Competition Tribunal Tribunal de la Concurrence

CT - 98 / 02 – doc # 9

IN THE MATTER of the *Competition Act*, R.S.C. 1985, c. C-34,
and the *Competition Tribunal Rules*, SOR/94-290, as amended;

AND IN THE MATTER of an inquiry pursuant to subsection 10(1)(b) of the
Competition Act relating to the proposed acquisition of ICG Propane Inc.
by Superior Propane Inc.;

AND IN THE MATTER of an application by the Director of Investigation and
Research for an interim order pursuant to section 100 of the *Competition Act*.

B E T W E E N:

The Director of Investigation and Research

Applicant

- and -

Superior Propane Inc.
Petro-Canada Inc.
The Chancellor Holdings Corporation
ICG Propane Inc.

Respondents

REASONS FOR ORDER REGARDING APPLICATION FOR INTERIM ORDER UNDER SECTION 100 OF THE *COMPETITION ACT*

Date of Hearing:

December 4-6, 1998

Presiding Member:

The Honourable Mr. Justice Marshall Rothstein

Counsel for the Applicant:

The Director of Investigation and Research

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The Chancellor Holdings Corporation
ICG Propane Inc.

Randal T. Hughes

COMPETITION TRIBUNAL

REASONS FOR ORDER REGARDING APPLICATION FOR INTERIM ORDER UNDER SECTION 100 OF THE *COMPETITION ACT*

The Director of Investigation and Research

v.

Superior Propane Inc. et al.

[1] This is an application by the Director of Investigation and Research (the "Director") pursuant to section 100 of the Competition Act[1] (the "Act") for an interim order in respect of a proposed merger, enjoining the respondents from completing the acquisition by Superior Propane Inc. ("Superior") of all of the issued and outstanding shares of ICG Propane Inc. ("ICG") from The Chancellor Holdings Corporation ("CHC"), a wholly-owned subsidiary of Petro-Canada Inc. ("Petro-Canada"). Practically, the Director seeks to prohibit the closing of the transaction between the respondents scheduled for December 7, 1998. This application was filed on December 1, 1998. The hearing took place on December 4 and 5, 1998 and the decision must be issued prior to December 7th. The matter is obviously urgent and that is why I am giving you these reasons this evening, December 6, 1998.

SECTION 100 LEGAL ANALYSIS

[2] The Tribunal has not previously dealt with an application under section 100 and it is therefore necessary to address its interpretation. Section 100 provides:

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[1] R.C.S. 1985, c. C-34.

100. (1) Where, on application by the Director, the Tribunal finds, in respect of a proposed merger in respect of which an application has not been made under section 92 or previously under this section, that

(*a*) the proposed merger is reasonably likely to prevent or lessen competition substantially and, in the opinion of the Tribunal, in the absence of an interim order a party to the proposed merger or any other person is likely to take an action that would substantially impair the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 92 because that action would be difficult to reverse, or
(*b*) there has been a failure to comply with section 114 in respect of the proposed merger,

the Tribunal may issue an interim order forbidding any person named in the application from doing any act or thing that it appears to the Tribunal may constitute or be directed toward the completion or implementation of the proposed merger.

(2) Subject to subsection (3), at least forty-eight hours notice of an application for an interim order under subsection (1) shall be given by or on behalf of the Director to each person against whom the order is sought.

(3) Where the Tribunal is satisfied, in respect of an application made under subsection (1), that

(*a*) subsection (2) cannot reasonably be complied with, or
(*b*) the urgency of the situation is such that service of notice in accordance with subsection (2) would not be in the public interest,

it may proceed with the application *ex parte*.

(4) An interim order issued under subsection (1)

(*a*) shall be on such terms as the Tribunal considers necessary and sufficient to meet the circumstances of the case; and
(*b*) subject to subsection (5), shall have effect for such period of time as is specified therein.

(5) An interim order issued under subsection (1) in respect of a proposed merger shall cease to have effect

(*a*) in the case of an interim order issued on *ex parte* application, not later than ten days, or
(*b*) in any other case, not later than twenty-one days,

after the interim order comes into effect or, in the circumstances referred to in paragraph (1)(*b*), after section 114 is complied with.

(6) Where an interim order is issued under paragraph (1)(*a*), the Director shall proceed as expeditiously as possible to commence and complete proceedings under section 92 in respect of the proposed merger.

[3] In order to properly interpret subsection 100(1), reference must also be made to sections 92 and 104. Under section 92, the Director may file an application for dissolution, divestiture or other relief in a case of a merger or proposed merger. If the Tribunal finds that the merger or proposed merger will prevent or lessen, or is likely to[2] prevent or lessen, competition substantially, it may grant the relief provided in section 92. Under section 104, after an application has been filed under section 92, the Tribunal may, upon application by the Director, issue such interim order as it considers appropriate. Sections 92 and 104 provide:

> **92.** (1) Where, on application by the Director, the Tribunal finds that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially
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> (*a*) in a trade, industry or profession,
> (*b*) among the sources from which a trade, industry or profession obtains a product,
> (*c*) among the outlets through which a trade, industry or profession disposes of a product, or
> (*d*) otherwise than as described in paragraphs (*a*) to (*c*),
>
> the Tribunal may, subject to sections 94 to 96,
>
> (*e*) in the case of a completed merger, order any party to the merger or any other person
> (i) to dissolve the merger in such manner as the Tribunal directs,
> (ii) to dispose of assets or shares designated by the Tribunal in such manner as the Tribunal directs, or
> (iii) in addition to or in lieu of the action referred to in subparagraph (i) or (ii), with the consent of the person against whom the order is directed and the Director, to take any other action, or
> (*f*) in the case of a proposed merger, make an order directed against any party to the proposed merger or any other person
> (i) ordering the person against whom the order is directed not to proceed with the merger,
> (ii) ordering the person against whom the order is directed not to proceed with a part of the merger, or
> (iii) in addition to or in lieu of the order referred to in subparagraph (ii), either or both
>
> (A) prohibiting the person against whom the order is directed, should the merger or part thereof be completed, from doing any act or thing the prohibition of which the Tribunal determines to be necessary to

[2] As contrasted with the words "is reasonably likely to" in para. 100(1)(*a*).

> ensure that the merger or part thereof does not prevent or lessen competition substantially, or
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> (B) with the consent of the person against whom the order is directed and the Director, ordering the person to take any other action.
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> (2) For the purpose of this section, the Tribunal shall not find that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially solely on the basis of evidence of concentration or market share.

> **104.** (1) Where an application has been made for an order under this Part, other than an interim order under section 100, the Tribunal, on application by the Director, may issue such interim order as it considers appropriate, having regard to the principles ordinarily considered by superior courts when granting interlocutory or injunctive relief.
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> (2) An interim order issued under subsection (1) shall be on such terms, and shall have effect for such period of time, as the Tribunal considers necessary and sufficient to meet the circumstances of the case.
>
> (3) Where an interim order issued under subsection (1) is in effect, the Director shall proceed as expeditiously as possible to complete proceedings under this Part arising out of the conduct in respect of which the order was issued.

[4] Section 100 is invoked by the Director prior to making an application under section 92. In the case of an order made on notice under section 100, i.e., not *ex parte*, the maximum duration of the order is 21 days after it comes into effect.[3] It is during this period of time that the Director, if relief is to continue without interruption, must commence proceedings under section 92 and then, make an application under section 104 for further interim relief until the hearing and determination of the application.

[3] The maximum duration could be longer in circumstances referred to in para. 114(1)(*b*), but that is not relevant in this case.

[5] Under section 104, in considering whether to grant interim relief, the Tribunal is required to have regard to principles ordinarily considered by superior courts when granting interlocutory or injunctive relief. In summary, that means that the Tribunal must consider whether the Director has made out a serious issue, that irreparable harm would ensue if the interim relief was not granted and that the balance of inconvenience favors the Director.[4]

[6] In section 100, no reference is made to principles ordinarily applicable to the granting of interlocutory or injunctive relief. Rather, a more specific code is set forth. The Tribunal must first find that the proposed merger is reasonably likely to prevent or lessen competition substantially. It must then form the opinion that in the absence of an interim order, an action will be taken that would substantially impair the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 92 because that action would be difficult to reverse. Provided these two conditions are met, the Tribunal may issue an interim order forbidding any act or thing that may constitute or be directed toward the completion or implementation of the proposed merger.

Reasonably Likely

[7] It is apparent that to find that the proposed merger is reasonably likely to prevent or lessen competition substantially requires the Tribunal to embark upon a consideration, at least to some extent, of the merits of the Director's position. It is insufficient for the Tribunal to simply be satisfied that there is a serious issue or that the matter is not frivolous or vexatious as in the case of ordinary interlocutory or injunctive relief and therefore, as would be the case under

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[4] *RJR-MacDonald Inc. v. A.G. Canada,* [1994] 1 S.C.R. 311.

section 104. On the other hand, the Tribunal is not making a final determination and need only find that the proposed merger is reasonably likely to prevent or lessen competition substantially. Therefore, the standard of proof to be met by the Director is less than applicable after a full hearing of an application under section 92, but higher than that required under section 104.

[8] It is not entirely clear why a higher standard than that applicable in injunction proceedings, i.e., serious issue, is mandated by Parliament under section 100. The interim order that may be granted is for a maximum of 21 days. One would think that such a limited interim order would justify a low threshold. Further applications under section 100 are brought on relatively short notice, or even *ex parte*. The Tribunal will likely have little time to consider the matter.

[9] Exceptionally, injunction principles do import a higher standard than serious issue when a determination on an interlocutory motion would amount to a final determination of the action.[5] In such cases, a more extensive review of the merits must be undertaken. However, it is not apparent why applications under section 100, as contrasted with applications under section 104, would be seen by Parliament as bringing an end to a transaction which the Director opposed or otherwise as finally disposing of the matter.[6]

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[5] *Ibid.* at 338.

[6] In this case it is argued that Petro-Canada may exercise an option to terminate its transaction with Superior if a prohibition on closing applies on or before December 15, 1998. I am not satisfied that this option is sufficient to have the Tribunal assume that the transaction will definitely be cancelled if a prohibition order is made. Therefore even in the circumstances of this case, I am not satisfied that granting the Director's application would bring an end to the transaction or otherwise finally dispose of it.

[10] Having said this, the Tribunal must still adhere to the requirements of section 100. The words require the Tribunal to make a finding that the proposed merger is reasonably likely to prevent or lessen competition substantially.

Substantially Impair

[11] The second requirement of paragraph 100(1)(*a*) is that the Tribunal must form the opinion that:

> . . . in the absence of an interim order a party to the proposed merger or any other person is likely to take an action that would substantially impair the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 92 because that action would be difficult to reverse. . .

[12] The Director argues that these words mean that the Tribunal must forbid the closing scheduled for December 7, 1998. He says that if the Tribunal concludes that the closing would be difficult to reverse, the Tribunal must grant the interim order sought.

[13] The respondents say that this is too narrow a view of the words in paragraph 100(1)(*a*). The argument is, that under section 92, the Tribunal has a number of alternative remedies including divestiture of assets or ordering that a part of a merger not be proceeded with, as well as dissolution. They say that as long as the Tribunal is satisfied it retains the ability to remedy the effect of a proposed merger on competition under section 92, it may consider alternatives to the interim order sought by the Director. In this case, the respondents have put forward a form of hold-separate order which they say is sufficient to preserve the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 92.

[14] I agree with the respondents that what is relevant is whether the Tribunal's ability to remedy the effect of the proposed merger on competition is substantially impaired. However, I do not think the Tribunal, at this stage of proceedings, should foreclose any of the remedies under section 92.

[15] What the Tribunal may order under subsection 100(1) is narrowly defined. It is:

> . . . an interim order forbidding any person named in the application from doing any act or thing that it appears to the Tribunal may constitute or be directed toward the completion or implementation of the proposed merger.

[16] The focus is on forbidding any act or thing that may constitute or be directed toward the completion or implementation of the proposed merger. In this case, the closing on December 7, 1998 is certainly such an act or thing. While a hold-separate order might be a preferred course of action for the respondents, I do not think it is open to the Tribunal to make such an order on this application. To do so would be to make an order that allows an act or thing that is directed toward completion or implementation of the proposed merger, but subject to conditions. Given the nature of the interim order, i.e., for a maximum of 21 days, and the fact that no section 92 application has been filed and no relief yet claimed by the Director, I do not read section 100 to contemplate the type of hold-separate order put forward by the respondents. The intent of Parliament is to preserve the pre-merger status quo and all the remedies provided under section 92, not to allow the merger subject to conditions.

[17] The respondents refer to paragraph 100(4)(*a)* which provides that:

> An interim order issued under subsection (1):
>
> (*a*) shall be on such terms as the Tribunal considers necessary and sufficient to meet the circumstances of the case;

[18] I agree that this provision provides some discretion to the Tribunal to impose terms with respect to the order sought by the Director. However, I think that the words of paragraph 100(4)(*a*) must be read in the context of the nature of the order described in subsection 100(1). The order must still be an order forbidding an act or thing that is directed toward the completion or implementation of a proposed merger. Paragraph 100(4)(*a*) is not an open invitation to the Tribunal to make whatever order it considers appropriate in the circumstances. In this respect, the words of subsection 100(1) are to be contrasted with the words of subsection 104(1) where the Tribunal "may issue such interim order as it considers appropriate." If that would have been Parliament's intention in section 100, it could have easily used these words. It did not do so and it is not open to the Tribunal to deviate from the words Parliament used.

Tribunal's Discretion Under Section 100

[19] Finally, there is a question of what additional considerations the Tribunal may take into account beyond those set forth in paragraph 100(1)(*a*). Subsection 100(1) is worded in a form of a code whereby, if certain conditions are met, the order sought may be granted. The Director argues that once the conditions are met, the Tribunal should grant the order sought. While the jurisdiction being exercised by the Tribunal is statutory, it is an extraordinary type of jurisdiction in that it grants the Director a form of relief, not only before trial, but before his pleadings have been filed. The word "may" in subsection 100(1) indicates that the decision to be made is

discretionary. In other words, even if the Tribunal is satisfied that the conditions under paragraph 100(1)(*a)* are met by the Director, the Tribunal may still reject the application. I do not think Parliament intended to deprive the Tribunal of discretion in considering whether or not to make an order under section 100. However, as the Director points out, he is presumed to act in the public interest. To the extent the exercise of the Tribunal's discretion is a weighing of public interest consideration versus those of the respondents, the onus of proof on the Director is minimal and significant weight would have to be given to public interest considerations.[7]

IS THE PROPOSED MERGER REASONABLY LIKELY TO PREVENT OR LESSEN COMPETITION SUBSTANTIALLY

[20] While, as previously said, the standard of proof on the Director is less than under section 92, what is required is more than that there is a serious issue to be tried or that the case is not frivolous or vexatious. The word "reasonably" implies that the question be considered objectively. This means that there must be evidence that will, on a balance of probabilities, support the necessary finding.

[21] The analysis the Tribunal must perform under section 100, I think, should be guided by the considerations set forth in subsection 92(2) and section 93 of the Act, i.e., concentration or market share, barriers to entry, etc. Under subsection 92(2), while significant concentration or market share is a necessary factor, this consideration cannot be the sole basis for a finding that a proposed merger is likely to prevent or lessen competition substantially. Under section 100, generally I think some evidence of significant concentration or market share must also be present

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[7] *Supra*, note 4 at 346.

to support a finding that a proposed merger is reasonably likely to prevent or lessen competition substantially. However, section 100 is silent on whether evidence of concentration or market share alone is sufficient to support such a finding. While I think this is probably the case given the lower standard of proof, for purposes of this application, I need not decide the question. Both the Director and the respondents have referred to other factors and I take account of all of the evidence in making the finding required under section 100.

Market Definition and Concentration

[22] However, I start with a consideration of concentration and market share. In order to make any determination about concentration and market share, the market must be defined in terms of product and geography. Market definition is a first step in determining whether a proposed merger is reasonably likely to prevent or lessen competition substantially. Depending upon the definition of the market, the merged entity could have either a large or small market share. A large market share, say in excess of 35 percent,[8] is an indication that the proposed merger is reasonably likely to prevent or lessen competition substantially. A small market share is an indication of the opposite.

[23] The Director's view on this issue is contained in paragraphs 17 and 18 of the affidavit of John Pecman, Senior Commerce Officer with the Competition Bureau:

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[8] Consumer and Corporate Affairs Canada, Director of Investigation and Research, *Merger Enforcement Guidelines*, Information Bulletin No. 5 (Supply and Services Canada, March 1991).

> The relevant product market is the supply and delivery of bulk propane; the supply and delivery of propane equipment (or accessories); and service and maintenance of propane equipment (or accessories) to retail and wholesale customers. Product markets may be further broken down into the following categories: residential, commercial, industrial, agricultural, automotive, wholesale, and national and major accounts. National accounts are those national buyers who require delivery of propane across large geographic areas. There appear to be administrative economies to large, multi-location customers in contracting with one supplier for the supply of propane.
>
> The relevant geographic markets are considered to be local markets centred around branches/satellites, with the exception of national accounts where the relevant geographic market includes the supply and delivery of propane and auxiliary products to retail and wholesale customers throughout Canada or in several provinces.

Although the Director uses the term "relevant product market," he refers initially to three product markets, bulk propane, propane equipment and service and maintenance of propane equipment. He then refers to "product markets" being further broken down into categories, e.g, residential, commercial, automotive. It is therefore not entirely clear as to the precise definition of the product market advanced by the Director.

[24] The Director's market share evidence appears to be based on propane sales' volume. Therefore, for purposes of market definition on this application, the relevant product market asserted by the Director is assumed to be the supply and delivery of propane ("propane"). On the basis of this definition of the product market, the Director has introduced substantial evidence of high market shares by a merged Superior and ICG. In his analysis of 80 markets out of approximately 110 to 120, the Director's data show that the combined Superior and ICG would have a market share of over 90 percent in 17 markets. In 58 markets out of the 80 considered, the combined Superior and ICG would have a market share in excess of 35 percent. The Director's evidence also demonstrates that the combined entity would be dominant in the national market.

Overall, the Director's evidence is that the merged operation would have a Canadian market share of over 70 percent. The respondents' evidence does not materially challenge these figures.

[25] If the product market is indeed propane, the market shares shown are impressive and this consideration would weigh heavily in favor of the Director on this application.

[26] However, the Tribunal cannot merely assume that the Director's market definition is the correct one. This must be established in the evidence at least to the standard of proof required by section 100.

[27] In *R. v. J.W. Mills and Sons Ltd*., Gibson J. stated:

> Defining the relevant market in a particular case, therefore, requires a balanced consideration of a number of characteristics or dimensions to meet the analytical needs of the specific matter under consideration.[9]

This dictum was cited with approval in *Director of Investigation and Research v. Southam Inc.*[10] The observations of Iacobucci J. in *Southam* are also relevant to the Tribunal's function in respect of market definition:

> However, as I have already noted, the weighing of criteria in a balancing test must be largely a matter of discretion. The very purpose of a multi-factored test, such as the one that the Tribunal used to determine the dimensions of the relevant product market, is to permit triers of fact to do justice in diverse particular cases.
> As a general matter, in cases like this one, the aims and objectives of the statute may not be served by assigning principal or overriding importance to any one factor.[11]

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9 [1968] 2 Ex. C.R. 275 at 305.

10 [1997] 1 S.C.R. 748 at 784.

Substitutability

[28] The fundamental test for determining the boundaries of the relevant market is substitutability. Products must be close substitutes in order to be placed in the same product market. The question is whether there are close substitutes for propane in the relevant geographic markets. In the present case, functional interchangeability, views of customers, comments of the merging parties, pricing practices, switching costs, and other factors have all been considered in determining whether propane is in a market by itself or whether it is part of a larger energy market.

[29] The respondents' evidence is that propane accounts for approximately two percent of Canada's total energy market. The Director does not take issue with this figure.

[30] The evidence of Mark Schweitzer, Executive Vice-President and Chief Financial Officer of Superior, at paragraph 29 of his affidavit is:

> Propane accounts for approximately 2% of Canada's total energy requirements; this share is dropping as a result of competition from other sources of energy, including natural gas, fuel oil, electricity and wood in the traditional industry segments, and with gasoline, diesel and other alternative fuels in the automotive industry segment.

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[11] *Ibid.* at 781.

[31] Mr. Schweitzer says that propane demand in the automotive segment has increased sharply since 1980 but that it is now decreasing by about 10-15 percent per year. In the traditional industry segments, demand has decreased by approximately 30 percent since 1980.

[32] Mr. Schweitzer gives an explanation as to how and when other energy sources would be substituted for propane. In the case of natural gas, he says at paragraphs 32 and 34 of his affidavit:

> Whenever natural gas becomes available, demand for propane for heating and many other end-uses disappears due to the substantial price advantage natural gas has over propane. This transition is facilitated by the fact that propane appliances and furnaces can be adapted for natural gas use with a few, very minor, adjustments.
>
> In rural areas, natural gas becomes available as soon as a sufficient number of potential customers is identified to justify installing pipeline connections. A single industrial customer in a remote location is enough to drive such expansion into previously uncharted locales. In the event that the price differential between propane and natural gas were to increase, the natural gas grid infrastructure would expand even more rapidly than it currently is, to capture an increasing number of isolated communities, farms and cottages. . . .

Mr. Schweitzer's evidence also deals with electricity, wood and fuel oil as substitutes.

[33] With respect to the automotive propane segment which accounts for 33 and 27 percent of Superior's and ICG's sales volume respectively, Mr. Schweitzer says that propane competes with fuels such as gasoline, diesel fuel, natural gas, electricity, methanol and ethanol. Since the mid 1990's, demand for automotive propane has been declining, at a rate of 10 percent to 15 percent per year.

[34] The evidence submitted by the Director respecting substitutability is mixed. While making some general references to alternate fuels not being close substitutes, details and other support for non substitutability is not provided. Indeed the evidence recognizes the switching from one fuel source to another:

> ... parties target users of alternate fuels as potential customers & some propane customers switch to other energy forms.
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> ... alternatives vary across applications (eg. natural gas frequently displaces propane for heating purposes).
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> ...
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> propane is differentiated from other form of energy - portable, clean burning & high energy traits. Product lines eg. food service & forklift, have few, if any alternatives due to these characteristics.
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> lost customer reports of parties show propane customers more likely to switch intra product, many face significant switching costs to alternate fuels.
>
> Bureau customer survey also supports conclusion that alternate fuels are not usually close substitutes for propane.[12]

[35] Of some significance is the fact that the Director has provided no evidence as to whether propane pricing is or is not observed to be disciplined by other fuel prices. One would expect that if the relevant market was limited to propane, that there would be some evidence that propane pricing was independent of the pricing of other fuel sources. There is no such evidence. On the contrary, there is evidence from the respondents that pricing practices are governed by alternative fuel cost comparisons.[13]

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[12] Superior Propane Proposed Acquisition of ICG Propane, Case Assessment Slide Deck for the Parties, November 30, 1998: Exhibit G to affidavit of J. Pecman (30 November 1998) at 15-16.

[13] See for example, Superior 1997 Annual Report: Exhibit E to affidavit of M. Schweitzer (3 December 1998) at 9, 13.

[36] Of some significance are statements in an ICG prospectus of April 22, 1998, issued prior to the proposed merger, when ICG was contemplating the issuance of trust units and statements in the Superior Propane Inc. Income Fund, 1997 Annual Report.[14] I will not quote verbatim from the prospectus or annual report. It is sufficient to say that the prospectus and annual report are consistent with Mr. Schweitzer's evidence before the Tribunal. They were issued for other purposes, to attract and satisfy unit holders and to meet other legal requirements, not to make a case before the Tribunal. Therefore, I place weight on the statements in these documents. If propane was not faced with serious competition from other energy sources, one would expect to see such a business advantage referred to in those documents. On the contrary, the prospectus and annual report make it clear that while propane has advantages such as cleanliness, portability and versatility, it competes against alternative energy sources on a cost basis. The documents note that propane is vulnerable to natural gas expansion and alternative fuels for automobiles. Reference is made to the agricultural and automotive markets as being "extremely competitive" and "highly competitive."[15]

[37] From their prospectus and annual report, the view of the respondents is that they are competing in a wide energy market. While obviously there is intra propane competition that is not, in the view of these participants in the industry, to the exclusion of effective competition from other energy sources.

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[14] Exhibits D and E to affidavit of M. Schweitzer (3 December 1998).

[15] Superior 1997 Annual Report at 8 and ICG Prospectus at 20: Exhibits D and E to affidavit of M. Schweitzer (3 December 1998)

[38] The Director submits that certain uses are essentially unique to propane. He refers to agricultural and other drying uses in areas where natural gas is not easily available, heating in remote confined areas such as construction sites, mines, oil wells and forestry operations, portable home use, and non polluting fleet automotive use. He also says that the market is stable or declining.

[39] On the basis of the record before me, I do not find the Director's general evidence of unique use persuasive. With respect to uses where natural gas is not easily available, Mr. Schweitzer's evidence is that "[i]n the event that the price differential between propane and natural gas were to increase, the natural gas grid infrastructure would expand even more rapidly than it currently is, to capture an increasing number of isolated communities, farms and cottages."[16] The ICG prospectus says that "competition is aggressive in this (agricultural) market as buyers are very sensitive to propane and other energy costs."[17] The Superior Annual Report says that the agricultural market is extremely competitive, particularly as natural gas availability expands into rural markets.[18] Automotive use of propane is declining. While Mr. Pecman asserts that non polluting fleet automotive use is unique to propane, I think the more persuasive evidence is that propane competes with other automotive fuels on the basis of fuel and engine maintenance costs to the users. While I do not in any way disparage the objective and use of non polluting fuels, and in this respect note the evidence that ethanol and methanol are used as fuel sources, I think, practicality suggests that automobile fleet operators are generally more concerned with costs of relative fuel sources.

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[16] Affidavit of M. Schweitzer (3 December 1998) at para. 34.

[17] ICG Prospectus: Exhibit D to affidavit of M. Schweitzer (3 December 1998) at 20.

[18] Superior Annual Report: Exhibit E to affidavit of M. Schweitzer (3 December 1998) at 8.

[40] With respect to the use of propane at construction sites, mines, oil wells and forestry operations, the Director's evidence provides no information. The Director's detailed market evidence is with respect to large and small communities throughout Canada. His geographic market definition does not refer to these locations specifically. There is virtually no evidence about these locations. On the basis of the record before me, I do not have sufficient information about these locations to accord them any significant weight in making a determination of market definition in this application under section 100.

[41] The Director obtained the views of customers of Superior and ICG. Approximately 7,500 surveys were sent to customers, 705 were returned. Two thirds of the respondents expressed a concern about the proposed merger. The concern was essentially with respect to price of propane after the merger.

[42] I think survey information can be valuable to ascertain the views of buyers. With respect to market definition, the question is whether buyers consider that they have close substitutes. It is trite to say that a survey must be carefully interpreted. It should meet statistical tests to ensure that the answers are reliable. The Director does not suggest that this survey meets any statistical criteria. Where a random sample is statistically valid, it will be presumed that the sample is indicative of the whole universe. I cannot make such presumption in the case of this survey. In other words, I cannot presume that the 10 percent who responded were indicative of the 90 percent who did not.

[43] As I have said, for purposes of product market definition, what is significant is whether customers feel they have close substitutes. From this survey, 90 per cent of persons or companies surveyed did not respond. How are the non responses to be interpreted? In the case of this survey, the non responses from 90 percent of customers may be indicating that the merger is not important to that population. In other words, it is not possible to presume that because two-thirds of those who did respond expressed concerns, that two-thirds of the entire population were concerned. It may be equally possible that the 90 percent who did not respond had no concern. I do not find they had no concern. All that I can say is that it is not possible to tell.

[44] Even if one were to take account of the survey, the results are ambiguous in respect of the question of substitutability. An expression of concern does not expressly answer the specific question of whether there are close substitutes. An expression of concern is so general that to suggest it means there are no close substitutes would be speculative. Indeed, in all but one category of users in the survey, there are expressions of both concern and no concern. In the case of forklifts, for which the Director says there are few, if any alternatives, 23 out of 42 who responded, or 55 percent, expressed no concern. For these reasons, I place little weight on the survey for purposes of ascertaining the product market.

[45] There is some evidence that switching costs may be a factor in users of propane being able to switch to other fuel sources. In a submission from the Department of Economic Development of the Yukon to the Director dated November 1998, costs of $2,500-$5,000 to switch from propane to oil in a residence were identified.[19] The submission goes on to say that

the conversion cost might be expected to be recovered in 5-10 years, presumably through lower cost of oil. In case of restaurants, conversion is said to be from propane to electricity which is more expensive.

[46] Mr. Schweitzer's affidavit indicates that in the non automotive segment of the propane industry, demand has gone down by 30 percent since 1980. In residential energy demand, propane use has declined while natural gas and electricity have increased. Automotive propane demand is also declining.

[47] While undoubtedly there is evidence of switching costs, switching is taking place as propane's share in different market segments varies. On the basis of this evidence, I cannot conclude that switching costs prevent substitutability of other energy sources so that propane is in a separate product market.

[48] The Director places some emphasis on one-, three- and five-year contracts that are entered into between Superior and ICG and their respective customers. The shorter-term contracts have tended to be with residential and agricultural customers while longer term contracts are with the automotive, commercial, industrial and other agricultural customers. The Director says that these contracts demonstrate that customers become locked-in to propane and cannot use other forms of energy.

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[19] Exhibit C to affidavit of J. Pecman (30 November 1998) at 4.

[49] On the basis of the record before me, I do not have sufficient information to tell what effect these contracts really have. If they were intended to offer favourable prices to customers in consideration for a long-term commitment to use propane, I do not think that is an indication propane is in a market by itself. On the contrary, the contracts may indicate that propane is highly competitive with other energy sources and the contracts are intended as a competitive tool to secure customers to propane. Perhaps the contracts are intended to secure a particular customer to one or other propane supplier. Again, the contract is an indicator of competition and while it precludes the customer from switching suppliers or energy sources, this is presumably done for a price consideration. One way or the other, on the evidence before me, I cannot conclude that the existence of contracts in this business is evidence that other energy sources are not close substitutes.

[50] Finally, there is evidence that the Director, in 1993, was of the view that there was competition as between propane and gasoline and natural gas. That observation, together with his conclusion that the industry had relatively low entry barriers caused him to conclude that a merger between Superior and Premier Propane Inc. would not likely result in a substantial lessening of competition. At this point, what is significant is that the Director himself recognized that there were substitute products for propane. The Director in these proceedings has not indicated what has changed since 1993.

[51] For all these reasons, I am not satisfied that the relevant product market is as defined by the Director. On the basis of substitutability with other energy sources, propane appears to have a market share of approximately two percent in the energy market. Even in the Yukon, propane's

share is only five to six percent of energy supply. I therefore must conclude that a high market share within the propane industry itself does not imply that the proposed merger is reasonably likely to prevent or lessen competition substantially.

BARRIERS TO ENTRY

[52] While I do not think it is necessary to go further in view of this finding, for completeness, I will make a few further observations with respect to barriers to entry. Mr. Pecman says the industry is declining and time is needed for an entrant to install storage capacity and to acquire a reputation. Further he says that contracts would restrain customers from switching from existing suppliers. New entrants would face economies of scale from a combined Superior/ICG. He says these considerations, in combination, make effective entry unlikely.

[53] Mr. Schweitzer says that there are few requirements to enter the industry. He says that all that is necessary is access to a propane supplier, delivery vehicles, storage facilities and a small workforce. He says there are 105 propane retailers across Canada including multi-regional marketers, regional competitors and small low-cost competitors. He says there is a continuous pattern of new entry evidenced by 29 new marketers who entered during the last two to four years.

[54] With respect to contracts, the respondents have said they are prepared, voluntarily, to not enforce five-year terms in existing customer contracts so that customers do not face a legal impediment to switch suppliers, that they will waive contractual terms calling for liquidated damages, that they will waive contractual rights to match lower prices quoted by competitors and

will waive contractual terms restricting the right of previous customers and contractors to enter into the propane business. Even if one assumes that the existence of these contracts is an indication of market power, whatever market power they provide will be eliminated, according to the evidence.

[55] Again, I note that in 1993 with respect to the Superior/Premier Propane Inc. merger, the Director was of the view that entry barriers were relatively low in this industry.

[56] Given evidence of entry into the industry over the past four years, the Director's own position on the matter in 1993 and the elimination of restrictive contractual provisions, significant entry barriers are far from obvious. Of course, capital is required and a reputation must be built up. But I do not regard these as reasons to believe there is no potential competition from new entrants as well, of course, as competition from existing participants in the market.

CONCLUSION

[57] I have considered the balance of the evidence. However, it is not necessary to go into detail. The Director has the obligation to satisfy the Tribunal that the proposed merger is reasonably likely to prevent or lessen competition substantially. On the basis of the record before me he has not done so.

[58] I reiterate that the decision is based on the record before me. I have applied the lower standard of reasonably likely. On the basis of the evidence and applying this standard of proof, I find that a required condition for an order under section 100 is not satisfied by the Director. The application must be dismissed.

DATED at Ottawa, this 6th day of December, 1998.

SIGNED on behalf of the Tribunal by the presiding judicial member.

(s) Marshall Rothstein
Marshall Rothstein