

CT-2005-09

THE COMPETITION TRIBUNAL

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

IN THE MATTER OF an application by the Commissioner of
Competition under section 92 of the *Competition Act*;

AND IN THE MATTER OF a joint venture between
Saskatchewan Wheat Pool Inc. and James Richardson International
Limited in respect of port terminal grain handling in the Port of
Vancouver.

BETWEEN:

THE COMMISSIONER OF COMPETITION

Applicant

- and -

**SASKATCHEWAN WHEAT POOL INC.
JAMES RICHARDSON INTERNATIONAL LIMITED
6362681 CANADA LTD. AND 6362699 CANADA LTD.**

Respondents

**RESPONSE OF SASKATCHEWAN WHEAT POOL INC.,
6362681 CANADA LTD. AND 6362699 CANADA LTD.**

COMPETITION TRIBUNAL
TRIBUNAL DE LA CONCURRENCE

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PART I. SUMMARY OF RESPONSE

1. This Response is filed on behalf of Saskatchewan Wheat Pool Inc. (“SWP”), 6362681 Canada Ltd. and 6362699 Canada Ltd. (SWP, 6362681 Canada Ltd. and 6362699 Canada Ltd. will be referred to collectively hereinafter as the “Respondents”). SWP has entered into several agreements with the Co-respondent, James Richardson International Limited (“JRI”), for the purpose of jointly operating their grain handling facilities at the Port of Vancouver through a joint venture (the “Joint Venture”). 6362681 Canada Ltd. and 6362699 Canada Ltd. (the “JV companies”) were formed to act as the operator and marketer of the services of the Joint Venture.

2. The Respondents say that the Joint Venture has not and will not result in a substantial lessening of competition as alleged. The Respondents submit that the premises and analysis upon which the present application is founded, as set out in the Statement of Grounds and Material Facts (“SGMF”) filed by the Commissioner of Competition (the “Commissioner”) in support of her application, are fundamentally flawed in numerous respects.

3. First, the SGMF errs in its definition of the relevant market and of its assessment of competitors within that market. The SGMF defines the product market as port terminal grain handling services, but the services provided by the Joint Venture comprise a set of distinct services, nearly all of which are also provided by, among others, primary grain elevators throughout Western Canada. As a result, the SGMF misapprehends the product market. The SGMF also defines far too narrowly the geographic market within which the Joint Venture operates. In respect of all of the services it provides, the Joint Venture competes with primary grain elevators; other port terminals located in Vancouver and Prince Rupert, British Columbia, and in Churchill Manitoba, Thunder Bay, Ontario, and other Canadian locations; domestic grain processors and users; and others. Finally the SGMF fails to give adequate consideration to competitors of the Joint Venture located on the West Coast. As a result of these errors in defining the market, the Commissioner errs in her competitive analysis of the impact of the Joint Venture. For example, the Joint Venture will not, contrary to the Commissioner’s assertion, have the ability and incentive to increase tariff charges for grain handling services and to reduce

incentive payments or diversion premiums paid to grain companies that do not own terminals in the Port of Vancouver (“Non-Integrated Graincos”).

4. Second, the Commissioner has failed to consider the limitations on operating capacity of each of the terminals owned by SWP and JRI and the improvements in working capacity that are achieved by operating the terminals jointly. Joint management of the two terminals will result in greater throughput capacity, through more efficient handling, cleaning and storage of grain. The Respondents have projected that the overall operating capacity of the two terminals will increase by as much as **[Confidential]**%. These improvements in efficiency and productivity of the terminals are necessary to accommodate greater volumes resulting from a return to normal growing conditions and average crop production in Western Canada. Adding additional capacity through more efficient management will ensure that the terminals can continue to provide prompt service to Non-Integrated Graincos, including prompt authorization upon reasonable notice to ship their grain to the Joint Venture for export. **[Confidential]** However, the additional capacity generated by the joint management of the two terminals will permit the terminals to continue to compete for the provision of services to Non-Integrated Graincos while absorbing the increased volumes of the owners.

5. Third, the allegation that the Joint Venture will lessen competitive options is based upon an incorrect analysis of the relevant market and a failure to consider the impact of higher crop production on the capacity of the Joint Venture terminals. **[Confidential]** SWP and JRI have not been in the past and, because of the capacity constraints at the two terminals, will not have the ability to be vigorous and effective competitors for shipments from Non-Integrated Graincos. By contrast, because of the Joint Venture’s ability to manage grain throughput more efficiently, it will be able to offer grain handling services to Non-Integrated Graincos. Accordingly, the Joint Venture will result in more choice for Non-Integrated Graincos in shipping their grain to the West Coast. The Joint Venture will not increase the costs of Non-Integrated Graincos or limit their ability or incentive to compete with SWP or JRI in local primary handling grain markets; rather, by providing an additional bulk grain handling option for Non-Integrated Graincos in the

Port of Vancouver, the Joint Venture will enhance their ability to compete for grain purchases from farmers.

6. Fourth, the SGMF fails to take into account the substantial efficiency gains that the parties will realize as a result of the Joint Venture, which gains will offset any alleged anticompetitive effects of the Joint Venture. These efficiency gains are discussed in more detail below.

PART II. ADMISSIONS AND DENIALS

7. The Respondents admit the first sentence of paragraph 1, and paragraphs 7 to 15, 17, 20, 21, 24, and 26 of the SGMF.

8. The Respondents deny the balance of paragraph 1, and paragraphs 2 to 5, 16, 18, 19, 22, 23, 25, 27 to 32 and 33 to 65 of the SGMF.

PART III. THE PARTIES

9. Saskatchewan Wheat Pool Inc. is a business corporation incorporated under the laws of Canada with its head office in Regina, Saskatchewan. SWP's operations in the agricultural industry include three business areas: sale of agri-products such as crop inputs, grain handling and marketing, and processing of agricultural food products. SWP's grain handling and marketing activities include receiving, elevation, cleaning, drying, blending, and storage of grain through its primary elevator system, and loading of rail cars for shipment to domestic buyers or for sale to export markets. SWP's primary elevator system includes 43 high throughput primary terminals located in Manitoba, Saskatchewan, and Alberta. SWP also owns port terminals in Vancouver and Thunder Bay and SWP is a joint venture partner in Ridley Grain Ltd., which operates a terminal as Prince Rupert Grain Ltd. ("PRG") in Prince Rupert, British Columbia.

10. In addition to handling grain originated in SWP's own primary elevator system, SWP's port terminal provides grain handling and related services, to grain companies that do not own terminals in the Port of Vancouver (previously defined as "Non-Integrated Graincos"). These services include unloading of railcars, elevation, cleaning, drying, blending grain to required specifications, storage, and loading grain into ocean-going vessels for export.

11. James Richardson International Limited (previously defined as "JRI") is a Canada business corporation with its head office in Winnipeg, Manitoba. JRI also supplies grain handling and marketing services through its primary elevator system in Western Canada, and engages in the related businesses of sales of agri-products and processing of agricultural products. JRI owns a port terminal in Vancouver adjacent to SWP's port terminal, as well as other port terminals at other Canadian locations, in Thunder Bay, Hamilton and Port Stanley, Ontario, and, Sorel, Québec. JRI is also a joint venture partner in Ridley Grain Ltd.

12. 6362681 Canada Ltd. and 6362699 Canada Ltd. (previously defined as the "JV companies") are business corporations under the laws of Canada, created by SWP and JRI for the purpose of operating and marketing the Joint Venture. SWP and JRI each own half of the issued and outstanding share capital of the JV companies. On June 10, 2005, the name of 6362699 Canada Ltd. was changed to Pacific Gateway Terminals Limited ("PGTL").

13. The Commissioner is appointed under section 7 of the *Competition Act* and charged with the administration of the Act.

PART IV. THE JOINT VENTURE

14. On April 6, 2005, SWP and James Richardson International Limited ("JRI") publicly announced the creation of a joint venture (the "Joint Venture") for the joint operation of their adjacent grain handling facilities located on the North shore of Vancouver's Burrard Inlet. Under the agreements governing the Joint Venture, both SWP and JRI continue to own their respective port terminals, and remain responsible to pay a portion of fixed costs, including such items as

power, taxes, insurance on their assets [**Confidential**]. Net revenues are distributed to SWP and JRI under an agreed formula. The Joint Venture operator manages all aspects of the operation of the terminals and is responsible to plan for the efficient throughput of grain, including grain originated by SWP and JRI and grain from Non-Integrated Graincos.

15. The Joint Venture commenced operation on July 11, 2005. A Consent Interim Agreement entered into between the parties and the Commissioner, registered with the Competition Tribunal on July 5, 2005, prevented the Joint Venture operator from marketing the services of the Joint Venture to Non-Integrated Graincos. The Consent Interim Agreement was extended several times, expiring on November 10, 2005. In all other respects the operations of the terminals have been integrated.

16. SWP and JRI entered into the Joint Venture in order to improve operating efficiencies, productivity and throughput potential through effective management and coordination of the combined space, better railcar utilization and shipping capacity. These efficiencies are described in greater detail below.

17. By jointly operating the two facilities, SWP and JRI are able to increase their effective working capacity through more efficient use of their storage facilities. Terminal operators are required to store separately, or segregate, grain of different grades and other quality factors like protein, cleanliness, and moisture content. Hundreds of distinct grain segregations are required, which greatly undermines the overall effective storage capacity and productivity of the terminal. Grain stocks may be segregated by type of grain (e.g., wheat or barley), class of grain (e.g., red spring wheat or winter wheat), variety of grain (e.g., Manley or Harrington malting barleys), grade of grain (e.g., No. 1 or No. 2), protein content, and other factors, according to standards established by the CGC. Additional segregations to meet particular customer needs may also be required by the CWB. The Joint Venture allows SWP and JRI to amalgamate their grain stocks, approximately halving the total number of segregations maintained by the two terminals. This frees up storage space that would not otherwise be available, thereby augmenting the effective operating capacity of the terminals.

18. In addition to combining grain stocks having the same characteristics, the Joint Venture is also able to specialize the two terminals, so that each facility can be dedicated primarily to throughput of different classes of grain. Because of certain comparative advantages of each of the two terminals, the SWP facility with its greater storage capacity will primarily handle wheat and barley, which require greater numbers of segregations, while the JRI facility will handle other grains, such as canola and peas. The SWP terminal has a much greater storage capacity and a greater number of storage bins to accommodate CGC and CWB requirements for separate binning of large numbers of segregations. Specializing the terminal operations allows for more expeditious railcar unloading, which reduces the parties' and other shippers' exposure to certain risks, including penalties known as demurrage imposed by railway companies for delays in railcar unloading. Amalgamating grain stocks also permits longer cleaning runs and the specialization of grain cleaning equipment, which will reduce costs and permit better reclamation of good quality grain removed during the cleaning process. In addition, the JRI terminal is able to clean canola at a comparatively greater rate. Having larger lots of grain stored in each facility also provides more opportunities to blend stocks of grain having different grades, protein and moisture content, or other characteristics, resulting in product that more closely matches the contractual specifications required by shippers and overseas customers.

19. Combining grain stocks will also permit more efficient vessel loading, including greater opportunities to load vessels on one berth, which will reduce the cost of vessel freight to SWP and JRI and other shippers, as well as enhance the overall efficiency of the Port of Vancouver. In addition, SWP, JRI and other shippers will be less exposed to penalties by vessel owners for delays in loading of ocean-going vessels and the risk of failing to meet contractual deadlines for vessel loading.

20. Terminal elevators rely upon coordination between, among other things, three major processes: receiving of grain in railcars; storage of grain either before or after processing; and loading of grain onto vessels. For a terminal to work effectively these three activities must be

coordinated, otherwise one of the processes will create a bottleneck which will constrain the other processes from operating at full capacity.

21. Given the number of grain segregations required, and with the current crop mix, SWP estimates that its Vancouver terminal has on its own annual throughput capacity of about **[Confidential]** tonnes. SWP has exceeded this volume only once since 1984, in 1992, when it shipped **[Confidential]** tonnes. SWP's constraint on capacity is due to its limited railcar spot, which only allows about **[Confidential]** cars to be unloaded during any shift. **[Confidential]**

22. SWP estimates that JRI annual throughput capacity is approximately **[Confidential]** tonnes per year. The constraint on JRI's capacity is its limited storage. JRI's smaller storage area has increasingly constrained its throughput capacity because of changes to railcar demurrage and the elimination of railcar pooling in the Port of Vancouver. JRI used to be able to stage railcars in its large rail yard for unloading at a later time, effectively adding to the storage capacity of its physical plan. However, rail companies have reduced the time for unloading before demurrage penalties are imposed, from five days to 48 hours. Further, railcars are no longer "pooled" in the Port of Vancouver, so JRI is no longer able to specialize its facility by allocating railcars from its primary elevator system containing certain commodities such as durum to other port terminals in exchange for railcars destined for those facilities containing commodities handled in larger quantities by JRI's facility. Railcar pooling permitted JRI to make better utilization of its limited bin space. By specializing the types of commodities stored in each of the two terminals, the Joint Venture will recapture many of the advantages lost when car pooling was eliminated.

23. The Joint Venture will be able to achieve significant gains in throughput capacity by improving the effectiveness of SWP's limited railcar spot and the specialization of the terminals, allowing greater efficiencies at both plants. For example, the Joint Venture is able to unload larger numbers of railcars at the SWP terminal per shift, by taking advantage of JRI's larger rail yard. Specialization of the terminals will also alleviate potential bottlenecks affecting vessel loading. With larger stocks of grain having the similar characteristics, larger quantities of grain

per ship can be loaded from the SWP terminal, reducing down time lost because of greater vessel movements when smaller quantities of grain are loaded.

24. The throughput capacity of the JRI terminal will benefit because specialization will reduce the number of separate segregations stored in the facility. Working capacity will also benefit because turnover of Non-Board Grains is more frequent due to better inventory management.

25. The result of these efficiency improvements is that the throughput capacity of the two terminals will increase by approximately [Confidential] tonnes per year, from [Confidential] tonnes (SWP: [Confidential] tonnes; JRI: [Confidential] tonnes) to [Confidential] tonnes.

26. The additional blending opportunities afforded by the Joint Venture also allow for improved returns obtained under a canola credit program, under which maximum gains are achieved by blending canola grains and canola dockage to precise specifications established by foreign importers.

27. Operating the facilities jointly also permits savings of certain variable costs, including labour, maintenance and repair expenses, and power consumption.

28. SWP has entered into [Confidential] terminal handling agreements with other grain companies that do not own terminals in the Port of Vancouver (“Non-Integrated Graincos”). Under these agreements, SWP agrees to pay to Non-Integrated Graincos an incentive, called a diversion premium, on a per-tonne basis, in consideration for which Non-Integrated Graincos agree to use the services of SWP’s terminal exclusively for all shipments to the Port of Vancouver. JRI has also entered into similar agreements with other Non-Integrated Graincos. If, as expected, crop production in Western Canada returns to average historic levels following successive years of reduced yields, [Confidential]. Under the Joint Venture, the combined working capacity of SWP’s and JRI’s terminals will be substantially increased, permitting better

service to Non-Integrated Graincos, fewer delays, and reduced risk of demurrage and other penalties.

29. **[Confidential]**

30. SWP and JRI continue to operate their primary grain elevators entirely independently of each other and to compete for the provision of grain handling services and for sales of crop inputs to farmers through their primary elevator systems. SWP and JRI also continue to operate their other port terminal facilities entirely independently of each other. Finally, they continue to compete for the purchase of Non-Board Grains for their own account from grain producers and other grain companies, and for sales of such grain to domestic and foreign markets.

PART V. INDUSTRY OVERVIEW

31. As the SGMF indicates at paragraph 15, the Canadian grain handling and transportation system involves numerous industry participants, including:

- (a) Grain producers. Grain and other commodities, such as wheat, durum, barley, canola, peas, oats and flaxseed, are grown on thousands of farms across Western Canada. Farmers may store their crops on farm, typically in hopper bottomed grain bins, for periods of months or years. Farmers have several options for transportation and sale of their crops: for example, they may ship it by truck and sell it directly to a processor, such as a canola crushing plant or a feed mill; they may truck it to a loading point for loading into producer railcars and shipment by railcar to a port terminal; or they may deliver it by truck to a licensed primary elevator operated by a grain company.
- (b) The Canadian Wheat Board (“CWB”). As described in more detail below, the CWB has a monopoly over the purchase of all wheat and barley for export and for domestic human consumption. The CWB has an important role in allocating

railcar arrivals at port terminals, through its general allocation and railcar tendering programs. Of approximately [**Confidential**] railcars that arrive for unloading at the Joint Venture per week, more than half may contain Board Grains. The Joint Venture usually is advised of its allocation of railcars containing Board Grain one week in advance of its arrival. Under its tendering program, grain companies submit bids to the CWB for railcar allocation, offering rebates on their posted tariff rates in exchange for improved advance (2 to 3 weeks) notice of railcar allocation. However, only 20% of railcars are allocated through the tendering process.

- (c) Grain companies, such as SWP and JRI. As at January 9, 2006, grain companies operate 346 primary grain elevators, located in the grain production areas of Manitoba, Saskatchewan, Alberta and parts of British Columbia, that compete for delivery of grain from farmers. These facilities provide a variety of services, including unloading of grain, elevation, cleaning, drying, storage, and loading of grain into railcars. Grain companies charge a tariff at published rates for many of these services. Beginning in about 1998, grain companies began to replace their existing infrastructure of predominantly small, wooden elevators with large, high throughput primary elevators able to provide all of these services. Presently, approximately 80% of all grain shipped by rail in Western Canada is loaded into railcars at just 80 points. Consequently, services such as cleaning and drying are now widely offered at primary grain elevators throughout Western Canada. With their greater storage space and higher grain volumes, these large facilities are also able to blend grain stocks in order to closely match grading and other specifications that affect pricing and in order to meet customer requirements for specific grain characteristics. Grain may be officially inspected by Canadian Grain Commission inspectors at primary elevators in order to ensure that it meets export standards. Grain shipments can depart high throughput primary elevators ready, without requirements for further processing, for overseas markets.

- (d) Railway companies. Typically railway companies transport bulk grain in hopper cars from primary grain elevators and other points along their rail networks to port terminals in Canada or the United States or to end users. Grain processed and graded to export standards can also be shipped by rail in containers. Railcars are loaded by grain companies at primary elevators and at other locations by farmers themselves. Railway companies provide incentives in the form of discounts to encourage shipments in large multiple-car blocks of 50-99 railcars and 100 or more railcars, with greater discounts payable for 100-car blocks. Railway companies also charge grain shippers a penalty, referred to as demurrage, for delays in loading railcars at primary grain elevators and in unloading railcars once they arrive at port. As these penalties can be very substantial, managing the timing of shipments and the logistics of elevator operations efficiently is critical to minimize the risk of losses. Although the application of penalty charges may vary, demurrage at origin can be \$75.00/railcar for shipments taking longer than 24 hours to load, and demurrage at destination is \$75.00/railcar for shipments taking longer than 48 hours to unload.
- (e) Port terminals. As discussed above, the Joint Venture involves the terminal elevators owned by SWP and JRI in the Port of Vancouver. Other port terminals to which grain is shipped directly by rail within Canada are located in Prince Rupert and Vancouver, British Columbia; Churchill, Manitoba; Thunder Bay, Ontario; and at several points along the St. Lawrence Seaway. As with primary grain elevators, terminal elevators often provide handling services such as unloading grain from railcars, elevation, cleaning, drying, blending and storage of grain. Terminal elevators also provide the service of loading grain onto ocean-going vessels for delivery to customers outside of Canada. As grain is loaded into vessels, it is officially inspected by Canadian Grain Commission inspectors.
- (f) Ocean-going vessels. Grain may be loaded onto ocean-going vessels by port terminals or containerized shipping facilities. Among ocean going vessels

commonly berthed in the Port of Vancouver, Panamax vessels carry cargoes of 50,000 to 70,000 tonnes and are designed to be accommodated by most shipping facilities, including the Panama Canal. Handimax vessels carry cargoes of 40,000 to 50,000 tonnes, while Handi-sized vessels carry 25,000 to 30,000 and can service smaller ports. Most vessels seen in the Port of Vancouver are Handimax and Handi-size, but Panamax vessels are also commonly loaded for large overseas customers, such as China. Vessel sizes in the Ports of Vancouver and Prince Rupert average 35,000 to 40,000 tonnes in most years. Vessel owners also charge grain shippers demurrage for delays in vessel loading. These charges can be very large, ranging from US\$10,000/ship per day to US\$20,000/ship per day or more. Despite these significant penalties, terminal operators often have only 1 day to 2 weeks advance notice of their arrival on berth, and this notice may be inaccurate due to contingencies such as weather, diversion of the vessel to another terminal or another port, and so on. Vessel owners also pay per-hour per-metre berthing charges to terminal owners for the time spent on berth loading grain, and pay dispatch if loading is completed ahead of schedule. In order to avoid losses and earn additional revenues, terminal operators must ensure that the correct stocks of grain are available and ready to be loaded and be able to load vessels in a timely manner. By operating their facilities jointly, SWP and JRI are better able to manage the risks to themselves and other shippers of incurring significant demurrage penalties and enhance their opportunities to earn additional dispatch and berthage revenues.

32. In response to paragraph 16, the Respondents say that, through their primary elevator systems, grain companies compete for the purchase of grain from farmers, including by offering to assign a higher grade to grain for the purpose of settlement on price, discounting the cost of services offered by the grain company, and offering discounts on the purchase of products such as crop inputs. For the purpose of this Response, grain companies that operate primary elevators and terminal elevators in the Port of Vancouver are referred to as “Integrated Graincos,” and grain companies that do not own a terminal in the Port of Vancouver are referred to as “Non-

Integrated Graincos”, although they may own a terminal elevator in another port. As noted above, the Joint Venture does not involve the primary grain elevators of SWP and JRI or their terminal elevators located in other ports.

33. In response to paragraphs 17 and 18, Integrated Graincos have increasingly in recent years entered into terminal handling agreements with Non-Integrated Graincos for the provision of services by Integrated Graincos at their terminal elevators. The duration of these agreements is usually **[Confidential]**. Integrated Graincos agree to pay Non-Integrated Graincos a per-tonne payment, referred to as a diversion premium, in exchange for the Non-Integrated Grainco agreeing to use exclusively the services of a particular terminal for shipments to that relevant port and to provide advance notice of its shipping requirements. This enables the Integrated Grainco to make maximum use of its excess storage capacity and to coordinate the receipt of its shipments and shipments from the Non-Integrated Grainco into its facility, while providing certain service commitments and a financial incentive to the Non-Integrated Grainco. The amount of diversion premiums payable under such agreements varies, and may differ depending upon the type of grain shipped and whether it arrives at the terminal cleaned or uncleaned. As discussed below, the incentive for Integrated Graincos to enter into such agreements diminishes as their own grain shipments from primary elevators increase and as they approach the maximum operating capacity of their port terminals. SWP first began receiving shipments of grain from **[Confidential]** a Non-Integrated Grainco, during the crop year ending on July 31, 2002, **[Confidential]**. Prior to these arrangements, SWP had not actively competed for third party tonnes because its own originations and those of an affiliated grain company exhausted the capacity of its Vancouver terminal. With a return to average crop production in Western Canada, SWP’s and JRI’s grain volumes generated internally through their primary elevator systems will rise. **[Confidential]**

34. Western Canadian grain production varies drastically from year to year. During the ten year period from 1995-2004, farmers produced an average of 46.8 million tonnes of the six major grains (all wheat [including durum], barley, canola, flaxseed, peas and oats), from a low of 30.0 million tonnes in 2002-3 to a high of 54.5 million tonnes in 1996-1997. During that same

period, Canadian grain exports through all points of exit averaged 24.2 million tonnes, ranging from 13.6 million tonnes to 28.3 million tonnes. Approximately 51.6% of grain produced in Western Canada is exported to international markets; 34.5% is used for domestic animal feed consumption, and 13.2% is used for domestic processing, such as flourmills and crushing plants. Production of grain and other commodities is estimated at 53.3 million tonnes for 2005-2006, which would be the second largest total yield ever and represent a 10 million tonne increase (a 26% improvement) over the drought-reduced average of 43.3 million tonnes recorded between the years 2000/04.

35. Seeded acreage of the six major grains and special crops (rye, lentils, chickpeas, mustard and canary seed) grown in Western Canada has been fairly consistent over the past five years at just under 62 million acres. However over that period, droughts have dramatically impacted both harvested acreage (down 20% in 2002/03) and production (down 23%, 41% and 11% in 2001/02, 2002/03 and 2003/04 respectively). The decline is also reflected in receipts at primary grain elevators, which fell dramatically in the drought-affected years. Even though production recovered in 2004/05 to near the pre-drought average, deliveries to licensed elevators were only slightly higher than in the previous year (when production was down 11%). The main factor causing the reduction in marketing was frost in much of Saskatchewan and eastern Manitoba, which reduced the volume of export quality grains in 2004/05.

Percent of Pre Drought Average for Western Canada (1995/97 to 2000/01)				
	Seeded Acreage	Harvested Acreage	Production	CGC Receipts
2000/01	102%	104%	101%	99%
2001/02	97%	97%	77%	75%
2002/03	99%	81%	59%	58%
2003/04	101%	101%	89%	85%
2004/05	101%	101%	101%	87%
2005/06	99%	100%	105%	[Confidential]

36. The impact on SWP and JRI volumes has been even more pronounced because both have a higher level of market share in Saskatchewan than they have in Western Canada as a whole. Saskatchewan was even more severely impacted by the droughts and by the frost in 2004/05 than

Western Canada as a whole. This explains why SWP and JRI grain originations in total and therefore to Vancouver were reduced during the past five years.

37. SWP's expectation that it will increase its shipments of grain generated through its primary elevator system over and above the volumes seen during the past five years is based upon an expectation of recovery in exports from all export corridors. Actual exports through licensed facilities and the CWB's projected exports as provided in its long-term trade forecasts are as follows:

Export Corridors (000 tonnes)					
	West Coast	Churchill	East Coast	Prairie Direct	Total
5 year avg. pre-drought*	14,571	385	6,752	3,204	24,912
10 year rolling average	12,844	408	6,558	2,981	22,791
5 year rolling average	11,463	426	5,987	2,802	20,678
2000/01	14,621	516	6,478	3,204	24,819
2001/02	11,242	475	6,441	3,226	21,385
2002/03	6,035	352	4,709	1,564	12,660
2003/04	12,070	518	7,342	2,976	22,905
2004/05	12,480	400	5,439	2,266	20,585
2006/07**	14,300	500	6,000	3,700	24,500
2011/12**	14,900	600	6,200	4,100	25,800
* 5 year average pre drought from 1996/97 to 2000/01					
** CWB forecast					

38. Forecasts suggest a recovery in exports to all ports. The West Coast 5 year average pre-drought is consistent with the CWB's long-term projections, and is over 3 million tonnes greater than volumes shipped to the West Coast during the rolling five-year average period of 2000/01 to 2004/05.

39. The annual working capacity of SWP's port terminal, operated outside of the Joint Venture, is approximately [Confidential] tonnes. [Confidential]

A. *Regulatory Environment*

40. In response to paragraphs 20 to 26 of the SGMF, SWP says that the Canadian grain handling and transportation system is highly regulated. For grain handling companies, the principal regulatory regimes are the *Canada Grain Act* and the *Canadian Wheat Board Act*.

1. *Canadian Grain Commission*

41. The Canadian Grain Commission (“hereinafter “CGC”) is created pursuant to the provisions of the *Canada Grain Act*, R.S.C. 1985, c. G-10, with the mandate to “establish and maintain standards of quality for Canadian grain and regulate grain handling in Canada, to ensure a dependable commodity for domestic and export markets”: *Canada Grain Act*, s. 13.

42. In furtherance of these objects, the CGC is responsible for, *inter alia*: establishing grain grades and standards; implementing a system for grading and inspecting grain; and establishing and applying standards and procedures for handling, transportation and storage of grain and facilities used for these purposes: *Canada Grain Act*, s. 14. CGC grain inspectors may conduct official inspections of grain at such places as the CGC may determine: *Canada Grain Act*, ss. 29, 30.

43. The CGC is also responsible to establish by regulation conditions for licensure of different classes of grain elevators, including primary and terminal elevators, and for issuance of such licenses: *Canada Grain Act*, ss. 42, 43.

44. Before the start of a crop year, SWP and JRI and all other licensees are required to file with the CGC a schedule of tariffs to be charged for services provided at their primary grain elevators and port terminals, which they can subsequently amend during the crop year. These tariff schedules are published by the CGC, and licensees may not charge any sums greater than their posted tariffs for the services they provide. In addition, upon written complaint and after a hearing the CGC may by order fix a maximum charge for services provided by a licensee. The

CGC may also in certain circumstances fix, by regulation, a special maximum storage charge relating to any type of storage of grain, grain products or screenings in licensed elevators of any type: *Canada Grain Act*, s. 50, 51, 53. The CGC may also, with the approval of the Governor-in-Council, make regulations fixing or determining a manner for fixing charges for services provided by licensees: *Canada Grain Act*, s. 116(m). Licensees file tariffs independently for elevation of grain, cleaning, storage and drying.

45. As discussed in more detail below, pursuant to Section 69 of the *Canada Grain Act*, the operator of every licensed terminal operator is obligated, “at all reasonable hours on each day on which the elevator is open, without discrimination and in the order in which grain arrives and is lawfully offered at the elevator, [to] receive into the elevator all grain so lawfully offered for which there is, in the elevator, available storage accommodation of the type required by the person by whom the grain is offered.” The CGC may also order the operator of a licensed terminal elevator to receive grain for storage in other circumstances.

46. Prior to or upon receipt into port terminals, shipments of grain must be officially inspected by a CGC inspector. The operator of a licensed terminal is also required to cause grain to be officially weighed and inspected upon discharge from the terminal into a vessel. The operator is also required to provide stock reports to the CGC at prescribed intervals and to submit to periodic grain audits by the CGC at prescribed intervals: *Canada Grain Act*, s. 70, 79, 80.

2. Canadian Wheat Board

47. The Canadian Wheat Board is continued under the *Canadian Wheat Board Act*, R.S.C. 1985, c. C-24 (the “*CWB Act*”), for the purpose of marketing, in interprovincial and export trade, wheat and barley grown in Canada: *CWB Act*, s. 5. The CWB has a monopoly over the purchase of all wheat and barley (“Board Grain”) produced in a designated area, composed of the three prairie provinces and part of British Columbia. The CWB also has a monopoly over the interprovincial and international marketing (sometimes referred to as “single-desk selling”) of wheat and barley. The CWB’s monopoly does not include wheat and barley sold for domestic

consumption by livestock or poultry, nor does it include other commodities such as canola (collectively, “Non-Board Grains”).

48. The *CWB Act* prohibits anyone other than the CWB from exporting from Canada wheat or wheat products and barley or barley products, or transporting, buying or selling such products interprovincially: *CWB Act*, s. 45.

49. All Board Grain entering interprovincial and foreign trade is purchased and marketed by the CWB; Board Grain purchased directly from the farmers on the prairies cannot be shipped to another province without the production of a license from the CWB: *CWB Act*, s. 45. The CWB is responsible for marketing all Board Grain delivered either to elevators or railway cars: *CWB Act*, s. 32.

50. Although the CWB does not own or operate grain elevators, the *CWB Act* provides that grain elevators are operated on behalf of the CWB and no one other than an agent of the CWB may operate an elevator: *CWB Act*, s. 20. Among other things, when Board Grain is delivered to an elevator, the elevator operator is required to record the grade and net weight received, after deducting dockage: *CWB Act*, s. 24(2).

51. In accordance with the *CWB Act*, SWP and JRI act as agents for the CWB in respect of the receipt, storage, cleaning, drying, and loading into railcars of CWB Grains at their primary elevators and their port terminal facilities. The CWB is by far the largest purchaser of services from the Joint Venture: approximately [Confidential]% of the grain received by the Joint Venture since operations began has been Board Grain. During the three years prior to the Joint Venture, [Confidential]% of the grain received by SWP’s terminal was Board Grain. From time to time the CWB requests services in addition to the services for which licensed elevator operators have filed a tariff. When these requests arise, an industry association will negotiate a charge for this service with the CWB on behalf of the industry. Failing agreement, in certain instances the CWB has simply unilaterally advised grain companies the amount that it will pay for a service and tendered payment for that amount.

3. Terminal Authorization

52. Terminal authorization means that a terminal will accept a shipment of grain when it arrives by railcar for unloading. As noted above, the operator of a licensed terminal is required to accept delivery of all grain in the order in which it arrives for which there is in the terminal storage available of the type required: *Canada Grain Act*, s. 69. In order to ensure that appropriate storage will be available at the terminal when grain arrives by railcar, railway companies require all shippers to obtain terminal authorization before they will authorize placement of railcars for loading. Terminal authorization is granted by terminal operators on a “ship-to-sales” basis, meaning that product is being shipped to meet an actual sale, rather than speculation on a future or possible sale. This prevents unsold stocks from accumulating in the limited storage available at port terminal elevators and reduces the incidence of demurrage charges when railcars cannot be unloaded on a timely basis. The principle of granting terminal authorization on a “ship-to-sales” basis is essential for ensuring the efficient performance of port terminals and for maximizing their productivity. It ensures that grain shippers, including Non-Integrated Graincos, do not incur unnecessary storage fees or sustain avoidable demurrage penalties.

PART VI. MARKET DEFINITIONS

A. Product Market

53. In response to paragraph 27 of the SGMF, SWP denies that port terminal grain handling services is an appropriate definition of the relevant product market. “Port terminal grain handling services” comprises a number of distinct services, and they are not, collectively, a unique service for which there are no substitutes.

54. At paragraph 28, the SGMF identifies “elevation, cleaning, segregation, drying, storage, grading, blending and loading onto a vessel” as “Port terminal grain handling services.” These are separate and distinct services, most of which are also supplied by primary grain elevators and others. The relevant product market for each of these services is different and each product market must be defined separately.

55. Elevation refers to the process of lifting grain from a collection area called a pit, to the top of an elevator, after which it can be directed into storage bins, cleaning machinery, loading spouts for discharge from the elevator, and so on. This service is provided at primary grain elevators as well as port grain handling terminals.

56. Cleaning is the removal of dockage, which is separable foreign material such as weed seeds, other grains, straw, small stones, and so on, from grain using cleaning machines. Cleaning services are provided at many primary grain elevators and other facilities across Western Canada. Grain may be transported cleaned or uncleaned by railcar to port terminals. With the construction of high throughput primary elevators, grain is increasingly cleaned before shipment by rail. During the last 3 crop years, on average [Confidential]% of grain shipped to the SWP terminal arrived previously cleaned.

57. Segregation is the separate storing of grains having different grades and characteristics. Grain may be segregated in primary grain elevators or in port terminals facilities.

58. Drying involves the removal of some of the moisture from grain by mechanically moving air through grain after it has been harvested. Demand for these services varies depending upon the drying conditions in the field prior to harvest. Drying services are provided at many primary grain elevators and other facilities throughout Western Canada. Drying grain before shipment reduces rail transportation costs. Only a small percentage of grain which arrives at the Port of Vancouver requires drying. For example, in 2004/05, SWP dried [Confidential] tonnes of grain at its primary grain elevators, and [Confidential] at its Vancouver terminal.

59. Grain may be stored by grain producers in bins on their farms for significant periods of time. In addition, storage is provided as a service throughout the primary elevator system. Port terminals do not derive significant revenue from grain storage and, because of the need for efficient throughput, storage of grain for any length of time in terminal elevators is discouraged.

60. Ideally, grain is stored in terminal elevators for short periods, between the time that grain can be unloaded from railcars, processed, and loaded onto vessels. Storage of grain stocks also permits blending of large quantities of grain to particular specifications. Grain may be stored for much longer periods in the primary elevator system without undermining the productivity or efficiency of those facilities to nearly the same degree it affects terminal elevators.

61. Grading is not a discrete service provided by the Joint Venture, although grading takes place at the Joint Venture. When SWP and JRI purchase grain from farmers or other grain companies, on their own account in the case of Non-Board Grains or as agents of the CWB in the case of Board Grains, SWP and JRI determine the price payable for such grain on the basis of their assessment of the grade and other qualities of the grain. However, as discussed above, CGC inspectors perform official inspections of grain bound for export. All grain loaded onto vessels by the Joint Venture is graded during loading by CGC inspectors. Official grading can be done at any location, including at primary grain elevators throughout Western Canada.

62. Blending is the process by which grain stocks are combined in order to match certain specifications required by customers. Grain companies will often blend grain having different grades or protein content or other characteristics in order to achieve a uniform product with a higher total value. The Joint Venture may blend different grain stocks at the direction of the CWB in order to meet its requirements. Blending to meet export requirements is often completed at primary grain elevators and shipped to the Joint Venture and other port terminals ready for export.

63. Bulk loading of grain onto ocean-going vessels is a service offered by the Joint Venture, four other terminals in the Port of Vancouver (Cascadia, UGG, Pacific, and Vancouver Wharves); Neptune Bulk Terminals Canada Ltd., a bulk container loading facility located in the Port of Vancouver; and terminals located in other Canadian and U.S. ports.

64. As the foregoing suggests, few of the services that comprise "Port terminal grain handling services" as defined by the Commissioner are provided exclusively by port terminal

operators. Consequently, the relevant product market asserted by the Commissioner is incorrect. Only two services comprising the set of services identified by the Commissioner, storage of grain between unloading of railcars and vessel loading, and vessel loading itself, are not provided by primary grain elevators. There are numerous competitors for the supply of these two services, as noted above.

65. Approximately 48% of the major grains produced in Western Canada are not exported. Of exported grain, almost 6% (3% of total production) is exported directly by truck, rail or container and does not enter the primary elevator system or port terminals. For instance, in 2004 in the Port of Vancouver 14% of grain traffic (and 4% of the six major grains) moved in containers outside of the bulk handling system. Of the grain that enters the primary elevator system in Western Canada, a significant portion (12.5% over the past ten years) is exported directly, rather than through licensed terminal elevators. Grain can be readily exported from any primary grain elevator by rail to customers in the United States and Mexico, as well as to U.S. export ports for further shipment overseas.

66. The CWB and Non-Integrated Graincos are able to bypass port terminals altogether in shipping grain to foreign customers. Grain may be shipped to northern U.S. customers by truck or rail, and by rail to more distant destinations in North America.

67. In response to paragraph 30, the Respondents say that grain may be cleaned to export standards and blended to meet customer requirements at primary grain elevators, and then shipped directly to a loading facility for direct loading onto ocean-going vessels at port. These “direct hit” shipments permit shippers to bypass port terminal facilities completely.

68. With the expansion of services that primary grain elevators can provide, including drying, cleaning and blending grain to meet export standards and the contractual specifications of foreign customers, grain may also be loaded into containers, in bulk or bags of varying sizes, and shipped by rail to port or to other destinations. Containerized shipping is another means by which shippers can bypass the bulk handling facilities of port terminals completely.

Containerized shipping also permits certain efficiencies for railways, because they can maximize the use of containers that might otherwise return empty to port from inland locations. Limited railcar supply and frequent bottlenecks make the alternative of containerized shipping of grain a viable alternative to bulk handling. Additional container shipping capacity is presently being added by Canadian National Railway to the Port of Prince Rupert and is projected to be operational in 2007.

69. For these reasons, the Respondents submit that the Commissioner's definition of the relevant product market is inaccurate. Each service provided by the Joint Venture is within a separate and distinct product market. An appropriate delineation of these markets is necessary to distinguish among the different services comprising the set of services provided by port terminal elevators, among others. The definition must reflect the comparable grain handling services supplied by primary grain elevators as well as other methods for the export of grain, including shipment by truck and rail to continental customers and direct hit shipments to ocean-going vessels. In addition, the relevant product market must include alternate means for the transportation of grain, such as containerized shipments.

B. Geographic Market

70. In response to paragraphs 32 to 35 of the SGMF, the Respondents say that the Port of Vancouver or, alternatively, the Ports of Vancouver and Prince Rupert, is not an appropriate definition of the relevant geographic market. In respect of the set of services provided by the Joint Venture but not separately identified by the Commissioner, the Joint Venture competes with primary grain elevators located throughout Western Canada. In addition, the Joint Venture competes with other licensed terminals located in British Columbia and elsewhere in Canada and the United States.

71. As the Commissioner states in the SGMF at paragraph 15(d), rail transportation charges account for about half of the costs of handling and transportation grain bound for export. Other

charges that may be incurred to ship grain from farm to foreign customer include: trucking charges to transport grain from farm to primary grain elevator; charges by the primary grain elevator for such services as elevation, storage, drying and cleaning; charges by the port terminal operator for services at port; CGC inspection fees; vessel freight charges and any other transportation costs incurred before the grain reaches its destination. Fees charged by the port terminal operator are a small component of this total cost. Changes to any of the other component costs from farm to export customer can have a significant effect on the decision to sell and the export corridor used to effect the sale.

72. Shippers have many alternatives to using the services of the Joint Venture as a conduit for grain shipments to foreign customers. They may choose to use the services of other terminals in the Port of Vancouver, ship grain through other Canadian ports, such as Prince Rupert or Thunder Bay or they may ship their grain in containers, bypassing terminal elevators altogether. They may ship grain by truck or rail into the United States for export or they may elect to sell their grain domestically or to North American customers.

73. There is no defined dividing line determining whether shipments of grain by railcar from Western Canada travel westward to the Ports of Vancouver and Prince Rupert, north-eastward to the Port of Churchill, or eastward to Thunder Bay, Montreal and other eastern ports. The CWB, for example, sometimes chooses to incur adverse freight by shipping grain eastward or westward even though the differential cost of rail transportation cannot be recovered from the grain producer because a price had previously been settled upon for the farmer's grain basis shipment by an alternate export corridor. Changes to other components of the grain handling and transportation system, such as vessel charges, may greatly influence the direction in which grain flows.

74. Therefore, the Respondents submit that the terminal elevators located in the Port of Vancouver and Prince Rupert compete with terminals in other Canadian ports, including Thunder Bay. An indication of this competition is the similarity of tariff rates for grain handling

services published by the terminals in Vancouver, Prince Rupert and Thunder Bay. An appropriate definition of the relevant geographic market cannot exclude these other facilities.

75. In addition to shipments through the numerous Canadian ports, several ports in the United States offer competitive alternatives. These ports are typically public warehouses and as such have to provide service to the public at published tariffs, which are typically substantially lower than those in Canada. Relevant ports include those in the Pacific Northwest, such as Seattle, Tacoma and Portland. Grain produced in Canada could reach these ports through several channels including direct rail, as well as cross-border movement by truck to primary grain elevators in the United States. Other market corridors include the locations in the United States along the Gulf of Mexico, which can be reached directly by rail or transloading into barges. No American or Canadian regulatory barriers prohibit such flows, and both the CWB and CGC have investigated the practicality of such movements.

76. Therefore, the Respondents submit that the Port of Vancouver is not the relevant geographic market for the supply of the set of services described by the Commissioner as “Port terminal grain handling services.” The relevant geographic market includes other port terminal elevators located at Prince Rupert, Churchill, Thunder Bay, Sorel, Quebec City and Montreal, as well as port terminals in the United States.

PART VII. COMPETITIVE ANALYSIS

77. The Respondents submit that the Joint Venture has not and is not likely to substantially prevent or lessen competition in any appropriately defined relevant market. The Joint Venture permits SWP and JRI to continue to compete for grain shipments from Non-Integrated Graincos, which they will otherwise not compete for effectively or vigorously during years of average crop production and average exports. The Joint Venture will also continue to compete with port terminals located at the Port of Vancouver and other Canadian ports, and with alternatives means of shipment of grain and alternate domestic uses for grain. Contrary to the allegations in the SGMF, the Joint Venture will not be able to sustain a material price increase in tariffs or a

reduction in diversion premiums without market discipline from rivals, nor will it be able to reduce service to Non-Integrated Graincos.

78. In response to paragraph 36, for the reasons outlined above the Respondents say that the list of port terminals located in Vancouver and Prince Rupert is an incomplete summary of competitors of the Joint Venture. Further the Respondents submit that the relevant market definition cannot be restricted to “Canadian West Coast Port Terminals.”

A. *Market Shares*

79. In response to paragraph 37 of the SGMF, and for the reasons previously outlined above, the values given for market shares of the respective competitors in the market as defined by the Commissioner are incomplete because they disregard receipts at terminals not located in the Port of Vancouver and those terminals’ storage capacity. The Commissioner also disregards other competitors that comprise the relevant geographic market and also fails to distinguish among the distinct services provided by Joint Venture, including storage, cleaning, drying, and blending of grain, and the relevant competitors for the supply of those services. It does not differentiate between receipts of Board and Non-Board Grains at the terminals or the terminal owners’ originations of grain through their own primary elevator systems and grain shipped by Non-Integrated Graincos.

80. In the case of SWP, grain originated through its primary elevator system accounted for **[Confidential]**% of all grain handled at its Port of Vancouver terminal prior to November 2002. During the subsequent years of below average grain production in Western Canada, SWP’s own originations of grain dropped. SWP attempted to fill some of its unused capacity at the Port of Vancouver by entering into terminal handling agreements with Non-Integrated Graincos, as outlined above. Between the 2001/02 and 2004/05 crop years, approximately **[Confidential]**% of grain receipts at SWP’s Vancouver terminal were shipped by Non-Integrated Graincos pursuant to terminal handling agreements. **[Confidential]**

81. The Respondents submit that the capacity available at the port terminals for supplying services to Non-Integrated Graincos, not the total capacity of the terminals, is relevant for analyzing the effect of the Joint Venture on Non-Integrated Graincos. In addition, any assessment of the operational capacity not required by the terminal owners for grain volumes generated through their own primary elevator system, which is therefore available to receive shipments from Non-Integrated Graincos, must take into account that volumes in the Port of Vancouver during the past five years were unusually low as a result of below average grain production and, in one year, a lengthy work stoppage. A more accurate measure of this excess capacity should reflect SWP's and JRI's internal originations of grain during years of average grain production and their reasonable projections for such volumes in the future.

82. In the case of SWP, grain shipments from its own primary elevator system are projected to exceed [**Confidential**] tonnes by the 2007/08 crop year [**Confidential**].

83. In the alternative, although the Commissioner apparently concedes that the Port of Prince Rupert is within the relevant market, the Commissioner has omitted the capacity and receipts from Prince Rupert Grain Ltd. from the table at paragraph 37 of the SGMF purporting to identify market shares in the relevant market. In a market definition that includes only the Ports of Vancouver and Prince Rupert, the combined market share of the Joint Venture would be less than the 35% threshold set out in the *Merger Enforcement Guidelines* (Competition Bureau, September 2004), p. 17, para. 4.12.

B. Barriers to Entry

84. At paragraphs 41 to 45 of the SGMF, the Commissioner alleges that barriers to entry are very high. However, the Commissioner's consideration of possible entrants in the market considers only the costs of construction of a new terminal elevator, limitations on land available for such a facility, and difficulties involved in securing rail and vessel access in the Port of Vancouver. This analysis flawed both because it is based upon an incorrect definition of the

relevant geographic and product markets and because it fails to consider other potential competitors in the Port of Vancouver.

85. For example, the Commissioner fails to consider whether Vancouver Wharves could increase its supply of services to Non-Integrated Graincos. Vancouver Wharves is a terminal elevator located in the Port of Vancouver, with a licensed capacity of 25,000 tonnes. While Vancouver Wharves does not presently offer grain cleaning services, it could add cleaning machines with a moderate investment of capital. Because grain is increasingly cleaned in the primary elevator system, the present lack of such facilities is not a significant barrier to this entrant. Vancouver Wharves is also configured so that it could add additional storage capacity to its existing facility. None of the impediments to construction of a new facility described at paragraph 43 of the SGMF would hinder Vancouver Wharves' ability to add additional capacity and provide additional services.

86. The Commissioner also fails to consider the possibility of increased containerized shipping of grain. As noted above, Canadian National Railway is planning a container shipping facility for the Port of Prince Rupert, which could be used for shipments of grain cleaned and graded to export standards at primary grain elevators. Containerized shipping is also presently available in the Port of Vancouver. The limited financial investment necessary for a competitor to offer alternate grain shipment services to bulk grain handling by Integrated Graincos would not be a significant obstacle.

87. The Commissioner alleges at paragraph 48 of the SGMF that Cargill Limited ("Cargill") is not an effective remaining competitor to the Joint Venture. However, Cargill presently owns 50% of the Cascadia terminal located in the Port of Vancouver and, [Confidential]. There do not appear to be any barriers to entry for Cargill, given its co-ownership of an operating terminal facility, which is in fact the largest licensed facility in the Port of Vancouver.

88. Finally, as noted at paragraph 45 of the SGMF, Agricore United ("AU") was required pursuant to the terms of a Consent Agreement filed with the Competition Tribunal on October

17, 2002, to divest of either the UGG or Pacific Elevators terminals locate on the South Shore of Burrard Inlet at the Port of Vancouver. AU has made an application under s. 106 of the *Competition Act* to be relieved of this obligation, but if the application is dismissed, a new competitor could enter at the Port of Vancouver through the acquisition of AU's facility.

C. *Removal of a Vigorous and Effective Competitor*

89. Full implementation of the Joint Venture, including contracting by the Joint Venture directly with Non-Integrated Graincos, will not eliminate a vigorous and effective competitor from the market, properly defined. SWP and JRI have not been vigorous and effective competitors for shipments from Non-Integrated Graincos. First, SWP only began entering into formal terminal handling agreements in [Confidential] in order to mitigate the reduction in volumes at its Vancouver terminal resulting from poor crop production. As grain production returns to historic levels, SWP's incentive to compete for third party grain will diminish because its own requirements for the grain handling services of its facility will rise. Second, there have been only [Confidential] instances since [Confidential] in which SWP has entered into terminal handling agreements with Non-Integrated Graincos that had previously contracted with JRI. [Confidential] circumstance demonstrates that SWP and JRI have vigorously and effectively competed with one another. For example, in the case of [Confidential], SWP was able, because of the larger capacity of its terminal, to meet [Confidential] complete requirements for services, whereas JRI could not do so.

D. *Effective Remaining Competition*

90. In response to paragraphs 48 and 49, the Respondents deny that the creation of the Joint Venture means that the only effective remaining competitor in the Port of Vancouver is Agricore United and further deny that the Joint Venture has resulted in a duopoly. As outlined above, the Respondents dispute the narrow market definition proposed by the Commissioner. In addition, as outlined above, without the Joint Venture neither SWP nor JRI can continue to compete with Agricore United or other terminal operators for the provision of terminal services to Non-

Integrated Graincos in the Port of Vancouver. Therefore, the Joint Venture will add an effective competitor to the market even as narrowly defined by the Commissioner.

91. In response to paragraphs 36 and 50 to 55, the Respondents deny that Prince Rupert Grain Ltd. (“PRG”) is not a vigorous and effective competitor to the Joint Venture. The terminal operated by PRG in the Port of Prince Rupert provides many of the same grain handling services as the Joint Venture, including cleaning, segregating, blending, drying, elevating, storing and unloading grain. Although SWP and JRI each have an ownership interest in the PRG terminal, they do not individually or collectively have a controlling interest in the terminal and all decisions for the owners of PRG require their unanimous approval. PRG’s management decides independently of PRG’s owners whether and for how long the terminal will operate each year. Continuous operation of PRG throughout the year is largely dependent upon CN and CWB interest; as a result of its successful marketing efforts, PRG has operated year-round in each of the last three years. The CWB, not PRG’s owners, has the greatest influence on PRG’s window of operations through the year.

92. PRG’s management operates the facility independently and competes vigorously for additional grain volumes, including with respect to service and pricing. PRG has certain efficiency advantages over Vancouver facilities that it markets to CN and the CWB in order to encourage further grain shipments to Prince Rupert. PRG competes with respect to pricing by, *inter alia*, participating in programs that offer reduced costs to the CWB. While PRG does not have direct rail service from the CP rail network, PRG is in no different position than the Joint Venture in this regard and CP-originated grain shipments have moved to PRG during each of the last two years. From most locations in Western Canada, the cost of rail transportation to Prince Rupert is the same as to Vancouver. Finally, while PRG is not presently configured to clean canola, it could provide this service with minimal investment of time and capital.

93. In addition, the SGMF ignores the presence of Vancouver Wharves in the Port of Vancouver. Vancouver Wharves is a licensed grain terminal, has provided grain handling services in recent years, including unloading, elevation, storage and loading of grain onto

vessels. As discussed above, while Vancouver Wharves does not presently have cleaning capacity, it could add cleaning machines with minimal investment. Vancouver Wharves also has the ability to add additional storage capacity to its present operations.

E. Foreign Competition

94. At paragraph 56 of the SGMF, the Commissioner alleges that port terminals operating in the Pacific North-West of the United States are not close substitutes for port terminal services at Canadian West Coast Ports. As argued above, the Respondents do not accept the market definition advanced by the Commissioner and therefore say that the Commissioner's analysis of the substitutability of the services of foreign competitors for those of the Joint Venture is too narrow. In addition, the Respondents say that rail costs to ship grain by rail from Western Canada to U.S. ports are variable depending upon location and are only one component of the cost of shipping grain from grain producers to overseas markets. Other costs, such as terminal charges, regulatory fees, and vessel freight may offset higher rail freight. Grain may also be shipped by truck or rail to U.S. destinations, and by rail and barge to U.S. ports on the Gulf of Mexico.

95. Accordingly, the Respondents submit that foreign competitors are likely to provide effective competition to the Joint Venture.

F. Competitive Effects

96. In response to paragraph 57 of the SGMF, the Respondents submit that, if the market is properly defined, the market for the various services offered by the Joint Venture is not highly concentrated nor has the Joint Venture resulted in a duopoly. As discussed above, the Joint Venture will provide additional choice for Non-Integrated Graincos; **[Confidential]**. The Respondents anticipate that JRI will have similar difficulties meeting the requirements of Non-Integrated Graincos. Operating its terminal independently, JRI cannot compete for shipments from **[Confidential]** since, with its existing obligations to Non-Integrated Graincos, it would have no ability to handle these companies' volumes. However, the Joint Venture will have capacity to solicit additional shipments from Non-Integrated Graincos.

G. *Alleged Unilateral Effects*

97. For reasons discussed above, the Respondents deny that the unilateral exercise of market power is likely as a result of the Joint Venture. Contrary to paragraph 58 of the SGMF, the Joint Venture does not “remove a service provider to whom buyers would otherwise turn in response to a price increase”; instead, it will offer to Non-Integrated Graincos another alternative to facilities controlled by Agricore United in the Port of Vancouver. Through efficient joint management of the two facilities, the Joint Venture operator will be able to increase their combined operational capacity. This will ensure that the Joint Venture has an incentive to solicit third party shipments and ensure that it is able to offer timely service to Non-Integrated Graincos. As SWP and JRI have not been effective competitors for shipments from Non-Integrated Graincos, even during successive years of crop failure, they would be even less able and have little incentive to compete with one another for third party shipments once their internal generations of grain return to levels expected during average crop years.

98. The level of diversion premiums offered by Integrated Graincos to Non-Integrated Graincos to induce them to enter into terminal handling agreements depends upon two main factors:

- excess capacity at the terminals in Vancouver (demand for third party grain); and
- supply of grain to Vancouver by Non-Integrated Graincos (supply of third party grain).

99. The excess capacity of the major terminals in Vancouver is in turn determined by three main factors:

- overall working capacity of their plants, given the current crop mix and policy environment;
- supply of grain to Vancouver from their integrated facilities; and
- supply of grain to Vancouver from facilities where they have third party agreements.

100. As discussed above, West Coast volumes have been down 3 million tonnes during the past 5 years from the pre-drought average of 14.5 million tonnes and down about the same amount from the CWB's long term projection. As a result, during the past 5 years the excess capacity of the terminals (demand for third party volumes) has been larger than average and the supply of third party volumes has been lower than average. If the CWB's projections for a return to normal volumes are correct, there will be pressure on diversion premiums because of increased supplies of grain generated internally by Integrated Graincos and increased supplies of grain from Non-Integrated Graincos.

101. **[Confidential]** SWP estimates that, together, SWP and JRI will originate **[Confidential]** tonnes of grain shipments. Without the Joint Venture, they would have combined annual throughput capacity of approximately **[Confidential]** tonnes, leaving them only **[Confidential]** tonnes of capacity to compete separately for shipments from Non-Integrated Graincos. In that circumstance neither will be a significant competitor in the marketplace. With the Joint Venture, annual throughput capacity of the two facilities has increased to about **[Confidential]** tonnes. The result will be that the Joint Venture will have capacity in excess of current terminal handling agreements, which will permit the Joint Venture to compete with South Shore terminals for additional third party tonnes. This should relieve downward pressure on diversion premiums resulting from higher supply of grain.

102. Moreover, the Joint Venture will be subject to effective discipline by competitive responses from rivals. The Joint Venture competes not only with grain handling facilities on the South Shore of Burrard Inlet in Vancouver, but with numerous alternate port terminals located at Prince Rupert, Churchill, Thunder Bay, Montreal, among other Canadian locations, as well as U.S. ports located in the Pacific North-West and the Gulf of Mexico. The Joint Venture also competes with domestic end-users of grain and with alternate methods for shipping grain from Western Canada to overseas markets, including containerized and direct-hit shipments. These alternate competitors will effectively constrain the Joint Venture's ability to raise tariffs unilaterally, eliminate diversion premiums, or limit timely access to the Joint Venture facilities.

103. Excess capacity and high fixed costs of operation will prevent the Joint Venture from raising tariffs substantially. For example, if the Joint Venture attempted to sustain a 5% increase in tariffs, Agricore United could take advantage of its excess capacity on the South Shore of the Port of Vancouver and draw third party shipments away from the Joint Venture. Accordingly, such an increase would not be sustainable. If anything, tariffs are more likely to increase if SWP and JRI, operating their terminals separately, approach the limits of their working capacity. Tariffs are less likely to increase if SWP and JRI add [**Confidential**] tonnes of working capacity in the Port of Vancouver.

104. Even if the narrow market definition advanced by the Commissioner were correct, the Respondents submit that the Joint Venture would be unable to sustain a unilateral price increase. Such a price increase would not be profitable because other terminal operators in the Port of Vancouver would be able to absorb the demand for alternate sources of supply. As the SGMF illustrates at paragraph 37, the capacity of the three other grain handling terminals in the Port of Vancouver (the Cascadia, UGG and Pacific Elevators terminals) is substantially greater than that of the Joint Venture and those facilities are also under-utilized. For example, while the Pacific Elevators facility has 25.5% of the licensed storage capacity, its share of grain receipts in 2003-2004 was only 6%.

H. Alleged Coordinated Effects

105. For many of the reasons discussed above, the Respondents deny that the Joint Venture will result in coordinated effects. Because the relevant market is substantially broader than the Commissioner asserts, coordinated behaviour among the operators of terminals located in Vancouver and Prince Rupert will not be possible or sustainable. In addition, the proposed Joint Venture permits the SWP and JRI facilities to continue to compete for shipments from Non-Integrated Graincos; without this additional working capacity, neither will have significant incentive to offer diversion premiums or the ability to provide timely access to shipments from Non-Integrated Graincos. Furthermore, as the Joint Venture and other terminals in the Port of Vancouver compete with terminals in other ports, with primary grain elevators, and with

alternate modes of grain transportation, they will not be able to raise tariff rates to levels that would be obtained in a monopoly market as the Commissioner alleges at paragraph 61 of the SGMF.

106. Coordinated behaviour is only likely to be sustainable when competitors are able to monitor one another's conduct and respond to any deviations from the coordinated behaviour through credible deterrent mechanisms, such as lowering prices. While each grain companies' published schedule of tariffs for grain handling services is highly transparent, the terms and provisions of terminal handling agreements between terminal operators and Non-Integrated Graincos, including the amount of diversion premiums and any service commitments, are considered confidential in the industry. Accordingly, competitors will not be able to engage in coordinated behaviour by monitoring each other's conduct in respect of pricing and service standards offered to Non-Integrated Graincos.

107. Other factors also suggest that terminal owners would have an incentive to deviate from coordinated behaviour. The size and frequency of the transactions in question – terminal handling agreements between terminal owners and Non-Integrated Graincos – suggests that deviations from coordinated behaviour would be more profitable, making coordinated behaviour less likely. As discussed above, the term of terminal handling agreements is typically **[Confidential]**, and the agreements usually contemplate shipments of substantial quantities of grain likely to generate substantial revenues for terminal operators. In addition, the number of Non-Integrated Graincos participating in the grain industry and interested in entering into such agreements is small. Accordingly, there is substantial incentive for competitors to deviate from coordinated behaviour. Assuming that they have the capacity to satisfy the requirements of Non-Integrated Graincos, the revenues earned by terminal owners from such agreements are attractive as against the high fixed costs of operating such facilities.

108. The Respondents say, therefore, that the most likely impact of the Joint Venture on the "competitive dynamic" at the Port of Vancouver will be to increase the choice for Non-

Integrated Graincos by ensuring that the Joint Venture has the capacity and incentive to seek to enter into terminal handling agreements with them on competitive terms.

I. Alleged Anti-Competitive Effects

1. No Substantial Lessening of Competition in Port Terminal Grain Handling Services

109. In response to paragraphs 62 and 63 of the SGMF, the Respondents deny that the Joint Venture is likely to prevent or lessen competition substantially in the relevant market, as defined appropriately, or at all.

110. The Joint Venture will not be able to exercise market power in the provision of grain handling services at the Port of Vancouver, by unilaterally raising tariffs or lowering diversion premiums paid to Non-Integrated Graincos. The Joint Venture has no ability to unilaterally effect a material price increase for its services because grain shippers will shift their demand for the Joint Venture's services to alternate suppliers. For example, the Cascadia, Pacific and UGG terminals on the South Shore of the Port of Vancouver are under-utilized. If the Joint Venture attempted to unilaterally raise prices or lower diversion premiums, these three terminals could readily absorb demand for additional services from Non-Integrated Graincos or the CWB. In addition, Vancouver Wharves could provide additional services to grain shippers diverted from the Joint Venture. The CWB and Non-Integrated Graincos could redirect grain shipments to other ports, including Prince Rupert and Thunder Bay. As discussed elsewhere, grain could be shipped to overseas markets through alternate export corridors and by alternate means.

2. No Anti-Competitive Impact on Primary Grain Elevator Markets

111. At paragraphs 64 and 65 of the SGMF, the Commissioner alleges that increased concentration of grain handling services in the Port of Vancouver will result in increased concentration in primary grain markets. As discussed above, the Commissioner's contention is founded upon an erroneous market definition, both as to the relevant product market and the

relevant geographic market. The Joint Venture does not result increased concentration of the market in respect of the discrete services of elevation, storage, drying, cleaning, blending, loading and unloading of grain, and grading of grain, because all of these services are offered at numerous other port terminals and most of them at primary grain elevators within the relevant geographic market.

112. Moreover, the Joint Venture will not make it more difficult for Non-Integrated Graincos to obtain terminal authorization in the Port of Vancouver, which as explained above is necessary for shippers to obtain railcar allocation from CN and CP. Rather, the Joint Venture will be able to grant such authorization more readily than would either SWP or JRI operating their facilities separately, because the Joint Venture will experience fewer circumstances when it is unable to accommodate additional throughput. All things being equal, terminal operators have a significant incentive to accommodate requests for services from Non-Integrated Graincos, in order to maximize the owners' return on fixed assets. The Joint Venture operator will have an incentive to operate at or near full capacity, while avoiding unacceptable levels of risk of railcar and vessel demurrage, contract extension penalties, and contract cancellations resulting from undue delays due to unmanageable grain shipments. A compelling reason for SWP and JRI to enter into the Joint Venture was the possibility that they would be able to meet their own increasing needs for grain handling services from their terminals, while also satisfying demand for terminal services from third parties.

113. If Non-Integrated Graincos have more secure access to port terminal services, as efficient co-management of the SWP and JRI terminals will ensure, there will be no upward pressure on their per-unit costs as alleged by the Commissioner and they will be able to compete vigorously for grain purchases from farmers in primary grain elevator markets.

114. The Joint Venture involves SWP's and JRI's terminal elevators in the Port of Vancouver only. SWP plans to continue to compete vigorously for deliveries to its primary elevator system from farmers in Western Canada. Grain producers have many choices for the sale of their grain, and SWP has no ability to sustain a unilateral increase in tariffs charged by its primary grain

elevators. Furthermore, SWP will have to continue to offer competitive incentives to farmers to induce them to deliver to its facilities, failing which they will elect to obtain services and purchase crop inputs from other grain companies. As the incentives offered to farmers are not transparent, coordinated behaviour among all grain companies offering primary elevator services would be impossible

115. SWP and JRI also actively compete for purchases of Non-Board Grain from other grain companies and will continue to do so under the Joint Venture. The competition arises from the actively traded track market in Vancouver (particularly in canola), where grain companies purchase grain for their own account and are responsible themselves for all subsequent port terminal charges. This market is often used to fill vessels and improve logistical performance. This track market reflects a true open market for grains arriving or planned to arrive at port. When grain supply is short in the port, track bids increase relative to FOB offers. When grain is in surplus at the port, track bids are discounted as compared to FOB offers.

116. The Respondents submit that the impact on primary grain elevator markets alleged by the Commissioner is purely speculative and based upon numerous unsound assumptions.

J. Countervailing Power

117. The Respondents submit that the CWB, which has a statutory monopoly over the sale of wheat and barley for domestic human consumption and for export, has a countervailing ability to constrain an attempted exercise of market power by the Joint Venture. The CWB is able to exercise countervailing power in several ways. First, at times the Board has unilaterally decided to pay to all grain companies the lowest tariff posted by one company for a particular service, rather than the tariffs actually filed with the CGC by each of them for their services. The CWB has also unilaterally determined the charge it will pay for additional services not included in grain companies' posted schedules of tariffs.

118. The CWB can also direct grain to other ports in response to a rise in tariffs at the Port of Vancouver. Rail transportation costs to Vancouver and Prince Rupert are identical from many points in Western Canada. Thus, the CWB can direct shipments to Prince Rupert without incurring additional costs. Alternatively, the CWB could also direct shipments to other Ports. Other grain shippers, such as large Non-Integrated Graincos, may also exercise countervailing power by directing shipments of Non-Board Grains to other ports.

PART VIII. EFFICIENCIES

119. In the alternative, the Respondents say that the Joint Venture has brought about and is likely to bring about substantial gains in efficiency. Although SWP does not admit that the Joint Venture will result in the prevention or lessening of competition, SWP says that the gains in efficiency from the Joint Venture will offset any such alleged anticompetitive effects. Further, SWP says that the gains in efficiency would not likely be attained if the order solicited by the Commissioner is made.

A. Savings resulting from specialization of the SWP and JRI facilities

120. In general SWP's facility will handle Board Grains (wheat and barley) and JRI's facility will handle Non-Board Grains, such as canola and peas, although this specialization of throughput will not be exclusive or rigid. The Joint Venture will use flexible specialization to ensure that it is capturing both the gains from specializing production at each terminal and the benefits of having the logistical flexibility to put any given program or shipment through either terminal and efficiently manage the respective cost and revenues at both terminals.

121. For instance, since SWP's terminal has greater storage capacity and a greater number of bins it will be better suited to handle Board Grains, which involve a greater number of segregations of grain. JRI's terminal will focus on canola and other Non-Board Grains where segregation is not as significant a factor. This will also tend to specialize the grain cleaning function, which will take advantage of the JRI terminal's ability to clean canola at a comparatively greater rate and will increase recapture of good canola often lost with screenings removed during cleaning.

B. Reduced penalties such as rail and vessel demurrage

122. By consolidating grain stocks and improving coordination of shipments, railcar unloading, grain storage and cleaning, and vessel loading, the Joint Venture will encounter fewer incidents in which it is unable to unload railcars or load vessels in a timely manner, in contrast to SWP and JRI operating these facilities independently. More efficient throughput will result in fewer lost opportunities to earn incentives for rapid unloading and fewer circumstances where the Joint Venture is penalized with the imposition of demurrage charges.

C. Increased opportunities for blending grains

123. The Joint Venture will enhance opportunities for blending grains of different grades and qualities in order to obtain a blended product that obtains the highest possible grade overall. The Joint Venture will specialize the two terminals, by typically storing together larger quantities of grains of one variety but having different grades or other characteristics. As a result, the Joint Venture will have a greater opportunity to blend grain stocks to result in more precise blending to match specifications required by grain purchasers. The Joint Venture will be able to achieve these results because each facility will have larger quantities of particular varieties of grain, more available storage bin space and the ability to store segregations for longer periods without limiting throughput, and increased economies of scale in blending.

D. More effective reclaiming of grain from screenings

124. Savings will result from more efficient reclaiming of good quality grain from screenings. Due to economies of scale and specialization, the Joint Venture will be able to recover grain by reclaiming grain otherwise lost during processing. The cleaning process in each terminal can be better fine-tuned to the grains each terminal will specialize in cleaning. When grain is cleaned, the material removed during the screening process includes, for example, whole grain of other classes than the grain being cleaned. Specialization of reclaim systems will allow much more of this grain to be recovered than was possible prior to the Joint Venture.

E. More accurate blending of canola to precise export requirements

125. Port terminal operators earn a credit from canola exporters by ensuring that canola shipments match closely a dockage allowance of 2.0%. Canola credits are a dockage allowance granted on export shipments under an agreement with exporters to ship canola at 2.0% dockage rather than the 2.5% allowed by the CGC standards. Specializing the terminals permits the Joint Venture to concentrate canola stocks in one facility, thereby providing more opportunity for blending canola stocks to the precise requirements of this program and for reclaiming good canola lost during the cleaning process. SWP and JRI have been increasingly unable to fully capture the benefit of this program, because of increased canola cleaning activity at primary elevator terminals and reduced canola dockage levels in general due to improved herbicide tolerance in varieties.

F. Reduced Berthing Costs.

126. Consolidation of grain stocks in the terminals will result in larger quantities being available in one terminal and reduce the necessity of vessel movements between the two terminals. Berthing is the activity of bringing the vessel from the channel into the port area, bringing it alongside the berth of the terminal and tying (securing) the vessel to the berth for safe loading. Every separate berth requires down time for the vessel because it is time that the vessel is neither loading, unloading nor traveling to a destination market. As compensation for this lost time vessel owners charge an additional half-day of vessel time against any additional berths.

G. Reduced labour, maintenance and overhead costs

127. Through specialization of the terminals, the Joint Venture will be better able to match its existing volumes and labour requirements to shift labour available at the two terminals. The Joint Venture will also have larger consolidated shippable quantities to load per shift, which should improve the productivity of labor. In addition, the Joint Venture has been able to eliminate some duplication of management personnel.

128. Specialization of the terminals improves the logistics of grain handling, thereby reducing the circumstances when grain must be repeatedly handled. This will decrease wear and tear on equipment in the facilities, and reduce the facilities power requirements. In addition, specializing the processing will also result in longer production runs with shorter startup and shut down periods, thereby minimizing conditions that put stress on equipment and electric motors.

H. Conclusion Regarding Efficiencies

129. While the foregoing list of efficiencies is not intended to be exhaustive, the Respondents submit that the efficiency gains resulting from the Joint Venture are substantial and will be greater than and offset any alleged anticompetitive effects resulting from the Joint Venture.

PART IX. RELIEF SOUGHT

130. The Respondents therefore request that the Commissioner's application be dismissed, with costs in accordance with section 8.1 of the *Competition Tribunal Act*, R.S.C. 1985, c. 19 (2nd Supp.). For all of the reasons outlined above, the Joint Venture is not likely to bring about a substantial lessening or prevention of competition. In addition, the Joint Venture will produce significant efficiency gains which would outweigh any anticompetitive effects alleged by the Commissioner.

131. The Respondents further submit that the remedy sought by the Commissioner, an Order to dissolve the Joint Venture, would not be appropriate under any circumstance. Alternative mechanisms exist within the regulatory regime governing the grain industry to provide a remedy to parties that claim to be aggrieved as a result of the harm alleged by the Commissioner, a rise in charges for terminal services and difficulty among Non-Integrated Graincos to obtain terminal authorization. Effective remedies exist under the *Canada Grain Act* by which aggrieved parties can seek redress for any of these problems, should they arise. Accordingly, the extreme step of dissolving the Joint Venture would be a disproportionate response to the speculative concerns of

the Commissioner, since there are other means available to constrain the Joint Venture's behaviour.

PART X. PROCEDURAL MATTERS

132. In response to paragraph 67 of the SGMF, the Respondents oppose the hearing of this matter in Ottawa, Ontario. This application concerns port terminals located in Vancouver, British Columbia. SWP is headquartered in Regina, Saskatchewan, and its operations are concentrated in Western Canada. JRI, the Co-Respondent, has its headquarters in Winnipeg, Manitoba. The facts and matters in issue in the application have no immediate connection to Ottawa, Ontario. Given the location of the terminals directly affected by the remedy sought by the Commissioner, SWP requests that the hearing take place in Vancouver, British Columbia.

133. The Respondents submit that the hearing in this matter should be conducted in English.

DATED the 3rd day of February, 2006.

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THE COMPETITION TRIBUNAL

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

IN THE MATTER OF an application by the Commissioner of Competition for an Order Pursuant to section 92 of the *Competition Act*;

AND IN THE MATTER OF joint venture between Saskatchewan Wheat Pool Inc. and James Richardson International Limited in respect of port terminal grain handling in the Port Vancouver.

BETWEEN:

**THE COMMISSIONER OF
COMPETITION**

Applicant

- AND -

**SASKATCHEWAN WHEAT POOL
INC., JAMES RICHARDSON
INTERNATIONAL LIMITED,
6362681 CANADA LTD. AND
6362699 CANADA LTD.**

Respondents

**RESPONSE OF SASKATCHEWAN
WHEAT POOL INC., 6362681 CANADA
LTD. AND 6362699 CANADA LTD.**

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