Competition Tribunal Tribunal de la Concurrence

**CT-1989 / 001 – Doc # 101a**

IN THE MA ITER OF an application by the Director of Investigation and Research under sections 92 and 105 of the *Competition Act*, R.S.C., 1985, c. C-34, as amended;

AND IN THE MATTER OF the proposed acquisition by Asea Brown Boveri Inc. of certain assets and property comprising the electrical transmission and distribution business of Westinghouse Canada Inc., including those of its wholly-owned subsidiary Transelectrix Technology Inc.

BETWEEN:

The Director of Investigation and Research

Applicant

and

Asea Brown Boveri Inc.
Westinghouse Canada Inc.
Transelectrix Technology Inc.

Respondents

**REASONS FOR CONSENT ORDER DATED JUNE 15, 1989**

**Date of Hearing:**

June 15, 1989

**Presiding Member:**

The Honourable Mr. Justice Barry L. Strayer

**Lay Members:**

Dr. Frank Roseman
Madame Marie-Helene Sarrazin

**Counsel for the Applicant:**

**Director of Investigation and Research**

William J. Miller
John S. Tyhurst

**Counsel for the Respondents:**

**(a) Asea Brown Boveri Inc.**

Michael L. Phelan
Timothy Kennish
Peter L. Glossop

**(b) Westinghouse Canada Inc.**

Transelectrix Canada Inc.
John W. Brown, Q.C.
Iain W.M. Hendry, Q.C.
John J. Quinn

**COMPETITION TRIBUNAL**

**REASONS FOR CONSENT ORDER DATED JUNE 15, 1989**

---

***The Director of Investigation and Research***

***V.***

***Asea Brown Boveri Inc. et al.***

## Introduction

On April 26, 1989, the Director filed a notice of application with the Tribunal under sections 92 and 105 of the *Competition Act*, R.S.C., 1985, c. C-34, as amended, naming as respondents Asea Brown Boveri Inc. (ABB Canada), Westinghouse Canada Inc. (WECAN), and Transelectrix Technology Inc. (TTl). The relief requested by the Director was restricted to the plea for an order, under section 105, in the form of the Draft Consent Order attached to the notice as Schedule A. A consent order in a slightly modified form was issued by the Tribunal on June 15, 1989 with an indication that reasons would be issued later. Following are those reasons.

## The Merger and Its Competitive Impact

The Director alleges that the respondents "have proposed to effect a Merger which prevents or lessens or is likely to prevent or lessen competition substantially in the market for Subject Power Transformers ... in Canada within the meaning of section 92 of the Competition Act."[1]

---

1 Paragraph 1 of the notice of application.

The facts related herein are for the most part drawn from the Director's notice of application and have not been contested by the respondents, although the respondents, of course, do not necessarily agree with the conclusions he has drawn therefrom. The merger in question is between ABB Canada and WE CAN. By agreement dated February 14, 1989, ABB Canada proposed to acquire the electrical transmission and distribution equipment manufacturing operations of WECAN. (That transaction was closed subsequent to the issuance of a consent order by this Tribunal on June 15, 1989.)

ABB Canada is the wholly-owned Canadian subsidiary of ABB Asea Brown Boveri Ltd, a Swiss and Swedish owned corporation which ranks as the world's largest electrical equipment manufacturing company. WECAN is a wholly-owned Canadian subsidiary of Westinghouse Electric Corporation, an American corporation which also figures among the world's leading producers of electric power equipment. TTl is a wholly-owned subsidiary of WECAN[2]. The acquisition of these assets of WECAN represents only a part of a much larger integration by ABB Asea Brown Boveri Ltd and Westinghouse Electric Corporation of their worldwide electrical transmission and distribution assets.

The Director is concerned about the possible anticompetitive effects of the merger only as it relates to the market for Subject Power Transformers (SPT) in Canada. Generally speaking, these are the larger power transformers, whether rated by power (MVA, mega or million volt-amperes) or by maximum voltage handling capacity (kv, kilovolts). These transformers are primarily used by the utility companies to convert low voltage electricity produced by a

[2]Since June 1988. Prior to that time Canadian General Electric Company Limited (CGE) owned 40 per cent of TTl pursuant to a 1986 acquisition by WECAN of CGE's power transformer assets and operations. See paragraph 13 of the notice of application.

generating unit to higher voltages that are more efficiently carried over transmission lines and to reduce the voltage at the other end in order to deliver electricity safely to the end users.[3] The rating of a transformer is determinative of its use; for any specific application a customer would normally be unable to substitute a transformer with different specifications.[4]

For purposes of the consent order the class of SPT is further broken down into two groups, each of which is subject to somewhat different remedies. These two groups are defined by reference to the type of transformer and to power and voltage ratings. The range of transformers falling into each group has undergone some refinement since the original draft consent order was filed with the notice of application, mainly in response to the public comment process which is described below. Suffice it to say here that the two groups of SPT may be referred to as the "large" transformers, which for convenience will be referred to as Group B in these reasons, and the "very large" transformers, which for convenience will be referred to as Group A in these reasons.

The assets WECAN which were acquired by ABB Canada include the two TTl facilities that are capable of manufacturing power transformers. These are the Beach Road, Hamilton and the Guelph facilities (the "Hamilton business" and the "Guelph business", respectively). The Guelph business manufactures SPT while the Hamilton business currently produces only smaller transformers. It is the Guelph manufacturing capacity that is of competitive concern.

---

3 Paragraph 17 of the notice of application.

4 *Ibid.*, paragraph 33.

Prior to the merger there were five producers of power transformers in Canada. In descending order of size as a manufacturer and supplier, these were WECAN/TTI, ABB Canada, Federal Pioneer Limited, Hammond Manufacturing Company Limited (Moloney Electric Corporation) and NEI Ferranti-Packard Transformers. Moloney and NEI do not manufacture any transformers within the range of SPT.

Post-merger there will be two manufacturers of Group B SPT, ABB Canada and Federal Pioneer, and only one manufacturer of Group A SPT, ABB Canada. The Director states that, post-merger, ABB Canada will have approximately 75 per cent of the total Canadian SPT market.[5]

The notice of application filed by the Director also lists several other factors which give rise to post-merger competitive concerns, in particular, the tariff and non-tariff barriers to entry into the Canadian market.

Historically, imports of SPT into Canada have not been extensive.[6] The most significant reason for this phenomenon cited by the Director is the high tariff barriers. The current Most-Favoured-Nation (MFN) rate on imports of transformers with a power handling capacity exceeding 10,000 kVA (or 10 MVA), which constitute an undifferentiated class in the existing tariff, is 15 per cent. The MFN tariff is extended to imports from other member nations of the General Agreement on Tariffs and Trade (GATT). The General Preferential Tariff (GPT), which

---

[5] *Ibid.*, paragraph 27.

[6] The notice of application states that imports have accounted for less than ten per cent of the total Canadian purchases of power transformers rated over 50 MY A during the period 1983 to 1987. See paragraph 30.

is further extended to GATT members who are recognized as less-developed countries, is currently 10 per cent. The tariff on imports from the United States, which would otherwise be subject to the MFN rate, was reduced to 13.5 per cent on January 1, 1989, in the first of ten equal annual reductions required by the Canada-United States Free Trade Agreement (FT A).[7]

Other non-tariff barriers which particularly affect offshore manufacturers are mentioned by the Director. These include a history of effective anti-dumping protection, domestic purchasing preference policies on the part of many Canadian provincial electric utilities, lack of benchmark sales and demonstrated service and quality history by certain offshore suppliers, shipping costs and exchange rate exposure.[8] New entry or expansion by existing domestic producers of smaller transformers into the SPT market, he further alleges, would also be subject to significant non-tariff barriers. There are substantial sunk costs and time lags associated with the necessary investment in highly specialized assets, technology and skilled labour to manufacture large transformers; it is necessary for even a domestic producer to become a "qualified supplier" approved by the major utilities.[9]

> In summary, the Director's position is:
> The Merger, should it proceed as proposed, would put the majority of the capacity for the manufacture of Subject Power Transformers in Canada under the control of a single company, operating in a market environment protected by tariffs and other factors. The Director states that the utility companies, who are the major purchasers of the Subject Power Transformers, will have limited ability to exercise effective countervailing power given the limited competitive alternatives available. Transformers represent a relatively small portion of the total cost of operating a transmission and distribution

7 See item 8504.23.00 of Schedule 1 to the *Customs Tariff*, R.S.C., 1985 (3d Supp.), c. 41, as am. *Canada-United States Free Trade Agreement Implementation Act*,S.C. 1988, c. 65, ss 87 and 106.

8 Paragraph 31 of the notice of application.

9 *Ibid.*, paragraph 34.

> system. However, transformers are a critical component in such systems and any increased costs may ultimately be passed on to consumers.[10]

## Evidence Submitted

In considering the consent order the Tribunal had before it the following evidence: the affidavit of Professor Frank Mathewson, of the Department of Economics of the University of Toronto and the Institute for Policy Analysis, filed by the Director on May 8, 1989; the affidavit of lain W.M. Hendry, Vice President and General Counsel of WECAN, filed by the respondents on May 8, 1989; and the affidavit of Brooke Townsend, partner in the firm of Woods Gordon, management consultants, filed by the respondents on June 12, 1989. Both the affidavits of Mr. Hendry and of Mr. Townsend appear on the public record in expurgated form. Confidential versions of those affidavits, which contain detailed financial, accounting and other commercially sensitive information, were available to the Tribunal in its deliberations. The evidence received by the Tribunal was solely in affidavit form; the Tribunal did not consider oral evidence to be necessary.

## The Consent Order

The consent order contains three types of remedies designed to alleviate the alleged anticompetitive effects of the merger as originally proposed. These remedies are (i) the hold separate, (ii) tariff remission or reduction, and (iii) divestiture. Although not mentioned in the order, an undertaking by WECAN to release CGE from a non-competition clause concerning the manufacture of SPT in Canada[11], an undertaking by WECAN and ABB Canada to reduce the

---

[10] *Ibid.,* paragraph 39.

[11] This clause was entered into pursuant to the original purchase by WECAN of the TTl assets from CGE.

non-competition period between them from seven to three years, and an undertaking by ABB Canada to forego bringing any antidumping proceedings for five years, were also filed with the Tribunal prior to the grant of the consent order.

*(i) Hold Separate*

The hold separate mechanism used in the order is an interim measure designed to preserve the status quo until either the more permanent remedies come into effect or it becomes apparent that they will not be achieved. The hold separate applies to the assets and operations of TTl acquired by ABB Canada pursuant to the merger and came into effect upon issuance of the order.

The order sets out in some detail how the hold separate is to be implemented, including the establishment of a separate, identifiable division of ABB Canada to administer those assets (the TTl Division) and the appointment of a manager to maintain that division as an independent and viable business[12].

> This arrangement is intended to ensure that the assets are preserved, maintained in a viable state and are kept competitively independent pending any divestiture. For example, the TTl Division will continue to place competitive tenders separate Jrom ABB Canada for the period of the hold separate[13].

*ii) Tariff Remission or Reduction*

There are two types of tariff remedies in the order, one for Group A SPT and one for Group B SPT.

---

12 Order, paragraphs 3-9.

13 Paragraph 15 of the Consent Order Impact Statement, filed by the Director on April 26, 1989.

With respect to Group A SPT, of which ABB Canada will be the sole Canadian manufacturer, the order requires that by January 1, 1990 the necessary regulatory approvals will have been obtained for a full duty remission on worldwide imports of such transformers for not less than five years, effective on that date[14].

Tariff remission, which merely suspends the duty for the specified time period, is a type of discretionary relief under the *Customs Tariff* and may be accomplished by Order in Council. 15 To this end, the respondents will petition the Department of Finance for the necessary changes.

If the respondents are not successful in obtaining the tariff remission on Group A SPT, then ABB Canada will be required to divest either the entire TTl Division or the Guelph business, at the option of the Director.

With respect to Group B SPT, of which ABB Canada and Federal Pioneer will be the only two domestic producers, the order requires that by January 1, 1990, the necessary regulatory approvals will have been obtained to reduce the tariff on imports from the United States at a rate faster than required by the FT A: to a maximum of 6 per cent effective January 1, 1990, 3 per cent effective January 1, 1991 and zero per cent effective January 1, 1992[16]. The respondents

---

[14] Subparagraph 10(a) of the consent order. Group A SPT are: ... transformers of base MV A as follows:
(i) auto-transformers greater than 300 MV A; (ii) other transformers greater than 275 MV A;
and/or a voltage classification of 765 kv class or greater

[15] *Customs Tariff, supra,* note 7, s. 101.

16 Subparagraph 10(b) of the consent order. Group B SPT are: ... transformers of base MV A as follows:
(i) auto-transformer greater than 100 MV A up to and including 300 MY A;
(ii) other transformer greater than 50 MY A up to and including 275 MY A;
and/or a voltage classification of 765 KY class or greater

are also required to obtain, by June 16, 1989, the agreement of Federal Pioneer to the proposed tariff reductions or a written indication from the appropriate authority that the reductions would be recommended to the Privy Council. In fact, the agreement of Federal Pioneer was filed with the Tribunal on June 14, 1989.

Article 401.5 of the Canada-United States FT A provides a mechanism for accelerated reduction of tariffs by agreement between the parties. If the respondents are successful in obtaining the tariff reductions m the time specified, then, assuming that they were also successful in obtaining the tariff remission, the hold separate will end by January 1, 1990, and ABB Canada will be permitted to integrate the TTl Division into its own operations.

If the respondents are not successful in obtaining the tariff reductions in respect of Group B SPT, ABB Canada must divest the Hamilton business in accordance with the procedure set out in the order. If divestiture of the Hamilton business is not accomplished within the time limits specified, ABB Canada will be required to divest either the Guelph business or the entire TTI Division, at the option of the Director.

*(iii) Divestiture*

The divestiture procedure is stipulated in the order[17]. Most significantly, the divestiture requirements are time limited. Once a requirement of divestiture comes into effect, ABB Canada will initially be given 120 days to divest itself of the business in question or the Division. If the assets are not sold within that time, the Tribunal, on application by the Director, may appoint a trustee nominated by the Director to carry out the sale of the assets. The trustee then has 60 days

[17] Paragraphs 15 to 29.

from his appointment to divest the assets. If he is unsuccessful, one of two things may occur, depending on the scope of the required divestiture. If the trustee were dealing only with the Hamilton business (following a failure to achieve tariff reduction on Group B SPT), then a subsequent failure of that limited divestiture would trigger a mandatory divestiture of either the entire Division or the Guelph business, at the Director's option. ABB Canada would then get a second chance at voluntary divestiture on the same conditions as before and the process would start over. If the trustee were already dealing with the Division or the Guelph business, he would have to report back to the Tribunal which would then have the option of extending his term or of itself causing the sale to take place.

**Public Comment Process**

Subsection 35(1) of the *Competition Tribunal Rules*[18] provides that, when a notice is published by the Registrar in the *Canada Gazette* and the newspapers consequent upon the filing of an application for a consent order,

> ... the notice shall also state ... the day on or before which any representations or comments on the application must be filed with the Registrar, which day shall not be earlier than 21 days after the date of publication of the notice in the *Canada Gazette.*

Subsection 35(2) ensures that copies of any such representations or comments are provided to the Director, the persons in respect of whom an order is sought and any intervenors. Subsection 35(3) states that any of those persons may file replies to such representations or comments within seven days.

---

18 SOR/87-373.

In this case, various comments were received by the Tribunal from the following: Ms. Toni Sutherland, NEI Ferranti-Packard Transformers, British Columbia Hydro and Power Authority and Hydro-Quebec. Replies to the comments submitted to the Tribunal pursuant to its rules were filed by the Director and the respondents.

The Tribunal welcomed these written representations. It was perhaps not surprising, given the nature of the subject matter, that there were no requests for participation in the hearing by would-be intervenors. It was, however, useful to the Tribunal in making its decision to have the benefit both of outside comment and of the Director's explanation of his response to that comment. The efforts of the parties to accommodate most of the relevant concerns of those making representations were also appreciated.

The Director was in communication with most of the commenters in the case at bar, as well as with Federal Pioneer Limited, and the proposed order was modified to meet many of the concerns expressed. The highly technical terminology in the order was brought into line with industry standard usage. The subclass of "auto-transformers" was specifically added to the definition of SPT. The limits of the ranges of Group A and Group B SPT were refined to better accord with actual and projected manufacturing capability of other producers. In response to comments of a major user of SPT, an additional parameter was added to the definition of each group by incorporating a rating based solely on voltage (kv) for a particular type of transformer. Throughout this process, the basic thrust of the order was nonetheless maintained: where only one domestic manufacturer remains post-merger, tariff remission is the preferred solution; where two remain, accelerated tariff reduction vis-à-vis the United States is required if divestiture is to be avoided.

**Role of the Tribunal in a Consent Order Proceeding**

The Tribunal has a somewhat limited role in the matter of consent orders. By virtue of the circumscribed nature of the proceedings and the limited evidence before it, the Tribunal must attach considerable weight to the fact that the parties, the companies directly affected and the Director, have judged these measures to be reasonable. It is also fully cognizant of the savings to be realized from the settlement of litigation and the service thereby to the public interest.

That is not to say that the parties' judgment will be determinative and the Tribunal a mere rubber stamp; the Tribunal has a mandate to ensure that the proposed order is within a range which may be reasonably expected to meet the objectives of the *Competition Act.* This will obviously include some consideration of the appropriateness of these measures to combat an alleged substantial lessening of competition, their enforceability and the efforts that were made by those proposing the solution to meet the legitimate concerns of both producers and consumers in the relevant market.

**The Merits of the Proposed Order**

The arguments made to and the evidence placed before the Tribunal satisfy us that the consent order will be enforceable and that the overall result will most probably be to prevent any substantial lessening of competition as a result of the merger.

The Director takes the position, and we accept that the scheme of tariff relief and, alternatively, divestiture contained in the order will operate to ensure that the merged entity will face competition in the SPT market either internationally or domestically. The Director argues:

> Remission of tariffs on power transformers ... will enable foreign manufacturers to lower significantly their selling prices in Canada, and thus act as an effective competitive disciplinary force on the pricing behaviour of ABB Canada.
>
> Many of the off-shore manufacturers of power transformers ... already have a presence in the Canadian market, selling other types of power transmission, distribution and generation equipment. ... It is expected that ... Canadian power utility companies will seek out and approve off-shore manufacturers of power transformers as qualified suppliers ... [19].

With respect to imports from the United States under the accelerated tariff reduction scheme, he further states:

> In addition to enabling McGraw- Edison, a United States manufacturer of the full range of Subject Power Transformers, to become an effective competitor in the Canadian Subject Power Transformers market, this remedy will enable a number of manufacturers of Subject Power Transformers of lower MY A ratings (up to approximately 100 MY A) to compete more effectively in the Canadian power transformer market. An important factor in this regard is that power transformer manufacturers in the United States of America are not necessarily disadvantaged vis-à-vis shipping costs in serving many parts of Canada.
>
> Because orders for power transformers are generally placed approximately 18 months in advance of delivery, the proposed tariff acceleration would place U.S. imports on an equal footing with domestic production from a tariff standpoint within approximately one year of the issuance of the proposed Consent Order if granted[20].

---

[19] Paragraphs 16 and 18 of the Consent Order Impact Statement.

20 *Ibid.*, paragraphs 22 and 23.

The expert evidence filed by the Director supports his position that the tariff relief, when combined with the antidumping undertaking of ABB Canada, will result in effective competition by foreign producers of SPT. In his affidavit, Professor Frank Mathewson predicts that:

> ... the changes specified in the settlement mean that we can expect an enhanced numbers [sic] of bids from foreign sources. Even if these bids are unsuccessful in the sense that contracts are awarded to the Canadian suppliers, their presence will serve the critical role of disciplining Canadian producers to submit efficient bids that reflect their production costs[21].

Although Professor Mathewson identifies the five-year limit on the remission (given the time lag between orders and delivery of these transformers and the sunk costs associated with entry into a new foreign market), and the "buy-local" policies of some provincial utilities, as potential limitations on the effectiveness of this solution, he concludes that these are not critical[22].

In the "best-case" scenario the respondents will be successful in their petition for both tariff remission and reduction. The Director submits that there is a "high probability" of this outcome given that ABB Canada, one of the consenting parties to the order, will be the only domestic producer of the transformers subject to full remission and that Federal Pioneer, the only other producer of transformers subject to tariff reduction, has already consented to the acceleration[23].

If, on the other hand, the tariff relief is not achieved or 1s only partially achieved, then at least some divestiture will occur. The Tribunal has before it considerable evidence on the potential viability of the Hamilton business as a stand-alone manufacturer of SPT. The order

---

21 Paragraph 18.
22 Paragraphs 19 to 24.
23 See page 71 of the transcript.

requires any purchaser of the Hamilton business to compete in the manufacture and sale of SPT[24].

The engineering evidence submitted by the parties indicates that the Hamilton business has the necessary physical plant and equipment to resume production of the larger transformers[25]. The evidence of the management consultants indicates that the Hamilton facility could become a viable, independent business. It is not clear, however, that it would necessarily thereby become a viable competitor in the SPT market. As the consultants' report states:

> Historically, the profit margins on large transformers have been larger than the small ones which gives the facility an economic incentive to produce the large units. However, much of the question as to whether the new operation [the divested Hamilton business] will continue to build D and E class transformers [or "large" and "very large" transformers] will depend on whether the major Canadian utilities support the new venture with sufficient business to provide themselves with another Canadian source of supply. Beyond this, little assurance can be given or enforced that requires the new owner to produce D and E transformers[26].

The Tribunal had some concerns as to the conclusions in this report. Had we been of the opinion that divestiture of the Hamilton business alone was a key element in the order, then we might well have wanted to pursue the entire issue further through oral evidence.

**Conclusion**

The Tribunal is satisfied that the measures proposed in the consent order are sufficiently

---

[24] Paragraph 15.

[25] Letter from J.L. Harbell to I.W.M. Hendry, dated April 24, 1989, concerning "Equipment and Facilities Review: Hamilton Beach Road Plant". Attached as Exhibit 3 to the affidavit of I.W.M. Hendry.

[26] Woods Gordon, "Business Assessment of the Transelectrix Technology Inc. Beach Road Power Transformer Facility Plan: Summary Report", June 1989, at 6. Attached to the affidavit of Brooke Townsend as Exhibit P-9.

well defined to be effective and to be enforceable, unlike the proposed order in *Director of Investigation and Research v. Palm Dairies Ltd*[27]. These are not vague objectives which may continue in perpetuity in some indefinite state of achievement. If the tariff solution is proven impossible then the alternative of divestiture provides a final, definitive solution to any competitive problems.

The Tribunal also notes that a serious effort was made to respond to the comments received through the public comment process and that this is reflected in the order as issued.

The Tribunal believes that the measures proposed are adequate to meet the objectives of the *Competition Act* and that they are well within the range of reasonableness. The Tribunal is not, however, making a finding that these are the best possible remedies to solve the problem. Such a finding would be outside of its role.

**DATED** at Ottawa, this 6th day of September, 1989.

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

(s) B.L. Strayer
B .L. Strayer

[27] (1986), 12 C.P.R. (3d) 540 (Competition Trib.).