiles that can be held **[CONFIDENTIAL]**.

---

[13] Undertakings on the Examination for Discovery of Robert Rosatelli.

[14] https://www.certapay.com/en/.

[15] Undertakings on the Examination for Discovery of Robert Rosatelli.

[16] Confidential transcript of Raymond Grace.

[17] Affidavit Evidence of Colin Cook.

[18] Confidential transcript of Raymond Grace.

16. Raymond Grace has indicated that Canadian banks grant EMT limits on the basis of a profile as opposed to the actual number of accounts. Profiles are calculated on a "per connection" basis. In other words, if Mr. Grace had six **[CONFIDENTIAL]** accounts **[CONFIDENTIAL]** at a particular bank, this would be considered one profile. **[CONFIDENTIAL].**[19]

III. Timeline of the GPay Service

17. The remainder of this section provides a timeline of key events in the evolution of GPay, including its bill payee status at Canadian banks and its acquisition of various deposit accounts for the receipt of EMTs.

- Raymond Grace incorporates B-Filer and begins using the GPAY GuaranteedPayment business name in September 1997

- Between September 1997 and some time in 1999, Mr. Grace obtained bill payee status and biller accounts for B-Filer at all five major Canadian chartered banks (CIBC , TD Bank, Royal Bank, Bank of Montreal, and Scotiabank) and Alberta Treasury Branches ("ATB")

- GPay and UseMyBank entered into a joint venture agreement in September 2002

- The GPay service began operations in December 2002, and GPay signed its first customer in March 2003.

<u>GPay's Bill Payee Status</u>

- GPay has had bill payee status at Bank of Montreal and Royal Bank since inception, and at Caisse Populaire since 2004; this status continues at these banks

- GPay had bill payee status at TD Canada Trust, CIBC, and Alberta Treasury Branches since inception until late 2003, when these financial institutions terminated GPay's status as a bill payee on their bill payment systems

- GPay had bill payee status at Scotiabank since inception until Scotiabank's termination of GPay's banking services in September 2005.

<u>GPay Accounts for Receipt of EMTs</u>

---

[19] Confidential transcript of Raymond Grace.

18. GPay controls a number of **[CONFIDENTIAL]** accounts into which GPay payments are transferred *via* EMT. As explained above, GPay uses EMTs only to receive payments initiated from accounts at banks with which GPay does not have bill payee status.

19. GPay-controlled **[CONFIDENTIAL]** account profiles are **[CONFIDENTIAL]**.[20] As a result, GPay can receive up to $170,000 per day, $1,190,000 per seven day period, and $5,100,000 per thirty day period into the accounts that it currently controls. This is in addition to the unlimited amounts that it can deposit into its accounts *via* the online bill payment systems at Bank of Montreal, Royal Bank, and Caisse Populaire. Up to June 2006, the maximum volume of bill payee and EMT transfers that GPay processed in any month was $5,196,221, and the maximum total volume that GPay has processed via just EMTs in any month was $2,589,433. Mr. Grace has testified that several of his profiles are 'back up' profiles, which he uses infrequently, and only when his main profiles reach their capacity. Mr. Grace's evidence on his confidential transcript in June 2006 is to the effect that the Applicants have never had to turn away a single customer wishing to transfer money using UseMyBank, because they have never reached full capacity.

20. There is no evidence on the record that indicates that there are any limits to the number of profiles under GPay's control for receipt of EMT transfers. GPay can increase its capacity to accept EMTs by simply opening new profiles **[CONFIDENTIAL]**.

F. PRODUCT MARKET

21. In their Amended Application, Applicants assert that they are unable to obtain adequate supplies of the following two products: (i) Scotiabank Biller Services; and (ii) E-mail business deposit accounts.[21] In effect, the Applicants and their economic expert have claimed that each of these products is a product market for the purposes of section 75(1)(a) and 75(1) (b) of the *Competition Act*. Sections 75(1)(a) and (b) of the *Act* read as follows:

> **75.** (1) Where, on application by the Commissioner or a person granted leave under section 103.1, the Tribunal finds that
>
> (*a*) a person is substantially affected in his business or is precluded from carrying on business due to his inability to obtain adequate supplies of a product anywhere in a market on usual trade terms,
> (b) the person referred to in paragraph (a) is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market

[20] BFI001581 ("**[CONFIDENTIAL]** accounts where GPay can deposit EMT's") and Discovery of Raymond Grace, July 28, 2006.

[21] Amended Notice of Application Pursuant to Sections 75 and 77 of the Competition Act, 8.1.

> the Tribunal may order that one or more suppliers of the product in the market accept the person as a customer within a specified time on usual trade terms...

22. In previous refusal to deal cases, for purposes of section 75(1)(a), the Tribunal found that the 'product' must be defined in relation to the effect of the refusal on the business of the person denied. In *Chrysler*, for example, the Tribunal wrote: "In the case of paragraph 75(1)(a), the ultimate test concerns the effect on the business of the person refused supplies."

23. Accordingly, when assessing the substitutability of other products for 'Scotiabank Biller Services' to determine whether these other products belong in the same product market, the operative principle is that other products are substitutes if the purchaser's business is not substantially affected by switching to these other services. In other words, if GPay, or a supplier of similar services, can switch from Scotiabank Biller Services to an alternative, say product A, without its business being substantially affected because of this switch, then product A belongs in the same product market with Scotiabank Biller Services.

Overview of the Economics of the GPay Service

24. Payment cards are an example of a two-sided market where buyers and sellers interact through a 'platform'. In a payment card system, the buyer is the cardholder, and the seller is the merchant. Benefits accrue to both the cardholder and the merchant when the cardholder uses her card to make a payment. The value of the net benefit to each depends on usage charges, which are set by the owner of the platform. This mutual interdependence derives from a network effect: the cardholder is better off the greater the number of merchants that accept the card and the merchants are better off the greater the number of consumers who use the card. A larger customer group may also endow the card user customers with enhanced group purchasing power.

25. In the case of GPay's service, only merchants bear the usage charges, and GPay charges no fees to payers. GPay charges a remittance fee to the merchant, which is the sum that it subtracts from the payment that it transfers to the merchant from payers. The remittance fee currently ranges up to **[CONFIDENTIAL]** percent of the amount of the payment to the merchant,[22] and the discount for a particular merchant is the result of a negotiation between GPay and the merchant. GPay's average remittance fee on payments made between January and November

[22] BF001532 ("GPay Client Rates as of June 2006")

2005 was **[CONFIDENTIAL]** percent.[23] This means that for every $100 in payments through the GPay system, GPay receives on average $**[CONFIDENTIAL]**.

26. Although payers in GPay's system do not pay any charges directly to GPay, they may incur charges, paid to their bank, which are associated with the transactions made from their accounts by GPay. When GPay processes a payer's payment as a bill payee at the payer's bank, the payer pays any fees associated with the bill payment. At most banks, an online bill payment is considered to be a transaction which either counts as a 'free' transaction if the account's free transaction limit has not yet been reached, or the account holder is charged for the transaction if she has exceeded her limit of free transactions. When GPay makes a payment from a payer's account using an EMT, the payer bears the EMT charge and it also pays any applicable transaction fees. As with online bill payments, EMTs normally count as transactions for which the account holder may be charged, depending on the details of the account.

27. In order to generate revenues, GPay needs to attract both merchants and payers. As a general matter, there will be some price elasticity in the demand on both sides of the market: the higher the costs to the merchant (in particular through higher merchant discounts), the fewer the number of merchants who will want to participate. The higher the transaction fees paid by payers, the lower will be the realized value on their transactions. Some of the costs incurred by merchants and buyers are not chosen directly by GPay. As discussed above, they are set by payers' banks. These bank fees and restrictions are the primary subject of this case. On the payer side, different payment methods used by GPay (i.e. Biller Services and EMTs) result in different overall charges to payers, since the payer is responsible for all bank transaction fees and EMT and online bill payments attract different levels of fees. On the merchant side, the profitability of participating in the GPay service depends on a number of factors, such as transaction limits, speed of payment, and finality of payment. As explained below, Scotiabank's termination of GPay's banking services may have an impact on these profitability factors, and to the extent that they affect the number of GPay transactions, the termination can also potentially affect GPay's profitability.

28. This serves as product background to permit an analysis of product markets and the competitive implications of Scotiabank's termination of GPay's banking services.

[23] Calculations based on Exhibit 4 to Answers to Undertakings of Ray Grace.

IV. *Is access to Scotiabank Biller Services a 'Product'?*

29. The product market definition principle discussed above implies that Scotiabank Biller Services is a product market only if the purchaser of Scotiabank Biller Services (i.e. GPay) cannot switch to other substitute products without being substantially affected in its business. A determination of which other products should be included in the product market requires a consideration of GPay's options when Scotiabank terminated GPay's bill payee status.

30. GPay used Scotiabank Biller Services only when it processed payments from Scotiabank accounts. As outlined above, GPay would enter the Scotiabank account of the payee and make a bill payment to itself using Scotiabank online banking. The payer would incur no fees except for any transaction fees associated with making an online bill payment. These fees vary with the type of account, and most Scotiabank accounts allow some fixed number of 'free' transactions per month, with a $0.50 fee for every transaction in excess of the monthly limit. GPay itself would incur no fees when receiving a payment as a bill payee.[24]

31. The most obvious potential substitute for bill payee status at Scotiabank is the use of EMTs. This alternative is the most obvious because: (i) it is the option chosen by GPay when Scotiabank terminated GPay's bill payee status (along with GPay's other Scotiabank services) in September 2005; and (ii) it is the alternative to bill payee status at TD Canada Trust, CIBC, and ATB chosen by GPay when these banks terminated GPay's bill payee status in 2003.

32. There are three potential ways in which the switch from Scotiabank bill payee status to the use of EMTs to process payments from Scotiabank customers could have a detrimental effect on GPay's business. These are: 1) the limits on the amount that can be transferred via EMT are lower than the limits on online bill payments, and this could prevent GPay from processing payments from Scotiabank accounts which exceed these limits; 2) there are fees (payable by the banking customer but not by GPay) associated with sending funds through EMTs, which could reduce the demand for GPay services by Scotiabank account holders; and 3) the use of EMTs may increase GPay's costs of processing payments, which could render GPay a less effective competitor and reduce its profits. The discussion below deals with each of these in turn.

<u>EMT Transfer Limits</u>

[24] Undertakings on the Examination for Discovery of Robert Rosatelli.

33. Most banks impose limits on the amount of money that can be sent in an individual EMT and on the amount that can be sent in a twenty-four hour period from a single profile. For most banks, these limits are $1,000 per transaction and $1,000 per day. The limit on the value of a payment that can be made through online bill payment at Scotiabank is $49,999. By substituting EMT transfers for Biller Services for payments from Scotiabank accounts, GPay is potentially losing revenue by not having the ability to process transactions with a value of over $1,000 and by not having the ability to allow payers to make payments with a total value of over $1,000 in a twenty four hour period.

34. When Mr. Grace was asked on discovery how many GPay payments from accounts at Bank of Montreal, Royal Bank, and Caisse Populaire – all banks where GPay has Biller Services – exceeded $1,000, he said he didn't know.[25] Scotiabank has provided useful information in this regard. The bank has provided data on individual GPay payments made from Scotiabank accounts in April 2005, the last full month before Scotiabank terminated GPay's banking services.[26] In that month, according to Scotiabank, GPay processed 5,667 payments from Scotiabank accounts, for total dollar value of $**[CONFIDENTIAL]**. The number of transactions with value over $1,000 during this month was fifteen, representing just 0.26 percent of the total number of transactions. The sum of the value of transactions for more than $1,000 was $22,383, or 4.6 percent of the total value of transactions. Applicants have subsequently provided monthly data on the total value of individual GPay payments exceeding $1,000 from Scotiabank accounts before Scotiabank's termination in September 2005 (i.e. when GPay processed these accounts through Biller Services rather than EMTs). Between June 2004 and August 2005, GPay payments from Scotiabank accounts exceeding $1,000 accounted for 7 percent of all payments from Scotiabank accounts over this period.[27]

35. These percentages represent an upper bound on the reduction in GPay payments that would have occurred had the EMT limit on transactions been in place at the time. Because of the $1,000 limit on transfers, individuals wishing to transfer more than $1,000 are given a message that they must try a lower amount. The vast majority of GPay payments are made to online casinos (or their management companies), so that the amount of the transfer to the merchant is discretionary; it

---

25 383. Q. With respect to the financial institutions where you still have bill payee status, which is Royal Bank, Bank of Montreal and Caisse Populaire, what percentage of the payments made are for payments greater than $1,000 at those banks?

A. Offhand, I don't know.

26 The source of this data was an analysis undertaken by Scotiabank Manager of Bill Payment Services, Nellie Marcoux.

27 BFI001585 ("GPay payments from Scotiabank accounts over $1,000").

is therefore reasonable to assume that, a banking customer who tried unsuccessfully to transfer, say, $1,250 through GPay to a casino, would retry the transfer at $1,000 and would be successful. The EMT limit is therefore likely only to reduce the value of individual payments made through GPay, rather than eliminate them altogether. Furthermore, since these fifteen payments from Scotiabank in April 2005 were accounted for by just four individuals, it is reasonable to expect that had the limit on GPay transactions from Scotiabank accounts been $1,000 at the time, these individuals had the option to open (or use existing) accounts at other banks where bill payment status is still available (Royal Bank, Bank of Montreal, and Caisse Populaire) and made payments to GPay from these accounts.

36. There is no evidence on the record indicating that the EMT limits prevented any merchants with sales potentially exceeding $1,000 from signing up with GPay. In response to a question for discovery with respect to whether the EMT limits on GPay payments from CIBC and TD Canada Trust deterred any merchants from participating in the GPay system, Mr. Grace responded that he didn't know:

> Q. At any time prior to September 2005; in other words, while you still had your banking services at Scotiabank, was there any circumstance where the joint venture entered into discussions with a prospective merchant, but the merchant didn't ultimately sign up with UseMyBank because banking at TD and CIBC were limited to a $1,000 payment because you had to transfer by EMT?
>
> A. I don't really know.[28]

37. Mr. Grace responded in a similar manner to a more general question about whether the EMT limit had any effect on the decisions of merchants to participate in the GPay system:

> Q. Mr. Grace, are you aware of any merchant that wouldn't sign up with UseMyBank because some banking customers are limited to $1,000 transaction limit?
>
> A. That have told me that that was the reason?
>
> Q. Not that they have told you personally, but you are aware of through any source?
>
> A. I don't believe so. I don't know. No one ever specifically said that and no one ever implied that, so I don't know.[29]

38. Based on the lack of evidence that the EMT limit deters any transactions from occurring (in addition to the relatively low value of transactions exceeding $1,000) or limits the ability of GPay to

[28] Transcript for Discovery of Raymond Grace, June 27, 2006, Question 412.

[29] Transcript for Discovery of Raymond Grace, June 27, 2006, Questions 416 and 417.

sign up merchants, the conclusion appears to be that the limit on EMT transactions does not prevent EMTs from being included in the same product market with Biller Services.

EMT Fees

39. Payers whose payments are transferred by GPay through the EMT system must pay a fee for each EMT, in addition to any account fees. Each EMT sent from an account is counted as a transaction under Scotiabank's account plans, and account holders who make an EMT will either reduce their number of remaining 'free' account transactions or will pay a transaction fee. The fee for EMTs is currently $1.50 per transaction. This EMT fee effectively increases the cost to the payer of making a payment through GPay, and although GPay does not absorb this fee in any way, payers may reduce their demand for GPay's service because their 'all in' cost of making a payment has increased. This reduction in payments could, in turn, reduce demand by merchants to sign on to be GPay merchants and may therefore reduce GPay's revenues and profits.

40. This additional fee will reduce GPay's revenues only if Scotiabank payers respond to this price increase by reducing the value of transactions they make through GPay. The value of payments processed by GPay would decrease if payers would forego spending on the same products in response to the price increase, if they would stop purchasing online and instead use other channels to make their purchases, or if they would continue to spend the same amount online but would use another online payment method, such as a credit card or e-wallets, such as PayPal, instead.

41. The average value of a GPay transaction from a Scotiabank account in the year prior to termination (September 2004 to August 2005) was about $90.[30] An additional fee of $1.50 would result in an increase in the average price paid for a payer's purchase of about 1.7 percent. While it is an empirical matter, it seems unlikely that GPay payers would either forego purchasing altogether or switch to another distribution channel in response to such a small price increase, especially given the nature of most of GPay's merchants: as noted, about 98 percent of GPay payments are made to fund participation in online casinos,[31] and by their nature these products cannot be purchased other than on the internet. The expectation is, therefore, that GPay payments from Scotiabank accounts would decrease only if payers would switch to other means of online payments.

---

[30] BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

[31] Answers to Undertakings of Ray Grace.

42. There does not appear to have been any switching by Scotiabank payers towards Interac Online after GPay began using EMTs to process payments from Scotiabank account holders. There is no overlap in the merchants served by each of GPay and Interac Online. The total value of Interac Online payments made from accounts at all participating banks in October 2005, the month after termination, **[CONFIDENTIAL]**,[32] amounting to only about **[CONFIDENTIAL]** of the $**[CONFIDENTIAL]** in payments processed by GPay from Scotiabank accounts. It therefore seems unlikely that Scotiabank account holders switched to Interac Online in response to the introduction of the EMT fee.

43. It is again informative to examine the actual behaviour of Scotiabank account holders after GPay began processing their payments through EMTs rather than Biller Services. The expectation is that since the EMT charge applies to each transaction, and does not increase with the value of the transaction, then if the charge has any effect on the demand for GPay services, it would reduce the *number* of transactions, but not necessarily the average value of transactions. However, by December 2005, the third month after Scotiabank's termination of GPay, the number of GPay payments from Scotiabank's accounts was higher than it was in any previous month (including the months when GPay had bill payee status with Scotiabank).[33] Although the number of payments from Scotiabank accounts increased by less than the increase in the number of payments from Bank of Montreal and Royal Bank, that they increased is consistent with the view that the switch to EMT did not have a major effect on Scotiabank account holders' behaviour with respect to the GPay service.

Effect on GPay's Costs

44. Mr. Grace has indicated that GPay's costs of processing payments *via* EMTs are higher than its costs of processing using Biller Services. In his answer to an undertaking, Mr. Grace stated that

> The additional costs of processing EMTs include the following: (i) increased accounting costs for managing EMT deposits and transfers from EMT deposit account; (ii) increased programming costs; (iii) increased bank fees, and (iv) GPAY maintains a $5,000 balance in each account used for EMT deposits. To deal with EMT accounting and management, UseMyBank has hired two new employees since September 2005 to deal with the increased

32 Data provided by Scotiabank.

33 BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

workload associated with EMTs; Kevin Edgar, a GPAY employee spends about 10 hours per week dealing with EMT cancellations. [34]

These statements neither quantify the additional costs of using EMTs rather than Biller Services for processing Scotiabank payments, nor provide a reasonable basis for doing so. Furthermore, there does there appear to be any information on the record that would permit a quantification of such costs. With the available information, it is impossible to determine whether the alleged increase in costs suffered by GPay because it switched to EMTs from Biller Services could be said to have substantially affected GPay's business.

V. *Are 'EMT Business Deposit Accounts' a 'Product'?*

45. GPay uses what it calls EMT Business Deposit Accounts to receive payments that it transfers *via* EMT from payers' accounts. As explained above, GPay uses EMTs to process payments from accounts at banks where it does not have bill payee status. Only Scotiabank and Royal Bank allow EMTs to be deposited directly into business accounts (but only into small business accounts, not commercial banking accounts), and GPay claims that with Scotiabank's termination of GPay's banking services, GPay has access to only Royal Bank's business accounts for receipt of EMTs.

46. The analysis above of the product market for Scotiabank Biller Services began with a consideration of the actions actually taken by GPay in response to Scotiabank's termination of GPay's accounts. In October 2005, the month after Scotiabank's termination of GPay, GPay processed payments totalling $**[CONFIDENTIAL]** through EMTs (i.e. from accounts held at Scotiabank, CIBC, and TD Canada Trust).[35] These amounts had to be received into accounts at one or more of the Canadian banks that allow for the receipt of EMTs.

47. Applicants have testified that they are allowed only one **[CONFIDENTIAL]** profile at Royal Bank, and that this profile has a limit of $300,000 in EMT receipts per month, which is just over 20 percent of the total value of transactions processed by GPay through EMTs in October 2005. As noted above, Mr. Grace said during his discovery and confirmed in his answers to undertakings that GPay controls **[CONFIDENTIAL]** profiles, which he uses to receive EMTs.[36] There appears to be

---

[34] Answers to Undertakings of Ray Grace, Question 1244.

[35] Total value of payments processed by GPay in October 2005 was $**[CONFIDENTIAL]**. BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

[36] BFI001581 ("**[CONFIDENTIAL]** accounts where GPay can deposit EMT's"), and Discovery of Raymond Grace, July 28, 2006.

no evidence on the record that indicates that there are any disadvantages whatsoever arising from receiving EMTs into **[CONFIDENTIAL]** deposit accounts rather than **[CONFIDENTIAL]** deposit accounts. Nor does there appear to be any evidence on the record that **[CONFIDENTIAL]** accounts have any features that are lacking in **[CONFIDENTIAL]** deposit accounts that are relevant for the current proceedings. In fact, the only suggestion that **[CONFIDENTIAL]** accounts are not in the same market as **[CONFIDENTIAL]** accounts on the record, as far as currently known, is in the Applicants' claim in its Amended Application that 'EMT **[CONFIDENTIAL]** Deposit Accounts are a distinct product market.[37]

GPay's Performance After Scotiabank's Termination of its Banking Services

48. This analysis of product markets points to GPay's ability to turn to other products as substitutes for Scotiabank Biller Services and EMT Business Deposit Accounts. Speculation on this matter is not required as again there is evidence. Other products are substitutes for the terminated Scotiabank services if GPay could turn to them without suffering substantial harm. To explore this possibility, consider (i) those products GPay has substituted towards after termination by Scotiabank, and (ii) the effects of this substitution on GPay's business. Doing so will speak to the product market definition and whether that definition should be as narrow as alleged by Applicants and their economic expert. The description above sets out those alternatives chosen by GPay after Scotiabank's termination. Next, this report explores how the choice of these alternatives has affected GPay's business.

49. Scotiabank terminated GPay's banking services in September 2005.[38] The following facts are useful for assessing whether the alternatives chosen by GPay caused its business to be substantially effected:[39]

- In the first full quarter after termination (October to December 2005), GPay volumes processed from accounts at all banks increased by just over 1 percent compared to the previous quarter, when GPay still had access to Scotiabank's banking services. This compares to a growth rate of just under 14 percent between the second and third quarters of 2005;

---

[37] Amended Notice of Application Pursuant to Sections 75 and 77 of the Competition Act, 8.12-8.15.

[38] GPay began using EMTs to process payments from Scotiabank accounts on September 18, 2005. Answers to Undertakings of Ray Grace.

[39] The source for the data in this discussion is BFI001644 to BFI001670 ("Monthly payment data, graphs, projections").

- GPay volumes processed from Scotiabank accounts fell by almost 34 percent between the third and fourth quarters of 2005 (which correspond to the last quarter in which GPay had Scotiabank services and the first quarter in which it did not). GPay volumes processed from Royal Bank, a bank at which GPay maintained bill payee status, also fell, by 8.5 percent. The volumes processed by GPay from accounts at the other two banks with which GPay maintained bill payee status, Bank of Montreal and Caisse Populaire, increased over this period, by 41.6 percent and 25.3 percent, respectively.

50. While these comparisons suggest that the substitutions made by GPay after Scotiabank's termination may have had a negative effect on GPay's business, a more careful consideration of GPay volume data indicates that the effect of this substitution was not substantial (as required by the product market definition test). After a drop in Scotiabank volumes processed between September and October of 2005, volumes recovered through the rest of 2005. In November, GPay's Scotiabank dollar volumes increased by almost 10 percent, and there was a further increase of 13 percent in December. Between October and December 2005, dollar volumes of GPay transactions from Scotiabank accounts increased by almost 25 percent. This compares to a 4 percent fall in volumes processed from accounts at banks other than Scotiabank, and an almost 6 percent fall in volumes processed at all other banks with which GPay has bill payee status. This indicates that the reduction in GPay volumes processed from Scotiabank's accounts after Scotiabank's termination was a short-term phenomenon. GPay's Scotiabank payments have now fully recovered their pre-termination levels. GPay's average monthly payments from Scotiabank accounts between June and August of 2005 were $**[CONFIDENTIAL]**, but by the second quarter of 2006, average monthly volumes, at $**[CONFIDENTIAL]**, already exceeded their pre-merger averages.[40]

51. It appears, therefore, that GPay's substitution towards EMTs as an alternative to Scotiabank Biller Services and towards **[CONFIDENTIAL]** accounts as an alternative to **[CONFIDENTIAL]** accounts, had a negative but short-lived effect on GPay's business. Together with the analysis of substitutability, this leads to the opinion that product markets are wider than claimed by the Applicants. In particular, a product market that includes Scotiabank Biller Services also includes EMTs, and a product market with 'EMT **[CONFIDENTIAL]** deposit accounts' also includes **[CONFIDENTIAL]** deposit accounts.

---

[40] BFI001644 to BFI001670 ("Monthly payment data, graphs, projections"). September 2005 is excluded from the calculations since GPay's volumes during that month appear to be anomalously high.

G. EFFECT ON COMPETITION

52. In analyzing the potential effect on competition of Scotiabank's terminating GPay's banking services, consideration was given to the possible impact of termination on any hypothetical market power accruing to Scotiabank, in particular to its Interac Online service. Doing so is consistent with the Tribunal's findings in previous abuse of dominance cases, where the test with respect to competition (which in an abuse of dominance case is a substantial lessening of competition test) is whether a practice of a claimed anti-competitive act preserves or enhances the market power of a firm allegedly engaging in the practices. In a refusal to deal case, the analogous test is whether the alleged refusal by a firm (in this case Scotiabank) to supply another firm (GPay) will preserve or enhance the market power of the firm (Scotiabank) allegedly refusing to supply. In the matter at hand, the question is this: does Scotiabank's termination of GPay's banking services increase any hypothetical market power accruing to Scotiabank's Interac Online?

53. The most likely anti-competitive claim in this case appears to be that, by terminating GPay's banking services, Scotiabank would increase GPay's production costs or otherwise hinder its ability to attract customers, thereby rendering GPay a less effective competitor to Interac Online. In competition terms, this claim would be labelled "raising a rival's costs". Faced with a less effective competitor, according to this theory, Scotiabank's market power is enhanced.

54. For Scotiabank to enhance its market power (with respect to Interac Online) by weakening GPay, GPay must be an effective competitor to begin with, and it must be a more effective competitor than other suppliers of substitute services, such as credit cards. If these two things do not hold, then Scotiabank's refusal cannot increase any hypothetical market power.

55. Consider the discussion (above) of the economics of the GPay service. GPay earns its revenues by charging merchants a remittance fee of up to **[CONFIDENTIAL]** percent where GPay processes payments, with an average remittance fee of about **[CONFIDENTIAL]** percent. Interac Online also earns revenues from merchants. At the present time, there are no fees charged to the banking customer who uses Interac Online, except account level fees. Scotiabank indicates that it will collect a $1.50 fee for an Interac Online transaction from the banking customer, although it does not intend to start charging this fee until 2007, at the earliest.

56. Payments systems compete for both payers and merchants; there is a 'network externality' because increasing the number of customers on one side of the market increases the demand on the other side, all else remaining equal. For example, as noted above, an increase in the number of GPay merchants will increase the demand for the GPay service by consumers because that service

becomes more valuable. Similarly, an increase in the number of payers who are able to access the GPay service will increase demand by merchants to become payees on the service.

57. To assess the extent to which GPay and Interac Online compete, therefore, what is critical is whether these services compete for both merchants and payers. The first consideration is whether there is significant overlap in the types of merchants that sign up with GPay and Interac Online. If Interac Online and GPay were direct competitors, the expectation is that merchants that accept Interac Online payments would also accept GPay payments, just as many merchants accept both Visa and MasterCard for credit card payments.

58. It appears, however, that no merchants that accept Interac Online payments also accept payments via GPay, and no merchants that accept GPay payments also accept Interac Online payments. A visit to the websites of all merchants listed as 'participating merchants' by Interac Online reveals that there are twenty-eight such merchants.[41] None of these merchants accept GPay as a payment method. A visit to the websites of several of the merchants listed by GPay as clients (as at November 30, 2005) reveals that none of these merchants accept Interac Online.[42]

59. Furthermore, virtually all of the twenty-eight Interac Online 'participating merchants' accept credit card payments, including Visa, MasterCard, and in many cases American Express; and almost all of the listed GPay merchants accept credit cards or other forms of online payment, such as PayPal and NetTeller.

60. This lack of overlap between GPay and Interac Online, along with the observation that virtually every GPay and Interac Online merchant accepts credit cards or other alternative payment methods, suggests that GPay and Interac Online are not close competitors, and that other payment methods, especially credit cards, are more effective competitors to each.

61. There is an issue of whether Scotiabank's termination of GPay banking services represents a significant increment in costs to GPay. GPay claims that its costs have increased. Mr. Grace, in his answers to undertakings, lists several incremental costs incurred as a consequence of Scotiabank's termination of GPay's banking privileges.[43] As noted above, these claimed costs are not measured. Nor is it clear whether these claimed incremental costs are solely because of Scotiabank's termination or the termination by other banks as well.

---

[41] 'Participating merchants' of Interac Online are listed at http://www.interaconline.com/merchants_merchants.php.

[42] GPay's clients are listed in BFI000399 ("List of Merchant Clients as at November 30, 2005").

[43] Answers to Undertakings of Ray Grace, Question 1244.

62. Next consider the impact of the termination on consumers and shareholders. There are two categories to consider: (i) current and future Scotiabank customers who use GPay; and (ii) current and future Scotiabank customers who do not use GPay; and (iii) current Scotiabank shareholders.

63. Consider GPay's current Scotiabank consumers and ask whether these consumers are harmed by Scotiabank's termination of GPay's banking services. If other payment options include prearranged debit payments, credit cards and EMTs, then these consumers have alternatives to meet their needs, albeit at a slightly higher cost to them and a possible constraint on the size of transfers that, as outlined above, may have no bite for most consumers. If the demand for online offshore gambling is relatively price inelastic, then GPay's gambling consumers choosing to use EMTs and facing a $1.50 price increment will suffer a relatively small loss of consumer surplus.

64. Consider GPay's future Scotiabank customers. One claim advanced by the applicants and their expert is that the loss of bill payee status at Scotiabank will harm the ability of GPay to become an alternative payment mechanism for merchants other than online gambling providers. There is no evidence presented by the applicants that GPay will develop into a viable and sustainable payment mechanism as a substitute for instruments such as debit and credit cards and other online payment instruments.

65. As noted by Applicants' economic expert, economics has little to say about the legal status of offshore online gambling in Canada. Economics, however, does have something to say about the business rationale advanced by Scotiabank for the termination of GPay's banking services. Scotiabank terminated its banking relationship with GPay for a number of reasons, including the fact that GPay's manner of conducting business requires banking customers to disclose their online banking password. Scotiabank also had regard to legal, reputational, and regulatory risks associated with continuing to do business with GPay. Scotiabank made a business decision that it does not wish to have its brand name associated with the online, offshore gambling business that constitutes 98 percent of GPay's current business.[44] That Scotiabank possesses significant brand name recognition is evidenced by the report in The Globe and Mail's Report on Business of July 24, 2006 reporting on survey results that rank Scotiabank's brand as ninth in the top twenty-five of Canadian brands. (Of the other Canadian chartered banks, Royal Bank is ranked first; TD Canada

[44] Affidavit Evidence of Robert Rosatelli.

Trust is ranked second; the Bank of Montreal is ranked seventh, CIBC is ranked thirteenth, and National Bank of Canada is ranked sixteenth).[45]

66. Brand name capital is sunk capital based on the business track record of firms producing products and services that consumers wish of a desired quality. Scotiabank has decided that continued provision of bill payee status and associated banking privileges to GPay is not in Scotiabank's interest. One business reason given is that there is risk associated with these bank transfers and the information required to move the desired funds from the accounts of Scotiabank customers. Permitting GPay to have access to individual accounts and customer passwords violates the terms under which Scotiabank provides these banking services. This holds the potential for risk accruing to Scotiabank customers from inappropriate movements of funds from their accounts. Scotiabank also has concerns about the legality in Canada of online, offshore gambling, by Canadians located in Canada.

67. These two issues expose Scotiabank and its shareholders to risk that Scotiabank does not wish to assume. This risk and the association with a possibly illegal activity hold the potential to do damage to Scotiabank's brand name capital, capital which is sunk and whose accumulation has taken considerable investment effort over a long period of time. This offers a bona fide business explanation for the decision of Scotiabank to terminate its banking business with GPay.

68. In contrast, GPay and its economic expert opine that Scotiabank's termination holds the anticompetitive potential to harm future consumers by dampening competition for Scotiabank's Interac Online debit service. The evidence to date is that Scotiabank's net revenues from Interac Online **[CONFIDENTIAL]**. Furthermore, there is no evidence presented that GPay's entry into the non-gambling merchant business in Canada is viable and sustainable. GPay's current business portfolio may be the best indicator of its viable future business portfolio, a business that Scotiabank does not wish to serve.

69. In sum, these facts indicate that Scotiabank's termination is not driven by a strategic attempt to disadvantage a potential rival, to dampen competition for the online business of non-gambling merchants both current and future.

---

[45] This article is available on the Internet at http://www.theglobeandmail.com/servlet/story/LAC.20060724.RBRANDSMAIN24/EmailTPStory/.

H. SUMMARY AND CONCLUSIONS

70. My economic opinion is that Scotiabank Biller Services and EMT **[CONFIDENTIAL]** Deposit Accounts, are not, as claimed by Applicants, properly defined product markets for the purposes of this case. In particular:

1) **[CONFIDENTIAL]** deposit accounts are in the same product market with 'EMT **[CONFIDENTIAL]** Deposit Accounts. The relevant features of **[CONFIDENTIAL]** deposit accounts are identical, and Applicants use their **[CONFIDENTIAL]** deposit accounts at Royal Bank, Bank of Montreal, and CIBC to receive EMTs in the same way that they use their **[CONFIDENTIAL]** deposit accounts at Royal Bank. There appears to be no evidence on the record that **[CONFIDENTIAL]** deposit accounts are not substitutable for **[CONFIDENTIAL]** deposit accounts for receiving EMTs;

2) Scotiabank Biller Services is not a product market, and the market that includes Biller Services also includes EMT **[CONFIDENTIAL]** deposit accounts. GPay substituted towards deposits of EMTs into **[CONFIDENTIAL]** deposit accounts after Scotiabank terminated GPay's bill payee status, and while payments processed by GPay from Scotiabank accounts fell immediately after termination, the volume of GPay payments has now recovered to pre-termination levels. The effects of this substitution on GPay's business therefore cannot be said to be 'substantial'. There is no empirical evidence that Scotiabank's termination has substantially increased GPay's costs, and the only evidence in this regard is that Scotiabank's termination has caused some inconvenience for GPay.

With respect to the effect of Scotiabank's termination on downstream competition, the conclusion is as follows:

3) Scotiabank's termination of its relationship with GPay will have a minimal, if any, effect on competition. The Applicants' service and the service with which Scotiabank is associated, Interac Online, appear not to be close substitutes, and consequently the Applicants' service would not constrain any hypothetical attempt by Scotiabank to exercise any supposed market power with respect to Interac Online. GPay does not compete for the same merchants or payers as Interac Online: 98 percent of current payments processed by GPay are made to online casinos, and Interac Online does not, nor does it intend to, serve this market segment. Furthermore, there are many other forms of payment for online purchases, such as credit cards and e-wallets, that are likely to be closer substitutes for Interac Online than GPay is.

71. If other payment options include prearranged debit payments, credit cards and EMTs, then existing Scotiabank consumers who wish to use GPay have alternatives to meet their needs, albeit at a slightly higher cost to them and a possible constraint on the size of transfers that, as outlined above, may have no bite for most consumers. If the demand for online offshore gambling is relative price inelastic, then these consumers facing any incremental cost of using GPay will suffer a relatively small loss of consumer surplus. With respect to future consumers, there is no evidence presented by the applicants that GPay will develop into a viable and sustainable payment mechanism as a substitute for instruments such as debit and credit cards and other online payment instruments. GPay's current business portfolio may be the best indicator of its viable future business portfolio, a business that Scotiabank does not wish to serve.

72. Scotiabank terminated its banking relationship with GPay for a number of reasons including the fact that GPay's manner of conducting business requires banking customers to disclose their online banking password. Scotiabank also had regard to legal, reputational, and regulatory risks associated with continuing to do business with GPay. Brand name capital is sunk capital based on the business track record of firms producing products and services that consumers wish of a desired quality. Scotiabank has decided that continued provision of bill payee status and associated banking privileges to GPay is not in Scotiabank's interest. One business reason given is that there is risk associated with these bank transfers and the information required to move the desired funds from the accounts of Scotiabank customers. Permitting GPay to have access to individual accounts and customer passwords violates the terms under which Scotiabank provides these banking services. This holds the potential for risk accruing to Scotiabank customers from inappropriate movements of funds from their accounts. Scotiabank also has concerns about the legality in Canada of online, offshore gambling, by Canadians located in Canada.

73. These facts indicate that Scotiabank's termination is not driven by a strategic attempt to disadvantage a potential rival, or to dampen competition for the online business of non-gambling merchants both current and future.

I. DISCUSSION OF THE SCHWARTZ REPORT

74. In paragraph 11, Dr. Schwartz states that "B-Filer *requires* (emphasis added) biller status at the financial institutions whose depositors wish to use GPay Service." The use of the verb 'requires' indicates 'demand for success' and thus in Dr. Schwartz's view, biller status is an essential input into the provision of B-Filer's online debit payment. In economics, an essential input is one for which there is no substitute so that if this input is unavailable, the corresponding output would be zero. Both TD Canada Trust and CIBC, as well as Scotiabank more recently, do not offer GPay biller

status and yet the payments generated to GPay through each of these financial institutions are substantial and not zero.

75. In paragraph 13 and throughout this report, the claim is that the use of EMTs to process online payment transactions for GPay has made B-Filer's daily business operations "more complicated and costly compared to the situation where it had received biller status." Yet neither the applicants nor Dr. Schwartz offer any empirical evidence on the increase in the costs accruing to B-Filer as a result of these terminations of biller status, either at Scotiabank or any other bank.

76. The main feature of the menu of accounts open to Scotiabank customers is that these accounts have several features, including where applicable the monthly fee; a per-transaction fee; tiered interest; minimum daily account balances; fee for debit transactions, bill payment, and cheques; limit on zero-priced debit transactions; fee for teller-handled cash withdrawal.

77. Dr. Schwartz opines that the Competition Act gives no guidance on how the market and the adverse effect referred to S.75 should be identified and proposes to use the hypothetical monopoly test set forth in the Merger Enforcement Guidelines for the purposes of market definition. In applying these guidelines to defining the market, the economic agents considered in Dr. Schwartz's report are (i) Scotiabank's depositors; (ii) merchants who wish to permit online access for their customers, and finally (iii) GPay itself as supplier of online services and whether it is able to obtain supplies of its "required" inputs elsewhere.

78. Dr. Schwartz proposes to use the SSNIP test of where a small but significant (5 percent) and non-transitory (1 year) increase in price could be sustained by a hypothetical collective of firms. If yes, these firms and their products constitute a market; if no, then look to the next best substitutes and apply the SSNIP test to the newly defined coalition that now includes these next best substitutes and again ask the question. Continue adding substitutes until the answer is yes. One issue concerns the application of this test when the 'price' features of the product have several dimensions. Thus a 5 percent increase in the 'price' of a bank account could mean a 5 percent increase in any monthly fee or an appropriate increase in the required daily balance in terms of foregone alternatives or a reduction in interest paid on balances or an appropriate reduction in the number of zero-priced transaction such as cheques or online transfers. Applying the test (as in paragraphs 47 and 48) to a zero-priced transaction and then concluding that 5 percent of zero is zero and thus a zero price increase is insufficient to cause any consumers to look for substitute financial arrangements is inappropriate, whether this price increase is current or forever into the future. This cannot lead to the conclusion that with a zero price increase the "relevant product

market is immediately limited to the GPay Service at Scotiabank because Scotiabank depositors will not open transaction accounts at other banks in consequence."

79. A further question is whether this hypothetical test is required when the terminations of GPay accounts and privileges by CIBC, TD Canada Trust and Scotiabank reveal evidence on how the agents defined above did respond. Put succinctly why doesn't the market evidence on what consumers did dominate hypothetical tests in response to terminations of financial services by the three banks?

80. The mobility of consumers to other financial institutions in light of a 5 percent price increase in some aspect of the consumer's product or service at a current financial institution is an empirical question; there is no hard evidence of any potential response. One possibility is that consumers already have accounts and privileges at more than one financial institution, which makes transition for consumers less costly in light of any price increase. As any consumer response to a price hike remains an open and unanswered empirical matter, a categorical conclusion which removes all other financial institutions from the market seems unwarranted.

81. The discussion of the features and use of credit and debit cards by consumers is qualitative and non-empirical. It is insufficient to reach the conclusions that (i) "the evidence tends to suggest that Scotiabank deposit customers using the GPay service would not switch to credit cards;" and (ii) "it appears that credit and debit cardholders use their cards for different purposes and purchases and this, together with the other available information tends to suggest that Scotiabank depositors would not switch to online payment by credit cards in significant numbers in the event of a small but significant increase in the price of the GPAY service" These appear to be assertions. What would be required to draw this conclusion is evidence on what customers of Scotiabank (and TD Canada Trust and CIBC for corroboration) wishing to use GPay did when the GPay's biller status was terminated at the respective bank.

82. Scotiabank has stated as a business decision that it does not seek to service the online offshore gambling market, a market that accounts for approximately 98 percent of GPay's business. Dr. Schwartz opines that GPay is attempting to compete with Interac Online. However, as indicated above, an examination of GPay's non-gambling clientele and Interac's merchants reveals little attempt at competition. As indicated above, Scotiabank's Interac Online business is currently relatively small with no overlap of GPay's merchants. Scotiabank's merchant list all accept Visa and Mastercard and not GPay leading to the impression that these credit cards are more likely substitutes for Scotiabank's Interac Online business. On the issue of whether GPay would be viable and sustainable in the non-gambling merchant business, Dr. Schwartz states that "it must be

assumed, if only for analytical purposes (i.e., without making a forecast as to B-Filer's likely success or failure in merchant recruitment), that B-Filer could recruit sufficient merchants in the future and that Interac Online would be a good substitute for Scotiabank." The waiver notwithstanding, this appears to mean that Dr. Schwartz simply assumes that these two services will compete at some unknown future date.

83. This brings up the question of whether EMTs are a substitute for Biller status. As noted above, EMTs do have a fixed fee per transaction ($1.50) and a daily limit ($1000). For Scotiabank GPay customers whose transfers are below the limit, the limit is irrelevant. The issue of whether the per-transaction fee has bite is again an empirical one. As noted above, this fee as a percentage of the average Scotiabank customer's transfer using GPay was about 1.7 percent, which is below the 5 percent in the SSNIP test. As noted above, if the demand for online offshore gambling is relative price inelastic, then GPay's gambling consumers choosing to use EMTs and facing a $1.50 price increment will suffer a relatively small loss of consumer surplus.

84. Dr. Schwartz notes that the terminations by Scotiabank of GPay's accounts and biller status have not driven GPay from the market even though earlier these accounts and status were deemed to be "required" by GPay. Dr. Schwartz also opines that these terminations have "doubtless" made B-Filer less efficient. This opinion is unsupported by any empirical evidence on the impact of termination on GPay's costs.

85. Dr. Schwartz opines that GPay provides an efficient middleman role between merchants and providers of financial services. The exact role of GPay is best revealed by the class of merchants that it serves namely online offshore gambling establishments for the most part. But this is a class of business where Scotiabank has no desire to participate.

86. Dr. Schwartz does not comment on Scotiabank's rationale for the termination of GPay's services at Scotiabank saying that it is a legal matter. As noted above, while the legal status of online, offshore gambling in Canada is an open legal question, Scotiabank's reasons for terminating GPay's status and accounts at Scotiabank do warrant an economic commentary. Scotiabank seeks to minimize its legal and regulatory risk and to protect its sunk investment in its brand name capital as a prudent provider of financial service in both Canada and abroad. This desire is a sufficient reason to terminate GPay's financial privileges with Scotiabank in light of GPay's principal merchant base and GPay's method of transferring funds from the accounts of Scotiabank customers to gambling merchants.

Appendix A: Curriculum Vitae

Academic Positions

1996–Present	*Director*, Institute for Policy Analysis, University of Toronto
1969–Present	*Professor of Economics*, Department of Economics, University of Toronto
1969–Present	*Research Associate*, Institute for Policy Analysis, University of Toronto
1995–1996	*Acting Chair*, Department of Economics, University of Toronto
1985	*Visiting Professor*, Center for the Study of the Economy and the State, University of Chicago, Spring Quarter
1984	*Visiting Scholar*, Graduate School of Business, University of Chicago, Spring Quarter
1978–1983	*Associate Chairman and Director of Graduate Studies*, Department of Economics, University of Toronto
1970–1982	*Professor of Economics*, Faculty of Management Studies, University of Toronto
1978–1979	*Senior Research Associate*, Ontario Economic Council
1976–1977	*Visiting Research Fellow*, Department of Political Economy, University College, University of London

Education

Ph.D. Stanford University

B.Com. University of Toronto

Honors and Fellowships

Social Science and Humanities Research Council Research Fellowship: 1994, 1991, 1989, 1987, 1986, 1985

Social Science and Humanities Research Council Leave Fellowship: 1983–1984

Canadian Council Leave Fellowship: 1976–1977

Canada Council Doctoral Fellowship: 1966–1969

Woodrow Wilson Fellowship: 1965

Professional Affiliations

Editorial Board, *Journal of Economics of Business*, 1992–Present.

Editorial Board, *Managerial and Decision Economics*, 1994–Present.

Editorial Board, *Economic Inquiry*, 1987–1997.

Editorial Board, *Journal of Industrial Economics*, 1990–1995.

Associate Editor, *International Journal of Industrial Organization*, 1982–1988.

Co-editor with M. Trebilcock and M. Walker. The Law and Economics of Competition Policy, Vancouver: The Fraser Institute, 1990.

Co-editor with J. Stiglitz. New Developments in the Analysis of Market Structures, Cambridge: MIT Press, 1985.

Program Committee, European Association for Research in Industrial Economics, 1983–1991.

Program Committee, Conference on Industrial Organization, International Economics Association, 1982.

Publications

"Sales Contracts with Long-Term Customer Relationships (with Ig Horstmann and Neil Quigley)" *Journal of Labor Economics*, July 2005 Vol. 23(3): 589 – 608.

"Revisiting Main and Bay Street: Comments," in T.J. Courchene and E.H. Neave (eds) *Framing Financial Structure in an Information Environment*, Conference Proceedings, 2001, Kingston: John Deutsch Institute.

"Market Power Thresholds: Theory and Competition Cases Related to Barriers to Entry, Oligopoly and Joint Dominance" with Neil Quigley in *Competition Law at the Turn of the Century* (2003) eds. Mark Berry and Lewis Evans, Wellington: Victoria University Press.

"The Analysis of Efficiencies in *Superior Propane:* Correct Criterion Incorrectly Applied." With Ralph Winter. *Canadian Competition Record*, Fall 2000, 20(2): 88–97.

"Professional Corporations and Limited Liability." With Michael Smart, in Peter Newman (ed.) *Palgrave Dictionary in Economics and the Law*, 140–143 London: MacMillan Reference Limited, 1999.

"Law Firms." With Jack Carr, in Peter Newman (ed.) *Palgrave Dictionary in Economics and the Law*, 497–500, London: MacMillan Reference Limited, 1998.

"Canadian Bank Mergers: Efficiency and Consumer Gain versus Market Power" With Neil Quigley CD Howe Institute, Occasional Paper, No. 108, June 1998.

"To Merge or not to Merge: Is that the Question?" With Neil Quigely. CD Howe Institute. Occasional Paper, No. 108, 1998.

"The Law and Economics of Resale Price Maintenance." With Ralph Winter. *Review of Industrial Organization*, 13:1-2, 57-84, April 1998.

"What's Essential, What's Prudential, What Can Competition Provide?" With Neil Quigley. *Canadian Competition Record* 18:2, 11–28, 1997.

"Reforming the Bank Act: Regulation, Public Policy, and the Market" With Neil Quigley. *Canadian Business Law Journal* 29:1, 1–16, 1997.

"Ensuring Competition: Bank Distribution of Insurance Products: Prospects and Implications for Canada." With Ignatious Horstmann and Neil Quigley. Toronto: CD Howe Institute, 1996.

"Buyer Groups and Exclusivity: Towards a Theory of Managed Competition." With Ralph Winter. *International Journal of Industrial Organization* 15:2, 137–164, 1997. (Presented at the EARIE Conference, Tel Aviv, Israel, 1993.)

"Tying As a Response to Demand Uncertainty." With Ralph Winter. *The RAND Journal of Economics* 28:3, 566–583, 1997. (Presented at the EARIE Conference, Lisbon, Portugal, 1990.)

"Stability in the Absence of Deposit Insurance: The Canadian Banking System 1890–1966." With Jack Carr and Neil Quigley. *Journal of Money, Credit and Banking* 27:4, 1137–1158, 1995.

"Ensuring Failure." With Jack Carr and Neil Quigley. Toronto: CD Howe Institute, 1994.

"Territorial Rights in Franchise Contracts." With Ralph Winter. *Economic Inquiry* 32:2, 181–192, 1994. (Presented at the EARIE Conference, Budapest, Hungary, 1989.)

"Reply to R. Gilson." With Jack Carr. *Journal of Political Economy* 99:2, 426– 428, 1991.

"The Economics of Law Firms: A Study in the Legal Organization of the Firm." With Jack Carr. *Journal of Law and Economics* 33:2, 307–330, 1990.

"The Economic Effects of Automobile Dealer Regulation." With Ralph Winter. *Annales d'Economie et de Statistique* 15/16, 409– 426, Juillet-Décembre 1989.

"Unlimited Liability and Free Banking in Scotland: A Note." With Jack Carr and S. Glied. *Journal of Economic History* 49:4, 974–978, 1989.

"Vertical Restraints and the Law: A Reply." With Ralph Winter. *RAND Journal of Economics*, 19:2, 298–301, Summer 1988.

"Unlimited Liability as a Barrier to Entry." With Jack Carr. *Journal of Political Economy* 96:4, 766–784, August 1988.

"Is Exclusive Dealing Anti-Competitive?" With Ralph Winter. *American Economic Review* 77:5, 1057–1062, December 1987.

"Advertising and Consumer Learning." With Y. Kotowitz in FTC Conference Volume, *Consumer Protection Economics*, 1986. (Paper presented at the FTC Conference on Advertising, Washington, 1984.)

"Competition Policy and Vertical Exchange." With Ralph Winter. Royal Commission on the Economic Union and Development Prospects for Canada, University of Toronto Press, 1985.

"The Economics of Franchise Contracts." With Ralph Winter. *Journal of Law and Economics* 3, 503–526, October 1985. (Paper presented at the EARIE Conference, Fontainebleau, 1984.)

"The Economics of Life Insurance Regulation: Valuation Constraints." With Ralph Winter in J. Finsinger and M. Pauly (eds.), *The Economics of Insurance Regulation*, MacMillan and Company Limited, 1986. (Paper presented at IIM Conference on Regulation in Insurance Markets, Berlin, 1984.)

"The Economics of Vertical Restraints in Distribution." With Ralph Winter in J. Stiglitz and G.F. Mathewson (eds.), *New Developments in the Analysis of Market Structure*, MIT Press, 1986.

"An Economic Theory of Vertical Restraints." With Ralph Winter. *RAND Journal of Economics* 15:1, 27–38, Spring 1984. (Reprinted in *The Economics of Marketing*, Cheltenham, UK: Edward Elgar Publishing Limited, 1998.)

"Information, Search and Price Variability of Individual Life Insurance Contracts." *Journal of Industrial Economics* 32:2, 131–148, December 1983. (Paper presented at the Canadian Economics Association Meetings, Montreal, 1980.)

"The Incentives for Resale Price Maintenance." With Ralph Winter. *Economic Inquiry* 21:3, 337–348, July 1983. (Paper presented at the Western Economic Association Meetings, San Francisco, 1981.)

"Vertical Integration by Contractual Restraints in Spatial Markets." With Ralph Winter. *Journal of Business* 56:4, 497–518, October 1983.

"Entry, Size Distribution, Scale, and Scope Economies in the Life Insurance Industry." With S. Kellner. *Journal of Business* 56:1, 25–44, January 1983.

"Regulation of Canadian Markets for Life Insurance." With Ralph Winter. Department of Consumer and Corporate Affairs, Government of Canada, 1983.

"The Rationale for Government Regulation of Quality" and "Policy Alternatives in Quality Regulation." With D. Dewees and M. Trebilcock. "Markets for Insurance: A Selective Survey of Economic Issues," in D. Dewees (ed.), The Regulation of Quality, Toronto: Butterworths, 1983.

"An Economic Theory of Union-Controlled Firms." With Y. Kotowitz. *Economica* 49:196, 421–433, November 1982. (Paper presented at the Canadian Economics Association Meetings, Quebec City, 1978.)

"Advertising, Consumer Information and Product Quality." With Y. Kotowitz. *Bell Journal of Economics* 10:2, 566–588, Fall 1979. (Paper presented at the European Econometric Society Meetings, Geneva, 1978.)

"Informative Advertising and Welfare." With Y. Kotowitz. *American Economic Review* 69:3, 284–294, June 1979.

"Information, Entry and Regulation in Markets for Life Insurance." Ontario Economic Council Research Studies, University of Toronto Press, 1982.

"Some Issues on Public Advertising." With Y. Kotowitz. *Journal of Contemporary Business* 7:4, 123–124, 1979.

"Economics of Fiscal Transfer Pricing in Multinational Corporations." With G.D. Quirin. Ontario Economic Council Research Studies, University of Toronto Press, 1978.

"The Residential Demand for Electrical Energy and Natural Gas: A Model Estimated for Canada." With R. Hyndman and Y. Kotowitz in W.T. Ziemba *et al.* (eds.), *Energy Policy Modelling: United States and Canadian Experiences*, Martinus Nijhoff Press, 86–102, 1980. (Paper presented at the Canadian Energy Policy Modelling Conference, Vancouver, 1978.)

"Economies of Scale in Financial Institutions: Reply." With P. Halpern. *Journal of Monetary Economics* 3, 127–131, 1977.

"The Benefits and Costs of Rate of Return Regulation." With J. Callen and H. Mohring. *American Economic Review* 66:5, 290–297, June 1976.

"Economies of Scale in Financial Institutions: A General Model Applied to Insurance." With P. Halpern. *Journal of Monetary Economics* 1:2, 203–220, April 1975.

"Price Effects of Market Power in the Canadian Newspaper Industry: Reply." *Canadian Journal of Economics* 7:1, 130–132, February 1974.

Cents and Nonsense: The Economics of Canadian Policy Issues. With J. Carr and J. McManus. Holt, Rinehart, and Winston, 1972.

"Metering Costs and Marginal Cost Pricing in Public Utilities." With G.D. Quirin. *Bell Journal of Economics* 3:1, 335–339, May 1972.

"A Note on the Price Effects of Market Power in the Canadian Newspaper Industry." *Canadian Journal of Economics* 5:2, 298–301, May 1972.

"A Consumer Theory of Demand for the Media." *Journal of Business* 45:2, 212–224, April 1972.

WORKS IN PROGRESS

Coordination, Specialization and Incentives within the Firm (with Ig Horstmann).

Vertical Restrictions and Efficiency: Beer Distribution in the Nineteenth Century (with Neil Quigley).

The Economics of Most-Favoured-Nations Clauses (with Ig Horstmann)

Appendix B: Documents Relied Upon

Transcript for Discovery of Raymond Grace, July 27 and July 28, 2006.

Discovery of Raymond Grace, July 28, 2006

Answers to Undertakings of Ray Grace, Delivered July 24, 2006, including Exhibits

Transcript for Discovery of Robert Rosatelli, June 12 and June 13, 2006

Undertakings on the Examination for Discovery of Robert Rosatelli Taken on June 12 and 13, 2006

Affidavit Evidence of Raymond Grace

Affidavit Evidence of Joseph Iuso

Affidavit Evidence of David Stafford

Affidavit Evidence of Robert Rosatelli

Affidavit Evidence of Colin Cook

Affidavit Evidence of Ryan Woodward

Affidavit Evidence of David Metcalfe

Internal confidential data from Scotiabank

Data from analysis undertaken by Scotiabank Manager of Bill Payment Services, Nellie Marcoux

Amended Notice of Application Pursuant to Sections 75 and 77 of the Competition Act

Response to Amended Notice of Application Pursuant to Section 75 of the Competition Act

Affidavit of Lawrence P. Schwartz

B-Filer Productions BFI000007-BFI000569, BFI001532, BFI001581, BFI001585, BFI001644 to BFI001670

BNS Productions BNS000001-BNS004530

Various websites:

https://www.certapay.com/en/newsEvents/factSheet.html

https://www.certapay.com/en/

http://www.acxsys.ca/about.php

http://www.interaconline.com/merchants_merchants.php

http://www.theglobeandmail.com/servlet/story/LAC.20060724.RBRANDSMAIN24/EmailTPStory/.

BETWEEN:

B-FILER INC.
Applicants

- and -

THE BANK OF NOVA SCOTIA
Respondent

Court File No. CT

COMPETITION TRIBUN

AFFIDAVIT OF
FRANK MATHEWSON

McCarthy Tétrault LLP
Barristers & Solicitors
Box 48, Suite 4700
Toronto Dominion Bank To
Toronto, ON M5K 1E6

F. Paul Morrison LSUC #:
Tel: (416) 601-7887
Fax (416) 868-0673

Lisa M. Constantine LSUC
Tel: (416) 601-7652
Fax: (416) 868-0673

Solicitors for the Responde
4206718