Exhibit I-59(b)
public

CT - 94/01

IN THE MATTER OF an application by the Director of Investigation and Research under section 79 of the *Competition Act*, R.S.C. 1985, c. C-34;

AND IN THE MATTER OF certain practices by A.C. Nielsen Company of Canada Limited

B E T W E E N:

THE DIRECTOR OF INVESTIGATION AND RESEARCH

Applicant

- and -

THE D&B COMPANIES OF CANADA LTD.

Respondent

- and -

INFORMATION RESOURCES, INC.

Intervenor

AFFIDAVIT

I, ANDREW M. ROSENFIELD, of the City of Lake Forest, Illinois, make oath and say as follows:

1. I am an economist and, together with Dr. John P. Gould, I was retained by counsel for Information Resources, Inc. ("IRI") to undertake an analysis of the economic and industrial organization aspects of certain issues raised in the Application filed by the Director of Investigation and Research in this proceeding. A true copy of the report prepared for counsel to IRI pursuant to the aforesaid request was attached as Exhibit "A" to my Affidavit sworn

September 20, 1994.

2. I have been provided with a copy of the Affidavits of Professor Frank Mathewson and of Margaret Guerin-Calvert, both sworn September 20, 1994, as well as the reports attached to such Affidavits. I understand that these Affidavits and the reports attached thereto were prepared at the request of the Respondent in connection with this proceeding. I am advised by counsel for IRI and verily believe that, prior to providing me with a copy of the reports attached to such Affidavits, such counsel had removed therefrom any information that had been identified by counsel for the Respondent as confidential to the Respondent.

3. Together with Dr. Gould, I was asked by counsel for IRI to prepare a response to such Affidavits. Attached as Exhibit "A" to my Affidavit is a true copy of the report prepared for counsel to IRI pursuant to the aforesaid request.

SWORN before me at the City)
of Chicago, in the State of)
Illinois this 4th day)
of October, 1994)

Andrew M. Rosenfield

Notary Public

"OFFICIAL SEAL"
RUTH ANN JOHNSON
Notary Public, State of Illinois
My Commission Expires Nov. 20, 1994

EXHIBIT "A"

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RESPONSE AFFIDAVIT OF JOHN P. GOULD AND ANDREW M. ROSENFIELD

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1. We have been asked by counsel for Information Resources, Inc. ("IRI") to provide a written response to the reports attached to the Affidavits of Professor Frank Mathewson and Margaret Guerin-Calvert, both of which were sworn September 20, 1994 and prepared for the Respondent, The D&B Companies of Canada Ltd. ("Nielsen"), in this proceeding.

2. Our report and opinions are based on our professional training and experience as economists and on information provided to us by IRI regarding the market structure and marketing practices in the U.S. and Canadian markets for market tracking services. We have also had access to publicly available materials on information services available from IRI, Nielsen and others. We have discussed industry practices in detail with IRI and with certain executives of consumer packaged goods companies that carry on business in both Canada and the United States that use scanner-based industry research. We also have had access to certain summaries of interviews conducted by Professor Donald N. Thompson, a Canadian economist also retained by counsel for IRI and we have had discussions with Professor Thompson as well. Finally, we have reviewed other documents of a general nature pertaining to this matter that were provided to us by counsel for IRI.

3. Nielsen's economists use various theoretical arguments that purport to show that Nielsen does not have market power in Canada, thus suggesting that Nielsen's practices in Canada cannot harm competition or consumers. In this response, we explain why each of their arguments is incorrect. Moreover, we believe that what is <u>not</u> in the Nielsen economists' affidavits is especially telling: First, they make no attempt to provide <u>any</u> procompetitive justification or explanation for Nielsen's exclusive contracts with retailers; Second, they make no attempt to explain why the market tracking service Nielsen currently offers in Canada is more expensive and of inferior quality than what IRI and Nielsen offer in the United States. Put simply, these affidavits attempt to use (in our view, erroneously) various theoretical arguments about market definition and market power to deflect the basic fact that Nielsen's practices have in fact prevented entry and injured consumers. In short, they provide no justification for the exclusive arrangements between Nielsen and the large grocery retail chains.

4. We begin by noting that we have in this case a kind of a controlled experiment of the type that is rather rare in economic analysis. This controlled comparison arises because we can compare the U.S. market for scanner-based market tracking services, where exclusives are absent and both IRI and Nielsen compete, with the market in Canada where exclusive contracts are in force making Nielsen the only supplier of any scanner-based service. As we have explained in greater detail in our earlier affidavit, there is an enormous difference in the quality and quantity of the scanner-based market tracking information available to customers in the United States as compared to Canada. Most, if not all, of the major users of scanner tracking information in the United States also sell their products in Canada so this large difference in the quality and quantity of the data is not due to a difference in the sophistication or needs of the client firms that are users of the service. Moreover, we understand from discussions and meetings with technical personnel at IRI that it would be possible to provide scanner-based market tracking information in Canada that is similar in quality and quantity to that provided in the United States if IRI had access to the Canadian scanner data that Nielsen controls through its exclusive contracts. Neither of the affidavits of the Nielsen economists addresses or even acknowledges this dramatic difference in the quality and quantity of scanner-based market tracking information between the United States and Canada. We believe this empirically observable difference shows that the argument that the exclusive contracts in Canada do not have anticompetitive effects is unsupported by actual experience and economic facts. We now turn to an analysis of and response to the theoretical arguments found in the affidavits of the Nielsen economists.

5. The Nielsen economists present essentially three arguments why Nielsen does not have market power: (1) they argue that the relevant product market in this case is broader than scanner-based market tracking services and that Nielsen therefore does not have signifi-

cant market power because it is only one competitor among others and that firms including perhaps IRI could enter by using panel, store-audit, or warehouse-withdrawal-based data sources; (2) they argue that major purchasers of market tracking services are large consumer goods firms and, therefore, have sufficient power in their own right to prevent the exercise of market power; and (3) they argue that IRI had the opportunity to sign exclusive contracts with retailers in 1986 and attempted to do so.

6. With regard to market definition, we believe that Nielsen's economists have not adequately taken into account an important consideration in the economics of market definition -- namely, the so-called "cellophane fallacy." This problem is so named because it arose in the Supreme Court's opinion in United States v. E.I. duPont de Nemours & Co. 351 U.S. 377 (1956) ("the Cellophane Case"), and the economic mistake made there is now part of the historiography of law and economics. In the Cellophane Case, the defendant, DuPont, was accused of monopolizing the cellophane market. DuPont defended in part by arguing that the market was much broader than cellophane. In particular, it argued that all products to which consumers were turning as substitutes for cellophane (all "flexible packaging materials") should be included within the market. Using the language of economics, DuPont argued that all products that were "cross-elastic" with cellophane at its current selling price should be included within the market. The Supreme Court was confused on this point and, at a time when the economics of antitrust was still in its infancy, expanded the market to include some of the other products to which consumers were turning as substitutes for cellophane.

7. Economists were quick to point out the obvious error. A monopolist of any product always raises the price of that product until substitution to other products occurs. Thus, at the monopoly price, some other products (however remote they may seem from the monopolized

product) must be substitutes. If the monopolist failed to raise price to a level at which some other products are substitutes, it obviously could make more money simply by raising price further because it then would receive greater revenue and would have to forego very few sales since, by definition, consumers have no substitutes. For this reason, an elementary proposition in antitrust economics is that a monopolist sets price in the elastic region of the demand curve where consumers at the margin have good substitutes and where some have switched to other products -- only by doing so can a monopolist earn the full monopoly return. At this price, we expect to see other products that are cross-elastic with the monopolized product, but that does not contradict the fact that these products would not be substitutes at the competitive price.

8. That is why economists (and other commentators) insist that in a monopoly case the relevant market must be defined at the competitive price and not at the monopoly price. For example, Richard Posner and Frank Easterbrook (both of whom now are judges on the United States Court of Appeals for the Seventh Circuit) explain the cellophane fallacy in this way in their casebook:

> DuPont was the sole supplier of cellophane and the question was whether cellophane should be deemed the relevant product market or whether the market should be expanded to include products (other flexible packaging materials) that exhibited a high cross-elasticity of demand with cellophane at the existing price of cellophane. But to include products that were good substitutes for cellophane at the price at which cellophane was being sold by this sole producer begged the question whether the producer had a monopoly. If he had a monopoly and was charging the monopoly price, that would make attractive substitutes which at the competitive price would be considered grossly inferior.

Posner and Easterbrook, Antitrust 2d (1981) at 361-2 (emphasis in original).

9. Put simply, the question "what is the relevant market in this case?" must be answered by imagining that the market for scanner-based market tracking service were behaving

competitively (which it is not in Canada). We must examine what would happen if customers in Canada were being offered scanner-based market tracking services of the same quality and price as those available in the United States. Then the question is: Would a small but significant and non-transitory price increase (say, five percent) cause so much substitution away from scanner-based market tracking services to other products such as panel, store-audit, or warehouse-withdrawal-based services that an increase in price would itself be uneconomical? If so, the market is indeed broader than scanner-based market tracking service. If not, scanner-based services are a market. Or, to ask the question slightly differently: what other services would buyers of scanner-based market tracking service regard as substitutes with such services if its price were to rise only a little bit above the competitive level?

10. The fact that some producers of consumer goods today may substitute to panel, store-audit, or warehouse-withdrawal-based market tracking services in Canada has nothing to do with the correct definition of the relevant market. But for Nielsen's practices, there would be (at least) two firms offering scanner-based market tracking services in Canada, and the Canadian market would perform much like the market in the United States. We already have noted that in the United States the quality and quantity of scanner-based market tracking service is substantially better than in Canada and, more directly to the point, this service has all but driven out market tracking services based on other data sources. This fact proves that Nielsen's economists are wrong in concluding that Nielsen's practices have not affected competition and that Nielsen lacks power. Nielsen's position in the Canadian market and its exclusive access to retailer scanner data have worked directly to injure consumers.

11. Once the correct question is asked, the answer is obvious. If Canadian consumer packaged goods producers were offered scanner-based market tracking service like those

available in the United States at a price close to the price of such service in the United States, they would buy scanner-based market tracking service and would not regard panel, store-audit, or warehouse-withdrawal-based services as a substitute for market tracking services that are based on scanning data. Such producers might still use some non-scanner-based services as a complement to scanner-based market tracking service (as sometimes happens in the United States), but they would not regard non-scanner-based services as a substitute for scanner-based market tracking service. We know this because we can observe in the United States a competitive scanner-based market tracking industry and we do not believe anyone would contend that non-scanner-based market tracking services provide a constraint on the prices charged by Nielsen and IRI in the United States for scanner-based market tracking services. Indeed, that is why the U.S. Federal Trade Commission prohibited a merger between Nielsen and IRI in the late 1980's. If panel, store-audit, or warehouse-withdrawal-based services were competitive with scanner-based services or entry into the scanner-based market tracking industry were easy, a combination of the two firms providing scanner-based market tracking service would not have raised competitive concerns. Thus, the observation that some packaged goods producers in Canada made an effort to avoid Nielsen and instead use non-scanner-based services because they face a low quality, monopolistically priced market tracking service is both irrelevant and an example of the classic cellophane fallacy.

12. The affidavits of the Nielsen economists suggest, moreover, that competition in the provision of scanner-based market tracking service can be achieved simply by acquiring data in a secondary fashion, for example from the end user. As Professor Mathewson states: "Nothing prevents any end user from purchasing the data from one source and then using another consultant as a marketing advisor to the firm." The problem with such an argument is

that if the exclusive contracts permit Nielsen to price the data monopolistically, then nothing about competition in the market to analyze the data will be able to counteract that monopolistic power. The key anticompetitive issue then has to do with the acquisition of the actual scanner data not the subsequent analysis of these data. As we noted in our earlier affidavit, these raw scanner data coming from the retail stores are an essential facility and monopolistic control of those data is all that is needed to establish noncompetitive prices throughout the market.

13. To see the flaw in Professor Mathewson's argument, consider a simple example. Suppose that the market for personal computer operating systems were monopolized and that the market for personal computer word processing software were intensively competitive. It would be absurd to argue that competition in the market for word processors (which are used together with an operating system) would counteract monopoly power in the market for operating systems because word processing software is not a substitute for an operating system.

14. The Nielsen economists also seem to suggest that competition on a regional basis might be possible if one or two retailers could be persuaded not to use an exclusive contract. While it is possible that regional information is of use to some end users (say manufacturers and producers of locally or regionally distributed products), such limited data does not allow IRI or any other firm to be competitive in the broader market for national data. Thus, even entry on a regional basis (if feasible) would not be an effective economic response to the anticompetitive situation in the national market. It is important for potential competitors in the scanner-based market tracking business to have access to all the data for their services to be truly comparable and effectively competitive because major consumer goods companies want

national coverage. For example, we understand that all 25 of IRI's largest customers in the United States purchase IRI's national market tracking service as well as more disaggregate information such as "key account" service.

15. Professor Mathewson suggests that IRI could enter Canada by using a "toehold-entry strategy of building from a regional or key account to a national service." We do not believe that this strategy would be very effective in view of Nielsen's complete control of the market because Nielsen can use this dominance to block or hinder such efforts. However, even if IRI (or any other firm) could use such a strategy to somehow inch its way to the point where it could offer a national service eventually, which is doubtful, Nielsen would continue to be a monopolist for the entire transition period. At best, this path to competition in the scanner-based market tracking services market would be long, costly, tedious, and uncertain; however, the same goal can be more easily and directly realized simply by prohibiting Nielsen's exclusive contracts. As we have pointed out, Nielsen's economists have offered no procompetitive justification for Nielsen's exclusive contracts with retailers. Thus, the contracts are exclusionary and, consequently, anticompetitive.

16. Having asserted in one part of his affidavit that there are many ways to compete in providing market tracking services in Canada and that the "toehold" strategy would be viable for IRI, we find it curious that in section 2.4.2 of his affidavit, Professor Mathewson argues just the opposite point.

> 2.4.2 Confronted with the fact that IRI had initiated a bidding game based on exclusivity, it is reasonable to claim that Nielsen had little choice but to respond with [sic] exclusive contract proposal of its own. If Nielsen had responded with non-exclusive contractual bids, then one outcome unfavourable to Nielsen would be for IRI to have secured some exclusive retail customers and for Nielsen to have secured some customers on a non-exclusive basis. These retail customers then would have been in a position to also sell their data to IRI giving IRI the opportunity to secure a national

> sample, sufficiently reliable to market a national scanning-based market tracking service. Under this outcome, Nielsen could have secured some retail customers but found itself unrepresented in certain regions of the country. Furthermore, Nielsen would be in a weak position to strike a deal to secure IRI's exclusive data. To produce national data, Nielsen would have had to replace the missing data with data from other sources. If this were grossly inferior, Nielsen would have had to abandon its attempt to produce national marketing tracking data services. Of course, Nielsen could have developed a regional market tracking service.

In this statement, Professor Mathewson effectively acknowledges that the options left to a market tracking firm (either Nielsen or IRI) when it does not have access to a national sample of scanner data are not very good substitutes for such a sample (otherwise Nielsen would not care if IRI had exclusive contracts). Moreover, in this section of his affidavit, he himself shows why the "toehold" strategy he advocates elsewhere would not be effective against the exclusive contracts.

17. Turning next to the Nielsen economists' argument that consumers of market tracking services have sufficient bargaining power to prevent monopoly conduct by Nielsen, it is easy to see that this argument is incorrect as well. Nielsen's service is of lower quality and higher cost in Canada than it is in the United States, proving that Procter & Gamble, Campbell's, and others cannot create competition when competition has been prevented by Nielsen's exclusive licensing practices. Moreover, we understand that consumer packaged goods producers would welcome IRI's entry into Canada and are not satisfied with the status quo.

18. Finally, the Nielsen economists also appear to justify Nielsen's exclusionary staggered exclusive contracts by referencing the fact that in 1986 IRI sought to launch a scanner-based market tracking service using exclusive contracts. We believe this fact too has no relevance to the present issue. At that time, no one anywhere had launched a scanner-based market tracking service -- the first successful such service was offered in the United States beginning

In 1987. Second, scanners were not ubiquitous in grocery stores in Canada as they are now. Third, IRI faced a dominant established rival that was taking the position that scanner-based market tracking service was not reliable and inferior to audit-based service. Fourth, IRI was a small firm with meager resources and needed to assure itself that it would have some time period during which it could attempt to distinguish itself from Nielsen. In our view, these factors distinguish IRI's efforts in the middle 1980's from Nielsen's practices today. More importantly, however, if today IRI were the firm with staggered exclusive contracts giving it unique access to scanner-based data and it were IRI that dominated the Canadian scanner-based market tracking industry, it would then be our view that IRI injured competition by using exclusive contracts with grocery retailers to foreclose entry by rivals. Put simply, it is the control of exclusive access to the necessary scanner data which, in turn, results in dominance that creates the competitive problem here, not the identity of the firm that uses such practices. In our earlier affidavit, we described Nielsen's historical position only to explain why it used its then existing dominant position to prevent entry; but the essence of its abuse of dominant position resides in its current practice of using exclusive contracts to prevent entry by competition.

19. The Nielsen economists suggest that the exclusive contracts emerge not solely because of Nielsen's actions and policies in the Canadian market but partially because of the concentrated structure of the retail grocery industry in Canada. Even if true, we believe that this factor has no relevance to the economic issues raised in this proceeding. The real economic concern here is the use of the exclusive contract that precludes IRI or other firms from entering competitively. The incremental (or marginal) cost of having the retail scanner data made available to more than one market analysis firm (such as Nielsen or IRI) is zero or very low. Thus, prohibiting retailers and market analysis firms from having exclusive contracts

on the use of the scanner data unambiguously confers competitive benefits. The scanner data have aspects of a public good in the sense that their use by one market tracking service firm does not prevent their use by other firms. This is the basis for the more competitive market conditions we observe in the acquisition and use of these data in the U.S. market.

20. In conclusion, Nielsen's economists have not identified any benefit to consumers resulting from Nielsen's exclusive access to scanner data, but instead have advocated arguments about market definition and market power that are rebutted by the facts. Seen from another perspective, we believe it likely that Nielsen's exclusive contracts cost Nielsen more money than would non-exclusive access to the underlying scanner data. That expense makes sense for Nielsen only because it prevents entry by rivals -- most obviously IRI. The Nielsen economists point to no benefits for consumers from this expenditure. This, in itself, shows that Nielsen's practice is exclusionary. For all the reasons we explained in our earlier affidavit, we remain convinced that an end to exclusivity will provide direct and tangible benefits to Canadian consumers.