**CT-2019-005**

**THE COMPETITION TRIBUNAL**

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

**AND IN THE MATTER OF** the acquisition by Parrish & Heimbecker, Limited of certain grain elevators and related assets from Louis Dreyfus Company Canada ULC;

**AND IN THE MATTER OF** an application by the Commissioner of Competition for one or more orders pursuant to section 92 of the *Competition Act*.

**BETWEEN:**

**THE COMMISSIONER OF COMPETITION**

**Applicant**

**– and –**

**PARRISH & HEIMBECKER, LIMITED**

**Respondent**

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# COMMISSIONER'S BOOK OF AUTHORITIES CHALLENGING THE ADMISSIBILITY OF CERTAIN PROPOSED EVIDENCE FROM JOHN HEIMBECKER

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# *Canada (Commissioner of Competition) v. Vancouver Airport Authority, [2018] C.C.T.D. No. 15*

Canada Competition Tribunal Decisions

Canada Competition Tribunal

Ottawa, Ontario

Panel: D. Gascon J., Chairperson

Heard: September 24, 2018.

Decision: September 28, 2018.

File No.: CT-2016-015

Registry Document No.: 351

**[2018] C.C.T.D. No. 15** | 2018 Comp. Trib. 15

IN THE MATTER OF an application by the Commissioner of Competition for one or more orders pursuant to section 79 of the Competition Act, RSC 1985, c C-34 as amended; AND IN THE MATTER OF a motion by Vancouver Airport Authority objecting to the admissibility of certain proposed evidence; Between The Commissioner of Competition (applicant), and Vancouver Airport Authority (respondent)

(26 paras.)

## Appearances

For the Applicant:

The Commissioner of Competition: Jonathan Hood, Katherine Rydel, Ryan Caron, Antonio Di Domenico.

For the Respondent:

Vancouver Airport Authority: Julie Rosenthal, Rebecca Olscher.

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**ORDER RELATING TO THE MOTION BY VANCOUVER**

**AIRPORT AUTHORITY OBJECTING TO**

**THE ADMISSIBILITY OF CERTAIN PROPOSED EVIDENCE**

**1 FURTHER TO** the application filed by the applicant, the Commissioner of Competition ("**Commissioner**"), against the respondent, Vancouver Airport Authority ("**VAA**"), pursuant to section 79 of the *Competition Act*, *RSC 1985, c C-34*, as amended ("**Application**");

**2 AND FURTHER TO** the witness statements of Ms. Barbara Stewart, former Senior Director of Procurement at Air Transat A.T. Inc. ("**Air Transat**"), and of Ms. Rhonda Bishop, Director for In-flight Services and Onboard Product of Jazz Aviation LP ("**Jazz**"), that were served by the Commissioner on VAA and filed with the Tribunal on July 4, 2018 ("**Witness Statements**");

**3 AND FURTHER TO** a motion filed by VAA on September 10, 2018, objecting to the admissibility, as proposed evidence in this Application, of certain portions of the Witness Statements on the basis that they constitute improper opinion evidence by lay witnesses and/or inadmissible hearsay ("**Disputed Evidence**"), and asking the Tribunal to immediately rule that the Disputed Evidence is inadmissible ("**Motion**");

**4 AND UPON** reviewing the Witness Statements and considering the materials and written submissions filed by both parties with respect to the Motion;

**5 AND UPON** hearing the oral submissions made by counsel for both parties at a hearing held on September 24, 2018;

**6 AND UPON** considering that, in its submissions, VAA alleges that:

A. In their respective Witness Statements, Ms. Stewart and Ms. Bishop testify as to what their respective companies would have saved and as to increased expenses incurred (or to be incurred in the future), but the Witness Statements contain no indication as to who performed the calculations to arrive at the Disputed Evidence, how the figures were calculated, which data was used, and?or who prepared the documents attached to support these figures;

B. Ms. Stewart and Ms. Bishop express opinions with respect to the Disputed Evidence but did not personally observe (and do not testify to) the facts upon which their respective opinions are purportedly based, and lay out insufficient evidentiary foundations to be able to testify on their conclusions;

C. The conclusions reached by Ms. Stewart and Ms. Bishop with respect to the Disputed Evidence are not within their personal knowledge and appear to be those of other unknown persons, based on facts observed and calculations performed by other unknown persons;

D. The Disputed Evidence should not be admitted into evidence and be excluded as it contains improper opinion evidence and inadmissible hearsay.

**7 AND UPON** considering the following elements with respect to the Witness Statements:

A. In her witness statement dated October 31, 2017, Ms. Stewart states that, in 2015, Air Transat completed a request-for-proposal process for in-flight catering ("**Air Transat 2015 RFP process**") and refers to savings allegedly realized, or to be realized in the future, at airports across Canada except for the Vancouver International Airport ("**YVR**"), as well as to increased expenses allegedly incurred, or to be incurred in the future, by Air Transat at YVR as a result of that process;

B. In her witness statement (including Exhibits 10 and 13) dated November 10, 2017, Ms. Bishop states that, in 2014, Jazz conducted a requestfor- proposal process for in-flight catering ("**Jazz 2014 RFP process**") and refers to savings allegedly realized, or to be realized in the future, at airports across Canada except for YVR, as well as to increased expenses allegedly incurred, or to be incurred in the future, by Jazz at YVR as a result of that process;

C. In their respective Witness Statements, Ms. Stewart and Ms. Bishop each state that they have "personal knowledge of the matters" discussed in the statements unless indicated otherwise, and provide background information on their specific experience, credentials and roles in their respective companies;

D. In her witness statement, Ms. Stewart indicates that she was responsible for all procurement activities regarding in-flight catering at Air Transat from 2014 to 2017, including the Air Transat 2015 RFP process. She also sets out some background information with respect to her role in the RFP process and to the alleged savings and increased expenses at Air Transat;

E. In her witness statement, Ms. Bishop indicates that she had day-to-day responsibility for the Jazz 2014 RFP process and provided strategic direction to the 2014 RFP process team. She also mentions that she conducted monthly reviews to maintain targets and costs in all areas and oversaw the budget and billings for all in-flight catering, and she provides some background information with respect to the alleged savings and increased expenses at Jazz;

**8 AND UPON** observing that, in its written submissions to the Tribunal, VAA frequently states that the paragraphs containing the Disputed Evidence "appear" not to be within the personal knowledge of Ms. Stewart and Ms. Bishop, and "appear" to be based on reports and calculations from other unknown persons;

**9 AND UPON** noting the statement made by counsel for VAA at the September 24, 2018 hearing to the effect that representations made by counsel for the Commissioner at the hearing have dealt with some of her objections to the admissibility of parts of Ms. Stewart's witness statement;

**10 AND UPON** considering that evidence from lay witnesses is generally admissible if a witness has personal knowledge of the observed facts and testifies to facts within his or her observation, experience and understanding of events, conduct or actions (*Graat v The Queen*, *[1982] 2 SCR 819* at page 835; *Toronto Real Estate Board v Commissioner of Competition*, *2017 FCA 236* at paras 79-81, leave to appeal to SCC refused, 37932 (23 August 2018); *Commissioner of Competition v Imperial Brush Co Ltd and Kel Kem Ltd (cob as Imperial Manufacturing Group)*, *2007 Comp Trib 22* at para 11);

**11 AND UPON** considering that, on this Motion, the question to be determined by the Tribunal is whether, at this preliminary stage, VAA has established on a balance of probabilities that the paragraphs containing the Disputed Evidence, as read in the context of the Witness Statements, constitute improper opinion evidence and/or inadmissible hearsay;

**12 AND UPON** considering that an assumption of lack of personal knowledge needs to be established in order to convince the Tribunal that proposed evidence should be ruled inadmissible at an early stage, and that only in clear cases would the Tribunal be ready to find proposed lay witness evidence inadmissible on a preliminary motion, prior to the witness being examined and cross-examined;

**13 AND UPON** finding that, at this stage, VAA has not persuaded the Tribunal that the facts as set out in the Witness Statements are not within the knowledge, understanding, observation or experience of Ms. Stewart and Ms. Bishop, or that Ms. Stewart and Ms. Bishop did not observe the facts contained in their respective Witness Statements with respect to the Disputed Evidence;

**14 AND WHEREAS** the Tribunal acknowledges that VAA was within its right to bring this issue of admissibility of proposed evidence to the Tribunal's attention at this early stage, as dates had been set aside in the Scheduling Order for this Application to deal with motions relating to the evidence;

**15 AND WHEREAS** the Tribunal however has the discretion, depending on the factual circumstances before it, to defer a ruling on admissibility of evidence until later, as long as fairness is respected;

**16 AND WHEREAS**, given the language used by Ms. Stewart and Ms. Bishop in their respective Witness Statements, the Tribunal considers that it will be best placed at the hearing to determine whether or not the Disputed Evidence constitutes improper lay opinion evidence and/or inadmissible hearsay, and to rule on its admissibility;

**17 AND WHEREAS** both Ms. Stewart and Ms. Bishop will be called to testify by the Commissioner, under oath before the Tribunal, where they will be subject to examination by counsel for the Commissioner, to cross-examination by counsel for VAA and to questioning by the panel;

**18 AND WHEREAS** the scope of personal knowledge of Mss. Stewart and Bishop with respect to the Disputed Evidence is a matter that will be clarified at the time of their testimonies before the Tribunal;

**19 AND WHEREAS** the testimonies of Mss. Stewart and Bishop will provide better factual context to assist the Tribunal in making a determination on the admissibility of the Disputed Evidence;

**20 AND WHEREAS** the Tribunal is therefore of the view that, in the circumstances of this case, the preferable approach is to wait for the hearing before making a ruling on the admissibility of the Disputed Evidence, to allow the Disputed Evidence to be subject to cross-examination, and to then determine its admissibility if needed (*Boroumand v Canada*, *2016 FCA 313* at para 6; *Nadeau Poultry Farm Ltd v Groupe Westco Inc*, *2009 Comp Trib 6* at paras 80-81, aff'd *2011 FCA 188*, leave to appeal to SCC refused, 34401 (22 December 2011));

**21 AND WHEREAS** VAA has not established that it would suffer prejudice if the Disputed Evidence is not ruled inadmissible at this time and, since VAA will have the ability to test the Disputed Evidence on cross-examination, the Tribunal is satisfied that no issue of procedural fairness arises if the Tribunal rules on the admissibility of the Disputed Evidence at a later stage;

**22 AND WHEREAS**, in exercising its discretion to defer ruling on the admissibility of the Disputed Evidence at this stage, the Tribunal still retains the ability to reject such evidence as inadmissible at the hearing, after the testimonies of each of Ms. Stewart and Ms. Bishop, or at the time of its decision on the merits;

**23 AND WHEREAS**, for the above reasons and in light of the particular circumstances of this case, a conclusion on the admissibility of the Disputed Evidence would be premature;

**24 AND WHEREAS** the written submissions and the oral submissions presented at the hearing of the Motion fail to satisfy the Tribunal that, at this stage, VAA's Motion should be granted;

**THE TRIBUNAL ORDERS THAT**:

**25** VAA's Motion is dismissed, without prejudice to bring a motion at the hearing of the Application, further to the testimonies of each of Ms. Stewart and Ms. Bishop, with respect to the admissibility of the Disputed Evidence, or parts of it;

**26** The decision as to costs is reserved until the Tribunal generally addresses the issue of costs.

DATED at Ottawa, this 28th day of September 2018

SIGNED on behalf of the Tribunal by the Chairperson

(s) Denis Gascon

# White Burgess Langille Inman v. Abbott and Haliburton Co., [2015] 2 S.C.R. 182

Supreme Court Reports

Supreme Court of Canada

Present: McLachlin C.J. and Abella, Rothstein, Cromwell, Moldaver, Wagner and Gascon JJ.

Heard: October 7, 2014;

Judgment: April 30, 2015.

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**[2015] 2 S.C.R. 182** | *[2015] 2 R.C.S. 182* | *[2015] S.C.J. No. 23* | *[2015] A.C.S. no 23* | *2015 SCC 23* File No.: 35492.

White Burgess Langille Inman, carrying on business as WBLI Chartered Accountants and R. Brian Burgess, Appellants; v. Abbott and Haliburton Company Limited, A.W. Allen & Son Limited, Berwick Building Supplies Limited, Bishop's Falls Building Supplies Limited, Arthur Boudreau & Fils Ltée, Brennan Contractors & Supplies Ltd., F. J. Brideau & Fils Limitée, Cabot Building Supplies Company (1988) Limited, Robert Churchill Building Supplies Limited, CDL Holdings Limited, formerly Chester Dawe Limited, Fraser Supplies (1980) Ltd., R. D. Gillis Building Supplies Limited, Yvon Godin Ltd., Truro Wood Industries Limited/Home Care Properties Limited, Hann's Hardware and Sporting Goods Limited, Harbour Breton Building Supplies Limited, Hillier's Trades Limited, Hubcraft Building Supplies Limited, Lumbermart Limited, Maple Leaf Farm Supplies Limited, S.W. Mifflin Ltd., Nauss Brothers Limited, O'Leary Farmers' Co-operative Ass'n. Ltd., Pellerin Building Supplies Inc., Pleasant Supplies Incorporated, J. I. Pritchett & Sons Limited, Centre Multi-Décor de Richibucto Ltée., U. J. Robichaud & Sons Woodworkers Limited, Quincaillerie Saint-Louis Ltée, R & J Swinamer's Supplies Limited, 508686 N.B. INC. operating as T.N.T. Insulation and Building Supplies, Taylor Lumber and Building Supplies Limited, Two by Four Lumber Sales Ltd., Walbourne Enterprises Ltd., Western Bay Hardware Limited, White's Construction Limited, D. J. Williams and Sons Limited and Woodland Building Supplies Limited, Respondents, and Attorney General of Canada and Criminal Lawyers' Association (Ontario), Interveners.

(63 paras.)

**Appeal From:**

ON APPEAL FROM THE COURT OF APPEAL FOR NOVA SCOTIA

## Case Summary

**Catchwords:**

**Evidence — Admissibility — Expert evidence — Basic standards for admissibility — Qualified expert — Independence and impartiality — Nature of expert's duty to court — How expert's duty relates to admissibility of expert's evidence — Forensic accountant providing opinion on whether former auditors were negligent in performance of duties — Former auditors applying to strike out expert's affidavit on grounds she was not impartial expert witness — Whether elements of expert's duty to court go to admissibility of evidence rather than simply to its weight — If so, whether there is a threshold admissibility requirement in relation to independence and impartiality.**

**Summary:**

The shareholders started a professional negligence action against the former auditors of their company after they had retained a different accounting firm, the Kentville office of GT, to perform various accounting tasks and which in their view revealed problems with the former auditors' work. The auditors brought a motion for summary judgment seeking to have the shareholders' action dismissed. In response, the shareholders retained M, a forensic accounting partner at the Halifax office of GT, to review all the relevant materials and to prepare a report of her findings. Her affidavit set out her findings, including her opinion that the auditors had not complied with their professional obligations to the shareholders. The auditors applied to strike out M's affidavit on the grounds that she was not an impartial expert witness.

The motions judge essentially agreed with the auditors and struck out M's affidavit in its entirety. The majority of the Court of Appeal concluded that the motions judge erred in excluding M's affidavit and allowed the appeal.

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*Held*: The appeal should be dismissed.

The inquiry for determining the admissibility of expert opinion evidence is divided into two steps. At the first step, the proponent of the evidence must establish the threshold requirements of admissibility. These are the four factors set out in *R. v. Mohan*, *[1994] 2 S.C.R. 9* (relevance, necessity, absence of an exclusionary rule and a properly qualified expert). Evidence that does not meet these threshold requirements should be excluded. At the second discretionary gatekeeping step, the trial judge must decide whether expert evidence that meets the preconditions to admissibility is sufficiently beneficial to the trial process to warrant its admission despite the potential harm to the trial process that may flow from the admission of the expert evidence.

Expert witnesses have a duty to the court to give fair, objective and non-partisan opinion evidence. They must be aware of this duty and able and willing to carry it out. The expert's opinion must be impartial in the sense that it reflects an objective assessment of the questions at hand. It must be independent in the sense that it is the product of the expert's independent judgment, uninfluenced by who has retained him or her or the outcome of the litigation. It must be unbiased in the sense that it does not unfairly favour one party's position over another. The acid test is whether the expert's opinion would not change regardless of which party retained him or her. These concepts, of course, must be applied to the realities of adversary litigation.

Concerns related to the expert's duty to the court and his or her willingness and capacity to comply with it are best addressed initially in the "qualified expert" element of the *Mohan* framework. A proposed expert witness who is unable or unwilling to fulfill his or her duty to the court is not properly qualified to perform the role of an expert. If the expert witness does not meet this threshold admissibility requirement, his or her evidence should not be admitted. Once this threshold is met, however, remaining concerns about an expert witness's compliance with his or her duty should be considered as part of the overall cost-benefit analysis which the judge conducts to carry out his or her gatekeeping role.

Imposing this additional threshold requirement is not intended to and should not result in trials becoming longer or more complex. The trial judge must determine, having regard to both the particular circumstances of the proposed expert and the substance of the proposed evidence, whether the expert is able and willing to carry out his or her primary duty to the court. Absent challenge, the [page185] expert's attestation or testimony recognizing and accepting the duty will generally be sufficient to establish that this threshold is met. However, if a party opposing admissibility shows that there is a realistic concern that the expert is unable and/or unwilling to comply with his or her duty, the proponent of the evidence has the burden of establishing its admissibility. Exclusion at the threshold stage of the analysis should occur only in very clear cases in which the proposed expert is unable or unwilling to provide the court with fair, objective and non-partisan evidence. Anything less than clear unwillingness or inability to do so should not lead to exclusion, but be taken into account in the overall weighing of costs and benefits of receiving the evidence.

The concept of apparent bias is not relevant to the question of whether or not an expert witness will be unable or unwilling to fulfill its primary duty to the court. When looking at an expert's interest or relationship with a party, the question is not whether a reasonable observer would think that the expert is not independent. The question is

whether the relationship or interest results in the expert being unable or unwilling to carry out his or her primary duty to the court to provide fair, non-partisan and objective assistance.

In this case, there was no basis disclosed in the record to find that M's evidence should be excluded because she was not able and willing to provide the court with fair, objective and non-partisan evidence. The majority of the Court of Appeal was correct in concluding that the motions judge committed a palpable and overriding error in determining that M was in a conflict of interest that prevented her from giving impartial and objective evidence.

## Cases Cited

**Applied:** *R. v. Mohan*, [1994] 2 S.C.R. 9; *Mouvement laique québécois v. Saguenay (City)*, 2015 SCC 16, [2015] 2 S.C.R. 3; **adopted:** *R. v. Abbey*, 2009 ONCA 624, 97 O.R. (3d) 330, leave to appeal refused, [2010] 2 S.C.R. v; **referred to:** *Lord Abinger v. Ashton* (1873), L.R. 17 Eq. 358; *R. v. D.D.*, 2000 SCC 43, [2000] 2 S.C.R. 275; *Graat v. The Queen*, [1982] 2 S.C.R. 819; *R. v. Abbey*, [1982] 2 S.C.R. 24; *R. v. J.-L.J.*, 2000 SCC 51, [2000] 2 S.C.R. 600; *R. v. Sekhon*, 2014 SCC 15, [2014] 1 S.C.R. 272; *Masterpiece Inc. v. Alavida Lifestyles Inc.*, 2011 SCC 27, [2011] 2 S.C.R. 387; *R. v. Trochym*, 2007 SCC 6, [2007] 1 S.C.R. 239; *R. v. Boswell*, 2011 ONCA 283, 85 C.R. (6th) 290; *R. v. C. (M.)*, 2014 ONCA 611, 13 C.R. (7th) 396; [page186] *National Justice Compania Naviera S.A. v. Prudential Assurance Co.*, [1993] 2 Lloyd's Rep. 68, rev'd [1995] 1 Lloyd's Rep. 455; *Fellowes, McNeil v. Kansa General International Insurance Co.* (1998), 40 O.R. (3d) 456; *Royal Trust Corp. of Canada v. Fisherman* (2000), 49 O.R. (3d) 187; *R. v. Docherty*, 2010 ONSC 3628; *Ocean v. Economical Mutual Insurance Co.*, 2010 NSSC 315, 293 N.S.R. (2d) 394; *Handley v. Punnett*, 2003 BCSC 294; *Bank of Montreal v. Citak*, [2001] O.J. No. 1096 (QL); *Dean Construction Co. v. M.J. Dixon Construction Ltd.*, 2011 ONSC 4629, 5 C.L.R. (4th) 240; *Hutchingame v. Johnstone*, 2006 BCSC 271; *Alfano v. Piersanti*, 2012 ONCA 297, 291 O.A.C. 62; *Kirby Lowbed Services Ltd. v. Bank of Nova Scotia*, 2003 BCSC 617; *Gould v. Western Coal Corp.*, 2012 ONSC 5184, 7 B.L.R. (5th) 19; *United City Properties Ltd. v. Tong*, 2010 BCSC 111; *R. v. INCO Ltd.* (2006), 80 O.R. (3d) 594; *R. v. Klassen*, 2003 MBQB 253, 179 Man. R. (2d) 115; *Gallant v. Brake-Patten*, 2012 NLCA 23, 321 Nfld. & P.E.I.R. 77; *R. v. Violette*, 2008 BCSC 920; *Armchair Passenger Transport Ltd. v. Helical Bar Plc*, [2003] EWHC 367; *R. (Factortame Ltd.) v. Secretary of State for Transport*, [2002] EWCA Civ 932, [2003] Q.B. 381; *Gallaher International Ltd. v. Tlais Enterprises Ltd.*, [2007] EWHC 464; *Meat Corp. of Namibia Ltd. v. Dawn Meats (U.K.) Ltd.*, [2011] EWHC 474; *Matchbet Ltd. v. Openbet Retail Ltd.*, [2013] EWHC 3067; *FGT Custodians Pty. Ltd. v. Fagenblat*, [2003] VSCA 33; *Collins Thomson v. Clayton*, [2002] NSWSC 366; *Kirch Communications Pty Ltd. v. Gene Engineering Pty Ltd.*, [2002] NSWSC 485; *SmithKline Beecham (Australia) Pty Ltd. v. Chipman*, [2003] FCA 796, 131 F.C.R. 500; *Rodriguez v. Pacificare of Texas, Inc.*, 980 F.2d 1014 (1993); *Tagatz v. Marquette University*, 861 F.2d 1040 (1988); *Apple Inc. v. Motorola, Inc.*, 757 F.3d 1286 (2014); *Agribrands Purina Canada Inc. v. Kasamekas*, 2010 ONSC 166; *R. v. Demetrius*, 2009 CanLII 22797; *International Hi-Tech Industries Inc. v. FANUC Robotics Canada Ltd.*, 2006 BCSC 2011; *Casurina Ltd. Partnership v. Rio Algom Ltd.* (2002), 28 B.L.R. (3d) 44; *Prairie Well Servicing Ltd. v. Tundra Oil and Gas Ltd.*, 2000 MBQB 52, 146 Man. R. (2d) 284; *Deemar v. College of Veterinarians of Ontario*, 2008 ONCA 600, 92 O.R. (3d) 97; *Coady v. Burton Canada Co.*, 2013 NSCA 95, 333 N.S.R. (2d) 348; *Fougere v. Blunden Construction Ltd.*, 2014 NSCA 52, 345 N.S.R. (2d) 385.

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*Civil Procedure Rules* (Nova Scotia), rr. 55.01(2), 55.04(1)(a), (b), (c).

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*Federal Courts Rules*, SOR/98-106, r. 52.2(1)(*c*).

*Queen's Bench Rules* (Saskatchewan), r. 5-37.

*Rules of Civil Procedure*, *R.R.O. 1990, Reg. 194*, rr. 4.1.01(1), (2), 53.03(2.1).

*Rules of Civil Procedure* (Prince Edward Island), r. 53.03(3)(g).

*Rules of Court*, *Y.O.I.C. 2009/65, r. 34*(23).

*Supreme Court Civil Rules*, *B.C. Reg. 168/2009*, rr. 11-2(1), (2).

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**History and Disposition:**

APPEAL from a judgment of the Nova Scotia Court of Appeal (MacDonald C.J. and Oland and Beveridge JJ.A.), *2013 NSCA 66*, *330 N.S.R. (2d) 301*, *361 D.L.R. (4th) 659*, *36 C.P.C. (7th) 22*, *[2013] N.S.J. No. 259* (QL), *2013 CarswellNS 360* (WL Can.), setting aside in part a decision of Pickup J., *2012 NSSC 210*, *317 N.S.R. (2d) 283*, *26 C.P.C. (7th) 280*, *[2012] N.S.J. No. 289* (QL), *2012 CarswellNS 376* (WL Can.). Appeal dismissed.

## Counsel

*Alan D'Silva*, *James Wilson* and *Aaron Kreaden*, for the appellants.

*Jon Laxer* and *Brian F. P. Murphy*, for the respondents.

*Michael H. Morris*, for the intervener the Attorney General of Canada.

*Matthew Gourlay*, for the intervener the Criminal Lawyers' Association (Ontario).

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The judgment of the Court was delivered by

## CROMWELL J.

I. Introduction and Issues

**1** Expert opinion evidence can be a key element in the search for truth, but it may also pose special dangers. To guard against them, the Court over the last 20 years or so has progressively tightened the rules of admissibility and enhanced the trial judge's gatekeeping role. These developments seek to ensure that expert opinion evidence meets certain basic standards before it is admitted. The question on this appeal is whether one of these basic standards for admissibility should relate to the proposed expert's independence and impartiality. In my view, it should.

**2** Expert witnesses have a special duty to the court to provide fair, objective and non-partisan assistance. A proposed expert witness who is unable or unwilling to comply with this duty is not qualified to give expert opinion evidence and should not be permitted to do so. Less fundamental concerns about an expert's independence and impartiality should be taken into account in the broader, overall weighing of the costs and benefits of receiving the evidence.

**3** Applying these principles, I agree with the conclusion reached by the majority of the Nova Scotia Court of Appeal and would therefore dismiss this appeal with costs.

## II. Overview of the Facts and Judicial History

### A. *Facts and Proceedings*

**4** The appeal arises out of a professional negligence action by the respondents (who I will call the shareholders) against the appellants, the former auditors of their company (I will refer to them as the auditors). The shareholders started the action after they had retained a different accounting firm, the [page190] Kentville office of Grant Thornton LLP, to perform various accounting tasks and which in their view revealed problems with the auditors' previous work. The central allegation in the action is that the auditors' failure to apply generally accepted auditing and accounting standards while carrying out their functions caused financial loss to the shareholders. The main question in the action boils down to whether the auditors were negligent in the performance of their professional duties.

**5** The auditors brought a motion for summary judgment in August of 2010, seeking to have the shareholders' action dismissed. In response, the shareholders retained Susan MacMillan, a forensic accounting partner at the Halifax office of Grant Thornton, to review all the relevant materials, including the documents filed in the action, and to prepare a report of her findings. Her affidavit set out her findings, including her opinion that the auditors had not complied with their professional obligations to the shareholders. The auditors applied to strike out Ms. MacMillan's affidavit on the grounds that she was not an impartial expert witness. They argued that the action comes down to a battle of opinion between two accounting firms - the auditors' and the expert witness's. Ms. MacMillan's firm could be exposed to liability if its approach was not accepted by the court and, as a partner, Ms. MacMillan could be personally liable. Her potential liability if her opinion were not accepted gives her a personal financial interest in the outcome of the litigations and this, in the auditors' submission, ought to disqualify her from testifying.

**6** The proceedings since have been neither summary nor resulted in a judgment. Instead, the litigation has been focused on the expert evidence issue; the summary judgment application has not yet been heard on its merits.

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### B. *Judgments Below*

#### (1) Nova Scotia Supreme Court: *2012 NSSC 210*, *317 N.S.R. (2d) 283* (Pickup J.)

**7** Pickup J. essentially agreed with the auditors and struck out the MacMillan affidavit in its entirety: para. 106. He found that, in order to be admissible, an expert's evidence "must be, and be seen to be, independent and impartial": para. 99. Applying that test, he concluded that this was one of those "clearest of cases where the reliability of the

expert ... does not meet the threshold requirements for admissibility": para. 101.

(2) Nova Scotia Court of Appeal: *2013 NSCA 66*, *330 N.S.R. (2d) 301* (Beveridge J.A., Oland J.A. Concurring; MacDonald C.J.N.S. Dissenting)

**8** The majority of the Court of Appeal concluded that the motions judge erred in excluding Ms. MacMillan's affidavit. Beveridge J.A. wrote that while the court has discretion to exclude expert evidence due to actual bias or partiality, the test adopted by the motions judge - that an expert "must be, and be seen to be, independent and impartial" - was wrong in law. He ought not to have ruled her evidence inadmissible and struck out her affidavit.

**9** MacDonald C.J.N.S., dissenting, would have upheld the motions judge's decision because he had properly articulated and applied the relevant legal principles.

## III. Analysis

### A. *Overview*

**10** In my view, expert witnesses have a duty to the court to give fair, objective and non-partisan opinion evidence. They must be aware of this duty and able and willing to carry it out. If they do not meet this threshold requirement, their evidence should not be admitted. Once this threshold is met, [page192] however, concerns about an expert witness's independence or impartiality should be considered as part of the overall weighing of the costs and benefits of admitting the evidence. This common law approach is, of course, subject to statutory and related provisions which may establish different rules of admissibility.

### B. *Expert Witness Independence and Impartiality*

**11** There have been long-standing concerns about whether expert witnesses hired by the parties are impartial in the sense that they are expressing their own unbiased professional opinion and whether they are independent in the sense that their opinion is the product of their own, independent conclusions based on their own knowledge and judgment: see, e.g., G. R. Anderson, *Expert Evidence* (3rd ed. 2014), at p. 509; S. N. Lederman, A. W. Bryant and M. K. Fuerst, *The Law of Evidence in Canada* (4th ed. 2014), at p. 783. As Sir George Jessel, M.R., put it in the 1870s, "[u]ndoubtedly there is a natural bias to do something serviceable for those who employ you and adequately remunerate you. It is very natural, and it is so effectual, that we constantly see persons, instead of considering themselves witnesses, rather consider themselves as the paid agents of the person who employs them": *Lord Abinger v. Ashton* (1873), L.R. 17 Eq. 358, at p. 374.

**12** Recent experience has only exacerbated these concerns; we are now all too aware that an expert's lack of independence and impartiality can result in egregious miscarriages of justice: *R. v. D.D.*, *2000 SCC 43*, *[2000] 2 S.C.R. 275*, at para. 52. As observed by Beveridge J.A. in this case, *The Commission on Proceedings Involving Guy Paul Morin: Report* (1998) authored by the Honourable Fred Kaufman and the *Inquiry into Pediatric Forensic Pathology in Ontario: Report* (2008) conducted by the Honourable Stephen T. Goudge provide two striking examples where "[s]eemingly solid and impartial, but flawed, forensic scientific opinion has played a prominent role in miscarriages of justice?: para. 105. Other reports outline the critical need for impartial and independent expert evidence in civil litigation: *ibid.*, at para. 106; see the Right [page193] Honourable Lord Woolf, *Access to Justice: Final Report* (1996); the Honourable Coulter A. Osborne, *Civil Justice Reform Project: Summary of Findings & Recommendations* (2007).

**13** To decide how our law of evidence should best respond to these concerns, we must confront several questions: Should concerns about potentially biased expert opinion go to admissibility or only to weight?; If to admissibility, should these concerns be addressed by a threshold requirement for admissibility, by a judicial discretion to exclude, or both?; At what point do these concerns justify exclusion of the evidence?; And finally, how is our response to these concerns integrated into the existing legal framework governing the admissibility of expert opinion evidence?

To answer these questions, we must first consider the existing legal framework governing admissibility, identify the duties that an expert witness has to the court and then turn to how those duties are best reflected in that legal framework.

C. *The Legal Framework*

(1) The Exclusionary Rule for Opinion Evidence

**14** To the modern general rule that all relevant evidence is admissible there are many qualifications. One of them relates to opinion evidence, which is the subject of a complicated exclusionary rule. Witnesses are to testify as to the facts which they perceived, not as to the inferences - that is, the opinions - that they drew from them. As one great evidence scholar put it long ago, it is "for the jury to form opinions, and draw inferences and conclusions, and not for the witness": J. B. Thayer, *A Preliminary Treatise on Evidence at the Common Law* (1898; reprinted 1969), at p. 524; see also C. Tapper, *Cross and Tapper on Evidence* (12th ed. 2010), at p. 530. While various rationales have been offered for this exclusionary rule, the most convincing is probably that these ready-formed inferences are not helpful to the trier of fact and might even be misleading: see, e.g., *Graat v. The Queen*, [page194] [*[1982] 2 S.C.R. 819*], at p. 836; *Halsbury's Laws of Canada: Evidence* (2014 Reissue), at para. [*HEV-137*] "General rule against opinion evidence".

**15** Not all opinion evidence is excluded, however. Most relevant for this case is the exception for expert opinion evidence on matters requiring specialized knowledge. As Prof. Tapper put it, "the law recognizes that, so far as matters calling for special knowledge or skill are concerned, judges and jurors are not necessarily equipped to draw true inferences from facts stated by witnesses. A witness is therefore allowed to state his opinion about such matters, provided he is expert in them": p. 530; see also *R. v. Abbey*, [*[1982] 2 S.C.R. 24*], at p. 42.

(2) The Current Legal Framework for Expert Opinion Evidence

**16** Since at least the mid-1990s, the Court has responded to a number of concerns about the impact on the litigation process of expert evidence of dubious value. The jurisprudence has clarified and tightened the threshold requirements for admissibility, added new requirements in order to assure reliability, particularly of novel scientific evidence, and emphasized the important role that judges should play as "gatekeepers" to screen out proposed evidence whose value does not justify the risk of confusion, time and expense that may result from its admission.

**17** We can take as the starting point for these developments the Court's decision in *R. v. Mohan*, [*[1994] 2 S.C.R. 9*]. That case described the potential dangers of expert evidence and established a four-part threshold test for admissibility. The dangers are well known. One is that the trier of fact will inappropriately defer to the expert's opinion rather [page195] than carefully evaluate it. As Sopinka J. observed in *Mohan*:

> There is a danger that expert evidence will be misused and will distort the fact-finding process. Dressed up in scientific language which the jury does not easily understand and submitted through a witness of impressive antecedents, this evidence is apt to be accepted by the jury as being virtually infallible and as having more weight than it deserves. [p. 21]

(See also *D.D.*, at para. 53; *R. v. J.-L.J.*, [*2000 SCC 51*], [*[2000] 2 S.C.R. 600*], at paras. 25-26; *R. v. Sekhon*, [*2014 SCC 15*], [*[2014] 1 S.C.R. 272*], at para. 46.)

**18** The point is to preserve trial by judge and jury, not devolve to trial by expert. There is a risk that the jury "will be unable to make an effective and critical assessment of the evidence?: *R. v. Abbey*, [*2009 ONCA 624*], [*97 O.R. (3d) 330*], at para. 90, leave to appeal refused, [2010] 2 S.C.R. v. The trier of fact must be able to use its "informed judgment", not simply decide on the basis of an "act of faith" in the expert's opinion: *J.-L.J.*, at para. 56. The risk of "attornment to the opinion of the expert? is also exacerbated by the fact that expert evidence is resistant to effective cross-examination by counsel who are not experts in that field: *D.D.*, at para. 54. The cases address a number of other related concerns: the potential prejudice created by the expert's reliance on unproven material not subject to

cross-examination (*D.D.*, at para. 55); the risk of admitting "junk science" (*J.-L.J.*, at para. 25); and the risk that a "contest of experts" distracts rather than assists the trier of fact (*Mohan*, at p. 24). Another well-known danger associated with the admissibility of expert evidence is that it may lead to an inordinate expenditure of time and money: *Mohan*, at p. 21; *D.D.*, at para. 56; *Masterpiece Inc. v. Alavida Lifestyles Inc.*, *2011 SCC 27*, *[2011] 2 S.C.R. 387*, at para. 76.

**19** To address these dangers, *Mohan* established a basic structure for the law relating to the admissibility [page196] of expert opinion evidence. That structure has two main components. First, there are four threshold requirements that the proponent of the evidence must establish in order for proposed expert opinion evidence to be admissible: (1) relevance; (2) necessity in assisting the trier of fact; (3) absence of an exclusionary rule; and (4) a properly qualified expert (*Mohan*, at pp. 20-25; see also *Sekhon*, at para. 43). *Mohan* also underlined the important role of trial judges in assessing whether otherwise admissible expert evidence should be excluded because its probative value was overborne by its prejudicial effect - a residual discretion to exclude evidence based on a cost-benefit analysis: p. 21. This is the second component, which the subsequent jurisprudence has further emphasized: Lederman, Bryant and Fuerst, at pp. 789-90; *J.-L.J.*, at para. 28.

**20** *Mohan* and the jurisprudence since, however, have not explicitly addressed how this "cost-benefit" component fits into the overall analysis. The reasons in *Mohan* engaged in a cost-benefit analysis with respect to particular elements of the four threshold requirements, but they also noted that the cost-benefit analysis could be an aspect of exercising the overall discretion to exclude evidence whose probative value does not justify its admission in light of its potentially prejudicial effects: p. 21. The jurisprudence since *Mohan* has also focused on particular aspects of expert opinion evidence, but again without always being explicit about where additional concerns fit into the analysis. The unmistakable overall trend of the jurisprudence, however, has been to tighten the admissibility requirements and to enhance the judge's gatekeeping role.

**21** So, for example, the necessity threshold criterion was emphasized in cases such as *D.D.* The majority underlined that the necessity requirement exists "to ensure that the dangers associated with expert evidence are not lightly tolerated" and that "[m]ere relevance or 'helpfulness' is not enough": para. 46. Other cases have addressed the reliability of the science underlying an opinion and indeed technical evidence in general: *J.-L.J.*; *R. v. Trochym*, *2007 SCC 6*, *[2007] 1 S.C.R. 239*. The question remains, however, as to where the cost-benefit analysis [page197] and concerns such as those about reliability fit into the overall analysis.

**22** *Abbey* (ONCA) introduced helpful analytical clarity by dividing the inquiry into two steps. With minor adjustments, I would adopt that approach.

**23** At the first step, the proponent of the evidence must establish the threshold requirements of admissibility. These are the four *Mohan* factors (relevance, necessity, absence of an exclusionary rule and a properly qualified expert) and in addition, in the case of an opinion based on novel or contested science or science used for a novel purpose, the reliability of the underlying science for that purpose: *J.-L.J.*, at paras. 33, 35-36 and 47; *Trochym*, at para. 27; Lederman, Bryant and Fuerst, at pp. 788-89 and 800-801. Relevance at this threshold stage refers to logical relevance: *Abbey* (ONCA), at para. 82; *J.-L.J.*, at para. 47. Evidence that does not meet these threshold requirements should be excluded. Note that I would retain necessity as a threshold requirement: *D.D.*, at para. 57; see D. M. Paciocco and L. Stuesser, *The Law of Evidence* (7th ed. 2015), at pp. 209-10; *R. v. Boswell*, *2011 ONCA 283*, *85 C.R. (6th) 290*, at para. 13; *R. v. C. (M.)*, *2014 ONCA 611*, *13 C.R. (7th) 396*, at para. 72.

**24** At the second discretionary gatekeeping step, the judge balances the potential risks and benefits of admitting the evidence in order to decide whether the potential benefits justify the risks. The required balancing exercise has been described in various ways. In *Mohan*, Sopinka J. spoke of the "reliability versus effect factor" (p. 21), while in *J.-L.J.*, Binnie J. spoke about "relevance, reliability and necessity" being "measured against the counterweights of consumption of time, prejudice and confusion": para. 47. Doherty J.A. summed it up well in *Abbey*, stating that the "trial judge must decide whether expert evidence that meets the preconditions to admissibility is sufficiently beneficial to the trial process to warrant its admission despite the potential harm to the trial process that may flow from the admission of the expert evidence": para. 76.

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**25** With this delineation of the analytical framework, we can turn to the nature of an expert's duty to the court and where it fits into that framework.

D. *The Expert's Duty to the Court or Tribunal*

**26** There is little controversy about the broad outlines of the expert witness's duty to the court. As Anderson writes, "[t]he duty to provide independent assistance to the Court by way of objective unbiased opinion has been stated many times by common law courts around the world": p. 227. I would add that a similar duty exists in the civil law of Quebec: J.-C. Royer and S. Lavallée, *La preuve civile* (4th ed. 2008), at para. 468; D. Béchard, with the collaboration of J. Béchard, *L'expert* (2011), c. 9; *An Act to establish the new Code of Civil Procedure*, S.Q. 2014, c. 1, art. 22 (not yet in force); L. Chamberland, *Le nouveau Code de procédure civile commenté* (2014), at pp. 14 and 121.

**27** One influential statement of the elements of this duty are found in the English case *National Justice Compania Naviera S.A. v. Prudential Assurance Co.*, [1993] 2 Lloyd's Rep. 68 (Q.B.). Following an 87-day trial, Cresswell J. believed that a misunderstanding of the duties and responsibilities of expert witnesses contributed to the length of the trial. He listed in *obiter dictum* duties and responsibilities of experts, the first two of which have particularly influenced the development of Canadian law:

> 1. Expert evidence presented to the Court should be, and should be seen to be, the independent product of the expert uninfluenced as to form or content by the exigencies of litigation ... .
>
> 2. An expert witness should provide independent assistance to the Court by way of objective unbiased opinion in relation to matters within his [or her] expertise ... . An expert witness in the High Court should [page199] never assume the role of an advocate. [Emphasis added; citation omitted; p. 81.]

(These duties were endorsed on appeal: [1995] 1 Lloyd's Rep. 455 (C.A.), at p. 496.)

**28** Many provinces and territories have provided explicit guidance related to the duty of expert witnesses. In Nova Scotia, for example, the *Civil Procedure Rules* require that an expert's report be signed by the expert who must make (among others) the following representations to the court: that the expert is providing an objective opinion for the assistance of the court; that the expert is prepared to apply independent judgment when assisting the court; and that the report includes everything the expert regards as relevant to the expressed opinion and draws attention to anything that could reasonably lead to a different conclusion (r. 55.04(1)(a), (b) and (c)). While these requirements do not affect the rules of evidence by which expert opinion is determined to be admissible or inadmissible, they provide a convenient summary of a fairly broadly shared sense of the duties of an expert witness to the court.

**29** There are similar descriptions of the expert's duty in the civil procedure rules in other Canadian jurisdictions: Anderson, at p. 227; *The Queen's Bench Rules* (Saskatchewan), r. 5-37; *Supreme Court Civil Rules*, *B.C. Reg. 168/2009, r. 11-2*(1); *Rules of Civil Procedure*, *R.R.O. 1990, Reg. 194, r. 4.1.01*(1); *Rules of Court*, *Y.O.I.C. 2009/65, r. 34*(23); *An Act to establish the new Code of Civil Procedure*, art. 22. Moreover, the rules in Saskatchewan, British Columbia, Ontario, Nova Scotia, Prince Edward Island, Quebec and the Federal Courts require experts to certify that they are aware of and will comply with their duty to the court: Anderson, at p. 228; Saskatchewan *Queen's Bench Rules*, r. 5-37(3); British Columbia *Supreme Court Civil Rules*, r. 11-2(2); Ontario *Rules of Civil Procedure*, r. 53.03(2.1); Nova Scotia *Civil Procedure Rules*, r. 55.04(1)(a); Prince Edward Island *Rules of Civil Procedure*, r. 53.03(3)(g); *An Act to establish the new Code of [page200] Civil Procedure*, art. 235 (not yet in force); *Federal Courts Rules*, *SOR/98-106, r. 52.2*(1)(*c*).

**30** The formulation in the Ontario *Rules of Civil Procedure* is perhaps the most succinct and complete statement of the expert's duty to the court: to provide opinion evidence that is fair, objective and non-partisan (r. 4.1.01(1)(a)).

The *Rules* are also explicit that this duty to the court prevails over any obligation owed by the expert to a party (r. 4.1.01(2)). Likewise, the newly adopted *Act to establish the new Code of Civil Procedure* of Quebec explicitly provides, as a guiding principle, that the expert's duty to the court overrides the parties' interests, and that the expert must fulfill his or her primary duty to the court "objectively, impartially and thoroughly": art. 22; Chamberland, at pp. 14 and 121.

**31** Many of the relevant rules of court simply reflect the duty that an expert witness owes to the court at common law: Anderson, at p. 227. In my opinion, this is true of the Nova Scotia rules that apply in this case. Of course, it is always open to each jurisdiction to impose different rules of admissibility, but in the absence of a clear indication to that effect, the common law rules apply in common law cases. I note that in Nova Scotia, the *Civil Procedure Rules* explicitly provide that they do not change the rules of evidence by which the admissibility of expert opinion evidence is determined: r. 55.01(2).

**32** Underlying the various formulations of the duty are three related concepts: impartiality, independence and absence of bias. The expert's opinion must be impartial in the sense that it reflects an objective assessment of the questions at hand. It must be independent in the sense that it is the product of the expert's independent judgment, uninfluenced by who has retained him or her or the outcome of the litigation. It must be unbiased in the sense that it does not unfairly favour one party's [page201] position over another. The acid test is whether the expert's opinion would not change regardless of which party retained him or her: P. Michell and R. Mandhane, "The Uncertain Duty of the Expert Witness" *(2005), 42 Alta. L. Rev. 635*, at pp. 638-39. These concepts, of course, must be applied to the realities of adversary litigation. Experts are generally retained, instructed and paid by one of the adversaries. These facts alone do not undermine the expert's independence, impartiality and freedom from bias.

E. *The Expert's Duties and Admissibility*

**33** As we have seen, there is a broad consensus about the nature of an expert's duty to the court. There is no such consensus, however, about how that duty relates to the admissibility of an expert's evidence. There are two main questions: Should the elements of this duty go to admissibility of the evidence rather than simply to its weight?; And, if so, is there a threshold admissibility requirement in relation to independence and impartiality?

**34** In this section, I will explain my view that the answer to both questions is yes: a proposed expert's independence and impartiality go to admissibility and not simply to weight and there is a threshold admissibility requirement in relation to this duty. Once that threshold is met, remaining concerns about the expert's compliance with his or her duty should be considered as part of the overall cost-benefit analysis which the judge conducts to carry out his or her gatekeeping role.

(1) Admissibility or Only Weight?

(a) *The Canadian Law*

**35** The weight of authority strongly supports the conclusion that at a certain point, expert evidence should be ruled inadmissible due to the expert's lack of impartiality and/or independence.

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**36** Our Court has confirmed this position in a recent decision that was not available to the courts below:

> It is well established that an expert's opinion must be independent, impartial and objective, and given with a view to providing assistance to the decision maker (J.?C. Royer and S. Lavallée, *La preuve civile* (4th ed. 2008), at No. 468; D. Béchard, with the collaboration of J. Béchard, *L'expert* (2011), chap. 9; *An Act to establish the new Code of Civil Procedure*, S.Q. 2014, c. 1, s. 22 (not yet in force)). However, these factors generally have an impact on the probative value of the expert's opinion and are not always insurmountable barriers to the admissibility of his or her testimony. Nor do they necessarily "disqualify" the expert (L.

> Ducharme and C.-M. Panaccio, *L'administration de la preuve* (4th ed. 2010), at Nos. 590?91 and 605). For expert testimony to be inadmissible, more than a simple appearance of bias is necessary. The question is not whether a reasonable person would consider that the expert is not independent. Rather, what must be determined is whether the expert's lack of independence renders him or her incapable of giving an impartial opinion in the specific circumstances of the case (D. M. Paciocco, "Unplugging Jukebox Testimony in an Adversarial System: Strategies for Changing the Tune on Partial Experts" *(2009), 34 Queen's L.J. 565*, at pp. 598-99).

(*Mouvement laique québécois v. Saguenay (City)*, *2015 SCC 16*, *[2015] 2 S.C.R. 3*, at para. 106)

**37** I will refer to a number of other cases that support this view. I do so by way of illustration and without commenting on the outcome of particular cases. An expert's interest in the litigation or relationship to the parties has led to exclusion in a number of cases: see, e.g., *Fellowes, McNeil v. Kansa General International Insurance Co. (1998), 40 O.R. (3d) 456* (Gen. Div.) (proposed expert was the defendant's lawyer in related matters and had investigated from the outset of his retainer the matter of a potential negligence claim against the plaintiff); *Royal Trust Corp. of Canada v. Fisherman (2000), 49 O.R. (3d) 187* (S.C.J.) (expert was the party's lawyer in related U.S. proceedings); *R. v. Docherty*, *2010 ONSC 3628* (expert was the defence counsel's father); *Ocean v. Economical Mutual Insurance Co.*, *2010 NSSC 315*, *293 N.S.R. (2d) 394* (expert was also a party to the litigation); *Handley v. Punnett*, [page203] *2003 BCSC 294* (expert was also a party to the litigation); *Bank of Montreal v. Citak*, *[2001] O.J. No. 1096* (QL) (S.C.J.) (expert was effectively a "co-venturer" in the case due in part to the fact that 40 percent of his remuneration was contingent upon success at trial: para. 7); *Dean Construction Co. v. M.J. Dixon Construction Ltd.*, *2011 ONSC 4629*, *5 C.L.R. (4th) 240* (expert's retainer agreement was inappropriate); *Hutchingame v. Johnstone*, *2006 BCSC 271* (expert stood to incur liability depending on the result of the trial). In other cases, the expert's stance or behaviour as an advocate has justified exclusion: see, e.g., *Alfano v. Piersanti*, *2012 ONCA 297*, *291 O.A.C. 62*; *Kirby Lowbed Services Ltd. v. Bank of Nova Scotia*, *2003 BCSC 617*; *Gould v. Western Coal Corp.*, *2012 ONSC 5184*, *7 B.L.R. (5th) 19*.

**38** Many other cases have accepted, in principle, that lack of independence or impartiality can lead to exclusion, but have ruled that the expert evidence did not warrant rejection on the particular facts: see, e.g., *United City Properties Ltd. v. Tong*, *2010 BCSC 111*; *R. v. INCO Ltd. (2006), 80 O.R. (3d) 594* (S.C.J.). This was the position of the Court of Appeal in this case: para. 109; see also para. 121.

**39** Some Canadian courts, however, have treated these matters as going exclusively to weight rather than to admissibility. The most often cited cases for this proposition are probably *R. v. Klassen*, *2003 MBQB 253*, *179 Man. R. (2d) 115*, and *Gallant v. Brake-Patten*, *2012 NLCA 23*, *321 Nfld. & P.E.I.R. 77*. *Klassen* holds as admissible any expert evidence meeting the criteria from *Mohan*, with bias only becoming a factor as to the weight to be given to the evidence: see also *R. v. Violette*, *2008 BCSC 920*. Similarly, the court in *Gallant* determined that a challenge to expert evidence that is based on the expert having a connection to a party or an issue in the case [page204] or a possible predetermined position on the case cannot take place at the admissibility stage: para. 89.

**40** I conclude that the dominant approach in Canadian common law is to treat independence and impartiality as bearing not just on the weight but also on the admissibility of the evidence. I note that while the shareholders submit that issues regarding expert independence should go only to weight, they rely on cases such as *INCO* that specifically accept that a finding of lack of independence or impartiality can lead to inadmissibility in certain circumstances: R.F., at paras. 52-53.

(b) *Other Jurisdictions*

**41** Outside Canada, the concerns related to independence and impartiality have been addressed in a number of ways. Some are similar to the approach in Canadian law.

**42** For example, summarizing the applicable principles in British law, Nelson J. in *Armchair Passenger Transport*

*Ltd. v. Helical Bar Plc*, [2003] EWHC 367 (Q.B.), underlined that when an expert has an interest or connection with the litigation or a party thereto, exclusion will be warranted if it is determined that the expert is unwilling or unable to carry out his or her primary duty to the court: see also H. M. Malek et al., eds., *Phipson on Evidence* (18th ed. 2013), at pp. 1158-59. The mere fact of an interest or connection will not disqualify, but it nonetheless may do so in light of the nature and extent of the interest or connection in particular circumstances. As Lord Phillips of Worth Matravers, M.R., put it in a leading case, "[i]t is always desirable that an expert should have no actual or apparent interest in the outcome of the proceedings in which he gives evidence, but such disinterest is not automatically a precondition to the admissibility of his evidence": *R. (Factortame Ltd.) v. Secretary of State for Transport*, [2002] EWCA Civ 932, [page205] [2003] Q.B. 381, at para. 70; see also *Gallaher International Ltd. v. Tlais Enterprises Ltd.*, [2007] EWHC 464 (Comm.); *Meat Corp. of Namibia Ltd. v. Dawn Meats (U.K.) Ltd.*, [2011] EWHC 474 (Ch. D.); *Matchbet Ltd. v. Openbet Retail Ltd.*, [2013] EWHC 3067 (Ch. D.), at paras. 312-17.

**43** In Australia, the expert's objectivity and impartiality will generally go to weight, not to admissibility: I. Freckelton and H. Selby, *Expert Evidence: Law, Practice, Procedure and Advocacy* (5th ed. 2013), at p. 35. As the Court of Appeal of the State of Victoria put it: "... to the extent that it is desirable that expert witnesses should be under a duty to assist the Court, that has not been held and should not be held as disqualifying, in itself, an 'interested' witness from being competent to give expert evidence" (*FGT Custodians Pty. Ltd. v. Fagenblat*, [2003] VSCA 33, at para. 26 (AustLII); see also Freckelton and Selby, at pp. 186-88; *Collins Thomson v. Clayton*, [2002] NSWSC 366; *Kirch Communications Pty Ltd. v. Gene Engineering Pty Ltd.*, [2002] NSWSC 485; *SmithKline Beecham (Australia) Pty Ltd. v. Chipman*, [2003] FCA 796, 131 F.C.R. 500).

**44** In the United States, at the federal level, the independence of the expert is a consideration that goes to the weight of the evidence, and a party may testify as an expert in his own case: *Rodriguez v. Pacificare of Texas, Inc.*, 980 F.2d 1014 (5th Cir. 1993), at p. 1019; *Tagatz v. Marquette University*, 861 F.2d 1040 (7th Cir. 1988); *Apple Inc. v. Motorola, Inc.*, 757 F.3d 1286 (Fed. Cir. 2014), at p. 1321. This also seems to be a fair characterization of the situation in the states (*Corpus Juris Secundum*, vol. 32 (2008), at p. 325: "The bias or interest of the witness does not affect his or her qualification, but only the weight to be given the testimony.").

(c) *Conclusion*

**45** Following what I take to be the dominant view in the Canadian cases, I would hold that an expert's lack of independence and impartiality goes to the admissibility of the evidence in addition to being considered in relation to the weight to be given to [page206] the evidence if admitted. That approach seems to me to be more in line with the basic structure of our law relating to expert evidence and with the importance our jurisprudence has attached to the gatekeeping role of trial judges. Binnie J. summed up the Canadian approach well in *J.-L.J.*: "The admissibility of the expert evidence should be scrutinized at the time it is proffered, and not allowed too easy an entry on the basis that all of the frailties could go at the end of the day to weight rather than admissibility" (para. 28).

(2) The Appropriate Threshold

**46** I have already described the duty owed by an expert witness to the court: the expert must be fair, objective and non-partisan. As I see it, the appropriate threshold for admissibility flows from this duty. I agree with Prof. (now Justice of the Ontario Court of Justice) Paciocco that "the common law has come to accept ... that expert witnesses have a duty to assist the court that overrides their obligation to the party calling them. If a witness is unable or unwilling to fulfill that duty, they do not qualify to perform the role of an expert and should be excluded": "Taking a 'Goudge' out of Bluster and Blarney: an 'Evidence-Based Approach' to Expert Testimony" (2009), 13 *Can. Crim. L.R.* 135, at p. 152 (footnote omitted). The expert witnesses must, therefore, be aware of this primary duty to the court and able and willing to carry it out.

**47** Imposing this additional threshold requirement is not intended to and should not result in trials becoming longer or more complex. As Prof. Paciocco aptly observed, "if inquiries about bias or partiality become routine during *Mohan voir dires*, trial testimony will become nothing more than an inefficient reprise of the admissibility hearing":

"Unplugging Jukebox Testimony in an Adversarial System: Strategies for Changing the Tune on Partial Experts" *(2009), 34 Queen's L.J. 565* ("Jukebox?), at p. 597. While I would not go so far as to hold that the expert's independence and impartiality should be presumed absent challenge, my [page207] view is that absent such challenge, the expert's attestation or testimony recognizing and accepting the duty will generally be sufficient to establish that this threshold is met.

**48** Once the expert attests or testifies on oath to this effect, the burden is on the party opposing the admission of the evidence to show that there is a realistic concern that the expert's evidence should not be received because the expert is unable and/or unwilling to comply with that duty. If the opponent does so, the burden to establish on a balance of probabilities this aspect of the admissibility threshold remains on the party proposing to call the evidence. If this is not done, the evidence, or those parts of it that are tainted by a lack of independence or impartiality, should be excluded. This approach conforms to the general rule under the *Mohan* framework, and elsewhere in the law of evidence, that the proponent of the evidence has the burden of establishing its admissibility.

**49** This threshold requirement is not particularly onerous and it will likely be quite rare that a proposed expert's evidence would be ruled inadmissible for failing to meet it. The trial judge must determine, having regard to both the particular circumstances of the proposed expert and the substance of the proposed evidence, whether the expert is able and willing to carry out his or her primary duty to the court. For example, it is the nature and extent of the interest or connection with the litigation or a party thereto which matters, not the mere fact of the interest or connection; the existence of some interest or a relationship does not automatically render the evidence of the proposed expert inadmissible. In most cases, a mere employment relationship with the party calling the evidence will be insufficient to do so. On the other hand, a direct financial interest in the outcome of the litigation will be of more concern. The same can be said in the case of a very close familial relationship with one of the parties or situations in which the proposed expert will probably incur professional liability if his or her opinion is not accepted by the court. Similarly, an expert who, in his or her proposed evidence or otherwise, [page208] assumes the role of an advocate for a party is clearly unwilling and/or unable to carry out the primary duty to the court. I emphasize that exclusion at the threshold stage of the analysis should occur only in very clear cases in which the proposed expert is unable or unwilling to provide the court with fair, objective and non-partisan evidence. Anything less than clear unwillingness or inability to do so should not lead to exclusion, but be taken into account in the overall weighing of costs and benefits of receiving the evidence.

**50** As discussed in the English case law, the decision as to whether an expert should be permitted to give evidence despite having an interest or connection with the litigation is a matter of fact and degree. The concept of apparent bias is not relevant to the question of whether or not an expert witness will be unable or unwilling to fulfill its primary duty to the court. When looking at an expert's interest or relationship with a party, the question is not whether a reasonable observer would think that the expert is not independent. The question is whether the relationship or interest results in the expert being unable or unwilling to carry out his or her primary duty to the court to provide fair, non-partisan and objective assistance.

**51** Having established the analytical framework, described the expert's duty and determined that compliance with this duty goes to admissibility and not simply to weight, I turn now to where this duty fits into the analytical framework for admission of expert opinion evidence.

F. *Situating the Analysis in the Mohan Framework*

(1) The Threshold Inquiry

**52** Courts have addressed independence and impartiality at various points of the admissibility test. Almost every branch of the *Mohan* framework has been adapted to incorporate bias concerns one [page209] way or another: the proper qualifications component (see, e.g., *Bank of Montreal*; *Dean Construction*; *Agribrands Purina Canada Inc. v. Kasamekas*, *2010 ONSC 166*; *R. v. Demetrius*, *2009 CanLII 22797* (Ont. S.C.J.)); the necessity component (see, e.g., *Docherty*; *Alfano*); and during the discretionary cost-benefit analysis (see, e.g., *United City Properties*; *Abbey* (ONCA)). On other occasions, courts have found it to be a stand-alone requirement: see, e.g., *Docherty*;

*International Hi-Tech Industries Inc. v. FANUC Robotics Canada Ltd.*, 2006 BCSC 2011; *Casurina Ltd. Partnership v. Rio Algom Ltd.* (2002), 28 B.L.R. (3d) 44 (Ont. S.C.J.); *Prairie Well Servicing Ltd. v. Tundra Oil and Gas Ltd.*, 2000 MBQB 52, 146 Man. R. (2d) 284. Some clarification of this point will therefore be useful.

**53** In my opinion, concerns related to the expert's duty to the court and his or her willingness and capacity to comply with it are best addressed initially in the "qualified expert" element of the *Mohan* framework: S. C. Hill, D. M. Tanovich and L. P. Strezos, *McWilliams' Canadian Criminal Evidence* (5th ed. (loose-leaf)), at 12: 30.20.50; see also *Deemar v. College of Veterinarians of Ontario*, 2008 ONCA 600, 92 O.R. (3d) 97, at para. 21; Lederman, Bryant and Fuerst, at pp. 826-27; *Halsbury's Laws of Canada: Evidence*, at para. HEV-152 "Partiality"; *The Canadian Encyclopedic Digest* (Ont. 4th ed. (loose-leaf)), vol. 24, Title 62 -- Evidence, at s.469. A proposed expert witness who is unable or unwilling to fulfill this duty to the court is not properly qualified to perform the role of an expert. Situating this concern in the "properly qualified expert" ensures that the courts will focus expressly on the important risks associated with biased experts: Hill, Tanovich and Strezos, at 12: 30.20.50; Paciocco, "Jukebox", at p. 595.

(2) The Gatekeeping Exclusionary Discretion

**54** Finding that expert evidence meets the basic threshold does not end the inquiry. Consistent with the structure of the analysis developed following *Mohan* which I have discussed earlier, the judge [page210] must still take concerns about the expert's independence and impartiality into account in weighing the evidence at the gatekeeping stage. At this point, relevance, necessity, reliability and absence of bias can helpfully be seen as part of a sliding scale where a basic level must first be achieved in order to meet the admissibility threshold and thereafter continue to play a role in weighing the overall competing considerations in admitting the evidence. At the end of the day, the judge must be satisfied that the potential helpfulness of the evidence is not outweighed by the risk of the dangers materializing that are associated with expert evidence.

G. *Expert Evidence and Summary Judgment*

**55** I must say a brief word about the procedural context in which this case originates - a summary judgment motion. (I note that these comments relate to the summary judgment regime under the Nova Scotia rules and that different considerations may arise under different rules.) It is common ground that the court hearing the motion can consider only admissible evidence. However, under the Nova Scotia jurisprudence, which is not questioned on this appeal, it is not the role of a judge hearing a summary judgment motion in Nova Scotia to weigh the evidence, draw reasonable inferences from evidence or settle matters of credibility: *Coady v. Burton Canada Co.*, 2013 NSCA 95, 333 N.S.R. (2d) 348, at paras. 42-44, 87 and 98; *Fougere v. Blunden Construction Ltd.*, 2014 NSCA 52, 345 N.S.R. (2d) 385, at paras. 6 and 12. Taking these two principles together, the result in my view is this. A motions judge hearing a summary judgment application under the Nova Scotia rules must be satisfied that proposed expert evidence meets the threshold requirements for admissibility at the first step of the analysis, but should generally not engage in the second step cost-benefit analysis. That cost-benefit analysis, in anything other than the most obvious cases of inadmissibility, inevitably involves assigning weight - or at least potential weight - to the evidence.

[page211]

H. *Application*

**56** I turn to the application of these principles to the facts of the case. In my respectful view, the record amply sustains the result reached by the majority of the Court of Appeal that Ms. MacMillan's evidence was admissible on the summary judgment application. Of course, the framework which I have set out in these reasons was not available to either the motions judge or to the Court of Appeal.

**57** There was no finding by the motions judge that Ms. MacMillan was in fact biased or not impartial or that she was acting as an advocate for the shareholders: C.A. reasons, at para. 122. On the contrary, she specifically

recognized that she was aware of the standards and requirements that experts be independent. She was aware of the precise guidelines in the accounting industry concerning accountants acting as expert witnesses. She testified that she owed an ultimate duty to the court in testifying as an expert witness: A.R., vol. III, at pp. 75-76; C.A. reasons, at para. 134. To the extent that the motions judge was concerned about the "appearance" of impartiality, this factor plays no part in the test for admissibility, as I have explained earlier.

**58** The auditors' claim that Ms. MacMillan lacks objectivity rests on two main points which I will address in turn.

**59** First, the auditors say that the earlier work done for the shareholders by the Kentville office of Grant Thornton "served as a catalyst and foundation for the claim of negligence" against the auditors and that this "precluded [Grant Thornton] from acting as 'independent' experts in this case": A.F., at paras. 17 and 19. Ms. MacMillan, the auditors submit, was in an "irreconcilable conflict of interest, in that she would inevitably have to opine on, and choose between, the actions taken and standard of care exercised by her own partners at Grant Thornton" and those of the auditors: A.F., at para. 21. This first submission, however, must be rejected.

[page212]

**60** The fact that one professional firm discovers what it thinks is or may be professional negligence does not, on its own, disqualify it from offering that opinion as an expert witness. Provided that the initial work is done independently and impartially and the person put forward as an expert understands and is able to comply with the duty to provide fair, objective and non-partisan assistance to the court, the expert meets the threshold qualification in that regard. There is no suggestion here that Grant Thornton was hired to take a position dictated to it by the shareholders or that there was anything more than a speculative possibility of Grant Thornton incurring liability to them if the firm's opinion was not ultimately accepted by the court. There was no finding that Ms. MacMillan was, in fact, biased or not impartial, or that she was acting as an advocate for the shareholders. The auditors' submission that she somehow "admitted" on her cross-examination that she was in an "irreconcilable conflict" is not borne out by a fair reading of her evidence in context: A.R., vol. III, at pp. 139-45. On the contrary, her evidence was clear that she understood her role as an expert and her duty to the court: *ibid.*, at pp. 75-76.

**61** The auditors' second main point was that Ms. MacMillan was not independent because she had "incorporated" some of the work done by the Kentville office of her firm. This contention is also ill founded. To begin, I do not accept that an expert lacks the threshold qualification in relation to the duty to give fair, objective and non-partisan evidence simply because the expert relies on the work of other professionals in reaching his or her own opinion. Moreover, as Beveridge J.A. concluded, what was "incorporated" was essentially an exercise in arithmetic that had nothing to do with any accounting opinion expressed by the Kentville office: C.A. reasons, at paras. 146-49.

**62** There was no basis disclosed in this record to find that Ms. MacMillan's evidence should be [page213] excluded because she was not able and willing to provide the court with fair, objective and non-partisan evidence. I agree with the majority of the Court of Appeal who concluded that the motions judge committed a palpable and overriding error in determining that Ms. MacMillan was in a conflict of interest that prevented her from giving impartial and objective evidence: paras. 136-50.

## IV. Disposition

**63** I would dismiss the appeal with costs.

*Appeal dismissed with costs.*

**Solicitors:**

*Solicitors for the appellants: Stikeman Elliott, Toronto.*

*Solicitors for the respondents: Lenczner Slaght Royce Smith Griffin, Toronto; Groupe Murphy Group, Moncton.*

*Solicitor for the intervener the Attorney General of Canada: Attorney General of Canada, Toronto.*

*Solicitors for the intervener the Criminal Lawyers' Association (Ontario): Henein Hutchison, Toronto.*

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# Toronto Real Estate Board v. Canada (Commissioner of Competition), [2018] 3 F.C.R. 563

Federal Courts Reports

Federal Court of Appeal

Nadon, Near and Rennie JJ.A.

Heard: Toronto, December 5, 2016;

Judgment: Ottawa, December 1, 2017.

No. A-174-16

**[2018] 3 F.C.R. 563** | [2018] 3 R.C.F. 563 | [2017] F.C.J. No. 1155 | [2017] A.C.F. no 1155 | 2017 FCA 236

The Toronto Real Estate Board (Appellant) v. Commissioner of Competition (Respondent) and The Canadian Real Estate Association (Intervener)

(197 paras.)

## Case Summary

**Catchwords:**

**Competition — Appeal from two decisions of Competition Tribunal holding that certain information-sharing practices of appellant preventing competition substantially in supply of residential real estate brokerage services in Greater Toronto Area (GTA) — Appellant maintaining database of information on available property listings in GTA, making some information available to members via electronic data feed — However, some data available in database not distributed via data feed — Respondent claiming appellant's actions violating Competition Act, s. 79(1) by preventing or lessening competition — Appellant, not-for-profit corporation, Canada's largest real estate board — Operating online system (Multiple Listing Service (MLS)) for collecting, distributing real estate information among members — Many brokers operating sections of websites called "virtual office websites" (VOWs) whereby appellant's data feed delivering information to brokers to populate websites — Tribunal concluding that VOW restrictions adversely affecting non-price competition in relevant market; also finding that appellant not leading sufficient evidence to demonstrate copyright in MLS database in question — Whether Tribunal erring in finding that appellant substantially reducing competition within meaning of Act, s. 79(1) — Most of appellant's arguments focussing on Act, ss. 79(1)(b),(c) — No dispute that appellant's VOW policies constituting practice in accordance with Act, s. 79(1)(b) — Tribunal applying correct framework respecting s. 79(1)(b) — Finding that evidence of subjective anti-competitive intent, reasonably foreseeable exclusionary effects outweighing very limited evidence adduced in support of alleged legitimate [page564] business justifications; tribunal's analysis not unreasonable — Also, Tribunal correctly understanding significance of word "substantially" in Act, s. 79(1)(c), test having to apply to determine whether appellant's practice regarding disputed data constituting practice having effect of preventing competition substantially in GTA — Understanding difference in nature between quantitative, qualitative evidence — Tribunal making findings of number of anti-competitive effects caused by VOW restrictions — Of opinion that, "but for" VOW restrictions, such anti-competitive effects would be considerably lower; concluding that anti-competitive effects on non-price dimensions amounting to substantial prevention of competition — In relying on qualitative evidence for findings of anti-competitive effects, conclusion on substantiality, Tribunal not making any reviewable error; thus no basis to interfere with determination under Act, s. 79(1)(c) — Grounds of appeal based on privacy concerns, copyright also failing — Appeal dismissed.**

**Privacy — Personal Information Protection and Electronic Documents Act — In appeal from two decisions of Competition Tribunal holding that certain information-sharing practices of appellant preventing competition substantially in supply of residential real estate brokerage services in Greater Toronto Area, appellant seeking to justify restriction on disclosure of disputed data on basis of privacy — Specifically claiming that privacy concerns of vendors, purchasers constituting business justification sufficient to escape liability under Competition Act, s. 79(1)(b), asserting that required to comply with Personal Information Protection and Electronic Documents Act (PIPEDA) — Whether Tribunal erring in failing to conclude that appellant's privacy concerns or statutory obligations constituting business justification within scope of Act, s. 79(1)(b) — Tribunal concluding that little evidentiary support for appellant's contention that restrictions motivated by privacy, finding that privacy concerns pretext for appellant's adoption, maintenance of restrictions of brokers' "virtual office websites" (VOWs)-- Tribunal also examining nature, scope of consent clause in Listing Agreement appellant using; concluding that consents provided thereto effective — Role of Tribunal to interpret scope of consents under ordinary law of contract, as informed by PIPEDA — Tribunal doing so [page565] thus not erring in conclusion reached — Listing Agreement at issue containing clause governing use, distribution of information — PIPEDA only requiring new consent by clients where information used for new purpose, not where information distributed via new methods — Introduction of VOWs not new purpose --- Ground of appeal therefore failing.**

**Copyright — Appeal from two decisions of Competition Tribunal holding that certain of appellant's information-sharing practices preventing competition substantially in supply of residential real estate brokerage services in Greater Toronto Area raising copyright issues of real estate information in appellant's MLS database — Whether Act, s. 79(5) precluding appellant, intervener from advancing copyright claim in MLS database — In light of determination that appellant's virtual office website policy anti-competitive, Competition Act, s. 79(5) precluding reliance on copyright as defence to anti-competitive act — This holding sufficient to dispose of appeal in respect of copyright.**

**Summary:**

This was an appeal from two decisions of the Competition Tribunal holding that certain information-sharing practices of the appellant prevented competition substantially in the supply of residential real estate brokerage services in the Greater Toronto Area (GTA). The appellant maintains a database of information on current and previously available property listings in the GTA making some of this information available to its members via an electronic data feed. However, some data available in the database is not distributed via the data feed and can only be viewed and distributed through more traditional channels. The respondent said that this disadvantages innovative brokers who would prefer to establish virtual offices resulting in a substantial prevention or lessening of competition in violation of subsection 79(1) of the *Competition Act*. The appellant claimed in particular that the restrictions do not have the effect of substantially preventing or lessening competition and that such restrictions are due to privacy concerns.

[page566]

The appellant is a not-for-profit corporation and is Canada's largest real estate board. It operates an online system for collecting and distributing real estate information among its members. This "Multiple Listing Service" or MLS system is not accessible to the general public. Part of the MLS system is a database (the MLS database) of information on properties including current listings. Many brokers operate sections of their websites called "virtual office websites" or VOWs. The appellant's data feed delivers information to brokers to populate these sections of their websites. Importantly, not all information in the MLS database is included in the data feed. The respondent first applied to the Tribunal, under subsection 79(1) of the Act, for an order prohibiting certain behaviours relating to the appellant's restrictive distribution of digitized data, but this application was dismissed

by the Tribunal. However, on appeal, the matter was referred back for reconsideration. The Tribunal made an order granting in part the respondent's application and made another order on the issue of remedy. Those were the decisions under appeal herein.

The Tribunal concluded that the VOW restrictions had adversely affected non-price competition in the relevant market to a degree that was material. In particular, it stated that the aggregate adverse impact of the VOW restrictions on non-price competition had been substantial. It also found that the duration and scope of the restrictions was substantial. Thus, the Tribunal found that all three of the subsection 79(1) requirements had been met and that the VOW restrictions were substantially preventing competition for residential real estate brokerage services in the GTA. Turning to copyright, the Tribunal found that the appellant did not lead sufficient evidence to demonstrate copyright in the MLS database.

The issues were whether the Tribunal erred in finding that the appellant had substantially reduced competition within the meaning of subsection 79(1) of the Act; whether the Tribunal erred in failing to conclude that the appellant's privacy concerns or statutory obligations constituted a business justification within the scope of paragraph 79(1)(b) of the Act; and whether subsection 79(5) of the Act precluded the appellant and intervener from advancing a claim in copyright in the MLS database.

[page567]

*Held*, the appeal should be dismissed.

Subsection 79(1) of the Act sets out the three requirements necessary to establish an abuse of dominant position. Most of the appellant's arguments focussed on paragraphs 79(1)(b) and (c) of the Act. There was no dispute that the appellant's VOW policies constitute a practice in accordance with paragraph 79(1)(b). The Tribunal applied the correct framework respecting paragraph 79(1)(b), stating that it was looking for a predatory, exclusionary, or disciplinary effect on a competitor. The Tribunal found that the evidence of subjective anti-competitive intent and reasonably foreseeable exclusionary effects outweighed the very limited evidence that was adduced in support of the alleged legitimate business justifications that the appellant claimed underpinned the development and implementation of the VOW restrictions and its analysis was not unreasonable.

The requirements of paragraph 79(1)(c) were examined. The alleged anti-competitive practices in this case related to what the appellant does with some of the data from the MLS system and what it allows its members to do with this data. The Tribunal correctly understood the significance of the word "substantially" in paragraph 79(1)(c) and the test it had to apply in determining whether or not, on the facts of this case, the appellant's practice regarding the disputed data was a practice that had the effect of preventing competition substantially in the GTA. The respondent, in seeking a determination under subsection 79(1), did not have a legal obligation to quantify all effects which could be quantified. The Tribunal understood the difference in nature between quantitative and qualitative evidence. On the basis of the qualitative evidence put forward by the respondent, the Tribunal made findings of a number of anti-competitive effects caused by the VOW restrictions. It was the Tribunal's opinion that, "but for" the VOW restrictions, such anti-competitive effects would be considerably lower; it concluded that, when considered in the aggregate, these anti-competitive effects on non-price dimensions amounted to a substantial prevention of competition. The arguments of the appellant and intervener regarding the Tribunal's reliance on qualitative evidence were without merit. In relying on qualitative evidence for its findings of anti-competitive effects and its ultimate conclusion on substantiality, the Tribunal made no reviewable error and there was no basis to interfere with its determination under paragraph 79(1)(c) of the Act.

The appellant sought to justify its restriction on disclosure of the disputed data on the basis that the privacy concerns of vendors and purchasers constituted a business justification sufficient to escape liability under paragraph 79(1)(b) of the Act. It also asserted that it was required to comply with the *Personal Information Protection and Electronic Documents [page568] Act* (PIPEDA) contending that this statutory requirement constituted a business justification. However, the Tribunal concluded that there was little evidentiary support for the contention that the restrictions were motivated by privacy concerns of the appellant's clients. The Tribunal also found that the privacy concerns were a pretext for the appellant's adoption and maintenance of the VOW restrictions. Regarding the establishment of a business justification within the meaning of paragraph 79(1)(b), in

this case the Tribunal assessed the evidence before it according to the correct principles and found it lacking. It concluded that the appellant was motivated by a desire to maintain control over the disputed data in an effort to forestall new forms of competition and not by any efficiency, pro-competition, or genuine privacy concerns.

The Tribunal also examined the nature and scope of the consent clause in the Listing Agreement the appellant used and concluded that the consents were effective. The role of the Tribunal was to interpret the scope of the consents under the ordinary law of contract, as informed by the purpose and objectives of PIPEDA. This is what it did and there was no error in the conclusion reached.

PIPEDA requires that individuals consent to the collection, use, and disclosure of their personal information. The Listing Agreement at issue contained a clause governing the use and distribution of information. This clause was broad and unrestricted. Nothing in the text implied the data would only be used during the time the listing was active. PIPEDA only requires new consent where information is used for a new purpose, not where it is distributed via new methods. The introduction of VOWs was not a new purpose. There was nothing in the evidence that would suggest that the appellant considered that the consents were inadequate or that the appellant drew a distinction between the means of communication of information. When the consents were considered in light of the nature of the privacy interests involved, the Tribunal's conclusion that they were sufficient took on added strength. This ground of appeal therefore failed.

With respect to the issue of copyright in the MLS Database, the ground of appeal that the Tribunal erred in finding that the appellant did not have copyright in the database failed. In light of the determination that the VOW policy was anti-competitive, subsection 79(5) of the Act precludes reliance on copyright as a defence to an anti-competitive act. This was [page569] sufficient to dispose of the appeal in respect of copyright. Moreover, although the Tribunal applied the incorrect legal test to determine whether copyright exists, it was an error of no consequence.

## Statutes and Regulations Cited

*Competition Act*, R.S.C., 1985, c. C-34, ss. 78, 79, 92, 96(1).

*Competition Tribunal Act*, R.S.C., 1985 (2nd Supp.), c. 19, s. 13(1),(2).

*Competition Tribunal Rules*, SOR/2008-141, rr. 68(2), 69(2).

*Copyright Act*, R.S.C., 1985, c. C-42, ss. 2 "compilation", 5.

*Personal Information Protection and Electronic Documents Act*, S.C. 2000, c. 5, s. 6.1, Sch. 1, clauses 4.3.1, 4.3.2.

## Cases Cited

Followed:

*Tervita Corp. v. Canada (Commissioner of Competition)*, 2015 SCC 3, [2015] 1 S.C.R. 161.

Applied:

*Tervita Corporation v. Canada (Commissioner of Competition)*, 2013 FCA 28, [2014] 2 F.C.R. 352 (as to standard of review); *Canada (Commissioner of Competition) v. Canada Pipe Co.*, 2006 FCA 233, [2007] 2 F.C.R. 3, leave to appeal to S.C.C. refused [2007] 1 S.C.R. vii; *Canada (Director of Investigation and Research, Competition Act) v.*

*NutraSweet Co.* (1990), 32 C.P.R. (3d) 1, [1990] C.C.T.D. No. 17 (QL) (Comp. Trib.); *CCH Canadian Ltd. v. Law Society of Upper Canada*, 2004 SCC 13, [2004] 1 S.C.R. 339.

## Considered:

*The Commissioner of Competition v. The Toronto Real Estate Board*, 2013 Comp. Trib. 9, 2013 CACT 9 (CanLII); *Commissioner of Competition v. Toronto Real Estate Board*, 2014 FCA 29, 456 N.R. 373, leave to appeal to S.C.C. refused [2014] 2 S.C.R. ix; *Nadeau Poultry Farm Limited v. Groupe Westco Inc.*, 2011 FCA 188, 419 N.R. 333; *Tele-Direct (Publications) Inc. v. American Business Information, Inc.*, [1998] 2 F.C. 22 (1997), 154 D.L.R. (4th) 328 (C.A.), leave to appeal to S.C.C. refused [1998] 1 S.C.R. xv; *Pfizer Canada Inc. v. Teva Canada Limited*, 2016 FCA 161, 400 D.L.R. (4th) 723; *Ellis-Don Ltd. v. [page570] Ontario (Labour Relations Board)*, 2001 SCC 4, [2001] 1 S.C.R. 221; *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633; *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23; *Canada (Office of the Information Commissioner) v. Calian Ltd.*, 2017 FCA 135, 414 D.L.R. (4th) 165; *Investors Compensation Scheme v. West Bromwich Building Society*, [1997] UKHL 28, [1998] 1 All E.R. 98; *Teal Cedar Products Ltd. v. British Columbia*, 2017 SCC 32, [2017] 1 S.C.R. 688, 411 D.L.R. (4th) 385; *ING Bank N.V. v. Canpotex Shipping Services Ltd.*, 2017 FCA 47; *Royal Bank of Canada v. Trang*, 2016 SCC 50, [2016] 2 S.C.R. 412; *Édutile Inc. v. Automobile Protection Assn.*, [2000] 4 F.C. 195, (2000), 6 C.P.R. (4th) 211 (C.A.); *Red Label Vacations Inc. (redtag.ca) v. 411 Travel Buys Ltd. (411travelbuys.ca)*, 2015 FC 18, 473 F.T.R. 38; *Delrina Corp. (cob Carolian Systems) v. TrioletSystems Inc.* (2002), 58 O.R. (3d) 339, 17 C.P.R. (4th) 289, leave to appeal to S.C.C. refused, [2002] 4 S.C.R. v; *Harmony Consulting Ltd. v. G.A. Foss Transport Ltd.*, 2011 FC 340, 92 C.P.R. (4th) 6, affd 2012 FCA 226, 107 C.P.R. (4th) 1; *Geophysical Service Inc. v. Encana Corp.*, 2016 ABQB 230, 38 Alta. L.R. (6th) 48; *Distrimedic Inc. v. Dispill Inc.*, 2013 FC 1043, 440 F.T.R. 209.

Referred to:

*Canada (Commissioner of Competition) v. Superior Propane Inc.*, 2001 FCA 104, [2001] 3 F.C. 185; *CarGurus, Inc. v. Trader Corporation*, 2017 FCA 181; *Graat v. The Queen*, [1982] 2 S.C.R. 819, (1982), 144 D.L.R. (3d) 267; *Hunt (Litigation guardian of) v. Sutton GroupIncentive Realty Inc.* (2002), 60 O.R. (3d) 665, 215 D.L.R. (4th) 193 (C.A.); *Benhaim v. St-Germain*, 2016 SCC 48, [2016] 2 S.C.R. 352; *WIC Radio Ltd. v. Simpson*, 2008 SCC 40, [2008] 2 S.C.R. 420; *Edmonton (City) v. Edmonton East (Capilano) Shopping Centres Ltd.*, 2016 SCC 47, [2016] 2 S.C.R. 293.

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Bryant, Alan W. *et al. The Law of Evidence in Canada*, 4th ed. Markham, Ont.: LexisNexis Canada, 2014.

Delisle Ron *et al. Evidence: Principles and Problems*, 11th ed. Toronto: Thompson Reuters, 2015.

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**History and Disposition:**

APPEAL from two decisions (2016 Comp. Trib. 7; 2016 Comp. Trib. 8) of the Competition Tribunal holding that certain information-sharing practices of the appellant prevented competition substantially in the [page571] supply of residential real estate brokerage services in the Greater Toronto Area. Appeal dismissed.

**Appearances:**

*William V. Sasso*, *Jacqueline Horvat* and *Carol Hitchman* for appellant.

*John F. Rook Q.C.*, *Andrew D. Little* and *Emrys Davis* for respondent.

*Sandra A. Forbes* and *Michael Finley* for intervener.

**Solicitors of record:**

*Strosberg Sasso Sutts LLP*, Windsor, *Spark LLP* and *Gardiner Roberts LLP*, Toronto

for appellant.

*Bennett Jones LLP*, Toronto, for respondent.

*Davies Ward Phillips & Vineberg LLP*, Toronto, for intervener.

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*The following are the reasons for judgment rendered in English by*

## NADON AND RENNIE JJ.A.

I. Introduction

**1** This is a statutory appeal from two decisions of the Competition Tribunal (the Tribunal) which held that certain information-sharing practices of the Toronto Real Estate Board (TREB) prevented competition substantially in the supply of residential real estate brokerage services in the Greater Toronto Area (GTA): *The Commissioner of Competition v. The Toronto Real Estate Board*, *2016 Comp. Trib. 7* (Tribunal Reasons, TR) and *The Commissioner of Competition v. The Toronto Real Estate Board*, *2016 Comp. Trib. 8* (the order).

**2** TREB maintains a database of information on current and previously available property listings in the GTA. TREB makes some of this information available to its members via an electronic data feed, which its members can then use to populate their websites. [page572] However, some data available in the database is not distributed via the data feed, and can only be viewed and distributed through more traditional channels. The Commissioner of Competition says this disadvantages innovative brokers who would prefer to establish virtual offices, resulting in a substantial prevention or lessening of competition in violation of subsection 79(1) of the *Competition Act*, R.S.C., 1985, c. C-34 (*Competition Act*). TREB says that the restrictions do not have the effect of substantially preventing or lessening competition. Furthermore, TREB claims the restrictions are due to privacy concerns and that its brokers' clients have not consented to such disclosure of their information. TREB also claims a copyright interest in the database it has compiled, and that under subsection 79(5) of the *Competition Act*, the assertion of an intellectual property right cannot be an anti-competitive act.

**3** For the reasons that follow, we would dismiss the appeal.

II. Background and Procedural History

**4** TREB, the appellant, is a not-for-profit corporation incorporated under the laws of Ontario. With approximately 46 000 members, it is Canada's largest real estate board. TREB itself is not licensed to trade in real estate and does not do so.

**5** TREB operates an online system for collecting and distributing real estate information among its members. This "Multiple Listing Service" or MLS system is not accessible to the general public. Part of the MLS system is a database (the MLS database) of information on properties, including, *inter alia*: addresses, list prices, interior and exterior photographs, length of time for sale, whether the listing was withdrawn or expired, etc. The information is entered by TREB's member brokers into the system and appears almost instantly on the MLS database. When inputting information, some fields are mandatory and others are optional. The MLS database contains both current listings and an archive of [page573] inactive listings going back to 1986. TREB's members have full access to the database at any time.

**6** Many brokers operate sections of their websites where their clients can log in and view information, called "virtual office websites" or VOWs. TREB's data feed delivers information to brokers to populate these sections of their websites. Importantly, not all information in the MLS database is included in the data feed. Certain data is excluded (the "disputed data"). However, TREB's VOW Policy contains no restriction upon how its members can communicate the same disputed data to their clients through other delivery mechanisms. Consequentially, some information cannot be shared with clients in a VOW, but can be shared with them by other methods, such as in person, by email, or by fax.

**7** In May 2011, the Commissioner first applied to the Tribunal, under subsection 79(1) of the *Competition Act*, for an order prohibiting certain behaviours related to TREB's restrictive distribution of digitized data. The Commissioner alleged that TREB's policies excluded, prevented, or impeded the emergence of innovative business models and service offerings in respect of the supply of residential real estate brokerage services in the GTA.

**8** In April 2013, the Tribunal dismissed the Commissioner's application, finding that the abuse of dominance provisions of the *Competition Act* could not apply to TREB because, as a trade organization, TREB did not compete with its members (*The Commissioner of Competition v. The Toronto Real Estate Board*, *2013 Comp. Trib. 9*, 2013 CACT 9 (CanLII)). However, on appeal in February 2014, this Court set aside the Tribunal's order and referred the matter back for reconsideration, finding that subsection 79(1) of the *Competition Act* could apply to TREB (*Commissioner of Competition v. Toronto Real Estate Board*, *2014 FCA 29*, [page574] *456 N.R. 373* (*TREB FCA 1*), leave to appeal to S.C.C. refused, 35799 (24 July 2014) [2014] 2 S.C.R. ix]).

**9** The matter was reconsidered by a different panel of the Tribunal in the fall of 2015. On April 27, 2016, the Tribunal issued its reasons on the merits and made an order granting, in part, the Commissioner's application (*The Commissioner of Competition v. The Toronto Real Estate Board*, *2016 Comp. Trib. 7* [cited above]). The issue of remedy was the subject of a further hearing and order of the Tribunal on June 3, 2016 (*The Commissioner of Competition v. The Toronto Real Estate Board*, *2016 Comp. Trib. 8* [cited above]). Those two decisions are now on appeal before this Court.

**10** The intervener in this case is the Canadian Real Estate Association (CREA), a national organization representing the real estate industry in Canada. TREB is a member of CREA. CREA owns the MLS trademarks. The MLS system is operated by local boards (in this case, by TREB) under license from CREA.

## III. The Tribunal Decision

**11** The Tribunal first addressed the abuse of dominance issue by defining the relevant market to be "the supply of MLS-based residential real estate brokerage services in the GTA" (TR, at paragraph 161). The Tribunal then addressed the three-part test in subsection 79(1) of the *Competition Act*. For ease of reference, we reproduce the

provision here:

> **Prohibition where abuse of dominant position**
>
> **79 (1)** Where, on application by the Commissioner, the Tribunal finds that
>
> **(a)** one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,
>
> **(b)** that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and
>
> [page575]
>
> **(c)** the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market,
>
> the Tribunal may make an order prohibiting all or any of those persons from engaging in that practice.

**12** The Tribunal found that TREB "substantially or completely controls the supply of MLS-based residential real estate brokerage services in the GTA" and therefore the terms of paragraph 79(1)(a) were met (TR, at paragraph 162).

**13** With respect to paragraph 79(1)(b), the Tribunal found that TREB had engaged in, and continued to engage in a practice of anti-competitive acts (TR, at paragraph 454). TREB took the position that its actions were motivated by concern for the privacy of real estate buyers' and sellers' information, and that this concern constituted a legitimate business justification for the VOW restrictions which had to be balanced against the evidence of anti-competitive intent (TR, at paragraphs 21, 285-287 and 321).

**14** In this context, the Tribunal found TREB's concern with privacy to be unpersuasive. We will turn to this issue in greater detail later in these reasons; suffice to say at this point that, looking at the record before it, the Tribunal found little evidence that TREB's VOW committee had considered or acted upon privacy concerns before establishing TREB's VOW Policy (TR, at paragraphs 321, 360 and 390).

**15** Turning to paragraph 79(1)(c), the Tribunal found that the VOW restrictions prevented competition substantially in the market. After describing this branch of the test (TR, at paragraphs 456-483), the Tribunal adopted a "but for" approach to this analysis, comparing the real world with the hypothetical world in which the VOW restrictions did not exist. Thus, in the Tribunal's view, it was the burden of the Commissioner to adduce evidence to prove "a substantial difference between the level of actual or likely competition in the relevant [page576] market in the presence of the impugned practice and the level of competition that likely would have prevailed in the absence of that practice" (TR, at paragraph 482).

**16** In describing the applicable test, the Tribunal made the point that the Commissioner could bring either quantitative or qualitative evidence, or both, to meet his burden. Because of its view that "dynamic competition is generally more difficult to measure and to quantify", there may be a greater need for the Commissioner to rely on qualitative evidence. This is particularly so in innovation cases. However, the Tribunal also recognized "that it may be more difficult to meet this burden when the Commissioner relies largely on qualitative evidence" (TR, at paragraphs 471 and 470).

**17** After reviewing the parties' submissions on the evidence with respect to a lessening of competition (TR, at paragraphs 484-499), the Tribunal noted that "there is a high degree of competition in the Relevant Market, as reflected in considerable ongoing entry and exit, a significant degree of discounting activity with respect to net

commissions, and a significant level of ongoing technological and other innovation, including with respect to quality and variety and through Internet-based data-sharing vehicles" (TR, at paragraph 501).

**18** Nonetheless, in addressing the "but for" question, the Tribunal found that the VOW restrictions prevented competition in five ways: by increasing barriers to entry and expansion; by increasing costs imposed on VOWs; by reducing the range of brokerage services available in the market; by reducing the quality of brokerage service offerings; and by reducing innovation (TR, at paragraphs 505-619).

**19** However, the Tribunal found that the Commissioner had failed to prove that the VOW restrictions were preventing competition in three other manners: by reducing downward pressure on broker commission rates; by reducing output; and by maintaining incentives [page577] for brokers to steer clients away from inefficient transactions (TR, at paragraphs 620-638).

**20** After satisfying itself that the VOW restrictions were preventing competition in five ways, the Tribunal then addressed the substantiality of those anti-competitive effects. Turning first to magnitude and degree, the Tribunal framed the question as whether "full-information VOW brokerages likely would be hired by significantly more clients as a real estate brokerage, but for' the *aggregate impact* of the three components of TREB's practice of anti-competitive acts" as a result of being able to display the disputed data (TR, at paragraph 646 (emphasis in original)).

**21** TREB had argued that without conversion of website viewers into clients, the popularity of a website was irrelevant (TR, at paragraphs 645 and 648). However, the Tribunal found that website innovation could also be relevant if it spurred other competitors to compete (TR, at paragraph 649).

**22** After noting that the Commissioner had failed to conduct an empirical assessment with regard to local markets where sold information (the final price at which a house sold) was available through VOWs and other local markets where such information was not available through VOWs, the Tribunal declined to draw the adverse inference against the Commissioner which TREB argued it should draw. The Tribunal noted that "as a statutory authority, the Commissioner has to be prudent with, and make difficult decisions regarding the allocation of, the limited public funds available for administering and enforcing the Act at any given time" (TR, at paragraph 656).

**23** The Tribunal also considered, in refusing to draw the inference, the fact that the Commissioner's expert, Dr. Vistnes, had advised the Commissioner that an [page578] empirical assessment would be costly, difficult, and of little value. Notwithstanding its refusal to draw the adverse inference sought by TREB, the Tribunal made it clear that the Commissioner continued to bear the burden of proving that the required elements of his application were met which "may well be a more challenging task in the absence of quantitative evidence" (TR, at paragraph 656).

**24** The Tribunal then stated that it was prepared to draw an adverse inference against the Commissioner in regard to the testimony of two of its witnesses, Messrs. Nagel and McMullin, whose brokerages (respectively Redfin Corporation and Viewpoint Realty Services Inc.) conducted business in areas where the disputed data was available and in other areas where such data was not available (Nova Scotia and parts of the United States). Because neither witness presented evidence with regard to these other markets, the Tribunal inferred that the conversion rates of those websites would not be helpful to the Commissioner's case. However, the Tribunal then noted that it would not give much weight to its inference because of Dr. Vistnes' opinion that the low conversion rates could be the result of local differences in the relevant markets.

**25** The Tribunal also commented that "even a limited comparison between one local U.S. market where sold information is available and one local U.S. market where such information is not available may have been at least somewhat helpful", adding that the same comment applied to Nova Scotia with respect to pending sold prices. The Tribunal also commented that the absence of such a comparison made its task with regard to the "substantiality" element of paragraph 79(1)(c) much more difficult. The Tribunal concluded by saying that the absence of such comparison "resulted in this case being much more of a close call,' than it otherwise may have been" (TR, at paragraph 658).

**26** However, the Tribunal highlighted the little weight it gave to the low conversion rates [TR, at paragraph 662]:

[page579]

> The Tribunal does not accord much significance to the fact that the low conversion rates of firms such as ViewPoint, Redfin and TheRedPin suggest that many consumers are evidently treating the information available on their websites as complements to the information available from the (different) broker they ultimately use to list or purchase their home. The fact remains that the innovative tools, features and other services available on those websites is assisting them to compete, and is forcing traditional brokerages to respond.

In other words, if we understand the Tribunal correctly, it was not prepared to, in effect, give any weight to the fact that the conversion rates of ViewPoint, Redfin, and TheRedPin were not significant. However, later in its reasons, the Tribunal makes the finding that if the disputed data were available to these firms in the GTA, they likely would have been successful in converting "an increasing and significant number of website users into clients." Paragraph 676 reads:

> The Tribunal concludes that being able to obtain sold information from the VOW Data Feed, and to work with that data as they see fit, would likely enable full-information VOWs, including ViewPoint and those such as TheRedPin who would like to become full-information VOWs, to convert an increasing and significant number of website users into clients.

**27** Then, in dealing with the issue of qualitative evidence, the Tribunal made six observations based on the evidence adduced on behalf of the Commissioner [TR, at paragraphs 666-670 and 672]:

> First ... the Disputed Data is very important, if not critical, in assisting Internet-based brokerages to distinguish themselves from incumbent traditional brokerages....
>
> Second, home purchasers and sellers value being able to obtain information with respect to sold prices, the conditional sale status of homes in the market, firm "pending sold" information, [withdrawn, expired, suspended or terminated] listings and cooperating broker commissions *prior to* meeting with their broker/agent, or [page580] in any event *prior to* finalizing the listing price of their homes or making an offer on a home.
>
> Third, an inability to display and use the Disputed Data to develop innovative products has been preventing, and is likely to continue to prevent, ViewPoint from entering the Relevant Market. This has also prevented Realosophy and TheRedPin from growing as much as they likely would have grown .... this also prevented Sam & Andy from expanding within the Relevant Market, and prevented their brokerage customers from doing the same.
>
> Fourth, ViewPoint, Realosophy and TheRedPin are Internet-based innovative brokerages that, in aggregate, likely would have introduced a considerably broader range of brokerage services, increased the quality of some important services (such as CMAs), benefited from lower operating costs and considerably increased the overall level of innovation in the Relevant Market, "but for" the VOW Restrictions. ...
> Fifth, the VOW Restrictions have erected barriers to the entry and expansion of innovative brokers in the Relevant Market....
>
> ...
>
> Sixth, the VOW Restrictions have stifled innovation in the supply of Internet-based real estate brokerage services in the GTA. [Emphasis in original.]

**28** The Tribunal then discussed the importance of the disputed data fields to brokers and consumers, finding that sold data, pending and conditional solds, and withdrawn, expired, suspended or terminated listings were valued by home buyers and sellers (TR, at paragraphs 675-685). In the Tribunal's opinion, making cooperating broker commissions available would also increase transparency in the market and would allow brokers to distinguish themselves by providing more information (TR, at paragraphs 686-690).

[page581]

**29** The Tribunal then reviewed counterarguments to its above findings. The Tribunal did not find significant that some VOW operators in Nova Scotia, which does not have any VOW restrictions, had abandoned their VOWs (TR, at paragraph 693). Likewise, the Tribunal did not find significant the fact that statistics from the National Association of Realtors in the United States indicated that customers did not value the disputed data fields that highly (TR, at paragraphs 694-696). The Tribunal noted that in the United States, where sold information was "widely displayed by competitor websites", the National Association of Realtors had started displaying sold information on what appeared to be its official website (TR, at paragraph 700). In addition, the Tribunal was satisfied that the fact that brokers displayed the disputed data when permitted indicated that that information was of value to home buyers; otherwise brokers would not display it (TR, at paragraph 701).

**30** The Tribunal stated its conclusion on the magnitude of the effect of the VOW restrictions on competition in the following way [TR, at paragraph 702]:

> For the reasons set forth above, the Tribunal concludes that the VOW Restrictions have adversely affected non-price competition in the Relevant Market to a degree that is material. Indeed, the Tribunal concludes that the aggregate adverse impact of the VOW Restrictions on non-price competition has been substantial, having regard to the considerable negative effect on the range of brokerage services, the negative effect on the quality of service offerings, and the considerable adverse impact on innovation in the Relevant Market. In the absence of an order, this substantial adverse impact is likely to continue. The Tribunal has reached this conclusion despite the fact that, the quantitative evidence on commission rates does not indicate that net commissions for real estate brokerage services were, are or likely would be, materially higher than in the absence of the VOW Restrictions. [Emphasis added.]

**31** Then, turning to duration and scope, the Tribunal found that, as the VOW restrictions had been in place since 2011, the duration was substantial. Likewise, as the effects were present throughout the GTA, a substantial part of the market was impacted (TR, at paragraphs 703-704).

[page582]

**32** Thus, the Tribunal found that all three of the subsection 79(1) requirements had been met and that the VOW restrictions were substantially preventing competition for residential real estate brokerage services in the GTA. At paragraphs 705 to 715 of its reasons, the Tribunal summarized its views on the three elements of subsection 79(1).

**33** Turning to copyright, the Tribunal found that TREB did not lead sufficient evidence to demonstrate copyright in the MLS database. Copyright in a database exists where the "selection or arrangement of data" is original (TR, at paragraph 732). The Tribunal found that TREB's evidence did not speak to skill and judgment in compiling the database, but rather illustrated that it was a more mechanical exercise. The Tribunal pointed to many facts including: TREB did not present witnesses on the arrangement of the data; a third party corrects errors in the

database; contracts referencing copyright are not evidence that copyright exists; members provide the information which is uploaded "almost instantaneously" to the database; TREB's database is in line with industry norms across Canada; and creating rules on accuracy and quality of the information does not reflect the originality of the work (TR, at paragraph 737).

**34** In the alternative, the Tribunal found that, even if TREB had copyright in the database, it would not enjoy the protection offered by subsection 79(5) because TREB's conduct amounted to more than the "mere exercise" of its intellectual property rights (TR, at paragraphs 720-721 and 746-758).

## IV. Issues

**35** In order to dispose of this appeal, we must determine the three following issues:

1. Did the Tribunal err in finding that TREB had substantially reduced competition within the [page583] meaning of subsection 79(1) of the *Competition Act*?
2. Did the Tribunal err in failing to conclude that TREB's privacy concerns or statutory obligations constituted a business justification within the scope of paragraph 79(1)(b)?
3. Does subsection 79(5) of the *Competition Act* preclude TREB and CREA from advancing a claim in copyright in the MLS database? If not, did the Tribunal err in its consideration of TREB's claim of copyright?

## V. Analysis

### A. *Standard of Review*

**36** Before addressing the three issues, a few words on the standard of review are necessary.

**37** There is a statutory right of appeal to this Court from decisions of the Tribunal. Subsection 13(1) of the *Competition Tribunal Act*, R.S.C., 1985 (2nd Supp.), c. 19 (*Competition Tribunal Act*) provides that any decision or order can be appealed "as if it were a judgment of the Federal Court." In *Tervita Corporation v. Canada (Commissioner of Competition)*, 2013 FCA 28, [2014] 2 F.C.R. 352 (*Tervita FCA*), our Court held that questions of law arising from decisions of the Tribunal were to be reviewed on the standard of correctness (TR, at paragraphs 53-59; see also *Canada (Commissioner of Competition) v. Superior Propane Inc.*, 2001 FCA 104, [2001] 3 F.C. 185, at paragraph 88). That determination was upheld by the Supreme Court of Canada in *Tervita Corp. v. Canada (Commissioner of Competition)*, 2015 SCC 3, [2015] 1 S.C.R. 161 (*Tervita SCC*).

**38** As to questions of mixed fact and law, the Supreme Court in *Tervita SCC* also upheld this Court's [page584] determination in *Tervita FCA* that such questions were to be determined on the standard of reasonableness. With regard to questions of fact, leave of this Court is required (*Competition Tribunal Act*, subsection 13(2)). In the present matter, no such leave was sought and consequently we cannot interfere with the Tribunal's findings of fact (see *CarGurus, Inc. v. Trader Corporation*, 2017 FCA 181, at paragraph 17; *Nadeau Poultry Farm Limited v. Groupe Westco Inc.*, 2011 FCA 188, 419 N.R. 333 (*Nadeau Poultry Farm*), at paragraph 47).

### B. *Substantial Reduction in Competition*

#### (1) TREB's and CREA's Submissions

**39** TREB submits that the Tribunal erred in finding that the test under subsection 79(1) of the *Competition Act* was made out. In its view, the Commissioner bore the burden of proving each element of the test and did not discharge that burden on any of the three elements.

**40** TREB asserts that since it does not control the relevant market, paragraph 79(1)(a) has not been established.

**41** TREB submits that it did not act with the necessary anti-competitive purpose, therefore the Tribunal erred in finding that paragraph 79(1)(b) was made out. In its view, the VOW Policy was meant to allow its members to offer VOWs and thus reach a greater range of potential buyers. The exclusion of some data from the data feed was made for legitimate privacy related reasons.

**42** With respect to paragraph 79(1)(c), TREB submits that the Tribunal erred in accepting speculative qualitative evidence. Actual quantitative evidence was available and should have been brought forward by the Commissioner. His failure to do so should have led the Tribunal to make an adverse inference against him. CREA, the intervener, agrees with TREB's submissions on these three points.

[page585]

**43** CREA further argues that the Tribunal read out, for all intents and purposes, the requirement of "substantiality" from the subsection 79(1) test. In its view, statements by brokers are insufficient to establish that access to the disputed data would increase competition substantially. While access to the disputed data may help brokers improve their services, this is not equivalent to a competitive benefit. CREA points to other evidence it claims demonstrates that brokers operating with the current VOW data feed are equally or more competitive than those with access to more data. Furthermore, CREA asserts that there is no proven link between broker success and receiving more data.

(2) The Commissioner's Submissions

**44** The Commissioner asserts that TREB's policies regarding the disputed data comprise at least three acts that constitute an anti-competitive practice, as quoted by the Tribunal at paragraph 320 of its reasons:

i. The exclusion of the Disputed Data from TREB's VOW Data Feed;

ii. Provisions in TREB's VOW Policy and Rules that prohibit Members who want to provide services through a VOW from using the information included in the VOW Data Feed for any purpose other than display on a website; and

iii. Prohibiting TREB's Members from displaying certain information, including the Disputed Data, on their VOWs.... This prohibition is reinforced by terms in TREB's Data Feed Agreement that limit the use of the MLS data in the VOW Data Feed to a purpose that is narrower than the corresponding provision in the [authorized user agreement] that applies to Members using the Stratus system.

**45** In other words, the Commissioner argues that it is anti-competitive to prohibit the disputed data from being distributed via the data feed.

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**46** The Commissioner further submits that the Tribunal's paragraph 79(1)(b) analysis is reasonable, entitled to deference, and supported by the evidence. The Tribunal applied the correct legal test, and its finding regarding TREB's purpose in implementing the VOW restrictions is one of fact, and therefore not reviewable on this appeal. In the alternative, the Commissioner submits that the facts indicate that the Tribunal's finding on this point was reasonable. The Tribunal looked at the evidence as a whole and determined that, while privacy concerns were

mentioned at TREB's VOW taskforce meetings, they were not a principal motivating factor. Furthermore, this finding turned on a credibility assessment of the testimony of Mr. Richardson, TREB's CEO, which is entitled to deference.

**47** Regarding paragraph 79(1)(c), the Commissioner submits that the Tribunal once again applied the correct legal test. TREB and CREA misstate the law when they say that the Commissioner must provide quantitative evidence to prove a substantial lessening or prevention of competition. In the Commissioner's view, this position is not supported by the case law. The Commissioner differentiates *Tervita SCC*, which found quantification necessary for a merger test under a different section of the *Competition Act*, namely subsection 96(1). Indeed, according to the Commissioner, non-price effects such as service quality, range of products, and innovation are not amenable to quantification. The Commissioner submits that TREB and CREA are de facto arguing that he has a legal burden to quantify the substantial lessening or preventing of competition. In addition, the Commissioner says that the Tribunal's refusal to draw an adverse inference against him on this point is entitled to deference.

(3) The Abuse of Dominance Framework

**48** Subsection 79(1), which is reproduced at paragraph 11 above, sets out the three requirements necessary to establish an abuse of dominant position. The [page587] Commissioner bears the burden of establishing each of these elements (*Canada (Commissioner of Competition) v. Canada Pipe Co.*, 2006 FCA 233, [2007] 2 F.C.R. 3, 268 D.L.R. (4th) 193 (*Canada Pipe*), at paragraph 46, leave to appeal to S.C.C. refused, 31637 (10 May 2007) [2007] 1 S.C.R. vii]).The burden of proof with respect to each element is the balance of probabilities (*Canada Pipe*, at paragraph 46; TR, at paragraph 34).

**49** Once the Commissioner establishes each element of subsection 79(1), the person or persons against whom the Commissioner's proceedings are directed, in this case TREB, can avoid sanction if they demonstrate that the impugned practice falls under one of the statutory exemptions. The only provision relevant to this case is subsection 79(5) of the *Competition Act*, which states that "an act engaged in pursuant only to the exercise of any right or enjoyment of any interest" derived under certain legislation pertaining to intellectual or industrial property, including the *Copyright Act*, R.S.C., 1985, c. C-42 (*Copyright Act*), is not an anti-competitive act.

**50** TREB says, in its written submissions, that it "does not control the relevant market(s)" (TREB's memorandum of fact and law, at paragraph 66). However, this is the extent of its submissions on the issue. As TREB's substantive arguments clearly focus on paragraphs 79(1)(b) and (c), we continue on to examine in more depth the requirements of those provisions.

(4) Paragraph 79(1)(b)

**51** Paragraph 79(1)(b) requires that the person or persons "have engaged in or are engaging in a practice of anti-competitive acts". There is no dispute that TREB's VOW policies constitute a practice. An indicative list of anti-competitive acts is provided in the *Competition Act* at section 78. None of those acts are directly relevant to this appeal. However, that list is non-exhaustive.

**52** This Court in *Canada Pipe* found that an anti-competitive act is defined by reference to its purpose. Drawing on the Tribunal's decision in *Canada [page588] (Director of Investigation and Research, Competition Act) v. NutraSweet Co.* (1990), 32 C.P.R. (3d) 1 (Comp. Trib.) (*NutraSweet*), this Court said that the requisite purpose is "an intended predatory, exclusionary or disciplinary negative effect on a competitor" (*Canada Pipe*, at paras. 66 and 74. See also *NutraSweet*, at page 34).

**53** To be more precise, *NutraSweet* pointed out that the "purpose common to all acts [listed in section 78], save that found in paragraph 78(f), is an intended negative effect on a competitor that is predatory, exclusionary or disciplinary" (at page 34). Indeed, paragraph 78(1)(f) cannot apply to a competitor, as it reads:

**Definition of anti-competitive act**

> **78 (1)** For the purposes of section 79, ***anti-competitive act***, without restricting the generality of the term, includes any of the following acts:
>
> ...
>
> **(*f*)** buying up of products to prevent the erosion of existing price levels.

**54** In *TREB FCA 1*, Sharlow J.A. determined that the "on the competitor" language from *NutraSweet* and *Canada Pipe* could not mean "on a competitor of the person accused of anti-competitive practices" (at paragraphs 19-20). On that premise, requiring a predatory, exclusionary, or disciplinary negative effect on a competitor in all cases would render paragraph 78(1)(f) meaningless. Paragraph (f) reflects a self-serving intent, not a relative one intended to harm a competitor. Yet it has been defined by Parliament to constitute an anti-competitive act.

**55** With this in mind, we believe that the Tribunal applied the correct framework with respect to paragraph 79(1)(b). The Tribunal stated that it was looking for a predatory, exclusionary, or disciplinary effect on a competitor (TR, at paragraph 272). Acting on the direction given by *TREB FCA 1*, the Tribunal defined [page589] competitor to mean "*a person who competes in the relevant market, or who is a potential entrant into that market*" and not a "competitor" of TREB (TR, at paragraph 277 [emphasis in original]).

**56** The Tribunal correctly noted that subjective or objective intent could be used to demonstrate the requisite intent (TR, at paragraphs 274 and 283; *Canada Pipe*, at paragraph 72). It closely scrutinized the evidence of TREB's subjective intent (TR, at paragraphs 319-431). The Tribunal also looked to the "reasonably foreseeable or expected objective effects of the act (from which intention may be deemed ...)" (TR, at paragraphs 432-451) as instructed by *Canada Pipe*, at paragraph 67 (see also *Tele-Direct (Publications) Inc. v. American Business Information, Inc.*, *[1998] 2 F.C. 22* *154 D.L.R. (4th) 328* (C.A.) (*Tele-Direct*), leave to appeal refused, 26403 (21 May, 1998) [1998] 1 S.C.R. xv]). The Tribunal conducted a balancing exercise between the exclusionary effects (evidenced by subjective intent) and TREB's alleged legitimate business justifications (TR, at paragraphs 319-431; *Canada Pipe*, at paragraph 73).

**57** The application of this test to the facts is a question of mixed law and fact. Ultimately, the Tribunal found that "the evidence of subjective anti-competitive intent and reasonably foreseeable exclusionary effects outweighs the very limited evidence that was adduced in support of the alleged legitimate business justifications that TREB claims underpinned the development and implementation of the VOW Restrictions" (TR, at paragraph 452). This is a very fact-driven analysis. The Tribunal weighed the evidence, heard competing witnesses, and made findings of credibility. We see no error that would make this analysis unreasonable.

(5) Paragraph 79(1)(c)

**58** Paragraph 79(1)(c) requires that "the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market" (underlining added). The market in question is not [page590] contested. The Tribunal defined the market to be "the supply of MLS-based residential real estate brokerage services in the GTA" (TR, at paragraph 161). We now turn to address the five other elements, as underlined above, in turn.

(a) **The Practice**

**59** The Commissioner's notice of application was filed in May 2011, before TREB's current VOW Policy and Rules were in place. In November 2011, TREB enacted its new rules. The Commissioner accordingly amended her statement of claim. Nonetheless, the statement of claim remains broadly worded and does not specify which particular parts of TREB's rules and policies the Commissioner is impugning.

**60** The alleged anti-competitive practices relate to what TREB does with some of the data from the MLS system

and what TREB allows its members to do with this data. This "disputed data" is defined by the Tribunal, at paragraph 14 of its reasons, to include four types of information:

* sold data
* pending sold data

* withdrawn, expired, suspended, or terminated listings (WESTs)

* offers of commission to the successful home buyer's real estate broker, also called the cooperating broker.

The utility of this data is described in the Tribunal's reasons at paragraphs 675 to 691, which fall within the "Substantiality" section of the reasons.

**61** The parties' submissions and the evidence centred almost entirely on three particular practices, which the Tribunal collectively refers to as the "VOW Restrictions" (TR, at paragraph 14). Those practices were the focus of the Tribunal's reasons and, after [page591] separate written and oral submissions on remedy, these restrictions remained the focus of the Tribunal's order. The following chart provides an overview of the restrictions, as listed in the Tribunal's reasons, at paragraph 14, and their sources.

| Restriction | Source |
|---|---|
| The exclusion of the disputed data from the VOW Datafeed | Policy articles 17, 15, 24 |
| The prohibition on the display of the disputed data on a VOW | Rule 823; Datafeed Agreement clause 6.3(a) |
| The prohibition on the use of the VOW Datafeed information for any purpose other than display on a website | Datafeed Agreement clause 6.2(f), (g) |

**62** It is worth noting that the following TREB rules and policies are not affected by the Tribunal's order.

| Restriction | Source |
|---|---|
| An individual needs the permission of their broker of record to establish a VOW | Datafeed Agreement clause 6.3(g) |
| Before viewing listing information on a VOW, a | Rules 805, 809(i), (iii) |

| | |
|---|---|
| consumer must enter a lawful broker-consumer relationship with the brokerage; this includes agreeing to terms and conditions acknowledging entering into such a relationship and declaring that the consumer has a bona fide interest in the purchase, sale or lease of residential real estate | Policy articles 1, 6, 7(iii) |

[page592]

| Restriction | Source |
|---|---|
| An individual needs the permission of their broker of record to establish a VOW | Rules 828, 829 |

(b) **Temporal Requirement**

**63** The temporal aspect of paragraph 79(1)(c) is not in issue. The effect on competition can be past, present, or future (*Canada Pipe*, at paragraph 44) The Tribunal found that the VOW restrictions had anti-competitive effects in the past, present and future (TR, at paragraph 706).

**64** A duration of two years will usually be sufficient to establish an effect (*Tervita FCA*, at paragraph 85). Here, TREB's VOW restrictions came into force in November 2011 and the Tribunal found the anti-competitive effects had been occurring for a substantial period of time (TR, at paragraphs 703 and 708).

(c) **Preventing or Lessening**

**65** Paragraph 79(1)(c) refers to either a prevention and/or lessening of competition. The Tribunal found a prevention of competition (TR, at paragraph 705). This means that there is no past time that the Tribunal can look at to compare with the present: the Tribunal must look at the present state of competition compared to a hypothetical world in which the VOW restrictions did not exist. This approach is not contested.

(d) **Competition**

**66** Paragraph 79(1)(c) looks to the level of competition, as opposed to any effects of the behaviour on competitors (*Canada Pipe*, at paragraphs 68-69). A "but for" inquiry is an acceptable method of analysis (*Canada Pipe*, at

paragraphs 39-40). This is a relative [page593] assessment: the current intensity of competition is not relevant in isolation.

**67** Two questions must be asked regarding the nature of the competition element. The first is: competition for what? Here, the relevant competition is over real estate brokerage clients (TR, at paragraphs 645-646). It is important to distinguish this competition from other, related, competition: for example, all websites want to attract web traffic in order to compete for advertising dollars.

**68** Second, we must ask: competition between whom? This case is about competition in the "the supply of MLS-based residential real estate brokerage services in the GTA" (TR, at paragraph 161). In order to supply MLS-based services, a broker must be a member of TREB. Therefore, we are really discussing competition between segments of TREB members.

**69** The use of imprecise terminology sometimes makes it difficult to distinguish between competing TREB members. The Tribunal uses the terms "full information VOW-based brokerages" or "full information VOW brokerages" in contrast to "traditional bricks-and-mortar' brokerages." The Commissioner uses the terms "genuine VOWs" and "innovative brokers" in contrast to "VOWs." Dr. Vistnes, the Commissioner's expert witness, uses the terms "innovative VOW-based brokers" or "VOW-based brokers" in contrast with "traditional brick-and-mortar brokers".

**70** However, for the purpose of the legal analysis required by paragraph 79(1)(c), the current competition between any two groups is not important per se. Rather, it is the general competition in the defined market between all participants now (with the VOW restrictions) and in the hypothetical "but for" world (without the VOW restrictions).

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(e) **Substantiality**

**71** The final element requiring elaboration is substantiality: the difference between the present and "but for" worlds must be substantial (*Canada Pipe*, at paragraph 36). In its reasons, the Tribunal addressed substantiality in a separate section of its reasons (TR, at paragraphs 640-704).

(i) Overview of the Evidence on Paragraph 79(1)(c)

**72** There were eight expert reports in evidence before the Tribunal, four from the initial hearing in 2012 and four from the redetermination hearing in 2015.

**73** Generally, the Tribunal found the evidence of the Commissioner's expert Dr. Vistnes to be credible and persuasive. However, on the particular issue of 79(1)(c) the Tribunal found that his evidence had missed the mark, saying that "Dr. Vistnes did not have a good understanding of the legal test for what constitutes a substantial' prevention or lessening of competition, as contemplated by paragraph 79(1)(*c*) of the Act. For this reason, the Tribunal refrained from accepting Dr. Vistnes' evidence on that particular issue" (TR, at paragraph 108).

**74** The Tribunal found Dr. Church, called by TREB, "to be less forthright, objective and helpful than Dr. Vistnes or Dr. Flyer." The Tribunal also found Dr. Church "to be evasive at several points during his cross-examination and to have made unsupported, speculative assertions at various points in his testimony and in his written expert reports" (TR, at paragraph 109). Dr. Church's evidence on the issue of whether the prevention of competition was "substantial" is neither referred to nor mentioned in the Tribunal's reasons.

**75** The Tribunal found Dr. Flyer, called by CREA, to be generally objective and forthcoming. However, it also found that "his testimony often remained general and high-level, and that he did not immerse himself in [page595] the details of the Canadian real estate industry and in the specific evidence and matters at issue in this proceeding to the same degree as Dr. Vistnes and Dr. Church" (TR, at paragraph 110) (We note, parenthetically, that given the Tribunal's view of Dr. Church's evidence, the criticism of Dr. Flyer on the basis that his evidence was not as detailed as Dr. Church is somewhat incongruous.) Dr. Flyer focused on the economic impact of the requested remedy on CREA, with considerable attention to the impact on CREA's trademarks. In our view, his reports are of little help in analyzing paragraph 79(1)(c).

**76** In addition, there are a total of 23 witness statements from 15 witnesses. The names and the firms of the witnesses whose testimonies (and statements) are most relevant to the Tribunal's determination of substantial prevention of competition are the following:

* William McMullin, Chief Executive Officer of ViewPoint Realty Services Inc. (Viewpoint)

* Shayan Hamidi and Tarik Gidamy, co-founders of TheRedPin.com Realty Inc. (TheRedPin)

* Joel Silver, Managing Director of Trilogy Growth, LP (Trilogy)

* Mark Enchin, Sales Representative of Realty Executives Plus Ltd. (Realty Executives)

* Scott Nagel, Chief Executive Officer of Redfin Corporation (Redfin)

* Sam Prochazka, Chief Executive Officer of Sam & Andy Inc. (Sam & Andy)

* Urmi Desai and John Pasalis, co-founders of Realosophy Realty Inc. (Realosophy)

**77** TREB and CREA do not challenge the admissibility of the statements and testimonies of the lay witnesses on which the Tribunal relies for the findings which form the basis of its conclusion that the [page596] anti-competitive effects resulting from the VOW restrictions lead, or are likely to lead, to a substantial prevention of competition in the GTA. Nevertheless, we believe that some guidance with respect to the evidence of lay witnesses in the context of a case like the one now before us might be useful.

**78** Generally, the evidence of lay witnesses is limited to facts of which they are aware (David Paciocco and Lee Stuesser, *The Law of Evidence*, 7th ed. (Toronto: Irwin Law, 2015) at page195; Ron Delisle *et al.*, *Evidence: Principles and Problems*, 11th ed. (Toronto: Thompson Reuters, 2015), at page 874). This principle is reflected in subrules 68(2) and 69(2) of the *Competition Tribunal Rules*, SOR/2008-141, which are identical, and read "[u]nless the parties otherwise agree, the witness statements shall include only fact evidence that could be given orally by the witness together with admissible documents as attachments or references to those documents."

**79** However, opinion evidence from lay witnesses is acceptable in limited circumstances: where the witness is in a better position than the trier of fact to form the conclusions; the conclusions are ones that a person of ordinary experience can make; the witnesses have the experiential capacity to make the conclusions; or where giving opinions is a convenient mode of stating facts too subtle or complicated to be narrated as facts (*Graat v. The Queen*, [1982] 2 S.C.R. 819, at pages 836-839, 144 D.L.R. (3d) 267; *Hunt (Litigation guardian of) v. Sutton GroupIncentive Realty Inc.* (2002), 60 O.R. (3d) 665, 215 D.L.R. (4th) 193 (C.A.), at paragraph 17, quoting with approval Alan W. Bryant, Sidney N. Lederman & Michelle K. Fuerst, *The Law of Evidence in Canada*, 4th ed. (Markham, Ont.: LexisNexis Canada, 2014), at page 12.14. See also Paciocco and Stuesser, above, at pages 197-198 and Delisle *et al.*, above, at pages 874-876).

**80** The question of opinion evidence given by lay witnesses was recently addressed by this Court in *Pfizer Canada Inc. v. Teva Canada Limited*, 2016 FCA 161, [page597] 400 D.L.R. (4th) 723, where Stratas J.A., writing for this Court, upheld the Federal Court's acceptance of a corporate executive's testimony about what his pharmaceutical company would have done in the "but for" world in circumstances where the witness had actual knowledge of the company's relevant, real world, operations (at paragraphs 105-108, 112 and 121).

**81** Nevertheless, we think it is clear that lay witnesses cannot testify on matters beyond *their own conduct* and that of *their businesses* in the "but for" world. Lay witnesses are not in a better position than the trier of fact to form conclusions about the greater economic consequences of the "but for" world, nor do they have the experiential competence. While questions pertaining to how their particular business might have responded to the hypothetical world are permissible provided the requisite evidentiary foundation is established, any witness testimony regarding the impact of the VOW restrictions on competition generally strays into the realm of inappropriate opinion evidence.

(ii) Substantiality Analysis

**82** Before addressing this important issue, it will be helpful to consider what the Supreme Court and this Court have said in regard to the expression "the effect of preventing or lessening competition substantially" found in paragraph 79(1)(c) of the *Competition Act* and the test relevant to a determination of substantial lessening or prevention of competition.

**83** First, in *Tervita SCC*, albeit in the context of the merger provisions of the *Competition Act*, the Supreme Court made the following comments at paragraphs 44 to 46 of its reasons:

> Generally, a merger will only be found to meet the "lessen or prevent substantially" standard where it [here, the "it" means the practice at issue] is "likely to create, maintain or enhance the ability of the merged entity to exercise market power, unilaterally or in coordination with other firms" .... Market power is the ability to "profitably influence price, quality, variety, service, advertising, innovation or other dimensions of competition" .... [page598] Or, in other words, market power is "the ability to maintain prices above the competitive level for a considerable period of time without such action being unprofitable" ...; where "price" is "generally used as shorthand for all aspects of a firm's actions that have an impact on buyers .... If a merger does not have or likely have market power effects, s. 92 will not generally be engaged ...
> The merger's likely effect on market power is what determines whether its effect on competition is likely to be "substantial". Two key components in assessing substantiality under the "lessening" branch are the degree and duration of the exercise of market power (*Hillsdown*, at pp. 328-29). There is no reason why degree and duration should not also be considered under the "prevention" branch.

What constitutes "substantial" will vary from case to case. The Tribunal has not found it useful to apply rigid numerical criteria:

> What will constitute a likely "substantial" lessening will depend on the circumstances of each case... .Various tests have been proposed: a likely 5% price rise sustainable for one year; a 5% price rise sustainable over two years; a small but significant and non-transitory price rise. The Tribunal does not find it useful to apply rigid numerical criteria although these may be useful for enforcement purposes.
>
> (*Hillsdown*, at pp. 328-329)
>
> [Emphasis added; references omitted.]

**84** Then, at paragraphs 50 to 51 of *Tervita SCC*, the Supreme Court indicated that the words of paragraph 79(1)(c) of the *Competition Act* and those of subsection 92(1) were similar and thus conveyed the same idea:

> *Canada Pipe* was a case involving abuse of dominance under s. 79(1)(*c*) of the Act. The words of s. 79(1)(*c*) _ "is having or is likely to have the effect of preventing or lessening competition substantially in a [page599] market" _ are very close to the words of s. 92(1) _ "likely to prevent or lessen" _ and convey the same ideas. In *Canada Pipe*, the Federal Court of Appeal employed a "but for" test to conduct the inquiry:
>
> > ... the Tribunal must compare the level of competitiveness in the presence of the impugned practice with that which would exist in the absence of the practice, and then determine whether the preve nting or lessening of competition, if any, is "substantial"... .

> The comparative interpretation described above is in my view equivalent to the "but for" test proposed by the appellant. [paras. 37-38]

A similar comparative analysis is conducted under s. 92(1). A merger review, by its nature, requires examining a counterfactual scenario: "... whether the merger will give the merged entity the ability to prevent or lessen competition substantially compared to the pre-merger benchmark or but for' world" (Facey and Brown, at p. 205). The "but for" test is the appropriate analytical framework under s. 92.

**85** Lastly, at paragraph 60 of its reasons in *Tervita SCC*, the Supreme Court made the following remarks regarding the "but for" test:

> The concern under the "prevention" branch of s. 92 is that a firm with market power will use a merger to prevent competition that could otherwise arise in a contestable market. The analysis under this branch requires looking to the "but for" market condition to assess the competitive landscape that would likely exist if there was no merger. It is necessary to identify the potential competitor, assess whether but for the merger [here "but for" the anti-competitive practice] that potential competitor is likely to enter the market and determine whether its effect on the market would likely be substantial. [Emphasis added.]

**86** In *Canada Pipe*, at paragraphs 36 to 38 and 45 to 46, this Court, in addressing the test required to make a determination under paragraph 79(1)(c), observed that the test is relative in nature. Rather than assessing the absolute level of competition in the market the Tribunal [page600] must assess the level of competition in the presence of the impugned practice and compare this with the level of competition that would exist in the absence of the practice. This difference can occur in the past, present or future and the test will be made out where the difference is substantial. This Court noted that it is the role of the Tribunal to adapt this assessment to the case before it.

**87** At paragraph 46 of *Canada Pipe*, this Court explicitly indicated that it was not dictating the type of evidence required, rather it wrote: "Ultimately, the Commissioner bears the burden of proof for each requisite element, and the Tribunal must be convinced on the balance of probabilities. The evidence required to meet this burden can only be determined by the Tribunal on a case-by-case basis."

**88** It is clear from *Canada Pipe* that what will constitute a "substantial" lessening or prevention of competition depends on the facts of the case and that the Tribunal is not bound to apply a particular test in determining the issue. However, it is clear that in order for the Tribunal to find that a substantial lessening of competition has been established, it must be able, on the evidence before it, to conclude that were it not for the anti-competitive effects of the practice at issue, the market at issue would be substantially more competitive. In other words, in the present matter, would there be a substantial incremental benefit to competition arising from the availability of the disputed data in TREB's VOW data feed?

**89** In the present matter the Tribunal turned its mind to both the meaning of "substantiality" and the appropriate test to be applied. The Tribunal noted, at paragraph 461 of its reasons, that substantiality is an assessment of the exercise of market power. Market power, as the Tribunal defines it in paragraph 165 of its reasons, is the ability to control either prices or non-price dimensions of competition for a significant time. Non-price dimensions of competition include innovation and quality of service, among others.

**90** At paragraph 480 of its reasons, the Tribunal acknowledges that the test for substantiality is relative in [page601] nature. That is, the Tribunal is to compare the level of competition that exists in the actual world with the level of competition that would exist, but for, the impugned practices. The test then, is to assess whether the difference between these two worlds is substantial. The Tribunal indicates that this test will be met where either price is materially higher, or one or more non-price dimension are materially lower than in the absence of the practices.

**91** In making this assessment the Tribunal will have regard to the overall economic conditions of the relevant

market. As explained in paragraph 468 of its reasons, this means that the duration of the impact will be considered along with the relative size of impact to determine whether the impact is substantial.

**92** In our view, the Tribunal correctly understood the significance of the word "substantially" and the test which it had to apply in determining whether or not, on the facts of this case, TREB's practice regarding the disputed data was a practice which had the effect of preventing competition substantially in the GTA.

**93** With these comments in mind, we now turn to TREB's and CREA's submissions as to why we should intervene. Their principal submission on substantiality is that it was improper for the Tribunal to determine whether the anti-competitive effects led to a substantial prevention of competition on the basis of qualitative evidence only. In their view, this led the Tribunal to determine the issue on "speculative opinion evidence unsupported by available empirical evidence" (TREB's memorandum of fact and law, at paragraph 14).

**94** In making this submission, TREB and CREA put forward two arguments. The first is that in *Tervita SCC*, the Supreme Court held that the Commissioner had an obligation to quantify any quantifiable anti-competitive effect and that failure to do so would prevent him from relying on qualitative evidence in respect of effects which could have been quantified. Thus, in the view of TREB and CREA, anti-competitive effects can be considered qualitatively by the Tribunal only if they cannot be quantitatively estimated.

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**95** TREB and CREA further say that the Tribunal erred in concluding (TR, at paragraphs 469-470) that the aforementioned principle, enunciated by the Supreme Court in *Tervita SCC* at paragraph 124 of its reasons, did not apply to a determination made under section 92 of the *Competition Act* or under subsection 79(1) thereof. In other words, they submit that the Tribunal erred in finding that the Supreme Court's holding in *Tervita SCC*, on which TREB and CREA rely, was limited to determinations under subsection 96(1).

**96** More particularly, TREB and CREA say that the rationale underlying the Supreme Court's statement of principle in *Tervita SCC* not only applies to determinations under subsection 96(1), but also to determinations arising under both section 92 and subsection 79(1). In support of this view, they rely on that part of paragraph 124 of *Tervita SCC* which we have underlined herein below.

> The Commissioner argues that quantification is not a legal prerequisite to considering anti-competitive effects (R.F., paras. 84 and 88). On the contrary, the Commissioner's legal burden is to quantify the quantifiable anti-competitive effects upon which reliance is placed. Where effects are measurable, they must be estimated. Effects will only be considered qualitatively if they cannot be quantitatively estimated. A failure to quantify quantifiable effects will not result in such effects being considered qualitatively (*Superior Propane IV*, at para. 35). <u>This approach minimizes the degree of subjective judgment necessary in the analysis and enables the Tribunal to make the most objective assessment possible in the circumstances</u> (*Superior Propane IV*, at para. 38). <u>An approach that would permit the Commissioner to meet her burden without at least establishing estimates of the quantifiable anti-competitive effects fails to provide the merging parties with the information they need to know the case</u> they have to meet. [Emphasis added.]

**97** TREB's and CREA's second argument is that the Tribunal should have drawn an adverse inference against the Commissioner by reason of his failure to adduce empirical evidence concerning competition on price and dynamic competition in markets (United States and [page603] Nova Scotia) where full information VOWs exist and in respect of which it was possible to measure the actual effects on competition. They say that the Commissioner deliberately decided not to perform a quantitative analysis of competition effects in these markets. More particularly, TREB and CREA argue that the Tribunal should have drawn the only inference possible resulting from the Commissioner's failure to adduce quantitative evidence, "namely that there was no substantial prevention or lessening of

competition, dynamic or otherwise, that could be demonstrated on a balance of probabilities" (TREB's memorandum of fact and law, at paragraph 77).

**98** TREB and CREA then address the reasons given by the Tribunal for not drawing an adverse inference against the Commissioner, namely that the Commissioner had to be prudent with regard to the spending of the funds under his authority and because of Dr. Vistnes' advice to the Commissioner that a study of the United States' experience would constitute a difficult and expensive endeavour that would likely not yield useful answers. (TREB and CREA say that Dr. Vistnes' testimony on this point constitutes an off the cuff response to a question posed by the Tribunal during the hearing.) TREB and CREA say that the reasons given by the Tribunal for refusing to draw the adverse inference are improper and cannot be right.

**99** In our respectful view, TREB's and CREA's submissions cannot succeed. First in *Tervita SCC*, the Supreme Court did not, contrary to TREB's and CREA's assertion, make any pronouncement pertaining to section 92 of the *Competition Act* regarding the necessity of quantifying effects which could be quantified. To the contrary, at paragraph 166 of its reasons in *Tervita SCC*, the Supreme Court indicated that there was no obligation on the part of the Commissioner to quantify anti-competitive effects under section 92:

> It may seem paradoxical to hold that the Tribunal was correct in finding a likely substantial prevention of competition, only to then conduct the s. 96 balancing test and find zero anti-competitive effects. However, this result merely appears paradoxical in view of the particular facts of this case. Here, as discussed above, the Tribunal was able to consider evidence as to the effect on the [page604] market of the emergence of likely competitors, whether acceptable substitutes existed, and so on. Section 93 expressly permits the consideration of these factors in and of themselves. Ordinarily, the Commissioner would also use the evidence bearing on those factors to quantify the net effect of those factors on the economy in the form of deadweight loss. However, the statutory scheme does not bar a finding of likely substantial prevention where there has been a failure to quantify deadweight loss, and thus the Commissioner's failure to do so in this case was not fatal to the s. 92 determination. By contrast, the balancing test under s. 96 does require that quantifiable anti-competitive effects be quantified in order to be considered. As such, the failure to quantify deadweight loss in this case barred consideration, under s. 96, of the quantifiable effects that supported a finding of likely substantial prevention under s. 92. In circumstances where quantifiable effects were in fact quantified, a finding of likely substantial prevention under s. 92 would be accompanied by the consideration of quantified anti-competitive effects under the s. 96 analysis. [Emphasis added.]

**100** Although we agree, as a matter of logic, that the Supreme Court's rationale in *Tervita SCC* for requiring that quantifiable effects be quantified could equally be applied to determinations made under both subsection 79(1) and section 92, there can be no doubt that the Supreme Court made it clear, at paragraph 166 cited above, that the principle did not apply to section 92. That being the case, we have no choice but to hold that the principle requiring quantification of quantifiable effects cannot be applied to subsection 79(1). Had it been open to us to decide the issue afresh, we would have held that the principle applied to determinations under subsection 79(1).

**101** Consequently, TREB and CREA cannot succeed on their assertion that the Commissioner, in seeking a determination under subsection 79(1), had a legal obligation to quantify all effects which could be quantified. [page605] On the basis of *Tervita SCC*, the Commissioner did not have such an obligation.

**102** We now turn to the Tribunal's refusal to make the adverse inference against the Commissioner which TREB and CREA sought because the Commissioner had failed to provide an empirical assessment "of the incremental effect of sold and other Disputed Data in increasing a full-information VOW operator's ability to generate clients" (TR, at paragraph 653). This submission, in our respectful view, is also without merit.

**103** To begin, we agree with the Commissioner that TREB's and CREA's argument is tantamount to arguing that the Commissioner had a legal burden to adduce quantifiable evidence. As we have just indicated, no such obligation arises under subsection 79(1).

**104** Considering that the Commissioner had no such legal obligation, he, like any other plaintiff, had to decide what evidence he had to put forward to prove his case. As we know, he chose to do so by way of qualitative evidence and in so doing, he took the risk of failing to persuade the Tribunal that the anti-competitive effects of TREB's practice resulted in a substantial prevention of competition. As it turned out, the Tribunal was persuaded by the qualitative evidence adduced by the Commissioner.

**105** We have carefully considered the case law and cannot see any basis to accept TREB's and CREA's proposition that the Tribunal ought to have drawn an adverse inference against the Commissioner for failing to conduct an empirical assessment of markets in the United States and in Nova Scotia, or for that matter in the GTA. That, in our respectful view, would be akin to giving the Tribunal the power to dictate to the Commissioner how he should present his case. There is no authority for such a proposition.

**106** We agree with TREB and CREA in one respect. Had there been a valid basis to draw an adverse inference against the Commissioner, the reasons for refusing [page606] to draw the inference given by the Tribunal would clearly not have withstood scrutiny. The fact that the Commissioner has limited funds to spend may be a reality, but it is of no relevance to a determination of whether or not an adverse inference should be made. As to Dr. Vistnes' view with regard to the utility and cost of producing an empirical assessment, that, in our view, is also an irrelevant consideration. Whether the study would have been useful is a matter which the Tribunal would have had to appreciate and determine. It was clearly not up to Dr. Vistnes to make that determination. In any event, it is doubtful that Dr. Vistnes could provide that opinion to the Tribunal as it does not appear in his expert reports. However, as we are satisfied that there was no basis to draw the inference sought by TREB and CREA, the reasons given by the Tribunal, even though misguided, are of no consequence.

**107** Additionally, it should be remembered that in *Ellis-Don Ltd. v. Ontario (Labour Relations Board)*, 2001 SCC 4, [2001] 1 S.C.R. 221, at paragraph 73, the Supreme Court made the following point: "Whether or not an adverse inference is warranted on particular facts is bound up inextricably with the adjudication of the facts" (see also *Benhaim v. St-Germain*, 2016 SCC 48 at para. 52, [2016] 2 S.C.R. 352). Thus, the Tribunal's refusal to draw an inference against the Commissioner is subject to the standard of reasonableness. We see no basis to conclude that the Tribunal's refusal to draw the inference is unreasonable.

**108** TREB and CREA make a further submission regarding the Tribunal's determination that the prevention of competition was substantial. They say that, in any event, it was an error for the Tribunal to rely on evidence which they characterize as speculative qualitative evidence. At paragraph 75 of its memorandum of fact and law, TREB defines quantitative evidence as "empirical evidence of the actual effect of certain impugned acts on competition in an existing real estate market" and defines qualitative evidence as "a reference essentially to opinion and anecdotal evidence of what might happen in the market if certain acts are permitted or not permitted".

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**109** More particularly (the argument which we now explain is one put forward mainly by CREA), they make four points. First, they say that the Tribunal erred in concluding, on the basis of statements made by brokers to the effect that they needed the disputed data in their VOWs so as to improve their offerings to the public and that their clients, i.e. buyers and sellers, valued the opportunity of accessing the disputed data on their VOWs, that the availability of the disputed data would result in a substantial incremental competition benefit.

**110** In TREB's and CREA's view, the Tribunal's conclusion on substantiality which results from its finding with respect to the anti-competitive effects of TREB's practice was tantamount to reading out the word "substantial" from the statutory provision. They say that, at best, the aforementioned witness statements constitute evidence of "an

effect" on competition but clearly not of a substantial incremental competition benefit arising from the availability of the disputed data on the VOWs.

**111** Second, TREB and CREA say that it was an error on the part of the Tribunal to find, on the basis of the evidence of William McMullin, that Viewpoint was prevented from entering the GTA market because of the unavailability of the disputed data. They say that Mr. McMullin's evidence on this point, in light of the overall evidence, was not credible adding that, in any event, the Tribunal erred in finding that Viewpoint's entry into the GTA would have had a substantial competitive effect considering that Viewpoint was less competitive (if one considers Viewpoint's commission rates and lack of rebates) in terms of price than other brokerages such as Realosophy and TheRedPin.

**112** Third, TREB and CREA say that the Tribunal made a further error in finding that the Commissioner had met his burden of proof on the basis of qualitative benefits asserted by brokers when the evidence showed [page608] that brokers operating in the GTA with VOWs fed by TREB's VOW data feed (i.e. without the disputed data) were equally or more competitive than brokers operating on a data feed that included some of the disputed data.

**113** Fourth, TREB and CREA say that the Tribunal also erred in finding that a substantial prevention of competition had been demonstrated by the Commissioner because there was a lack of evidence showing a link between the success of brokerages such as Redfin and Viewpoint and the availability of the disputed data in a VOW. In making this point, TREB and CREA argue that it was clear from the evidence that there was no causal relationship between being able to convert website users into clients and the availability of the disputed data on one's VOWs.

**114** TREB and CREA conclude on this point by saying that the evidence regarding conversion rates was extremely important because the purpose of designing attractive websites was to convert viewers into clients.

**115** TREB and CREA also point out that after finding that the evidence regarding conversion rates did not support the Commissioner's case, the Tribunal downplayed the importance of conversion rates on the basis of Dr. Vistnes' opinion that local differences in the markets under consideration probably explained why the conversion rates were low. TREB and CREA say that there was no evidence of these local differences before the Tribunal on which Dr. Vistnes could give the opinion that he gave. Dr. Vistnes' opinion, in their view, was entirely speculative.

**116** Finally, TREB and CREA conclude their arguments regarding conversion rates by saying that even though the Tribunal refused to give any weight to the evidence showing low conversion rates, it nonetheless found, at paragraph 676 of its reasons, that if the disputed data was made available on TREB's data feed, [page609] web based brokerages would likely be successful in converting "an increasing and significant number of website users into clients."

**117** To place TREB's and CREA's arguments in perspective, it is important to point out that the Tribunal understood the difference in nature between quantitative and qualitative evidence and that it recognized that it was more difficult for the Commissioner to prove his case on the basis of mostly qualitative evidence. The Tribunal indicated that in a case like the one before it, which pertained mostly to dynamic competition, it was inevitable that the Commissioner would have to rely on qualitative evidence in the form of business documents, witness statements, and testimonies, adding, however, that it remained the Commissioner's burden to prove his case on a balance of probabilities (TR, at paragraphs 469-471).

**118** On the basis of the qualitative evidence put forward by the Commissioner and in particular on the basis of the witness statements and testimonies of the persons referred to at paragraph 76 of these reasons, namely Messrs. McMullin, Hamidi, Gidamy, Silver, Enchin, Prochazka, Desai, and Pasalis, the Tribunal made findings of a number of anti-competitive effects caused by the VOW restrictions. In each case, the Tribunal found both that an anti-competitive effect existed and emphasized the relative significance of that effect as follows:

* The prevention of a considerably broader range of broker services in the GTA (TR, at paragraph 583)

* The prevention of an increase in the quality of these services in a significant way (TR, at paragraph 598)

* The prevention of the advent of considerably more innovation (TR, at paragraph 616)

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* The significant adverse impact on entry into, and expansion within the relevant market (TR, at paragraph 550)

**119** It was the Tribunal's opinion that "but for" the VOW restrictions these anti-competitive effects would be considerably lower. At paragraph 702 of its reasons, the Tribunal concluded that when considered in the aggregate, these anti-competitive effects on non-price dimensions amounted to a substantial prevention of competition.

**120** In other words, the Tribunal held that the ultimate consequence of the anti-competitive effects found to exist was the maintenance of TREB and its members' collective market power in respect of residential brokerage services in the GTA (TR, at paragraph 709) and that failing an order on its part, that market power would likely continue (TR, at paragraph 712).

**121** In our view, TREB's and CREA's arguments regarding the Tribunal's reliance on qualitative evidence are without merit.

**122** First, it is clear that most of the points which TREB and CREA make on this issue are to the effect that many of the Tribunal's crucial findings are not supported by the evidence. This is particularly so in regard to their criticism of Mr. McMullin's evidence and in regard to Viewpoint's entry into the GTA. Although we have some misgivings in regard to a number of the findings made by the Tribunal, it must be remembered that these findings result from the Tribunal's assessment of the evidence before it. The same goes with respect to the weight which the Tribunal gave to that evidence. As we have already indicated, TREB and CREA, not having sought leave to challenge questions of fact on this appeal, cannot pursue this line of attack. TREB and CREA, without so saying, are inviting us to reassess the evidence before the Tribunal and to make different findings. We clearly cannot do so. Further, as this Court indicated in *Nadeau Poultry Farm*, at paragraph 47, parties cannot "under cover of challenging a question of mixed fact and law, revisit the Tribunal's factual conclusions."

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**123** Second, it is also important to repeat that TREB and CREA do not challenge the admissibility of the statements nor of the testimonies given by the lay witnesses upon which the Tribunal relies for its findings.

**124** Third, in our respectful opinion, the underlying premise behind TREB's and CREA's challenge on this point is that qualitative evidence without quantified evidence, which they say was available to the Commissioner, should not be considered nor given any weight. We have already determined that this premise is not well founded.

**125** We agree, however, with TREB and CREA that the evidence pertaining to conversion rates does not support the Commissioner's case. Had the conversion rates been the determinative factor in this appeal, we would have intervened. We cannot see how the Tribunal can say, as it does at paragraph 676 of its reasons, that if Viewpoint and others could use the disputed data they would be in a position "to convert an increasing and significant number of website users into clients." The Tribunal's findings on conversion rates, which appear at paragraphs 653, 657, 658, and 664 of their reasons, show that the evidence before it did not support the Commissioner's case.

**126** However, as the Commissioner argues, the Tribunal, although recognizing that conversion rates were low, made the point that his application was primarily concerned with dynamic competition and innovation and that, in the absence of quantifiable evidence on point, it had no choice but to determine the matter on the evidence before it, mostly qualitative evidence. More particularly, at paragraph 662 of its reasons, the Tribunal indicated in no uncertain terms that the additional innovation developed by full information VOW brokerages was not only helpful in their attempts to compete but was "forcing traditional brokerages to respond" to this new type of competition.

**127** We are therefore satisfied that in relying on qualitative evidence for its findings of anti-competitive [page612] effects and its ultimate conclusion on substantiality, the Tribunal made no reviewable error. Consequently, we have not been persuaded, in light of the Tribunal's findings and of the applicable test, that there is any basis for us to interfere with the Tribunal's determination under paragraph 79(1)(c) of the *Competition Act*.

**128** We now turn to the second issue raised by this appeal.

C. *Privacy*

**129** TREB sought to justify its restriction on disclosure of the disputed data on the basis that the privacy concerns of vendors and purchasers constituted a business justification sufficient to escape liability under paragraph 79(1)(b) of the *Competition Act*. TREB asserted that privacy was integral to its business operations; more specifically, privacy was an aspect of maintaining the reputation and professionalism of its members, central to the interests of purchasers and sellers and to the cooperative nature and efficiency of the MLS system.

**130** TREB also asserted that it was required, as a matter of law, to comply with the *Personal Information Protection and Electronic Documents Act*, S.C. 2000, c. 5 (PIPEDA). It contended that this statutory requirement constituted a business justification, separate and apart from any question of the underlying motive TREB may have had for the VOW Policy and its anti-competitive effects. Characterized differently, having concluded that the policy was not motivated by subjective privacy concerns, the Tribunal was nevertheless obligated to continue and also determine, one way or another, whether the policy was mandated by PIPEDA. Had the Tribunal considered the consents in light of the requirements of PIPEDA, it would have found them lacking, and insufficient to authorize disclosure. This would lead, in TREB's submissions, to the conclusion that the restrictions on disclosure were necessary to [page613] comply with the legislation and constitute a business justification.

(1) The Tribunal's Decision

**131** In considering privacy as a business justification under paragraph 79(1)(b), the Tribunal found [at paragraph 430] that the "principal motivation in implementing the VOW Restrictions was to insulate its Members from the disruptive competition that [motivated], Internet-based brokerages". It concluded that there was little evidentiary support for the contention that the restrictions were motivated by privacy concerns of TREB's clients. The Tribunal also found scant evidence that, in the development of the VOW Policy, the VOW committee had considered, been motivated by, or acted upon privacy considerations (TR, at paragraph 321). The privacy concerns were "an afterthought and continue to be a pretext for TREB's adoption and maintenance of the VOW Restrictions" (TR, at paragraph 390).

**132** The Tribunal found the business justification argument simply did not mesh with the evidence. At paragraphs 395 to 398 of its reasons, the Tribunal observed that it was "difficult to reconcile" TREB's privacy arguments with the fact that the disputed data was made available to:

* All 42,500 TREB members via its Stratus system;
* The members of most other Ontario real estate boards through the data sharing program CONNECT;
* Clients of all TREB members and clients of members of most other Ontario real estate boards;

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* Some appraisers;
* Third party industry stakeholders including CREA, Altus Group Limited, the CD Howe Institute, and Interactive Mapping Inc. (albeit for confidential use); and
* Customers via email subscription services or regular emails sent by members.

**133** Further, the Tribunal noted that for many months TREB did nothing regarding two brokers who displayed the disputed data in apparent violation of TREB's policy (TR, at paragraphs 372-374). It observed that few clients had reported concerns to TREB about their data being displayed and distributed online (TR, at paragraph. 386-387) and that TREB did not produce evidence to support its allegation that including the disputed data in the data feed would push consumers away from using MLS-based services (TR, at paragraph 423).

**134** Additionally, agents were entitled to, and routinely did, distribute detailed seller information, including sold prices, to their own clients without any restriction on further dissemination. Moreover, TREB's own intranet system enables TREB's members to forward by email up to 100 sold listings at a time to anyone (TR, at paragraph 398).

**135** The Tribunal found no evidentiary foundation to support the assertion that the policy was genuinely motivated by a concern about compliance with PIPEDA. Although the need to abide by PIPEDA was mentioned in the testimony of TREB's Chief Executive Officer, the Tribunal noted the absence of evidence from TREB's Board of Directors, its Chief Privacy Officer or its Chief Information Officer, which would support the conclusion that compliance with PIPEDA necessitated the policy (TR, at paragraphs 378-379).

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**136** The Tribunal noted that while TREB implemented its privacy policy in 2004 and had appointed a Chief Privacy Officer, there was no evidence that the VOW Policy was directed towards compliance. TREB's only contact with the Privacy Commissioner was to ask for an opinion on a different document (a "Questions and Answers" document addressing a number of privacy related topics) in August 2012. These did not include questions related to the disputed data, and, in any event, these communications took place only after the VOW Policy and Rules were set (TR, at paragraphs 375-376).

**137** The Tribunal also noted at paragraph 407 of its reasons that Mr. Richardson, the CEO of TREB during the relevant time, operated on the assumption that the wording in the consents in the Listing Agreement was sufficient to permit disclosure.

**138** In argument, TREB pointed to a 2009 decision of the Privacy Commissioner which held that an advertisement which said that a property sold at 99.3 percent of the list price contravened PIPEDA because it allowed the public to calculate the selling price. The Office of the Privacy Commissioner held that the exception for publicly available information did not apply because the information was obtained under the purchase agreement to which the salesperson was not privy and was not actually drawn from the Ontario registry or any source accessible to the public (TR, at paragraph 388).

**139** The Tribunal rejected TREB's assertion that this decision influenced the VOW Policy. It noted that, with two exceptions (the meetings of May 12 and May 20, 2011), privacy concerns were not reflected in the minutes or

discussion pertaining to the development of the VOW Policy (see e.g. TR, at paragraph 351). It [page616] concluded that privacy considerations were an *ex post facto* attempt to justify the policy.

**140** The Tribunal then considered CREA's argument that consumers were concerned about their property information being disclosed on a public website. The Tribunal concluded that the evidence was very limited and not persuasive (TR, at paragraph 776).

**141** The Tribunal then examined the consent clauses contained in the Listing Agreement and concluded that the consents permitted the disclosure of the data. This point will be expanded upon below.

(2) Burden of Proof

**142** Before turning to the substance of this issue, the parties raise a point concerning the burden of proof.

**143** The Commissioner and TREB agree that TREB is bound by the provisions of PIPEDA. However, TREB contends that it was the Commissioner's burden to disprove TREB's assertion that the VOW Policy was required by PIPEDA. We do not agree. Neither this contention, nor the law, shifts the legal or evidentiary burden to the Commissioner to disprove the assertion that the policy is necessary as a matter of regulatory compliance.

**144** The normal evidentiary burden applies. The party who asserts must prove: *WIC Radio Ltd. v. Simpson*, *2008 SCC 40*, *[2008] 2 S.C.R. 420*, at paragraph 30. TREB has offered no compelling reason as to why this principle should not apply in respect of a business justification under section 79. In consequence, if TREB seeks to establish that regulatory compliance would be compromised, the onus is on it to lead the relevant evidence as part of its evidentiary burden, and to establish the consequential legal conclusions as part of its argument.

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(3) A Business Justification was not Established

**145** To begin, we reject the argument that the Tribunal did not consider the possibility that independent of motivation, regulatory compliance with PIPEDA could constitute a justification. Having reviewed the law, the Tribunal concluded that the business justification analysis was "subject to the important caveat that legal considerations, such as privacy, may provide a legitimate justification for an impugned practice" (TR, at paragraph 302).

**146** However, earlier in its reasons, the Tribunal wrote that "legal considerations, such as privacy laws, [may] legitimately justify an impugned practice, provided that the evidence supports that the impugned conduct was primarily motivated by such considerations" (TR, at paragraph 294). We appreciate TREB's point that the Tribunal's reasons on this issue are equivocal. In our view, to the extent that the Tribunal required regulatory compliance to be the motivation behind the VOW Policy, it did so in error. If it can be established that a business practice or policy exists as a matter of a statutory or regulatory requirement, whether compliance was the original or seminal motivation for the policy is of no consequence.

**147** This does not, however, eliminate the burden on the corporation to establish a factual and legal nexus between that which the statute or regulation requires and the impugned policy.

**148** In order to establish a business justification within the meaning of paragraph 79(1)(b) of the *Competition Act*, a party must establish "a credible efficiency or pro-competitive rationale for the conduct in question, attributable to the respondent, which relates to and counterbalances the anti-competitive effects and/or subjective intent of the acts":

*Canada Pipe*, at paragraph 73. Proof of a "valid business justification ... is not an absolute defence for paragraph 79(1)(*b*)"; it must provide an explanation why the dominant corporation engaged in the allegedly anti-competitive conduct: *Canada Pipe*, [page618] at paragraphs 88-91. As this Court explained in *Canada Pipe*, at paragraph 87:

> ... A business justification for an impugned act is properly relevant only in so far as it is pertinent and probative in relation to the determination required by paragraph 79(1)(*b*), namely the determination as to whether the purpose for which the act was performed was a predatory, exclusionary or disciplinary negative effect on a competitor.... [A] valid business justification can, in appropriate circumstances, overcome the deemed intention arising from the actual or foreseeable negative effects of the conduct on competitors, by demonstrating that such anti-competitive effects are not in fact the overriding purpose of the conduct in question. In this way, a valid business justification essentially provides an alternative explanation as to why the impugned act was performed, which in the right circumstances might be sufficient to counterbalance the evidence of negative effects on competitors or subjective intent in this vein.

**149** In sum, two facts must be established before an impugned practice can shelter behind paragraph 79(1)(b). First, there must be a credible efficiency or pro-competitive rationale for the practice. Second, the efficiencies or competitive advantages, whether on price or non-price issues, must accrue to the appellant. Put otherwise, the evidence must demonstrate how the practice generates benefits which allow it to better compete in the relevant market.

**150** The Tribunal assessed the evidence before it according to the correct principles and found it lacking. The Tribunal concluded that TREB was motivated by a desire to maintain control over the disputed data in an effort to forestall new forms of competition, and not by any efficiency, pro-competition, or genuine privacy concerns (TR, at paragraphs.369 and 389-390). It was fair for the Tribunal to consider that, had regulatory compliance been a concern, there would have been evidence of such communications. It concluded that there was "no evidence" that TREB's privacy policies received much, if any, consideration during the development of TREB's VOW Policy and Rules.

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**151** The evidence, some of which we have summarized earlier, is compelling. As leave to challenge these findings was not sought, the Tribunal's conclusion that there were no pro-competitive business or efficiency justifications for the policy is reasonable and will not be disturbed. This sets the stage for TREB's second and, we believe, principal argument.

(4) Privacy Obligations under PIPEDA

**152** TREB submits that the Tribunal erred in failing to engage in a stand-alone assessment of TREB's responsibilities under PIPEDA regarding the collection and use of personal information.

**153** In its reasons, the Tribunal considered PIPEDA and whether its requirements mandated the policy. In this regard, it looked at the extent to which TREB engaged with the Privacy Commissioner and considered the provisions of PIPEDA. It also examined the nature and scope of the consent clause in the Listing Agreement. It proceeded on the understanding that the data was confidential and then considered the scope and effect of the consents governing its use. It concluded that the consents were effective.

**154** In our view, the role of the Tribunal was to interpret the scope of the consents under the ordinary law of contract, as informed by the purpose and objectives of PIPEDA. This is what it did, and we find no error in the conclusion reached.

(a) **The Standard of Review**

**155** As a preliminary matter, we consider that in reviewing the consent in the Listing Agreements, the [page620] Tribunal was interpreting a standard form contract. As such, the standard of review is correctness.

**156** Generally speaking, contractual interpretation involves questions of mixed law and fact and, thus, is reviewable on a deferential standard: *Sattva Capital Corp. v. Creston Moly Corp.*, *2014 SCC 53*, *[2014] 2 S.C.R. 633* (*Sattva*), at paragraph 50. The interpretation of standard form contracts is an exception to this rule. Their interpretation constitutes a question of law and, thus, is reviewable for correctness: *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, *2016 SCC 37*, *[2016] 2 S.C.R. 23* (*Ledcor*), at paragraph 46. Determining the interplay between a statutory provision and a contractual term is also an exception and is reviewable for correctness: *Canada (Office of the Information Commissioner) v. Calian Ltd.*, *2017 FCA 135*, *414 D.L.R. (4th) 165* (*Calian*), at paragraph 37. Statutory rights of appeal do not necessarily convert a reasonableness standard to a correctness one-it depends on the exact language of the legislative provision: *Edmonton (City) v. Edmonton East (Capilano) Shopping Centres Ltd.*, *2016 SCC 47*, *[2016] 2 S.C.R. 293*, at paragraph 31.

**157** MLS Rules specify that brokers cannot change or delete any part of clause 11 of the Listing Agreement (rule 340). The *Frequently Asked Privacy Questions* provided by CREA states that "[b]oth current and historical data is essential to the operation of the MLS(R) system and by placing your listing on the MLS(R) system you are agreeing to allow this ongoing use of listing and sales information". The Listing Agreement is, at least for the purposes of these proceedings, a contract of adhesion or standard form.

(b) **The Consents**

**158** PIPEDA requires that individuals consent to the collection, use, and disclosure of their personal [page621] information (Schedule 1, clause 4.3.1). This consent must be informed (Schedule 1, clause 4.3.2). Amendments in 2015 to this principle specified that for consent to be informed, the person must understand the "nature, purpose and consequences of the collection, use or disclosure of the personal information" (section 6.1).

**159** As noted earlier, the Tribunal proceeded on the basis that the sale price of property is personal information and therefore subject to the terms of PIPEDA, which mandates informed consent to the use of personal information.

**160** While the Listing Agreement used by TREB provides consent to some uses of personal information, TREB asserts that had the Tribunal examined it more closely, it would have found that the Listing Agreement did not provide sufficiently specific wording to permit disclosure of personal information in the VOW data feed. Specifically, TREB contends that the consents do not permit the distribution of the data over the internet, and that is qualitatively different from the distribution of the same information by person, fax, or email.

**161** The Listing Agreement contains a clause governing the "Use and Distribution of Information". TREB focuses on the consent to the collection, use, and disclosure of information for the purpose of listing and marketing of the Property itself but omits that part of the consent (in the same clause) that says the real estate board may "make such other use of the information as the Brokerage and/or real estate board(s) deem appropriate, in connection with the listing, marketing and selling of real estate during the term of the listing and thereafter". The Commissioner contends that this latter part of the consent (in the same clause) is the pertinent part and that it is sufficient to permit the ongoing use and disclosure of information, even after the listing is no longer active. We agree with the Commissioner's position.

**162** The Tribunal had before it the Listing Agreements used from 2003 to 2015. Although there is data in the MLS database dating back to 1986, Listing Agreements prior to 2003 were not before the Tribunal or this Court. Therefore, this Court expresses no opinion regarding the information obtained prior to 2003 or any information that may have entered the database without being subject to the 2003 to 2015 Listing Agreements.

**163** The Listing Agreement was created by the Ontario Real Estate Association and recommended by TREB to its members (TR, at paragraph 64). In the most recent version before the Court, the relevant section of the Use and Distribution of Information clause reads:

> ...The Seller acknowledges that the database, within the board's MLS System is the property of the real estate board(s) and can be licensed, resold, or otherwise dealt with by the board(s). The Seller further acknowledges that the real estate board(s) may, during the term of the listing and thereafter, distribute the information in the database, within the board's MLS System to any persons authorized to use such service which may include other brokerages, government departments, appraisers, municipal organizations and others; market the Property, at its option, in any medium, including electronic media; during the term of the listing and thereafter, compile, retain and publish any statistics including historical data within the board's MLS System and retain, reproduce and display photographs, images, graphics, audio and video recordings, virtual tours, drawings, floor plans, architectural designs, artistic renderings, surveys and listing descriptions which may be used by board members to conduct comparative analyses; and make such other use of the information as the Brokerage and/or real estate board(s) deem appropriate, in connection with the listing, marketing and selling of real estate during the term of the listing and thereafter. [Emphasis added.]

**164** The wording in the Listing Agreements from 2003 onwards is substantially similar to that quoted above. However, the phrase "during the term of the listing [page623] and thereafter" (underlined above), first appears in 2012. The Use and Distribution of Information clause in the Listing Agreement is broad and unrestricted. Sellers are informed that their data could be used for several purposes: for distribution in the database to market their house; to compile, retain, and publish statistics; for use as part of comparative market analysis; and any other use in connection with the listing, marketing, and selling of real estate. Nothing in the text implies the data would only be used during the time the listing is active. Indeed, the use of data for historical statistics of selling prices necessitates that the data will be kept. The Tribunal noted that TREB's policies 102 and 103 add that, apart from inaccurate data, "[n]o other changes will be made in the historical data" (TR, at paragraph 401). We note as well that clause 11 of the Listing Agreement allows for the property to be marketed "using any medium, including the internet".

**165** PIPEDA only requires new consent where information is used for a new purpose, not where it is distributed via new methods. The introduction of VOWs is not a new purpose-the purpose remains to provide residential real estate services and the Use and Distribution of Information clause contemplates the uses in question. The argument that the consents were insufficientbecause they did not contemplate use of the internet in the manner targeted by the VOW Policy-does not accord with the unequivocal language of the consent.

(c) **Conduct of the Parties**

**166** The conduct of the parties may be considered in the interpretation of a contract. Given our conclusion as to the correct interpretation of the consents, it is not necessary to consider the contextual elements or conduct of [page624] the parties. However, we choose to do so here because it illuminates and reinforces our conclusion arising from the terms of the contract itself.

**167** In *Sattva*, the Supreme Court of Canada stated that, with some limitations, a contract's factual matrix includes "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable [person]" (*Sattva*, at paragraph 58 citing *Investors Compensation Scheme v. West Bromwich Building Society*, [1997] UKHL 28, [1998] 1 All E.R. 98, at page 114). Thus, the conduct of the parties forms part of the factual matrix of the contract and can, subject to some restrictions, inform the interpretation of its terms.

**168** The extent to which the factual matrix, including the parties' conduct, may inform the interpretation is subject to the "overwhelming principle" (formulated in *Sattva*, but characterized as such in *Teal Cedar Products Ltd. v. British Columbia*, *2017 SCC 32*, *[2017] 1 S.C.R. 688*, *411 D.L.R. (4th) 385* (*Teal Cedar*), at paragraph 55). There are two elements to the overwhelming principle. The factual matrix cannot be given excessive weight (so as to "overwhelm" the contract); and the factual matrix cannot be interpreted in such isolation from the text of the contract such that a new agreement is effectively created (*Sattva*, at paragraph 57; *Teal Cedar*, at paragraphs 55-56 and 62).

**169** In *Calian*, this Court observed that "the clear language of a contract must always prevail over the surrounding circumstances" (*Calian*, at paragraph 59). Further, the factual matrix may only be considered to the extent that it helps determine the "mutual and objective intentions of the parties as expressed in the words of the contract" (*Sattva*, at paragraph 57). Indeed, only evidence revealing "knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting" may inform the interpretation of the contract (*Sattva*, at paragraph 58). For example, the subjective intention of one party cannot be relied upon to interpret the meaning of a contract (*Sattva*, at paragraph 59; *ING Bank N.V. v. Canpotex [page625] Shipping Services Ltd.*, *2017 FCA 47* (*ING Bank*), at paragraphs 112 and 121). Reliance of that sort would offend the parol evidence rule, i.e., that evidence external to the contract that would "add to, subtract from, vary, or contradict a contract that has been wholly reduced to writing" is inadmissible (*Sattva*, at paragraph 59; *ING Bank*, at paragraphs 112 and 121).

**170** As far as standard form contracts are concerned, the factual matrix is less relevant (*Ledcor*, at paragraphs 28 and 32). This is in keeping with the rationale underlying the correctness standard for standard form contracts: that contracts of this nature are not negotiated, but rather offered on a "take-it-or-leave-it" basis. However, in *Ledcor*, Wagner J. observed at paragraph 31 that some surrounding circumstances, such as the purpose of the contract, the nature of the relationship it creates, and the market or industry in which it operates, may be considered:

> I agree that factors such as the purpose of the contract, the nature of the relationship it creates, and the market or industry in which it operates should be considered when interpreting a standard form contract. However, those considerations are generally not "inherently fact specific?: *Sattva*, at paragraph 55. Rather, they will usually be the same for everyone who may be a party to a particular standard form contract. This underscores the need for standard form contracts to be interpreted consistently, a point to which I will return below.

**171** Applying these principles to the facts as found by the Tribunal, there is nothing in the evidence that would suggest that TREB considered that the consents were inadequate or that TREB drew a distinction between the means of communication of information. To the contrary, TREB's conduct, as well as the testimony of its CEO, are only consistent with the conclusion that it considered the consents were sufficiently specific to be compliant with PIPEDA in the electronic distribution of the disputed data on a VOW, and that it drew no distinction between the means of distribution.

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**172** We note as well that TREB's position that PIPEDA mandates the VOW Policy is inconsistent with some of its own evidence. For example, TREB refused a request by a seller to remove the seller's MLS listing information, noting that its policy respected PIPEDA requirements (TR, at paragraph 400).

**173** The Tribunal also noted that TREB sought legal advice with respect to whether the consents were adequate to address the privacy issues related to the posting of photographs of the interior of homes, and, consequentially changed the consent to provide express authorization with respect to images. There was no evidence that similar steps were contemplated or taken with respect to the sold or pending sold information. Similarly, TREB sought legal advice with respect to the provision of sold data to members. That advice noted that "a strong argument can be

made that the words conduct comparative market analyses'" in the consents authorised disclosure of selling price information to prospective clients.

**174** Finally, the Tribunal's view on the scope of consents is consistent with the direction of the Supreme Court of Canada in *Royal Bank of Canada v. Trang*, *2016 SCC 50*, *[2016] 2 S.C.R. 412*, at paragraphs 36-42. There the Court held that a mortgage balance was less sensitive information because the principal, the rate of interest, and due dates were all publicly available under provincial land registry legislation. In this case, the selling price of every home in Ontario is publicly available under the same legislation. When the consents are considered in light of the nature of the privacy interests involved, the Tribunal's conclusion that they were sufficient takes on added strength.

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**175** This ground of appeal therefore fails and we now turn to the last issue raised by the appeal.

D. *Copyright in the MLS Database*

**176** TREB and CREA submit that the Tribunal erred in finding that TREB does not have copyright in the database. In our view this ground of appeal fails. In light of the determination that the VOW Policy was anti-competitive, subsection 79(5) of the *Competition Act* precludes reliance on copyright as a defence to an anti-competitive act. This is sufficient to dispose of the appeal in respect of copyright.

**177** While not strictly necessary to do so, we will address CREA's contention that the Tribunal applied the incorrect legal test to determine whether copyright exists. On this point we agree. It is, however, an error of no consequence. The same result is reached on the application of the correct law.

**178** We turn to the Subsection 79(5) issue. Subsection 79(5) of the *Competition Act* provides:

> **79** ...
>
> **Exception**
>
> **(5)** For the purpose of this section, an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the *Copyright Act*, *Industrial Design Act*, *Integrated Circuit Topography Act*, *Patent Act*, *Trade-marks Act* or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act.

**179** Subsection 79(5) seeks to protect the rights granted by Parliament to patent and copyright holders and, at the same time, ensure that the monopoly and exclusivity rights created are not exercised in an anti-competitive manner. The language of subsection 79(5) is unequivocal. It does not state, as [page628] is contended, that any assertion of an intellectual property right shields what would otherwise be an anti-competitive act.

**180** Parliament clearly signaled, through the use of the word "only", to insulate intellectual property rights from allegations of anti-competitive conduct in circumstances where the right granted by Parliament, in this case, copyright, is the sole purpose of exercise or use. Put otherwise, anti-competitive behaviour cannot shelter behind a claim of copyright unless the use or protection of the copyright is the sole justification for the practice.

**181** TREB attached conditions to the use of its claimed copyright rights in the disputed data. For the reasons given earlier, we see no error in the Tribunal's findings as to the anti-competitive purpose or effect of the VOW Policy. The Tribunal found that the purpose and effect of those conditions was to insulate members from new entrants and new forms of competition. The purpose, therefore, of any asserted copyright was not "only" to exercise a copyright interest.

**182** While this is sufficient to dispose of this ground of appeal, as noted earlier, we will, for the sake of completeness, address the second alleged error in the Tribunal's analysis of copyright.

**183** Copyright is a creature of statute. The *Copyright Act* provides that copyright exists for "every original literary, dramatic, musical and artistic work" created by Canadians (section 5). This phrase is defined at section 2 to include compilations, which is in turn defined to include works "resulting from the selection or arrangement of ... data". The classification of the database as a compilation is not contested on appeal.

**184** The meaning of the word "original" in section 5 of the Copyright Act was considered by the Supreme [page629] Court in *CCH Canadian Ltd. v. Law Society of Upper Canada*, 2004 SCC 13, [2004] 1 S.C.R. 339 (*CCH*) [at paragraph 16]:

> ... For a work to be "original" within the meaning of the *Copyright Act*, it must be more than a mere copy of another work. At the same time, it need not be creative, in the sense of being novel or unique. What is required to attract copyright protection in the expression of an idea is an exercise of skill and judgment. By skill, I mean the use of one's knowledge, developed aptitude or practised ability in producing the work. By judgment, I mean the use of one's capacity for discernment or ability to form an opinion or evaluation by comparing different possible options in producing the work. This exercise of skill and judgment will necessarily involve intellectual effort. The exercise of skill and judgment required to produce the work must not be so trivial that it could be characterized as a purely mechanical exercise. For example, any skill and judgment that might be involved in simply changing the font of a work to produce "another" work would be too trivial to merit copyright protection as an "original" work.

**185** The point of demarcation between a work of sufficient skill and judgment to warrant a finding of originality and something less than that_a mere mechanical exercise_is not always self-evident. This is particularly so in the case of compilations. It is, however, within the parameters of the legal test, a highly contextual and factual determination.

**186** This is not a new observation. In *Édutile Inc. v. Automobile Protection Assn.*, [2000] 4 F.C. 195 (2000), 6 C.P.R. (4th) 211 (C.A.) the Court acknowledged that "[i]t is not easy in compilation situations to draw a line between what signifies a minimal degree of skill, judgment and labour and what indicates no creative element" (at paragraph 13). Although decided before *CCH*, the observation remains apposite.

**187** There is, however, guidance in the case law as to the criteria relevant to the determination of whether the threshold of originality is met. In *Red Label Vacations Inc. (redtag.ca) v. 411 Travel Buys Ltd. (411travelbuys.ca)*, 2015 FC 18, 473 F.T.R. 38, [page630] Manson J. noted that "when an idea can be expressed in only a limited number of ways, then its expression is not protected as the threshold of originality is not met" (at paragraph 98, citing *Delrina Corp. (cob Carolian Systems) v. TrioletSystems Inc.* (2002), 58 O.R. (3d) 339, 17 C.P.R. (4th) 289, at paragraphs 48-52, leave to appeal to S.C.C. refused, 29190 (28 November, 2002) [2002] 4 S.C.R. v]).

**188** In *Tele-Direct* the Court found a compilation not to be original in part because it was done in accordance with "commonplace standards of selection in the industry" (at paragraphs 6-7). Although *Tele-Direct* predates *CCH*, the proposition that industry standards may be relevant to the originality analysis is a legitimate, residual consideration (see e.g. *Harmony Consulting Ltd. v. G.A. Foss Transport Ltd.*, 2011 FC 340, 92 C.P.R. (4th) 6, at paragraphs 34, 39, 65, 77 and 182-188, affd 2012 FCA 226, 107 C.P.R. (4th) 1 (*Harmony FCA*), at paragraphs 37-38; *Geophysical Service Inc. v Encana Corp.*, 2016 ABQB 230, 38 Alta. L.R. (6th) 48 (*Geophysical*), at paragraph 105).

**189** Applying the guidance of the Supreme Court in *CCH*, it is important to view adherence to industry standards as, at best, one factor to be considered amongst many. In *Geophysical*, Eidsvik J. explained there is no steadfast rule that "there is no entitlement to copyright protection ... where the selection or arrangement is directed by accepted and common industry practices" (at paragraphs 100-101):

> ... these cases [that considered "common industry practices"] do not stand for such steadfast rules or copyright criteria. Certainly, these considerations were part of the analysis in those cases in deciding whether the production was an original work, but they are not the test. The judge in each case made a factual determination about whether sufficient skill and judgment was brought to the work to merit the "original" finding.

[page631]

**190** However, if observing industry standards amounts merely to "mechanical amendments", originality will not be found (*Harmony FCA*, at paragraph 37).

**191** In *Distrimedic Inc. v. Dispill Inc.*, *2013 FC 1043*, *440 F.T.R. 209*, de Montigny J. (as he then was) wrote that "when the content and layout of a form is largely dictated by utility and/or legislative requirements, it is not to be considered original" (at paragraph 324). He continued and observed that compilations (at paragraph 325):

> ... will not be considered to have a sufficient degree of originality when the selection of the elements entering into the work are dictated by function and/or law, and where their arrangement into a tangible form of expression is not original. Only the visual aspect of the work is susceptible to copyright protection, if original.

**192** In this context, TREB and CREA argue that the Tribunal wrongly required proof of creativity and went beyond the appropriate test for originality. After reviewing the MLS database, the Tribunal noted the "absence of a creative element" (TR, at paragraph 732). Further, while the Tribunal cited *CCH* for the correct originality test in paragraph 733, it then relied on *Tele-Direct* to invoke and apply the element of creativity which, post-*CCH*, is not the correct test (*CCH*, at paragraph 25).

**193** We agree with the appellant on this point. However, in view of the Tribunal's findings of fact, applying the correct test, we reach the same result.

**194** The Tribunal considered a number of criteria relevant to the determination of originality (at paragraphs 737-738 and 740-745). Those included the process of data entry and its "almost instantaneous" appearance in the database. It found that "TREB's specific compilation of data from real estate listings amounts to a mechanical exercise" (TR at para. 740). We [page632] find, on these facts, that the originality threshold was not met.

**195** In addition, we do not find persuasive the evidence that TREB has put forward relating to the use of the database. How a "work" is used casts little light on the question of originality. In addition, we agree with the Tribunal's finding that while "TREB's contracts with third parties refer to its copyright, [...] that does not amount to proving the degree of skill, judgment or labour needed to show originality and to satisfy the copyright requirements" (TR, at paragraph 737).

**196** We would therefore dismiss this ground of appeal.

## VI. Conclusion

**197** For the reasons above, we would dismiss the appeal with costs.

NEAR J.A.:— I agree.

# Canada (Commissioner of Competition) v. CCS Corp., [2012] C.C.T.D. No. 14

Canada Competition Tribunal Decisions

Canada Competition Tribunal

Ottawa, Ontario

Panel: S. Simpson J. (Chairperson), P. Crampton C.J. and Dr. W. Askanas

Heard: November 16-18, 22-25, 29-30 and December 1-2, 13-14,

2011.

Decision: May 29, 2012.

File No.: CT-2011-002

Registry Document No.: 189

**[2012] C.C.T.D. No. 14** | *[2012] D.T.C.C. no 14* | *2012 Comp. Trib. 14*

Reasons for Order and Order IN THE MATTER OF the Competition Act, R.S.C. 1985, c. C-34, as amended; AND IN THE MATTER OF an Application by the Commissioner of Competition for an Order pursuant to section 92 of the Competition Act; AND IN THE MATTER OF the acquisition by CCS Corporation of Complete Environmental Inc. Between The Commissioner of Competition (applicant), and CCS Corporation, Complete Environmental Inc., Babkirk Land Services Inc., Karen Louise Baker, Ronald John Baker, Kenneth Scott Watson, Randy John Wolsey, and Thomas Craig Wolsey (respondents)

(409 paras.)

## Case Summary

**Commercial law — Competition — Restrictive trade practices — Mergers — Powers of Competition Tribunal — Factors to be considered — Barriers to entry — Whether effective competition will remain — Removal of a competitor — Order in respect of completed merger — Application by Competition Commissioner for order pursuant to s. 92 of Competition Act allowed — CCS purchased shares of Complete Environmental, acquiring Babkirk Land Services facility — Commissioner alleged prevention of competition between secure landfills taking hazardous solid waste — Despite likely un-profitability of bioremediation processing, Babkirk facility would have operated in meaningful competition with a CCS secure landfill site in area until spring 2013 — Efficiencies claimed by CCS did not satisfy s. 96 of Act, as meaningful competition would have reduced tipping fees by 10 per cent — Least intrusive remedy was order for divesture of shares — Competition Act, ss. 2(1), 91, 92, 96.**

Application by the Commissioner of Competition for an order pursuant to s. 92 of the Competition Act. CCS was a private energy and environmental waste management company that served oil and gas producers in Western Canada. It owned the only two secure landfills in North-Eastern British Columbia permitted to accept solid hazardous waste. Babkirk Land Services (BLS) operated a facility with a permit for treatment and short-term storage of hazardous waste. The facility stopped accepting waste and steps were taken to obtain permits for construction of a secure landfill capable of accepting solid, hazardous waste at the Babkirk site. In 2009, Complete Environmental was created to acquire the shares of BLS from its original principals. Complete Environmental operated other landfill and solid waste business interests. In February 2010, BLS received a permit authorizing construction of a secure landfill, but had not commenced operations. In January 2011, CCS

acquired the shares of Complete Environmental and ownership of BLS. The Commissioner alleged that the merger was likely to prevent competition substantially in the market for hazardous waste disposal services in North-Eastern British Columbia. The Commissioner alleged that CCS owned the only two operational secure landfills for solid hazardous waste in the area and thus had a monopoly and market power that allowed price discrimination and pricing of tipping fees above a competitive level. The Commissioner alleged that, as at the date of the merger, Complete Environmental was a poised entrant to the market, as it had obtained the regulatory approvals needed to operate a secure landfill for hazardous solid waste at the Babkirk site. The Commissioner applied for an order dissolving the transaction, or alternatively, a divestiture order requiring CCS to dispose of the shares or assets of BLS in a manner to be directed by the Tribunal. The respondents submitted that a merger was not effected within the contemplation of the Competition Act, as there was no business in operation at the Babkirk site. They contended that Complete Environmental was not a viable market entrant and that in the absence of the merger, the vendors would likely have processed waste using bioremediation, a type of treatment that would not have resulted in meaningful competition with CCS in respect of the supply of secure landfill services. They further challenged the Commissioner's interpretation of the potentially contestable area, and the quantifiable effects of the merger.

HELD: Application allowed.

The acquisition constituted a merger under the Competition Act, as Complete Environmental was actively engaged in the development of the Babkirk Site as a hazardous waste treatment facility at the time of the transaction. The merger was likely to prevent competition substantially in the market for the supply of secure landfill services for solid hazardous waste from oil and gas producers in the geographic market, or potentially contestable area, as identified by the CCS expert. The significant time and uncertainty associated with market entry required 30 months from site selection to the completed construction and operation of a secure landfill in the relevant market. In the absence of the merger, the vendors would likely have operated the Babkirk facility themselves and constructed a new secure landfill by October 2011, operating as a complement to their bioremediation business until no later than October 2012. The bioremediation business would likely have been unprofitable, requiring the vendors to either focus on the secure landfill business, or sell the facility to a secure landfill operator. In either case, until no later than spring 2013, the Babkirk facility would have operated in meaningful competition with one of the CCS secure landfill sites in the area. The prevention of that competition by the merger constituted a likely substantial prevention of competition for the purpose of the Act. The efficiencies claimed by CCS did not meet the requirements of s. 96 of the Act given the absence of meaningful competition. CCS was a monopolist in that market and its significant exercise of market power was maintained as a result of the merger. A decrease in average tipping fees of at least 10 per cent was prevented by the merger. Divestiture was an effective remedy and was the least intrusive option. The Tribunal thus ordered CCS to divest the shares or assets of BLS.

## Statutes, Regulations and Rules Cited:

Competition Act, *R.S.C. 1985, c. C-34, s. 2*(1), s. 45, s. 45.1, s. 79, s. 79(7), s. 90.1, s. 90.1(10), s. 91, s. 92, s. 93, s. 96, s. 96(1), s. 96(3), s. 100

Environmental Management Act, *SBC 2003, c 53*,

Hazardous Waste Regulation, (*B.C. Reg. 63/88*),

Interpretation Act, *R.S.C. 1985, c. I-21, s. 12*

Investment Canada Act, *R.S.C. 1985, c. 28 (1st Supp.)*,

## Appearances

For the applicant:

The Commissioner of Competition:

Nikiforos Iatrou Jonathan Hood

For the respondents:

CCS Corporation, Complete Environmental Inc. and Babkirk Land Services Inc.:

Linda Plumpton Crawford Smith Dany Assaf Justin Necpal

Karen Louise Baker, Ronald John Baker, Kenneth Scott Watson, Randy John Wolsey, and Thomas Craig Wolsey:

J. Kevin Wright Morgan Burris Brent Meckling

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## REASONS FOR ORDER AND ORDER

### A. EXECUTIVE SUMMARY

**1** The Tribunal has decided on a balance of probabilities that the Merger is likely to prevent competition substantially in the market for the supply of secure landfill services for solid hazardous waste from oil and gas producers in a geographic market which, at a minimum, is the area identified by CCS' expert, Dr. Kahwaty, as the "Potentially Contestable Area".

**2** The Tribunal has concluded that CCS is a monopolist in the geographic market and that it exercises significant market power which is being maintained as a result of the Merger.

**3** Although Dr. Baye, the Commissioner's expert, suggested a wide range of likely price decreases in the absence of the Merger, the Tribunal has found that a decrease in average tipping fees of at least 10% was prevented by the Merger.

**4** There is significant time and uncertainty associated with entry. The Tribunal has concluded that effective entry would likely take a minimum of 30 months from site selection to the completed construction and operation of a secure landfill in the relevant market.

**5** The Tribunal has also decided that, in the absence of the Merger, the Vendors would likely not have sold the Babkirk Facility in the summer of 2010 but would have operated it themselves and would have constructed a new secure landfill with a capacity of 125,000 tonnes by October of 2011. This landfill would likely have operated as a complement to the Vendors' bioremediation business until no later than October 2012.

**6** The Tribunal has also concluded that the Vendors' bioremediation business would likely have been unprofitable and that by October 2012, the Vendors would likely have changed their business plan to significantly focus on the secure landfill part of their business or would have sold the Babkirk Facility to a secure landfill operator. In either case, no later than the spring of 2013, the Babkirk Facility would have operated in meaningful competition with CCS' Silverberry secure landfill. It is the prevention of this competition by the Merger which constitutes a likely substantial prevention of competition.

**7** The efficiencies claimed by CCS do not meet the requirements of section 96 of the Act.

**8** Divestiture is an effective remedy and is the least intrusive option.

**9** The application has been allowed. The Tribunal has ordered CCS to divest the shares or assets of BLS.

**10** In dealing with the facts of this case, the Tribunal's conclusions were all based on an analysis of whether the events at issue were likely to occur.

**B. INTRODUCTION**

**11** The Commissioner of Competition (the "Commissioner") has applied for an order under section 92 of the *Competition Act*, *R.S.C. 1985, c. C-34*, as amended (the "Act"), dissolving a transaction in which CCS Corporation ("CCS") acquired the shares of Complete Environmental Inc. ("Complete") and ownership of its wholly-owned subsidiary Babkirk Land Services Inc. ("BLS") on January 7, 2011 (the "Merger"). In the alternative, the Commissioner requests a divestiture order requiring CCS to dispose of the shares or assets of BLS in a manner to be directed by the Tribunal.

**12** In her application (the "Application"), the Commissioner alleges that the Merger is likely to prevent competition substantially in the market for hazardous waste disposal services in North-Eastern British Columbia ("NEBC") because, at the date of the Merger, Complete was a poised entrant by reason of having obtained the regulatory approvals needed to operate a secure landfill for hazardous solid waste on a site at Mile 115, Alaska Highway, Wonowon, B.C. (the "Babkirk Site").

**13** Pending the Tribunal's decision on this application, CCS undertook to maintain all approvals, registrations, consents, licenses, permits, certificates and other authorizations necessary for the operation of a hazardous waste disposal facility (the "Babkirk Facility" or "Babkirk") on the Babkirk Site. Complete's other assets and businesses were not subject to this undertaking.

**C. THE PARTIES**

**14** The Commissioner is the public official who is responsible for the enforcement of the Act.

**15** CCS is a private energy and environmental waste management company. Its customers are mainly oil and gas producers in Western Canada. CCS owns the only two operating secure landfills in NEBC that are permitted to accept solid hazardous waste. One is the Silverberry secure landfill ("Silverberry"). It opened in 2002. It is located approximately 50 km north-west of Fort St. John. The other is called Northern Rockies secure landfill ("Northern Rockies"). It opened in 2009 and is situated about 340 km northwest of Silverberry, about 260 km from the Babkirk Site and approximately 20 km south of Ft. Nelson. CCS also operates a variety of different types of secure landfills in Alberta and Saskatchewan and owns a separate waste management business called Hazco Waste Management ("Hazco"). Schedule "A" hereto is a map showing the locations of the landfills which are relevant to this Application.

**16** BLS was founded in 1996 by Murray and Kathy Babkirk (the "Babkirks"). BLS operated a facility which was not a secure landfill. It had a permit for the treatment and short-term storage of hazardous waste on the 150 acre (approx.) Babkirk Site. It is located approximately 81 km or 1 1/2 hours by car, northwest of Silverberry. The Babkirks operated their facility for approximately six years under a permit from the British Columbia Ministry of the Environment ("MOE") which was issued in 1998. However, in 2004, they stopped accepting waste. Two years later, the Babkirks retained SNC Lavalin ("SNCL") to prepare the documents BLS needed to apply for permits for the construction of a secure landfill capable of accepting solid, hazardous waste at the Babkirk Site.

**17** The individual Respondents are the former shareholders of Complete who sold their shares to CCS in the Merger. Karen and Ron Baker are married and Ken Watson is their son-in-law. Tom Wolsey is Randy Wolsey's father. The former shareholders will be referred collectively as the "Vendors". All the Vendors, except Tom Wolsey, gave evidence in this proceeding.

**18** In November of 2006, Randy Wolsey, acting on his own behalf and on behalf of other individual Respondents,

negotiated a "handshake agreement" with the Babkirks to purchase the shares of BLS. The deal was conditional on BLS obtaining approval for the secure landfill from the Environmental Assessment Office ("EAO"). In April 2007, the Vendors incorporated Complete (initially called Newco) to be the company that would eventually purchase the shares of BLS. After an extensive process of consultation and review, the EAO issued a certificate (the "EA Certificate") to BLS on December 3, 2008. Four months later, in April 2009, Complete acquired all the outstanding shares of BLS and it became a wholly-owned subsidiary of Complete. Thereafter, on February 26, 2010, BLS received a permit from the MOE authorizing the construction of a secure landfill, with a maximum storage capacity of 750,000 tonnes, and a storage and treatment facility with a maximum capacity of 90,000 tonnes (the "MOE Permit").

**19** At the time of the Merger, Complete had other business interests. It operated municipal solid waste landfills for the Peace River Regional District as well as a solid waste transfer station. In addition, it owned a roll-off container rental business (the "Roll-off Bin Business"). Since the Merger, those businesses have been operated by Hazco.

**20** CCS, Complete and BLS will be described collectively as the "Corporate Respondents".

**D. THE PARTIES' POSITIONS The Commissioner**

**21** The Commissioner alleges that because CCS owns the only two operational secure landfills for solid hazardous waste in NEBC, it has a monopoly and associated market power which allows it to price discriminate between different customers and set the prices for hazardous waste disposal above a competitive level. These prices are known as "Tipping Fees".

**22** The Commissioner alleges that Complete was ready to enter the market for secure landfill services in NEBC and that it was likely that competition between Complete and CCS would have caused a decline in average Tipping Fees in NEBC of at least 10%. Alternatively, the Commissioner alleges that the Vendors would have sold Complete to a purchaser which would have operated a secure landfill in competition with CCS. Finally, the Commissioner maintains that any efficiencies associated with the Merger are likely to be *de minimis*.

**The Respondents**

**23** The Vendors submit that their sale of Complete was not a Merger under the Act because there was no business in operation at the Babkirk Site. They also deny (i) that Complete was poised to enter the market for the direct disposal of hazardous waste into a secure landfill and (ii) that, in the absence of the Merger, an alternative buyer would have purchased Complete and operated a secure landfill. The Respondents maintain that if the Vendors had not sold Complete to CCS, they would likely have processed hazardous waste at the Babkirk Facility using a treatment technique called bioremediation. This type of treatment would have been complemented by a half cell (125,000 tonnes) of secure landfill. The secure landfill would only have been used to store the small amount of hazardous waste that could not be successfully treated, and would not have been used to engage in meaningful competition with CCS in respect of the supply of secure landfill services.

**24** The Corporate Respondents challenge both the Commissioner's interpretation of CCS' pricing behaviour and her prediction of the anti-competitive effects she has alleged would likely result from the Merger. Among other things, they allege that the Commissioner's approach to market definition is fundamentally flawed and that the area in which there is scope for competition between the Babkirk and Silverberry facilities is, at best, limited to the very small "Potentially Contestable Area" identified by CCS' expert, Dr. Kahwaty (the "Contestable Area").

**25** The Corporate Respondents also submit that the efficiencies resulting from the Merger are likely to be greater than, and will offset, the effects of any prevention of competition brought about by the Merger. They further argue that the Commissioner failed to meet her burden of quantifying the deadweight loss as part of her case in chief. As a result, they say that the Tribunal should conclude that the Merger is not likely to result in any quantifiable effects.

**26** Finally, all the Respondents submit that if there is to be remedy, it should be divestiture, rather than dissolution.

**E. THE EVIDENCE**

**27** Attached as Schedule "B" is a list of the witnesses who testified for each party and a description of the documentary evidence.

**F. INDUSTRY BACKGROUND**

**28** The management of solid hazardous waste generated by oil and gas operators is regulated in British Columbia by the *Environmental Management Act*, *SBC 2003, c 53* (the "EMA") and regulations. If the waste produced meets the definition of "hazardous waste" found in the *Hazardous Waste Regulation*, (*B.C. Reg. 63/88*) (the "HW Regulation"), oil and gas operators wishing to dispose of hazardous waste must do so within the confines of the legislative framework. The MOE is responsible for administering the EMA and HW Regulation. Hereinafter, hazardous waste as defined in the HW Regulation which is solid will be described as "Hazardous Waste".

**29** Under the HW Regulation, a person must receive a permit from the MOE to operate a facility called a secure landfill that can accept Hazardous Waste for disposal. A "secure landfill" is defined in the HW Regulation as a disposal facility where Hazardous Waste is placed in or on land that is designed, constructed and operated to prevent any pollution from being caused by the facility outside of the area of the facility ("Secure Landfill").

**Disposal at Secure Landfills**

**30** Oil and gas drilling operators (also called waste generators) produce two major types of Hazardous Waste that can be disposed of at a Secure Landfill: contaminated soil and drill cuttings. The contaminants are typically hydrocarbons, salts, and metals.

**31** Hydrocarbons are categorized as light-end hydrocarbons and heavy-end hydrocarbons. The evidence shows that Hazardous Waste often includes hydrocarbons of both types.

**32** Oil and gas generators can contaminate soil with salt when, among other things, they inadvertently spill produced water or brine. Produced water is water that has been trapped in underground formations and is brought to the surface along with the oil or gas. Metals can be found in Hazardous Waste because they occur naturally or because they have been included in additives used in drilling.

**33** The HW Regulation states that a Secure Landfill cannot be used to dispose of liquid hazardous waste.

**34** Hazardous Waste from "legacy sites" can also be disposed of at Secure Landfills. Dr. Baye defined legacy waste as "accumulated waste from decades of drilling activity that has been left at the drilling site" ("Legacy Waste").

**35** Operators pay third-party trucking companies to transport Hazardous Waste to Secure Landfills. Transportation costs are typically a substantial portion of waste generators' overall costs of disposal. Dr. Baye estimated that a generator would pay $4 to $6 per tonne for every hour spent transporting waste from, and returning to a generator's site.

**36** At the hearing, Mr. **[CONFIDENTIAL]** and Mr. **[CONFIDENTIAL]**, indicated that no ongoing liability is shown on their books once Hazardous Waste is sent to Secure Landfills, even though generators could be liable if a Secure Landfill operator goes bankrupt or if the landfill fails and Hazardous Waste leaches out of the facility.

**37** The MOE has issued five permits for Secure Landfills. Four of them are in NEBC and are currently valid: Silverberry, Northern Rockies, Babkirk and Peejay.

**38** Silverberry has a permitted capacity which allows it to accept 6,000,000 tonnes of waste. At 1.52 tonnes per

cubic meter, which is the same figure used to calculate tonnes at Silverberry, Northern Rockies' permitted capacity is 3,344,000 tonnes. In 2010, **[CONFIDENTIAL]** tonnes of Hazardous Waste was tipped at Silverberry and, in that year, Northern Rockies accepted **[CONFIDENTIAL]** tonnes.

**39** Tipping Fees vary depending on the type of waste. According to the evidence given by Dr. Baye, the average Tipping Fee for all substances at Silverberry was **[CONFIDENTIAL]** per tonne in 2010 and the average Tipping Fee for all waste tipped at Northern Rockies in the same year was **[CONFIDENTIAL]** per tonne.

**40** Peejay is located in a relatively inaccessible area near the Alberta border. It was developed by a First Nations community to serve nearby drilling operators such as Canadian Natural Resources Limited ("CNRL"). Construction specifications and an operational plan for Peejay were approved by the MOE on March 11, 2009. However, the Secure Landfill has not yet been constructed and there may be financial difficulties at the project.

**41** There are presently no Secure Landfills in operation in NEBC which are owned by oil and gas generators.

**Bioremediation - Methodology**

**42** Bioremediation is a method of treating soil by using micro-organisms to reduce contamination. The microbes can be naturally occurring or they can be deliberately added to facilitate bioremediation. In NEBC, bioremediation usually takes place on an oil and gas producing site where the waste is generated. Bioremediation can also be undertaken offsite but the evidence indicates that there are no offsite bioremediation facilities currently operating in NEBC.

**43** A common bioremediation technique is landfarming. In landfarming, contaminated waste is placed on impermeable liners and is periodically aerated by being turned over or tilled. The landfarming technique the Vendors planned to use involves turning soil to create windrows which are **[CONFIDENTIAL]** triangular-shaped piles of soil **[CONFIDENTIAL]**.

**44** The preponderance of the evidence showed that, given sufficient time, light-end hydrocarbons can be successfully bioremediated in NEBC despite the cold if the clay soil is broken up. However, the Tribunal has concluded that soil contaminated with heavy-end hydrocarbons is not amenable to cost effective bioremediation because it is difficult, unpredictable, and very time consuming. Further, waste contaminated with metals and salts cannot be effectively bioremediated with technologies currently approved for use in Canada.

**45** Once bioremediation is complete, an operator will normally hire a consultant to determine whether the Hazardous Waste can be certified as "delisted" in accordance with a delisting protocol. If so, there is no further liability associated with that particular waste.

**46** Mr. Watson testified that his company, Integrated Resource Technologies Ltd. ("IRTL"), had successfully bioremediated hydrocarbon-contaminated soil throughout the winter in NEBC and Northern Alberta. Since about 2002, he has been using a specially designed machine from Finland, the "ALLU AS-38H". This machine **[CONFIDENTIAL]** is capable of breaking up heavy clay so that bacteria can enter the windrow and consume the hydrocarbon contaminants.

**G. THE ISSUES**

**47** The following broad issues are raised in this proceeding:

1. Is CCS' acquisition of Complete a "merger"?
2. What is the product dimension of the relevant market?
3. What is the geographic dimension of the relevant market?

4. Is the Merger Pro-Competitive?
5. What is the analytical framework in a "prevent" case?
6. Is the Merger likely to prevent competition substantially?
7. What is the burden of proof on the Commissioner and on a Respondent when the efficiencies defence is pleaded pursuant to section 96 of the Act?
8. Has CCS successfully established an efficiencies defence?
9. Is the appropriate remedy dissolution or divestiture?

**ISSUE 1** **IS CCS' ACQUISITION OF COMPLETE A MERGER?**

**48** As a threshold matter, the Vendors submit that the Application should be dismissed because, at the date of the Merger, Complete was not a "business" within the meaning of section 91 of the Act, given that it was not actively accepting and treating Hazardous Waste, and was not otherwise operational in relation to the supply of Secure Landfill services. Instead, they maintain that Complete was simply an entity which held the assets of BLS, i.e. permits and property. Accordingly, the Vendors' position is that, because CCS acquired assets which had not yet been deployed, it did not acquire a "business", as contemplated by section 91 of the Act. The Vendors also submit that the other businesses owned by Complete and acquired in the Merger are not relevant for the purposes of this Application because the Commissioner does not allege that they caused or contributed to a substantial prevention of competition.

**49** A merger is defined in section 91 as the acquisition of a "business". The section reads as follows:

> In sections 92 to 100, "merger" means the acquisition or establishment, direct or indirect, by one or more persons, whether by purchase or lease of shares or assets, by amalgamation or by combination or otherwise, of control over or significant interest in the whole or a part of a business of a competitor, supplier, customer or other person.
>
> * * *
>
> Pour l'application des articles 92 à 100, "fusionnement" désigne l'acquisition ou l'établissement, par une ou plusieurs personnes, directement ou indirectement, soit par achat ou location d'actions ou d'éléments d'actif, soit par fusion, association d'intérêts ou autrement, du contrôle sur la totalité ou quelque partie d'une entreprise d'un concurrent, d'un fournisseur, d'un client, ou d'une autre personne, ou encore d'un intérêt relativement important dans la totalité ou quelque partie d'une telle entreprise.

**50** Business is defined as follows in subsection 2(1) of the Act (the "Definition"):

> "business" includes the business of
>
> (*a*) manufacturing, producing, transporting, acquiring, supplying, storing and otherwise dealing in articles, and
>
> (*b*) acquiring, supplying and otherwise dealing in services.
>
> It also includes the raising of funds for charitable or other non-profit purposes.
>
> * * *
>
> "entreprise" Sont comprises parmi les entreprises les entreprises :

*a*) de fabrication, de production, de transport, d'acquisition, de fourniture, d'emmagasinage et de tout autre commerce portant sur des articles;

*b*) d'acquisition, de prestation de services et de tout autre commerce portant sur des services.

Est également comprise parmi les entreprises la collecte de fonds à des fins de charité ou à d'autres fins non lucratives.

**51** The Tribunal notes two features of the Definition. First, it uses the word "includes", which means that it is not exhaustive. Second, unlike the definitions of the term "business" found in statutes such as the *Investment Canada Act*, *R.S.C. 1985, c. 28 (1st Supp.)*, the Definition makes no reference to generating profits or revenues.

**52** Turning to the facts, it is the Tribunal's view that, for the reasons described below, Complete was actively engaged in the development of the Babkirk Site as a hazardous waste treatment facility.

**53** Before the Merger, Complete had taken the following steps:

* It had purchased the shares of BLS, thereby acquiring the EA Certificate and the Babkirk Site;
* It had continued the application process and had secured the MOE Permit;
* It had held numerous shareholders' meetings to plan how the Babkirk Site would be developed as a bioremediation facility and how that facility would operate in conjunction with other businesses owned by the Vendors;
* Its shareholders had discussed bioremediation with Petro-Canada and had solicited its interest in becoming a customer for both bioremediation and Secure Landfill services;
* It had hired IRTL and had paid it **[CONFIDENTIAL]** to bioremediate the soil in cell #1 at the Babkirk Facility. This work was undertaken because it was a condition precedent to the construction of the half cell of Secure Landfill;
* It was developing an operations plan for the Babkirk Facility.

**54** In the Tribunal's view, these activities demonstrate that Complete was engaged in the business of developing the Babkirk Site as a Hazardous Waste treatment service that included a Secure Landfill. Since the Definition is not exhaustive, the Tribunal has concluded that it encompasses the activities in which Complete and its shareholders had been engaged at the time of its purchase by CCS. Further, the absence of a requirement for revenue in the Definition suggests to the Tribunal that it covers a business in its developmental stage.

**55** For all these reasons, the Tribunal has concluded that Complete was a business under section 91 of the Act at the date of the Merger.

**56** In view of this conclusion, it is not necessary to decide whether Complete's Roll-off Bin Business or its management of municipal dumps could be businesses for the purposes of section 91 of the Act.

**57** However, in the Chairperson's view, a business being acquired in a merger must have some relevance to a Commissioner's application. In other words, it must have the potential to impact competition in the markets at issue. This observation means that, in this case, Complete's Roll-off Bin Business and its management of municipal dumps would not have been caught by the definition in section 91 because they are not involved in any way in the disposal or treatment of Hazardous Waste. In his separate reasons, Crampton C.J. has taken a different position on this point.

**ISSUE 2 WHAT IS THE PRODUCT DIMENSION OF THE RELEVANT MARKET?**

**The Analysis**

**58** In defining relevant markets, the Tribunal generally follows the hypothetical monopolist approach. As noted in *Commissioner of Competition v. Superior Propane,* 2000 Comp. Trib. 15, 7 C.P.R. (4th) 385 (Comp. Trib.) ("*Propane 1*"), at para. 57, the Tribunal embraces the description of that approach set forth at paragraph 4.3 in the Commissioner's Merger Enforcement Guidelines ("MEGs"), which state:

> Conceptually, a relevant market is defined as the smallest group of products, including at least one product of the merging parties, and the smallest geographic area, in which a sole profit-maximizing seller (a "hypothetical monopolist") would impose and sustain a small but significant and non-transitory increase in price ("SSNIP") above levels that would likely exist in the absence of the merger.

**59** The price that would likely have existed in the absence of or "but for" the merger in a "prevent case" is the Base Price. The burden is on the Commissioner to demonstrate the "Base Price". In this case, Dr. Baye has predicted a decrease in Tipping Fees in the absence of the Merger of at least 10% and in some of his economic modelling the price decrease is as large as 21%. In *The Commissioner of Competition v. Canadian Waste Services Holdings Inc.,* 2001 Comp. Trib. 3; 11 C.P.R. (4th) 425; aff'd 2003 FCA 131, at para. 92, the Tribunal observed that, when a price change can be predicted with confidence, it is appropriate to delineate markets based on the likely future price even if the future level of that price cannot be predicted precisely. In such cases, it may be sufficient for the Commissioner to demonstrate a range in which the likely future price would have fallen.

**60** However, if a reasonable approximation of the likely future price cannot be demonstrated, it may be difficult for the Tribunal to clearly define the boundaries of the relevant market. In such cases, it will nevertheless be helpful for the Tribunal to be provided with sufficient evidence to demonstrate why substitutes that appear to be acceptable at the prevailing price level would or would not remain acceptable at price levels that would likely exist "but for" the merger or anti-competitive practice in question. In any event, evidence about various practical indicia is typically required to apply the hypothetical monopolist approach. The Tribunal recognizes that, like other approaches to market definition, the hypothetical monopolist approach is susceptible to being somewhat subjective in its practical application, in the absence of some indication of what constitutes a "small but significant and non-transitory increase in price" (SSNIP). For this reason, objective benchmarks such as a five percent price increase lasting one year, can be helpful in circumscribing and focusing the inquiry.

**61** In the Application at paragraph 11, the Commissioner alleged that "[t]he anti-competitive effects of the Merger "primarily" affect oil and gas companies disposing of Hazardous Waste produced at oil and gas fields within NEBC." [our emphasis]. However, in his initial report Dr. Baye did not limit the product market to Hazardous Waste produced at oil and gas fields. Nevertheless, during the hearing, Dr. Baye and Dr. Kahwaty essentially agreed that the amount of solid hazardous waste generated by non-oil and gas sources and tipped at Secure Landfills in British Columbia is so small that it does not warrant consideration in these proceedings. Accordingly, in the Tribunal's view, the Commissioner's product market definition is "solid hazardous waste generated by oil and gas producers and tipped into secure landfills in NEBC".

**62** However, the Respondents deny that the product market is as narrow as the Commissioner suggests. They say that it also includes bioremediation and the storage or risk management of waste on the sites where the waste was generated. They assert that these options constrain any market power that CCS may have. We will deal with these positions in turn.

**Evidence about the Use of Bioremediation**

**63** Bioremediation has been described above and the evidence is clear that it is not an acceptable substitute for generators of Hazardous Waste if soil is contaminated with salts or metals. The Tribunal also accepts that, if heavy-end hydrocarbons are present, bioremediation is not cost effective or successful in a reasonable timeframe.

**64** Mr. Andrews gave evidence about the use of bioremediation. He joined the MOE in January 2011. At that time, he was asked to review the E-Licensing Database, which keeps track of the progress made by operators who are bioremediating Hazardous Waste. He found that approximately 50% of the operators who had entries in the Database had reported no annual activity. He said that this indicated that many operators "had stopped actively treating H[azardous] W[aste] at these sites, or at least had stopped reporting any activities to the MOE."

**65** He therefore contacted Conoco Philips Canada, Suncor Energy Inc. ("Suncor"), Progress, Devon Canada Corporation ("Devon") and Apache Canada Ltd. ("Apache"). They accounted for 80% of the registered sites with no reported activity. Among other things, he asked these operators to update their operations plans and submit annual reports.

**66** According to Mr. Andrews' witness statement, three of the operators reported that they had dealt with the Hazardous Waste they were bioremediating by sending it to a Secure Landfill and he anticipated that the remaining operators would do the same because bioremediation had failed. Mr. Andrews also said that Suncor filed an operations plan for its registered bioremediation sites which stated that, in the future, it would be sending all its Hazardous Waste to a Secure Landfill.

**67** Mr. Andrews also described his experience with onsite treatment before he joined the MOE. He stated the following in his witness statement [paragraphs 23-26]:

> I managed the HW at seven sites that CNRL had registered. These sites were allocated north of Fort St John and on existing oil and gas lease sites or on abandoned sites. There were approximately 50,000 tonnes of HW at these sites.
>
> Initially, we tried treating the HW onsite. At each of these sites we put the HW into windrows and used a turner to turn the HW three times per year at each site. Hazco Environmental Services was the contractor that provided the windrow turner. We also added fertilizers and nutrients in the soil to assist in the bioremediation process. The fertilizer is meant to add additional nutrients to aid the bacteria to process the hydrocarbons.
>
> CNRL pursued this treatment process for two years. While CNRL was able to reduce the contaminants in the HW at these sites, it failed to reduce the contaminants enough to "delist" the HW. Delisting HW means reducing the presence of contaminants low enough so that the soil is no longer considered to be HW. CNRL spent significant amounts of money on treatment because the sites required constant monitoring. The sites would get wet and require dewatering out to prevent berm overflow and enable equipment access.
>
> Ultimately, after two years of treatment, it was clear that bioremediation would not work to address the contamination issues. CNRL decided to send the remaining HW to a Secure Landfill, specifically Silverberry, which was the landfill closest to the sites. I was also responsible for this process. It took CNRL approximately 2-3 years and several million dollars to send all the waste to Silverberry.

**68** **[CONFIDENTIAL]**, who works as a Contracting and Procurement Analysist for **[CONFIDENTIAL]**, testified that its current operations in NEBC are in two fields called **[CONFIDENTIAL]**. He indicated that **[CONFIDENTIAL]** uses Secure Landfills to dispose of its Hazardous Waste and that it does not bioremediate because of the associated costs, the time necessary to bioremediate, and the manpower required to undertake bioremediation. He stated that liability has the potential to remain if the Hazardous Waste is not effectively bioremediated and that additional costs might be incurred if the Hazardous Waste, which is not effectively treated, must be tipped into a Secure Landfill. He added that there is ongoing uncertainty about whether bioremediation is effective or not.

**69** **[CONFIDENTIAL]**, the Vice-President of Operations at **[CONFIDENTIAL]**, testified that **[CONFIDENTIAL]** uses an oil-based mud system to reduce friction on horizontal wells and that the oil-based mud cuttings are typically tipped into Secure Landfills. He also stated that **[CONFIDENTIAL]** sees disposal at a Secure Landfill as the most economic alternative for dealing with the Hazardous Waste from drilling, as disposal eliminates the increased

environmental risk and cost of long term storage and/or site remediation. He explained that "[c]ontainment, transport and disposal of hazardous waste generated from drilling operations is currently the only option used by **[CONFIDENTIAL]** for managing hazardous waste generated from drilling." Accordingly, it is clear that, at its current drilling sites, only Secure Landfills are used for disposal.

**70** However, with respect to the Legacy Waste in NEBC on drilling sites which **[CONFIDENTIAL]**, Mr. **[CONFIDENTIAL]** testified that **[CONFIDENTIAL]** will bioremediate some of the waste on these sites. He explained that bioremediation of the Legacy Waste had already been started by **[CONFIDENTIAL]**. He stated that the decision to dispose of Hazardous Waste instead of treating it is taken on a case-by-case basis, and depends on the type and amount of Hazardous Waste present on the legacy site, the likelihood of successful remediation, and the cost of excavation, transport and disposal.

**71** During a review of the HW Regulation undertaken by the MOE, the MOE retained Conestoga-Rovers & Associates to conduct a report on Secure Landfill disposal. The report is entitled "Secure Landfill Disposal Policy Review" and dated March 2011. It states:

> Based on equal weighting of cost, cost variability, timeline, and treatment certainty landfilling [Secure Landfill] is the preferred option under all scenarios. Landfarming [bioremediation] can be an appropriate method for treating hydrocarbon contaminated soils given appropriate concentrations and a multi-year timeline.

**72** Devin Scheck, the Director of Waste Management and Reclamation at the British Columbia Oil and Gas Commission, testified that many operators still choose to dispose of their contaminated soils in Secure Landfills, even in situations where bioremediation is feasible, because of the associated costs and timeframe. He said the following in his witness statement [paragraphs 25-27]:

> In my experience, a significant number of the sites that Operators seek to remediate are remediated by the Operator disposing of the contaminated soils at a landfill. With sites that are only contaminated with light end hydrocarbons, Operators may seek to bioremediate the soil on site, but heavy end hydrocarbons tend to have a poor response to bioremediation. As well, tight clay (which is prevalent in North Eastern B.C. where the oil and gas activity is most prevalent) makes bioremediation difficult, as does the relatively cold weather in the region. The presence of other contaminants, such as salts or metals that exceed CSR standards, prevent bioremediation from being an appropriate option, as salts and metals cannot be bioremediated.
>
> Accordingly, when dealing with anything other than light end hydrocarbons, my experience is that Operators will usually dig up the soil, and dispose of it at a Secure Landfill like Silverberry in B.C. or a closer landfill across the Alberta border, such as the CCS Class II Alberta Landfill at LaGlace.
>
> In my experience, even where bioremediation may be feasible, many Operators will still choose to landfill their contaminated soils. With bioremediation there is much uncertainty about costs, and the timeframe required for treatment is also uncertain. Weather conditions, site access issues, amount/type of treatment, future equipment and labour costs, as well as the costs of ongoing access for treatment and sampling to determine if the soils are remediated contribute to this uncertainty.

**73** Mark Polet, an expert environmental biologist with specialized knowledge in environmental assessment, remediation and reclamation, as well as waste facility management development, stated as follows in paragraph 17 of his expert report:

> Once an Operator in NEBC decides to clean up its waste, the two most practical options available are: 1) the disposal of the waste at an appropriate landfill; or 2) the treatment of the waste onsite through a process known as bioremediation. Operators do not have a uniform preference for either option but, in my experience, will choose an option based on cost, risk, efficacy and other reasons such as environmental stewardship.

**74** At the hearing, Mr. Polet testified that the costs of bioremediation and secure landfilling can be comparable. He stated:

> Once you define the types [of contaminants], you can decide on the most prudent response. And so, for instance, if I found on a site just the light end hydrocarbons with no other types of contamination mixed with it, I would look at bioremediation as an alternative. If it had salts and metals associated with the contamination, as well, then I would lean very strongly to landfill. If it had heavier end hydrocarbons, I would lean strongly to landfill, as well.
>
> In terms of cost, there -- can be quite comparable in price, but of course bioremediation is very limited in what it can be applied to. And the one thing that we've noticed in working in the field is that when bioremediation is not managed properly, then much material actually lands back up in the landfill, anyway. So it has to be well managed to work properly.

**75** There is also evidence about bioremediation in the Statement of Agreed Facts (the "Agreed Facts"). However, at the hearing it became clear that, contrary to the way in which they are presented, some of the facts were not actually agreed. The problematic evidence concerns bioremediation and was gathered in two ways. The evidence in paragraphs 63-67 of the Agreed Facts was given directly to the Commissioner's staff. This evidence will be called "Evidence A".

**76** Evidence A has two significant characteristics. The sources are not named and the Agreed Facts state in paragraph 63 that "...the Bureau has not confirmed the truth of the facts communicated to it by the operators..." Evidence A is in the Agreed Facts because CCS insisted that it be included and CCS asks the Tribunal to give it weight and assume it is true.

**77** Evidence A reflects that operator "F" bioremediates at least 70% of its waste in BC because it considers bioremediation to be better for the environment. Operators "H" and "J" bioremediate about 50% their waste. These operators appear to be bioremediating on their drilling sites to avoid the transportation charges and Tipping Fees associated with Secure Landfills.

**78** Although the Commissioner cannot confirm its truth, the Tribunal is nevertheless prepared to give Evidence A some weight because it can see no reason why industry participants would lie to the Commissioner about their use of onsite bioremediation. However, without knowing the volume of waste produced by "F", "H" and "J", it is impossible to determine whether bioremediation is being undertaken on a significant scale. In any event, it is clear that, even for these waste generators, there is a substantial portion of Hazardous Waste in respect of which bioremediation is not used.

**79** The second category of evidence is found in paragraphs 69-74 of the Agreed Facts. It was gathered in July 2011 by representatives of National Economic Research Associates ("NERA"). Dr. Baye works at NERA and it appears that NERA was retained by the Commissioner to interview industry participants. The Commissioner's staff attended these interviews and the six sources are named (**[CONFIDENTIAL]**). No concern is expressed about the reliability of this evidence. This evidence will be called "Evidence B".

**80** The Commissioner only called witnesses from **[CONFIDENTIAL]** and **[CONFIDENTIAL]** who, as discussed above, indicated that they do not bioremediate as a matter of policy **[CONFIDENTIAL]**.

**81** CCS states the evidence of the other four operators, described in Evidence B, shows that they are active bioremediators and CCS asks the Tribunal to draw an adverse inference from the fact that they were not called by the Commissioner. However, in the Tribunal's view, no such inference should be drawn because the Commissioner had no obligation to adduce the evidence and it was open to CCS to do so.

**82** Evidence B shows that **[CONFIDENTIAL]** bioremediates 10-15% of its waste. **[CONFIDENTIAL]** engages in

some bioremediation at about 70% of its sites and **[CONFIDENTIAL]** bioremediates about 75% of its treatable material onsite. (It also appears to treat the balance of treatable material offsite but this is not explained. Since there are no offsite bioremediation facilities in NEBC, the Tribunal has concluded that this statement must refer to offsite treatment elsewhere.) **[CONFIDENTIAL]** bioremediates onsite and sometimes moves waste between its sites for bioremediation. In the last 3-4 years, it has bioremediated 60-70% of its abandoned well waste.

**83** It is noteworthy that this evidence gives no volumes for treatable and Legacy Hazardous Waste. In these circumstances, and given that the Respondent did not call witnesses from these four operators or other operators, the Tribunal is not persuaded that bioremediation is being undertaken on a significant scale in NEBC.

**Evidence about Storage and Risk Management**

**84** Storage means that Hazardous Waste is left untreated on a drilling site which is still under lease. As long as the MOE does not order a cleanup, this option is available even though drilling has finished, as long as the operator continues to make the lease/tenure payments for the site. Since such payments are low compared to the cost of cleaning up the site, doing nothing may be an attractive option in some cases and the evidence from Trevor Mackay's examination for discovery is that "many" operators have waste stored on their sites. However, Mr. **[CONFIDENTIAL]** testified that **[CONFIDENTIAL]** does not store the Hazardous Waste generated from drilling operations for long periods of time, due to the cost and potential liability issues. He explained that the typical well site storage costs during drilling operations are **[CONFIDENTIAL]** per well.

**85** Risk Management is a process undertaken when drilling is finished and an operator wishes to terminate a lease. The operator must restore the site's surface as nearly as possible to the condition it was in before drilling. Once this has been accomplished, a Certificate of Restoration (also referred to as a Certificate of Compliance) is issued and the operator's lease is terminated. However, the operator remains liable for any issues arising from the Hazardous Waste that is left behind and is obliged to comply with conditions such as monitoring even after the certificate is issued.

**86** On this topic, Mark Polet said the following in his reply report:

> Based on my experience, Operators use risk management as a last resort if treatment or disposal are not practical. I rarely recommend it because even if approval is obtained, which in my experience is very difficult, the Operator retains liability and there is a recognition that the site may need to be revisited if issues arise.

**87** Pete Marshal, an expert in Hazardous Waste management, testified that, although disposal in a Secure Landfill, bioremediation and risk management are each potentially available methods for dealing with Hazardous Waste, he did not know how many operators choose risk management.

**88** This evidence leads the Tribunal to conclude that risk management is seldom used and is not considered to be an acceptable substitute for disposing of Hazardous Waste in a Secure Landfill.

**Conclusions about the Product Market**

**89** Although some operators with Hazardous Waste which is contaminated with light-end hydrocarbons consider bioremediation to be an acceptable substitute for disposal in a Secure Landfill, there is no evidence about the volumes of waste which are successfully bioremediated. More importantly, there is no evidence that the availability of bioremediation has any constraining impact on Tipping Fees in NEBC. In addition, the Tribunal finds that bioremediation is not considered by at least some waste generators to be an acceptable substitute for disposal in a Secure Landfill, particularly in respect of soil that is contaminated with heavy-end hydro-carbons, salts or metals.

**90** With regard to storage and risk management, there was no evidence about the volumes stored in NEBC and no

evidence to suggest that the tenure payments or the cost to obtain a certificate of restoration have any impact on Tipping Fees at Silverberry.

**91** Because bioremediation is not cost effective and is slow for a substantial volume of contaminated soil in NEBC and because it does not work at all on salts and metals, the Tribunal is satisfied that a substantial number of generators do not consider bioremediation to be a good substitute for the disposal of such Hazardous Waste in a Secure Landfill and would not likely switch to bioremediation in response to a SSNIP. Accordingly, the Tribunal is satisfied that the relevant product is "solid hazardous waste generated by oil and gas producers and tipped into secure landfills in NEBC".

**ISSUE 3 WHAT IS THE GEOGRAPHIC DIMENSION OF THE RELEVANT MARKET?**

**92** The Tribunal and the courts have traditionally considered it necessary to define a relevant market before proceeding to assess the competitive effects of mergers under the Act. (See, for example, *Director of Investigation and Research v. Hillsdown Holdings (Canada) Ltd.* *(1992), 41 C.P.R. (3d) 289*, at 297; *Canada (Director of Investigation and Research) v. Southam Inc*, *[1997] 1 S.C.R. 748*, at para. 79). However, they have cautioned against losing sight of the ultimate inquiry, which is whether the merger being assessed prevents or lessens, or is likely to prevent or lessen, competition substantially. (*Southam*, above; "*Propane 1*", above, at para. 48). With this admonition in mind, it is the Tribunal's view that, in this case, the Tribunal may evaluate the competitive effects of the Merger without precisely defining the relevant geographic market.

**93** This conclusion is important because, as will be discussed below, the evidence that has been adduced does not permit the Tribunal to delineate the exact boundaries of the geographic market.

**94** The Tribunal agrees with the approach taken in the MEGs. The process begins with a small area around one of the merging parties' locations (in this case, a Secure Landfill site) and then asks whether all rivals operating at locations in that area, if acting as a hypothetical monopolist, would have the ability and incentive to impose a small but significant price increase (typically 5%) and sustain that increase for a non-transitory period of time (typically one year). If the postulated price increase would likely cause purchasers of the relevant product in that area to switch sufficient quantities of their purchases to suppliers located outside that area to render the price increase unprofitable, then the geographic dimension of the relevant market would be progressively expanded until the point at which a seller of the relevant product, if acting as a hypothetical monopolist, would have the ability and incentive to impose a SSNIP.

**95** In the case at bar, the evidence dealt with three geographic regions:

I. **The Contestable Area** - this was identified by Dr. Kahwaty on behalf of CCS.

II. **All of NEBC** - the Commissioner, supported by her expert Dr. Baye, submitted this definition of the geographic market.

III. **The Babkirk Polygon** - this area was identified in internal CCS documents dealing with the potential impact of the Babkirk Facility on CCS.

**I. The Contestable Area**

**96** In broad terms, the Contestable Area identified by Dr. Kahwaty encompasses an hourglass shaped area of 11,000 square kilometres which lies between the Babkirk Site and Silverberry. In his analysis, the road network in this area is such that there are some areas in which both Silverberry and a potential landfill at the Babkirk Site may be viable disposal options for customers with well sites in those areas. Dr. Kahwaty acknowledges that the transportation costs required to reach Silverberry or the Babkirk Site are such that both may be economic

alternatives for these customers. In Dr. Kahwaty's view, the geographic scope of the relevant market should be limited to this area.

**97** Dr. Kahwaty used Dr. Baye's 10% predicted decline in Tipping Fees as his benchmark for defining the geographic scope of the relevant market. In short, he assessed every well site and calculated whether, if given a 10% reduction off the Tipping Fees paid at Silverberry, the customer would be indifferent as between tipping at Babkirk and Silverberry, having regard for the fact that their total disposal cost (transportation plus Tipping Fee) would be the same for each Secure Landfill. Twelve such customers were identified, accounting for approximately 41,900 tonnes in the Contestable Area. Dr. Kahwaty acknowledged that a larger critical price discount would produce a larger contestable area.

**98** The Tribunal is satisfied that a hypothetical monopolist supplying Secure Landfill services to these twelve customers in respect of the Hazardous Waste generated in the Contestable Area would have the ability and incentive to impose and sustain a SSNIP above levels that would likely exist in the absence of the Merger.

**99** Indeed, the Tribunal considers that the Contestable Area is likely understated and, in fact, smaller than the minimum area in which a hypothetical monopolist would have the ability and incentive to impose and sustain a SSNIP. The Tribunal has reached this view for several reasons. First, the Tribunal accepts Dr. Baye's position that "Babkirk need not have a location advantage for a customer - and the customer need not switch from Silverberry to Babkirk - for that customer to significantly benefit from the lower Tipping Fees stemming from competition". Second, the evidence suggests that new wells are likely to be drilled in the area between Babkirk and Northern Rockies, and that there is Legacy Waste sitting on abandoned well-sites in that region. Meaningful price and non-price competition between Babkirk and Northern Rockies for at least some of that waste likely would have developed in the absence of the Merger. Third, the geographic extent of the Contestable Area is necessarily limited by Dr. Kahwaty's assumption of a base price that is only 10% below prevailing levels. If that figure is too low Dr. Kahwaty admitted that the geographic market would be larger than the Contestable Area.

**100** In addition, the Tribunal notes that the volume of Hazardous Waste generated in the Contestable Area likely is greater than reported by Dr. Kahwaty because he only used data for 2010. Moreover, Dr. Kahwaty excluded CCS' national customers from his analysis and this may also have resulted in an understated geographic market.

**101** With respect to the possibility that Secure Landfills in Alberta might be economically accessible for generators of waste in the Contested Area, Dr. Kahwaty stated that "transportation costs are too great for [customers located to the south and east of Silverberry, who currently tip their waste in Alberta] to opt to dispose at a potential landfill at the Babkirk site (even with a significant discount) as compared to disposing at Silverberry at current prices." The Tribunal extrapolates from this and concludes that customers generating Hazardous Waste in the Contestable Area are unlikely to transport their waste to secure landfill sites in Alberta due to the significant transportation costs and potential liability that would be associated with hauling waste over such a long distance.

**102** For all these reasons, the Tribunal concludes that the geographic market is at least as large as the Contestable Area. We now turn to whether it could be as large as all of NEBC.

**II. All of NEBC**

**103** NEBC covers approximately 118,800 square kilometres and is vast in comparison to Dr. Kahwaty's Contestable Area. NEBC and the much smaller Contestable Area are compared on the map attached hereto as Schedule "C", which is taken from Tab 29 of Dr. Kahwaty's report of October 21, 2011.

**104** Dr. Baye concludes that the relevant geographic market is NEBC on the basis that this is the region where targeted customers are located, including current customers at both Silverberry and Northern Rockies Secure Landfills.

**105** In reaching this conclusion, Dr. Baye relies on an economic theory of market equilibrium which predicts that

CCS would have an incentive to compete with an independently operated Babkirk Facility for customers located outside of Dr. Kahwaty's Contested Area. This theory is based on his understanding that CCS' average 2010 Tipping Fees at Silverberry were approximately **[CONFIDENTIAL]** per tonne and its average landfill costs were approximately **[CONFIDENTIAL]** per tonne, yielding a margin in excess of 60%. Using these figures, Dr. Baye assumes that CCS would be prepared to reduce its Tipping Fees by 25% or greater in some areas to retain business in the face of competition from an independent Babkirk Facility.

**106** However, among other problems, Dr. Baye's theory fails to take into account the opportunity cost to CCS that would be associated with substantially reducing its Tipping Fees to sell landfill capacity today, which could be sold in the future at higher Tipping Fees to customers located closer to Silverberry. In the absence of any analysis of how this opportunity cost would factor into CCS' current decision-making process, the Tribunal finds that the economic theory relied on by Dr. Baye is not particularly helpful in defining the geographic scope of the relevant market.

**107** In his initial report, Dr. Baye also provides estimates based on econometric regression models which he asserts are consistent with this theory and his definition of the geographic market as extending throughout all of NEBC. The first set of models, found at Exhibits 19 and 20 of Dr. Baye's initial report, test his hypothesis that the distance between a Secure Landfill and its closest competitor is a significant predictor of the average Tipping Fees at that landfill.

**108** Exhibit 20 predicts that the opening of an independent landfill at the Babkirk Site will result in a large decline in average Tipping Fees at Northern Rockies, because it would reduce the distance to Northern Rockies' nearest competitor to three hours and 49 minutes. However, this ignores (i) the substantial transportation costs that the vast majority of customers who tip at Northern Rockies would have to incur to transport their waste to Babkirk, (ii) the very small number of well-sites located between those two facilities, and (iii) the apparent absence of any incentive for CCS to alter its Tipping Fees at Northern Rockies in response to entry at Babkirk.

**109** The second set of regression models are estimates offered by Dr. Baye which relate to a "natural experiment" involving SES' entry at Willesden Green, Alberta, in December 2008. That facility became the closest competitor to CCS' Rocky Mountain House landfill ("Rocky"), located approximately one hour away. In his analysis of CCS' 2010 transactions data, Dr. Baye discovered that CCS substantially reduced the Tipping Fees it charged to several customers subsequent to the opening of SES' facility at Willesden Green.

**110** To address the possibility that these substantial price reductions were purely coincidental, Dr. Baye developed "difference in difference" ("DiD") regression models, reported at Exhibit 26 of his initial report. The DiD approach controls for unobserved events, other than SES' entry at Willesden Green, which might have led to the observed decline in Tipping Fees at Rocky. In short, the DiD models include a "treatment" setting in which the event (in this case, entry) occurred and a "control" setting in which the event did not occur. Dr. Baye took the change in Tipping Fees that occurred in the treatment setting and subtracted any change that occurred in the control setting. He interpreted the difference in the change (or the "difference in difference") as the effect of entry at Willesden Green on Tipping Fees at Rocky.

**111** It is significant that, in selecting a control landfill, Dr. Baye considered it important to pick a site that "is unlikely to be affected by the treatment event - in this case entry at Willesden Green." One of the principal criteria that he employed in making that selection was that the control landfill had to be "at least 300 km away" from Willesden Green. The same logic would imply that entry at Babkirk would not likely affect Tipping Fees at Northern Rockies, which is situated 260 km away from the Babkirk Site. A key assumption underlying Dr. Baye's DiD models is therefore inconsistent with his definition of the geographic market as all of NEBC. This, together with the fact that Northern Rockies is almost four times further away from Babkirk than SES' Willesden Green facility is away from CCS' Rocky facility, lead the Tribunal to conclude that Dr. Baye's DiD analysis is not particularly helpful in defining the geographic scope of the relevant market. That said, as discussed in detail below, the transactions data which reveals substantial price reductions by CCS to seven of its customers following SES' entry at Willesden Green is relevant to the Tribunal's assessment of the likely competitive effects of the Merger.

**112** Finally, the Tribunal notes that Dr. Baye also points to internal documents of CCS which he says are consistent with his definition of the relevant geographic market. However, those documents simply: (i) make projections of the overall annual operating margin (**[CONFIDENTIAL]**) that CCS stood to lose at Silverberry and Northern Rockies were an independent landfill to open at the Babkirk Site; (ii) predict a pricing war if the Babkirk Facility was operated independently or acquired by a third party; (iii) discuss the likelihood of having to compete through "value propositions"; and (iv) reflect that CCS likely takes into account its customers' transportation costs to the next closest competing landfill in setting its Tipping Fees. While these types of statements assist in assessing whether the Merger is likely to prevent competition substantially, they are not particularly helpful to the Tribunal in defining the geographic scope of the relevant market.

**III. The Babkirk Polygon**

**113** The Babkirk Polygon is the third area that was discussed at the hearing. That area was identified by a member of CCS' business development team who was asked to project Babkirk's market capture area. The Tribunal has added a rough depiction of that area on Schedule "C" hereto.

**114** The Babkirk Polygon was apparently intended to identify the locations of existing Silverberry customers who would be likely to tip at Babkirk rather than at Silverberry, if Babkirk was operated as a Secure Landfill. In other words, the Babkirk Polygon was CCS' representation of the geographic locations of business it risked losing if Babkirk opened as a Secure Landfill. It includes territory north and west of Babkirk and is a larger area than Dr. Kahwaty's Contestable Area.

**115** The Tribunal is satisfied that the locational advantage that the Babkirk Facility would enjoy for customers with drilling operations situated to its north and west is such that those customers would not likely tip at Silverberry in the absence of a very substantial reduction in its Tipping Fees. Given the opportunity cost that CCS would incur by offering such a substantial reduction in its Tipping Fees, and given the absence of any analysis by the Commissioner or Dr. Baye of the impact of that opportunity cost on CCS's decision-making, the Tribunal is not persuaded that CCS would have an incentive to compete for those customers in the absence of the Merger.

**116** Likewise, the Tribunal has not been persuaded on a balance of probabilities that such customers who operate to the north and west of the Babkirk Facility would tip at Silverberry, in response to a SSNIP above the maximum average tipping fee level that it believes is likely to exist in the absence of the Merger. For the reasons discussed below, the Tribunal has concluded that such price level will be at least 10% below existing levels. However, transportation costs and the liability associated with transporting Hazardous Waste over the long distance to Silverberry are such that it would require more than a SSNIP to induce waste generators located in those regions to tip their Hazardous Waste at Silverberry.

**117** The Tribunal has concluded that the geographic scope of the relevant market is at least as large as the Contestable Area identified by Dr. Kahwaty, and likely falls between the limits of that area and the bounds of the Babkirk Polygon, which includes some of the Contestable Area, but adds significant territory north and west of Babkirk.

**118** The Tribunal is satisfied that it would not matter if the geographic scope of the relevant market actually includes additional customer locations in the Babkirk Polygon, beyond the Contestable Area, because CCS would remain the sole supplier of Secure Landfill services to any reasonably defined broader group of customers.

**ISSUE 4 IS THE MERGER PRO-COMPETITIVE?**

**119** CCS has suggested that the Merger is pro-competitive because it brings to the market a new Secure Landfill at the Babkirk Site. CCS further asserts that the Merger will most quickly transform the Babkirk Site into a Secure Landfill to complement CCS' existing business and serve the growing oil and gas industry in NEBC. CCS says that these facts explain its customers' failure to complain about the Merger.

**120** The Tribunal disagrees. In its view, a merger which prevents all actual or likely rivalry in a relevant market cannot be "pro-competitive," even if it expands market demand more quickly than might otherwise be the case. Such a merger might be efficiency-enhancing, as contemplated by the efficiency defence in section 96 of the Act. However, it has adverse consequences for the dynamic process of competition and the benefits that such process typically yields. In the absence of actual rivalry, or a very real and credible threat of future rivalry, meaningful competition does not exist.

**ISSUE 5 WHAT IS THE ANALYTICAL FRAMEWORK IN A "PREVENT CASE?**

**121** The "prevention" branch of section 92 was raised in three previous Tribunal cases: *Canada (Director of Investigation and Research) v. Southam Inc.* *(1992), 43 C.P.R. (3d) 161* (Comp. Trib.), rev'd on other grounds *(1995), 63 C.P.R. (3d) 1* (F.C.A.), rev'd, *[1997] 1 S.C.R. 748*, *Propane 1* and *Canadian Waste Services*. However, since those cases were primarily concerned with allegations involving a substantial lessening of competition, the Tribunal did not address in any detail the analytical framework applicable to the assessment of an alleged substantial prevention of competition.

**122** In determining whether competition is likely to be prevented, the Tribunal will assess whether a merger is more likely than not to maintain the ability of the merged entity to exercise greater market power than in the absence of the merger, acting alone or interdependently with one or more rivals. For the purposes of this case, this requires comparing a world in which CCS owns the relevant Secure Landfills in NEBC (i.e. Northern Rockies, Silverberry and Babkirk) with a world in which Babkirk is independently operated as a Secure Landfill.

**123** In assessing cases under the "prevent" branch of section 92, the Tribunal focuses on the new entry, or the increased competition from within the relevant market, that the Commissioner alleges was, or would be, prevented by the merger in question. In the case of a proposed merger, the Tribunal assesses whether it is likely that new entry or expansion would be sufficiently timely, and occur on a sufficient scale, to result in: (i) a material reduction of prices, or in a material increase in non-price competition, relative to prevailing price and non-price levels of competition, (ii) in a significant (i.e., non-trivial) part of the relevant market, and (iii) for a period of approximately two years. If so and if the entry or expansion likely would occur within a reasonable period of time, the Tribunal will conclude that the prevention of competition is likely to be substantial.

**124** The Tribunal also considers whether other firms would be likely to enter or expand on a scale similar to that which was prevented or forestalled by the merger, and in a similar timeframe. Where the Tribunal finds that such entry or expansion would probably occur, it is unlikely to conclude that the merger is likely to prevent competition substantially.

**125** As noted earlier and as recognized by all parties, the price against which the prevailing prices will be compared will be the price that would likely have existed in the absence of the merger. The burden will be on the Commissioner to demonstrate that price level, or the range of prices, that likely would have existed "but for" the merger.

**126** In final argument, the Commissioner and CCS suggested that helpful guidance on the approach that should be taken to prevention of competition cases can be provided by the U.S. jurisprudence pertaining to mergers that have been alleged to reduce potential competition. In the Tribunal's view, that jurisprudence is not particularly helpful to merger assessment under the Act, because it was developed in respect of a different statutory test and, for the most part, many years ago. (It appears that the US Supreme Court and the federal appellate courts have not had an opportunity to revisit that jurisprudence since the 1980s. See M. Sean Royall and Adam J. Di Vincenzo, "Evaluating Mergers between Potential Competitors under the New Horizontal Merger Guidelines", *Antitrust* (Fall 2010) 33, at 35.)

**ISSUE 6 IS THERE A SUBSTANTIAL PREVENTION OF COMPETITION?**

**A. The "But For" analysis**

*Introduction*

**127** In *Commissioner of Competition v. Canada Pipe Company Ltd.*, *2006 FCA 233*, the Federal Court of Appeal decided that a "but for" analysis was the appropriate approach to take when considering whether, under paragraph 79(1)(c) of the Act, "...the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially." The specific question to be asked is stated, as follows, at paragraph 38 of the decision "...would the relevant markets - in the past, present or future - be substantially more competitive but for the impugned practice of anti-competitive acts?"

**128** Language similar to that found in section 79 appears in section 92 of the Act. Section 92 says that an order may be made where "...the Tribunal finds that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen competition substantially." For this reason, the parties and the Tribunal have determined that the "but for" approach is also appropriate for use in cases under section 92 of the Act. The parties recognize that the findings will be forward looking in nature and CCS has cautioned the Tribunal against unfounded speculation. With this background, we turn to the "but for" analysis.

**129** The discussion below will address the threshold issue of whether effective competition in the supply of Secure Landfill services in the Contestable Area identified by Dr. Kahwaty likely would have materialized in the absence of the Merger. Stated alternatively, would effective competition in the relevant market likely have emerged "but for" the Merger? After addressing this issue, the Tribunal will turn to the section 93 factors that are relevant in this case, as well as the issue of countervailing power.

**130** In undertaking the "but for" analysis, the Tribunal will consider the following questions:

(i) If the Merger had not occurred, what new competition, if any, would likely have emerged in the Contestable Area?

(ii) If the Merger had not occurred, what would have been the likely scale of that new competition?

(iii) If the Merger had not occurred, when would the new competition likely have entered the market?

**131** The Commissioner suggested that either June or July, 2010 be used as the timeframe for considering the "but for" world. CCS, on the other hand, was more precise and suggested that the relevant time for this purpose should be the end of July 2010, when CCS and Complete signed the letter of intent which led to the Merger. Since the parties have essentially agreed, the Tribunal will focus on the end of July.

**132** The Tribunal's view is that, as of the end of July 2010, there were only two realistic scenarios for the Babkirk Site absent the Merger. They were:

1. The Vendors would have sold to a waste company called Secure Energy Services Inc. ("SES"), which would have operated a Secure Landfill; or
2. The Vendors would have operated a bioremediation facility together with a half cell of Secure Landfill.

**133** Extensive evidence was adduced on these topics. The discussion below summarizes the most important aspects of that evidence.

**Scenario #1 - A sale of Complete to SES**

**134** In February of 2007 when the Vendors first met to organize Complete, they decided that their exit strategy would be to sell the company to Newalta Corporation or to CCS. Newalta is a waste company which operates Secure Landfills in Alberta. However, it was always the Vendors' intention to sell only when they could achieve an acceptable return on their investment.

**135** In November 2007, Canaccord Capital sent a four-person investment team to Fort St. John to investigate the purchase of a number of the Vendors' companies, including Complete. At that time, the Vendors' intentions about a sale of Complete were recorded in the company's minutes, which, among other things, stated:

> ...consensus at Complete's meeting was to carry on the way we are going unless we are presented with a very attractive proposal from outside. We don't want to do all the work for the benefit of others - better to take a longer time, but to have higher rewards for ourselves...

**136** Subsequently, a Vision Statement, dated June 22, 2008, was prepared by Karen Baker. That document stated that they wanted to make a "good return on sale of company". The Statement also observed:

> The VISION of Complete Environmental Inc. is to become a diversified, highly efficient, environmental corporation in NEBC generating a high profit margin thus, presenting itself as an attractive acquisition to multiple potential purchasers.

**137** After Complete received its MOE Permit on February 26, 2010, Ken Watson's company, IRTL, offered to purchase Complete for **[CONFIDENTIAL]**. Before that offer was made, the Vendors had not been actively considering a sale. However, IRTL's offer spurred them to seriously consider the matter and, before they responded to IRTL's, they authorized Randy Wolsey to contact CCS and SES for expressions of interest.

**138** On March 23, 2010, Randy Wolsey spoke to SES but was told that it had no interest in making an offer because it was busy with its initial public share offering. However, SES did indicate a possible future interest and stated that it valued BLS at approximately **[CONFIDENTIAL]** in either mixed cash and shares or **[CONFIDENTIAL]** plus a share offering. In contrast, CCS expressed immediate interest and Dan Wallace of CCS verbally offered **[CONFIDENTIAL]** for BLS.

**139** The Vendors eventually decided to sell Complete to IRTL. However, IRTL's offer was withdrawn in early June 2010 after Ken Watson learned that, contrary to his expectations, Canaccord Capital would not finance IRTL's acquisition of Complete. After Cannacord declined, he did not have time to arrange alternative financing.

**140** According to Karen Baker, after IRTL's offer was withdrawn, the Vendors decided to try to sell Complete one last time. They concluded that, if they did not receive an interesting offer, they would operate the Babkirk Facility themselves. This would involve moving forward with an operating plan and constructing a half cell of Secure Landfill. To ascertain if a sale was possible, Randy Wolsey was again asked to contact CCS and SES. In addition, he was asked to contact Newalta. He did so, but Newalta did not respond to his email.

**141** At about that time, Dan Wallace of CCS apparently heard that IRTL's offer had fallen through and sent Randy Wolsey an email asking if CCS could renew its earlier offer. Mr. Wolsey responded by offering to sell BLS for **[CONFIDENTIAL]**. On June 22, 2010, CCS agreed to purchase the shares of BLS for that amount.

**142** Inexplicably, Randy Wolsey did not tell the other Vendors about his deal with CCS. Instead, he arranged a meeting with SES (the "Meeting"). It was held on June 29, 2010 and was attended by Rene Amirault, President and

CEO of SES, Dan Steinke, SES' Vice-President of Business Development, and Corey Higham, SES' Business Development Representative (the "SES Group").

**143** According to the Vendors, the SES Group spent much of the Meeting giving a presentation to show that SES was an attractive investment. An SES brochure prepared for potential investors was used for this purpose. However, the Vendors were not interested in acquiring shares of SES and they testified that no price for BLS or Complete was ever suggested and no offer was discussed.

**144** According to Mr. Amirault, he indicated during the Meeting that an all cash offer could be made. The Vendors denied this. Since this evidence is significant and was not included in Mr. Amirault's witness statement, the Tribunal has concluded an all cash offer was not mentioned and that the Vendors understood that SES would only purchase Complete if it could use its shares to finance part of the purchase price.

**145** During the Meeting, the SES Group had questions about how to secure the necessary regulatory approvals to allow SES to expand the permitted capacity of the Babkirk Facility and to upgrade the design of the Secure Landfill cells (the "Questions"). The Vendors could not answer the Questions and Mr. Amirault testified that he asked for and was refused permission to speak to Del Reinheimer about the Questions. However, some Vendors could not remember anyone from the SES Group asking for permission to speak to Del Reinheimer about the Questions and other Vendors denied that anyone asked for such permission at that time. Mr. Reinheimer was the Section Head, Environmental Management in the Environmental Protection Division of the MOE.

**146** Mr. Amirault stated that following the Meeting, SES was actively interested in purchasing Complete and gave the following reasons to explain its failure to make an offer or submit a letter of intent in July 2010:

* The Questions had to be answered before a price could be established.
* There was no particular urgency about making an offer because there were no other buyers. Mr. Amirault testified that the Vendors had indicated at the Meeting that Complete had promised a First Nation that it would not sell to CCS and the SES Group knew that Newalta was not interested.

**147** Mr. Amirault acknowledged that the Questions were about process i.e. "how to" go about getting approvals for increased permitted capacity and enhanced cell design. He also stated that he had no doubt that the approvals would be forthcoming. In these circumstances and because, as described below, SES was actively engaged in the development of another Secure Landfill, it is the Tribunal's view that SES would have known what it needed to spend to increase the permitted capacity and upgrade the landfill cells at the Babkirk Site. Accordingly, the Tribunal does not accept Mr. Amirault's evidence that SES could not establish a purchase price without the answers to the Questions.

**148** There is a dispute about whether, on July 6, 2010, Corey Higham sent Ron Baker an email setting out the Questions which had been discussed at the Meeting. Mr. Amirault stated in hearsay evidence in his witness statement that Corey Higham had told him that the email had been sent. A photocopy of that alleged email was appended to Mr. Amirault's witness statement. However, after Ron Baker made a witness statement stating that he did not recall having received the email, no reply evidence was filed by Corey Higham to say that it had, in fact, been sent. The email is an important document to the extent that it evidences an ongoing interest by SES in receiving answers to the Questions. However, given that it was not properly adduced, the Tribunal gives it no weight.

**149** As mentioned above, Mr. Amirault testified that Ron Baker told the SES Group during the Meeting that he had promised a First Nation that the Vendors would not sell the Babkirk Facility to CCS. This meant that SES understood that the Vendors were not likely to receive a competing offer. However, this apparently significant detail did not appear in Mr. Amirault's witness statement and was not referred to in his examination-in-chief. It was mentioned for the first time in answer to a question posed by the Tribunal. For this reason, this evidence is not accepted as an explanation for SES' failure to show a more active interest in purchasing Complete.

**150** Mr. Amirault acknowledged that the window for undertaking construction in 2010 "...was closing, closing fast" and that SES wanted to begin construction at Babkirk at the end of August or by mid-September at the latest. This meant that, if SES had been actively interested in acquiring Complete, it would have moved quickly to present the Vendors with a letter of intent. Mr. Amirault also testified that, apart from updating its earlier market study of the Babkirk Facility, no further due diligence was required. In addition, he testified that he did not need the approval of his Board of Directors to deliver a letter of intent. In these circumstances, the Tribunal has concluded that SES' failure to follow up more quickly on its meeting with the Vendors and its failure to demonstrate any interest in making an offer at that time are attributable to a lack of active interest in acquiring BLS in July 2010.

**151** Ron Baker recalls that he was called by Corey Higham on July 28, 2010. However, Mr. Baker does not remember what Mr. Higham said during that telephone call. Since Corey Higham did not give evidence, the Tribunal considers it fair to assume that he did not make an offer to purchase Complete or propose a letter of intent. Although Mr. Baker does not recall much of his own side of the conversation, he does remember telling Mr. Higham that Complete had just signed a letter of intent with CCS.

**152** The Tribunal considers it noteworthy that, since 2007, SES had been developing a new Secure Landfill called Heritage. It was located approximately 153 km south of the Babkirk Site. However, it was not favourably received during public consultations because it was to be located near a populated area and on a site where a landslide had occurred. Corey Higham of SES was told on July 26, 2010 that the EA's review of the Heritage Project had been "suspended" pending further evidence from SES about the suitability of the site. SES eventually abandoned the project in December of 2010.

**153** Based on this evidence, the Tribunal has concluded that SES had an ongoing general interest in the Babkirk Facility. It had spoken to Murray Babkirk when he owned BLS and it had indicated possible future interest when Randy Wolsey contacted it in March of 2010. SES also sent its most senior executive to the Meeting in June 2010. However, the Tribunal has also concluded that SES was not actively interested in a purchase in July 2010. It never discussed a potential price, and, although it asked the Questions, the answers were not crucial to setting the price and SES already knew that it would be granted the additional approvals it sought. Finally, although Mr. Amirault testified that there was no due diligence of any consequence to be undertaken, SES did not send a letter of intent and there are no internal SES documents showing that it was preparing to make an offer. The Tribunal has concluded that SES' failure to take a more active interest in purchasing Babkirk is explained by the fact that it was still giving priority to its project at the Heritage site. This is understandable, since it had already invested three years and approximately $1.3 million in developing the project.

**154** In all these circumstances, the Tribunal has concluded, on a balance of probabilities, that SES likely would not have made an acceptable offer for Complete by the end of July 2010 or at any time in the summer of 2010 and that the Vendors would have moved forward with their own plans to develop the Babkirk Facility.

**Scenario #2 - The Vendors Operate Babkirk**

**155** The Vendors' position is that Complete was created to purchase BLS and to operate a bioremediation facility on the Babkirk Site. They assert that their plan was to accept only Hazardous Waste contaminated with light-end hydrocarbons which could be treated using bioremediation.

**156** However, the Vendors recognized that bioremediation might sometimes fail and that they might be left with clumps of contaminated soil ("Hot Spots") after the surrounding waste had been successfully treated. The Vendors understood that the contaminated soil would have to be placed in a Secure Landfill before the remaining soil could be tested and de-listed as non-hazardous waste.

**157** To enable BLS to permanently dispose of the contaminated soil from the Hot Spots and to attract customers to the Babkirk Facility, the Vendors proposed to construct a Secure Landfill on the Babkirk Site, which they described as "incidental" to their treatment operation. This meant that only soil that was not successfully treated using

bioremediation would be moved into the Secure Landfill. The Tribunal will give this meaning to the term "Incidental" in the context of the Vendors' Secure Landfill in the balance of this decision.

**158** The Commissioner denies that the Vendors' Secure Landfill was only to be used on an Incidental basis. She maintains that the Vendors always intended to accept and directly and permanently dispose of all types of Hazardous Waste in their Secure Landfill. We will refer to this business model as a "Full Service" Secure Landfill. To support her position, the Commissioner relies, in part, on the documents used to obtain the EA Certificate and the MOE Permit. These documents will be described collectively as the Regulatory Approval Documents ("RADs"). As discussed below, the RADs clearly indicate that a Secure Landfill was to be opened on the Babkirk Site. The Commissioner also relies on the Draft Operations Plans (the "Operations Plan") for the Babkirk Site, which show that a Full Service Secure Landfill was planned.

**159** Finally, the Commissioner relies on statements in a variety of documents which she asserts reflect that the Vendors intended to compete with CCS. She submits that references in those documents to competing with CCS meant operating the Babkirk Facility as a Full Service Secure Landfill.

**The Vendors' Documents**

**160** The Vendors explained that they needed an EA Certificate and an MOE Permit for a Secure Landfill in order to accept Hazardous Waste of any kind for any type of treatment at the Babkirk Facility. However, they also stated that neither document required them to operate on a Full Service basis. In other words, although they were entitled to do so, they were not required to accept all types of Hazardous Waste for direct disposal. Instead, they were free to operate an "Incidental" Secure Landfill.

**161** The Vendors ask the Tribunal to focus on the documents which were prepared when Complete was being incorporated and when the MOE Permit was finally granted, as the best evidence of their intention, which they say was to use the Secure Landfill on the Babkirk Site only as Incidental to their bioremediation. The five documents in this category will be described as the "Vendors' Documents". We will deal with them in turn below.

**162 Minutes of a meeting that Randy Wolsey and Ken Watson attended with Del Reinheimer and other MOE and EAO officials on January 24, 2007.** The minutes state:

> Ken [Watson] discussed the remediation side of the facility's operations, which will continue even after (if) the landfill is constructed. He stated that he has had interest expressed from companies who wish to pursue remediation as well as landfilling. Ken outlined some of the practices and equipment currently used in other operations with which he is involved, and showed some pictures and videos of the equipment (e.g. ALLU AS 38 composting machine) in action.
>
> Ken and Randy stated that their intention would be to have an ALLU AS 38 kept at the facility full-time. They cited that it would be capable of processing up to about 25,000m per day of Peace River region clay.

[our emphasis]

**163** In his testimony, Mr. Reinheimer agreed that his understanding was that the Vendors were going to operate a bioremediation facility and that it was an open question whether or not the Secure Landfill, for which application had been made, would ever be built. In the Tribunal's view, this evidence supports the Incidental nature of the Secure Landfill.

**164 Minutes of a Newco meeting dated in February 2007**. These minutes record the Vendors' vision for their new business, which was to become Complete. The minutes make no mention of a Secure Landfill at the Babkirk Site. They speak only of processing waste. The document also describes CNRL and Petro-Canada as customers

for treatment and indicates that Petro-Canada has been interested for years. In context, it is clear that Petro-Canada's interest was in bioremediation. The fact that a Secure Landfill is not mentioned even though the application for its approval was already underway, strongly suggests that it was to play an Incidental role in Complete's business at the Babkirk Site.

**165** The minutes read as follows:

> **Newco name** should be "**Environmental Services Co**." not "Waste Management (Facility) Co." **Services** to be offered by Newco were suggested to include drilling for sites in the 115 area, remediation on clients' sites, excavation at client sites, and processing at 115 landfill. We could also coordinate the trucking to haul clients' contaminated dirt that we would excavate at client sites to Mile 115 for processing, although we would not own such trucks.
>
> The **Target Market** would be environmental engineering companies and end-user oil and gas companies such as PetroCanada and CNRL. It would be good if we could get a letter from PetroCan/Matrix regarding the potential amount of work. Our services are needed - PetroCan has been interested for years now. This should be a "Market Pull" rather than "Product Push" situation.
>
> There would considerable **landfill preparation** at Mile 115 [the Babkirk Site]. Randy suggested Tom would probably like to be involved here with heavy equipment operation. We expect to have the permit by Nov 1/07. It would probably take 1 year for money to come in from sales for the landfill itself since we have to build the cells.
>
> [the emphasis is in the original]

**166** The Tribunal has studied the final passage quoted above and has concluded that, although the term "landfill" is used, the topic under discussion was actually bioremediation and the Vendors' plan to sell the successfully treated soil.

**167 A diagram outlining Newco's operation**. This document shows how Complete's treatment facility on the Babkirk Site would complement other businesses operated by the Vendors. The diagram does not refer to the existence of a Secure Landfill. This omission also suggests that a Secure Landfill was not a significant part of Complete's business or of the Vendors' plan to integrate a number of their businesses.

**168 Minutes of January 20, 2010**. This document describes a meeting that Ken Watson and Ron Baker attended with Del Reinheimer and other officials from the MOE to discuss the Vendors' plans for the Babkirk Site. By this time, Complete owned Babkirk and had received the EA Certificate. The issuance of the MOE Permit for the Secure Landfill was the next step. The relevant portions of the minutes read as follows:

> Ken [Watson] and Ron [Baker] both stressed that although they would rather not use Babkirk as a Landfill but as a treatment facility, industry demands that Babkirk is Permitted as a Secure Landfill prior to transporting materials to or using Babkirk in any way. The term "Secure" appears to be of utmost importance to all major oil and gas companies.
>
> * Although Del [Reinheimer of the MOE] didn't understand why industry perceives as such, he realized the concern.
> * He stated that even though the Permit may be approved, operation of a Secure Landfill may not begin until the Operating Plan is also approved and the landfill has been constructed.
> * Ken and Ron agreed it is rather the perception of the word "Secure" that is required at this time to entice clients, than the use of an actual operating landfill.
> * Ken suggested that prior to approved Secure Landfill operations, unacceptable material could be sent to CCS (small amount around contamination source) and the remainder could be accepted at Babkirk.

> All agreed construction of the landfill is to commence within 2 years of Permit issuance; and that the Landfill Operating Plan must be completed prior to construction but the issuance of the Permit itself is not affected by the existence or not of the Operating Plan.
>
> Ron [Baker] suggested that the Permit read that the construction phase of the landfill be completed in small segments of a 1/2 cell over a period of time rather than the construction of a full 1/2 cell at one time (as suggested by Reg).
>
> [our emphasis]

**169** In the Tribunal's view, there are several reasons why this document indicates that the Secure Landfill at the Babkirk Site was to be Incidental. First, Ron Baker was suggesting that even a half cell was not needed and proposed that smaller segments be constructed. This approach makes sense only if the Secure Landfill was to be Incidental. No one intending to compete with CCS' Full Service Secure Landfill at Silverberry would contemplate the construction of a small segment of a half cell.

**170** Second, the Incidental nature of the Secure Landfill is disclosed when Ken Watson suggested that, before the Secure Landfill was operational at Babkirk, unacceptable material could be moved to CCS. The interesting point is that the unacceptable material is not material delivered by waste generators for direct disposal into the Secure Landfill at the Babkirk Site. Rather, it is only the "small amount around [the] contamination source" or, in other words, the material around Hot Spots. Once again, this confirms that the Vendors' intention was that their Secure Landfill would only be used on an Incidental basis.

**171 Minutes dated March 20, 2010**. These minutes reflect the Vendors' thinking in response to the offer to purchase that they received from IRTL. The minutes indicate that, at that time, they believed they had the following three options:

1. Operate start first secure cell and bioremediate [inc salt];
2. Bioremediate without cell;
3. Sell ???

The Minutes also stated:

> "Need 12 month season to see how well bioremediation works."

**172** The Vendors ask the Tribunal to note that this evidence all predates CCS' purchase of Complete and the Commissioner's interest in the Merger. The Vendors also submit that their evidence at the hearing was consistent with their intention to operate only an Incidental Secure Landfill. Both the proposed manager of the Babkirk Facility (Randy Wolsey) and the man who would be in charge of daily operations (Ken Watson) testified that the only waste they intended to accept at Babkirk was waste which could be bioremediated.

**The RADs**

**173** There are numerous RADs, however, those which are particularly relevant are: the "Terms of Reference" dated August 29, 2007; the "Application for an Environmental Assessment Certificate" dated February 11, 2008; the "Babkirk Secure Landfill Project Assessment Report" dated November 12, 2008; and a "BC Information Bulletin" dated December 9, 2008.

**174** The first significant RAD is the Terms of Reference for the Babkirk Secure Landfill Project. It was approved by the EAO on August 29, 2007.

**175** Section 3.1 reads as follows:

> The Proponent [Murray Babkirk] has experienced a considerable decline in the amount of waste brought to the existing facility for storage and treatment since the approval of the Silverberry Secure Landfill Facility application (north of Fort St. John, B.C.) as understandably, direct disposal forms a more cost effective option for clients than treatment and disposal. The conversion of the existing facility from a purely Short-term Storage and Treatment Facility to a Secure Landfill and Short-term Storage and Treatment Facility will allow fair competition between the Proponent and Silverberry facilities in providing responsible waste management solutions for local industry.
>
> [...]
>
> This section will provide:
>
> [...]
>
> - a list of the materials to be accepted at the Project for disposal;
>
> - a general description of the criteria that will be used to determine whether contaminated soil will be disposed of directly into the secure landfill or treated by bioremediation;
>
> [...]
>
> [our emphasis]

**176** This document suggests that the proposed facility on the Babkirk Site would accept Hazardous Waste for direct disposal into the Secure Landfill and that the Secure Landfill was being developed so that the Babkirk Site could compete with CCS at Silverberry. This document was first drafted by SNCL on the instructions of Murray Babkirk, who was effectively the proponent, since, with his wife, he owned BLS. However, as discussed below, some of the Vendors later reviewed it and they did not suggest changes to reflect their intention to operate only an Incidental Secure Landfill. Since the further RADs contain similar language, it is not necessary to describe them in detail. The Tribunal is satisfied that they all indicate that there would be a Full Service Secure Landfill on the Babkirk Site.

**177** It is clear that some of the Vendors were, in Karen Baker's words, "integrally involved" during the regulatory process leading to the EA Certificate. Some attended and assisted with information sessions, consultation meetings, and presentations to First Nations; some were included in correspondence regarding the EA Certificate; some participated directly in drafting or reviewing some of the RADs; and some assisted the Babkirks with technical matters. The Vendors also advanced funds which the Babkirks were able to use to finance the environmental assessment process and pay the fees charged by SNCL. This financial support totalled approximately $300,000 and was deducted from the purchase price that Complete eventually paid the Babkirks for the BLS shares. In all these circumstances, the Commissioner submits that the RADs reflect the Vendors' true intentions.

**178** However, the Vendors state that while the RADs authorized the construction of a Full Service Secure Landfill, they say nothing about the Vendors' intentions. Mr. Baker explained that, as far as the Vendors were concerned, as long as they had an approval for a Secure Landfill, no one would complain if they chose to operate it on an Incidental basis. He also stated that, if they had asked to amend the Terms of Reference, which is clearly the document on which the later RADs were based, it would have slowed down the approval process for changes that, in the Vendors' opinion, were unnecessary.

**179** The Tribunal has concluded that this explanation is reasonable and that it underpins Mr. Baker's response when he was asked why the Vendors didn't correct the Terms of Reference to reflect their intention to operate an Incidental Secure Landfill. He testified:

> [...] There was nothing in it that was that onerous to us or important to us to warrant changing.

**180** In view of this explanation and in view of the Vendors' Documents which, starting in January 2007, consistently show that their plan was to operate an Incidental Secure Landfill, the Tribunal concludes that, although the RADs accurately described what could be offered at the Babkirk Facility, they did not accurately reflect the Vendors' intentions.

**The Operations Plan**

**181** The Vendors never completed an Operations Plan for the Secure Landfill on the Babkirk Site.

**182** The first Operations Plan was prepared by SNCL. An early and incomplete draft of that document is dated January 9, 2008. The evidence showed that a revision was prepared in December 2008. The Tribunal is satisfied that both versions provided in several places that the Secure Landfill could be operated on a Full Service basis. For example:

> [...] The addition of secure landfill capabilities to this facility would allow for direct disposal in addition to treatment and remediation of contaminated soil. This addition would allow the Babkirk facility to compete with the nearby Silverberry Secure Landfill facilities. The proposed facilities would be contained entirely within the footprint of the former facilities.
>
> [our emphasis]

**183** Mr. Baker's evidence was that the Vendors worked directly with SNCL on the Operations Plan and that they had worked "quite a little bit" on revisions to the first draft. However, he testified that when the Vendors reviewed the revised version they were not satisfied and decided to prepare their own plan. He added that writing a new plan would have taken "months" of work.

**184** However, other evidence makes it clear that the Vendors did not pursue the idea of rewriting the Operations Plan. Minutes of Complete's meeting, which Ron Baker attended in March 2010, show that the Vendors then thought that it was "mostly in order" and that only a couple of weeks were needed to put it in final form for the MOE. Minutes of a later meeting in May 2010 suggest that the Operations Plan needed "4-5 days work".

**185** Mr. Baker acknowledged that he understood the Operations Plan to be saying that waste generators could directly and finally dispose of untreatable Hazardous Waste into the Secure Landfill at the Babkirk Site. In this regard, the transcript of his cross-examination at p. 1212 reads:

> **Mr. Iatrou**: So you would accept waste. Some of it might be highly contaminated, not really treatable. That would stay in [the secure landfill], but the stuff that could be treated would come out of that cell as capacity and the bioremediation cell was freed up?
>
> **Mr. Baker**: That's correct.

**186** However, a review of Mr. Baker's entire cross-examination on the Operations Plan reveals, in the Tribunal's view, that when he gave that answer, he was not saying that the Vendors intended to operate a Full Service Secure Landfill. Rather, he was describing what was possible under the plan. This difference becomes clear in the following

exchange:

> **Mr. Iatrou**: You would accept the same sort of material that you could take to Silverberry?
>
> **Mr. Baker:** Yes, correct. We could accept it. Our plan was not to accept the type of soil that can only go to Silverberry, if you get my drift here. I suppose I have to explain that slightly.

[our emphasis]

**187** Towards the end of his cross-examination, Mr. Baker began to answer questions from the Vendors' perspective. For example, when asked about the section of the Operations Plan that spoke about closing secure cells once they were filled, he stated "This was the concept, that if we ever got around to using the Secure Landfill section of our facility..." [our emphasis].

**188** And at the end of his examination, when asked whether or not all three secure cells had to be built at once, Mr. Baker said "No, no, no. This whole idea of graded construction was that we - our intention half of one cell and never have to do anything further. That was our intention. We would store so little of this landfillable material in that portion of a cell that it would last us the lifetime of our interest in this operation." [our emphasis].

**189** In the Tribunal's view, it is clear that the Vendors' approach to the Operations Plan was the same as it had been to the RADs. A plan that permitted the direct disposal of Hazardous Waste did not oblige the Vendors to accept it. It is obvious to the Tribunal that, from the early days of Newco in 2007, the Vendors wanted to make the Babkirk Facility as attractive as possible for sale and this meant that it had to be capable of being operated as a Full Service Secure Landfill. However, this does not mean that the Vendors intended to operate the Babkirk Facility in that manner given their long expressed preference for a bioremediation facility with an Incidental Secure Landfill.

**Was Babkirk Going to Compete with CCS?**

**190** The Commissioner also relies on what she describes as the Vendors' expressed intention to compete with CCS to support her allegation that Complete was poised to operate a Full Service Secure Landfill at the Babkirk Site. The statements on which she relies are found in the RADs, the Operations Plan and in Complete's minutes.

**191** There is no doubt that, in 2006 when the Babkirks approached SNCL to work on documents for the EA Certificate, they intended to operate a Full Service Secure Landfill on the Babkirk Site once the approvals were in place. As noted earlier, the original project description prepared by SNCL makes this clear when it says:

> The Proponent [BLS owned by the Babkirks] has reportedly experienced a considerable decline in his soil storage and treatment business since the approval of the Silverberry Secure Landfill Facility application (north of Fort St. John, BC) as understandably, direct disposal forms a more cost effective option for clients than treatment and disposal. The conversion of the existing facility from a purely Short-term Storage and Treatment Facility to a Secure Landfill and Short-term Storage and Treatment Facility will allow fair competition between the Proponent and Silverberry facilities in providing responsible waste management solutions for local industry.

[our emphasis]

**192** This language is repeated in the Terms of Reference and the point is made even more clearly in the application for the EA Certificate. It states that the proposed facility would allow the proponent to provide "market

competition for direct disposal of waste soil" and speaks of the Babkirk Facility being in "direct competition" with CCS at Silverberry.

**193** The Vendors' Operations Plan also mentions that the Secure Landfill has been added to the Babkirk Site to allow it to compete with Silverberry and, in the Vision Statement she wrote for Newco, which is attached to minutes dated June 22, 2008, Karen Baker stated that the Vendors wanted Complete "...to become the Number One Competitor to the industry leader [CCS/Newalta]".

**194** In his cross-examination at the hearing, Randy Wolsey acknowledged an intention to compete with CCS. However, he testified that while landfilling and competing with Silverberry was "going to happen", it would be on a "very different scale" because the Vendors were going to supply a "brand new service".

**195** Mr. Baker also acknowledged in his testimony that the Vendors did intend to compete with CCS and others, but not on price. He stated that they were going to compete by offering a service that was different from anything offered by CCS or Newalta.

**196** The Tribunal has concluded that Complete intended to "compete" with Silverberry by offering a new bioremediation service, and that its statements about competition were not intended to mean that the Vendors planned to operate a Full Service Secure Landfill on the Babkirk Site.

**Conclusions**

**197** If the Merger had not occurred, it is the Tribunal's view that, at the end of July 2010, in the absence of a letter of intent from SES, the Vendors would have proceeded to develop the Babkirk Facility. This would have involved:

* Completing the Operations Plan;
* Securing the MOE's approval for the Operations Plan;
* Constructing a half cell of Secure Landfill capacity i.e. 125,000 tonnes; and
* Accepting Hazardous Waste for bioremediation and moving waste that could not be successfully bioremediated into the Incidental Secure Landfill.

**198** Although there was evidence to suggest that the Vendors might have decided to start accepting waste for bioremediation without any Secure Landfill capacity, the Tribunal has concluded that the Vendors would likely have built their half cell of Secure Landfill as soon as possible for two reasons. First, the Vendors told Del Reinheimer of the MOE on January 20, 2010 about the importance customers placed on having Secure Landfill capacity available. Indeed, Petro-Canada had refused to deliver waste for bioremediation until the Vendors opened a Secure Landfill. Second, Ken Watson testified that the plan was to store in the Secure Landfill all waste that was awaiting treatment. Presumably, this storage capacity would have been needed as soon as the business started in earnest.

**199** The Tribunal has also concluded that it is more likely than not that the Vendors would have had an approved operations plan by the end of October 2010 and that the three months of preparatory work, which Ken Watson testified was needed before the Babkirk Facility could accept waste, would have been substantially completed by the end of October 2010.

**200** This means that in the spring of 2011, the Vendors would have been able to accept waste for bioremediation. However, since generators had advised that they would not tip until a Secure Landfill was available, it is unlikely that any meaningful quantity of waste would have been delivered. Construction of the half cell of Incidental Secure Landfill would have begun as soon as the construction season opened in June 2011. Accordingly, given that the evidence showed that the construction would take three or four months, the Tribunal has concluded that the Babkirk Facility would have been fully operational by October 2011.

**201** The evidence establishes that the Vendors felt that a twelve month period was needed to see how well bioremediation would work. The Tribunal therefore considers it reasonable to project that the Vendors would have carried on with bioremediation as their principal focus through the fall of 2012. However, the Tribunal has also concluded that, notwithstanding Ken Watson's contacts and his experience with bioremediation, the Vendors' bioremediation business would have been unprofitable for the reasons discussed below.

**202** There would have been few if any customers for two reasons. First, while the evidence showed that there is a significant amount of treatable soil on drilling sites in the area around the Babkirk Facility, the bioremediation that presently occurs is done by generators on their own sites. There was no evidence that any companies are paying to transport waste to offsite bioremediation facilities in NEBC. Although Ken Watson testified that he expected that CNRL, Encana, and Bonavista would be interested in disposing of their waste in this fashion and, although Petro-Canada had been interested, the Vendors did not call evidence from any prospective customers to say that they would be prepared to truck their waste to the Babkirk Facility for bioremediation. Further, the Vendors provided the Commissioner with a list of potential customers and **[CONFIDENTIAL]** was first on that list. However, Mr. **[CONFIDENTIAL],** Vice-President, Operations at **[CONFIDENTIAL]**, testified for the Commissioner that **[CONFIDENTIAL]** philosophy is "going to landfill". In other words, his company was not a significant potential customer for the Vendors' bioremediation facility.

**203** Second, the Vendors testified that the Tipping Fees they would charge for bioremediation would be significantly higher than Silverberry's Tipping Fees for Secure Landfill services. It is difficult to imagine that generators with waste that could be bioremediated on their own sites would pay large sums to transport their Hazardous Waste to Babkirk and tip there at rates higher than those at Silverberry, given that they could continue to bioremediate on their own sites or tip for less at Silverberry.

**204** Further, there was no evidence from any potential purchasers who might have bought treated waste from Complete for use as cover for municipal dumps or as backfill for excavations. It does not appear that any such sales would have been available to generate revenue for Complete.

**205** It is not clear how long the Vendors would have been prepared to operate on an unprofitable basis, without beginning to accept more waste at the Secure Landfill part of the Babkirk Facility. In their final written submissions, the Vendors ask the Tribunal to assume that they would have incurred losses for two years before they decided that their venture had failed.

**206** However, the Tribunal has concluded that, because there was no evidence that the Vendors have deep pockets or significant borrowing power, it is unreasonable to suppose that they would have been prepared to operate unprofitably beyond the fall of 2012, when they could have generated additional revenues by accepting more waste into the Secure Landfill part of their facility.

**207** Accordingly, it is the Tribunal's view that the Vendors would have started to operate a Full Service Secure Landfill at least by the spring of 2013. In other words, they would have begun to accept significant quantities of Hazardous Waste for direct disposal into Babkirk's Secure Landfill, in competition with CCS. In the alternative, they would have sold Complete or BLS to a purchaser which would have operated a Full Service Secure Landfill. Given that the Vendors had a valuable and scarce asset and given the evidence that demand for Secure Landfill services has, for some time, been projected to increase as new drilling is undertaken in the area north and west of Babkirk, the Tribunal is satisfied that such a sale would have been readily available to the Vendors. Finally, whether Babkirk was operated by the Vendors or a new owner, Babkirk and Silverberry would have become direct and serious competitors by no later than the spring of 2013.

**208** We have reached this conclusion notwithstanding CCS' submission that the Vendors' lack of experience and the smaller capacity of the Babkirk Facility would have constrained it from functioning as a serious competitor. In our view, as they had done in the past when they retained IRTL, the Vendors would have hired experts, if needed,

to redress their lack of expertise. Moreover, 750,000 tonnes of permitted capacity was sufficient to allow the Vendors or a purchaser to compete effectively with CCS at Silverberry.

**209** To summarize, the Tribunal has decided that it is likely that the Vendors would have operated a bioremediation treatment facility with an Incidental Secure Landfill for approximately one year from October 2011 to October 2012 (the "Initial Operating Period"). Thereafter, in the spring of 2013, the Babkirk Facility would have become a Full Service Secure Landfill.

**210** Turning to the impact of these developments, it is the Tribunal's view that, as soon as the half cell of the Secure Landfill capacity at the Babkirk Facility was operational in October of 2011, waste generators who tipped at Silverberry would have seen that there was a potential alternative to Silverberry at the Babkirk Facility. The Tribunal cannot predict what would actually have happened. However, we can reasonably expect that, during the Initial Operating Period, some generators of Hazardous Waste would have asked the Vendors to take their waste for direct disposal, if only to use the possibility of disposing at Babkirk as a basis for negotiating lower Tipping Fees at Silverberry. This would have been possible because many oil and gas producers have one year non-exclusive contracts with CCS.

**211** As well, given that the Vendors would have needed revenue and given that it might have been convenient for some of their customers, it is reasonable to assume that the Vendors would have accepted at least some Hazardous Waste for direct disposal during the Initial Operating Period, in spite of their evidence that this was not their intention. This possibility was foreseen by Ron Baker when, in his cross-examination, he was asked about the decision matrix in the Operations Plan which reflected that soil which arrived and could not be bioremediated would be landfilled with other soil that could not be bioremediated. He said that, "if we had room", "chances are" such soil would be put in the Secure Landfill.

**212** The question is whether this competition afforded by Babkirk in the Initial Operating Period can be considered substantial. In *Director of Investigation and Research v. Tele-Direct (Publications) Inc.* *(1997), 73 C.P.R. (3d) 1*, the Tribunal addressed the question of the potential importance of a small amount of competition, in the course of examining the impact on Yellow Pages consultants of Tele-Direct's discriminatory anti-competitive practices. In that case, the Tribunal was considering whether there had been a substantial lessening of competition.

**213** The Tribunal heard evidence that consultants, who charged fees to place Yellow Pages advertisements, had lost time and money and that their ability to attract new customers had been damaged by Tele-Direct's conduct. The Tribunal also found that, although the consultants only occupied a small segment of the market and had a limited and fragile ability to compete with Tele-Direct, they had had a significant positive influence on the level of service Tele-Direct provided to customers who were purchasing yellow pages advertisements. In this context the Tribunal stated at paragraph 758:

> Where a firm with a high degree of market power [Tele-Direct] is found to have engaged in anti-competitive conduct, smaller impacts on competition resulting from that conduct will meet the test of being "substantial" than where the market situation was less uncompetitive to begin with. In these circumstances, particularly Tele-Direct's overwhelming market power, even a small impact on the volume of consultants' business, of which there is some evidence, by the anti-competitive acts must be considered substantial.

**214** In contrast, in this case, the Tribunal has concluded that the competition offered by the Babkirk Facility in the Initial Operating Period would likely have had no material, let alone significant, impact on pricing at Silverberry, because any competition would have been offered on an extremely small scale. In our view, during the Initial Operating Period, Silverberry could have ignored any requests by customers for lower prices because the Babkirk Facility would not have been a viable alternative for the volumes of Hazardous Waste oil and gas producers tipped at Silverberry. This means that the prevention of any competition that would have developed in the Initial Operating Period would not have been "substantial".

**215** Turning to the spring of 2013, the competition that would have been offered by Babkirk as a Full Service

Secure Landfill would have been direct and substantial and, as discussed below, it is this competition that was substantially prevented by the Merger.

**B. What are the Relevant Assessment Factors?**

*Conditions of Entry*

**216** The conditions of entry into a relevant market can be a decisive factor in the Tribunal's assessment of whether a merger is likely to prevent or lessen competition substantially. This is because, "[i]n the absence of significant entry barriers it is unlikely that a merged firm, regardless of market share or concentration, could maintain supra-competitive pricing for any length of time"( *Hillsdown*, above, at 324; see also *Propane 1*, above, at para. 127).

**217** To be effective, entry must be timely, likely and sufficient to ensure that any prevention of future competition will not be substantial.

**218** CCS maintains that the evidence in this case is that the Secure Landfill business is not characterized by significant entry barriers and that the conditions for entry are conducive for potential competitors. In this regard, CCS asserts that (i) the regulatory regime is permissive, as evidenced by the fact that a number of permits to operate a Secure Landfill have been granted in NEBC in recent years, (ii) there is a growing market in the NEBC region for oil and gas drilling and related services, coupled with a growing demand and pressure for socially responsible waste management alternatives, and (iii) the industry practice of engaging in short-term contracts is conducive to entry. CCS further asserts that the Commissioner's reliance on the fact that BLS took nearly four years to obtain its Secure Landfill permit is misplaced, most importantly because BLS did not pursue concurrent permitting. Concurrent permitting allows an applicant to pursue applications for EA Certificates and an MOE Permits (together the "Authorizations") in tandem. CCS also asserts that entry is much less time consuming if a remote area near Babkirk is selected. Thus, attempts to develop secure landfills in populated areas around Dawson Creek should not be accepted as precedents for the timing that entry might involve near Babkirk.

**219** Among other things, prior to seeking the Authorizations, a new entrant must spend several months selecting a site from among various potential sites. This involves drilling test holes to determine whether the site's subsurface characteristics are appropriate for Secure Landfilling. If so, a further assessment is undertaken which involves drilling multiple test holes and installing monitoring equipment. There is no evidence about the time needed to complete only a site selection. However, **[CONFIDENTIAL]** spent 15 to 18 months on site selection and the preparation of an application for a potential landfill.

**220** Once a potential entrant has completed the site selection described above, it must then obtain the required Authorizations. The evidence is that this process would likely take at least 18-24 months and that a further 3 to 4 months are needed for construction.

**221** Notwithstanding the time and money ($1.3 million) it spent during the development process, as described earlier, SES abandoned its plans to open the Heritage landfill and, after spending $885,000.00, CCS abandoned its proposed Sunrise Landfill in NEBC, due to opposition from local residents. These two incidents of site abandonment by knowledgeable industry participants underscore the risk and uncertainty associated with new entry, as well as the "sunk" nature of the entry costs in the event that an entry initiative is unsuccessful.

**222** Based on this evidence, the Tribunal has concluded that, even in a remote location and even with concurrent permitting, it would take a new entrant at least 30 months to complete the process of selecting a new site, obtaining the required Authorizations and constructing a new Secure Landfill. That said, the Tribunal notes that there is no evidence of any proposed entry in the Contestable Area.

*Absence of Acceptable Substitutes/Effective Remaining Competition*

**223** For the reasons given earlier, the Tribunal is satisfied that, for some product and for some generators,

bioremediation does not compete in the same market as the supply of Secure Landfill services and does not exercise any constraining influence on price or non-price competition within the latter market.

**224** This conclusion is supported by the fact that CCS' Tipping Fees are significantly higher in areas where it does not face competition from other Secure Landfill operators, than they are in areas where CCS does face such competition. In addition, the "natural experiment" that occurred when SES opened its facility in Willesden Green Alberta, and CCS substantially reduced its Tipping Fees to seven of its significant customers, strongly suggests that CCS' pricing behaviour is primarily determined by reference to the location of competing suppliers of Secure Landfill services, rather than by competition with suppliers of bioremediation services.

**225** Dr. Baye provided extensive evidence with respect to CCS' alleged ability to price discriminate in order to show that it had market power. However, given the foregoing and because CCS is a monopolist in the relevant market and is not constrained by any actual or potential competition from within or outside the market, it is clear that CCS has significant market power. This conclusion is further supported by the discussion of countervailing market power immediately below. For this reason, it is not necessary to consider the allegation of price discrimination.

*Countervailing Power*

**226** CCS correctly notes that none of its customers have complained about the Merger. CCS encourages the Tribunal to infer from this that the Merger is not likely to prevent competition substantially. However, the Tribunal is not persuaded that this is a reasonable inference.

**227** The Tribunal recognizes that CCS' largest customers pay lower Tipping Fees than its smaller customers. However, the Tribunal notes that Dr. Baye's report indicates that even CCS' largest customers are forced to pay higher Tipping Fees in areas where CCS faces no competition than in areas where such competition exists and this evidence was not contested. In 2010, the average Tipping Fees at Silverberry and Northern Rockies were **[CONFIDENTIAL]** and **[CONFIDENTIAL]** respectively. However, Tipping Fees at CCS' South Grande Prairie **[CONFIDENTIAL]** and Rocky **[CONFIDENTIAL]** in Alberta were significantly lower because they both face competition from SES. This no doubt explains why Mr. **[CONFIDENTIAL]**, who testified for the Commissioner, made it clear in his testimony that he would welcome competition for CCS in NEBC.

**228** The attenuated or limited nature of any countervailing power that may be in the hands of CCS' largest customers is also reflected in the evidence that written requests by them for price relief were rejected by CCS during the industry downturn in late 2008 and early 2009.

**C. Conclusions**

**229**

(i) Based on all of the foregoing, the Tribunal has concluded that the Merger is likely to prevent competition substantially. The Merger prevented likely future competition between the Vendors and CCS in the supply of Secure Landfilling services in, at the very least, the Contestable Area. Although the competition that was prevented in 2012 is not likely to be substantial, the Tribunal is satisfied that by no later than the spring of 2013, either the Vendors or a party that purchased the Babkirk Facility would have operated in direct and serious competition with CCS in the supply of Secure Landfill services in the Contestable Area.

(ii) In estimating the magnitude of the likely adverse price effects of the Merger, the Commissioner relied on expert evidence adduced by Dr. Baye. That evidence included economic theory and regression models. However, for reasons discussed below the Tribunal has not given significant weight to that economic theory or to those regression models in assessing the magnitude of the likely adverse price effects of the Merger. In reaching this decision, the Tribunal took into account the fact that the models do not control for costs, and the fact that, although Dr. Baye acknowledged

that his theory of spatial competition should only be used if other data were unavailable, he used his theory even though he had actual CCS data.

(iii) Nevertheless, as discussed below in connection with the "effects" element of section 96, the Tribunal is satisfied that prices likely would have been at least 10% lower in the Contestable Area in the absence of the Merger.

(iv) The Tribunal therefore finds that the Merger is more likely than not to maintain the ability of CCS to exercise materially greater market power than in the absence of the Merger, and that the Merger is likely to prevent competition substantially.

**ISSUE 7** **WHEN THE EFFICIENCIES DEFENCE IS PLEADED, WHAT IS THE BURDEN OF PROOF ON THE COMMISSIONER AND ON THE RESPONDENT?**

**230** CCS has alleged that the Commissioner failed to properly discharge her burden to prove the extent of the quantifiable effects of the Merger. CCS alleges that the Commissioner's failure to prove those effects in her case in chief has precluded CCS from being able to meet its overall burden to prove the elements of the efficiencies defence on a balance of probabilities. CCS asserts that the Commissioner's failure means that the effects should be zero and that the Application should therefore be dismissed.

**231** In paragraph 48 of its response to the Commissioner's Application, CCS pleaded the efficiencies defence in the following terms:

> The Acquisition has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention of competition that will result from the Acquisition, and the gains in efficiency will not likely be attained if the requested order or orders are made by the Tribunal.

**232** The burdens of proof under section 96 were established and applied over the course of the four decisions in *Propane* (*Propane 1*, at para. 48, rev'd on other grounds *2001 FCA 104*, *[2001] 3 F.C. 185* ("*Propane 2"*), leave to appeal to SCC refused, 28593 (September 13, 2001), redetermination, *The Commissioner of Competition v. Superior Propane Inc.*, *2002 Comp. Trib. 16*, *18 C.P.R. (4th) 417* ("*Propane 3*"), aff'd *2003 FCA 53*, *[2003] 3 F.C. 529* ("*Propane 4*")). "The effects of any prevention or lessening of competition" must be demonstrated by the Commissioner on balance of probabilities (*Propane 1*, above, at para. 402; *Propane 2*, above, at para. 177*, Propane 4,* at para. 17). Her burden is to prove (i) the extent of the *anti-competitive* effects in question where they are quantifiable, even if only roughly so (*Propane 4*, at paras. 35-38), and (ii) any non-quantifiable or qualitative *anti-competitive* effects of the merger. It also includes the burden to demonstrate the extent of any *socially adverse* effects that are likely to result from the merger, i.e., the proportion of the otherwise neutral wealth transfer that should be included in the trade-off assessment contemplated by section 96, as well as the weighting that should be given to those effects (*Propane 4*, above, at paras. 35-38, and 61-64). In this case, there being no socially adverse effects, the term "Effects" will be used to described quantifiable and non-quantifiable anti-competitive effects.

**233** That said, the respondents bear the burden on the ultimate issue, namely, that the efficiency gains are likely to be greater than, and to offset, the effects of any prevention or lessening of competition likely to result from the merger (*Propane 2*, above, at para. 154).

**234** There is no dispute about the fact that, in his expert report in chief, Dr. Baye only calculated that an average price decrease of at least 10% would be prevented by the Merger. This meant that CCS did not have a figure for the Effects and was obliged to serve its expert report on efficiencies with no ability to take a position about whether the number it calculated for its total efficiencies was greater than the Effects. As a result, CCS maintains that, as a matter of substantive and procedural fairness, it was effectively denied a right of response and the ability to properly

meet its own burden under section 96. It therefore asserts that the Tribunal should conclude that there are no quantified Effects as a result of the Merger.

**235** Dr. Baye did eventually quantify the Effects but not until he wrote his reply report, which was only made available to CCS two weeks before the hearing. By then, the Tribunal's Scheduling Order did not permit CCS to bring a motion or file a further expert report. In addition, the Tribunal accepts that, in practical terms, there was insufficient time before the hearing to permit CCS to move to strike Dr. Baye's report or to seek leave to file a further report in response to the Commissioner's quantification of the Effects.

**236** The Commissioner maintains that her substantive burden to quantify the Effects only arises once a respondent advances its affirmative defence by proving efficiencies. She submits that any other result would require her to respond to every bald assertion of efficiencies, regardless of whether a respondent actually relies on efficiencies at the hearing. She asserts in her final written argument that this "would be an incredible waste of resources, and one that is antithetical to the notion of responding to an affirmative defence".

**237** In the Tribunal's view, the Commissioner's argument about resources does not justify her failure to meet her burden to prove the Effects as part of her case in chief. Once CCS pleaded section 96, the efficiencies defence became part of the fabric of the case and, if it had not been pursued by CCS, the Commissioner would have been entitled to costs fully compensating her for work done by her experts to calculate the Effects.

**238** The Commissioner also defended her approach by stating that, until CCS served Dr. Kahwaty's report on efficiencies ("Efficiencies Report"), it was an open question whether it was going to pursue the efficiencies defence at all. In this regard, she noted that prior to serving that report, CCS advanced no facts or proof of efficiencies, and provided no guidance on the types of efficiencies that Dr. Kahwaty planned to identify and quantify. She also observed that the Tribunal's Revised Scheduling Order, dated August 19, 2011, indicated that CCS might not pursue the efficiencies defence.

**239** The revised scheduling order required the "Corporate Respondents to serve expert reports*, if any*, on efficiencies and provide them to the Tribunal" on or before October 7, 2011 (our emphasis). However, since the phrase "if any" was proposed by the Commissioner and not by CCS, the Tribunal does not accept that it suggests that CCS had resiled from its pleading.

**240** In addition, the Tribunal can find no basis in the record for concluding that CCS did not intend to mount the efficiencies defence. The Tribunal notes that the Commissioner asked questions about efficiencies during examination for discovery and asked, during a case management teleconference on August 15, 2011, that CCS be ordered to produce documents relevant to the issue. During that teleconference, the Presiding Judicial Member stated that efficiencies were at issue and that, if relevant documents existed, their production was required.

**241** Given the pleading of section 96 and these developments, the Tribunal concludes that there was no reason to doubt that CCS would pursue an efficiencies defence.

**242** The Commissioner further asserts that the legislation and the case law do not dictate how she must meet her burden to prove the extent of the Effects. She submits that she is not obliged in every case to lead evidence about demand elasticities and provide detailed calculations about the range of likely Effects. This is particularly so in a case such as this in which she asserts that the efficiencies are "plainly so minimal that it was an open question whether [the efficiencies defence would even be pursued]".

**243** The Tribunal acknowledges that the legislation and the jurisprudence do not dictate how the Commissioner must meet her burden. However, as noted above, where it is possible to quantify the Effects of a merger, even if only in "rough" terms, the Commissioner has the onus to provide an estimate of such Effects (*Propane 4*, above, at paras. 35 - 38).

**244** Indeed, where the necessary data can be obtained, the Commissioner will be expected in future cases to

provide estimates of market elasticity and the merged entity's own-price elasticity of demand in her case in chief. These estimates facilitate the calculation of the magnitude of the output reduction and price effects likely to result from the merger. They are also necessary in order to calculate the deadweight loss ("DWL") that will likely result from the output reduction and related price effects. DWL is the loss to the economy as a whole that results from the inefficient allocation of resources which occurs when (i) customers reduce their purchases of a product as its price rises, and shift their purchases to other products that they value less, and (ii) suppliers produce less of the product.

**245** Given that there will often be shortcomings in the data used to estimate market elasticities and the merged entity's own-price elasticity of demand, prudence dictates that a range of plausible elasticities should be calculated, to assist the Tribunal to understand the sensitivity of the Commissioner's estimates to changes in those elasticities. The Tribunal will be open to making its assessment of the quantitative extent of the Effects on the basis of persuasively supported "rough estimates" of those Effects, but only if the data required to reliably estimate elasticities cannot reasonably be obtained. Such rough estimates may be derived from evidence with respect to the magnitude of the likely price effects of the merger, including statements or projections made in the internal documents of the respondent or its advisors (including its investment bankers); persuasive estimates by customers, other lay witnesses, or expert witnesses; and persuasive evidence from "natural experiments."

**246** Although the Commissioner failed to meet her burden, in the unusual circumstances of this case, CCS was not prejudiced by that failure because, instead of doing the required independent analysis of elasticities, Dr. Baye relied on his assumed price decrease of at least 10% and on certain assumptions used by Dr. Kahwaty in calculating CCS' claimed market expansion efficiencies. In making that calculation, Dr. Kahwaty assumed that the opening of a Secure Landfill at Babkirk would lead waste generators to dispose of approximately **[CONFIDENTIAL]** additional tonnes of Hazardous Waste, as forecast in CCS' internal documents. Further, during the hearing. Dr. Kahwaty was able to effectively attack Dr. Baye's DWL calculations on various grounds, including his failure to base them on conventional calculations of elasticities when he could have obtained the data necessary to perform those calculations. In short, CCS was able to effectively assert the defence and argue that the efficiencies its expert presented were greater than the Effects (i.e. the DLW) calculated by Dr. Baye. For these reasons, the Tribunal declines to dismiss the Application.

**247** There is a second reason why CCS' request is being denied. CCS was also required to show that the cognizable efficiencies would be likely to *offset* the Effects. This means that even if the Tribunal had accepted CCS' submission that a zero weighting should be given to the quantifiable Effects, it would not necessarily follow that the Tribunal would find that the *offset* element of section 96 has been established on a balance of probabilities.

**248** This is so for two reasons. First, as noted in *Propane 3*, above, at para. 172, "it cannot be concluded that the Tribunal would find that efficiency gains (whether large or small) that marginally exceeded the effects (whether large or small) would necessarily offset those effects." This is because the loss of dynamic competition will always merit some non-trivial qualitative weighting in the trade-off assessment. Indeed, dynamic efficiencies and dynamic Effects can have a major impact on the trade-off assessment. Second, in this case, the Commissioner adduced evidence of *qualitative* Effects in Dr. Baye's expert report in chief. As well, CCS adduced evidence of qualitative efficiencies, such as improved service, reduced risk for customers and the environment, which put in play the issue of whether a substantial prevention of competition likely would adversely impact upon these matters.

**249** Accordingly, the Commissioner's failure to meet her burden to quantify the Effects, even in rough terms, at the appropriate time is not a sufficient reason to conclude that CCS is relieved of its obligation to meet its burden to meet the "offset" element in section 96.

**ISSUE 8 HAS CCS SUCCESSFULLY ESTABLISHED AN EFFICIENCIES DEFENCE?**

**What are the Claimed Efficiencies?**

**250** We now turn to summarizing the efficiencies claimed by CCS. In that regard, Dr. Kahwaty testified on behalf of CCS that the Merger would likely result in efficiencies that he grouped into the following five categories.

**251 Transportation efficiencies**: These were described as being productive efficiencies realized by those customers presently serviced at Silverberry, who have an aggregate of **[CONFIDENTIAL]** locations that are situated closer to the Babkirk Facility than to Silverberry. Once CCS opens the Babkirk as a Secure Landfill, those customers will realize significant transportation cost savings, thereby freeing up resources for other uses. Based on what he described as the "going rate" of approximately **[CONFIDENTIAL]** for trucking services, the number of loads shipped from each of the above-mentioned **[CONFIDENTIAL]** locations in 2010, and the time saved by tipping at Babkirk instead of Silverberry, Dr. Kahwaty estimated the annual aggregate transportation cost savings for the aforementioned customers to be **[CONFIDENTIAL]**. Using a lower trucking rate of **[CONFIDENTIAL]** per hour per load (or $5 per tonne per hour of transport), Dr. Kahwaty provided a second estimate of those annual transportation cost savings, which totaled **[CONFIDENTIAL]**. Dr. Kahwaty also calculated that his two estimates represented approximately **[CONFIDENTIAL]** and **[CONFIDENTIAL]** respectively of CCS' 2010 revenue derived from the **[CONFIDENTIAL]** customer locations in question.

**252 Market expansion efficiencies**: Dr. Kahwaty stated that, absent the opening of a Secure Landfill at Babkirk, a significant volume of existing Legacy Waste and newly generated Hazardous Waste, within the drawing area of the Babkirk Facility, would not have been transported to Silverberry due to the significant risk, and related financial liability, that would be associated with transporting such waste over the long distance to Silverberry. However, with the opening of a Secure Landfill at the Babkirk Site, CCS estimated that approximately **[CONFIDENTIAL]** tonnes per year of such waste ("Market Expansion Waste") likely would be transported for disposal at Babkirk. Dr. Kahwaty acknowledged that this estimate is "necessarily imprecise," and suggested that the incremental volume of Market Expansion Waste could substantially exceed CCS' estimate of **[CONFIDENTIAL]** tonnes per year. Based on the reported margin for Silverberry in 2009 of **[CONFIDENTIAL]** and a price of **[CONFIDENTIAL]** per tonne, Dr. Kahwaty estimated an increase in producer surplus from this incremental volume of **[CONFIDENTIAL]**. In addition, based on an estimated reduction in disposal costs of **[CONFIDENTIAL]** per tonne, Dr. Kahwaty estimated that customers would gain approximately **[CONFIDENTIAL]** per year in consumer surplus. This is only 50% of the product of multiplying **[CONFIDENTIAL]** by **[CONFIDENTIAL]**, because Dr. Kahwaty felt that customers do not gain the full reduction in the costs of disposal when they are induced to dispose of their waste by virtue of a lower overall cost of disposition. The sum of the estimated **[CONFIDENTIAL]** in producer surplus gains and the estimated **[CONFIDENTIAL]** in consumer gains, was a total of **[CONFIDENTIAL]** of annual market expansion efficiencies.

**253 Overhead Efficiencies**: Dr. Kahwaty estimated that the Merger would result in annual overhead savings of approximately **[CONFIDENTIAL]**. He stated that these savings likely would be achieved by virtue of the fact that CCS could draw upon its existing administrative staff (e.g., those persons who deal with legal, regulatory, marketing, engineering, financial and health & safety matters) in operating the Babkirk Facility. In the absence of the Merger, he stated that the Vendors likely would have had to incur expenses associated with these functions. In reaching his estimate of **[CONFIDENTIAL]**, Dr. Kahwaty used the cost reductions that CCS has achieved in operating Complete's Roll-off Bin Business as a proxy. In addition, he submitted that some "qualitative" credit should be given to this category of efficiencies, because Complete would otherwise need to expend resources developing administrative systems and to deal with some of the matters identified above.

**254 Roll-off Bin Business Efficiencies**: Dr. Kahwaty estimated that CCS's Merger of the Roll-off Bin Business has resulted in annual cost savings of approximately **[CONFIDENTIAL]**. These savings were described as having been achieved as a result of (i) the upgrading of its trucks to meet higher safety standards, (ii) investments in business development efforts, and (iii) the absorption of administrative functions, such as billing, into CCS' pre-existing corporate systems.

**255 Qualitative efficiencies**: Dr. Kahwaty listed the following qualitative efficiencies as being likely to result from the Merger:

a. the landfill services to be offered by CCS at the Babkirk Site will be of higher (and known) quality and involve less risk for customers due to CCS's knowledge and experience in the operation and management of hazardous waste landfills;

b. customers will benefit from being able to purchase bundled packages of services that may include, for example, loading, trucking and tipping services;

c. the landfill services to be offered by CCS at the Babkirk Site will reduce risks for customers due to CCS's substantial financial resources, which provide assurance to customers regarding the long-term management of the Babkirk Facility and the potential continuing liability for wastes disposed in that landfill;

d. CCS will have the capability and resources necessary to expand the Babkirk Facility as necessary and to meet special customer needs (e.g., rapid responses to increased disposal needs);

e. since landfilling is CCS' business and since the Vendors were not planning to operate a Secure Landfill, CCS will promote landfilling services to a greater extent than the Vendors would have done, once the Babkirk Site is operational, making trucking cost efficiencies available to more customers;

f. the provision of Secure Landfill services by CCS at the Babkirk Site will reduce risks for generators, trucking firms, and other road users related to the transportation of Hazardous Waste on roads over long distances;

g. increased competition in the Roll-off Bin Business will benefit roll-off customers and may reduce the extent of any DWL in the roll-off industry, which will increase the total surplus generated in the roll-off marketplace; and

h. increased site remediation from reduced trucking costs will benefit area residents, wildlife, and the overall environment, and will also further the government's policy of expanding contaminated site remediations.

**256** Dr. Kahwaty also stated that some or all of the efficiencies identified above would likely be achieved sooner by CCS than by Complete or by any third-party who might acquire the Babkirk Facility pursuant to an order of the Tribunal.

**257** In addition, Dr. Kahwaty stated that CCS should be given credit for some of the efficiencies that it has already achieved in respect of the Roll-off Bin Business.

**258** Finally, Dr. Kahwaty provided reasoned estimates about the extent to which the above-mentioned trucking and market expansion efficiencies would increase under market growth scenarios of 1%, 2% and 4% compounded annually over the next 10 years. Based on this work, he suggested that these increased efficiencies ought to be considered by the Tribunal.

**259** After providing his annual estimates of the quantifiable efficiencies, Dr. Kahwaty calculated the net present value of those efficiencies as of January 1, 2012 using three different discount rates: (i) a risk-free interest rate of 1%, which he described as being the annual yield on one to three year government of Canada marketable bonds over the 10 week period preceding the date of his report (October 7, 2011); (ii) an interest rate of 10%, which he described as being "roughly equivalent to rates prevailing in the oil and gas industry"; and (iii) an intermediate rate of 5.5%.

**260** The Tribunal accepts the evidence of Mr. Harrington, the Commissioner's expert, that, in broad terms, the discount rate used in calculating the net present value of efficiencies typically does not matter, so long as the same discount rate is used to calculate the net present value of the Effects. That said, the Tribunal also accepts Mr. Harrington's evidence that, (i) as a general principle, the appropriate discount rate to use in discounting a set of future cash flows is a function of the risk of those cash flows being wrong, (ii) there is some uncertainty associated with the efficiencies identified and estimated by Dr. Kahwaty and CCS, and therefore (iii) the midpoint (5.5%) of the

three discount rates identified by Dr. Kahwaty is the most defensible of the three rates to use in calculating efficiencies and Effects in this case.

**The assessment of the claimed efficiencies**

**261** In the initial stage of assessing efficiencies claimed under section 96 of the Act, the Tribunal applies five screens to eliminate efficiencies that are not cognizable under that section.

**262** The first screen eliminates claims that do not involve a type of productive or dynamic efficiency, or that are not otherwise likely to result in any increase in allocative efficiency. The second screen narrows the claimed efficiencies to those that the Tribunal is satisfied are *likely* to be brought about by the Merger. Efficiencies that cannot be demonstrated to be more likely than not to be attained in the Merger are filtered out at this stage. The third screen filters out claimed efficiency gains that would be brought about by reason only of a redistribution of income between two or more persons, as contemplated by subsection 96(3). These types of gains include savings that result solely from a reduction in output, service, quality or product choice, as well as from increases in bargaining leverage and reductions in taxes. The fourth screen filters out claimed efficiency gains that would be achieved outside Canada and would not flow back to shareholders in Canada as well as any savings from operations in Canada that would flow through to foreign shareholders.

**263** In the case at bar, the application of the first four screens does not result in the elimination of any of the claimed efficiencies.

**264** The fifth screen filters out claimed efficiencies that either (a) would likely be attained through alternative means if the Tribunal were to make the order that it determines would be necessary to ensure that the merger in question does not prevent or lessen competition substantially, or (b) would likely be attained through the Merger even if that order were made. This screen has a critical role to play in the case at bar.

**265** In this case, the fifth screen eliminates most of the efficiencies claimed by CCS. With three exceptions, being the one year of transportation efficiencies and the one year of market expansion efficiencies discussed at paragraph 269 below, as well as the overhead efficiencies discussed above, virtually all of the efficiencies claimed by CCS would likely be achieved even if the order referred to in the preceding paragraph is made. That order is an order for the divestiture of the shares or assets of BLS (the "Order").

**266** Although there is currently some uncertainty regarding the identity of a prospective purchaser, the Tribunal is satisfied that a divestiture will ultimately be made to a purchaser who will operate the Babkirk Facility and attract essentially the same volumes of Hazardous Waste as were assumed by Dr. Kahwaty in arriving at his estimates of transportation and market expansion efficiencies.

**267** The Tribunal has decided that, absent exceptional circumstances, it will not be prepared to conclude that the claimed efficiencies that would be realized by any acceptable alternative purchaser should be included in the trade-off assessment, on the basis that it is not possible to identify any particular *likely* purchaser of the shares or assets contemplated by the divestiture order.

Transportation and Market Expansion Efficiencies

**268** Based on the reasonable assumption that a purchaser under the Order will emerge and attract, in its first year of operation, the volume of Hazardous Waste that formed the basis for Dr. Kahwaty's estimates of CCS' claimed transportation and market expansion efficiencies, those efficiencies cannot be considered in the section 96 assessment because they are likely to be achieved even if the Order is made.

**269** A noteworthy exception to this conclusion concerns the transportation and market expansion efficiencies that CCS claims would be achieved more quickly by CCS than by a purchaser. In this regard, CCS asserted that it would already have been operating at Babkirk but for the Commissioner's intervention and that, in any event, it is

likely to be in a position to operate a Secure Landfill at the Babkirk Site by the summer of 2012. In contrast, CCS stated that a purchaser following a divestiture is unlikely to be in a position to operate a Secure Landfill facility at the Babkirk Site before mid-2013, having regard to the time required (i) for the Tribunal to render a decision in this proceeding, (ii) to effect the actual sale of the shares or assets of BLS (which it estimates to will require "at least six months, or more," inclusive of due diligence), (iii) to modify or prepare an operations plan for the landfill, (iv) for the MOE to approve the operations plan, and (v) for the purchaser to construct the landfill, bearing in mind that construction can only be undertaken between June and September.

**270** In the Tribunal's view, claimed efficiencies that would not likely be achieved by a purchaser under the Order, but that would likely be achieved by CCS solely because of the types of delays identified immediately above and associated with the implementation of the Order, are not cognizable efficiencies under section 96. These will be described as "Order Implementation Efficiencies". In the case at bar, CCS and the Vendors completed the Merger after being advised that the Commissioner intended to apply to the Tribunal. To give the Respondents the benefit of Order Implementation Efficiencies in such circumstances, and thereby potentially preclude the Tribunal from issuing the Order in respect of their anticompetitive Merger, would be contrary to the purposes of the Act.

**271** In any event, even if CCS were given full credit for the Order Implementation Efficiencies, those efficiencies are only likely to be between **[CONFIDENTIAL]** and **[CONFIDENTIAL]** (which represents one year of transportation cost savings) plus **[CONFIDENTIAL]** (which represents one year of annual market expansion efficiencies). As discussed below in connection with the Tribunal's treatment of the "offset" element of section 96, these efficiencies are not sufficient to change the Tribunal's overall determination with respect to section 96.

The Roll-off Bin Business Efficiencies

**272** The divestiture of the shares or assets of BLS will not have any impact on the Roll-off Bin Business efficiencies claimed by CCS. Stated alternatively, those efficiencies will likely be attained even if the Order is made. Accordingly, those efficiencies cannot be considered in the trade off assessment contemplated by section 96.

**273** CCS has also submitted that certain productive efficiencies have already been achieved as a result of (i) its upgrading and sale of trucks to meet higher safety standards and to operate more efficiently, and (ii) CCS having absorbed certain administrative functions into its pre-existing corporate functions. However, as Mr. Harrington testified on behalf of the Commissioner, these efficiencies would only be lost if CCS were required to divest the Roll-off Bin Business. Given that the Order does not include the Roll-off Bin Business, those efficiencies will not be affected by the Order as contemplated by subsection 96(1) of the Act. Accordingly, they are not cognizable. In any event, given the value of these efficiencies, which Dr. Kahwaty estimated to be approximately **[CONFIDENTIAL]**, the Tribunal's overall conclusion with respect to section 96, set forth below, would not change even if these efficiencies were given full value in the trade-off assessment.

**274** More generally, if certain efficiencies have already been achieved, they cannot be considered to be a potential "cost" of making the order contemplated by section 96. Therefore, they cannot be considered in the assessment under section 96. In other words, it cannot be said that those efficiencies "would not likely be attained if the order were made," as required by subsection 96(1).

The Overhead Efficiencies

**275** As has been noted, Dr. Kahwaty estimated that these efficiencies would likely total approximately **[CONFIDENTIAL]** per year. He arrived at this assessment by, among other things, using as a proxy the cost reductions that CCS has achieved in operating the Roll-off Bin Business. Those cost reductions amounted to approximately 21% of the overhead expenses that previously were incurred by Complete in operating the Roll-off Bin Business. Dr. Kahwaty applied this 21% to the overhead expenses incurred at Silverberry, to reach his estimate of approximately **[CONFIDENTIAL]** in annual overhead savings. Mr. Harrington took issue with this methodology, in part because the Roll-off Bin Business is different from the landfill business. In addition, he opined that if there is a divestiture, some of these savings, which he described as being equivalent to one-half of the annual cost of a full

time back-office employee, would likely be achieved by the purchaser. The Tribunal is persuaded by this reasoning and therefore accepts Mr. Harrington's conclusion that the annual overhead efficiencies which are cognizable under section 96 are reasonable but are probably somewhat less than the **[CONFIDENTIAL]** that CCS has claimed.

**276** As a practical matter, given the conclusion that the Tribunal has reached with respect to the "offset" element of section 96, discussed below, the fact that a more precise estimate of the cognizable overhead efficiencies is not available does not affect the Tribunal's overall determination with respect to the efficiencies defence in section 96.

The Qualitative Efficiencies

**277** As discussed above, Dr. Kahwaty identified eight types of qualitative efficiencies that he claimed would likely result from the Merger. The Tribunal is not persuaded that any of these efficiencies "would not likely be attained if the Order were made," as provided in subsection 96(1). Ultimately, the answer to that question is dependent upon the expertise, financial resources, and reputation of the purchaser under the Order. Given that the purchaser may well have the same expertise, financial resources and reputation as CCS, the Tribunal cannot give significant weight to these claimed efficiencies. Indeed, given that the purchaser will have to be approved by the Commissioner, the Tribunal is of the view that all, or virtually all, of these claimed efficiencies are likely to be achieved by that purchaser.

**278** Regardless of the identity of the purchaser, some of the types of qualitative efficiencies identified by Dr. Kahwaty will be achieved, including those related to the Roll-off Bin Business, the reduction of risks related to the transportation of Hazardous Waste over long distances and the increased site remediation that will benefit residents, wildlife, and the overall environment. In fact, to the extent that the Merger is likely to substantially prevent competition, as the Tribunal has found, we conclude that it is entirely appropriate to take into account, in the trade-off assessment, the likelihood that there will be less site clean-up and tipping of Hazardous Waste in Secure Landfills than otherwise would have occurred if an Order were made. This will be described below when non-quantifiable effects are considered.

**279** The Tribunal concludes that the only efficiencies claimed by CCS that are cognizable under section 96 are a maximum of **[CONFIDENTIAL]** in annual overhead efficiencies, having a net present value of approximately **[CONFIDENTIAL]**, using a discount rate of 5.5%.

**280** If, contrary to the Tribunal's conclusion, the Order Implementation Efficiencies are also cognizable under section 96, then it would be appropriate to include in the trade-off assessment further amounts of approximately **[CONFIDENTIAL]** to **[CONFIDENTIAL]** (i.e., one year of transportation cost savings) plus **[CONFIDENTIAL]** (i.e., one year of annual market expansion efficiencies).

**What are the Effects for the Purposes of Section 96 of the Act?**

**281** As CCS noted in its Final Argument, the total surplus approach remains the starting point in assessing the effects contemplated by section 96. Under that approach, the cognizable quantifiable efficiencies will be balanced against the DWL that is likely to result from a merger. In addition, the Tribunal considers any cognizable dynamic or other non-quantifiable efficiencies and *anti-competitive* Effects. Where there is evidence of important dynamic or other non-quantifiable efficiencies and anti-competitive effects, such evidence may be given substantial weight in the Tribunal's trade-off assessment.

**282** After the Tribunal has assessed the evidence with respect to the quantifiable (i.e., DWL) and non-quantifiable *anti-competitive* Effects of the merger, it will assess any evidence that has been tendered with respect to the other effects contemplated by section 96 and the purpose clause in section 1.1 of the Act. It is at this point that the Tribunal's assessment will proceed beyond the total surplus approach. In brief, at this stage of the Tribunal's assessment, it will determine whether there are likely to be any *socially adverse* effects associated with the merger. If so, it will be necessary to determine how to treat the wealth transfer that will be associated with any adverse price effects that are likely to result from the merger. In a merger among sellers of products, that wealth transfer will be

from the merging parties' customers to the merged entity. Of course, to the extent that the merging parties' rivals may be likely to follow such price effects, the wealth transfer would need to be calculated across the sales or purchases of such rivals as well.

**283** The Tribunal expects that in most cases, it will be readily apparent that the wealth transfer should be treated as neutral in its analysis, because the socio-economic profiles of consumers and the merged entity's shareholders will not be sufficiently different to warrant a conclusion that the wealth transfer is likely to lead to *socially adverse* Effects. For greater certainty, the cognizable social Effects under section 96 do not include broader social effects, such as those related to plant-closings and layoffs (*Propane 1*, at para. 444).

**284** In these proceedings, the Commissioner adduced no evidence with respect to *socially adverse* effects. Indeed, in her Final Argument (at para. 208) she conceded that the Merger is not likely to result in any such effects, and that the wealth transfer should be treated as being neutral in this case. Accordingly, the discussion below will be confined to *anti-competitive* effects. In other words, in making its determination under section 96 in the case at bar, the Tribunal will adopt the total surplus approach.

Quantifiable Effects

**285** Quantifiable *anti-competitive* Effects are generally limited to the DWL that is likely to result from a merger.

**286** In this case, the DWL is the future loss to the economy as a whole that will likely result from the fact that purchasers of Secure Landfill services in the Contestable Area will purchase less of those services than they would have purchased had the Tipping Fees for such services declined due to the competition that would likely have materialized between CCS and Babkirk operated as a Full Service Secure Landfill.

**287** The DWL that is likely to result from a merger is likely to be significantly greater when there is significant pre-existing market power than when the pre-merger situation is highly competitive (*Propane 3*, above, at para. 165). In the case at bar, as in *Propane*, the Commissioner did not adduce specific evidence of pre-existing market power, for example, with respect to the extent to which prevailing Tipping Fees exceed competitive levels. Therefore, the Tribunal is not in a position to quantify the impact that any such pre-existing market power likely would have on the extent of the DWL. Where, as in this case, the pre-existing market situation is characterized by a monopoly and the Tribunal is not provided with sufficient persuasive evidence to enable it to quantify the Effects associated with such market power, it will be open to the Tribunal to give qualitative weight to those Effects. Given the very limited nature of the cognizable efficiencies in this case, it has not been necessary for the Tribunal to attribute such a qualitative weighing to those Effects in making its determination under section 96.

**288** As discussed above, CCS submitted that the Tribunal should conclude that there are no quantifiable Effects as a result of the Merger, because the Commissioner did not lead any evidence with respect to such Effects until she served Dr. Baye's reply report, on November 4, 2011. The Tribunal has rejected that position because CCS was not ultimately prejudiced in this regard. The Tribunal will therefore proceed to address the evidence adduced in Dr. Baye's reply report. As will be noted below, the Tribunal is satisfied that CCS would not have met its burden under section 96, even if the quantifiable Effects had been deemed to be zero.

**289** At the outset of his reply report, Dr. Baye summarized a number of the conclusions set forth in his initial report, dated September 30, 2011. These included the following:

a. the Merger likely prevents the prices for the disposal of Hazardous Waste generated in NEBC from falling significantly for many customers;

b. the effects of the Merger are unlikely to be uniform across all customers in the relevant market; and

c. the average reduction in the Tipping Fees throughout NEBC is likely to be at least 10%, but the effects are likely to be significantly higher for customers generating Hazardous Waste in the vicinity

near Babkirk and Silverberry and lower for customers located near the southern and northern boundaries of NEBC.

**290** The Tribunal is satisfied, on a balance of probabilities, that with the exception of the geographic extent of the Effects, the foregoing conclusions are supported by the weight of the evidence that it has found to be credible and persuasive. As to the geographic region over which the aforementioned Effects are likely to result from the Merger, the Tribunal finds that, at a minimum, such Effects are likely to extend throughout the Contestable Area identified by Dr. Kahwaty. Given the conclusions that the Tribunal has reached regarding the minimal nature of the efficiencies claimed by CCS, it is unnecessary to define the scope of the anti-competitive Effects with greater precision.

**291** As Dr. Baye explicitly noted, his conclusions were based on a range of different sources of information and economic analyses, rather than on any specific source of information or economic methodology. Those sources included CCS' internal documents and a "natural experiment." The Tribunal has not placed weight on the economic models that are set forth in Dr. Baye's reports, for example, the tipping fee and DiD regressions presented at exhibits 20 and 26 of his initial Report, which are also briefly discussed in his reply report. In the Tribunal's view, some of the assumptions underlying those models are questionable. The same is true of some of the outcomes of those models, such as the prediction of greater adverse price effects for customers located closer to Northern Rockies than to Babkirk. In the Tribunal's view, those predictions of Dr. Baye's models are counterintuitive and are not supported by the weight of the other evidence adduced in these proceedings.

**292** More generally, as noted above, Dr. Baye's models do not account for the opportunity cost that CCS would incur if it were to lower Tipping Fees to the 20 - 25% range necessary to attract business from customers located farthest away from Silverberry and Babkirk, respectively, as discussed at paragraphs six and seven of his reply report. The Tribunal is not persuaded that it would be in CCS' interest to reduce prices to that extent in the near future, and to thereby deplete its finite Secure Landfill capacity at Silverberry, assuming that CCS would likely be able to attract business at higher Tipping Fees further in the future to fill that capacity.

**293** Notwithstanding the fact that the Tribunal has found the models at exhibits 20 and 26 to be unreliable, we are satisfied, on a balance of probabilities, that competition from an independently owned and operated Full Service Secure Landfill at the Babkirk Site likely would result in CCS reducing its prices by an average of at least 10% for customers in the geographic market described above. This conclusion is based on evidence from CCS' own internal documents, evidence given by **[CONFIDENTIAL]** of **[CONFIDENTIAL]** and the transactions data pertaining to the "natural experiment" at Willesden Green modelled in Dr. Baye's DiD analysis.

**294** The internal CCS documents referenced above include:

a. a slide presentation, dated August 26, 2010, which is attached at Exhibit K to Mr. D. Wallace's witness statement, **[CONFIDENTIAL]**

b. an e-mail, dated July 15, 2010, sent by Trevor Barclay to Ryan Hotston and Lance Kile, **[CONFIDENTIAL]**

c. a document, entitled **[CONFIDENTIAL]**, containing several slides dated "3/9/2009/ **[CONFIDENTIAL]**

d. a financial analysis prepared by Dan Wallace, attached to an e-mail dated March 31, 2010, and at Exhibit C to his witness statement, **[CONFIDENTIAL]**

e. a document dated March 31, 2010, entitled **[CONFIDENTIAL]**, attached at Exhibit D to Dan Wallace's witness statement, **[CONFIDENTIAL]**

f. a document, entitled **[CONFIDENTIAL]**, dated September 15, 2009 and included at Tab 32 of the Parties' Admissions Brief, **[CONFIDENTIAL]**.

**295** Turning to evidence from customers, there was, as mentioned earlier, an unusual paucity of such evidence in

this case. However, Mr. **[CONFIDENTIAL]**, Vice President, Operations, at **[CONFIDENTIAL]** testified that "competition, in our mind, provides a more competitive playing field in terms of your pricing setup" and that "in Northeast B.C. we currently don't have that same level of competition in this facet of our business."

**296** Lastly, the transactions data from the "natural experiment" at Willesden Green, which is found in Dr. Baye's initial report, demonstrates that CCS reduced its prices significantly to seven customers after SES' entry at South Grande Prairie.

**297** For all these reasons, we have concluded that, in the absence of the Merger, competition in the provision of Secure Landfill services at Silverberry and the Babkirk Site likely would have resulted in prices being, on average, at least 10% lower in the geographic market described above. This is a sufficient basis for concluding that the Merger likely will prevent competition substantially, particularly given that the Merger preserves a monopolistic market structure, and thereby prevents the emergence of potentially important competition.

**298** In his reply report, Dr. Baye opined that even if competition is only likely to be substantially prevented in the Contestable Area identified by Dr. Kahwaty, the welfare loss is likely to be significant. Specifically, Dr. Baye estimated that loss to be approximately **[CONFIDENTIAL]** annually. That estimate was based on an assumed price decrease of 10%, from **[CONFIDENTIAL]** to **[CONFIDENTIAL]** per tonne, and certain assumptions and estimates used by Dr. Kahwaty in calculating the market expansion efficiencies, discussed above. In making that calculation, Dr. Kahwaty assumed that the opening of a Secure Landfill facility at Babkirk would likely lead customers to dispose of approximately **[CONFIDENTIAL]** additional tonnes of Hazardous Waste, as forecast in CCS' internal documents. As discussed earlier in these reasons, that forecast increase in demand concerned Legacy Waste and future waste that would not otherwise be transported to Silverberry, due to (i) the level of the current disposal cost (Tipping Fees plus transportation cost) and (ii) the risk that would be associated with transporting Hazardous Waste to Silverberry. Dr. Kahwaty estimated that the total disposal costs of customers located in the Contestable Area that he identified likely would decline by approximately **[CONFIDENTIAL]** per tonne, due to the closer proximity of the Babkirk Facility, relative to Silverberry.

**299** Based on the foregoing numbers used by Dr. Kahwaty to estimate the market expansion efficiencies, and the linear demand that was assumed by Dr. Kahwaty, Dr. Baye estimated that a 10% price reduction (from **[CONFIDENTIAL]** to **[CONFIDENTIAL]**) for customers in the Contestable Area would increase the volume of waste disposed of by those customers from **[CONFIDENTIAL]** tonnes to **[CONFIDENTIAL]** tonnes, annually. He further estimated CCS' unit costs to be approximately **[CONFIDENTIAL]**, based on the average 2010 price at Silverberry of **[CONFIDENTIAL]** across all substances, and the **[CONFIDENTIAL]** landfill margin reported for Silverberry in 2009, which was used by Dr. Kahwaty in estimating the market expansion efficiencies.

**300** Given the foregoing estimates, Dr. Baye calculated the area under the demand curve for the Contestable Area to be (i) a rectangle that is approximately **[CONFIDENTIAL]** tonnes multiplied by **[CONFIDENTIAL]**, for a total of **[CONFIDENTIAL]**, plus (ii) a right triangle that is **[CONFIDENTIAL]** high and **[CONFIDENTIAL]** wide, for an area of **[CONFIDENTIAL]**. Summing (i) plus (ii) yielded a figure of **[CONFIDENTIAL]**. From this latter amount, Dr. Baye deducted CCS' unit cost of **[CONFIDENTIAL]** multiplied by **[CONFIDENTIAL]**, to arrive at an estimated welfare loss of **[CONFIDENTIAL]**.

**301** The Tribunal is persuaded that, on a balance of probabilities, the approach adopted by Dr. Baye, and the numbers he used in reaching his estimate of the likely DWL, are reasonable for the purposes of the Tribunal's assessment of Effects under section 96 of the Act. In the Tribunal's view, the manner in which Dr. Baye proceeded in this regard is sound, and the inputs that he used are reliable and conservative. The fact that Dr. Baye relied on certain assumptions made by Dr. Kahwaty is not particularly important for the purposes of the Tribunal's assessment under section 96. What is important is that there is reliable evidence before the Tribunal that permitted the DWL to be estimated.

**302** The Tribunal acknowledges Dr. Kahwaty's testimony that, to calculate the DWL, it is necessary to know the shape of the demand curve, and that, when prices are likely to differ across customers, it is necessary to have

customer-specific elasticity data. However, the Tribunal is persuaded that, in the absence of such information, a reliable "rough" estimate of the likely DWL can be obtained based on information such as that which was used by Dr. Baye in reaching his estimated annual welfare loss of approximately **[CONFIDENTIAL]**.

**303** Accordingly, the Tribunal accepts Dr. Baye's estimate of **[CONFIDENTIAL]**, as being the minimum annual DWL.

**304** Dr. Baye then speculated that, (i) if the average price decrease in that area was 21 percent, the annual DWL would be approximately **[CONFIDENTIAL]**, (ii) if prices across all Hazardous Waste tipped at Silverberry in 2010 decreased by 10%, the DWL would be approximately **[CONFIDENTIAL]**, and (iii) if prices across all such waste decreased by 21%, the DWL would be approximately **[CONFIDENTIAL]**. However, the Tribunal is not persuaded that these speculations about prices are reasonable.

Non-quantifiable Effects

**305** The Tribunal is satisfied that the Merger likely would result in certain important qualitative or other non-quantifiable Effects.

**306** In his initial report, Dr. Baye identified at least two important qualitative anti-competitive Effects of the Merger. First, at paragraph 157, he stated that lower Tipping Fees would induce waste generators to more actively clean up legacy sites in NEBC. At paragraph 91 of his report, he described this in terms of lower Tipping Fees inducing waste generators to substitute away from "delay," or bioremediation, towards disposal at a Secure Landfill. As Dr. Kahwaty noted at paragraph 96 of his Efficiencies Report, increased site remediation from lower disposal costs benefits "area residents, wildlife, and the overall environment."

**307** Second, at paragraph 137(c) of his initial report, Dr. Baye stated that, to retain its waste volumes in the face of competition from an independently owned and operated Babkirk Facility, CCS "would have had an incentive to compete through 'value propositions' that, among other things, link prices on various services to provide customers with a lower total cost for waste services." Although the services in question were not further discussed by Dr. Baye, they were addressed in "read-in" evidence adduced by the Commissioner and cited by Dr. Baye (at footnote 93 of his initial report). The Tribunal is satisfied, on a balance of probabilities, that competition between CCS and an independently owned and operated Babkirk Facility would have led to important non-price benefits to waste generators in the form of various "value propositions" that include either existing services being provided at lower prices, or new or enhanced services being provided that likely would not otherwise be provided if the Order is not made.

**Are the Cognizable Efficiencies Greater than and do they Offset the Effects?**

**308** Section 96 requires the Tribunal to determine whether the cognizable efficiencies "will be greater than, and will offset" the cognizable effects of any prevention or lessening of competition that will result or is likely to result from a merger.

**309** The Tribunal considers that the terms "greater than" and "offset" each contemplate both quantifiable and non-quantifiable (i.e., qualitative) efficiencies. In the Tribunal's view, "greater than" connotes that the efficiencies must be of larger magnitude, or more extensive than, the effects referred to in section 96. This contemplates a balancing of commensurables, even if some of the efficiencies being balanced are not capable of accurate or rough quantification. By contrast, the term "offset" is broad enough to connote a balancing of incommensurables (e.g., apples and oranges) that requires the exercise of subjective judgment to determine whether the efficiencies compensate for the likely effects referred to in section 96.

**310** In the case at bar, the Tribunal has found that the cognizable, quantifiable, efficiencies likely to result from the Merger will be a maximum of **[CONFIDENTIAL]** annually. Those are the overhead efficiencies estimated by Dr. Kahwaty. In addition, the Tribunal has found that CCS has not demonstrated, on a balance of probabilities, that the

qualitative efficiencies it has claimed are cognizable. In other words, it has not demonstrated that those efficiencies would not likely be attained if the Order were made.

**311** On the other hand, the Tribunal has found that the quantifiable Effects are likely to be at least **[CONFIDENTIAL]** annually. That is the value of the minimum DWL associated with the Contestable Area.

**312** Based on these findings, it is readily apparent that CCS has not demonstrated that the cognizable, *quantifiable*, efficiencies likely to be brought about by the Merger will likely be "greater than" the *quantifiable* Effects that are likely to result from the Merger. Using a 5.5% discount rate, CCS estimated that the present value of these (overhead) efficiencies to be approximately **[CONFIDENTIAL]**, in comparison with a present value of **[CONFIDENTIAL]** for the aforementioned Effects.

**313** Given the Tribunal's conclusion that the Merger would result in a number of important qualitative or other non-quantifiable effects, and that it would not likely bring about significant qualitative, cognizable, efficiencies, it is also readily apparent that the combined quantitative and qualitative efficiencies are not likely to be "greater than" the combined quantitative and qualitative Effects.

**314** In addition, the Tribunal is persuaded, on a balance of probabilities, that even if a zero weighting is given to the *quantifiable* Effects, as CCS submitted should be done, CCS has not satisfied the "offset" element of section 96. In short, the Tribunal is satisfied that the very minor *quantitative* efficiencies, (**[CONFIDENTIAL]** annually) that are cognizable, together with any qualitative or other non-quantifiable efficiencies that may be cognizable, would not "offset" the significant qualitative Effects that it has found are likely to result from the Merger.

**315** This conclusion would remain the same even if the Tribunal were to accept and give full weight to the Order Implementation Efficiencies, which only amount to a maximum of **[CONFIDENTIAL]** (which represents one year of transportation cost savings) plus **[CONFIDENTIAL]** (which represents one year of annual market expansion efficiencies).

**316** This is because, in the Tribunal's view, the qualitative Effects, when taken together merit substantial weight. That weight is greater than the weight attributable to the aggregate of the cognizable quantitative and qualitative efficiencies under any reasonable approach. In brief, those qualitative Effects are (i) reduced site clean-up and the benefits that such remediation would confer upon "area residents, wildlife, and the overall environment"; and, more importantly, (ii) reduced "value propositions" than would likely otherwise emerge in the relevant market, linking prices to various new or enhanced services.

**317** Most importantly, in the absence of the Order, the Merger will maintain a monopolistic structure in the relevant market. In other words, the Merger will not only give rise to the qualitative effects summarized immediately above, but it will also preclude benefits of competition that will arise in ways that will defy prediction.

**318** In summary, the Tribunal is satisfied that CCS has not met its burden to establish, on a balance of probabilities, the "greater than" or "offset" elements set forth in section 96.

## ISSUE 9 WHAT IS THE APPROPRIATE REMEDY - DISSOLUTION OR DIVESTITURE?

**319** An important question under this heading is whether SES is currently a willing purchaser for the Babkirk Site. Surprisingly, when Mr. Amirault of SES testified for the Commissioner, neither her counsel during questioning in chief nor counsel for the Vendors during cross-examination asked Mr. Amirault if SES is still interested in acquiring BLS.

**320** The Commissioner's position is that, once she showed that dissolution was an effective and available remedy,

the burden of proof shifted to the Vendors to demonstrate that divestiture was an available, effective and less intrusive remedy. The Commissioner maintains that the Vendors were obliged to ask Mr. Amirault if SES is still interested and, because they failed to ask that question and because they failed to lead any evidence about other prospective purchasers, they have no basis to argue that divestiture will be an effective remedy.

**321** The Tribunal does not accept the Commissioner's characterization of the onus. In the Tribunal's view, if the Commissioner proposes alternative remedies, as she did in this case, she bears the onus of showing that, although one may be preferable, each is available and effective. Accordingly, the Commissioner's counsel should have asked Mr. Amirault about SES' interest in purchasing the shares of BLS.

**322** The Tribunal notes that, in her written final argument, the Commissioner asks the Tribunal not to infer that SES is an interested purchaser. However, in contrast, in final oral argument, counsel for the Commissioner suggested that SES is an interested buyer.

**323** The Tribunal accepts the latter submission and has determined, for the following reasons, that SES is likely to make an offer to purchase the Babkirk Facility at some point during the divestiture process under the Order:

* SES has already decided to operate a Secure Landfill in NEBC. It tried unsuccessfully and at considerate expense to secure the Authorizations at its Heritage Site;
* Babkirk already has the necessary Authorizations and SES is confident that its plans to expand the permitted capacity at Babkirk and upgrade the cell design will be approved;
* SES has demonstrated an active and continuing interest in the Babkirk Facility since the Merger. Among other things, this is demonstrated by SES' lawyers' written submissions to the Commissioner and by the participation of its CEO, Mr. Amirault, as a witness in these proceedings.

**324** We now turn to the proposed remedies.

**325** The Commissioner wants the Babkirk Site operated as a competitive Full Service Secure Landfill and she believes that dissolution will produce this result more quickly than divestiture.

**326** Her submission is that, once the Vendors again hold the shares of Complete and have repaid CCS the purchase price, they will be highly motivated to resell Complete or the shares of BLS because this will enable them to recover their funds as soon as possible. However, this submission assumes that the Vendors will immediately be offered a price they are prepared to accept. In the Tribunal's view, there is no basis for this assumption. The evidence is clear that the Vendors have never been willing to be pushed into a quick sale.

**327** The Commissioner's submission also assumes that the Vendors will have an incentive to sell quickly because they will be short of funds as a result of having to repay CCS as soon as the shares of Complete are returned to them. This assumption is also questionable, in part because it appears that CCS has indemnified the Vendors against all claims arising from any investigation or actions by the Bureau with respect to the Merger. Given this background, it is possible that CCS may not insist on immediate payment.

**328** Even if the Commissioner is correct and the Vendors are cash-strapped and anxious to resell BLS or Complete, the Tribunal still anticipates that they will want an attractive price. It is also important to remember that all five individual Vendors must agree to accept an offer and they will not necessarily be like-minded, in part because some are near retirement and others are in mid-career.

**329** The Tribunal notes that two years will have passed since the Babkirk Facility was last for sale. This means that purchasers, other than SES, may show interest, especially given the increasing rate of gas production in the area northwest of Babkirk. Dr. Baye testified that he thought SES, Newalta and Clean Harbours were potential purchasers. As well, it is not unreasonable to think that an oil and gas producer may decide to own and operate a

Secure Landfill. The Tribunal heard evidence that **[CONFIDENTIAL]** is considering becoming a part-owner of the Secure Landfill at Peejay. If the Vendors receive multiple offers, protracted negotiations may follow.

**330** Finally, if they do not receive an offer they consider attractive, the Vendors are free to change their minds and resurrect their plan to operate a bioremediation facility with an Incidental Secure Landfill. This would not result in the competition the Commissioner seeks because it will only be realized if the Babkirk Facility operates as a Full Service Secure Landfill.

**331** There is also the question of whether a purchaser after dissolution will be an effective competitor. In the proposed order for dissolution found at the conclusion of the Commissioner's final argument, she does not seek the right to approve a purchaser and she only asks for notice of a future merger if it is "among the Respondents". In our view, this makes dissolution a less effective remedy.

**332** Given all these observations, the Tribunal is concerned that dissolution may not be effective in that it may not lead to a prompt sale and a timely opening of the Babkirk Facility as a Secure Landfill.

**333** It is also the case that dissolution is the more intrusive remedy.

**334** Three of the Vendors testified about the financial hardship they would face if dissolution were ordered by the Tribunal. Ken Watson's share of the proceeds of the transaction was **[CONFIDENTIAL]**. He testified that if ordered to return the proceeds to CCS, **[CONFIDENTIAL]**, he expects to face significant financial hardship.

**335** Randy Wolsey's share of the proceeds was approximately **[CONFIDENTIAL]**. He testified that almost half of the proceeds have been used to develop a property on which he is constructing a new family home. The balance has been invested in the purchase of various investment products. According to Mr. Wolsey, he expects to lose approximately **[CONFIDENTIAL]** if he is forced to make a quick sale on the residential property before the house under construction has been completed.

**336** Karen Baker testified that if required to return her share of the proceeds, approximately **[CONFIDENTIAL]**, then her ability to continue to provide financial support to certain small business will be compromised. She also indicated that if the transactions were to be dissolved, she expects that the "work required to reverse the sale and calculate the adjustments required to account for changes in Complete's assets, working capital and lost opportunity costs, as well as the opportunity costs in time away from the other businesses in which [she is] involved, and cost to some of those businesses for replacement personnel to do the work that [she] should be doing, would cause [her] significant stress and emotional hardship."

**337** The Commissioner asserts that, in the particular circumstances of this case, hardship is irrelevant, because she warned the Vendors that she would seek dissolution before they sold Complete to CCS. However, in the Tribunal's view it is the right of private parties to disagree with the Commissioner and make their case before the Tribunal. Accordingly, they are not estopped from raising issues of hardship.

**338** The Tribunal is also of the view that dissolution is overbroad, since it involves Complete's other businesses and not just BLS.

**339** In the spring of 2007, Complete acquired the assets of a municipal waste management business based in Dawson Creek, British Columbia. As noted earlier, those assets included contracts for the management of the Fort St. John and Bessborough municipal landfills and the Dawson Creek Transfer Station, the supply and hauling of roll-off bins, and the provision of rural refuse collections and transfer services. At the time of the Merger, those contracts and related equipment were transferred to CCS. Hazco has been responsible for this business since then.

**340** Mr. Garry Smith, the president of Hazco, testified that Hazco has upgraded Complete's trucks and has sold some older equipment which it considered surplus. The two municipal landfill contracts have been extended and are now held directly by Hazco. Complete's employees are now employed by Hazco and there have been

personnel changes. At the hearing, Mrs. Baker testified about the impact of the sale of some of the assets. She stated:

> Now, that equipment was older equipment. It wouldn't have brought big money, but the point is it was sufficient for us to do the work that we wanted it to do. Well, now the oil and gas industry is hot, hot up there. Trying to get equipment back, we certainly wouldn't get that equipment back. Any decent used equipment, I have no idea. The prices would be through the roof. Would we buy new equipment? I don't know. So right now, we don't even have the equipment to go back to work.

**341** To conclude, the Tribunal has decided that dissolution is intrusive, overbroad and will not necessarily lead to a timely opening of the Babkirk Facility as a Full Service Secure Landfill.

**342** Turning to divestiture, the Tribunal finds that it is an available and effective remedy. If reasonable but tight timelines are imposed, it will not matter if, as the Commissioner alleges, SES and CCS are reluctant to negotiate because of their outstanding litigation. In the end, if they cannot agree, a trustee will sell the shares or assets of BLS, either to SES or another purchaser approved by the Commissioner. In other words, divestiture will be effective.

**343** A divestiture with tight timelines has other advantages. The Commissioner will have the right to pre-approve the purchaser, the person responsible for effecting the divestiture will ultimately be CCS or a professional trustee, rather than five individuals, the timing will be certain, a sale will ultimately occur and the approved purchaser will compete with Silverberry on a Full Service basis.

**344** For all these reasons, the Tribunal will order CCS to divest the shares or assets of BLS.

**H. COSTS**

**345** The Commissioner chose dissolution as her preferred remedy when she commenced the Application. She made this choice because she believed that at the time of the Merger, the Vendors were about to construct and operate a Full Service Secure Landfill. For this reason she concluded that the most timely way to introduce competition was to return Babkirk to the Vendors.

**346** However, for the reasons given above, the Tribunal has concluded that the Vendors did not intend to operate a Full Service Secure Landfill. This means that the Commissioner has failed to prove the premise which caused her to name the individual Vendors as parties to the Application. In essence she failed to prove her case against them and for this reasons she is liable for their costs.

**347** However, during the Vendors' motion for summary disposition which was heard two weeks before the hearing, they indicated that, if the motion was successful and they were removed as parties, four of them would nevertheless attend the hearing to give evidence. The Tribunal assumes that, had done so, they would have been represented by one counsel. Accordingly, the Commissioner is to pay their costs less the legal fees which would have been incurred had they appeared as witnesses.

**I. FOR THESE REASONS THE TRIBUNAL ORDERS THAT:**

**348** CCS is to divest the shares or assets of BLS on or before December 28, 2012 failing which a trustee is to effect a sale on or before March 31, 2013. If possible, the terms for this process are to be agreed between the Commissioner and CCS and are to be submitted to the Tribunal on or before June 22, 2012. If the agreed terms are accepted by the Tribunal, they will be incorporated in a further order to be called the Divestiture Procedure Order. If the Commissioner and CCS cannot agree to terms, each party is to submit a proposed Divestiture Procedure Order on or before June 29, 2012. If necessary, the Tribunal will hear submissions about each party's proposal in early July and then make the Divestiture Procedure Order.

**349** CCS is to pay the Commissioner's costs and, because dissolution was not ordered, the Commissioner is to pay the Vendors' costs less the fees they would have paid for legal representation if they had attended as non-parties to give their evidence. The Commissioner is to prepare a bill of costs to be submitted to CCS and the Vendors are to submit a bill of costs to the Commissioner both on or before August 31, 2012. Both are to be prepared in accordance with Federal Court Tariff B at the mid-point of column 3. If by September 14, 2011 no agreement is reached about lump sums to be paid, the Tribunal will hear submissions and fix the awards of costs.

DATED at Ottawa, this 29th day of May, 2012.

SIGNED on behalf of the Tribunal by the Panel Members.

(s) Sandra J. Simpson J. (Chairperson)

(s) Paul Crampton C.J.

(s) Dr. Wiktor Askanas

**J. THE SCHEDULES**

**350** The schedules appear on the following pages:

Schedule A: Map Showing Secure Landfills (based on Exhibit 4-A to Dr. Baye's Expert Report)


Source: CCS, SES, and Newalta company websites.

This map may be printed in colour.

**SCHEDULE "B"**

**THE EVIDENCE**

**Witnesses who gave oral testimony**

**(in alphabetical order)**

**For the Commissioner of Competition**

* **Rene Amirault**

  President & CEO of Secure Energy Services Inc.

* **Robert Andrews**

  Section Head-Environmental Management, Government Unit in the British Columbia Ministry of the Environment.

* **Michael Baye**

  Expert Economist - Special Consultant at National Economic Research Associates, Inc. and the Bert Elwert Professor of Business Economics and Public Policy at the Indiana University Kelley School of Business.

* **Chris Hamilton**

  Project Assessment Director at the British Columbia Environmental Assessment Office.

* **Andrew Harrington**

  Expert on Efficiencies - Managing director of the Toronto office of Duff & Phelps.

* **[CONFIDENTIAL]**

  Contracting and Procurement Analyst for the **[CONFIDENTIAL]**.

* **[CONFIDENTIAL]**

  Vice-President, Operations at **[CONFIDENTIAL]**.

* **Mark Polet**

  Associate at Klohn Crippen Berger Ltd. ("KCB"). KCB is a private, specialized engineering and environmental consulting firm with its head office in Vancouver.

* **Del Reinheimer**

  Environmental Management Officer in the Environmental Protection Division at the British Columbia Ministry of the Environment.

* **Devin Scheck**

  Director, Waste Management & Reclamation at the British Columbia Oil and Gas Commission.

**For the Vendors**

* **Karen Baker**

  One of the founding shareholders of Complete Environmental Inc.

* **Ronald Baker**

  One of the founding shareholders of Complete Environmental Inc.

* **Kenneth Watson**

  One of the founding shareholders of Complete Environmental Inc.

* **Randy Wolsey**

One of the founding shareholders of Complete Environmental Inc.

**For the Corporate Respondents**

* **Trevor Barclay**

  Landfill Manager of the Northern Rockies Secure Landfill.

* **James Coughlan**

  Director of Sales and Marketing of CCS Corporation

* **Henry Kahwaty**

  Expert economist - Director with Berkeley Research Group, LLC.

* **Richard Lane**

  Vice-President of CCS Midstream Services, a division of CCS Corporation.

* **Pete Marshall**

  Principal of Adelantar Consulting, an environmental consultancy based in Edmonton, Alberta.

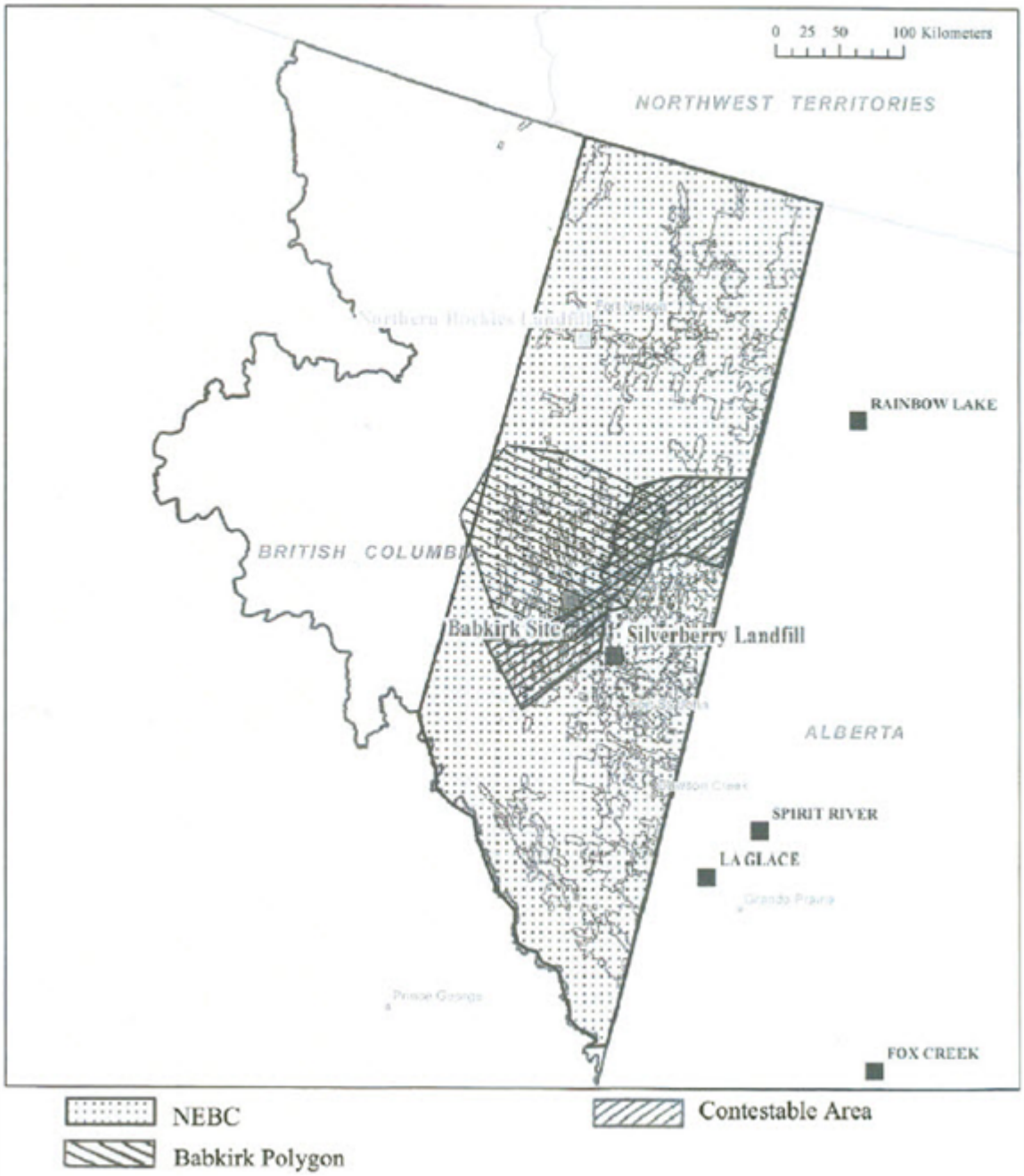
* **Daniel Wallace**

  Manager, Business Development of CCS Corporation's Midstream Services division

**Other Evidence**

* The witness statements from those who testified.
* Read-ins from Examinations for Discovery of Karen Baker and Kenneth Watson for the Vendors, Daniel Wallace for the Corporate Respondents and Trevor MacKay for the Commissioner of Competition
* The statement of agreed facts.
* The witness statements of **Robert Coutts**, President of SkyBase Geomatic Solutions Inc. and **Garry Smith**, President of Hazco Waste Management (owned by CCS). On consent these witnesses were not called to give oral testimony.
* A Joint list of agreed documents.
* The exhibits marked during the hearing.

Schedule C: Map of NEBC, the Contestable Area and the Babkirk Polygon




**K. CONCURRING REASONS BY P. CRAMPTON C.J.**

**351** Although I participated in the writing of, and signed, the Panel's decision in this case, I would like to comment on certain additional matters.

**A. IS CCS'S ACQUISITION OF COMPLETE A MERGER?**

**352** At paragraph 56 of the Panel's reasons, it is noted that it was not necessary to decide whether Complete's Roll-off Bin Business or its management of municipal dumps could be a business for the purposes of section 91 of

the Act. That said, the conclusion reached by the Chairperson on this point was articulated at paragraph 57. That conclusion was stated as follows:

> "[A] business being acquired in a merger must have some relevance to a Commissioner's application. In other words, it must have the potential to impact competition in the markets at issue. This observation means that, in this case, Complete's Roll-off Bin Business and its management of municipal dumps would not have been caught by the definition in section 91 because they are not involved in any way in the disposal or treatment of Hazardous Waste."

**353** I respectfully disagree. In my view, the term "business", as contemplated by section 91 of the Act, is not, as the Vendors maintained, confined to a business that competes with a business of an acquiring party. There is no such limitation in section 91 or in the definition of the term "business" that is set forth in subsection 2(1) of the Act.

**354** The Vendors attempted to support their position by noting that section 92 of the Act requires that a "merger" prevent or lessen, or be likely to prevent or lessen, competition substantially. However, it is not necessary for a merger to involve two or more competing businesses to have the potential to prevent or lessen competition substantially. For example, the inclusion of the terms "supplier" and "customer" in section 91 reflects Parliament's implicit recognition that a vertical merger may have such an effect. The words "or other person" in section 91 reflect that Parliament also did not wish to exclude the possibility that other types of non-horizontal mergers may also have such an effect.

**355** Considering the foregoing, I am not persuaded that the Vendors' position is assisted by reading the words of section 91 "in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament" (E. A. Driedger, *Construction of Statutes* (2nd ed. 1983), at p. 87, quoted in *Rizzo & Rizzo Shoes Ltd. (Re)*, *[1998] 1 S.C.R. 27*, at 41; and *Canada (Canadian Human Rights Commission) v. Canada (Attorney General)*, *2011 SCC 53*, at para. 33 ("*Mowat*")). In the absence of any apparent ambiguity, one must adopt an interpretation of section 91 "which respects the words chosen by Parliament" (*Mowat*, above). The principle that the Act be given "such fair, large and liberal construction and interpretation as best ensures the attainment of its objects" also supports the view that section 91 ought not be read in the limited manner suggested by the Vendors (*Interpretation Act*, *R.S.C. 1985, c. I-21, s. 12*).

**356** Indeed, if anything, a reading of section 91 in a manner that is harmonious with the scheme and object of the Act and the intention of Parliament arguably further supports interpreting section 91 in a way that does not require the type of assessment of competitive effects that is contemplated by the interpretation advanced by the Vendors. That is to say, when viewed in the context of the scheme and object of the Act as a whole, it is arguable that section 91 was intended by Parliament to be a gating provision, in respect of which an assessment ordinarily is to be made relatively early on in the evaluation contemplated by sections 92 and 93.

**357** For example, all but one of the assessment factors in the non-exhaustive list that is set forth in section 93 refer to the "merger or proposed merger" in respect of which an application under section 92 has been made. In my view, this suggests that the merger or proposed merger in question should be identified before the assessment contemplated by sections 92 and 93 is conducted.

**358** If an agreement, arrangement or practice cannot properly be characterized as a merger, it will fall to be investigated under another provision of the Act, such as section 45, section 79, or section 90.1, each of which has a substantive framework which differs in important respects from the framework set forth in section 92. Indeed, in the case of agreements or arrangements that may be investigated under section 45, which is a criminal provision, there are important procedural implications associated with the decision to pursue a matter under that section, versus under section 90.1, 79 or 92. I recognize that there may be cases in which it may be appropriate to assess a matter under section 92 as well as under one or more of the other provisions mentioned immediately above, for a period of time before an election is made under section 98, 45.1, 79(7) or 90.1(10). However, the scheme of the Act and the interests of administrative efficiency arguably support the view that a determination as to whether a matter ought to be investigated as a merger, rather than a type of conduct addressed elsewhere in the Act, ordinarily should be

made before the central substantive determinations under the applicable section of the Act are made. Among other things, such substantive determinations often take several months, and sometimes take much longer, to make.

**359** In summary, for all of the foregoing reasons, I have concluded that the term "business" in section 91 is sufficiently broad to include any business in respect of which there is an acquisition or establishment of control or a significant interest, as contemplated therein. In the case at bar, this would include Complete's Roll-off Bin Business, which was fully operational at the time of Complete's acquisition by CCS. It would also include Complete's management of municipal dumps.

### B. MARKET DEFINITION

**360** Market definition has traditionally been a central part of merger analysis in Canada and abroad for several reasons. These include (i) helping to focus the assessment on products and locations that are close substitutes for the products and locations of the merging parties, (ii) helping to focus the assessment on the central issue of market power, (iii) helping to identify the merging parties' competitors, (iv) helping to understand the basis for existing levels of price and non-price competition, and (v) facilitating the calculation of market shares and concentration levels. In turn, changes in market shares and concentration levels can be very helpful, albeit not determinative, in understanding the likely competitive effects of mergers and in assisting enforcement agencies to triage cases and to provide guidance to the public.

**361** In recent years, developments in antitrust economics have reached the point that the United States Department of Justice and Federal Trade Commission have begun to embrace approaches that "need not rely on market definition" (*Horizontal Merger Guidelines* (August 19, 2010), at s. 6.1). Likewise, the MEGs, at paragraph 3.1, have been amended to stipulate that market definition is not necessarily a required step in the Commissioner's assessment of a merger.

**362** These developments can be accommodated within the existing framework of the Act and the Tribunal's jurisprudence.

**363** In discussing market definition, the Panel noted, at paragraph 92 of its reasons, that the Tribunal has in the past cautioned against losing sight of the ultimate inquiry, which is whether the merger being assessed prevents or lessens, or is likely to prevent or lessen, competition substantially. The Tribunal has also previously noted that the Act does not require that a relevant market be defined in assessing whether competition is likely to be prevented or lessened substantially (*Propane 1*, above, at para. 56). The logical implication is that defining a relevant market is not a necessary step in assessing whether a merger prevents or lessens, or is likely to prevent or lessen, competition substantially. Accordingly, it will be open to the Tribunal, in an appropriate case, to make this assessment without defining a relevant market.

**364** That said, at this point in time, it is anticipated that such cases will be exceptional. Indeed, failing to define a relevant market may make it very difficult to calculate, or even to reasonably estimate, the actual or likely DWL associated with a merger, for the purposes of the efficiencies defence in section 96 of the Act.

### C. THE ANALYTICAL FRAMEWORK IN A "PREVENT" CASE

**365** At the outset of the Commissioner's final oral argument, her counsel urged the Tribunal to clarify the analytical approach applicable to three areas, namely, (i) the assessment of whether a merger prevents, or is likely to prevent, competition substantially, (ii) the efficiencies defence, and (iii) the circumstances in which the Tribunal will entertain the remedy of dissolution, and what factors will be taken into account in determining the appropriate remedy in any particular case.

**366** These topics are all addressed to some extent in the Panel's decision. I would simply like to add some additional comments, particularly with respect to the analytical framework applicable to the Tribunal's assessment of whether a merger prevents, or is likely to prevent, competition substantially.

**367** The Tribunal's general focus in assessing cases brought under the "substantial prevention of competition" and "substantial lessening of competition" branches of section 92 is essentially the same. In brief, that focus is upon whether the merged entity is likely to be able to exercise materially greater market power than in the absence of the merger. The same is true with respect to other sections of the Act that contain these words.

**368** In determining whether competition is likely to be *lessened*, the more particular focus of the assessment is upon whether the merger is likely to facilitate the exercise of new or increased market power by the merged entity, acting alone or interdependently with one or more rivals. In determining whether competition is likely to be *prevented*, that more particular focus is upon whether the merger is likely to preserve the existing market power of one or both of the merging parties, by preventing the erosion of such market power that otherwise likely would have taken place if the merger did not occur.

**369** In making its assessment in the latter context, and with respect to a proposed merger, the Tribunal compares (i) the state of competition that would likely exist if the merger were to proceed, with (ii) the state of competition that would likely exist if the merger did not proceed. Scenario (ii) typically is referred to as the "but for", or "counterfactual", scenario. In the case of a completed merger, that "but for" scenario is the market situation that would have been most likely to emerge had the merger not occurred.

**370** When the Tribunal determines that a merger is not likely to enable the merged entity to exercise greater market power than in the absence of the merger, the Tribunal generally will conclude that the merger is not likely to prevent or lessen competition at all, let alone substantially. With respect to allegations that competition is likely to be *lessened*, this conclusion generally will flow from a finding that the merger is not likely to enable the merged entity to *enhance existing, or to create new,* market power. With respect to allegations that competition is likely to be *prevented*, this conclusion generally will flow from a finding that the merger in question is not likely to enable the merged entity to *maintain* greater existing market power than in the absence of the merger. Once again, the foregoing also applies with respect to other sections of the Act that contain the "prevent or lessen competition substantially" test.

**371** With respect to sellers, market power is the ability to profitably maintain prices above the competitive level, or to reduce levels of non-price competition (such as service, quality or innovation), for an economically meaningful period of time. With respect to purchasers, market power is the ability to profitably depress prices below the competitive level, or to reduce levels of non-price competition, for such a period of time.

**372** In assessing whether market power is likely to be created, enhanced or maintained by a merger or a reviewable trade practice, the Tribunal assesses the intensity of competition, as reflected in its price and non-price dimensions. Competition is a dynamic, *rivalrous process* through which the exercise of market power is prevented or constrained as firms strive, among other things, to develop, produce, distribute, market and ultimately sell their products in rivalry with other firms. That rivalrous process generates the principal source of pressure on firms to innovate new or better products or business methods, and to deliver those products at competitive prices. In turn, those innovations and competitive prices serve to increase aggregate economic welfare in the economy, the economy's international competitiveness and the average standard of living of people in the economy.

**373** In assessing the intensity of price competition, the Tribunal focuses upon whether prices are likely to be higher than in the absence of the merger. In assessing the intensity of non-price competition, the Tribunal focuses upon whether levels of service, quality, innovation, or other important non-price dimensions of competition are likely to be lower than in the absence of the merger. This focus ensures that the assessment of the intensity of price and non-price dimensions of competition is *relative*, rather than *absolute*, in nature (*Canada Pipe*, above, at paras. 36 - 38). In short, the assessment of levels of price and non-price competition is made relative to the levels of price and non-price competition that likely would exist "but for" the merger. The same approach is taken with respect to non-merger matters that require an assessment of whether competition is likely to be prevented or lessened substantially.

**374** Competition may be said to be *prevented* when future competition is hindered or impeded from developing. Common examples of such prevention of competition in the merger context include (i) the acquisition of a potential or recent entrant that was likely to expand or to become a meaningful competitor in the relevant market, (ii) an acquisition of an incumbent firm by a potential entrant that otherwise likely would have entered the relevant market *de novo*, and (iii) an acquisition that prevents what otherwise would have been the likely emergence of an important source of competition from an existing or future rival.

**375** In determining whether a prevention or lessening of competition is likely to be *substantial*, the Tribunal typically will assess the likely magnitude, scope and duration of any adverse effects on prices or on non-price levels of competition that it may find are likely to result from the creation, enhancement or maintenance of the merged entity's market power. That is to say, the Tribunal assesses the likely degree of such price and non-price effects, the extent of sales within the relevant market in respect of which such effects are likely to be manifested, and the period of time over which such effects are likely to be sustained.

**376** With respect to magnitude or degree, the Tribunal has previously defined substantiality in terms of whether customers are "likely to be faced with *significantly* higher prices or *significantly* less choice over a *significant* period of time than they would be likely to experience in the absence of the acquisitions" (*Southam,* above, at 285, emphasis added). However, given that the Tribunal has now embraced the hypothetical monopolist framework and the SSNIP test for market definition, it is necessary to revisit this definition of substantiality. This is because if the degree of market power used to define relevant markets is the same as the degree of market power used to assess competitive effects, a merger would not be found to be likely to prevent or lessen competition substantially unless the degree of new, enhanced or maintained market power of the merged entity is the same degree of market power held by as the hypothetical monopolist that was conceptualized for the purposes of market definition.

**377** Accordingly, the degree of market power used in assessing whether competition is likely to be prevented or lessened substantially must be recalibrated downwards. That recalibrated degree of market power is a level of market power required to maintain prices *materially* higher, or to depress one or more forms of non-price competition to a level that is *materially* lower, than they likely would be in the absence of the merger. As a practical matter, in the case at bar, this distinction between "material" and "significant" is of little significance, because the Panel has found that prices are likely to be significantly (i.e., at least 10%) higher than they would likely have been in the absence of the Merger.

**378** Turning to the scope dimension of "substantiality", the Tribunal will assess whether the merged entity, acting alone or interdependently with other firms, likely would have the ability to impose the above-mentioned effects in a material part of the relevant market, or in a respect of a material volume of sales.

**379** With respect to the duration dimension of "substantiality", the Tribunal typically will assess whether the merged entity, acting alone or interdependently with other firms, likely would have the ability to sustain the above-mentioned effects for approximately two years or more, relative to the "but for" scenario. This explains why the Tribunal typically assesses future entry and the expansion of potential rivals to the merged entity by reference to a benchmark of approximately two years.

**380** When, as in this case, the merger has already occurred and the Commissioner alleges that the merger is likely to prevent competition substantially, the Tribunal's assessment of the duration dimension of "substantiality" will focus on two things. First, the Tribunal will assess whether the entry or expansion that was prevented or forestalled by the merger likely would have been sufficiently timely, and on a sufficient scale, to have resulted in a material reduction of prices, or a material increase in one or more non-price dimensions of competition, had the merger not occurred. If so, the Tribunal will assess whether the entry or expansion of third parties likely will achieve this result, notwithstanding the fact that the merger has occurred.

**381** Before assessing whether a likely prevention of future competition would be "substantial," the Tribunal also will assess whether that future competition likely would have materialized "but for" the merger in question. In this

regard, the Tribunal will assess whether such competition likely would have developed within a reasonable period of time.

**382** What constitutes a reasonable period of time will vary from case to case and will depend on the business under consideration. In situations where steps towards entry or expansion were being taken by the firm whose entry or expansion was prevented or forestalled by the merger, a reasonable period of time would be somewhere in the range of time that typically is required to complete the remaining steps to enter or expand on the scale described above. Similarly, in situations where the entry or expansion was simply in the planning stage, a reasonable period of time would be somewhere in the range of time that typically is required to complete the plans in question and then to complete the steps required to enter or expand on the scale described above. In situations where entry on such a scale cannot occur for several years because, for example, a new blockbuster drug is still in clinical trials, a reasonable period of time would be approximately the period of time that it typically would take for such trials to be completed, relevant regulatory approvals obtained, and commercial quantities of the drug produced and sold. In situations where entry on the scale described above cannot occur for several years because of long term contracts between customers and suppliers, a reasonable period of time would be approximately one year after a volume of business that is sufficient to permit entry or expansion on that scale becomes available.

**383** In all cases, the Tribunal must be satisfied that the future competition that is alleged to be prevented by the merger likely would have materialized within a reasonable period of time. If so, the Tribunal will assess whether the prevention of that competition likely would enable the merged entity to exercise materially greater market power than in the absence of the merger, for a period of approximately two years or more, subsequent to that time.

**384** Notwithstanding the foregoing, it is important to underscore that the magnitude, scope and duration dimensions of "substantiality" are interrelated. This means that where the merged entity is likely to have the ability to prevent a particularly large price decrease that likely would occur "but for" the merger, the volume of sales in respect of which the price decrease would have had to be experienced before it will be found to be "material" may be less than would otherwise be the case. The same is true with respect to the period of time in respect of which the likely adverse price effects must be experienced - it may be less than the two year period that typically is used. Likewise, where the volume of sales in respect of which a price decrease is likely to occur is particularly large, (i) the degree of price decrease required to meet the "materiality" threshold may be less than would otherwise be the case, and (ii) the period of time required for a prevention of competition to be considered to be "substantial" may be less than two years.

**385** In conducting its assessment of whether a merger is likely to prevent competition substantially, the Tribunal also assesses whether other firms likely would enter or expand on a scale similar to that which was prevented or forestalled by the merger, and in a similar timeframe. Where the Tribunal finds that such entry or expansion likely would occur even if the merger proceeds, it is unlikely to conclude that the merger is likely to prevent competition substantially.

**386** In summary, to demonstrate that a merger is likely to prevent competition substantially, the Commissioner must establish, on a balance of probabilities, that "but for" the merger, one of the merging parties likely would have entered or expanded within the relevant market within a reasonable period of time, and on a sufficient scale, to effect either a material reduction of prices or a material increase in one or more levels of non-price competition, in a material part of the market, for approximately two years. Alternatively, the Commissioner must establish a similar likely effect on prices or on levels of non-price dimensions of competition as a result of the development of another type of future competition that likely would have occurred "but for" the merger.

### D. WHEN EFFICIENCIES CAN BE CONSIDERED

**387** The Tribunal's decision in *Propane 3*, above, has been interpreted as suggesting that cost reductions and other efficiencies can never be considered prior to the triggering of the defence set forth in section 96. This appears to be a misreading of *Propane 3*. The source of this misunderstanding appears to be found in paragraph 137 of that decision. The focus of the discussion in that paragraph was on the differences between the Canadian and American

approaches to efficiencies, and, specifically, whether section 96 requires the efficiencies likely to result from a merger to be so great as to ensure that there are no adverse price effects of the merger.

**388** There may well be situations in which any cost reductions or other efficiencies likely to be attained through a merger will increase rivalry, and thereby increase competition, in certain ways. These include: (i) by enabling the merged entity to better compete with its rivals, for example, by assisting two smaller rivals to achieve economies of scale or scope enjoyed by one or more larger rivals, (ii) by increasing the merged entity's incentive to expand production and to reduce prices, thereby reducing its incentive to coordinate with other firms in the market post-merger, and (iii) by leading to the introduction of new or better products or processes.

**389** There is no "double counting" of such efficiencies when it is determined that the merger in question is likely to prevent or lessen competition substantially and a trade-off assessment is then conducted under section 96. This is because, in that assessment, such efficiencies would only be considered on the "efficiencies" side of the balancing process contemplated by section 96. They would not directly or indirectly be considered on the "effects" side of the balancing process, because they would not be part of any cognizable (i) quantitative effects (e.g., the DWL or any portion of the wealth transfer that may be established to represent socially adverse effects), or (ii) qualitative effects (e.g., a reduction in dynamic competition, service or quality). Moreover, at the section 92 stage of the analysis, they typically would not be found to be a source of any new, increased or maintained market power that must be identified in order to conclude that the merger is likely to prevent or lessen competition substantially.

### E. THE EFFICIENCIES DEFENCE

**390** The analytical framework applicable to the assessment of the efficiencies defence has been set forth in significant detail in the Panel's decision. I simply wish to make a few additional observations.

#### (i) Conceptual framework

**391** In broad terms, section 96 contemplates a balancing of (i) the "cost" to the economy that would be associated with making the order that the Tribunal has determined should otherwise be made under section 92 (the "Section 92 Order"), and (ii) the "cost" to the economy of not making the Section 92 Order. The former cost is the aggregate of the lost efficiencies that otherwise would likely be attained as a result of the merger. The latter cost is the aggregate of the effects of any prevention or lessening of competition likely to result from the merger, if the Section 92 Order is not made.

**392** Section 96 achieves this balancing of "costs" by (i) confining efficiencies that are cognizable in the trade-off assessment to those that "would not likely be attained if the [Section 92 Order] were made", as contemplated by subsection 96(1), and (ii) confining the effects that may be considered in the trade-off assessment to "the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger".

**393** In short, the efficiencies that are eliminated by this language in subsection 96(1), which is referred to at paragraph 264 of the Panel's decision as the fifth "screen" established by section 96, are not considered in the trade-off assessment because they would not represent a "cost" to society associated with making the Section 92 Order. That is to say, the efficiencies excluded by this screen either would likely be achieved through alternative means in any event, or they would be unaffected by the Section 92 Order. This could occur, for example, because they would be attained in one or more markets or parts of the merged entity's operations that would be unaffected by the Section 92 Order. It is in this sense that the assessment contemplated by section 96 is heavily dependent on the nature of the Section 92 Order.

**394** That said, to the extent that there are efficiencies in other markets that are so inextricably linked to the cognizable efficiencies in the relevant market(s) that they would not likely be attained if the Section 92 Order were made, they are cognizable under section 96 and will be included in the trade-off assessment.

**395** In assessing whether efficiencies are likely to be achieved through alternative means, the Tribunal will assess the realities of the market(s) concerned, and will not exclude efficiencies from its analysis on the basis of speculation that the efficiencies could *possibly* be achieved through such alternative means.

**396** It bears emphasizing that, under section 96, the relevant counterfactual is the scenario in which the Section 92 Order is made. This is not necessarily the scenario in which the merger does not occur.

(ii) Socially adverse effects

**397** At paragraph 284 of the Panel's decision, it was observed that the Commissioner adduced no evidence with respect to what the Tribunal in the past has characterized as being *socially adverse* effects. The Panel also observed that the Commissioner conceded that the merger is not likely to result in any such effects. Accordingly, the Panel confined its assessment to the *anti-competitive* effects claimed by the Commissioner.

**398** However, given that the Commissioner requested, in her final oral submissions, that the Panel clarify the analytical approach applicable to the efficiencies defence, the following observations will be provided with respect to the potential role of socially adverse effects in the trade-off analysis contemplated by section 96, in future cases.

**399** At paragraph 205 of its final argument, CCS characterized the approach established by the Federal Court of Appeal in *Propane 2*, above, as being the "balancing weights approach." This is the same terminology that was used by Dr. Baye at footnote 14 of his reply report, where he referred to the approach established in *Propane 3*, above, and *Propane 4*, above. However, as the Tribunal noted in *Propane 3*, at para. 336, balancing weights "is incomplete [as an approach] and useful only as a tool to assist in its broader inquiry" under section 96. With this in mind, the Tribunal characterized that broader inquiry mandated by *Propane 2* in terms of the "socially adverse effects" approach. However, on reflection, the term "weighted surplus" approach would seem to be preferable.

**400** As noted at paragraphs 281 - 283 of the Panel's decision, the total surplus approach remains the starting point for assessing the effects contemplated by the efficiencies defence set forth in section 96 of the Act. After the Tribunal has assessed the evidence with respect to the quantifiable (i.e., the DWL) and non-quantifiable anti-competitive effects of the merger in question, it will assess any evidence that has been tendered with respect to socially adverse effects. In other words, if the Commissioner alleges that the merger is likely to give rise to socially adverse effects, the Tribunal will determine how to treat the wealth transfer that is likely to be associated with any adverse price effects of the merger. The wealth transfer is briefly discussed at paragraph 282 of the Panel's decision.

**401** As the Tribunal observed in *Propane 3*, above, at para. 372, "demonstrating significant adverse redistributional effects in merger review will, in most instances, not be an easy task." Among other things, determining how to treat the wealth transfer will require "a value judgment and will depend on the characteristics of [the affected] consumers and shareholders" (*Propane 3*, above, at para. 329). It will "rarely [be] so clear where or how the redistributive effects are experienced" (*Propane 3*, above, at para. 329). In general, the exercise "will involve multiple social decisions" and "[f]airness and equity [will] require complete data on socio-economic profiles on [*sic* ] consumers and shareholders of producers to know whether the redistributive effects are socially neutral, positive or adverse" (*Propane 3*, above, at paras. 329 and 333).

**402** Where it is determined that the merger likely will result in a socially adverse transfer of wealth from one or more identified lower income group(s) to higher income shareholders of the merged entity, a subjective decision must be made as to how to weigh the relevant part(s) of the wealth transfer. (If the entire wealth transfer will involve a socially adverse transfer, then it would be necessary to decide how to weigh the full transfer.) If the income effect on some purchaser groups would be more severe than on others, different weightings among the groups may be required.

**403** It is at this point in the assessment that the balancing weights tool can be of some assistance. As proposed by Professor Peter Townley, one of the Commissioner's experts in *Propane*, above, this tool simply involves determining the weight that would have to be given to the aggregate reduction in consumer surplus (*i.e.*, the sum of the deadweight loss, including any deadweight loss attributable to pre-existing market power, plus the wealth transfer) in order for it to equal the increased producer surplus that would likely result from the merger (*i.e.*, the sum of the efficiency gains and the wealth transfer). (See the Affidavit of Peter G.C. Townley, submitted in *Propane*, above, (available at http://www.ct-tc.gc.ca/CMFiles/CT-1998-002_0115_38LES-1112005-8602.pdf).)

**404** For example, in *Propane*, the aggregate reduction in consumer surplus was estimated to be $43.5 million, *i.e.*, the estimated $40.5 million wealth transfer plus the estimated $3 million DWL. By comparison, the aggregate increase in producer surplus was estimated to be $69.7 million, *i.e.*, the sum of the efficiency gains accepted by the Tribunal, namely $29.2 million, plus the wealth transfer of $40.5 million. The balancing weight was therefore represented by *w* in the following formula: 1(69.7) - *w* ($43.5) = 0. Solving for *w* yielded a value of 1.6, which was the weight at which the consumer losses and the producer gains just balanced. (See *Propane 3*, above, at paras. 102-104.) Accordingly, for consumer losses to outweigh producer gains, they would have had to be given a weight of greater than 1.6, assuming that producer gains were given a weight of 1.

**405** Professor Townley's helpful insight was that members of the Tribunal often would be in a position to subjectively determine, even in the absence of substantial information, whether there was any reasonable basis for believing that a weighting greater than the balancing weight ought to be applied to the socially adverse portion(s) of the wealth transfer. If not, then notwithstanding an insufficiency of the information required to accurately calculate a full set of distributional weights, it could be concluded that the efficiencies likely to result from the merger would outweigh the adverse effects on consumer surplus. Unfortunately, there was not sufficient information adduced in *Propane* to permit the Tribunal to assess whether the estimated balancing weight of 1.6 was reasonable, given the socio-economic differences between and among consumers and shareholders (*Propane 3*, above, at para. 338).

**406** Where the balancing weights tool does not facilitate a determination of the weights to be assigned to any identified socially adverse effects, other evidence may be relied upon to assist in this regard. For example, in *Propane 3*, the Tribunal relied upon Statistics Canada's report entitled *Family Expenditure in Canada, 1996*, which suggested that only 4.7% of purchasers of bottled propane were from the lowest-income quintile, while 29.1% were from the highest-income quintile. The Tribunal ultimately determined that the redistributive effects of the merger on customers in the lowest-income quintile would be socially adverse, and included in its trade-off analysis an estimate of $2.6 million to reflect those adverse effects. Although it found that it had no basis upon which to determine whether the DWL should be weighted equally with adverse redistribution effects, the Tribunal ultimately concluded that, even if the $2.6 million in adverse distribution effects were weighted twice as heavily as the $3 million reduction in DWL and a further $3 million to represent the adverse qualitative effects of the merger, the combined adverse impact on consumer surplus would not exceed $11.2 million (*Propane 3*, above, at para. 371). Since that estimate was still far below the recognized efficiency gains of $29.2 million, it concluded that the defence in section 96 had been met. This conclusion was upheld on appeal.

(iii) Non-quantifiable/qualitative effects

**407** The Panel's assessment of the non-quantifiable effects that were considered in the section 96 trade-off assessment in this case is set forth at paragraphs 305-307 of its reasons.

**408** I simply wish to add that where there is not sufficient evidence to quantify, even roughly, effects that ordinarily would be quantifiable, it will remain open to the Tribunal to accord *qualitative* weight to such effects. For example, in the case at bar, it would have been open to accord qualitative weight to the anti-competitive effects of the Merger expected to occur outside the Contestable Area, given that the evidence established that such effects were likely, but could not be calculated due to shortcomings in the evidence. As it turned out, it was unnecessary for the Panel to give those effects any weighting whatsoever.

**409** Similarly, had the Panel not accepted the Commissioner's evidence with respect to the quantitative magnitude of the DWL, such that there was then no evidence on this specific matter, it would have been open to the Panel to accord qualitative weight to the fact that there would have been *some* significant DWL associated with the adverse price effects which it determined were likely to result from the Merger. The same will be true in other cases in which either it is not possible to reliably quantify the likely DWL, even in rough terms, or the Commissioner fails to adduce reliable evidence regarding the extent of the likely DWL, at the appropriate time.

DATED at Ottawa, this 29th day of May, 2012.

(s) Paul Crampton C.J.

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# Canada (Commissioner of Competition) v. Superior Propane Inc., [2000] C.C.T.D. No. 15

Canada Competition Tribunal Decisions

Canada Competition Tribunal

Ottawa, Ontario

Before: Nadon J., Presiding Judicial Member L.R. Bolton, C. Lloyd and L.P. Schwartz, Members

Heard: September 23, 24, 27-29, November 1-3, 23, 25,

29, 30, December 1-3, 6-9, 13, 14, 1999, January 19, 24,

31 and February 1-4, 7-9, 2000.

Decision: August 30, 2000

File no.: CT-1998-002

Registry document no.: 192b

**[2000] C.C.T.D. No. 15** | *[2000] D.T.C.C. no 15* | *2000 Comp. Trib. 15* | Also reported at:*7 C.P.R. (4th) 385*

Reasons and Order 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 Commissioner of Competition under section 92 of the Competition Act. Between: The Commissioner of Competition, (applicant), and Superior Propane Inc., ICG Propane Inc., (respondents)

(516 paras.)

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Reasons and Order

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## I. INTRODUCTION

**1** An application is brought by the Commissioner of Competition ("Commissioner") pursuant to section 92 of the Competition Act, *R.S.C. 1985, c. C-34*, (the "Act") for an order to dissolve the merger of Superior Propane Inc. ("Superior") and ICG Propane Inc. ("ICG") or otherwise remedy the substantial prevention or lessening of competition that is likely to occur in the market for propane in Canada upon the implementation of the said merger.

**2** The application arises by reason of Superior's acquisition of ICG on December 7, 1998. Prior to the acquisition,

Superior submitted a short-form prenotification filing pursuant to section 121 of the Act to the Competition Bureau regarding its proposed acquisition of all of the shares of The Chancellor Holdings Corporation, a wholly-owned subsidiary of Petro-Canada. The Chancellor Holdings Corporation, in turn, owned ICG. An inquiry into this merger was commenced by the Commissioner on August 14, 1998, pursuant to section 10 of the Act. On December 6, 1998, following two days of hearing, the Tribunal dismissed the Commissioner's application of December 1, 1998 brought under section 100 of the Act for an order forbidding the closing of the transaction for a period of 21 days. Further, on December 11, 1998, a consent interim order was issued by the Tribunal to hold separate the assets of Superior and ICG, excluding the non-overlapping locations situated in areas where Superior had no market presence.

**3** Superior is a corporation constituted under the laws of Canada and is engaged primarily in the retailing and wholesaling of propane, as well as in the sale of propane consuming appliances and equipment and related services in all 10 provinces and territories. All of the outstanding shares of Superior are owned by the Superior Income Trust Fund (the "Fund"), a limited purpose trust established for the purpose of holding debt and equity of Superior. The Fund has issued trust units which are listed on the Toronto Stock Exchange.

**4** ICG is a corporation constituted under the laws of Canada and is engaged in selling and distributing propane and providing related services to customers in all Canadian provinces and territories except Prince Edward Island, Newfoundland and to a lesser extent, Nova Scotia. ICG operates through a network of company-owned distribution outlets and independent dealers located throughout its sales and distribution areas. In 1990, Petro-Canada indirectly acquired ICG and combined Petro-Canada's retail propane operations with ICG's business.

**5** The Commissioner alleges that the merger will create a dominant national propane marketer and in several markets, a dominant local propane marketer. Both Superior and ICG compete against each other in the same geographic and product markets through their operations of propane distribution systems and wholesale supply of propane to agents and dealers.

**6** Interlocutory proceedings in this matter were lengthy and vigorously contested. Upon application by the Commissioner, an interim order was issued on December 11, 1998 to preserve ICG's business as independent and viable pending the Tribunal's decision on the application. Various orders regarding confidentiality of documents and the scope of discovery were issued by the Tribunal.

**7** Following the illness and inability of a panel member, Lorne Bolton, to attend the hearing in this matter, an Order Regarding the Constitution of a New Panel was issued on December 13, 1999. This order terminated the hearing before the panel constituted of Mr. Bolton, Dr. Schwartz, and Nadon J. and further constituted a new panel composed of Ms. Christine Lloyd, Dr. Schwartz and Nadon J. pursuant to section 10 and subsection 12(3) of the Competition Tribunal Act. The evidence on the record of the previous proceedings, including all the orders and rulings made by the Tribunal, were entered into the record of the hearing before the new panel pursuant to section 70 of the Competition Tribunal Rules.

**8** The hearing of this matter took 48 days, 91 witnesses including 17 expert witnesses were called and a large number of documents were entered as exhibits.

## II. PROPANE BUSINESS

**9** Propane is a chemical commodity produced as a by-product of natural gas extraction and of crude oil refining. In Canada, 85 percent of propane production is derived from natural gas and accordingly is produced in the Western Canadian Sedimentary Basin. Propane volumes from crude oil are produced at oil refineries that are generally closer to population centres where the consumption occurs (e.g., Edmonton, Southern Ontario, Montreal, Quebec City).

**10** Propane sourced from gas production is extracted and transported mixed with other natural gas liquids to

fractionation sites where separation into "specification propane" takes place. In Canada, raw natural gas liquids are transported from producing regions in Alberta and northeast British Columbia via pipelines to "hubs" at Edmonton/Ft. Saskatchewan and at Sarnia, Ontario, where fractionation takes place. Fractionation into specification propane also takes place at straddle plants along pipelines and gas field plants in Alberta for marketing to western Canada.

**11** Approximately 63 percent of propane produced in Canada is exported to the United States (expert affidavit of G. Mathieson (18 August 1999): exhibit A-2073 at 15). According to Statistics Canada data which are themselves disputed, total domestic consumption of approximately 77 million barrels per day ("mbpd") in 1998 occurred in the segments of residential/commercial/agricultural for space and water heating, cooking, appliances, crop drying (32 mbpd); industrial uses, e.g., forklifts, heating (17 mbpd), collectively, the "traditional segments"; in transportation, primarily automobile fuel (18 mbpd); and petrochemical feedstock (10 mbpd). Consistent with industry usage, "retail propane" includes total propane consumption less propane consumed as petrochemical feedstock and propane consumed by producers.

**12** Although it appears that there are discrepancies in the consumption data published by different sources, autopropane consumption seems to have peaked in 1994 at 23 mbpd, stimulated by government-supported fleet conversions, and then declined steadily as those programmes of financial assistance were ended along with other factors including the improved efficiency of gasoline engines.

**13** Consumption of propane used as a heating fuel is subject to seasonal fluctuation and dropped dramatically from 39 mbpd in 1997 to 32 mbpd in 1998 due to warmer weather. Consumption in the industrial and petrochemical feedstock segments appears to have levelled. It seems that Canadian propane consumption is characterized by stable demand or modest growth at best.

**14** There is some dispute as to the number of propane marketers operating in Canada. ICG's amended preliminary prospectus claims approximately 75 propane marketers including Superior, while Superior claims a total of 189 independent propane distributors. These propane marketers obtain propane supplies at refinery racks and at storage facilities owned by the major propane producers at prices based on postings at the Edmonton or Sarnia hubs and varying with the distance between these hubs and the supply point. Large marketers typically purchase their supplies under contracts that specify volume and price, or a pricing formula in terms of price per litre. These buyers may own or rent storage space close to the supply points which allows them to enter into "keep dry" arrangements at lower prices from producers. A keep-dry arrangement requires the buyer to take propane sufficiently regularly so that the producer does not have to maintain storage and, therefore, sells at a lower price to a buyer capable of honouring its commitments.

**15** These buyers transport propane by truck or rail to their local storage facilities (primary distribution). Secondary distribution occurs when delivery to customers is made, usually by truck, from these local storage facilities.

**16** Smaller propane marketers purchase propane on spot markets from the producers or from the larger marketers. In some cases, a smaller marketer acts as an agent in a local area for a major marketer that does not have a local delivery capability. For such arrangements, the customer contract is held by the major marketer who determines the pricing. Another relationship is the "bulk dealer", whereby a local company purchases propane from a major marketer under an agreement that specifies a territory in which that local dealer will not face competition from the major marketer or any of its other bulk dealers.

**17** Propane marketers tend to be local and regional in their operations. At present, only two companies, Superior and ICG, supply end-users across Canada, either directly or through agents and dealers. The merging parties are well suited to supply customers that demand propane at multiple locations across the country.

**18** The customer relationship is most frequently contractual. Almost all propane marketers undertake to deliver propane on a regular basis to customer locations at the prevailing price established by the marketer from time to time for a specific term with agreements lasting up to five years. The customer is free to terminate the contract on

sufficient notice, but as the contract will often contain "meet or beat" and/or "right of first refusal" clauses, the current supplier may be able to maintain the customer's business.

**19** In addition to delivering the propane, particularly to residential customers, the marketer usually provides customer storage tanks on a rental basis and installs and services propane-related equipment. It appears that most marketers do not fill a residential tank that they do not own.

**20** Propane delivery is a regulated activity in all jurisdictions. Propane storage tanks and customer tanks must meet various safety standards, and the individuals who handle the propane must be licensed.

**21** Although specification propane is a well defined commodity, the propane marketing companies generally differ with respect to reputation, length of time in the business, the terms and conditions they offer to customers, the ability to meet a customer's needs at multiple locations, etc. In addition, some marketers specialize in serving certain segments, while others seek customers in all segments. The result is that the "product" provided by a propane marketer is often differentiated on these dimensions from the offerings of its competitors.

## III. MARKET DEFINITION

### A. PRODUCT MARKET

**22** With respect to product market definition, the Commissioner submits in final argument that the relevant product market is the supply and delivery of propane, propane equipment and related services to retail and wholesale customers. The Commissioner also submits that the relevant product market can be further broken down into various end-uses and customer classifications including: residential, agricultural, commercial, industrial (collectively, the "traditional" segment), automotive, national and major account customers. As propane and related equipment and services appear to be strong complements, it will be convenient to define one product market rather than consider the three separate business lines mentioned.

**23** The Commissioner alleges, in effect, that retail propane constitutes, by itself, a market over which market power can be exercised. Such a market will be referred to as a "competition market". The respondents assert that it is not a competition market because alternate fuels exist and consumers can and do easily switch to these alternatives. Their position is that retail propane is part of a broad energy market and hence that any attempt to exercise market power over retail propane could not be successful.

#### (1) Commissioner's Position

**24** The Commissioner's experts, Richard Schwindt and Steven Globerman, presented a report evaluating the competitive effects of the proposed merger between Superior and ICG. With respect to product market definition, they provided opinion evidence that retail propane is the relevant competition market (expert affidavit of R. Schwindt and S. Globerman (16 August 1999): exhibit A-2056). They conclude that switching from propane to alternate fuels is difficult. For example, regarding residential heating applications, Professors Schwindt and Globerman observe, at page 10 of their report, that while most propane appliances can be readily converted to natural gas, nevertheless "in residential households where the piping from the outside of the house to the furnace is sized for propane and not for natural gas, conversion costs can be quite high". Further, regarding electricity, they observe at page 11 of their report that "at this time and into the foreseeable future, the price of electricity is so high relative to propane in several parts of the country that it is an unlikely substitute".

**25** Further, Professors Schwindt and Globerman observe that heating oil could be a substitute for propane although propane is superior to oil with respect to cleanliness, environmental impact and odour. Convenience, storage requirements and capital costs do not differ significantly between the two fuels. However, their estimated costs of converting a residence in the Lower Mainland of British Columbia from a propane to an oil fired forced air furnace range from $4,500 to $5,300. At pages 12 and A-2 of their report, they conclude that it would take very significant price increases, in the range of 50 to 60 percent, to justify a switch to fuel oil. At page A-3, they conduct a

similar analysis regarding switching from propane to heating oil in commercial heating and from propane to electricity for forklift trucks which leads to the same conclusion.

**26** Regarding autopropane, Professors Schwindt and Globerman note at page 19 of their report that substitutability of alternate fuels, particularly gasoline, depends upon whether the vehicle is dual-fuel or dedicated to propane. They infer from an Imperial Oil Limited ("IOL") document that 95 percent of conversions to propane in British Columbia in the early 1990's were for commercial vehicles and nearly all of those were "propane dedicated" rather than dual-fuel, suggesting that substitution is slight.

**27** The Commissioner further submits that switching costs are high and "create a lock-in effect for customers" with the result that cross-elasticity of demand is low.

**28** The Commissioner submits that the payback period for changing related equipment and appliances from propane to alternate fuels may be significant. He states that, for instance, the life-cycle for fuel related equipment and appliances for the traditional sector such as residential furnace is on average in the range of 15 to 25 years. Therefore, a customer facing a propane price increase would have to consider this factor before converting this equipment.

**29** In this regard, the Commissioner cites a study commissioned by ICG and produced by M. Paas Consulting Ltd. in August 1999, dealing with locations and markets where alternative fuels may pose either a competitive threat or an opportunity for ICG (exhibit A-2099). The study measures customer payback to switching fuel types (i.e., the time it would take for the savings in fuel costs to match the initial outlay for switching) under two scenarios: (a) when the existing appliance has useful life remaining, and (b) where the appliance requires replacement. The study demonstrates that converting from propane to electricity or fuel oil, for most of the seven end-uses analysed, involves long and, in many cases, infinite payback periods and hence does not make economical sense in the short to mid-term when factoring all the relevant switching costs and not only the cost of the fuel.

**30** The Commissioner also called a number of factual witnesses who testified that switching to alternate fuels was impeded by the difficulty and inconvenience of breaking existing contracts for supply and equipment. The inconvenience includes the difficulty in coordinating the removal of existing equipment and the installation of new supplier's equipment in a timely fashion (e.g., to avoid plant shut down or loss of residential heating), the cost of removing the leased equipment and the delays associated with getting a refund for the propane left in the tank. Superior's own public share offering documents (exhibits A-10 at 03890 and A-202 at 03899) emphasize these barriers to customer switching.

**31** With respect to conversion costs, the Commissioner presented the evidence of a factual witness, Marilyn Simons, a residential user of propane from Renfrew, Ontario, who evaluated the costs to convert her home furnace from propane to heating oil, her propane stove to an electric stove and to replace her propane fireplace with wood-burning equipment. The total conversion costs amounted to approximately $12,300. Some witnesses testified that conversion costs would prevent them from switching to alternate fuels while others testified that an increase in the price of propane would have to be very significant before such conversion was made.

**32** The Commissioner submits that there is only imperfect substitutability of alternate fuels for propane. In particular, he concedes that propane consumers do switch from propane to natural gas when this option is available and that, therefore, natural gas displaces rather than competes with propane.

**33** The Commissioner also introduced the expert evidence of David Ryan and André Plourde whose report provides "empirical evidence concerning the role, importance and substitutability of propane as an energy source in Canada" (expert affidavit of D. Ryan and A. Plourde (16 August 1999): exhibit A-2076 at paragraph 1(a)). They studied energy consumption for propane, electricity, natural gas, refined oil products and wood in three sectors (residential, industrial and commercial) for each province or region depending on data availability. Then, using Statistics Canada and other government data from 1982 to 1996, the last year for which all of the relevant data

series were available, they estimated short-run and long-run cross-price elasticities and own-price elasticities of propane demand for the years 1990 and 1996.

**34** At paragraph 6.3.4(a) of their report, Professors Ryan and Plourde find that in about 35 percent of the cases considered, the own-price elasticity of propane demand is negative and significant, while it is positive and significant in fewer than four percent of the cases. The own price elasticity of demand is the percentage change in quantity of the product consumed that results from a one percent price increase in its price. In all other situations considered, no significant relationship between the quantity of propane demanded and its price can be detected. They conclude that, in general, a change in the price of propane will lead to smaller than proportional reductions in propane consumption, i.e., that propane demand is inelastic.

**35** Regarding cross-price elasticity, statistically significant responses to propane price changes were identified in approximately 45 percent of the cases considered with substitution relationships outnumbering complementarity by a factor of about two-to-one. However, with the exception of oil products in Saskatchewan/residential and Quebec/industrial for 1996, all cross-price elasticities reported were less than one in absolute value. Indeed, in only two cases do cross-price elasticities exceed 0.6 in absolute value. They conclude that changes in propane prices induce proportionally smaller changes in the consumption of other energy types and, therefore, that propane and other energy types form different markets in the provinces/regions in Canada.

**36** Although arguing for an "all propane" product market, the Commissioner suggests through expert evidence that certain end-use segments constitute relevant markets in themselves. This would indicate that if, for example, market power could be exercised in residential propane but not in the other end-use segments, then it would properly constitute a relevant competition market, and total consumption and market shares would be calculated within that segment.

**37** At page 1 of their report (exhibit A-2056), Professors Schwindt and Globerman conclude that "retail propane distribution does constitute a relevant product market", despite the fact that they find evidence of segmentation among suppliers and customers and they suggest that this segmentation is strong enough to qualify theses segments as separate product markets. They conclude at page 23 of their report as follows:

> ... However, given the limited availability of data with respect to market structure by geographical market, application, and in some cases customer, it would not be possible to determine the differential effects of the merger on competitive conditions across more rigorously and narrowly defined product markets. Moreover, the analysis that follows would not be fundamentally altered by adopting a more refined product market definition. (emphasis added)

**38** Finally, the Commissioner argues that "national accounts" are a separate category of business in which the merged entity will be in a position to exercise market power. According to the Commissioner, a significant component of the customer base of each of the merging firms is the national and major accounts which have multiple locations spanning one or more regions across Canada.

(2) Respondents' Position

**39** The respondents' position on the relevant product market is that propane competes with alternative fuels in the energy market and for each end-use, different alternate fuels are substitutes. They assert that interchangeability of propane and alternate fuels together with the evidence of inter-industry competition and the views of industry participants strongly indicate that propane and alternate fuels compete in the same market.

**40** On the matter of customer switching, the respondents referred to the evidence of William Katz, a senior executive of AmeriGas Propane Inc. ("AmeriGas"), who testified that customers would switch to propane when it could be demonstrated that switching was economically attractive for them and not only at the end of the useful life

of the equipment (transcript at 15:2602-604 (19 October 1999)). Mr. Katz also indicated that AmeriGas had success in switching customers to propane well before the end of the useful life of their existing equipment.

**41** Further, the respondents assert that every year, a substantial number of propane and alternate fuel customers replace their existing equipment or make an initial fuel choice and accordingly choose from among the "entire menu" of fuel choices. The respondents note that customers making an initial fuel choice or replacing existing equipment face no incremental switching costs and, therefore, that customers whose equipment is in mid-life cycle pay the same price as those who are at the end of the cycle.

**42** The respondents argue that propane industry views support the substitutability of alternative fuels. They state as an example that Steven Sparling of Sparling's Propane Company Limited ("Sparling") testified that his company considered any energy provider a competitor. This includes electricity, natural gas, fuel oil and propane marketers.

**43** The respondents also submit that the Tribunal in the context of denying an injunction to the Commissioner in this case (see Director of Investigation and Research v. Superior Propane Inc. *(1998), 85 C.P.R. (3d) 194* at 207, 208, *[1998] C. C. T. D. No. 20* (QL)) acknowledged the statements made by Superior and ICG in their securities filings regarding competition between propane and alternate fuels. At the time, Rothstein J. accepted that they were competing in a wide energy market on the basis that the statements contained in the prospectus and annual reports and in ICG's preliminary prospectus were "of some significance" and something upon which he should "place weight".

**44** The respondents also assert that supply substitution is possible and that the relevant market should take account of firms that can easily switch their facilities to propane marketing. They submit that it is appropriate to include upstream industry participants and industrial gas companies as well as other distributors of alternate fuels.

**45** Finally, the respondents suggest that the analysis conducted by the Commissioner's experts, Professors Ryan and Plourde, explicitly recognizes that alternate fuels and propane are substitutes in various places at various times for various end-uses.

(3) Analysis

**46** There is clearly no commonality in the positions of the parties before the Tribunal on the appropriate definition of the product market. Accordingly, the Tribunal must decide which evidence is the more convincing.

**47** The purpose of defining the relevant product market is to identify the possibility for the exercise of market power. This purpose was clearly asserted in the two previous merger cases heard by the Tribunal. In Director of Investigation and Research v. Southam Inc. *(1992), 43 C.P.R. (3d) 161* at 177, 178, *[1992] C.C.T.D. No. 7* (QL), the Tribunal reiterated:

> The general issues with respect to the definition of a market in a merger case have been set in the Hillsdown Holdings (Canada) Ltd. decision, supra. The relevant market for purposes of merger analysis is one in which the merging firms acting alone or in concert with other firms could exercise market power. Market power is the ability of a firm or group of firms to maintain prices above the competitive level. Market power may also be exercised by offering, for example, poor service or quality or by restricting choice. When used in a general context, "price" is thus a shorthand for all aspects of firms' actions that bear on the interest of buyers ....
>
> The delineation of the relevant market is a means to the end of identifying the significant market forces that constrain or are likely to constrain the merged entity....
>
> The critical issue is to ensure that all factors have been considered that have a bearing on whether there has or is likely to be a prevention or lessening of competition to a substantial degree. (emphasis added)

**48** While market definitions should be as precise as possible within the limit of reasonableness to provide a

framework within which competition implications of a transaction can be analysed, the Tribunal should not be preoccupied with market definition to the point of losing sight of the purpose of the exercise under the Act which is to determine whether the merger is likely to lead to a substantial prevention or lessening of competition. As stated by the Supreme Court of Canada in Director of Investigation and Research v. Southam Inc., *[1997] 1 S.C.R. 748* at 788:

> ... More generally, I notice that the Tribunal seems to have been preoccupied with the definition of the relevant market. It is possible that the members may occasionally have lost sight of the ultimate inquiry, which is whether the acquisition of the community newspapers by Southam substantially lessened competition.

**49** In the Tribunal's view, the factual and expert evidence on substitutability is very important. The Tribunal distinguishes between "switching" in its common sense meaning and substitutability in the economic sense; it is the latter that is important in delineating a relevant product market. It may be, as the respondents claim, that at the end of the useful life of their heating or other energy-using equipment, consumers do switch to propane from alternate fuels depending, in part at least, on differences in fuel prices. However, this behaviour demonstrates de novo choice; at the end of their equipment life cycle, those consumers are in the same position as when they first chose a fuel. This behaviour is not evidence of substitutability, which refers to changing a consumption pattern in response to a price change with all other determinants of change, including the age of equipment, held constant.

**50** Mr. Katz stated that AmeriGas was successful in attracting customers to propane from other fuels before the end of the useful life of their existing equipment. However, he provided no quantitative evidence as to AmeriGas's success in this regard and accordingly, it is difficult for the Tribunal to judge the extent of such success.

**51** Mr. Sparling's testimony is that Sparling is seeking to attract new propane customers in the new housing developments. If Sparling is successful, it is evidence that such customers are making fuel choices as a consequence of a decision to relocate. While this residential location decision may involve a change in fuel, it does not demonstrate that the price of propane was the reason for the move and hence does not provide evidence of substitution.

**52** In its 10-K securities filing in the United States, AmeriGas makes similar comments about competition from alternate fuels. However, in the absence of evidence showing significant customer switching during the life of the existing equipment, the Tribunal is of the view that the evidence of AmeriGas does not support the substitutability of alternate fuels for competition market purposes.

**53** As to the views of industry participants, Sparling may well be correct in some long-term sense in its view that propane competes with all alternate fuels. However, no evidence indicates that Sparling's behaviour is affected by inter-fuel competition. According to Mr. Sparling, the company is mainly concerned about "consistent pricing" from customer to customer and not with pricing in relation to alternate fuels (transcript at 12:1731 (14 October 1999)). Moreover, Sparling has not experienced customers switching to other fuels other than natural gas (ibid. at 1733).

**54** Hence the Tribunal does not accept that propane industry views support the substitutability of alternate fuels in the mind of consumers. Indeed, witnesses consider alternate fuels for the most part at the end of equipment life cycle, rather than in a shorter period of time in which market power could be exercised and which is relevant for merger review.

**55** As to the conclusions drawn by Rothstein J. in denying the injunction sought by the Commissioner, it suffices to note that he did not have the benefit of the extensive record and expert opinions that were produced during the 48-day hearing of the application under section 92.

**56** The Tribunal notes that the Act does not require that markets be delineated. However, the Tribunal accepts that the delineation of competition markets is one way of demonstrating the likely competitive effect of a merger and that, where such an approach is valid, the competition market adopted must be relevant to the purposes and goals

of the merger provisions of the Act, which focus on the creation or enhancement of market power. In this connection, the Tribunal notes that there could be many competition markets containing retail propane. For example, it might be found that market power could be exercised over a product market consisting of retail propane, fuel oil, natural gas and electricity or any sub-group thereof. The share of retail propane in a market becomes larger as products are removed from the definition of the market. It is not clear, however, that any such market is the relevant competition market.

**57** The Tribunal believes that it is important to provide a principled basis in this regard in order to avoid gerrymandering of market boundaries. To determine which set of products is the relevant one for the purpose of merger review under the Act, the Tribunal agrees with the approach taken in the Merger Enforcement Guidelines ("MEG's") (Consumer and Corporate Affairs Canada, Director of Investigation and Research, Merger Enforcement Guidelines, Information Bulletin No. 5 (Supply and Services Canada, March 1991)), which seeks to identify the smallest competition market, in terms of the number of included products, over which market power could be exercised. Thus, if market power can be exercised over a market consisting only of retail propane, then that market is the competition market that is relevant for merger review.

**58** In this matter, the Tribunal accepts the statistical evidence of Professors Ryan and Plourde. Their evidence on cross-elasticity of demand clearly establishes that there are only a few areas of the country where substitution has occurred. Moreover, where substitution was found, the extent thereof was found to be small.

**59** The cross-price elasticity of demand concept is frequently used in market definition. This measure identifies a product as a substitute if its quantity demanded rises when the price of the good in question rises. For any pair of products A and B there will be two such elasticities (the percentage change in consumption of product A when the price of product B increases by one percent, and the percentage change in the consumption of product B when the price of product A increases by one percent). Absent direct evidence thereto, there is no reason to suppose that these two cross-price elasticities of demand will be equal or even that both will be positive; in short, there is no such thing as the cross-price elasticity of demand. Therefore, cross-elasticity evidence showing that B is a substitute for A does not establish that A and B are substitutes for each other and hence is not sufficient to place products A and B in the same competition market. To use cross-elasticity of demand for this purpose would require further evidence that A is also a substitute for B.

**60** The respondents' expert witness, Dennis Carlton, agreed in his testimony that both cross-elasticities of demand would be needed in order to place two products in the same competition market. The Commissioner implicitly adopts this approach when stating that, because of its lower price, natural gas "displaces" propane in an area when natural gas becomes available. This statement indicates the Commissioner's view that once propane users have switched to natural gas, they do not switch back; but since switching in the opposite direction does not occur, therefore, propane and natural gas cannot constitute a competition market. The Tribunal agrees that to show that natural gas and propane are in the same competition market would require evidence that propane customers switch to natural gas when the price of propane increases as well as evidence that natural gas customers switch to propane when the price of natural gas increases. In other words, reciprocal substitutability must be demonstrated. The displacement argument suggests only one-way substitutability between propane and natural gas. Therefore, the Tribunal is not convinced that natural gas and propane constitute a competition market.

**61** The more important limitation on the use of the concept of cross-price elasticity of demand to delineate markets is its indirect relevance to the exercise of market power. The definition of the relevant competition market does not depend on identifying particular substitutes in some pairwise fashion. Rather, the important question is whether, on a price increase by a firm, enough of its sales would be lost to all competing products, regardless of their number or identity, to make the price increase unprofitable. If this were the case, then a relevant competition market would not be found; that firm would not be able to exercise market power. A cross-elasticity estimate may identify a substitute and can be helpful in delineating a market, but it does not directly measure the ability of a firm to raise the price.

**62** As the Supreme Court of Canada stated in Southam, cited above at paragraph [48], at page 760, evidence of demand elasticities when available and reliable can be determinative for market definition. Thus, the Tribunal

believes that the own price elasticity of demand is the correct elasticity for defining competition markets and should be preferred over cross-price elasticity of demand for the reasons above.

**63** The Tribunal places greater weight on Professors Ryan and Plourde's evidence regarding the "own-price elasticity of demand" as this concept is directly related to the issue of market power and hence to market delineation. The evidence demonstrates that the demand for propane is inelastic with respect to changes in its price, i.e., that consumers reduce their consumption of propane only slightly when the price rises. Although the data did not permit Professors Ryan and Plourde to measure retail propane demand by local market, their results were not challenged on this basis and the Tribunal is satisfied that propane demand is inelastic with respect to price for time periods for which the Act is intended to apply.

**64** Thus, consistent with the approach taken in the MEG's, cited above at paragraph [57], if retail propane were hypothetically monopolized, that monopolist would face an inelastic demand curve and, according to conventional monopoly theory, would raise the price at least to the point where demand became elastic. Once the monopolist was operating on the elastic portion of the propane demand curve, further price increases would be imposed only if they were profitable.

**65** Accordingly, if retail propane demand is so price-sensitive (i.e., elastic) that a hypothetical monopolist that was the only current and future seller would not impose a significant and non-transitory price increase, then retail propane cannot be a relevant competition market and the market would have to be expanded to include another fuel. However, if the demand curve is sufficiently insensitive (i.e., inelastic) to price increases, then a monopolist would impose a significant price increase and the competition market would not be expanded. Therefore, there is a critical or "cutoff" level for the own-price elasticity of demand at the pre-merger price against which the measured own-price elasticity of the good under review could be compared in order to determine whether the relevant market has been identified. (For a general discussion of elasticities and market delineation, see G.J. Werden, "Demand Elasticities in Antitrust Analysis" (1998) 66 Antitrust L.J. at 363-414.)

**66** To counter a claim that a hypothetical monopolist would raise the price would require evidence that the pre-merger price was already above marginal costs. However, the respondents did not present such evidence.

**67** Other indicia such as functional interchangeability, inter-industry competition as well as the views of industry participants constitute indirect measures of substitutability and are often used to identify products in the relevant market, particularly when direct evidence on elasticities of demand is not available. However, it must be remembered that the relevant competition market is the smallest set of products over which market power can be exercised and these indirect measures do not identify that set of products for competition purposes. A competition market is defined for the express purpose of measuring market power and may only loosely be related to markets as defined by business people whose definition is determined by profit maximisation considerations.

**68** The respondents' definition of the product market relies heavily on the functional interchangeability of propane and alternate fuels (functional test) and the evidence of inter-industry competition of a few witnesses but does not consider the evidence of elasticities which had been considered by the Supreme Court in the Southam decision, cited above at paragraph [48], as determinative when available. While functional interchangeability can indicate something about the possibility of substitution between two or more products, it does not convey any information about the actual or likely consumer behaviour in response to the exercise of market power.

**69** In that regard the evidence drawn from actual behaviour (i.e., the elasticities) and the opinions provided by expert witnesses such as Professors Ryan, Plourde, Schwindt and Globerman carry more weight in the Tribunal's opinion as to what products constitute the relevant competition market. Consequently, the Tribunal finds that the relevant competition market is "retail propane" and excludes other fuels.

(4) Segmentation

**70** Evidence that propane consumers systematically pay different prices depending on their end-use, and that such differences are not justified on the basis of cost differences, is necessary to support a finding of separate competition markets by end-use. However, no such evidence has been provided. Professors Schwindt and Globerman examined individual end-use categories and seemed to suggest that since market power could be exercised in each segment, therefore, a monopolist of all segments would be able to price-discriminate. While this is certainly possible, one would need to be sure that the price elasticity of demand varied systematically across end-uses so that a monopolist could exploit those differences. Professors Schwindt and Globerman did not present evidence on such differences. Professors Ryan and Plourde's evidence was suggestive in that regard; however, they did not advocate end-use markets.

**71** Indeed, Professors Schwindt and Globerman suggest at page 36 of their report (exhibit A-2056) that there are price differences among propane consumers within the same segment; this could reflect perfect price discrimination. However, since demand elasticities are unlikely to vary significantly by consumer in the same end-use segment and geographic market, it is possible that they have identified price dispersion reflecting lack of complete consumer information rather than perfect price discrimination by end-use by a seller with market power.

**72** Finally, at page 2 of their report, Professors Schwindt and Globerman consider that supply side segmentation supports separate relevant competition markets by end-use. Their argument, which is premised on product differentiation, is confusing. Differences among suppliers do not indicate differences in price-elasticity of demand by end-use segment. In light of the evidence, the Tribunal is not satisfied that separate competition markets by end-use have been established.

(5) National Accounts

**73** The Commissioner alleges that national accounts are a separate category of business in which the merged entity will be in a position to exercise market power and that the appropriate geographic market for analyzing national account competition is Canada.

**74** The respondents submit that the Commissioner's experts, Professors Schwindt and Globerman, opined that national accounts did not constitute a separate product market.

**75** In the Tribunal's understanding, a national account customer is a consumer of propane at several sites across the country, or at least across a number of widely-dispersed geographic markets, such that the consumer finds it more convenient to contract for propane supply from one marketer with national operations or capabilities rather than from several marketers in local markets. Witnesses indicated a variety of reasons for preferring to obtain supply from a national marketer. John Fisher of U-Haul Ontario stated that one reason was the ability to negotiate a single price, or price formula, that allows U-Haul to charge the same price for propane at all of its 376 locations across the country. Michael Stewart of Canadian Tire emphasized the need for consistency of delivery, training and safety at all 96 store sites and 40 petroleum sites. Carole Bluteau of CN Rail noted the administrative problems of dealing with multiple local vendors given that propane represents such a small portion of CN's fuel purchases.

**76** Claude Massé of CP Rail noted that dealing with several suppliers was inconvenient not only in terms of multiple invoices and cheque handling, but also in problem-solving. In addition to centralized billing, he valued the capability with a national supplier of dealing with only one person to resolve issues at all sites, rather than contacting the local manager for each. Indeed, he allowed that there might even be some savings in direct costs of propane supply by using multiple, lower-priced suppliers because the administration of invoices (currently 100 bills per month) could be handled by existing personnel. However, propane pricing was not his reason for preferring a national supplier:

> ... But the pricing, it's not an issue - it's not the first base of this, the plan to go with one. It was more the product itself, the service.

> I would hate to go to a small company who the staff, if it doesn't have the expertise and the training, and then would fuel up a propane tank and then it blows up. The safety of our people is also important. transcript at 10:1506, 1507 (8 October 1999).

**77** It appears to the Tribunal that national account purchasers seek the management and administrative efficiencies that arise from doing business with a sole supplier. These efficiencies define a product that might be termed "national account coordination services", the price of which is difficult to observe because the product is bundled with the propane itself.

**78** National account coordination services are provided only by those propane marketers with national capabilities, specifically Superior and ICG. Several witnesses noted that when they tendered for a national supplier, they sought bids only from these companies. In addition, when a national account customer had a problem with its national supplier, it approached the other for supply.

**79** The evidence is that firms who use a national supplier do so for a variety of reasons largely unrelated to the price of propane. While the possibility exists that lower propane costs could be achieved through multiple suppliers, the evidence of several witnesses is that they did not even bother to investigate the prices and possible savings; Mr. Stewart of Canadian Tire was one such:

> MR. MILLER: Is the dealing with the one person and the one company across the country, is that of value to you?
>
> MR. STEWART: Absolutely.
>
> MR. MILLER: In what sense?
>
> MR. STEWART: Everything gets funneled through one person. I don't have to chase down the person who is responsible for different areas of the business. I can funnel all my questions through one and it gets distributed from there.
>
> MR. MILLER: Can you quantify this value in any fashion?
>
> MR. STEWART: I do not believe so.
>
> THE CHAIRMAN: I take it that you have never tried? Based on your answer, you've never tried to quantify it?
>
> MR. STEWART: No, we haven't.
>
> THE CHAIRMAN: Is that because it doesn't matter?
>
> MR. STEWART: At the time, it doesn't.
>
> THE CHAIRMAN: Very well.
>
> MR. MILLER: In the event of a price increase, how much of a price increase would you sustain before moving to some other arrangement?
>
> MR. STEWART: Well, it's hard to say at this point in time because it would take a lot of investigative work to ascertain costs and the costs involved with using alternate suppliers.
>
> MR. MILLER: Have you examined that at all?
>
> MR. STEWART: No.
>
> MR. MILLER: Thank you, sir. Those are all my questions.
>
> transcript at 11:1572, 1573 (13 October 1999).

**80** The evidence is that some large propane consumers with multiple sites acquire propane from multiple local suppliers, rather than from a national supplier. These consumers have decided to supply coordination services internally. In the Tribunal's view, it would not be unusual for firms to accomplish their propane supply objectives in

different ways. Internal coordination may well be efficient for some firms but not for others. However, the key question is not whether internal coordination is available as an alternative in the event of a small but significant price increase but, rather, whether national account customers would switch to multiple suppliers and internal coordination in that event.

**81** Although no expert witness has provided an opinion that national account coordination services constitute a relevant product market, the Tribunal is satisfied, in the light of the totality of the evidence, that national account coordination services constitute a product over which market power could be exercised.

**82** In light of comments regarding national accounts by both parties, it should be noted that product markets are defined in terms of products alone. For example, does the market for retail propane include natural gas, electricity, wood, etc.? Neither competitors nor customers can be said to be "in" or "out of" a product market. For this reason, the Tribunal defined a product "national account coordination services" and considered whether market power could be exercised over such product.

B. GEOGRAPHIC MARKET

(1) Local Markets

**83** The geographic market dimension of the relevant product is critical in this case because delivery is an important component of the product. Failure to define the proper geographic boundaries of retail propane markets would lead to the incorrect measure of market shares and hence of the ability to exercise post-merger market power. In this case, both parties submit that the geographic market is local in nature rather than provincial, national or international; but the dispute concerns the actual boundaries of these markets. The Commissioner presents a set of geographic markets based on Douglas West's spatial analysis approach which identifies joint service areas. The respondents criticize these markets as being too small when compared with Superior's actual travel patterns.

**84** The geographic boundaries of a market are established by asking what would happen if a hypothetical monopolist at a particular location attempted to impose a small but significant non-transitory price increase. If this price increase would likely cause buyers at that location to switch sufficient quantities of their purchases to products sold at other locations as to render the price increase unprofitable, then the geographic market would be expanded by adding the location to which customers switched their purchases. This question would be asked in relation to the expanded market repeatedly until a set of locations was identified over which a hypothetical monopolist could profitably impose a small but significant and non-transitory price increase. That area would be the smallest area over which market power could be exercised and would constitute the relevant geographic market for competition analysis.

**85** This area may bear little resemblance to service areas or trade areas as defined by particular sellers in the conduct of their business activities. These service or trade areas could be helpful in delineating relevant geographic markets but they do not define areas over which market power can be exercised.

**86** Professor West states that Superior and ICG had approximately 130 and 110 branches and satellite locations respectively in 1997. Professor West's procedure grouped these locations into 74 local geographic markets. In his opinion, these markets are relevant for the purpose of computing market shares and inferring post-merger market power (expert affidavit of D. West (17 August 1999): confidential exhibit CA-2051).

**87** Professor West's methodology, which is set out at pages 21-25 of his report, relies on set theory. First, he plots all branches and satellite locations of all propane dealers in operation in 1997. This accords with the view that the product of this merger is produced at the local storage facility and conforms with the approach that geographic markets should, in general, be delineated based at the point of production rather than at the point of consumption.

**88** For an initial Superior location, Professor West finds the "nearest point set". The boundary between that location

and another Superior location is the bisector of a straight line joining them. Bisectors for all adjoining Superior locations will completely specify the "market polygon" for that initial location. Similarly, Professor West determines the market polygon for each ICG location.

**89** Then, starting with a Superior location, Professor West assumes that the market polygon is part of the relevant market served by the branch at that location. If that polygon contains an ICG branch, then the Superior branch's market polygon is expanded to include the ICG branch's polygon. In essence, the market is defined as the union of the two polygons. If that ICG polygon includes a Superior branch/satellite location, the market is expanded again to include the union of the three polygons. The market is expanded in this way until no further polygons can be added to the union; at that point, Professor West defines a "candidate local market". He then undertakes the analysis for another Superior location.

**90** For each candidate local market, Professor West defines a buffer zone of 100 kilometers around the perimeter. He identifies all propane dealers with locations in that zone and considers, based on available information, whether those dealers can, in the event of a post-merger price increase, sell propane to customers located in the candidate market. Branches in the buffer that can compete with locations in the candidate market are included in the market for measuring market shares.

**91** Professor West notes that, in densely populated areas with many competing dealers, markets may be difficult to distinguish, particularly where branches of Superior or ICG are found in the buffer zone of a candidate local market. Such markets may be "linked". Accordingly, Professor West combines linked markets and re-estimates the market shares and reports that his market share estimates are not significantly altered in these larger markets.

**92** Professor West notes at page 3 of his report that:

> I have concluded that retail propane markets are local in geographic scope. They generally extend around 60 to100 kms. from the locations of SPI/ICG branches and satellites, depending on specific local market characteristics.

**93** The Commissioner further submits that Superior's own documents support Professor West's conclusion that the geographic market spans from 60 to 100 kilometers, as a general matter.

**94** With respect to the economical delivery distance, the 1997 Superior Propane Income Fund Annual Report (exhibit A-712) reads at page 07699:

> ... The further propane is transported, the higher the delivered cost, therefore, the competitive operating area is limited to a reasonable radius of 70 to 80 kilometres around the branch or satellite locations. (emphasis added)

**95** The 1998 Superior Propane Income Fund Annual Report (exhibit R-111, tab 1) reads at page 01189:

> ... The further propane is transported, the higher the delivered cost. Therefore, the competitive operating area is generally limited to a radius of 100 to 400 kilometres around branch or satellite locations. (emphasis added).

**96** The Commissioner also notes that, subsequent to the 1998 Superior annual report, the respondents took the position in their response to the Commissioner's application that Superior's appropriate delivery range is 50 to 300 kilometers.

**97** The respondents dispute that the relevant geographic market is 60 to 100 kilometers radius around Superior-ICG branches and satellites. They submit that Superior's trading areas have radii of 50 to 620 kilometers and that some competitors have even larger trading areas which contradict Professor West's conclusion that competition between propane distributors is limited to firms within a range of 60 to 100 kilometers of a given branch or satellite.

**98** The respondents also submit that Professor West's model has never been used for this type of competition analysis and he has not determined whether his geographic markets "function as markets".

**99** Mark Schweitzer, Superior's Chief Executive Officer, indicated that Superior's branches have been reorganized. For example, he testified that 10 branches have been closed, but most have been converted to satellite locations (transcript at 31: 5911, 5912 (3 December 1999)) so that other branches may serve now larger areas with a radius of 100 to 400 kilometers as stated in the 1998 Superior Propane Income Fund Annual Report (exhibit R-111, tab 1).

**100** The Tribunal is of the opinion that Professor West's analysis, while it does not follow the hypothetical monopolist approach entirely, nevertheless is similar in certain respects to that approach and can be used to identify relevant geographic markets (transcript at 22:3914 (29 October 1999)). Moreover, the respondents have not demonstrated that Professor West's spatial methodology was flawed in any significant respects. The respondents noted that the computer algorithm produced certain anomalies which led certain market boundaries to extend to the Arctic Ocean, but these criticisms were not crucial to the value of Professor West's approach since these are functions of the computer mapping procedure. In addition, the respondents dispute some of his market share calculations.

**101** As to the argument of the respondents that Professor West's markets may not function as markets, the Tribunal is of the view that there is no necessary correspondence between a competition market, which is an analytical construct, and a market defined by management for operational purposes.

**102** Further, the Tribunal notes that the respondents did not present an alternate set of geographic markets for the purpose of competition analysis. Rather, they seemed to suggest that the business-service areas of their branches and satellites were appropriate for this purpose.

**103** The Tribunal notes that Mr. Schweitzer testified that he knew of no branch which could provide service to customers only as far as 60 kilometers or under 90 kilometers, which contradicts Superior's own evidence in some of the 1998 branch templates (e.g., Calgary 50 kilometers). Further, the Tribunal does not find the explanation of Mr. Schweitzer convincing because many of the branches were converted into satellite locations. Therefore, the Tribunal does not understand why converting branches to satellites would modify the boundaries of a geographic market.

**104** The Tribunal notes that there is no evidence that using the furthest distance travelled from a branch constitutes a valid method for defining a relevant geographic market. Further, even if referring to the furthest point of a trading area were appropriate for defining such a market, the Tribunal would be concerned about adopting a method that would be based on the delivery to the exceptional customer located at great distance rather than considering the typical distance travelled for the majority of customers. There is no evidence that a Superior branch whose furthest customer is located 620 kilometers away serves all customers within that distance. Therefore, even if the Tribunal accepted in principle that a branch trading area could be a competition market, it could still not conclude that this trading area would have a radius of 620 kilometers.

**105** The respondents submit that some independent firms serve customers in many of Superior's trading areas and that their travel distances are longer because they have fewer branches. However, it is not clear that such firms serve the entire Superior branch trading area. In addition, serving adjacent Superior trading areas does not necessarily mean that these independent firms deliver propane over longer distances than Superior does. Also, if the respondents were correct in their submissions, it would remain unclear whether these independent firms supply many customers at longer distances; that is, their trading areas may not be measured by the longest distance travelled.

**106** As stated above, the Tribunal does not agree that areas over which market power can be exercised are necessarily coincident with existing business or service areas such as those of Superior. Accordingly, the Tribunal concludes that the "candidate local markets" produced by Professor West's methodology are reasonable and

appropriate for the purpose of identifying the relevant geographic markets in order to determine whether the merged entity will have the ability to exercise market power.

(2) National Accounts

**107** With respect to the geographic market relevant for national accounts, the Commissioner submits that the relevant geographic market for the analysis of the national accounts is Canada. The respondents do not address the relevant geographic dimension for national accounts.

## IV. SUBSTANTIAL PREVENTION OR LESSENING OF COMPETITION

**108** The Commissioner submits that there will be a likely substantial lessening of competition in many local retail propane markets, a likely substantial lessening of competition regarding national accounts and a likely prevention of competition in Atlantic Canada. The Commissioner also argues that there will be a likely substantial lessening of competition by virtue of the creation or enhancement of market power by the merged entity which he attempted to demonstrate with expert and factual witnesses. He argues that market power can be inferred from various factors such as high market shares and concentration, the high barriers to entry, the removal of ICG as a vigorous competitor, the lack of foreign competition and the fact that there is no effective remaining competition.

**109** The respondents submit that the merger is not likely to result in a substantial lessening of competition. They argue that the terms "likelihood of a substantial lessening of competition" are synonymous with "likely price increase" and that the Commissioner failed to demonstrate a likely post-merger price increase. They dispute the Commissioner's definitions of geographic and product markets, rely on the growth of independents' market share, advocate that ICG is not a vigorous and effective competitor and that barriers to entry in the retail propane business are low.

### A. MARKET SHARES AND CONCENTRATION

**110** The Commissioner's expert witness, Professor West, studied the combined market shares of Superior and ICG in 74 local markets for 1997 as stated above. He concludes at page 29 of his report (confidential exhibit CA-2051) that in 17 such markets, the combined market share is between 95 and 100 percent, that 32 markets have combined market shares in excess of 80 percent, that 46 markets have combined market shares of 70 percent, and that 66 markets have combined market shares in excess of 60 percent. In order to get these results, Professor West relies upon a set of completed surveys for the year 1997 that the Commissioner has received from responding propane dealers (the competitor survey) as well as, inter alia, internal business plans and data regarding sales volume and market shares of Superior and ICG. Professor West states that he has relied on Superior's data in the absence of sufficient data provided from competitors.

**111** The respondents criticize Professor West's market share estimates on the grounds that he uses volume information for 1997 and Superior and ICG branch locations for 1998. The Commissioner points out, however, that Professor West does not mix 1998 locations with 1997 volumes and further refers to page 21 of his report to demonstrate that he identifies all of Superior's, ICG's, and other propane dealers' satellite and branch locations in operation in 1997.

**112** Further, the respondents suggested to Professor West during cross-examination that he should have done a "reality check" by aggregating the volumes consumed in his 74 local candidate markets in 1997 with other measures of total consumption for that year. In final argument, they state that there were 200 competitors, only 67 of whom responded to the 1997 competitor survey. They also state that the 1998 volumes of the approximately 140 non-responding competitors would likely be a good estimate of those firms' volumes in 1997 and should have been used. The Commissioner points out that the competitor survey identified and sought responses from 118 competitors and that the figure of 200 is an internal estimate of Superior that includes agents of Superior and of ICG that Professor West specifically tried to eliminate. Moreover, the Tribunal heard evidence that 1998 volumes

declined from 1997 levels due to warmer weather; thus, there would be no reason to assume that the volumes of the non-responding firms would have remained the same in 1998.

**113** The respondents also criticize Professor West's estimates because the total of the 1997 volumes by market differs from the Statistics Canada data on total retail propane demand. During Professor West's cross-examination, the respondents pointed out that the aggregate volume calculated from Professor West's individual market analysis differed from the aggregate number provided by Statistics Canada, as cited by the Commissioner's expert witness, Mr. Mathieson. However, the Commissioner pointed out that the 74 markets identified by Professor West did not cover the entire country. For example, they did not include a large part of the Maritimes, Northern Manitoba or the Territories. In addition, Mr. Mathieson noted that errors in the Statistics Canada data meant that it should only be used to establish trends in propane demand rather than accurate annual estimates of consumption by end-use.

**114** The respondents' experts, Dennis W. Carlton and Gustavo E. Bamberger, criticize Professor West's 1997 market share estimates as being less reliable than information provided to them by Superior. Professor West replies that Superior's share estimates contained in its 1998 branch templates are based on an internal survey prepared after the commencement of the proceedings and conducted by branch managers who have no actual sales volume information for independents for that year (expert affidavit in reply of D. West (20 September 1999): confidential exhibit CA-2052 at 2).

**115** The respondents argue that Professor West does not allocate all of the various independents' volume of propane sold in the relevant geographic markets, as defined by him, and that the allocation is arbitrary. Professor West explained that he used Superior's own market share evaluation when he did not have the sales volume information from other independent competitors (transcript at 22:3931 (29 October 1999)) and that he reduced Superior and ICG's combined market share in some of the geographic markets by several percentage points to reflect the sales volumes of several small competitors for which he did not have specific volume information. The Commissioner states that if Professor West did not have adequate volume data to calculate market share, he did not attempt to invent one in order to allocate some volumes to the market.

**116** Professor West's results, set out at page 29 of his report (confidential exhibit CA-2051), are very similar to a frequency distribution of Superior/ICG market shares that Superior has estimated, apparently based on its branch trading areas. For example, Superior's own analysis indicates that 15 out of 116 branches have a market share of between 95 and 100 percent. Although the methodology of the two studies differ, this result is common to both and gives the Tribunal further confidence in Professor West's analysis.

**117** In addition, the Tribunal has reviewed the criticisms made by the respondents on a market by market basis of Professor West's market share estimates. After careful review of his explanations and methodology (and having examined certain markets in detail), the Tribunal accepts that Professor West's approach is appropriate for a competition analysis in this case and that his inferences and conclusions about market shares are reasonable given the available data and the limitations therein identified by him. The Tribunal is of the opinion that it can rely on these results and conclusions for the purpose of determining whether the merger will result in a likely substantial prevention or lessening of competition.

**118** The Commissioner's experts, Professors Schwindt and Globerman, classify markets on the basis of post-merger market share in their expert report (exhibit A-2056 at 27-41). Using Professor West's relevant geographic markets and market share estimates, they identified 16 local markets in which the merged entity would have combined market shares of 95 percent and higher, which they referred to as "merger to monopoly" markets. At page 28 of their report, they indicate that the merger will substantially increase the probability of a unilateral price increase in these markets.

**119** They further identify eight markets ("category 1"), in which the Superior or ICG pre-merger market share is relatively small. In these markets, the merger may have minimal impacts on competition between Superior and fringe competitors and, therefore, the main concern is the removal of ICG as a potential future competitor (ibid. at

37). In addition, the merger in these markets would eliminate competition for propane buyers who prefer to deal with one of the major companies.

**120** A third set of markets ("category 3") identifies 16 markets in which ICG has a substantial market share prior to the merger but where there are at least three competitors including Superior and ICG. In these markets, Professors Schwindt and Globerman expect that the elimination of ICG is likely to enhance interdependence and reduce competition (ibid. at 38, 40).

**121** The final set of markets ("category 2") includes 33 local markets in which a relatively fragmented fringe of firms compete against Superior and ICG and where the merging parties are the two largest sellers (ibid. at 40). They state that there is a substantial likelihood that the merger will significantly reduce competition in these markets by creating a dominant firm and enhancing interdependence.

**122** The respondents criticize Professors Schwindt and Globerman's analysis of the anti-competitive effects of the merger. First, they submit that Professors Schwindt and Globerman provide no opinion regarding the likelihood of a price increase in any market. Secondly, they submit that even Professors Schwindt and Globerman have minimal concerns about the anti-competitive effects of the merger in their category 1 and 2 markets. Thirdly, they argue that existing competitors will continue to compete vigorously in category 3 markets. Finally, they indicate that entry will restrain the merged entity from imposing a unilateral price increase in merger to monopoly markets.

**123** Further, the respondents' experts, Professor Carlton and Dr. Bamberger, state at page 4 of their report that Professors Schwindt and Globerman accept that the substantial presence of independent retailers can constrain the merged firm from raising retail propane prices (expert affidavit in reply of D.W. Carlton and G.E. Bamberger (14 September 1999): confidential exhibit CR-121). In the Tribunal's view, this is not an accurate characterization of Professors Schwindt and Globerman's opinion.

**124** The Tribunal believes that the respondents have incompletely depicted the opinion evidence of Professors Schwindt and Globerman and it accepts that, although they have not provided a firm opinion on the likelihood or quantum of a price increase, their conclusions regarding the anti-competitive effects of the merger are important and significant for the purpose of determining the likelihood of a substantial lessening of competition. The Tribunal will discuss the entry argument below under the heading "Evidence on Entry".

**125** A key issue in this case is the evaluation of the post-acquisition market share of the merged entity by market. The respondents argue strenuously that the post-merger market share on a national basis has been declining and may have reached between 50 and 60 percent in 1998. These national market shares were introduced to establish the significant growth of independent propane marketers over the period between 1990 to 1998. The Tribunal believes that since relevant geographic markets are local, evidence of high market shares on a local basis cannot be defeated by a trend of national market shares purporting to demonstrate that entry can overcome this substantial lessening of competition.

**126** Information on high market shares is, therefore, relevant but not determinative in respect of a finding of a likely substantial prevention or lessening of competition. However, the Tribunal notes that these market shares must be measured with respect to relevant product and geographic markets. In this case, since no national product market for retail propane has been demonstrated, information on market shares for Canada as a whole are not informative as to the exercise of market power in local markets.

## B. BARRIERS TO ENTRY

**127** As stated by the Tribunal in Director of Investigation and Research v. Hillsdown Holdings (Canada) Limited *(1992), 41 C.P.R. (3d) 289* at 324, *[1992] C.C.T.D. No. 4* (QL):

> In the absence of significant entry barriers it is unlikely that a merged firm, regardless of market share or concentration, could maintain supra-competitive pricing for any length of time. An attempt to do so would cause competitors to enter the market and the additional supplies created in that manner would drive prices back to the competitive level.

**128** This statement emphasises the economic effect of entry. Evidence of commencement of operations, per se, is insufficient to establish the competitive restraint on a supra-competitive price or a likely exercise of market power. Moreover, if the impact on price is delayed beyond a reasonable period, then entry for the purpose of the Act has not occurred even if new businesses have started their operations. The appropriate length of time for judging the impact of entry is a matter of opinion; however, the Tribunal notes that the MEG's, cited above at paragraph [57], refer to a period of two years.

**129** The Commissioner submits that there are high barriers to entry into the propane distribution business. The barriers include the nature and existence of customer contracts and tank ownership, switching costs, minimal required scale, reputation, maturity of the market, the competitive response to entry (including litigation threats), access to propane supply, capital requirements, sunk costs and the time to get the business profitable.

**130** The respondents dispute the existence and/or significance of these barriers mainly on the basis of their evidence of alleged entry and expansion by independent retail propane marketers.

(1) Contracts

**131** The Commissioner's expert, Michael D. Whinston, conducted an analysis of the customer contracts used by Superior and ICG and the likely competitive effects arising from the merger (expert affidavit of M.D. Whinston (18 August 1999): exhibit A-2063). Professor Whinston reviewed the standard form contracts offered by Superior and ICG and found several provisions that could limit entry and/or expansion. These provisions include long-term exclusivity, automatic renewal, termination fees, right of first refusal (Superior only), and tank ownership.

(a) Contract Duration and Exclusivity

**132** It is not disputed that a high percentage of propane customers take delivery under contracts. For example, Superior has estimated that 90 to 95 percent of its customers are under standard form contracts with the remaining 5 to 10 percent under negotiated non-standard contracts (confidential exhibit CA-701 at 06976). The Commissioner's expert, Professor Whinston, provides the same number with respect to ICG. According to Mr. Schweitzer, 70 percent of Superior's propane customers are under five-year term contracts: "Well, our standard that we discussed earlier today has a five-year term in it. My understanding is that about 70 percent of our customers have standard contracts" (transcript at 31:5894 (3 December 1999)).

**133** Professor Whinston notes that long-term exclusive contracts can have both efficiency-enhancing and anti-competitive effects. In the case of propane supply contracts, the term can be as long as five years. This duration limits customer switching and can lead the supplier to offer less competitive prices than it would absent the exclusivity provision. Although sophisticated consumers will take into account the impact of exclusivity and will insist on compensation for the lack of choice for the term of the contract, Professor Whinston suggests that most residential customers may not understand the limitation of choice and the impact of loss of competition for their custom.

**134** Professor Whinston is more concerned about the entry-deterring effect of long-term exclusive contracts for propane supply. Noting that economies of scale appear to characterize the propane delivery business, he suggests that a new entrant will have to acquire enough customers to achieve the minimum efficient scale of operation, failing which the entrant will operate at a cost disadvantage compared to incumbents. In light of the exclusive nature of propane contracts, a new entrant will seek to acquire customers whose contracts with incumbents are expiring, but the long terms may limit the number of such "free customers" in any year to a level at which new entry is not

profitable. He notes that this problem will be more severe when the contract expiration dates are staggered and when the contract terms are longer.

**135** Similar concerns will be raised for existing smaller firms that seek to invest in order to lower operating costs, expand capacity or improve quality. The "free customer" base may not justify such investment.

**136** Professor Whinston adopts the observation made by the Commissioner's expert, Terry Kemp, that the minimum efficient scale for a propane marketer is three million litres per year in order to demonstrate, in a general way, the impact of long-term exclusivity on the profitability of entry and expansion. If the average duration of contracts in a market is four years, then 25 percent of the contracted volume can be expected to come off-contract every year. If one new entrant could attract all of these free litres, then the market would require 12 million litres of total annual consumption in order for that new entrant to enter at the minimum efficient scale. Professor Whinston finds for example that the total consumption in 12 of 71 markets defined by Professor West is less than 12 million litres and concludes that entry will be difficult in these circumstances.

**137** The respondents submit that contract exclusivity is not a significant barrier to entry in this merger because only five markets will have less than 2.25 million litres required to support one new entrant. However, this result flows from assumptions that Professor Whinston regards as unrealistic.

**138** Professor Whinston recalculates the number of markets with minimum required volumes assuming that declining autopropane volumes will not be available to a new entrant in any markets as defined by Professor West, that the minimum efficient scale is six million litres per year and that all customers are on four-year contracts. On this basis, he finds that 37 out of 73 "West markets" will not be large enough to sustain one new entrant, even if right of first refusal clause and other contractual terms are not effective deterrents to switching.

**139** The Tribunal is of the view that the respondents' submission does not represent Professor Whinston's opinion. According to Professor Whinston's estimates, entry and expansion at minimum efficient scale are unlikely in many West markets.

(b) Automatic Renewal

**140** With respect to automatic renewal, Professor Whinston notes that the automatic renewal feature of propane customer contracts serves to increase the effective duration of these contracts, as the notice periods are long. For example, ICG's Fuel Supply and Equipment Agreement requires the customer to give notice of termination of 180 days, absent which the contract will be renewed at expiry for the original term of perhaps five years. Thus, in the event that a new entrant is successful in attracting an ICG customer under this contract, it would have to wait six months before commencing service.

(c) Right of First Refusal

**141** The right of first refusal clause in Superior's contracts also deters entry in Professor Whinston's opinion. Under this provision, Superior has the right to match the price offered by a competing supplier and the customer is required to provide the name of the competitor and its price. The result is that Superior is fully informed of the identity of any rival who is bidding for its customers and is better able to retaliate against it selectively.

**142** The right of first refusal clause greatly reduces the profitability of entry by new firms and expansion by existing firms. Since Superior can retain its customer by matching the new entrant's lower price (i.e., even if the entrant offers better quality service), a rival will have to offer a price that is below Superior's cost to make the offer unprofitable to Superior. Therefore, a rival with higher costs and quality may find a customer interested in switching but it cannot lower its price enough to avoid "matching" by Superior.

**143** The respondents do not challenge Professor Whinston's opinion on this point. Accordingly, the Tribunal

accepts Professor Whinston's opinion that right of first refusal clauses reduce the profitability of entry and expansion.

(d) Tank Ownership

**144** Professor Whinston draws attention to the provisions in Superior and ICG contracts under which they retain ownership of the propane storage tank at the customers' site. This is a feature of all contracts except for Superior's Industrial Agreement to industrial customers and it is a feature of contracts offered by virtually all propane marketers. He concludes that the practice of not selling tanks greatly increases the costs of a customer switching to another supplier. The tank rental requirement makes the customer much less likely to switch than if the tank were owned. Professor Whinston concludes that the rental requirement effectively increases the duration of the long-term exclusive contracts and further reduces the likelihood of new entry or expansion.

**145** Based on the evidence on the record, it appears that switching to an alternate propane supplier typically results in direct and indirect costs. The direct costs would include a restocking cost calculated by Superior at 15 percent of the total value of propane in the tank being removed. Indirect costs to switching include important delays between the time the existing supplier removes its tank and the time when the new supplier installs its equipment. Commercial, industrial, or agricultural customers may have to reduce or stop operations during this period. Residential customers will generally be unwilling to risk the loss of heating, particularly in winter months.

**146** The respondents submit that tank ownership by the marketer ensures proper tank inspection, maintenance and safety practices. They also allege that since independents are growing at the expense of Superior and ICG, tank ownership does not constrain independent entry or expansion.

**147** The Tribunal notes that there is no evidence that tank inspection, maintenance and safety practices have to be tied to tank ownership. Such services could be provided to a customer that owned the tank. Therefore, the Tribunal is of the view that tank ownership by the propane supplier makes customer switching more difficult and costly, and it accepts that it constitutes a barrier to entry and expansion. As to the alleged entry and growth of independents, the Tribunal will discuss that point below.

(e) Voluntary Undertakings

**148** Finally, Professor Whinston notes that Superior has indicated that if the merger is approved it will not enforce term provisions in its existing standard contracts for propane supply, that it will adopt 30-day notice periods in standard form customer agreements, that it will waive liquidated damages terms, and that it will waive right of first refusal provisions. He believes that these voluntary undertakings do not adequately address his concerns about the competition-reducing effects of Superior's and ICG's customer contracts. For example, he notes at paragraphs 97 to 104 of his report (exhibit A-2063) that Superior has not committed to actually advising its customers of these changes.

**149** The respondents submit that Superior and ICG do not enforce the provisions of their standard form contracts. Further, the respondents submit that only a few letters have been sent to customers and competitors in the last seven years addressing Superior's and ICG's legal rights but that neither Superior nor ICG has commenced litigation in regard to the matters raised in these letters.

(f) Conclusion on Contracts

**150** The Tribunal accepts that the provisions in the contracts, including long-term exclusivity, automatic renewal, termination fees, right of first refusal (Superior only), and tank ownership significantly raise the cost of entry and expansion and hence constitute a barrier to entry.

(2) Competitive Response to Entry

**151** An important component in the decision to enter the market is the assessment of the likelihood of a competitive response from the incumbents in the marketplace. The Commissioner introduced evidence in support of his argument that retaliation constitutes a response to competitors who have taken business away from Superior. This competitive response is generally in the form of intense price competition targeted at the entrant in order to affect its ability to compete in the market.

**152** The experience of Imperial Oil Limited ("IOL") demonstrates that even very large and sophisticated companies may not be able to enter the propane distribution business profitably. In 1990, IOL, the largest propane producer in Canada (following the Texaco merger), sought to expand its activities into propane distribution. The project manager, Meredith Milne, testified that IOL experienced a vigorous response from competitors following its attempt to enter the propane market. It found that margins were 30 percent lower than planned and 45 percent lower than in 1991. IOL found that incumbent marketers started to charge customers switching to IOL for tank removal and that they removed the tank rental charges.

**153** In addition to the competitive price response, IOL also found that it was difficult to get customers to switch due to the multi-year contracts and the "last look on tenders" available to incumbents. These were all elements that either increased IOL's costs or made it difficult to gain new accounts with the result that IOL exited the market (transcript at 13:1976 (15 October 1999)). Based on the evidence, the Tribunal notes that no other entry by companies of similar size or stature has occurred in this industry.

(3) Reputation

**154** The lack of a reputation for reliable supply and service can be an entry barrier. Reputation may be a crucial element in gaining customers, especially when services are an important element of the product.

**155** The Commissioner submitted evidence that reputation constitutes a barrier to entry in the propane supply and delivery market. In addition, the Commissioner's expert, Professor Globerman, stated that the incumbents had reputational advantages, which means that the entrant is likely to take longer to establish that critical mass in demand. The Canadian Market Research Study commissioned by Superior in October 1997 (confidential exhibit CA-1485) reads at page 17416:

> ... commercial and residential markets display a significant lack of awareness and familiarity with alternative suppliers.

Further, at page 17437:

> Currently, four in ten (39%) Superior [commercial] customers are not aware of an alternative propane supplier on an unaided basis .... ICG is the most formidable competitor in Ontario and Quebec .... 64% of competitor customers have unaided awareness of the Superior brand and 29% designate it as the alternative supplier with which they are most familiar.

And at page 17527:

> Residential propane users also exhibit a fundamental lack of awareness and familiarity with the range of alternative suppliers (more pronounced than the commercial market) ....
>
> In the shot [sic] term, competitive threats may be limited. Currently 58% of Superior customers are not aware of an alternative propane supplier on an unaided basis, and 74% say they are not familiar with an alternative.

**156** The respondents submit that the existence of a "proven track record", as in the case of Superior and ICG, is not an impediment to competition; rather, it is the natural result of competition.

**157** Loyalty is a related consideration. The Commissioner presented witnesses from cooperatives and credit union organizations whose sellers offer propane and give dividends to member customers based on such purchases. These customers have an incentive to continue to be loyal to their propane supplier. Based on the evidence submitted by factual witnesses, the Tribunal accepts that reputation is an important feature of propane suppliers to which customers attach value. It appears that this is particularly true for major account customers whose factual witnesses testified that the reputation of the companies capable of delivering propane is an important factor in their purchasing decision. The Tribunal notes that the time to gain a reputation may make profitable entry more difficult and hence delays the competitive impact that an entrant would have in the marketplace.

(4) Maturity of Market

**158** The Commissioner called witnesses who testified that the market was mature and that the demand was flat (see testimony of John A. Osland from Mutual Propane, transcript at 6:833 (4 October 1999) and testimony of Luc Sicotte from Gaz Métropolitain, transcript at 18:3148 (25 October 1999)). Mr. Schweitzer testified that it was a relatively mature market (transcript at 31:5920 (3 December 1999)).

**159** The Commissioner's experts, Professors Schwindt and Globerman, testified on the competitive impact of this mature market at page 48 of their report (exhibit A-2056):

> ... the industry is mature and has experienced slowly declining demand in recent years. As noted in the Merger Enforcement Guidelines, entry into start-up and growth markets is less difficult and time consuming than it is in relation to mature market.

**160** In light of the evidence submitted, the Tribunal is satisfied that the traditional retail propane market place can be qualified as mature.

(5) Access to Propane Supply

**161** The Commissioner refers to the opinion of many competitors that the ability to access propane supply is a "critical barrier to entry/expansion". Evidence in this regard consists of the disadvantages that independent firms face in obtaining supply that Superior and ICG do not face. For example, the respondents have established supply relationships and have invested in storage and transportation facilities that provide cost advantages over rivals who may be restricted to local pick-up from refinery racks. These arrangements are apparently valuable for serving branches particularly distant from refinery sites. Superior and ICG also have "scale demand" for propane which gives them an edge over traditional patterns of supply.

**162** One of the Commissioner's experts, Terry S. Kemp, observes at pages 15 and 16 of his report (expert affidavit of T.S. Kemp (18 August 1999): exhibit A-2070) that:

> Sup-ICG with the exception of a few selective refineries, will have access to supply at virtually every producing location in the country. Sup-ICG will thus have an implied supply advantage and flexibility that cannot be matched by any other retail propane competitor.
>
> Sup-ICG should be able to selectively choose the most advantageous supply locations and drop others, thereby extracting the most out of supply arrangements. Sup-ICG will also be in a position to leverage supply from location to location for trades and exchanges and, will in essence, be able to create preferential access to supply and location adjustments. These advantages can be utilized in a number of ways:

. Pressuring supplier price location arrangements

. Using competitive advantages when bidding on new contracts

. Servicing National accounts

. Negotiating more favourable bulk transportation rates (volume discounts) with trucking and rail companies.

**163** The Commissioner's expert, Mr. Mathieson, notes that the respondents have access to supply at prices more favourable than simply the posted or rack price. Mr. Kemp pointed out that propane producers generally prefer to supply those who have the ability to lift product on a regular basis. A new entrant would not be able to immediately demonstrate this ability and would be at a disadvantage to the respondents. The Commissioner's witness, Peter Renton of Gulf Midstream Services Ltd., confirmed that his company prefers customers who perform very well over those customers who fail to take a significant portion of their product each year and to whom sales would be reduced and rack prices charged.

**164** The Commissioner cites the Ontario Region 5 Year Strategic Plan from Superior (confidential exhibit CA-299) that indicates Superior's view that it creates barriers by "tying-up supply", specifically its ten-year supply arrangement with Shell. The respondents point out that the independent marketer, AutoGas, has a ten-year arrangement with IOL.

**165** Mr. Kemp observes at page 15 of his report (exhibit A-2070) that Superior's propane cavern storage allows it to purchase spot volumes at low prices and Mr. Mathieson is concerned that Superior's supply transportation costs are the lowest in the industry.

**166** The testimony indicates that in periods of tight demand, producers ration their supplies and give preference to their largest customers, causing some independents to deal with brokers. However, no independent testified that it could not obtain propane. The expert opinion evidence states that the merged entity will have advantages in acquiring propane that smaller competitors will not enjoy. The Tribunal accepts that new entrants and small firms seeking to expand bear the costs of investing in reputation with propane suppliers that incumbents do not have to bear and, to that extent, they face entry barriers. However, these costs are not a result of the merger and are not increased by it. Other advantages that reduce the cost of propane acquisition (such as buying at low "off season" prices and storing) to the respondents and the merged entity reflect efficiencies and do not create barriers to propane acquisition. The Tribunal does not agree that the new entrants and expanding firms face significant barriers to obtaining propane supply.

(6) Capital Requirements/Sunk Costs and Time to Get Business Profitable

(a) Scale of Entry or Expansion

**167** Several of the Commissioner's witnesses (Professors Globerman and Schwindt, Messrs. Kemp and

Mathieson) note in their expert reports that entry into the propane business is costly. Mr. Kemp, for example, suggests at page 7 of his report (exhibit A-2070) that the capital costs for a start up greenfield retail propane operation are in the range of $675,000 to $920,000 to support initial sales of two million litres per year which he regards as minimally-required for success. He estimates operating costs, at page 9 of his report, at approximately $300,000 per year. Several fact witnesses mentioned the high costs involved in obtaining storage tanks, transport and delivery trucks and customer tanks, particularly when certain customers have requirements for on-site storage.

**168** The respondents have submitted in their amended response that one can enter the propane distribution business for a total investment of $120,000 to $300,000. The Commissioner submits that even if entry of that scale is possible in certain geographic locations, the respondents have understated the costs for the most part. According to the Commissioner, such a small entrant would be an uncommitted entrant, unable to constrain Superior/ICG's market power.

**169** The Commissioner argues therefrom that high capital costs are themselves a barrier to entry, ostensibly on the basis that few people had the required financial resources to enter the industry. Competitors in the industry testified to the effect that costs of entry may vary. It cost Donald J. Edwards $935,000 to construct EDPRO Energy Group Inc.'s facility in London, Ontario, excluding the purchase of tanks for customer use (transcript at 6:1072, 1073 (6 October 1999)). Evidence was also submitted indicating that costs associated with meaningful entry might vary upon the end-use served.

**170** The Tribunal does not accept that high capital costs are inherently a barrier to entry. If a potential entrant's equity is insufficient to cover capital costs of entry at minimum efficient scale, then the balance can be obtained through credit markets providing that lenders are satisfied that the project is viable. In the event that lenders deny credit because of their assessment of the project, their reluctance to lend does not indicate that capital is not available. In response to a question from the Tribunal, Professor Schwindt stated that high costs, per se, did not constitute an entry barrier.

**171** On this latter point, the Commissioner accepts that high capital costs are not, in absolute dollars, an issue relevant to entry; rather, the relevant costs to be considered are the sunk costs because they represent what the entrant will lose in the event of failure.

(b) Sunk Costs

**172** It is generally agreed that the portion of costs that are not recoverable in the event of exit (the sunk costs) can, where they are significant, constitute a barrier to entry. The Commissioner suggests that the retail propane market is characterized by significant sunk costs. There is a dispute between the Commissioner and the respondents as to the proportion of the costs that can be qualified as sunk costs. The extent of these costs depends on a variety of factors.

**173** In the propane industry, the sunk costs would include the market development costs, site-preparation costs, and the discounts to purchase price that would be incurred on asset disposals. Mr. Milne of IOL estimated that 50 percent of its costs were non-recoverable when IOL entered the Camrose market. Mr. Katz from AmeriGas indicated that 30 to 80 percent of investment in propane operations would be non-recoverable. As well, salaries and other operating costs incurred to the date of exit would also be non-recoverable. The respondents' experts, Cole Valuation Partners Limited and A.T. Kearney (expert affidavit of C. O'Leary and E. Fergin (17 August 1999): confidential exhibit CR-112), recognize at page 202 of their report that certain costs are sunk. For example, they assume decommissioning costs of $50,000 per site for locations to be closed, which costs would be non-recoverable.

**174** The Commissioner's experts, Professors Schwindt and Globerman, emphasize the sunk cost of time required for a new entrant to develop a reputation for reliability, as well as for obtaining the necessary permits to install

storage capacity. They also characterize at page 49 of their report (exhibit A-2056) as sunk the cost penalty of operating below minimum efficient scale.

**175** The Tribunal is satisfied that sunk costs are meaningful in the industry and constitute a significant obstacle to a new entrant.

(7) Evidence on Entry

**176** The respondents seek to demonstrate that barriers to entry are low by presenting evidence on actual entry over time by independent firms. The respondents have chosen to rely, for the most part, on evidence of growing market shares of independent firms rather than presenting evidence contrary to each of the Commissioner's submissions regarding barriers to entry.

**177** The Commissioner submits that barriers to entry are high and that small scale entry is not an unusual event, but that entry occurs at a relatively low scale and expansion of entrants appears to be both modest and slow. Professors Schwindt and Globerman submit at page 53 of their report (exhibit A-2056) that small scale entry has occurred in the marketplace and that there is considerable turnover or "churn" among small scale entrants. They cite the membership list of the Propane Gas Association of Canada and state that there were 41 new memberships from 1994 to May 1999. They also find that 22 of those members had left the association by mid-1999. Further evidence from Superior also suggests that both entry and exit by small firms are high. Superior indicates that 45 new firms have entered the market since 1996. However, there is only one example of large scale entry, which is IOL's entry into the agricultural, commercial, industrial and automotive segment in western Canada. As noted above, this attempted entry failed.

(a) Basic Trend (1988-98)

**178** The respondents submit that there have been 45 new entrants across the country in the past three years, that there is no evidence of business failure, and that ICG's volume has declined by 26 percent due to its inefficiency over a period of eight years when the national demand for propane increased and independent volume doubled. The respondents further assert, on the basis of Superior's best estimates, that independents have increased their share of retail propane sales from 17 percent in 1989 to 42 percent in 1998 (exhibit R-111, tab 5). They also submit that independents have grown from 24 percent in 1990 to 46 percent in 1998 based on Statistics Canada data.

**179** At the hearing, the respondents introduced numerous calculations of Superior/ICG's combined market share, including a chart handed up in final argument ("Comparison of SPI Estimates Over Time with Statistics Canada Estimates Over Time") comparing Superior's internal market share estimates to market share estimates based on Statistics Canada data from 1988 to 1998. This chart demonstrates that Superior and ICG had a combined market share of 81 percent in 1988. This estimate arises from the market share estimates reported in the Minutes of Norcen Energy Resources Limited Board of Directors meeting on October 11, 1988 (exhibit R-88), in which Superior estimated its market share to be 41 percent, ICG to be 33.1 percent and Premier Propane Inc. ("Premier") to be 6.6 percent. The respondents submit that the Superior/ICG's combined market share was down to 60 percent in 1998 on the basis of market share estimates contained in the 1998 branch templates (exhibit R-111, tab 2).

**180** In response to this chart, the Commissioner points out that the 1988 share of 81 percent includes the volumes of Premier despite the fact that Superior did not acquire Premier until 1993. It is not clear to the Tribunal why Premier's volume was included in the respondents' 1988 combined market share estimate as that volume could not have contributed to the market power of a combined Superior and ICG in that year. Excluding that volume would indicate a 1988 combined Superior and ICG volume of approximately 74 percent.

**181** With regard to the 1998 estimate of 60 percent, the Commissioner submits that this estimate is not accurate. The Commissioner notes that in order to get to this estimate, the respondents calculated the total volume of each branch trading area using the Superior branch manager's estimate of Superior's market share in that area and

Superior's actual volumes for the branch from the 1998 branch templates. The respondents calculated the volumes of ICG and the independents by using that total volume number and the branch manager's volume estimates for competitors to calculate the market shares of ICG and the independents.

**182** According to the Commissioner, in a further adjustment of this 60 percent estimate, the respondents added 133 million litres based on the difference between the total independents' volumes reported in the 1997 competitor survey compiled by the Commissioner and Superior's 1998 estimates of independents' volumes. Adding this 133 million litres to the total volumes estimated by the branch managers led to a combined market share of 58 percent for Superior and ICG in 1998. This adjustment of the estimate assumes that the independents sold as much in 1998 as in 1997 despite the warmer weather and other factors that allegedly depressed the industry wide volumes.

(b) 1998 Branch Templates

**183** The Commissioner submits that the data supplied by the 1998 branch templates to arrive at approximately 58 percent are flawed and conflict with the historical and current position taken by Superior and ICG in their public disclosure statements, the industry practice and other data before the Tribunal.

**184** The Commissioner submits that the 1998 branch templates are flawed for various reasons. The Tribunal notes that it remains unclear whether Superior's own estimated market share for a branch area includes sales to agents. Indeed, Mr. Schweitzer could not confirm at the hearing which approach was used by the branch managers who prepared the templates; he indicated that different approaches may have been used by Superior's branch managers. Further, according to him, the estimates were reviewed at Superior's corporate office and "followed up where inconsistencies arose" (transcript at 32:6109 (6 December 1999)). This part of the process also remains unclear.

**185** In addition, Mr. Schweitzer testified that he expected that the branch managers estimated competitors' volumes by looking at the physical delivery equipment of the competitors which they could observe by driving down the road past the competitors' locations and estimating the number of litres "typically" delivered in a year by those types of vehicles (transcript at 35:7000-02 (9 December 1999)). These estimated volumes were then apparently used to estimate competitors' market shares.

**186** The Tribunal is of the view that the apparent capacity of competitors does not provide an appropriate estimate of sales volumes as conditions change. As an example, a competitor with 15 percent of truck delivery capacity in the market would not necessarily reduce that capacity quickly in the event of warmer weather or reduced sales volumes. There is no evidence that there is a direct correlation between the equipment that a competitor may have and the actual volume of propane sold by that competitor in the marketplace. Further, looking at the equipment is not informative of the intensity with which the assets are used. For example, it does not reflect how much propane is contained in a truck or how often it is filled up in a given week.

(c) 1998 Actual Volumes

**187** The Commissioner notes that actual volumes for 1998 for Superior and ICG were approximately 1.23 billion litres and 0.92 billion litres, respectively, for a combined total of 2.15 billion litres according to the Commissioner. According to internal Superior documents, Superior's management believed that its market share was unchanged at 40 percent since 1996. Using its stated approach, Superior management would have estimated total propane demand for 1998 as 3.08 billion litres (i.e., 1.23/0.4 ), and on this basis, would have concluded that the combined market share of Superior and ICG was 70 percent (i.e., 2.15/3.08). Internal Superior documents show that this was in fact the combined share that Superior management believed at the time when it was studying the acquisition of ICG.

**188** However, after reviewing its branch templates in 1999, Superior's management concluded that the combined market share for 1998 had declined. For the first time apparently, Superior's management determined that the

Statistics Canada estimate of total market demand, 3.95 billion litres in 1998, was the appropriate base for Superior's and ICG's combined share estimate and then calculated a market share of 54 percent using combined actual volumes (i.e., 2.15/3.95).

**189** The Commissioner attributes the decline in the 1998 volume to industry-wide factors. Indeed, the 1998 Superior Propane Income Fund Annual Report (exhibit R-111, tab 1) reads at page 01194:

> Gross profits of $203.5 million in 1998 (16.6 cents per litre of propane sold) declined from 1997 levels by 3%. Propane sales volume in 1998 were 14% lower as a result of reduced heating demand due to weather that was on average 12% warmer than 1997, reduced demand for auto propane due to a declining number of propane powered vehicles, lower oil field activity given the dramatic fall in oil prices in early 1998, and lower crop drying volumes in 1998 due to dry weather and low crop prices.

On this basis, the Commissioner disputes the respondents' claim that the decline in volume in 1998 was due to a decline in combined market share.

**190** In addition, the Commissioner's expert, Mr. Mathieson, estimated the 1998 retail demand to be three billion litres even though the Statistics Canada estimate for that year was 3.95 billion litres. Mr. Mathieson noted that Statistics Canada numbers were useful for establishing directional trends in demand in the industry, but that its annual consumption figures were distorted due to double counting. Until Superior management reviewed the 1998 branch templates in 1999, it did not accept Statistics Canada data and it believed that the combined market share was approximately 70 percent. Moreover, in the spring of 1999, Superior's management was of the view that Superior's market share was in excess of 40 percent of the estimated Canadian retail propane market and that there was no evidence at the time that Superior was losing market share to independents (see testimony of M. Schweitzer, transcript at 31:5861-84 (3 December 1999)).

**191** The Commissioner submits that the respondents have manipulated various data to show that Superior and ICG have been respectively losing market shares since 1989. The Commissioner notes further that Superior did not report this significant decline in its market share to its investors through its quarterly reports. Indeed, in the Commissioner's view, other sources of information for the year 1997, including the competitor survey, the business case and figures prepared by the respondents in preparation for the acquisition of ICG by Superior suggest otherwise.

**192** The Commissioner is critical of Superior's upward adjustment of 133 million litres to its estimate of independents' 1998 sales volumes in the 1998 branch templates summary. The Commissioner argues that an accurate estimate would reflect the decline in industry-wide demand in 1998, which was known when the templates were being prepared and analysed in 1999. The Commissioner argues that since the actual volumes of Superior and ICG has fallen by approximately 14 percent in 1998, the estimates of independents' volumes should be reduced by a similar percentage.

**193** The Commissioner points out that branch managers estimated 1998 competitor sales volume and market share by observing competitor capacity (e.g., number and size of trucks) in 1999, which likely overestimated 1998 sales volumes. He asserts that, although propane demand generally declined, capacity likely did not.

**194** Relying on Statistics Canada annual volume figures showing a decline in demand in 1998 of 511 million litres, the respondents reply that independents' aggregate volumes declined by only six percent. Further, these changes result in an increase in independents' aggregate market share of three percentage points that matches the equivalent decline in the combined market share of Superior and ICG.

**195** The Tribunal accepts the expert evidence of Mr. Mathieson that Statistics Canada data do not reflect actual demand for a given year, and hence doubts that propane demand declined by 511 million litres in 1998. As a result, the Tribunal is not persuaded by the respondents' submission that the independents' aggregate market share increased by three full percentage points in 1998 or that the combined share of Superior and ICG declined by three

percentage points.

(d) Other Sources Recognizing a Combined 70 Percent Market Share

**196** Various sources state that Superior and ICG have had so far a combined market share of 70 percent, that the total Canadian retail propane market has been in the order of 3.5 billion litres per annum and that it has remained stable for about the last 10 years.

**197** In 1996, Petro-Canada assisted by a consultant, Arthur D. Little, carried out a valuation of ICG's business. The study entitled "Petro-Canada - ICG Business Valuation" (confidential exhibit CA-1019), dated September 19, 1996, concludes at page 21997 that baseload propane equals 2.4 billion litres (Superior 45 percent, ICG 29 percent, regionals 16 percent, and independents 10 percent), and that autopropane equals 1.2 billion litres (Superior 45 percent, ICG 29 percent, regional 16 percent, and independents 10 percent).

**198** In 1998, the ICG prospectus and the information circular all referred to ICG maintaining an approximate 30 percent market share (exhibit R-47, tab 65, at 04373):

> 4.2 Who are your major competitors in the markets you serve ?
>
> Superior Propane Inc. is the largest Propane Company in Canada with approximately 40 % market share. Together, ICG and Superior serve approximately 70 % of the market. In most geographic areas, ICG has a 35-40 % market share or greater except for Ontario, where ICG is in the 15% range and the Maritimes where ICG is a small player. The rest of the market is served by 10 regional and 60 small independent competitors. Within the smaller participants the industry is very dynamic, with buyouts, startups and exits occurring regularly; however ICG's and Superior's combined market share has not materially changed in the past five years. (emphasis added)

**199** With respect to Superior's estimates, the Tribunal notes that a detailed analysis of the propane market in 1995-96 was conducted by Superior ("SPI Market Assessment 1995/96": exhibit A-10). This study, which examines each geographic market and end-use across the country, concludes that Superior holds 43 percent, ICG, 29 percent and others, 28 percent of the Canadian retail propane market. This study also states at paragraph 2 on page 00251:

> ... The sum of these Market estimates, which should theoretically be equal to total retail propane demand in Canada, was 3.45 billion litres, 13 % lower than Statistics Canada's latest estimate of 3.95 billion litres. (emphasis added)

**200** In 1996, Mr. Schweitzer attended and participated in the due diligence process which led to the 1996 Superior Propane Income Fund Annual Report. The prospectus, dated September 25, 1996 (exhibit A-202), states at page 03899:

> ... Superior operates in all ten Canadian provinces and one territory and is the country's largest and only national retail propane marketer with total sales volumes representing in excess of 40 % of the total estimated Canadian propane retail market. Although demand varies within market segments, overall market demand for propane is stable and Superior's size and breadth have historically resulted in consistent sales volumes. (emphasis added)

**201** The 1997 Superior Propane Income Fund Annual Report (exhibit A-712), which was released in the spring of 1998, confirms at page 07697 that Superior generates sales volumes "in excess of 40 percent of the total estimated Canadian retail propane market".

**202** Peter Jones, formerly Vice-President of Western Operations of Superior, prepared a business case document (confidential exhibit CA-193) when he was at Superior in May 1998 after the publication of the ICG prospectus. At pages 03374 and 03380, the document shows a 41 percent market share for Superior and a 32 percent market share for ICG, on the basis of national volumes of 3.321 billion litres of propane in 1997.

**203** The 1998 Superior Propane Income Fund Annual Report (exhibit R-5, tab 161) also states at page 01693 that "[t]ogether, Superior and ICG serve approximately 300,000 customers through 250 branches and satellite units, representing approximately 70 percent of the Canadian retail propane market" (emphasis added).

**204** The Tribunal also notes that even the quarterly report dated October 27, 1999 of Superior Propane Income Fund (exhibit A-3126), which was issued after Mr. Schweitzer became aware of the alleged drop in Superior's market share following Superior's review of the 1998 branch templates, does not report any change to that effect or any correction to the 1998 estimate previously presented. Indeed, page 1 of the quarterly report states:

> ... Results from the operations of Superior and ICG remained soft this quarter, largely due to lower overall propane demand experienced during the third quarter and pressure on margins, as wholesale propane costs continued to rise with the upsurge in crude oil pricing. Soft second and third quarter performance is not unusual in the propane business. Over 60 % of cash flow is usually generated during the winter October through March heating season. As crude oil prices have recently moderated and economic conditions have improved, the outlook for 1999 remains unchanged. (emphasis added)

**205** Therefore, it appears to the Tribunal that Superior chose not to report the alleged decline in Superior/ICG's historical 70 percent share of national propane sales to its investors through its quarterly reports.

(e) Conclusion on Market Shares

**206** The evidence suggests that the retail demand for propane was approximately 3.5 billion litres per year up to and including 1997. Similarly all the evidence, except Superior's 1998 branch templates summary, indicates that Superior's and ICG's market shares were approximately 40 percent and 30 percent, respectively, up to and including 1998. In contrast to the evidence stated above regarding Superior's and ICG's market shares, the 1998 branch templates estimates suggest that Superior's and ICG's market shares were 34 percent and 26 percent, respectively, in 1998. This single estimate apparently caused Superior's management to conclude that the drop in the 1998 volume resulted from the penetration of independents in the retail propane business rather than to the warmer weather during that year.

**207** The Tribunal has considerable doubt about the accuracy and validity of the information contained in the 1998 branch templates and hence in the branch templates summary for 1998. It appears to the Tribunal that the methodology for collecting and compiling the data was unsound. For example, errors by branch managers led particularly to double counting of propane volume sold by agents. Moreover, the branch managers' assessment of market shares of competitors were adjusted at Superior's corporate office so as to achieve agreement with Superior's total market size estimate. It appears that the branch templates and the summary thereof are flawed. Errors were made by some branch managers in completing the survey; the procedure for inferring competitor volume and market share from observed capacity likely overstates volume and sales. The Tribunal finds it surprising that Superior's branch managers were unaware until recently of the significant growth of independents' market shares over a ten-year period, but were able to provide accurate estimates of competitors' volume for 1998. Finally, the Tribunal is of the opinion that Superior's management did not properly design the questionnaires, collect the data, or ensure quality control to the extent needed to ensure reliability. Consequently, the Tribunal does not place any weight on the respondents' evidence regarding market shares from the branch templates.

**208** The Tribunal is further concerned about the addition of 133 million litres for the year 1998 to the competitors' aggregate volume in the branch templates summary. This addition was apparently done in recognition that the

branch templates summary understated competitor volumes for 1998 in comparison to 1997. The Tribunal believes that such adjustment was inappropriate given that industry-wide volumes declined in 1998.

**209** As noted above, the decline appears due to warmer weather and reduced economic activity in certain propane end-use segments. Given its concern about the branch templates, the Tribunal cannot attribute Superior's and ICG's decline in volume to the suggested increased penetration of independents. Indeed, aside from the 1998 branch templates, there is no evidence to support the changes in market shares claimed by the respondents. The evidence submitted for the period 1988 to 1998 and even for the year 1999 supports the stability of Superior and ICG's combined market share.

**210** As mentioned earlier, the Tribunal accepts that relevant geographic markets are local. Therefore, evidence of high market shares on a local basis can only be rebutted by evidence that entry on a local basis can constrain the exercise of market power. No evidence of that nature has been adduced in this case. Instead, the respondents rely for their evidence on entry and expansion on an alleged declining trend in the combined market share of the merging parties.

**211** In light of the evidence, the Tribunal cannot accept the assertion of the respondents regarding entry and expansion. The Tribunal is of the view that there have been no significant changes in Superior's and ICG's market shares that would suggest such a penetration by independents.

### C. REMOVAL OF A VIGOROUS AND EFFECTIVE COMPETITOR

**212** The Commissioner submits that the merger will result in a loss of an effective and vigorous competitor in the market. The Commissioner points out that Superior's own view is that ICG is an important competitor. Based on its internal documents, Superior refers to ICG as its "key-most" important competitor, to ICG's low prices and its low costs, that ICG uses discounted price to acquire new customers, etc. In addition, the Commissioner refers to the affidavit sworn by Mr. Jones in support of the section 100 application in which he said that under his management, ICG would continue as a vigorous competitor to Superior. In his testimony, Mr. Schweitzer also testified that ICG was Superior's most frequent competitor (transcript at 35:6925, 6926 (9 December 1999)).

**213** The Commissioner also refers to the prospectus of September 25, 1996 for the 1996 Superior Propane Income Fund (exhibit A-202) which states at page 03897:

> In addition to Superior, ICG Propane Inc. ("ICG"), which is wholly-owned by Petro-Canada, is the only other retail propane marketer with substantial interprovincial operations. Superior and ICG share approximately three quarters of the Canadian retail market with the balance of the market served by local and regional marketers.

**214** Finally, the Commissioner submits that innovative programs such as the Cap-It program and the Golf-Max program are not offered by any other competitor. The Commissioner argues that the Cap-It program has given ICG a competitive edge over its competitors, including Superior.

**215** The respondents argue that ICG is an ineffective and inefficient competitor. They refer to the testimony of Mr. Sparling who stated that "[i]n the markets where we are we have not seen them as an effective competitor" in support of that argument (confidential transcript at 6:122 (14 October 1999)). They also rely on Mr. Jones's evidence, who described ICG's inefficiency by reference to various cents per litre ("cpl") measures tied to ICG's declining volumes such as operating costs generally and administrative, fleet and delivery costs in particular (transcript at 35:7056-67 (9 December 1999)). They also rely on the expert evidence of Professor Carlton and Dr. Bamberger, who testified that their research was consistent with the evidence that independents, not ICG, constrain Superior's pricing.

**216** The Tribunal is not persuaded that ICG is an ineffective competitor. First, Professor Carlton's analysis of gross

margin and earnings before interest, taxes, depreciation and amortization ("EBITDA") in his report (expert affidavit of D. Carlton (17 August 1999): confidential exhibit CR-120) shows at table 2 that from 1994 to 1998, ICG's average gross margin, as a percentage of total revenue, was 44.7 while Superior's was 44.5. Similarly, table 3 of his report shows that ICG's average EBITDA, as a percentage of total revenue, was 11.2 and Superior's was 12.9 over the same period. These numbers may indicate that Superior's financial performance was somewhat better than ICG's but do not indicate that ICG was an ineffective competitor.

**217** Secondly, at page 12 of their report in rebuttal (expert rebuttal affidavit of R. Schwindt and S. Globerman (15 September 1999): confidential exhibit CA-2078), the Commissioner's experts, Professors Schwindt and Globerman, reviewed Professor Carlton's analysis of customers gained and lost which tends to show that Superior loses more or gains fewer customers to or from independents than to or from ICG . They challenge that conclusion noting the case of Bromont, Quebec, where the average size of an account challenged by ICG is three times greater than the average size of an account challenged by an independent. Thus, while ICG may figure in fewer competitive challenges with Superior compared to independents, it is a strong and aggressive competitor for large volume accounts. Accordingly, what appears to Superior as weak competition from ICG may simply be ICG's strategy of competing more intensively for larger accounts which are smaller in number than smaller accounts.

**218** Thirdly, the Tribunal reviewed the answer to undertaking 150 given by ICG on its examination for discovery. It provides a list of 18 services provided by ICG such as the Cap-It program, the Golf-Max program, the Auto-fill program, the SOS Cylinder Delivery and the Aquaculture program. This list also shows which competitors offer or do not offer such services by region. The Tribunal concludes that ICG is an important and aggressive competitor seeking to attract customers with these specialised services.

**219** It appears to the Tribunal that the respondents' submission concerns ICG's alleged financial performance rather than ICG's presence as an effective competitor in the market. The evidence before the Tribunal shows that ICG actively solicits customers from among the largest consumers and through specialised programs, that consumers from various end-uses recognize ICG as an alternative, that consumers use ICG to negotiate prices with Superior and that ICG's market share continues to be approximately 30 percent as indicated above. This evidence does not support the argument that ICG is an ineffective competitor. Professor Carlton's remaining evidence in this regard will be reviewed below.

## D. FOREIGN COMPETITION

**220** The Commissioner suggests that foreign competitors do not provide effective competition. The respondents' expert, Professor Carlton, suggests at paragraph 21 of his report (confidential exhibit CR-120) that propane distributors in border states can enter the Canadian market in the event of a post-merger price increase and that the 10 largest propane retailers in the United Sates have over 1,500 retail locations in states that border Canada. However, as the Commissioner points out, entry by propane marketers from the United States has been virtually non-existent in the past.

**221** There are three ways in which a propane marketer from the United States could enter the Canadian propane industry: (1) by serving border locations from existing storage points in the Unites States; (2) by establishing branches in Canada; and (3) by acquiring a Canadian propane marketer. The only evidence of any of these alternatives is that of Professor West's reference to the American company, Lake Gas, located in International Falls, Minnesota, which sells a small volume (50,000 litres of propane) directly across the border in Fort Frances, Ontario.

**222** There is no evidence that a propane marketer from the United States has ever established a branch in Canada. In early 1998, Gaz Metropolitan Inc. indicated its interest through a partnership with AmeriGas, one of the largest propane marketers in the United States, in acquiring ICG. No transaction was concluded and there is no other evidence of successful entry through acquisition by an American propane distributor.

**223** In addition to the barriers to entry discussed above, and for a variety of reasons including billing systems, foreign currency, language and different measurement systems, it appears to the Tribunal that American firms are unlikely to provide effective competition to the merged entity in the Canadian retail propane market.

## E. EFFECTIVE REMAINING COMPETITION

**224** The Commissioner alleges that competition following this merger will be weak and ineffective. The Commissioner refers in particular to evidence that shows that Superior and ICG are the price leaders and that the independent firms typically follow the prices set by Superior and ICG. Hence the disappearance of ICG would remove the only significant constraint on Superior's ability to set prices.

**225** Regarding the effectiveness of independent competitors and the constraining role of ICG, the respondents present the expert testimony and report of Professor Carlton, which will be addressed below. Other evidence suggests that the Commissioner's concern for effective remaining competition is well founded. For example, the merged firm will be the only one in Canada with the capability to serve national accounts at the level of service currently offered by Superior or ICG. None of the remaining firms can offer that level of service effectively and hence will not be effective competitors to the merged firm for the business of national accounts.

**226** According to Superior, there are up to 200 independent firms. The Commissioner points out that many of these firms are agents of the merging firms or are associated with them as "bulk dealers". A bulk dealer purchases propane, takes title to the product, and agrees with either ICG or Superior to market in well defined territories. With respect to its bulk dealers, ICG determines the price, holds the customer contract, and bills the client directly. The Tribunal does not regard these agents and bulk dealers as strong competitors to the merging parties, particularly with respect to existing customers.

**227** The Commissioner contends that fringe and regional competition exists in some local propane markets, but that sustained or significant competition exists only between the merging parties. The evidence for this submission is that independent propane marketers are price followers, they are in many cases unknown to consumers in their own markets, they differentiate their products and locations to avoid direct competition with the merging parties and they compete mainly among themselves. The latter point leads to Professors Schwindt and Globerman's reference to "churn". For example, Mr. Sparling submitted that Sparling does not actively solicit customers from rivals, particularly from Superior. He testified:

> MR. MILLER: Do you actively solicit customers from your rivals?
>
> MR. SPARLING: No.
>
> MR. MILLER: Do you have any instructions or directions to represent --
>
> MR. SPARLING: We discourage that. We refer to that as cold calling. It's not to say it doesn't happen in this industry, but we certainly discourage it, and we would define that as a sales person driving up and down a given road and wherever they see a tank they simply go in and cold call the customer. We discourage that.
>
> transcript at 12:1731 (14 October 1999).

**228** He also testified that Sparling does not seek to be a price leader; rather, Sparling emphasizes "consistent pricing" from customer to customer (transcript at 12:1728 (14 October 1999)). In the Tribunal's view, this comment can reflect consciously parallel behaviour that characterizes some oligopoly markets; possibly it reflects only that Superior and Sparling have highly differentiated marketing strategies and hence do not compete directly for this reason. In either case, it suggests that Sparling cannot be viewed as an effective competitor to Superior or to the merged entity.

**229** Further evidence of weak remaining competition is provided by Mr. Edwards of EDPRO Energy Group Inc. ("EDPRO") who established his company in June 1997. Mr. Edwards said that he established the business in

London, Ontario, because of its proximity to the Sarnia propane supply source and to avoid competing in a market with a dominant firm. Based on his experience in the Maritimes, Mr. Edwards felt that competing with a dominant propane marketer was not likely to yield success. Further, Mr. Edwards explained that after two years in the business, EDPRO's top three customers represent 75 percent of EDPRO's total volume.

**230** Moreover, EDPRO's own organization, effectively a franchise, indicates that its own dealer-associates operate as bulk dealers rather than as competitors. The dealer-associates purchase propane from EDPRO and operate under the EDPRO name in exclusive territories established by agreement with EDPRO.

**231** It appears to the Tribunal that residential customers are not well informed about alternate propane marketers serving their areas other than the merging parties. For instance, one of the Commissioner's factual witnesses, Ms. Simons, was unable to determine which suitable propane companies were delivering propane in Renfrew, Ontario. During cross-examination by the respondents, she stated that when building her house in Renfrew, she was aware only of Superior and ICG and selected ICG on the basis of price. She had not been solicited by any other propane suppliers and was only familiar with one other propane supplier, Rainbow Propane, which supplies 100-pound tanks to cottages (transcript at 19:3304 (26 October 1999)).

**232** The Tribunal also heard evidence that residential customers learn about competitors by word-of-mouth from neighbours. This lack of information regarding competitors suggests to the Tribunal that the independent firms do not market their services as aggressively as ICG or Superior and that customer awareness is weak as the Commissioner asserts.

**233** The respondents claim that certain firms could easily enter the retail propane business, and they twice quote part of paragraph 3.2.2.7 of the MEG's, cited above at paragraph [57], which indicates that, under certain conditions, potential competitors are considered at the stage of market delineation. On this basis, the respondents advocate including upstream propane producers, suppliers from distant locations, and suppliers of alternate fuels in the relevant market and they identify certain such firms by name. The respondents' quotation from paragraph 3.2.2.7 of the MEG's includes the following:

> ...Where it can be established that such a seller would likely adapt its existing facilities to produce the relevant product in sufficient quantities to constrain a significant and nontransitory price increase in the relevant market, this source of competition will generally be included within the relevant market.

**234** The Tribunal notes that the respondents have not provided any information on the sales of retail propane that the named potential competitors might reasonably be expected to make and, thus, have not established that such sales could exercise a constraining influence on the pricing of products sold within the relevant market.

**235** Claiming support from footnote 22 of the MEG's, the respondents also argue that, although market shares could not reasonably be attributed to these potential competitors, the existence of these firms implies that the market shares of actual propane retailers overstate the market position of the actual retailers. In effect, the respondents ask the Tribunal to place less weight on estimated market shares of Superior, ICG and presumably the independent firms because of the presence of potential competitors.

**236** In this regard, the Tribunal notes that the respondents have incompletely quoted from the MEG's which, immediately following their quoted passage, also state:

> ... However, potential competition from sellers who could produce the relevant product by adapting facilities that are actually producing another product will not be assessed at the market definition stage of the assessment of the merger where:
>
> (i) such a seller would likely encounter significant difficulty distributing or marketing the relevant product; or,
>
> (ii) new production or distribution facilities would be required to produce and sell on a significant scale.

> In these circumstances, this source of competition will instead be considered subsequent to the delineation of the relevant market, in assessment of the likelihood of future entry pursuant to section 93(d) of the Act.

**237** On the basis of the evidence in this case regarding, inter alia, customer contracts and scale economies, the Tribunal believes that the output of the potential entrants cited by the respondents would not be included in the relevant market if the MEG's were applied. As a consequence, there is no reason to believe that the market shares of actual competitors overstate their market positions.

**238** On the basis of the evidence submitted, the Tribunal believes that there is insufficient evidence to demonstrate that there will be effective remaining competition capable of constraining the exercise of market power by the merged entity.

**239** The respondents' main piece of evidence in this area is Professor Carlton's statistical analysis of Superior's margin. He concludes that, whereas a substantial presence by ICG in Superior's market area does not constrain Superior's pricing, the aggregate of the independents' volumes in that market does provide a competitive restraint on Superior's pricing. The Tribunal will discuss this opinion evidence below.

## F. PREVENTION OF COMPETITION

**240** In addition to the alleged substantial lessening of competition pursuant to sections 92 and 93 of the Act, the Commissioner submits that the merger will lead to a prevention of competition in the Maritimes that will be substantial.

**241** ICG serves the Maritimes provinces from its branch located in Moncton, New Brunswick. The Commissioner points out that ICG had extensive plans, prior to its acquisition by Superior, to expand its business in the Maritimes by establishing branch operations in Sydney, Nova Scotia.

**242** The Commissioner submits that Irving Oil Limited and Superior were the principal alternate competitors in this region and that the merger terminates ICG's activity as a competitor in Atlantic Canada. He submits that Superior and Irving Oil had a duopoly in the Maritimes. The Commissioner argues that ICG has developed and pursued competition in the Maritimes and has evident capability and plans to expand its presence in order to increase competition in the Maritimes. He introduced ICG's plans to obtain Canadian Tire's business where ICG stated clearly that they would dedicate a $200,000 tractor-trailer to service the Canadian Tire dealer network in the Atlantic provinces (exhibit A-851 at 10980). The Commissioner submits that the acquisition of ICG by Superior will substantially prevent competition in Atlantic Canada.

**243** The respondents did not call any evidence nor made any submissions regarding the Commissioner's allegation that a substantial prevention of competition is likely to occur in Atlantic Canada.

**244** The Tribunal recognizes that the concept of prevention of competition has not received much attention in Canadian jurisprudence. In Howard Smith Paper Mills, Ltd. et al. v. The Queen *(1957), 8 D.L.R. (2d) 449* (S.C.C.), the Supreme Court of Canada had to consider the meaning of the word "prevent" in relation to the word "unduly" and concluded that, when used together, the word "prevent" means "hinder or impede" in contrast to absolute elimination.

**245** The MEG's, cited above at paragraph [57], explain the expression "prevention of competition" at paragraph 2.3 as follows:

> Similarly, competition can be prevented by conduct that is either unilateral or interdependent. Competition can be prevented as a result of unilateral behaviour where a merger enables a single firm to maintain higher prices than what would exist in absence of the merger, by hindering or impeding the development of increased competition. For example, the acquisition of an increasingly vigorous competitor in the market or

of a potential entrant would likely impede the development of greater competition in the relevant market. Situations where a market leader pre-empts the acquisition of the acquiree by another competitor, or where a potential entrant acquires an existing business instead of establishing new facilities, can yield a similar result.

Competition can also be prevented where a merger will inhibit the development of greater rivalry in a market already characterized by interdependent behaviour. This can occur, for example, as a result of the acquisition of a future entrant or of an increasingly vigorous incumbent in a highly stable market.

**246** In light of ICG's plans to vigorously expand its activities in Atlantic Canada and in the absence of any evidence to the contrary, the Tribunal is of the view that there will likely be a substantial prevention of competition in Atlantic Canada as a result of the merger.

G. STATISTICAL AND ECONOMETRIC EVIDENCE

(1) Commissioner's Expert Evidence

**247** Michael R. Ward, one of the Commissioner's experts, provided econometric evidence about the likely effects of the merger on Superior's ability to exercise market power. He used the well established approach of "merger simulation", a method developed specifically for analysing the competitive effects of mergers in differentiated product industries. In such industries, the potential for a unilateral price increase is high when the merging parties place competitive constraints on each other by virtue of a high degree of substitutability between their products prior to the merger. Prior to a merger, a unilateral price increase by one firm may lead to a loss of sales to its closest competitors. However, a unilateral price increase following a merger among close competitors may lead to a reduced loss of sales when the products of the merging companies are closer substitutes for each other than for the products of other firms in the industry (see generally exhibit R-108, J.A. Hausman and G.K. Leonard, "Economic Analysis of Differentiated Products Mergers Using Real World Data" (1997) 5:3 George Mason L. Rev. 321).

**248** In the first part of his report (expert affidavit of M.R. Ward (30 August 1999): exhibit A-2059), Professor Ward estimates the structure of demand for propane. He then uses these estimates to simulate the instant merger's likely effects. In order to determine the degree of substitution between the products of the merging parties, Professor Ward obtained data on ICG and Superior branches in 46 out of 74 of Professor West's geographic markets for a period of 54 months up to 1998 for which data was available. He used Superior data on prices, sales, and product groupings, and ICG data on litres sold, dollar sales, gross profits, and product groupings to establish volumes and prices for each firm in four product segments: residential, industrial, autopropane, and "other" which includes construction, commercial, government and agriculture end-uses.

**249** With this data set, Professor Ward measures the extent to which consumers substitute between ICG and Superior using a linear approximation to the Almost Ideal Demand System, a widely-accepted approach to demand estimation. He finds that an increase in ICG's price results in a statistically significant increase in Superior's market share in the residential and industrial segments, and that an increase in Superior's price reduces its market share significantly in those segments. Professor Ward interprets these findings as evidence for consumer substitution between the products of ICG and Superior, i.e., that they compete directly and their products are close substitutes for each other in the eyes of consumers. His report shows at page 21 that the results for the autopropane segment have the expected signs but are not statistically significant; results for the "other" segment are not reported due to lack of significance or implied upward-sloping demand curves.

**250** Professor Ward's evidence at page 26 of his report also demonstrates that Superior reacts strategically to ICG's pricing behavior. He finds that when increases in ICG's unique costs result in a price increase of one percent, Superior increases its price by approximately two-thirds of a percent in the residential, industrial and automotive categories. He expects that ICG would respond to Superior's price increases but does not have the data to estimate that strategic relationship. In his simulation analyses, he makes the assumption that ICG will react to Superior's price changes in the same way as Superior reacts to ICG's pricing decisions as stated at page 27 of his report.

**251** Using the statistical results obtained with the Almost Ideal Demand System, Professor Ward estimates the own-price and cross-price elasticities of demand in order to estimate the impact of the merger on product prices, a step referred to as simulation. Since he did not know the price elasticity of demand for propane, he estimated firm-level elasticities with three different assumptions for that key measure. At table 6 on page 29 of this report, he finds, for example, that if the price elasticity of demand for propane is -1.5, then the price elasticity of demand for ICG propane is -2.40 in the residential segment and the corresponding Superior price elasticity is -1.97 with regional and discount dealers in the market. He assumes that substitutability between the merging parties and independent firms is exactly half as large as that between ICG and Superior.

**252** Combining the firm-level price elasticities with the evidence on strategic pricing (which would no longer occur post-merger), Professor Ward estimates the change in price due to the merger assuming there are no changes in marginal costs, i.e., no efficiency gains and no entry or supply-substitution by product segment. Depending on the elasticity assumed for propane demand, on the presence or absence of regional and discount dealers, and on the product segment, the average estimated price increases are between 1.4 percent and 15.1 percent. Table 7 on page 30 of his report shows that, using propane demand elasticity of -1.5, the average price increases are 8 percent in residential, 8.9 percent in industrial and 7.7 percent in automotive taking regional and discount dealers into account. He concludes at page 36:

> ... Fifth, ignoring possible price reductions from merger efficiencies, entry or supply-side substitution, the incorporation of these estimates into a merger simulation implies prices will increase due to the merger. The size of the price increase depends primarily on the demand for propane. Specifically, if propane demand is relatively inelastic, the merger is likely to raise average prices by 8 % or more.

**253** At the time of his analysis, Professor Ward did not have the statistical results of Professors Ryan and Plourde regarding the price elasticity of demand for propane. When this information was made available, he re-calculated the effects of the merger on prices using a propane demand elasticity of -1.0, based on their conclusion that the demand for propane was price-inelastic. In those calculations, he also relaxed his assumption that substitutability between independent firms and ICG and Superior was half that of the estimated substitutability between ICG and Superior. Instead, he assumed that they were equally substitutable. Table 2 on page 8 of his report in reply (expert reply affidavit of M.R. Ward (4 October 1999): confidential exhibit CA-2060) shows that he estimates that the average price increases for residential, industrial and automotive are 11.7 percent, 7.7 percent, and 8.7 percent, respectively, when independent firms are in the market.

**254** The respondents' experts, Professor Carlton and Dr. Bamberger, in their report in rebuttal (expert rebuttal affidavit of D.W. Carlton and G.E. Bamberger (27 September 1999): confidential exhibit CR-123), argue that Professor Ward's estimated price increases are overstated because he does not include the effects of efficiencies, entry or supply-side substitution in his analyses. They also criticize Professor Ward for not justifying his assumptions in this regard. They also consider that he has not adequately recognized the constraining effects of independent firms on Superior and ICG pricing. The respondents argue strenuously that Professor Ward did not provide an opinion as to the quantum of any likely price increases post-merger and, therefore, did not provide a basis for finding a substantial lessening of competition.

**255** Noting its earlier comments regarding the evidence of entry and of supply substitution, the Tribunal does not accept the criticisms of Professor Carlton and Dr. Bamberger in these areas.

**256** In reply to their criticism, Professor Ward re-calculated the price impacts including the effects of efficiencies and reported virtually identical price increases at all levels of efficiency gains up to and including $40 million per year, as shown at tables 3 to 5 on pages 10 to 12 of his report in reply (confidential exhibit CA-2060). In a further re-calculation, at the request of the respondents, that incorporated the approach to cost savings as outlined by Hausman and Leonard, cited above at paragraph [247], Professor Ward found that efficiencies had a stronger impact but resulted in price reductions of -0.9 percent in residential, -1.1 percent in industrial and -1.9 percent in automotive only at the $40 million level and then only if 100 percent of these efficiency gains resulted in variable-

cost savings (Ward Undertaking (16 November 1999): exhibit A-2079, tables 3-5). As discussed below, no one including the respondents' experts on efficiency gains has suggested that this merger will produce $40 million of annual savings in variable costs.

**257** In the Tribunal's view, Professor Ward's analysis, even though it does not take efficiencies into account, is highly relevant to a determination as to whether there is a likely substantial lessening of competition.

**258** The Tribunal concludes that evidence of an actual or likely price increase is not necessary to find a substantial lessening of competition. What is necessary is evidence that a merger will create or enhance market power which, according to paragraph 2.1 of the MEG's, cited above at paragraph [57], is "the ability to profitably influence price, quality, variety, service, advertising, innovation or other dimensions of competition". There is no requirement under the Act to find that the merged entity will likely raise the price (or reduce quality or service). The only requirement under section 92 is for the Tribunal to decide whether the merged entity has the ability to do so.

**259** For this reason, Professor Ward's simulations both in his report in reply and his undertaking which take efficiencies into account to address the respondents' criticism are irrelevant. The Tribunal infers from the results of his other simulations that the merged entity would have the ability to raise the price of propane.

**260** As to the respondents' claim that Professor Ward has not offered an opinion on the extent and likelihood of a price increase, the Tribunal notes that his initial simulation results at table 7, on page 30 of his report (exhibit A-2059), provided six sets of estimates that were calculated based on three assumed values for the price elasticity of propane demand and on two scenarios concerning the presence or absence of regional and discount dealers in the market. He concluded that the merger would lead to higher prices under all assumed conditions. In his re-calculations in reply at table 2, on page 8 of his report in reply (confidential exhibit CA-2060), Professor Ward further varied his assumptions and obtained similar results.

**261** The fact that Professor Ward simulated the merger's effects under a variety of assumptions and reached the same conclusion gives the Tribunal more confidence in his opinion than it would have if he had restricted his simulations to a narrowly defined set of assumptions. The Tribunal views Professor Ward's conclusion in his initial report, that average prices would rise by eight percent or more as a result of the merger assuming that propane demand is relatively inelastic, as a valid opinion, particularly given his further simulation results in reply.

(2) Respondents' Expert Evidence

**262** The respondents' experts, Professor Carlton and Dr. Bamberger, were asked to evaluate the Commissioner's claim that Superior's proposed acquisition of ICG would result in a substantial prevention or lessening of competition in the market for propane in Canada. They concluded that there was no systematic evidence that the proposed merger would have such effect. They considered the competitive restraint on Superior, customer gains and losses, gross profit margin and EBITDA.

(a) Competitive Restraint

**263** Professor Carlton presented econometric evidence that ICG has not provided a competitive restraint on Superior's pricing but that the independent propane dealers, in aggregate, have provided such constraint. This evidence contradicts the Commissioner's assertion that where significant competition takes place in the propane business, it is between ICG and Superior. If Professor Carlton is correct, then the removal by this merger of ICG as a competitor should not allow Superior to raise its price.

**264** In his econometric models, Professor Carlton posits a relationship between Superior's gross profit margin and the "substantial presence" of ICG and of the remaining firms in aggregate. A substantial presence is measured in four separate ways. In the first model, the presence of ICG and of the other firms in aggregate are deemed

substantial if their respective market shares are at least 15 percent. In the second and following models, a deemed substantial presence requires a market share of at least 20 percent, 25 percent and 30 percent, respectively.

**265** Professor Carlton measures these hypothesized relationships by applying the regression analysis technique of ordinary least squares ("OLS") to 1998 monthly data on Superior's prices, costs, margins and volumes at the branch level, hence pooling time-series and cross-sectional data. These data come from Superior's internal records as do the proxies for secondary distribution costs. The prices of alternative fuels come from Statistics Canada databases. The 1998 market share data used to define the dichotomous substantial presence variables are taken from the branch templates prepared by Superior's branch managers in 1999. Professor Carlton controls for a variety of other exogenous variables and conducts additional OLS regression analyses for 1997 (using 1998 market shares) and also by profit margin in various end-uses. His results in these latter OLS analyses appear to use similar models and definitions of variables and to support his 1998 results; accordingly, the 1998 OLS results will be the focus of the Tribunal's review.

**266** Professor Carlton finds that Superior's gross profit margin is higher where ICG has a substantial presence. Selecting model 1 as an example, Superior's margin is 1.47 cpl higher at locations where ICG has a substantial presence (i.e., 15 percent or greater market share) than where it does not. In all four models, the margin impact is positive and statistically significant.

**267** The results for the independent firms show that the aggregate substantial presence of those firms decreases Superior's margin. Where the aggregate market share of the other firms is at least 15 percent, Superior's margin is 0.80 cpl lower than where the aggregate market share is less than 15 percent. Similarly, where the aggregate market share of the other firms is at least 30 percent, Superior's margin is 0.56 cpl lower than where the aggregate market share is less than 30 percent. The effect on margin is negative and statistically significant in all four models.

**268** On the basis of these econometric results, Professor Carlton concludes that ICG does not constrain Superior's pricing behaviour, and that the merger will not enable Superior to increase prices, principally because of the discipline exerted by independent firms. At footnote 31, on page 15 of his report (confidential exhibit CR-120), Professor Carlton suggests that his results are consistent with the alleged "inefficiency" of ICG (i.e., that it has been badly managed).

**269** The Tribunal notes that Professor Carlton's finding that Superior's gross margin is higher at locations where ICG has a substantial presence is an unexpected and unusual result and it is perhaps his most important result. Several criticisms were offered; the Tribunal will comment on the ones that seem most significant.

**270** The Commissioner suggests that substantial presence variables may be proxies for market concentration. If this were the case, then Professor Carlton's results would tend to show that Superior's gross profit margin is higher in areas where concentration is higher, rather than demonstrating that ICG is a weak competitor. Despite Professor Carlton and Dr. Bamberger's reply on this point, when taken in conjunction with various internal Superior reports of challenging behaviour by ICG, the Tribunal believes that the better view is that Professor Carlton's results reflect concentration.

**271** The specification of the substantial presence of the independent firms is also problematic. Professor Carlton aggregates the volumes of all independent firms into one market share. Thus, as Professors Schwindt and Globerman point out at page 9 of their affidavit in rebuttal (confidential exhibit CA-2078), the statistical result would be the same whether the substantial presence variable combined market shares of many independent firms or represented the market share of one large independent firm. The Tribunal would expect different competitive effects if there were many independent firms with a certain combined share than if there were just one with that share. Hence the substantial presence variable that Professor Carlton used may not be a good measure of the competitive effect of independent firms.

**272** Professor Carlton's models posit that Superior's margin is affected by ICG's and the independents' substantial presence. The Commissioner suggests that the opposite relationship may also hold simultaneously and criticizes

Professor Carlton's statistical results for failing to take account of the simultaneous relationship between Superior's profits and the substantial presence variables. Such simultaneity is known to lead to biassed statistical estimates when the OLS method is used.

**273** Replying to a similar criticism of his OLS results from Professor Ward (expert rebuttal affidavit of M.R. Ward (14 September 1999): exhibit A-2080), Professor Carlton repeats his analysis using the method of two-stage least squares ("2SLS") in order to take simultaneity into account. This further work indicates to the Tribunal that Professor Carlton gives some credence to this criticism. Footnote 15 on page 12 of his report in reply (expert reply affidavit of D.W. Carlton and B.E. Bamberger (19 September 1999): confidential exhibit CR-122) states that the results therefrom:

> ... provide no systematic support for the Commissioner's claim that ICG significantly constrains Superior's retail propane prices. Full regression results are reported in Appendix G.

**274** It is instructive to compare Professor Carlton's 2SLS results with his OLS results. All four OLS models demonstrated that Superior's profit margin was higher where ICG had a substantial presence and that the positive relationship was statistically significant. With the method of 2SLS, one model results in a positive coefficient for ICG's substantial presence, three of the models now show negative coefficients for this relationship, and none of these four coefficients is statistically significant. These differences suggest to the Tribunal that Professor Carlton's OLS results are statistically biassed and not reliable.

**275** For example, where substantial presence is defined at the 15 percent level, Professor Carlton's OLS results indicate that Superior's margin is 1.47 cpl higher where ICG's presence is substantial than where it is not, and that the relationship is statistically significant. However, the 2SLS results indicate that Superior's margin is 1.60 cpl lower where ICG's presence is substantial than where it is not; the relationship is not statistically significant.

**276** Thus, while Professor Carlton is correct to claim that his 2SLS results do not provide systematic support for the Commissioner's claim, it also appears that they do not provide support for his own conclusions. In particular, the 2SLS results support neither the conclusion that Superior is more profitable at locations where ICG has a substantial presence nor the suggestion that ICG is an ineffective competitor. Indeed, the lack of statistical significance for ICG's substantial presence indicates that no relationship has been found.

**277** With respect to the presence of independents, Professor Carlton's 2SLS results for the aggregate effect thereof also differ from his OLS results. In all four models, the substantial presence of independents has a much stronger statistically significant effect on Superior's margin than with OLS methods. For example, with a 15 percent substantial presence, the OLS impact of independents is -0.80 cpl; with 2SLS, the impact is -3.49 cpl. Similar differences are found across all four models.

**278** The Tribunal observes that the measures of substantial presence for independent firms in aggregate depend on the market share data from Superior's branch templates, the limitations of which have already been noted. Simply put, the Tribunal believes that the substantial presence of independent firms has been measured with error and that the resulting coefficient estimates, whether OLS or 2SLS, are unreliable.

**279** The Tribunal regards Professor Ward's criticism regarding simultaneity as appropriate and, therefore, places greater weight on Professor Carlton's 2SLS results. The Tribunal rejects Professor Carlton's OLS results and the implications which he draws therefrom. Moreover, since Professor Carlton's 2SLS results provide no information on the relationship between Superior's margin and ICG's substantial presence, the Tribunal can only conclude that Professor Carlton's econometric results are not useful in this case.

(b) Acquisition of Premier

**280** To determine whether the merger is likely to result in a price increase, Professor Carlton examined the price

effects of Superior's acquisition of Premier, which was completed in 1994. Premier had been a strong competitor in British Columbia and Alberta. After studying Superior's prices in those provinces before and after the acquisition, Professor Carlton finds, at paragraph 47 of his report (confidential exhibit CR-120), that Superior's average margin is statistically lower after the acquisition and that end-use margins are significantly lower for three end-uses -- agent, automotive and residential.

**281** Apart from the statistical and interpretive problems which Professors Schwindt and Globerman find with Professor Carlton's evidence, they note at page 14 of their report in rebuttal (confidential exhibit CA-2078) that Premier's sales were more heavily oriented to autopropane than were Superior's and suggest that this is why the average margin declined post-merger. That the Premier merger lowered Superior's profit margin is surprising. Together with the differing circumstances of the instant merger and the absence of reply by Professor Carlton to Professors Schwindt and Globerman's rebuttal points, the Tribunal believes that Professor Carlton's analysis of the Premier merger does not provide a good indication of the likely effects of the merger under consideration here.

(c) Customer Gains and Losses

**282** Professor Carlton reports at paragraph 42 and table 12 of his report (confidential exhibit CR-120) his analysis of Superior's customer gains and losses. For 1996, his customer count data show that Superior experienced a net loss of 149 customers to ICG and 1,862 customers to independent firms. In 1997, Superior enjoyed a net gain of 157 customers from ICG but a net loss of 2,435 customers to independents. In 1998, Superior also had a net gain of 448 customers from ICG and a net loss of 995 customers to independents. He concludes that "Superior systematically loses more, or gains fewer, customers to or from independents than ICG. These results are consistent with my regression findings that independents, and not ICG, constrain Superior's propane prices" (ibid. at paragraph 42).

**283** The Tribunal finds Professor Carlton's conclusion somewhat difficult to understand. It is not the case that Superior gained fewer customers from independents than from ICG. In each of the three years, his data show that Superior gained more customers from independents than from ICG (1,298 from independents versus 793 from ICG in 1996; 1,201 versus 1,115 in 1997; and 1,207 versus 1,116 in 1998). On a net basis, Superior gained more customers from ICG than it lost in two of those years and lost more customers than it gained from ICG in one year. It is not clear to the Tribunal what systematic solutions can be drawn from these numbers.

**284** Professors Schwindt and Globerman, at page 12 of their report in rebuttal (confidential exhibit CA-2078), point out that the counting of actual customer gains and losses does not measure the number of customers that ICG challenged. Moreover, as they point out, counting customers will not reflect the size of those customers or the volumes won or lost. It may be, for example, that ICG's business strategy is more focussed on large-volume customers and hence, it may not challenge many small accounts that would likely be of interest to independent marketers. Referring to ICG's experience in Bromont, Quebec, they state that a simple counting of customers gained and lost is misleading.

**285** As Professor Carlton does not challenge these criticisms in his report in reply (confidential exhibit CR-121), the Tribunal is of the view that counting actual customers gained and lost does not, in itself, establish the ineffectiveness of ICG as a competitor to Superior.

(d) Gross Profit Margin

**286** In Professor Carlton's view, as stated at paragraph 12 of his report (confidential exhibit CR-120), the Commissioner's claim is that retail propane prices depend on the number of national suppliers in a country. If the Commissioner were correct, he argues, then gross profit margins of propane dealers should be higher in Canada where the industry is more concentrated than in the United States where there are more "national retail suppliers" competing in a local market. He presents evidence for the period 1994-98 showing that the average gross profit margin (i.e., gross profits as a percentage of revenues) was lower for Superior (44.5) and ICG (44.7) than for a

sample consisting of the seven largest American propane dealers with multi-market operations on which he could collect such data (47.9). This evidence, he argues, suggests that profitability is not a function of industry concentration and hence the merger of ICG and Superior will not present a problem for competition.

**287** The Commissioner's experts, Professors Schwindt and Globerman, criticize this statistical finding for failing to take differences in product mix into account. The overall gross margins of propane dealers might vary because of profitability differences in the end-use markets they serve. Accordingly, they argue, the lower gross profit margins of ICG and Superior reflect the fact that they are more heavily involved with low-margin autopropane supply and less involved with residential propane than their American counterparts. Once the gross margins are corrected for differences in product mix, the margins of ICG and Superior are higher than the ones of the dealers in the United States.

**288** At page 2 of his report in reply (confidential exhibit CR-122), Professor Carlton recalculates Superior's gross margin for 1998 assuming it had the same business mix as each of the three American propane dealers. The resulting average profit margin is higher than Superior's margin for that year and tends to support Professors Schwindt and Globerman's citation. Professor Carlton does not report such calculations for ICG. In the Tribunal's opinion, Professor Carlton has not shown that the Commissioner's business mix criticism is mistaken.

(e) EBITDA

**289** Professor Carlton's evidence at table 3 of his report (confidential exhibit CR-120) is that EBITDA as a percentage of revenues are lower for ICG (11.2) and Superior (12.9) than for his sample of American dealers (15.6) for the 1994-98 period. He interprets these data as further support for his view that profitability is not related to industry concentration.

**290** In the propane business, EBITDA equal gross profit less secondary distribution and other administrative costs, and hence, is a measure of net cash flow from operations. As a profit measure, it has the advantage of not being distorted by the arbitrary treatment of depreciation/amortization under generally accepted accounting rules, by the choice of capital structure which influences interest expense or by tax planning opportunities. Accordingly, EBITDA may be preferred to other profitability measures (such as net income) that measure profit with such distortions and are unreliable when making inter-firm comparisons.

**291** The Commissioner takes issue with Professor Carlton's interpretation, stating that differences in EBITDA can be due to differences in "net margin" across applications. He notes, for example, that net margins can differ due to differences in capital investment across end-uses with the resulting differences in depreciation expense across end-uses. This argument is similar to the business mix argument discussed above with respect to differences in gross profit margins across firms.

**292** In fact, Superior's own estimate of its 1996 net margins was 0.1118 cpl in the residential segment and -0.0032 cpl in auto. In 1995, those net margins were 0.1065 cpl and 0.0044 cpl, respectively (confidential exhibit CA-16 at 00923). The Commissioner appears to suggest that such differences in net margin account for differences in EBITDA/revenue between Canadian and American propane dealers as the former are more heavily involved in autopropane than are the latter.

**293** However, the definition of net margins is not clear. If, as it appears, it includes depreciation and other costs such as head office costs, interest expense and taxes that are not measured by end-use, then any attempt to allocate such expenses to end-uses served by a propane dealer will require arbitrary allocation rules that make the results similarly arbitrary, if not meaningless. For example, how should the depreciation on a delivery truck that serves both agricultural and residential customers be allocated between these end-uses? Should it be done proportionately to litres delivered, to the number of customers, to distances, to time involved? Each such allocation procedure is as good as any other, and equally arbitrary. Moreover, it is not clear how depreciation should be measured. Certainly, the accounting treatment of depreciation does not attempt to measure the "wear and tear" that

takes place; accounting rules attempt only to spread the purchase price of an asset over some period of time in order to match the cost of the asset against the revenue it generated in a particular period of time as required by accounting principles.

**294** The allocation procedures adopted by Superior illustrate the problem. Overhead costs were allocated to market segments and to geographic markets according to volumes, and operating costs according to the number of deliveries. The stated justification for these procedures is that "they appear to produce the best results" (confidential exhibit CA-16 at 00923).

**295** At paragraph 9 of his report in reply (confidential exhibit CR-122), Professor Carlton suggests that although gross margins differ according to business mix, they reflect differences in secondary distribution costs across end-uses. Presumably, he means that a firm requires a higher gross profit margin in an end-use with higher secondary costs than in an end-use with lower secondary costs in order to operate profitably. However, he presents no evidence that this relationship holds in the propane business. Indeed, he simply states that "[t]here is no reason to believe that prices for residential and auto end-uses differ substantially after all (not just primary distribution) costs are accounted for".

**296** The evidence cited above on Superior's net margins appears to provide a reason for such a belief. However, these margins depend crucially on the allocation procedures adopted.

**297** The Tribunal is not bound by the allocation procedures that Superior used, and it cannot be sure that other equally reasonable procedures would not produce very different net margins. The Tribunal believes that it cannot attribute differences in EBITDA to differences in margins across end-uses as suggested by the Commissioner. However, it cannot accept without evidence that gross profits reflect higher secondary costs across end-uses as Professor Carlton suggests. It may be that, as with gross profit margins, differences in business mix and secondary distribution costs account for some, possibly large, portion of the EBITDA differences between large Canadian and American dealers. Hence the Tribunal is not prepared to accept Professor Carlton's conclusion that ICG and Superior are less profitable than his sample of large American propane dealers.

## H. CONCLUSION

**298** The Commissioner submits that this merger will lead to a substantial lessening of competition in local markets other than "category 1" markets referred to by Professors Schwindt and Globerman, the linked market number one (markets numbers 3, 4, 6, 9, and 7, 27, 40, 50, and 53, as defined by Professor West) and the Sechelt-Powell River market of British Columbia; he also submits that the merger will lead to a prevention of competition in the Maritimes. The Commissioner also submits that national accounts are a separate category of business over which the merged entity will be in a position to exercise market power. In addition to the evidence of high market shares and the difficulty of entry, the Commissioner relies on the expert opinion of Professors Schwindt, Globerman and Ward as to the merger's impact on market structure and the ability of the merged entity to raise price unilaterally.

**299** The respondents argue that the impact of the merger on market structure will be minimal because ICG has not been a strong competitor. In particular, they rely on the expert opinion evidence of Professor Carlton who claims, on the basis of his statistical analysis, that ICG has not constrained Superior's prices in markets where they compete. On this basis, the respondents argue that the removal of ICG by this merger will have no significant competitive impact.

**300** The legal test to be applied under section 92 of the Act is whether the merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially.

**301** In Hillsdown, cited above at paragraph [127], at page 314, the Tribunal held that a finding of a substantial lessening of competition depends on whether the transaction will result in additional market power:

> ... In assessing the likely effects of a merger, one considers whether the merged firm will be able to exercise market power additional to that which could have been exercised had the merger not occurred. A merger will lessen competition if it enhances the ability of the merging parties to exercise "market power" by either preserving, adding to or creating the power to raise prices above competitive levels for a significant period of time. One considers the degree of any such likely increase and whether by reference to the particular facts of the case it should be characterized as substantial.

**302** The Tribunal is largely in agreement with this statement; however, it does not agree that a merger which merely preserves existing power over price should be seen as lessening competition. The objective of merger review is to determine whether market power is increased at the margin.

**303** In Southam, cited above at paragraph [47], at page 285, the Tribunal states:

> ... Most simply, are advertisers likely to be faced with significant higher prices or significantly less choice over a significant period of time than they would be likely to experience in the absence of the acquisitions? (emphasis added)

**304** Subsection 92(2) of the Act makes it clear that market shares and concentration, per se, cannot lead to a finding that a merger will likely prevent or lessen competition in a substantial way. It reads:

> 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.

**305** Although evidence of high market share or concentration is not sufficient to justify for finding that a merger is likely to prevent or lessen competition substantially, it is no doubt a relevant factor. This evidence will be particularly useful in identifying mergers that are likely to result in greater interdependence among the remaining firms in the market.

**306** In light of the evidence, the Tribunal is of the view that the merger is likely to lessen competition substantially in many local markets. The Tribunal accepts the opinion of Professors Schwindt and Globerman regarding the 16 local markets in which the merged entity will have post-merger combined market shares of 95 percent or more and which they referred to as "merger to monopoly". The Tribunal's concern in these markets is that the merged entity will have the ability to exercise market power by imposing a unilateral price increase.

**307** The Tribunal accepts the Commissioner's conclusion regarding the eight markets referred to as "category 1" because the merger is expected to have minimal impact on competition between Superior and fringe competitors.

**308** The Tribunal also finds that the merger is likely to lessen competition substantially in a set of markets referred to as "category 3" which identifies 16 markets in which ICG had a substantial market share prior to the merger but where there were at least three competitors including Superior and ICG. In these markets, the Tribunal expects that the elimination of ICG will enhance interdependence and reduce competition.

**309** Finally, the Tribunal finds that the merger is likely to lessen competition substantially through the creation of a dominant firm in the 33 local markets referred to as "category 2". In these markets, the Tribunal is concerned about the increased interdependence effects that the merger is likely to produce.

**310** The Tribunal finds that the merger is likely to lessen competition substantially in coordination services offered to national account customers. It is uncontested that only the merging firms provide these services across Canada. The merger will leave one remaining firm in Canada offering coordination services and there is no evidence to suggest that anyone capable of offering coordination services across Canada will commence those operations. The Tribunal recognizes that not all national account customers rely on these two companies for coordination services. However, the issue is to determine whether the merged firm will be able to exercise market power over its national

account customers by imposing a unilateral price increase. The Tribunal is of the view that the merged entity will have the ability to do so as some witnesses indicated that they would be willing to pay more for these services in order to avoid the higher costs of internal coordination.

**311** In coming to the conclusion that the merger will likely result in a substantial lessening of competition, the Tribunal considered the evidence of market shares and concentration provided by Professors West, Schwindt and Globerman and the econometric evidence of Professor Ward on the ability of the merged entity to impose unilateral price increases.

**312** The Tribunal also considers that barriers to entry in the retail propane business are high based on the evidence of Professor Whinston and of several factual witnesses. The Tribunal also notes that entry has occurred in the past but that no evidence demonstrates that it would occur within a reasonable period of time to prevent the exercise of market power. The Tribunal is of the view that Superior's and ICG's respective market shares have remained relatively constant through the last decade. Therefore, the Tribunal believes that Superior and ICG' combined market share constitutes approximately 70 percent of the market on a national basis despite entry by relatively small competitors.

**313** The Tribunal also finds that the merger is likely to prevent competition substantially in Atlantic Canada. In making this finding, the Tribunal relies on the evidence of ICG's plans to vigorously expand its activities in Atlantic Canada. In this respect, the Tribunal also considered the evidence of high market shares, the evidence of high barriers to entry and the lack of evidence that entry did occur in the past.

## V. REMEDY

**314** In light of the Tribunal's finding pursuant to section 92 of the Act that the merger is likely to lessen competition substantially in many local markets and for national account customers and that the merger is likely to prevent competition substantially in Atlantic Canada, the Tribunal is of the view that the sole remedy appropriate in this case would be the total divestiture by Superior of all of ICG's shares and assets (including those of the previously integrated branches thereof).

**315** We take note of the Supreme Court's direction in Southam, cited above at paragraph [48], at pages 789 and 790, regarding the appropriate remedy:

> The evil to which the drafters of the Competition Act addressed themselves is substantial lessening of competition. See Competition Act, s. 92(1). It hardly needs arguing that the appropriate remedy for a substantial lessening of competition is to restore competition to the point at which it can no longer be said to be substantially less than it was before the merger.

Further, the Supreme Court stated at page 791:

> ... If the choice is between a remedy that goes farther than is strictly necessary to restore competition to an acceptable level and a remedy that does not go far enough even to reach the acceptable level, then surely the former option must be preferred. At the very least, a remedy must be effective. If the least intrusive of the possible effective remedies overshoots the mark, that is perhaps unfortunate but, from a legal point of view, such a remedy is not defective.

**316** The Tribunal is of the view that since the merger between Superior and ICG is likely to prevent or lessen competition substantially in many local markets across Canada, an order for total divestiture is the sole effective remedy available to the Tribunal. Indeed, the Tribunal is of the view that any order for partial divestiture remedy, while less intrusive, would not effectively restore competition in these markets to the level at which it can no longer be said to be substantially less than it was prior to the merger.

**317** The Tribunal will now turn to the respondents' argument under section 96 of the Act in order to determine whether an order for total divestiture can be made.

## VI. EFFICIENCIES

### A. SUMMARY OF EFFICIENCY GAINS

**318** The respondents submit that the merger will allow Superior to achieve substantial gains in efficiency. They presented the opinion of Cole Valuation Partners Limited ("Cole") stating that the aggregate of such gains ("efficiency value") falls in the range of $381 million to $421 million measured in constant dollars over 10 years. Cole also opines that these efficiency gains cannot be achieved through other means common to industry practice (expert affidavit of C. O'Leary and E. Fergin (17 August 1999): confidential exhibit CR-112 at 2).

**319** Cole's report entitled "Quantification of the Efficiency Value Resulting from the Merger of Superior Propane and ICG Propane" is exhibit A. Appendix 1 to Cole's report is the report of A.T. Kearney Ltd., a management consulting firm with expertise in, inter alia, logistics and operations management. The two reports and opinions therein constitute the "Cole-Kearney report".

**320** The Cole-Kearney report is lengthy and detailed, but its main conclusions are the efficiency gains in each of the three major areas of operation: corporate centre, customer support and field operations. The corporate centre comprises the functions of corporate management and includes, inter alia, head office management activities, personnel and facilities, information systems technology, wholesale propane dealing and purchasing. The Cole-Kearney report projects that the merged entity will require 44 fewer employees in the head office functions than in the two companies separately, that the head office rent will decline, as will public company costs, legal, and marketing expenditures. The report states that estimated annualized savings of $15.4 million will arise from the elimination of redundancies and that, over 10 years, total projected savings will be $141.5 million taking into account certain one-time gains (e.g., on asset disposals) and costs (such as severance) of achieving those savings (ibid. at 9-12 and appendix 1 at section A).

**321** Customer support functions include sales force and related management, customer service and administration, and regulatory and safety. The Cole-Kearney report expects cost savings arising from the duplication of facilities and redundant personnel in areas where both merging companies operate and from the adoption of Superior's decentralized "business model" in which branches are supported by a centralized branch support centre and regional branch support centres. ICG's five customer care centres will be eliminated. Annualized savings of $7.2 million are projected, resulting in $65.7 million in savings over 10 years after including one-time items (ibid. at 13-16 and appendix 1 at section B). The Cole-Kearney report notes that its estimates of cost savings exclude the expected savings from restructurings that Superior and ICG had already planned independent of the merger (ibid. appendix 1, tab B1 at 135, 136).

**322** Field operations consist of field sites, branches and plant operations, delivery and service fleets, propane and tank inventory, and supply and transportation. Cost savings are anticipated to result from redundancies due to overlapping geographic markets and from the larger delivery volumes in each territory that will enable the merged entity to reduce supply and transportation costs. For example, the Cole-Kearney report projects 157 eliminated positions, a reduction of 17,694 tanks, and the elimination of 5.9 million litres of propane inventory. Annualized savings of $16.7 million are expected, for a total of $193.6 million over 10 years taking one-time items into account (ibid. at 17-20 and appendix 1 at section C).

**323** The aggregate cost savings identified in the Cole-Kearney report amount to $400.8 million (with a margin of approximately $20 million) over 10 years, for a projected efficiency gain of $40.08 million (with a margin of approximately $2 million) per year. The Cole-Kearney report asserts a very high level of confidence in its realization, in part because (a) $13 million to $21 million of savings that would likely be realized in the absence of the merger were excluded; (b) identified efficiency gains from the merger were included only if they could be

realized with a high degree of confidence; and (c) the efficiency gains are based on cost savings that are held to be more likely to be realized than revenue gains that are more speculative.

**324** For greater certainty, the Tribunal notes the distinction between "annualized savings" as used in the Cole-Kearney report and "annual savings". The former term is a representative amount of one-year savings in an item when that item's cashflows are measured year by year over 10 years, before taking one-time related cashflows (e.g., due to severance payments, or asset disposals) into account. Accordingly, the savings for that item over 10 years need not equal the annualized saving multiplied by 10. Adding the annualized savings from the three categories discussed above leads to annualized savings of $39.3 million when rounded to one decimal. The latter term refers to all cashflows; for example, if the total savings over 10 years are $400.8 million, then the annual savings are $40.08 million.

B. EFFICIENCY NET PRESENT VALUE

**325** The Cole-Kearney report also provides estimates of the discounted present value of the efficiency gains, the "efficiency net present value", which falls in the range of $291 million to $308 million (ibid. at 24). This calculation depends on the discount rate chosen and the particular set of cashflows evaluated (ibid., appendix 4 at 318). Cole adopts the midpoint of $300 million for the point estimate of the efficiency net present value.

C. TRIBUNAL'S SUMMARY AND EVALUATION

**326** The Commissioner argues, based on the report in rebuttal of Professors Schwindt and Globerman and Mr. Kemp (expert rebuttal affidavit of R. Schwindt, S. Globerman, and T. Kemp (15 September 1999): confidential exhibit CA-3131), that $38.51 million claimed annual savings overstate what the merger is likely to generate and that only $21.2 million thereof are appropriately considered. The Commissioner argues that many of the claimed gains in efficiency are cost savings that are pecuniary in nature and should, therefore, be disregarded because they do not represent savings of real economic resources that would be redeployed by other sectors of the economy. Similarly, the Commissioner asserts that certain real economic costs have been classified as pecuniary and hence ignored when they should be deducted from claimed efficiency gains.

**327** The Commissioner also asserts that the magnitudes of certain properly included efficiencies are overstated, and that costs incurred as a result of the merger have been inadequately treated.

**328** In reply, the respondents dispute several of the Commissioner's criticisms and they submit that the Commissioner's claims in these areas should be disregarded. As many of the Commissioner's concerns are not challenged (for example, the elimination of the "wellness programme" as pecuniary savings), the Tribunal is concerned only with those points of disagreement.

(1) Corporate Centre

**329** The Commissioner asserts that claimed cost savings in corporate centre are overstated by approximately $11.9 million per annum. Of these, the respondents defend their treatment of the Management Agreement, procurement, and public company costs which amount to $11.4 million per annum of the Commissioner's sought-after reduction in corporate centre cost savings.

(a) Management Agreement

**330** Superior is managed by Superior Management Services Limited Partnership ("SMS") which acquired the obligations and benefits (the "Management Agreement") of managing Superior from the previous manager, Union Pacific Resources Inc., in May 1998 for $5 million (Cole-Kearney Report Compendium Binder: confidential exhibit CR-114, tab A1, appendix B). Superior Incentive Trust ("Incentive Trust"), which holds the class A units of SMS,

receives distributions thereon of the management fees which Superior pays to SMS pursuant to the Management Agreement. The management group of Superior (Grant Billing, Mark Schweitzer and Geoff Mackey) owns 28 percent of Incentive Trust's units and hence is entitled to 28 percent of the distributions made by Incentive Trust. A group of investors, Enterprise Capital Management Inc. (the "Enterprise investors"), owns the remaining 72 percent of Incentive Trust's units.

**331** The Commissioner asserts that the schedule of management fees in the Management Agreement provides incentives to SMS to increase (a) the profitability of Superior, and (b) the cash distribution to unitholders of the Superior Income Fund ("cash distribution") which owns Superior. The schedule provides no entitlement to SMS when the cash distribution per unit is less than $1.27. For cash distributions between $1.27 and $1.45, SMS is entitled to an amount equal to 15 percent of those cash distributions and to 25 percent when the cash distribution per unit is between $1.45 and $1.89. Above $1.89, SMS receives an amount equal to 50 percent of the cash distributions.

**332** Accordingly, if the management group could achieve efficiencies that resulted in increased cash distributions, SMS would be entitled to the management fees in respect of such efficiency-based cash distributions. Assuming that the management group achieves the $40 million of efficiencies claimed in the Cole-Kearney report, the Commissioner estimates that SMS would receive management fees in respect thereof of approximately $7.5 million per annum. This amount is an average based on differing assumptions about Superior's future tax position given that management fees are a tax-deductible expense.

**333** In summary, the Commissioner asserts that the management fees arising from achieving efficiencies attributed to the instant merger are payments that compensate SMS for providing the additional management services that are required to achieve these efficiencies. Viewed in this light, these fees are a cost of achieving the efficiencies and should therefore be deducted from the $40 million per annum of efficiencies claimed by the respondents. The Commissioner submits that the full amount of these fees should be deducted, not just the 28 percent thereof that would be distributable to the management group, because the Enterprise investors have management obligations and involvement through representation on Superior's or ICG's boards.

**334** The respondents offer several objections (expert reply affidavit of S. Cole, C. O'Leary, J.P. Tuttle, and E. Fergin (5 October 1999): confidential exhibit CR-113 at 9-13), the main one being that the fees do not call forth additional management efforts by the management group because the managers were fully engaged prior to the merger and because there will be no material change in the level of services provided by the managers; hence, no increase in economic costs will arise (ibid. at 10). As a result, the respondents argue that no deduction of the fees against claimed efficiencies is warranted.

**335** The respondents indicate that the managers received interest-free, non-recourse loans from the Enterprise investors in order to facilitate the purchase of their 28 percent share in the Management Agreement (confidential exhibit CR-113, appendix B at 56).

**336** It appears to the Tribunal that the respondents' position is that the managers are being paid more for providing the same amount of management services and hence that the fees they receive in the form of distributions from Incentive Trust are a pecuniary cost only. In simpler terms, the Management Agreement redistributes some of Superior's profit to the managers at the expense of Superior's owners since no additional management effort is provided. If the respondents' view is correct, the Tribunal finds it a strange argument to make, as it amounts to a statement that, in effect, the management group will be overpaid for the services they provide.

**337** The respondents further argue that the Management Agreement is an investment made and paid for by the managers and that the payments they receive from Incentive Trust are distributions of profit rather than compensation for management services. They point out that the owners of the Management Agreement have the right to sell their interests therein. They also submit that since the Management Agreement predates the merger and has not been amended in this respect, the level of management services to be provided has not changed since

1996 when the terms of the agreement were established. Hence, the respondents argue that any change in payment must be a pecuniary transfer (confidential exhibit CR-113 at 11, 12).

**338** The Tribunal does not agree that the Management Agreement is solely an investment, although it may have aspects thereof. In view of the fact that the management fees paid to SMS pursuant to the Management Agreement are tax-deductible expenses to Superior, they cannot be distributions of after-tax profits. While the managers purchased for their interests in the Management Agreement supported in part by interest-free non-recourse loans, the Tribunal finds that the acquisition price they paid only provides further incentive to them to supply additional services that increase their remuneration. Moreover, it appears to the Tribunal that the managers' ability to transfer their interests in the Management Agreement is highly circumscribed by section 6.1 of the Unitholders Agreement (confidential exhibit CR-113, appendix G, tab 3).

**339** The Tribunal observes that managers of for-profit enterprises often receive compensation in the form of investments or investment-related vehicles, such as shares of the managed company, stock options on company shares, low-interest loans to acquire shares of the managed company, etc. Although the payments that they receive from these investments may be in the form of dividends or capital gains, these forms of managerial compensation are nonetheless techniques for improving the quality and quantity of managerial effort. In particular, these methods seek to align the interests of managers with those of owners so that managerial decisions benefit the latter group. Thus, even when the incentive payments are in the form of distributions on company securities held by the managers, their purpose is to provide incentive to managers to achieve corporate goals and those payments are properly viewed as compensation for effort.

**340** The Tribunal agrees with the Commissioner that, in all relevant respects, the Management Agreement provides additional compensation to the managers for supplying additional managerial effort. Thus, these additional management fees are a true economic cost of achieving the efficiencies claimed by the respondents and hence are properly deducted from those efficiencies.

**341** However, the Tribunal disagrees with the Commissioner regarding the appropriate amount of that deduction. The proper quantum is that amount that compensates the managers for additional effort and hence must be less than the total fees paid to SMS under the Management Agreement because 72 percent thereof accrues to the Enterprise investors. There is no evidence that Enterprise investors or their board representative are or will be involved in active management or in achieving the claimed efficiencies. Accordingly, they benefit from the additional efforts provided by the management group but supply none themselves.

**342** The Tribunal views the distributions on SMS's class A units by Incentive Trust to the Enterprise investors as a pecuniary redistribution of Superior's pre-tax profit from Superior's owners, particularly because those owners receive nothing from the Enterprise investors when the Management Agreement changed hands.

**343** The respondents calculate the payments to the managers under the Management Agreement under different assumptions about Superior's future tax position and conclude that the managers will receive between $1.5 million and $2.8 million per annum if $40 million of efficiencies are properly claimed and achieved. Following the Commissioner's approach, the Tribunal adopts the average thereof, $2.2 million as the deduction from the claimed efficiencies (confidential exhibit CR-113 at 13 and appendix B at B1).

**344** The Tribunal notes that the $7.5 million deduction claimed by the Commissioner is the Commissioner's estimate of the management fees payable to SMS in respect of this merger when the efficiency gains are $40 million per year. Since the Commissioner asserts that this amount is itself overstated for a variety of reasons, the amount of the management fees and hence any deduction in respect thereof must necessarily be lower if the Commissioner's assertion is correct.

**345** The Tribunal notes further that the Commissioner's amount of $7.5 million average estimated management fees equals 18.75 percent of the $40 million claimed efficiency gain. The $2.2 million average fees resulting from the respondents' calculations are 5.5 percent of those efficiencies. Since the Tribunal agrees with the respondents

as to exclusion of amounts received by the Enterprise investors, in determining the proper amount to deduct when efficiencies are less than $40 million, the Tribunal will use the latter percentage.

(b) Procurement

**346** The Cole-Kearney report indicates that suppliers to the merged company will experience cost savings as a result of the combination of purchasing activities in one company rather than two. The merged company will be able to demonstrate these savings and negotiate discounts in truck freight and rail freight rates, among other areas (confidential exhibit CR-112, tab A9 at 115). The Cole-Kearney report had claimed approximately $2.84 million per year in savings to the merged company, but revised its estimate to $3.28 million per year in reply to the report prepared by the Commissioner's experts in rebuttal to include cost savings at Superior's transportation affiliate, Energy Transportation Incorporated (confidential exhibit CR-114, tab 6).

**347** The Commissioner submits that the procurement savings of $3.28 million per year are largely pecuniary and not well documented. Indeed, in their report in rebuttal, the Commissioner's experts, Professors Schwindt and Globerman and Mr. Kemp, note that the estimates are based solely on A.T. Kearney's experience in negotiating transportation contracts for other clients (confidential exhibit CA-3131 at 19).

**348** The Tribunal finds that there is insufficient evidence to support the claimed savings in the Cole-Kearney report. The Tribunal accepts the Commissioner's criticisms and consequently concludes that no savings have been established.

(c) Public Company Costs

**349** The respondents claim an annual saving due to the merger of $660,000 in avoided public company costs. Such avoided costs include stock exchange listing fees, costs of outside directors, trustee's fees, regulatory filing costs, legal and audit fees, etc. Absent the merger, the respondents argue that ICG would have gone public and incurred these costs (confidential exhibit CR-112, tab A-8 at 111).

**350** The Commissioner's experts criticize these savings on the basis that ICG could plausibly have been acquired by another company and could have avoided these costs. As a result, they argue that the cost savings are not properly attributed to the instant merger (confidential exhibit CA-3131 at 18).

**351** The evidence of witness Henry Roberts, vice-president of Petro-Canada, is that arrangements had already been put in place to take ICG public through an offering of trust units when Superior made its offer to acquire ICG; ICG had already issued a preliminary prospectus and was promoting the offering via road shows. According to Mr. Roberts, Petro-Canada had received expressions of interest by a few potential buyers and had discussions with them; however, no such buyer made a binding offer to purchase ICG.

**352** History aside, will these savings likely be attained if the Tribunal orders total divestiture. At the present time, the Tribunal does not and cannot know how the ordered divestiture would take place. However, since Superior is claiming the savings in public company costs as efficiencies, it has the burden of demonstrating to the satisfaction of the Tribunal that those savings are properly included in the analysis under subsection 96(1). Thus, Superior must establish that it would or would likely take ICG public in the event of a total divestiture order. It has not done so, and the efficiency claim is therefore denied.

(2) Field Operations

(a) Fleet and Driver Reductions

**353** The Cole-Kearney report estimates that the merged entity will require fewer trucks of all types in the overlapping trade areas of the merging firms, so that a number of trucks and related delivery driver positions in

overlapping areas can, therefore, be eliminated. The efficiencies in these categories arise from the elimination of certain planned vehicle purchases, the elimination of the operating costs on vehicles removed from service, proceeds of disposal of certain delivery vehicles (confidential exhibit CR-112, section C, tab C4), and the savings in driver remuneration (ibid., tab C-5).

**354** The Cole-Kearney report uses statistical regression methods (as subsequently presented during the hearing in confidential exhibit CR-113, appendix G, tab 5) to determine the relationship between operating hours per bulk truck and three determinants thereof, a trade area proxy measure of distance travelled, volumes delivered, and number of calls. Based on this statistical analysis (Predictive Regression Model Results: exhibit A-3122 at 2), a reduction of 13.27 percent in operating hours was found to be achievable. With this relationship, they conclude that the merged firm will require 661 trucks of all types and that 80 trucks (75 bulk trucks and 5 cylinder trucks) currently serving the overlapping trade areas of the merging parties can be eliminated (confidential exhibit CR-112, tab C4 at 236, 237). Correspondingly, 80 fewer delivery drivers would be needed (ibid., tab C5 at 244).

**355** As a result of this analysis, the Cole-Kearney report estimates annualized savings of $2.6 million ($33.4 million over 10 years) through the elimination of these trucks, and annualized savings of $3.9 million ($36.3 million over 10 years) through eliminating delivery driver positions (confidential exhibit CR-112 at 18). These cost savings account for approximately 17 percent of the ten-year, total gains in efficiency claimed by the Cole-Kearney report.

**356** The Commissioner's experts, Professors Schwindt and Globerman, have criticized the methodology used by the Cole-Kearney report to predict the fleet and driver position reduction and the results therefrom (Evaluation of Appendix D of the Cole/Kearney Reply: exhibit A-3132). They note that the key variable for assessing savings is the average distance between customers, which is not measured by the Cole-Kearney report's trade area proxy. Moreover, they point out that while the Cole-Kearney report measures the relationship between operating hours per bulk truck in their sample and three determinants thereof including volume, their measure of that volume is total branch volume (including volumes delivered by cylinder trucks) rather than actual volumes delivered by those bulk trucks. Other problems include a poor statistical "goodness of fit" measure which the Commissioner's experts were able to improve on by using a different model.

**357** The Commissioner's experts recalculated the analysis of the Cole-Kearney report with the correct data and concluded that the estimated reduction in operating hours was 3.62 percent (exhibit A-3132, table A-4) versus the estimate of 13.27 percent in the Cole-Kearney report. Accordingly, 30 trucks (28 bulk trucks and 2 cylinder trucks) could be eliminated as compared with the estimate of 80 in the Cole-Kearney report. On this basis, the Commissioner submits that cost savings will be $1.69 million per year less than the annualized estimate in the Cole-Kearney report.

**358** Professors Schwindt and Globerman and Mr. Kemp note that since the truck reduction estimate in the Cole-Kearney report is too high, so accordingly is its estimated reduction in the number of delivery drivers (confidential exhibit A-3131 at 7). Assuming cost savings of $48,500 per driver (confidential exhibit CR-112 at 246) eliminated, the overstatement by 50 trucks means that Cole-Kearney's annualized cost savings from delivery driver elimination should be reduced by $2.43 million (i.e., 50 x $48,500). The Tribunal notes that the Commissioner's approach fails to consider the reduction in one-time severance costs that would result from terminating fewer drivers.

**359** In response, the respondents emphasize that the Commissioner's experts, Professors Schwindt and Globerman, have no experience in the propane business and have never adjusted distribution routes or implemented a merger of this type.

**360** In claiming a reduction of 28 bulk trucks in overlapping areas, the Commissioner's experts advocate a reduction of only 5.8 percent of the combined 481 bulk vehicles over 10 years, as compared with Cole-Kearney's estimated 15.6 percent reduction. In claiming a reduction of two cylinder trucks in overlapping areas, they advocate a 4.4 percent reduction over 10 years in the 45-vehicle cylinder fleet, as compared with Cole-Kearney's estimate of 11.1 percent.

**361** The Tribunal cannot endorse the truck reduction estimates of the Commissioner's experts. Although they have demonstrated that the Cole-Kearney's approach to estimating truck reductions is flawed by a serious data problem, the Tribunal recognizes that some gains in efficiency are likely to result from truck reduction, especially in light of the overlapping routes of the merging parties. In the Tribunal's view, the truck reductions estimated by the Commissioner's experts are, at best, the bare minimum of what might be achievable. Accordingly, the Tribunal is of the view that the Commissioner's claimed reduction of $1.69 million in Cole-Kearney's estimated savings from truck reductions is likely too high.

**362** The Tribunal believes that $1 million per year is a more realistic estimate of the savings from bulk truck reductions than the $770,000 calculated by the Commissioner's experts; a similar adjustment to their cylinder truck savings yields approximate annual savings of $150,000. With total estimated annual savings of $1.15 million, the Tribunal believes that Cole-Kearney's estimated annualized savings should be reduced by $1.43 million rather than by the Commissioner's figure of $1.69 million.

**363** Applying the same percentage adjustment to savings in delivery drivers, the Tribunal believes that the savings will be approximately $1.9 million, rather than the $1.46 million claimed by the Commissioner. Accordingly, the Cole-Kearney's estimate of savings of $3.88 million per year should be reduced by $1.98 million, rather than by the Commissioner's figure of $2.43 million.

(b) Propane Supply and Transport

**364** The Commissioner submits that Cole-Kearney's estimated cost savings of $1.39 million per year in this category are overstated. The Commissioner claims that cost savings due to bringing idle equipment into use rather than continue purchasing transport from independent haulers are pecuniary (i.e., that the idle capacity will be transferred from the merged entity to the private haulers that were formerly used). The Commissioner also submits that the savings attributed to reduction in the backup rail car fleet have not been established.

**365** The respondents do not challenge the Commissioner's submissions, except to point out an apparent difference in amounts claimed between the text of the Commissioner's memorandum at page 222 and the corresponding data in table E2. According to the Commissioner, the text error is typographical and the data in table E2 are correct.

**366** On this basis, the Tribunal accepts the Commissioner's criticisms of Cole-Kearney's cost savings.

(3) Other

(a) One-Time Items

**367** The Commissioner states that Cole-Kearney's "annual claimed savings" of $38.51 million are overly optimistic, unrealistic and exaggerated. The Commissioner claims that this figure should be reduced by $17.3 million to produce annual estimated savings of $21.21 million, a figure that would still be too high for lack of a contingency factor.

**368** The Cole-Kearney report claims cost savings of $400.8 million over 10 years with a contingency factor of approximately five percent, for a range of $381 million to $421 million. Thus, on an annual basis, claimed savings are approximately $40 million, the midpoint of the range of $38 million to $42 million, for 10 years.

**369** It appears to the Tribunal that table E2 in the Commissioner's memorandum lists and aggregates Cole-Kearney's "annualized savings" and rounds such items and their sum to two decimals; hence the Commissioner's figure of $38.51 million per year omits one-time expenditures and receipts. Accordingly, the Commissioner's estimate of $21.21 million in annual cost savings from the merger does not include the one-time costs and receipts that result from achieving efficiencies.

**370** In final argument, the Commissioner defended this exclusion in table E2 on the basis that it would be arbitrary to express any one-time cost or receipt as an annual amount by dividing by 10 years in order to add it to the recurring amounts. Indeed, dividing by any other number of years would be equally arbitrary. The Tribunal agrees that it is arbitrary to express a one-time cost or receipt as an annual amount over 10 years. However, the Tribunal does not agree that excluding these one-time amounts is appropriate.

**371** In the Tribunal's view, the appropriate way to value all costs and receipts resulting from the merger, whether one-time or recurring, is through discounting the cashflows at the time of disbursement or receipt at an appropriate discount rate to a present value. Cole-Kearney did this in calculating the efficiency net present value discussed above. The Commissioner did not question the methodology or the results of that calculation or offer corresponding calculations. Moreover, it appears to the Tribunal that the respondents abandoned this approach by the time the hearing started:

> DR. SCHWARTZ: No, I don't. I thought you had discounting in your report.
>
> MR. COLE: Yes. In the original report the $40 million, or the $39 million, and the $400 million are nominal dollars, and in all our discussions with you we have used that paradigm. So while here in Calgary, we have not discussed discounted dollars or net present values.
>
> In our original report there is discussion of that, if need be, but we have not discussed it with you here today or yesterday.
>
> transcript at 34:6863, 6864 (8 December 1999).

**372** Absent this approach, the Tribunal adopts as the basis for its consideration of cost savings the respondents' estimate of $400.8 million in total cost savings over 10 years or $40 million per annum, rather than $38.51 million per annum in annualized savings. This is done to recognize the one-time costs and receipts, although the Tribunal is well aware that a one-time cash receipt is more valuable the earlier it is received, while a one-time cost is more valuable the later the disbursement is made.

(b) Miscellaneous

**373** The Commissioner submits that the Cole-Kearney cost savings in several other areas are overstated by approximately $620,000 per year in aggregate. The respondents do not challenge the Commissioner's submissions. On this basis, the Tribunal accepts the Commissioner's claims in these areas.

(c) Property Tax

**374** The respondents claim that property tax payments saved by the merger are savings in user-based payments for local services that will not be needed after the merger and hence represent real savings to the municipalities. They say that the local property tax differs from income taxes in this respect. However, they also appear to recognize that not all of the municipal services supported by the property tax payments will be reduced. They claim that, absent a principled way to determine which resources will be saved, the full amount of property tax savings should be viewed as gains in efficiency.

**375** The MEG's, cited above at paragraph [57], refer to merger-based tax savings as redistribution of income from taxpayers to firms; hence tax-savings are pecuniary gains rather than true cost savings. The MEG's at paragraph 5.3 do not distinguish between income taxes and other taxes. At the local level, many services supported by the property tax will not be reduced by the merger (e.g., local spending on education, health, social assistance, road maintenance, councillors' salaries).

**376** At the hearing, the Tribunal suggested a principled way of distinguishing between pecuniary and real savings in the area of local services and taxes. If the firm receives an invoice for products or services provided by local

government (e.g., the water bill from the local authority) and if the merged entity will use less of that product or service, then the savings are appropriately regarded as resource savings. Where it is not possible to determine whether property tax savings represent real resource savings or a pecuniary redistribution, the Tribunal agrees with the Commissioner that no claimed efficiency savings should be allowed. However, in this case, as the amount claimed by the respondents is relatively small, the Commissioner does not seek to reduce the efficiencies by that amount.

(d) Integration Costs

**377** The Commissioner submits that the costs of the Cole-Kearney report should be deducted from claimed efficiencies as should the costs of management in planning the merger. The respondents dispute this submission regarding the Cole-Kearney report on the basis that the cost of retaining the consultants was incurred to satisfy the Commissioner.

**378** In the Tribunal's view, the costs of the Cole-Kearney report and pre-merger planning costs should not be deducted from claimed efficiencies. The reason is that these costs have already been incurred and do not depend on whether the merger is allowed to proceed or on whether the efficiencies will be achieved. These costs are sunk costs and hence differ from the costs (e.g., severance payments) that will only be incurred as a result of implementing the merger. Thus, as an economic matter, it would be appropriate to deduct the consultants' fees only, for example, if they were contingent on the outcome of the instant hearing, for in such case they would not be sunk.

**379** In any event, on the evidence before us, the Cole-Kearney consultants were only retained by the respondents after the December 1998 merger. Hence, it cannot be said that the costs of the Cole-Kearney report are costs which relate to the planning of the merger by management.

(4) Net Efficiencies

**380** As noted at paragraph [372], the Tribunal includes one-time items in its analysis and, therefore, accepts $40 million per annum as the starting point to assess efficiency claims. In view of our findings and conclusions regarding the Commissioner's criticisms of the Cole-Kearney report, we conclude that the efficiencies and deductions therefrom are as follows:

TABLE 1: Deductions in Efficiencies

| Deductions | Sought by Commissioner ($million/year) | Allowed by Tribunal ($million/year) |
|---|---|---|
| i) one-time items | $1.50 | $0.00 |
| ii) procurement | $3.28 | $3.28 |

| | | | |
|---|---|---|---|
| | iii) public company costs | $0.66 | $0.66 |
| | iv) delivery fleet | $1.69 | $1.43 |
| | v) delivery drivers | $2.43 | $1.98 |
| | vi) propane supply | $1.12 | $1.12 |
| | vii) other (excl. management fees) | $0.62 | $0.62 |
| | | --- | --- |
| (a) | Total deductions before management fees | $11.30 | $9.09 |
| (b) | Gross efficiencies claimed by respondents | $40.00 | $40.00 |
| (c) | Net efficiencies before management fees (b-a) | $28.70 | $30.91 |
| (d) | Deduction regarding management fees | $7.50 | $1.70 * |
| | | --- | --- |
| (e) | Net efficiencies (c-d) | $21.20 | $29.21 |

* 5.5 % of $30.91

**381** Apart from the specific adjustments to the gains in efficiency claimed in the Cole-Kearney report, the Commissioner states that even after reducing the efficiency gains to $21.2 million, that figure is still unrealistically high, in part because it allows for no contingency factor. The Commissioner submits that the Tribunal should keep this overstatement in mind when balancing claimed efficiencies against the anti-competitive effects of the merger.

**382** The Cole-Kearney report does not contain a deduction from claimed aggregate efficiency gains as a provision for the possibility that those gains may not be achieved. In this sense, there is no provision for contingency. Mr. Cole testified that the efficiency gains were estimated conservatively and were expressed in aggregate with a margin of approximately five percent. He also stated that, as described in the Cole-Kearney report (confidential exhibit CR-112, appendix 5), between $12 to $ 21 million of efficiency gains over 10 years were excluded because they could not be quantified precisely (transcript at 33: 6365-67 (7 December 1999)). The Tribunal is satisfied that there is a buffer zone around the estimated efficiency gains and is, therefore, of the view that the absence of an explicit contingency provision is immaterial.

**383** In this case, the Commissioner chose not to lead evidence on efficiency gains and, therefore, was limited to rebutting the expert opinion evidence of Cole-Kearney. On its view of the evidence concerning the respondents' efficiencies, the Tribunal is satisfied that these efficiencies of $29.2 million per year will likely be brought about by the merger.

D. LEGAL ANALYSIS

(1) Section 96 of the Act

**384** Section 96 provides that:

> 96.(1) The Tribunal shall not make an order under section 92 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.
>
> (2) In considering whether a merger or proposed merger is likely to bring about gains in efficiency described in subsection (1), the Tribunal shall consider whether such gains will result in
>
> (a) a significant increase in the real value of exports; or (b) a significant substitution of domestic products for imported products.

> (3) For the purposes of this section, the Tribunal shall not find that a merger or proposed merger has brought about or is likely to bring about gains in efficiency by reason only of a redistribution of income between two or more persons. (emphasis added)

**385** Section 96 states, in unequivocal terms, that the Tribunal is not to make an order under section 92 if efficiency gains are greater than and offset the effects of any prevention or lessening of competition. As stated above, the respondents claim that significant efficiencies will result from this merger. The Commissioner, however, disputes the efficiencies claimed and further argues that section 96 is not available, as a matter of law, to the respondents in this case.

(2) Position of the Parties

(a) Commissioner

**386** The Commissioner argues that section 96 is not available, as a matter of law, in cases where a merger eliminates competition and results in the creation of a monopoly in a relevant market. Further, he submits that in assessing the trade-off analysis in section 96, the Tribunal has a statutory responsibility to exercise its judgment as to the weight to be accorded to the transfer from consumers to producers, hence that applying a standard with a fixed predetermined weight is contrary to section 96.

**387** The Commissioner suggests that the balancing weight standard as introduced by his expert, Peter G.C. Townley, is consistent with a proper interpretation of section 96. He submits that the efficiency gains do not offset the anti-competitive effects caused to the economy as a whole by this merger.

**388** The Commissioner further submits that the respondents bear the onus of demonstrating all of the elements of the efficiency defence stated in section 96.

(b) Respondents

**389** The respondents claim that significant efficiencies in the range of $40 million per annum will result from the merger between Superior and ICG. They argue that the test to be met under section 96 is that the efficiencies must offset any substantial lessening of competition. They further argue that a substantial lessening of competition is permitted provided it is outweighed by the efficiencies attributable to the merger. They also submit that the effects of the substantial lessening are measured by the deadweight loss to the economy and exclude wealth transfers between producers and consumers which are neutral to the economy.

**390** Further, the respondents submit that the Commissioner is distancing himself from the MEG's, cited above at paragraph [57], by adopting a "distributional weights" approach articulated by his expert, Professor Townley. The respondents submit that the efficiencies will not be realized in the absence of the merger and that there is no evidence of any existing alternative proposals which could reasonably be expected to generate these efficiencies if a divestiture order were made under section 92.

**391** With respect to the burden of proof, they argue that the Commissioner has not met his burden of establishing the effects of the substantial lessening of competition and that the efficiencies might be achievable in some other way.

(3) Status of the MEG's

**392** The parties referred to the MEG's, cited above at paragraph [57], in their written submissions and in oral argument.

**393** Although the Tribunal and the Federal Court of Appeal have held in Director of Investigation and Research v.

Tele-Direct *(1997), 73 C.P.R. (3d) 1* (Comp. Trib.) at 37 and in Director of Investigation and Research v. Southam Inc. *(1995), 63 C.P.R. (3d) 1* (FCA) at 41, that the MEG's are not sacrosanct nor legally binding, the Tribunal notes that they provide important enforcement guidelines reflecting the Commissioner's view on how the Act should be interpreted. The MEG's, which were published in 1991, were prepared to inform the business community and the public as to how the Competition Bureau analyzes the competitive impact of mergers including how it considers efficiencies.

**394** The Tribunal takes notes that, since their adoption in 1991, no changes as to the interpretation of section 96 have been made to the MEG's. Indeed, even after the issuance of the decision in Hillsdown, cited above at paragraph [127], where Reed J. questioned whether the wealth transfer should be treated as neutral, the Commissioner continued, without amending his position, to apply the MEG's. Howard Wetston, the Director of Investigation and Research at the time, stated that he saw no need to revise the guidelines as the comment made by Reed J. in the Hillsdown decision was in obiter dictum.

**395** The total surplus standard was reiterated on July 14, 1998 with the publication of The Merger Enforcement Guidelines as Applied to a Bank Merger by the Competition Bureau at paragraph 109, online: Industry Canada < http://strategis.ic.gc.ca/SSG/ct01280e.html > (last modified: 5 July 1998):

> Where a merger results in a price increase, it brings about both a neutral redistribution effect and a negative resource allocation effect on the sum of producer and consumer surplus (total surplus) within Canada. Ordinarily, the Director measures the efficiency gains described above against the latter effect, i.e., the deadweight loss to the Canadian economy. (reference omitted)

**396** It is only after the Commissioner decided to file the application against the respondents in this case that changes to his position became apparent. Indeed, two recent speeches by Gwillym Allen, Assistant Deputy Commissioner of Competition, Economics and International Affairs, demonstrate a change in the Commissioner's interpretation of the efficiencies exception. In these speeches, Mr. Allen suggests that in some cases "it is more appropriate for the Competition Tribunal to determine whether the merger increases aggregate welfare or not" ("The treatment of Efficiencies in Merger Analysis": remarks given at "Meet the Competition Bureau" conference, Toronto, 3 May 1999) and that "given the evidence presented in a particular merger case, total surplus may not be an all-inclusive measure of the anticompetitive effects that are likely to arise from the merger". Hence, "other qualitative and quantitative subjective comparisons need to be performed in order to determine if the efficiency gains offset the anticompetitive effects" ("The Enforcement of the Efficiency Exception in Canadian Merger Cases": remarks given to the Competition Law Group, Stikeman Elliott, Barristers and Solicitors, Toronto, 25 June 1999).

**397** This change in position is quite surprising. It must not be forgotten that the point of view put forward in the MEG's represents the considered opinion of the Commissioner, the official appointed by the Governor in Council to administer and enforce the Act. That view, it goes without saying, is the view arrived at by the Commissioner following careful advice given to him by his legal and economic advisers regarding the meaning of the various provisions of the Act. Although the Commissioner is not bound by the MEG's nor are they binding upon this Tribunal, the MEG's should be given very serious consideration by this Tribunal. Needless to say the Tribunal can disagree and in fact should disagree if it is of the opinion that the interpretation proposed in the MEG's is wrong. However, when referring and considering the MEG's, one should bear in mind the comments in the preface to the MEG's made by Howard Wetston, then Director of Investigation and Research. He stated that the Merger Guidelines were published to promote a better understanding of the Director's merger enforcement policy and to facilitate business planning. He also noted the extensive consultation process which was followed in their preparation.

(4) Efficiency "Exception"

**398** The Commissioner submits that section 96 provides a defence to an otherwise anti-competitive merger to the respondents if they can demonstrate that the efficiency gains from the merger will be greater than and will offset the

effects of any prevention or lessening of competition resulting from the merger. The respondents, on the other hand, argue that section 96 constitutes rather a limitation on the Tribunal's jurisdiction to make an order under section 92.

**399** In Director of Investigation and Research v. Canadian Pacific Ltd. *(1997), 74 C.P.R. (3d) 55* at 63, *[1997] C.C.T.D. No. 7* (QL), the Tribunal held that section 96 was a defence available to the respondents. The Tribunal further held that the onus of alleging and proving the material facts which form the basis of the defence fell upon the respondents:

> In my view, the Director's request for particulars is reasonable. Under the Act, the existence of efficiencies essentially constitutes a defence to the Director's application. Just as it is improper for the Director to plead bald allegations without pleading the material facts upon which he relies, so too must the respondents plead the material facts which form the basis of a "defence" of efficiency gains. (emphasis added)

The Tribunal can see no reason to disagree with the above statement.

(5) Burden of Proof

(a) Commissioner

**400** The Commissioner submits that the respondents bear the burden of proving all the elements of the efficiency defence on a balance of probabilities and that, once a substantial lessening competition is established pursuant to section 92, the Tribunal should proceed to make an appropriate order unless the respondents are successful with their defence under section 96. The Commissioner suggests that the respondents must bear the onus of establishing all the elements because they have the best knowledge of what strategies are available to them to generate the efficiency gains that they claim and what, if any, alternate means would or would not be available to achieve those gains. Further, the Commissioner submits that the section 11 powers provided by the Act do not place the Commissioner in a position as knowledgeable as the respondents about their business strategies. In support of his argument, the Commissioner relies on two Tribunal decisions: Director of Investigation and Research v. Canadian Pacific Ltd., cited above at paragraph [399], at page 63, and Hillsdown, cited above at paragraph [127], at pages 332-34, where the Tribunal recognized that the burden of proving the elements of the "efficiency defence" falls on the respondents.

**401** The Commissioner also asserts that the respondents must show not only the likely efficiency gains but must also demonstrate the scope and extent of the anti-competitive effects of the merger, absent which the Tribunal is not in a position to determine whether the gains in efficiency are greater than and offset those effects and whether "the defence" has been established.

(b) Respondents

**402** Relying on the Hillsdown decision, cited above at paragraph [127], the respondents submit that they bear the onus of proving the existence of the efficiencies claimed or the likelihood of their existence if the merger has not been implemented. They claim that the Commissioner bears the burden of establishing the effects of the substantial lessening of competition (i.e., the deadweight loss) and that the efficiencies might be achievable in some other way (e.g., a sale to third party). Indeed, the respondents submit that the Commissioner is in a good position, in view of his investigatory powers pursuant to section 11 of the Act, to obtain third party information.

(c) Conclusion

**403** The Tribunal is of the view that the respondents bear the burden of proving all of the elements of section 96 on a balance of probabilities, except for "the effects of any prevention or lessening of competition", which must be

demonstrated by the Commissioner.

(6) Role of Efficiencies under the Act

**404** The Commissioner reminds us that section 1.1 states that the purpose of the Act is to "maintain and encourage competition in Canada" and that competition is not seen as an end in itself, but rather as a means to achieve the four objectives identified in section 1.1. The Commissioner further submits that no hierarchy is established among those "potentially conflicting" objectives. The Commissioner argues that it becomes clear when sections 96 and 1.1 are read together, that a section 96 defence will prevail only when a merger enhances the objectives of competition policy more than it diminishes them. The Commissioner argues that the Tribunal must decide whether Canadians and the Canadian economy are better off with or without the merger.

**405** The respondents submit that the Commissioner's interpretation of section 96 is wrong since section 96 is not subordinate to the purpose clause of section 1.1. Further, the respondents suggest that where there is a conflict between a purpose clause statement and a substantive provision, the latter must prevail.

**406** There are significant differences in the positions of the parties as to the proper interpretation of sections 1.1 (the purpose clause) and 96 (the efficiency exception) of the Act. Many of the issues raised are of long standing, in part because there have been so few litigated mergers in Canada since the Act was amended. In particular, no decision in a litigated merger has turned on the question of efficiency gains and hence it appears to the Tribunal that there is considerable confusion over the meaning of certain key terms. Before dealing with the positions of the parties, the Tribunal will set out its understanding of the relevant sections of the Act.

**407** The Act seeks to obtain the benefits of a competitive economy. As set out in the purpose clause, these benefits, which we have characterized as the objectives of competition policy, are economic efficiency and adaptability, the expansion of opportunities for Canadian participation in world markets and openness to foreign competition at home, opportunities for small businesses to participate in economic activity, and competitive consumer prices and product choices. Under the purpose clause, the Act seeks to achieve these objectives by maintaining and encouraging competition. To this end the Tribunal may, pursuant to section 92 of the Act, order divestiture where a merger is found to prevent or lessen competition substantially.

**408** There was some discussion at the hearing concerning the status that should be given to the stated objectives, particularly whether the ordering of objectives in the list contains any useful information in interpreting the Act. Such discussion is misdirected; the true goal specified in the purpose clause is the maintenance and encouragement of competition. It is noteworthy that the Act does not give the Tribunal the powers to achieve the objectives individually.

**409** For example, small businesses are not protected under the Act. The purpose clause indicates only that the opportunities for small businesses to participate in economic activity will result from maintaining and encouraging competition. Hence, no other powers are needed to realize this objective.

**410** Accordingly, the listing of objectives of competition policy simply presents the rationale for maintaining and encouraging competition. No hierarchy among the listed objectives is indicated and hence no meaning can be taken from the order in which the listed objectives of competition policy appear in the purpose clause. Under the purpose clause, all of the objectives flow from competition.

**411** There are, of course, other objectives that could be sought, one such being the proper distribution of income and wealth in society. It is clear, however, that when competition is maintained and encouraged, the resulting distribution of income and wealth may not be the proper one depending on one's political or social outlook. By not including distributional considerations in the list of objectives in the purpose clause, Parliament appears to have recognized this. Indeed, if distributional issues were a concern, Parliament might have felt it necessary to restrict or

place limits on competition in order to achieve the proper distribution of income and wealth in society. However, such limits would place competition policy at war with itself.

**412** Turning to section 96 of the Act, the "efficiency exception", the Tribunal notes that this section contains the only provision in the Act which limits or restricts the pursuit of competition. As noted above, section 1.1 states that competition should, in and of itself, promote efficiency; normally there will be no conflict between the statutory means (encouraging competition) and the desired end (efficiency). However, the existence of section 96 makes it clear that if competition and efficiency conflict in merger review, the latter is to prevail. Thus, an anti-competitive merger that created or increased market power but also increased efficiency could be approved. Addressing this possibility, the MEG's, cited above at paragraph [57], state at paragraph 5.1:

> One such circumstance is highlighted in section 96 of the Act, where it is recognized that some mergers may be both anticompetitive and efficiency enhancing. When a balancing of the anticompetitive effects and the efficiency gains likely to result from a merger demonstrates that the Canadian economy as a whole would benefit from the merger, section 96(1) explicitly resolves the conflict between the competition and efficiency goals in favor of efficiency.

The Tribunal cannot but agree with this view of section 96.

**413** The existence of section 96 signals the importance that Parliament attached to achieving efficiency in the Canadian economy. Indeed, in the view of the Tribunal, section 96 makes efficiency the paramount objective of the merger provisions of the Act and this paramountcy means that the efficiency exception cannot be impeded by other objectives, particularly when those other objectives are not stated in the purpose clause. To be more explicit, if, pursuant to the purpose clause, the pursuit of competition is not to be limited by distributional concerns, then as a matter of both law and logic, the attainment of efficiency in merger review cannot be limited thereby when competition and efficiency conflict.

(7) Commissioner's Position that Section 96 Does Not Apply to a Merger to Monopoly

**414** The Commissioner submits, as a matter of law, that section 96 does not apply in the circumstances of a merger-to-monopoly. The Commissioner's position is based on the underlying purpose of the Act stated in section 1.1 which is to "maintain and encourage competition". He submits that when a merger creates an absolute monopoly, competition is eliminated which runs counter to the underlying purpose of the Act. Further, the Commissioner submits that when one of the effects of a merger is the creation of a monopoly, that monopoly can never be offset or "neutralized" by efficiency gains regardless of how substantial they are. The Commissioner also argues that if section 96 were intended to allow mergers that eliminate competition to be saved, Parliament would have used some very specific language to so provide.

**415** The Commissioner argues that there is a distinction to be made between sections 92 and 96 of the Act. Subsection 92(2) means that one would not be able to find that a merger, for example, substantially lessens competition simply by virtue of it being a monopoly. That subsection specifically states:

> 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. (emphasis added)

**416** According to the Commissioner, subsection 92(2) is very specific and only applies for the purposes of that particular section, hence that a substantial lessening of competition leading to a 100 percent market share constitutes an elimination of competition which is not covered by section 96. In other words, the argument is that if a merger eliminates competition, the efficiency defence contemplated in section 96 should not apply.

**417** The Commissioner conceded at the hearing that, as a matter of law, a respondent could invoke the section 96

exception as long as its market share did not attain 100 percent:

> MS STREKAF: Our submissions are that there is a different standard in the legislation that we read into the Act in Section 96 in the case of 100 percent that would not apply in your example in the case of a 96 percent situation.
>
> If you had a 96 percent market share, we would say that it would be very difficult, in those cases, for the Respondents to demonstrate that you could offset the effects of a 96 percent market share. But that's a question where we nonetheless recognize and acknowledge that in those kind of situations the Section 96 balancing needs to be performed. Our position is different for 100 percent.
>
> THE CHAIRMAN: A 98 percent market share and a 100 percent market share, the difference may simply be theoretical. Practically, it may not mean anything insofar as consumers are concerned.
>
> But you are saying, in the case of the 98 market share, they could at least attempt to have resort to 96?
>
> MS STREKAF: That's correct.
>
> THE CHAIRMAN: And you are saying, when they reach 100, they shouldn't be entitled to stop at the barrier and go back home.
>
> MS STREKAF: Yes.
>
> transcript at 41:8234, 8235 (1 February 2000).

**418** The position taken by the Commissioner cannot be right. A merger that leads to a monopoly (i.e., where a merged entity has a 100 percent market share) is not, per se, a merger in regard to which the Tribunal may make an order under section 92. Subsection 92(2) requires, in effect, the Commissioner to adduce further evidence in order to show that the merger in question prevents or lessens or is likely to prevent or lessen competition substantially.

**419** If the Tribunal concludes that the merger is likely to prevent or lessen competition substantially, it may make an order under section 92, subject to sections 94 to 96. Section 96 clearly provides that the Tribunal is not to make an order under section 92 if the gains in efficiency resulting from the merger are greater than and will offset the effects of any prevention or lessening of competition. Section 96 does not make any distinction between the "elimination" and the "substantial lessening" of competition. The section applies to any merger in respect of which the Tribunal may make an order under section 92. A merger leading to monopoly and in respect of which the Tribunal has concluded that there will be a substantial lessening of competition, is without doubt a merger to which section 96 applies.

(8) Effects of a Merger

**420** In order to decide whether the efficiencies are greater than and offset the effects of any prevention or lessening of competition under section 96, the Commissioner suggests that the Tribunal should adopt the balancing weight standard described by his expert, Professor Townley. The Commissioner submits that using predetermined weights to the transfer would, as a matter of law, be contrary to section 96. According to the Commissioner, applying a predetermined weight would constitute an abrogation by the Tribunal of its statutory responsibility to exercise judgment. Professor Townley explained the reasons why the various approaches (price standard, the consumer surplus standard and the total surplus) are not consistent with a proper interpretation of section 96. In the Commissioner's view, only the balancing weight approach is consistent with a sound interpretation of section 96.

**421** The respondents submit that the total surplus standard, as stated in the MEG's, cited above at paragraph [57], is the proper standard. They note that the Tribunal's decision in Hillsdown, cited above at paragraph [127], dated March 9, 1992, where Reed J. in her obiter dictum, questioned the appropriateness of the total surplus standard, has not led to any change to the MEG's. Indeed, at page 343, Reed J., in response to the submission made by both parties that the wealth transfer from consumers to producers was neutral, raised as a question whether the transfer

is always neutral and suggested that it might be appropriate to include redistributional concerns when conducting the analysis required by subsection 96(1):

> One other consideration arises with respect to the arguments concerning the efficiency defence. The parties both rely on the judgment that the wealth transfer is a neutral one. A question posed during argument and which will be repeated here is: is this always so? If, for example, the merging parties in question were drug companies and the relevant product market related to a life-saving drug would economists say that the wealth transfer was neutral. The Tribunal does no more than raise this as a question. Another question respecting the alleged neutrality of the wealth transfer is: if the dominant firm which charges supra-competitive prices is foreign-owned so that all the wealth transfer leaves the country, should the transfer be considered neutral?

(a) Efficiency Effects and Redistributive Effects

**422** An anti-competitive horizontal merger is a transaction that creates or enhances market power in the merged entity, the exercise of which leads to a higher price for the same good or reduced quality therein at the same price. If competitive conditions prevailed before the merger, the exercise of market power has several effects.

**423** The economic effects of an anti-competitive merger are the effects on real resources, that is, the changes in the way the economy deploys those resources as the result of the merger. When market power results in an increase in the price of a product, allocative efficiency is reduced as consumers acquire less of the product and switch to lower-valued substitutes. Technical or productive efficiency is reduced because, with less consumption of the product, industry output falls and economic resources are diverted to the production of more costly substitute goods. A reduction in dynamic efficiencies as defined in the MEG's could also be an effect of an anti-competitive merger.

**424** Since consumers pay more for the quantity of the product at the higher price, they lose some of the surplus they had when they paid the competitive price. A portion of this loss in consumer surplus is realized by the firm and its shareholders in the form of higher profits. Such loss is not a social loss, but rather a redistribution of gains from the merger; real resource use is not affected by this transfer of income.

**425** However, the remaining loss of consumer surplus, beyond that realized by the shareholders in the form of increased profits, is a social loss and is often referred to as the "deadweight loss" because there are no offsetting gains. The lost value of output and consumption associated with the deadweight loss measures the allocative and technical inefficiency caused by the exercise of market power and represents the economic effect of the merger.

**426** As we have already stated, the Tribunal is of the view that nothing in the Act allows us to consider distributional goals in merger review. Had this been Parliament's intention, surely the Act would have been worded differently. Robert H. Bork, in his seminal work The Anti-Trust Paradox (New York: The Free Press, 1993), albeit in the American context, puts forward the view that income distribution and its effects are not to be considered in antitrust matters. The Tribunal agrees entirely with the following extract from pages 110 and 111:

> The model outlined addresses the total welfare of consumers as a class. It says nothing of how shares of consumption should be allocated through changes in the distribution of income. Yet all economic activity has income effects and, in particular, restriction of output by the exercise of monopoly power has income effects not taken into account by weighing only changes in allocative and productive efficiency. If the reader will look once more at Figure 4 he will see that at the competitive price, P1, there is a large area under the demand curve that lies above the market price. This area represents the amount above the actual price that consumers would be willing to pay rather than go without the product; it is generally called the "consumer's surplus," perhaps on some notion that the consumer gets surplus value for his money.
>
> > Those who continue to buy after a monopoly is formed pay more for the same output, and that shifts income from them to the monopoly and its owners, who are also consumers. This is not dead-weight loss due to restriction of output but merely a shift in income between two classes of consumers. The

> consumer welfare model, which views consumers as a collectivity, does not take this income effect into account. If it did, the results of trade-off calculations would be significantly altered. As Williamson notes, referring to his diagram: "The rectangle ... bounded by P2 and P1 at the top and bottom respectively and o and Q2 on the sides represents a loss of consumers' surplus (gain in monopoly profits) that the merger produces. ... Inasmuch as the income distribution which occurs is usually large relative to the size of the dead-weight loss, attaching even a slight weight to income distribution effects can sometimes influence the overall valuation significantly."
>
> The issue is not crucial, perhaps, since most antitrust cases do not involve trade-off. The law's mistake has generally consisted of seeing restriction of output where there is none, and in such cases there will be no loss of consumer surplus. But even in cases where the trade-off issue must be faced, it seems clear the income distribution effects of economic activity should be completely excluded from the determination of the antitrust legality of the activity. It may be sufficient to note that the shift in income distribution does not lessen total wealth, and a decision about it requires a choice between two groups of consumers that should be made by the legislature rather than by the judiciary. (reference omitted)

(b) Standard for Merger Review

**427** Assessing a merger's effects in this way is generally called the "total surplus standard". As discussed by the Commissioner's expert, Professor Townley (expert affidavit (16 August 1999): exhibit A-2081), and in a recent article by Michael Trebilcock and Ralph Winter, transfers from consumers to shareholders are not counted as losses under the total surplus standard. The anti-competitive effect of the merger is measured solely by the deadweight loss (M. Trebilcock and R. Winter, "The State of Efficiencies in Canadian Merger Policy" (1999-2000) 19:4 Canadian Competition Record 106). Under the total surplus standard, efficiencies need only exceed the deadweight loss to save an anti-competitive merger.

**428** Other standards have been proposed. Under a "price standard", efficiencies are not recognized as a justification for a merger which results in a price increase to consumers. Under a "consumer surplus standard", efficiencies can be considered in merger review only if they are sufficiently large as to prevent a price increase. Effectively, this means that transfers of income are considered as losses; hence efficiencies must exceed the sum of the transfer of income and the deadweight loss.

**429** From an economic point of view, the cost to society of an anti-competitive merger is the deadweight loss which measures lost economic resources. If, on the other hand, the merger generates efficiencies, it creates economic resources and hence the net economic effect of the merger in terms of resources may be much less than the deadweight loss. Indeed, the merger could be economically positive if efficiencies were sufficiently large, in which case society would benefit economically from allowing the merger.

**430** This possibility is the basis for considering efficiencies in merger review. It is not to determine whether shareholders will be better off at the expense of consumers, but rather whether the economy gains more resources than it loses through the transaction. For this reason, it is important to distinguish true efficiencies, those savings that enable the firm to produce the same amount with fewer inputs, from "pecuniary" economies, those savings that increase shareholder profits but do not allow the firm to be more productive. This distinction is recognized in subsection 96(3) which excludes pecuniary efficiencies from consideration. The only standard that addresses solely the effects of a merger on economic resources is the total surplus standard.

(c) Reasons for Total Surplus Standard

**431** Professor Townley offers an approach ("balancing weights") in which the members of the Tribunal are invited to use their individual judgment and discretion to evaluate whether the gains to shareholders are more or less important to society than the losses of surplus imposed on consumers by the exercise of market power. However, the members of the Tribunal are selected for their expertise and experience in order to evaluate evidence that is economic or commercial in nature, not to advance their views on the social merit of various groups in society. As noted by Iacobucci J. in the Supreme Court's decision in Southam, cited above at paragraph [48], at pages 773 and

774:

> As I have already said, the Tribunal's expertise lies in economics and in commerce. The Tribunal comprises not more than four judicial members, all of whom are judges of the Federal Court -- Trial Division, and not more than eight lay members, who are appointed on the advice of a council of persons learned in "economics, industry, commerce or public affairs". See Competition Tribunal Act, s.3. The preponderance of lay members reflects the judgment of Parliament that, for purposes of administering the Competition Act, economic or commercial expertise is more desirable and important than legal acumen.

**432** First, the Tribunal is of the view, as already stated, that distributional concerns do not fall within the ambit of the merger provisions of the Act. If Parliament had intended that transfers from consumers to shareholders be considered, it would no doubt have clearly stated this intent in the Act.

**433** Second, merger review must be predictable. Adopting Professor Townley's approach would result in decisions that vary from case to case depending on the views of the sitting members of the Tribunal regarding the groups affected by the mergers.

**434** Third, the deadweight loss resulting from a price increase is typically quite small as Professors Trebilcock and Winter note in their article, cited above at paragraph [427]. On the other hand, as the Commissioner observes, the transfer is much larger than the deadweight loss resulting from the instant merger. This being the case, a standard that includes the transfer as an effect under subsection 96(1) would effectively result in the unavailability of the section 96 defence.

**435** Professor Ward's evidence makes this clear. Using the calculations in table 8 of his initial report (exhibit A-2059 at 34), consider a large price increase of 15 percent. The resulting deadweight loss is 1.7 percent of sales but the transfer is 11.6 percent of sales when the price-elasticity of demand is -1.5. Accordingly, a merger that offered gains in efficiency of at least 1.7 percent of sales would be approved under a total surplus standard. However, under a consumer surplus standard, the efficiency gains would have to be at least 13.3 percent of sales.

**436** When the elasticity of demand is -2.5, the deadweight loss and transfer are 2.8 percent and 9.4 percent of sales respectively. Accordingly, the total surplus standard would approve a merger if efficiency gains were at least 2.8 percent of sales. However, a consumer surplus standard would reject a merger unless efficiency gains were at least 12.2 percent of sales.

**437** In an obiter dictum in the Hillsdown decision, cited above at paragraph [127], Reed J. appeared to favour the consumer surplus standard. However, as the above numbers indicate, applying a consumer surplus standard would lead the Tribunal to reject many efficiency-enhancing mergers on distributional grounds. As noted above, efficiency was Parliament's paramount objective in passing the merger provisions of the Act and it intended the efficiency exception in subsection 96(1) to be given effect. Accordingly, the Tribunal is not prepared to adopt a standard that frustrates the attainment of that objective.

**438** Fourth, omitting income and wealth redistributional concerns from merger review does not mean that these concerns are to be ignored by public policy. Indeed, governments at all levels have adopted specific tax and social policy measures to address their distributional objectives. The Tribunal regards these measures as more effective ways of meeting social policy goals. Blocking efficiency-enhancing mergers to achieve the same ends is, in our view, contrary to the Act.

**439** Fifth, the MEG's, cited above at paragraph [57], endorse the total surplus standard. Although the Tribunal is not bound by these guidelines, it recognizes that they contain a substantial degree of economic expertise and it agrees with the observation at footnote 57 therein that "[w]hen a dollar is transferred from a buyer to a seller, it cannot be determined a priori who is more deserving, or in whose hands it has a greater value".

(d) Other Effects

**440** The Commissioner submits that the ordinary meaning of "effect/effet", that is, something which flows causally from something else, is the most logical to apply to interpret that language used in section 96. The parties referred to The Shorter Oxford Dictionary, 3rd ed. (Oxford: Clarendon Press, 1973) at 631, which defines "effect" as "[s]omething caused or produced; a result, consequence. Correl. w. cause." Similarly, they referred to the Larousse de la Langue Française (Paris: Librairie Larousse, 1979) at 605, which defines "effet" as "[c]e qui est produit, entraîné par l'action d'une chose."

**441** The Commissioner further submits that, provided the effects flow from a prevention or lessening of competition resulting from the merger, section 96 does not place any other limitations upon the scope or range of "effects" to be considered, which includes detrimental effects of a merger that will affect consumers such as an increase in prices, a decrease in service, product choice or quality.

**442** The respondents submit that the test to be met under section 96 is that the efficiencies must offset any substantial lessening of competition. They further argue that a substantial lessening of competition is permitted provided it is outweighed by the efficiencies attributable to the merger. They also submit that the effects of the substantial lessening of competition are measured by the deadweight loss to the economy and exclude wealth transfers between consumers and producers, which are neutral to the economy.

**443** The Tribunal observes that an anti-competitive merger may well have other important economic and social effects. Job terminations and plant closures are often emphasized in the press, presumably because of their immediacy and significance to the people and communities involved.

**444** While not seeking to minimize the importance of these effects on those affected, the Tribunal wishes to point out that they are not restricted to anti-competitive mergers. Layoffs and closures often result from mergers and business restructurings that are not offensive and the Commissioner may take no notice thereof under the Act. Accordingly, the Tribunal is of the view that these effects are not to be considered when they result from anti-competitive mergers.

**445** As a result, the Tribunal cannot accept the Commissioner's submission that section 96 does not place any other limitations upon the scope or range of "effects" to be considered.

(e) Conclusion

**446** In final argument, the Commissioner refers to the "anti-competitive effects" of the merger as including the redistributive effects of the transfer. The Tribunal does not regard the redistributive effects of a merger as anti-competitive.

**447** The Tribunal further believes that the only effects that can be considered under subsection 96(1) are the effects on resource allocation, as measured in principle by the deadweight loss which takes both quantitative and qualitative effects into account. Accordingly, the Tribunal believes that the total surplus standard is the correct approach for analysing the effects of a merger under subsection 96(1).

**448** As a practical matter, the effects of an anti-competitive merger include effects that are difficult to quantify and may not be captured through statistical estimation of the deadweight loss. Subsection 96(1) specifically provides that gains in efficiency must both be greater than and offset the effects of any lessening of competition. Thus, it may be that, in a strict quantitative comparison of efficiencies and the estimated deadweight loss, the former exceeds the latter, yet the requirement to be "greater than" may not be met because of unmeasured qualitative effects.

**449** If the word "offset" (or in French, "neutraliseront") were taken to mean "prevent" or "neutralize", this would imply that efficiency gains had to prevent the estimated deadweight loss and the other effects of prevention or

lessening of competition from occurring or to neutralize these effects. Such interpretation would be inconsistent with the existence of the efficiency exception which clearly allows such effects. The Commissioner submits that "offset" (in French, "neutraliseront") must be interpreted to mean "compensate for" rather than "prevent" or "neutralize". The Tribunal agrees with this submission.

**450** Whether, in a given case, the efficiency gains "offset" the effects of any prevention or lessening is a matter which the Tribunal must assess and decide in light of the available evidence. However, the requirement to "offset" cannot be used to justify consideration of qualitative or other effects which are not open for consideration under the Act.

(9) Deadweight Loss

**451** In final argument, the Commissioner presented several estimates of deadweight loss, the transfer, and the balancing weights resulting from the calculations undertaken to apply Professor Townley's approach. Certain of these estimates were based on information provided in final argument that was excluded. Moreover, since the total surplus standard is, in our view, the correct standard to use in the trade-off analysis under subsection 96(1), the Tribunal will discuss only the deadweight loss estimate calculated from properly introduced information.

**452** The Commissioner adopts the approach presented in evidence by Professor Ward, whose expert report (exhibit A-2059) provides at table 8, on page 34, estimates of deadweight loss and consumer surplus transfer as percentages of initial sales under various assumed values of the price elasticity of demand. In that table, Professor Ward presents those percentage estimates for each of three values of the elasticity between -1.5 and -2.5 only, because at the time of his initial report, he did not have the evidence of Professors Plourde and Ryan that showed that demand for propane was inelastic and hence could not have a price-elasticity of less than -1.0.

**453** The Commissioner adopts Professor Ward's estimated price increases shown at table 2 on page 8 of his affidavit in reply (confidential exhibit CA-2060) for the residential, industrial, and automotive end-use segments of 11.7 percent, 7.7 percent and 8.7 percent respectively, and reduces each by 0.7 percent to take account of the pass-through of cost savings. Professor Ward obtained his estimates after the results of Professors Plourde and Ryan became available and, accordingly, he assumed an elasticity of -1.0 in obtaining those estimates. Since Professor Ward was not able to estimate the price increase for his "other" segment, the Commissioner adopts seven percent as appropriate for that segment because it was the smallest increase that Professor Ward found.

**454** The Commissioner presents estimates of 1998 combined sales of the merging companies in each of those segments: $94 million, $239 million, $139 million, and $113 million respectively, accounting for the combined total volumes sold by Superior and ICG. Thus, the Commissioner's segmented sales estimates are for combined total sales, not just the combined sales of the merging parties in overlapping areas. Since, according to Professor Ward's table, the deadweight loss varies directly with sales, the Commissioner's estimates thereof likely overstate the deadweight losses by segment in overlapping areas.

**455** The Commissioner obtains estimates of deadweight loss by segment by taking the segment sales and price increase information and applying them to Professor Ward's table where the assumed demand elasticity is -1.5. The resulting deadweight loss estimates based on 1998 sales data are as follows:

| | |
|---|---|
| residential | $0.8 million |
| industrial | $1.0 million |
| automotive | $0.7 million |
| other | $0.5 million |

| | |
|---|---|
| total | $3.0 million |

**456** The respondents point out that the estimates of deadweight loss would be lower had they been calculated at an industry demand of -1.0, as suggested by the work of Professors Plourde and Ryan. They also note the inconsistency in calculating deadweight losses assuming an elasticity of demand of -1.5 while using price increases estimated with an elasticity of demand of -1.0.

**457** The Commissioner submitted in final argument Table R1 which calculates the deadweight loss assuming a nine percent price increase across all segments in overlapping markets and a price elasticity of demand of -1.0. The resulting estimate of deadweight loss is $3.43 million, although the sales revenue figure used ($572 million) was among the materials submitted in final argument that were excluded.

**458** Even though it is probably overstated, the Tribunal is prepared to accept the deadweight loss estimate of $3.0 million put forward by the Commissioner, since the overstatement is inconsequential in view of our finding that the merger is likely to bring about gains in efficiency in the order of $29.2 million.

(10) Trade-off Analysis

**459** Pursuant to subsection 96(1), the Tribunal must ask whether the gains in efficiency exceed and offset the effects of any prevention or lessening of competition that the merger has brought about or is likely to bring about. The Tribunal observes that while the gains in efficiency claimed by the respondents have been measured and reduced to dollar figures, efficiency gains could also include qualitative elements such as, for example, better service and higher quality. No evidence of qualitative efficiency gains has been produced.

**460** Similarly, the effects of any lessening of competition can also have both measurable and qualitative elements. The estimated value of the deadweight loss, while measuring the effect of the higher price on resource allocation, may not capture lessening of service or quality reduction.

**461** For greater certainty, the Tribunal is of the view that all of the gains in efficiency must be compared with all of the effects of any prevention or lessening of competition, even though this requires judgment when combining measured gains (effects) with qualitative gains (effects).

**462** The Commissioner submits that subsection 96(1) requires the Tribunal to consider whether the efficiency gains would likely be realized absent the merger. The Commissioner criticizes the Cole-Kearney report for not considering whether claimed efficiencies could have been achieved through less anti-competitive means than a full scale merger. Following the decision on this point in Hillsdown, cited above at paragraph [127], at page 332, the Tribunal is of the view that the test to be applied is whether the efficiency gains would likely be realized in the absence of the merger. In dealing with this issue in Hillsdown, the Tribunal stated:

> The Director's position is that cost savings that do not arise uniquely out of the merger are not to be considered as efficiency gains. The respondents' position is that the test to be applied is whether the efficiency gains would likely have been realized in the absence of the merger. The tribunal accepts the respondents' position.

**463** The Tribunal finds that the estimated gains in efficiency from this merger are $29.2 million per year over 10 years and these gains in efficiency would not likely be attained if the order for total divestiture were made. The Tribunal finds that the estimated deadweight loss is approximately $3.0 million per year over the same ten-year period.

**464** The Commissioner submits that qualitative effects include distributional impacts and other qualitative elements

including changes to levels of service, product quality and product choice, increased probability of coordinated behaviour, and innovation. For the reasons already given, the Tribunal will not consider distribution impacts.

**465** The Tribunal took into account the increased probability of coordinated behaviour in its consideration of the evidence regarding a substantial lessening of competition. To the extent that the effect of such anti-competitive behaviour is a higher price, then it has already been reflected in the deadweight loss estimate. If there are other effects of coordinated behaviour to be considered under section 96, further and better evidence about those effects is required. It cannot suffice simply to restate the concern under section 92.

**466** A decline in service levels, holding quality of service constant, is also reflected in the deadweight loss estimate. However, the evidence indicates that ICG had established certain services and pricing arrangements (e.g., the Golf-Max program) that Superior and other propane marketers did not offer. Their removal or reduction would reduce the real output of the industry. Although no evidence was given on the likelihood or scope of the reduction or removal of these product offerings following the merger, the exercise of market power might take such forms together with, or instead of, a direct increase in price.

**467** The Tribunal must determine whether all of the gains in efficiency brought about or likely to be brought about by the instant merger are greater than the estimated deadweight loss and the negative qualitative effects resulting or likely to result therefrom. As noted above, this determination requires that the latter two components be combined and then compared with total efficiency gains. The Tribunal views the impact on resource allocation of the negative qualitative effects as minimal and as most unlikely to exceed in amount the estimated deadweight loss. Thus, the combined effects of lessening or prevention of competition from the instant merger cannot exceed, in the Tribunal's opinion, $6 million per year for 10 years. On this basis, the Tribunal finds that the gains in efficiency are greater than those effects.

**468** The Tribunal must also determine whether all of the gains in efficiency will offset those effects. Gains in efficiency exceed those effects by at least $23.2 million per year for 10 years and, in the Tribunal's opinion, adequately compensate society for those effects. Accordingly, the Tribunal finds that the gains in efficiency will offset those effects.

**469** For theses reasons, the Tribunal is of the view that the Commissioner's application for an order under section 92 of the Act should be denied.

## VII. DISSENT OPINION (MS. CHRISTINE LLOYD)

**470** There are several areas with respect to the appreciation of the facts underlying the efficiency defence and the legal interpretation of section 96 of the Act stated by the majority of the Tribunal with which I strongly disagree. The majority accepted for the most part the evidence on efficiencies claimed by the respondents, Superior and ICG. The respondents relied on the Cole-Kearney report; this expert report was prepared by two consulting firms whose mandate was to provide an opinion as to the value of the efficiencies that are likely to result from the merger. I have great concerns with certain aspects of the methodology and assumptions adopted by the experts that led to their calculations and resultant conclusions. Consequently, I am not satisfied, on a balance of probabilities, that the gains in efficiency as claimed by the respondents are likely to be brought about by the merger as required by subsection 96(1) and that the claimed efficiencies would not likely be attained if the order for total divestiture were made. Finally, when conducting the trade-off analysis in section 96, I conclude that even if $29.2 million of efficiencies were likely to be realized (as accepted by the majority), the proposed gains in efficiency will not be greater than and will not offset the effects of any prevention or lessening of competition that will result or is likely to result from the merger.

### A. QUANTUM OF EFFICIENCIES

#### (1) Problematic Aspects of the Methodology Used

**471** The respondents submit that the merger between Superior and ICG will allow them to achieve substantial gains in efficiency in the range of $40 million per annum based on the opinion of Cole-Kearney. They state that the aggregate of such gains is approximately $381 to $421 million measured in constant dollars over 10 years. I have great concerns regarding the respondents' efficiencies claimed in this proceeding as certain aspects of the methodology used to conduct the analysis are problematic.

**472** The efficiencies claimed by the respondents depend largely on the elimination of costs at the level of field operations, i.e., redundant branches and trucks and other related cost savings. Professors Schwindt and Globerman and Mr. Kemp state at page 23 of their report in rebuttal (confidential exhibit CA-3131) the following:

> C. Total Field Operations ($193.6 million, 48.3% of savings)
>
> Projected efficiencies generated at the field operations level are very significant, accounting for nearly half of the anticipated total. These efficiencies are largely attributable to the rationalization of the branch system and the improvement of delivery logistics. (emphasis added)

**473** These cost savings identified by Cole-Kearney are based on a definition of Superior's trade area size and overlaps with ICG's trade areas. The size of each trade area of Superior is defined on the basis of the farthest customer located from each respective branch as reported in the 1998 branch templates. This farthest distance then constitutes the radius of the trade area for each specific branch. The extent of the trade areas and trade area overlaps, in turn, constitute the framework on which the experts calculated the efficiencies claimed to result from the implementation of the merger of Superior and ICG.

**474** As stated above at paragraph [207] when assessing the validity of the 1998 branch templates, the Tribunal concludes that these templates are suspect and unreliable. Therefore, it appears that since Superior's trade areas may not be as large as 620 kilometers, relying on these estimates to determine the extent of the overlaps may well overstate the cost savings that can be realized. Consequently, the impact on the results of the calculated efficiencies remains unknown.

**475** Further, I have noted that the experts estimate trade area overlaps through a manual process which was not verified in a way to assure accuracy. In response to a question asked by the Tribunal, Eric Fergin, one of the respondents' experts responsible for this process, explained how these overlaps were identified:

> MS LLOYD: Getting back to the trade area size, Mr. Fergin, do you have any sort of scatter map or anything that indicates the customers so that we can actually see on a map indicating where the overlap is?
>
> MR. FERGIN: No, we don't. I don't have one with me. I know one was constructed -- sketches were constructed, because they were based on rough estimates looking at the two areas, the overall area that they overlaid, and based on the raw data that we had which was actually provided to the Bureau. I don't have a reference number for the documents.
>
> We did that, but unfortunately, no, I don't have a scatter map.
>
> MS LLOYD: It would be nice to see what that overlap is.
>
> MR. FERGIN: I'm afraid I don't have something like that. (emphasis added).
>
> transcript at 34:6722 (8 December 1999).

**476** As I mentioned earlier, the methodology to define the trade areas and their resultant overlaps raise significant concerns for errors that would impact on the quantum of the efficiencies claimed. By using the farthest point to

establish the radius as opposed to a defining line around the greatest density of customers, the respondents could have overstated the number of branches that could potentially be closed as well as the number of trucks and related equipment that could be eliminated. In fact, using smaller trade area definitions dictated by customer density may have resulted in no overlap between certain branches.

**477** Further, no mechanism or tools were used (other than the alleged review by Andrew Carroll of Superior, a process that remains unclear) to verify the validity of the analysis conducted by the respondents' experts. I am of the view that a thorough reality check should have been conducted. For instance, the respondents could have used a Geographic Information System (commonly referred to as "GIS") to create a scatter map to plot customer locations in relation to each of their respective branches. This system would have produced accurate trade area overlaps to assist the experts in determining the number of redundant branches and accurate drive time patterns. The fact that the experts did not have recourse to an equivalent safeguard, in my view, undermines greatly the validity of the findings made by the experts. They were discussed with Mr. Fergin at the hearing:

> MR. FERGIN: ... In fact, we don't have information of granularity to show where all the branches were in each particular area.
>
> I believe it was Ms Lloyd who asked us last Wednesday, in fact, if we had maps that plotted out the delivery sites relative to the branches, and as I stated at that time, we did not have that information.
>
> MS LLOYD: I thought you told me that you did it in lead-up to the analysis.
>
> MR. FERGIN: I'm sorry?
>
> MS LLOYD: I thought I understood that you actually did have it, but that was in the lead-up to the analysis, that you had done it. I must have misunderstood you.
>
> MR. FERGIN: We had done it for the areas that we rode along in during our ride-alongs, but we hadn't done it for all the particular customers that were served by a particular branch.
>
> MS LLOYD: I misunderstood you.
>
> MR. FERGIN: Okay. The other comment I have is: Mr. Schwindt indicated that our methodology in terms of determining the area served for Superior was based solely on the radius of the trade area as determined by the farthest customer.
>
> Now, that was the initial basis, but we didn't strictly use that information without going back to Andrew Carroll of Superior Propane, who was our key liaison on this project in terms of giving us information and validating information as to what areas, particular branches, particular satellites served to determine that would in fact be a valid area or it should be adjusted accordingly somewhat because of the fact that a situation like this might exist or there might be one far outlying branch.
>
> So the point I am trying to make is that: We did not simply use the branch radius as the only factor for determining the trade areas served by Superior for a given branch. (emphasis added)
>
> transcript at 37:7782, 7783 (14 December 1999).

**478** The only validation process presented by the respondents is that of the "ride-alongs", which were conducted to validate the model used to predict reduction in fleet and driver personnel and other results therefrom. They submit that these ride-alongs, which consist of spending a day with a driver delivering propane to customer locations, allow them to validate the model that they have developed. Yet, in cross-examination by the Commissioner, Mr. Fergin conceded that he had participated in only two ride-alongs in Sudbury (with Superior) and Stratford (with ICG) where a detailed analysis was done as to time spent on various activities (i.e., comparing time spent driving, pumping propane, delivering and generating delivery receipts). He mentioned that ride-alongs were also conducted without

tabulating the data in Moncton, Lloydminster, Concord, Vimont, Coquitlam and Burnaby (transcript at 37:7795 (14 December 1999)).

**479** I am of the view that the validation process that was conducted in this case is insufficient to provide the assurance that the quantum of the efficiencies claimed is accurate. Further, the validation process was only performed with respect to the efficiencies claimed at the field operations level, most particularly with respect to the fleet reduction (annualized savings of $2.6 million which represents $33.4 million over 10 years) and related costs. In addition, inadequacies are further demonstrated by the fact that ride-alongs were conducted and reported using a sample of only two locations, one Superior and one ICG. As well, no allowance for regional differences was accounted for in this analysis.

(2) Highly Optimistic Assessment (That Does Not Account for Any Costs)

**480** The Commissioner's experts point out that the evaluation made by Cole-Kearney of the efficiencies is highly optimistic not to say unrealistic because their projection of the efficiencies does not account for any costs resulting from the integration of the two companies. They point out at pages 9 and 10 of their report in rebuttal (confidential exhibit CA-3131) that Cole-Kearney did not account for transition and integration costs and some volume losses. As they stated:

> The projected efficiencies of this transaction are largely driven by the integration of customer support (the second tier of administration) and field operations. These two broad categories of activities account for nearly two-thirds of the estimated cost savings, and both are complex. The proposed integration would involve the merging of ICG's 100,000 customers with SPI's 200,000 customer base, the integration of and rationalization of ICG's 110 distribution sites with SPI's 140 sites, the integration of a substantial number of ICG's 700 employees into SPI's workforce of 1,300 people, and the integration and rationalization of an extensive delivery fleet. The business involves the distribution of propane, so integration will require the meshing of two complex networks. Moreover, the two enterprises have adopted fundamentally different operating philosophies. One, ICG, is moving towards a more centralized, information technology dependent model, while the other, SPI, continues to operate a more decentralized system. Given these facts, the integration of these two firms would appear to be a daunting task. However, the Kearney Report identifies very few costs attributable to the actual process of integration.

**481** It is indubitable that the rationalization of the two site networks will generate real resource savings. However, the respondents' experts did not account for any increases in operating expenditures or ongoing capital expenditures that will result from additional costs related to volumes, staffing levels and number of customers. I am in agreement with Professors Schwindt and Globerman and Mr. Kemp when they state in their report in rebuttal (confidential exhibit CA-3131) at page 24 that:

> ... Volumes in all rationalised trade areas will increase, and, at some, volumes will more than double. Staffing will increase at the branches .... [C]ustomers per branch will increase significantly, and this will increase the number of administrative staff required to serve these customers .... [M]any tasks will be reallocated to branch employees .... This will also increase staffing .... [I]ncreased volumes will require more delivery and service staff ....

**482** Further, Professors Schwindt and Globerman and Mr. Kemp point out that equipment located at the branch or operating from the branch (including storage tanks and trucks) will increase, which, in turn, will require more space and expanded infrastructure and further storage space for inventories (parts and customers tanks). This will result in increased costs that have not been accounted for by the respondents' experts. In support of their criticism, the Commissioner's experts examined changes to operations and used the example of the Peterborough branch (a branch where the rationalization is straight forward) to demonstrate the effects that the integration will have on costs, as shown at table 7 on page 26 of their report in rebuttal (confidential exhibit CA-3131). They conclude at

page 26 that:

> The staffing level will increase by 60 percent. Cylinder operations will be consolidated at this site which will increase cylinder truck traffic. The bulk delivery fleet will double. The increased fleet will require additional maintenance capacity on the site as well as general access and parking area. This could require reconfiguration of the site to handle the step change in delivery equipment. Bulk delivery volumes are projected to increase by 220 percent. Such a large increase will mean that both primary deliveries and bulk truck daily liftings will also increase proportionately. This suggests that the site will have to be reconfigured to handle the significant increase in load factors. (emphasis added)

**483** The expert opinion of Professors Schwindt and Globerman and Mr. Kemp, as stated above, supports the Commissioner' submission that the efficiencies claimed by the respondents are overstated and hence, have not been demonstrated on a balance of probabilities:

> Secondly, we reiterate that the efficiency gains that were used for the purposes of this calculation of 21.2 million, on an annualized basis, is overstated for the reasons that we set out in the quantitative section of our materials.
>
> While that represents taking off the deductions that we were able to specifically identify in the evidence of Professors Schwindt and Globerman and as detailed in the argument, we have pointed out many instances where the Respondents' efficiency gains are excessively optimistic, exaggerated, or don't meet the standard, in our submission, of being established on a balance of probabilities. (emphasis added)
>
> transcript at 44:8737 (4 February 2000).

**484** As stated in paragraph 5.7.2 of the MEG's, cited above at paragraph [57], and as discussed by the author A. Neil Campbell in Merger Law and Practice, The Regulation of Mergers under the Competition Act (Scarborough: Carswell 1997) at 162, I am of the view that efficiencies should be measured net of the implementation costs that would be incurred in obtaining them. Therefore, "retooling" and other costs necessary to achieve efficiency gains should be deducted from the total value of the efficiencies.

**485** In light of my remarks on the methodology used by the experts and the insufficient consideration being given to additional costs that will result from the integration of field sites, I am of the view that the respondents have not demonstrated on a balance of probabilities the existence of the claimed $40 million of efficiencies per annum. As I have explained earlier, some problems identified with the methodology undermines greatly the validity of the efficiencies claimed by the respondents. There is no question that efficiencies can be realized in any merger or most particularly in this merger. However, the requirement under section 96 of the Act is to demonstrate the existence or the likelihood that the gains in efficiency will be brought about by the merger, hence the quantum of the claimed efficiencies on a balance of probabilities. In my view, the respondents have not met their burden of proof on that crucial element of their efficiency defence. As a result, I do not accept the respondents' efficiencies claim of $40 million per annum nor the reduced quantum of $29.2 million of efficiencies as accepted by the majority. Since I am not able to measure the degree to which these errors have affected the results nor able to quantify the inevitable costs that will result from this merger, I am not in a position to assess the real value of the efficiencies that will result or is likely to result from the merger and, therefore, will not speculate on their quantum.

### B. THE MERGER HAS BROUGHT ABOUT OR IS LIKELY TO BRING ABOUT GAINS IN EFFICIENCY (I.E., LIKELY TO BE REALIZED POST-MERGER)

**486** The respondents have not convinced me on a balance of probabilities that the $40 million of efficiencies claimed will be realized for the reasons stated above. In addition, regardless of the quantum of efficiencies that theoretically could be realized, the Tribunal has not been provided, in my opinion, with any evidence that they are likely to materialize post-merger.

**487** In my view, the term "likely" used in section 96 requires more than the sole demonstration of the quantum of

possible efficiencies. Rather, I believe that the term "likely" requires some evidence of the implementation process leading to the materialization of the claimed efficiencies. It is my opinion that evidence of this nature is necessary to provide the Tribunal with a level of assurance necessary to conclude that the efficiencies are likely to be realized post-merger (i.e., implemented by management).

**488** Evidence before the Tribunal stresses the importance of the merging parties having a detailed plan to ensure success of the merger. On that point, Paul Inglis, one of the respondents' experts on efficiencies, discussed a study that examines 115 mergers that took place between 1993 and 1996 in North America and which identifies the factors contributing to a successful merger. In that regard, Mr. Inglis explained that the existence of a business plan was one of the key factors leading to a successful merger:

> Success in a merger is, in large part, determined during the planning stage, but of course is executed after the merger happens. You have to make sure that you follow through on the good plans that are made up front. And so I would like to talk about, once again, the post-merger factors; and that is once the deal has consummated, once the agreement has been made.
>
> What are the things that allow us to believe that there is a good chance that the merger will be executed? Again, there are five things that we believe correlate. Is there a clear vision and strategy for the company? Do they know who the management is going to be? Do they have a good plan for putting that management in place? Have they got the capabilities to show results early and to gain momentum from developing those results? Have they recognized that there are cultural differences and do they have a plan to break through those cultural differences and meld the two organizations together? And finally, have they got a communications plan in place that will help them to execute that change in the cultures?...
>
> Let me turn next to determine the management responsibility point. Now, already there has been an identification of how many people will be in the management team. They plan to go forward with ten senior management positions. And they have a pool of senior resources to draw from. And that pool includes the likes of Geoff Mackey and Peter Jones and the other people that are the senior managers at ICG, as well as the people inside Superior. (emphasis added)
>
> transcript at 33:6347, 6348, 6350 (7 December 1999).

**489** Mr. Inglis was touching upon a crucial point when addressing the importance of having an implementation plan in order to assure that the claimed efficiencies are executed. In the absence of such a plan, there is no assurance or any indication as to the degree of probability that this merger will achieve the efficiency gains identified by the experts.

**490** A business plan setting out the implementation process/action plan outlining time frames for each step of the integration of the merger is necessary to achieve the claimed efficiencies. I take note that Mr. Inglis mentioned that Superior had a plan that was well articulated and that had been scrutinized over a long time frame. Unfortunately, the Tribunal was not presented with that alleged plan or any other plan. In fact, no such evidence was presented at the hearing. Mr. Schweitzer, Superior's Chief Executive Officer, the sole representative of Superior's management who testified at the hearing, did not provide evidence of the existence of a post-merger plan. It appears to me that a detailed business plan which expresses clearly the commitment and accountability of Superior's management (including the commitment of the Chief Executive Officer) should have been demonstrated. Further, there is no evidence that any study or due diligence was conducted to determine the cost effectiveness of merging the two companies prior to the decision by Superior to acquire ICG. Had this exercise been undertaken, the cost savings presented by Cole-Kearney would have had more credibility. Consequently, it appears to me that the realization of the efficiencies claimed strictly remain possibilities and not probabilities hence, the respondents have not demonstrated on a balance of probabilities that the efficiencies are likely to be realized.

**491** One could argue that the Management Agreement referred to at paragraphs [330]-[345], which provides incentives to SMS to increase the profitability of Superior and the cash distribution to unitholders of the Superior Income Fund (cash distribution), further supports the view that the efficiencies are likely to be realized. However, since the additional profits, which lead to SMS's entitlements can come from either an increase in price resulting

from the exercise of market power and/or from cost reductions, I am of the view that the Management Agreement does not offer the level of assurance necessary to conclude that extra profits will be generated from the realization of the claimed efficiencies and hence, that these efficiencies are likely to be achieved.

**492** In the absence of any provision under the Act regarding the enforcement of the outcome, (i.e., the realization of the claimed efficiencies), it is even more critical that the respondents demonstrate that the merger is likely to bring about gains in efficiency not solely on a theoretical level through experts but also through direct evidence that this is the direction that management is committed to seriously undertake with some assurance of completion post-merger. Without such a crucial piece of evidence, it appears to me that the efficiencies claimed remain only a theoretical exercise that may never be implemented by management. This demonstration that the merger is likely to bring about gains in efficiency is an important element of the efficiency defence that they had to demonstrate in order to meet their burden of proof.

**493** In light of my previous comments regarding the efficiencies claimed by the respondents' experts and the lack of information regarding the alleged commitment of management to the actual implementation, including time frames dedicated to each step of the implementation process, I am of the view that the requirement that the respondents must demonstrate that the merger has brought about or is likely to bring about gains in efficiency has not been met.

## C. "THAT THE EFFICIENCIES WOULD NOT LIKELY BE ATTAINED IF THE ORDER WERE MADE"

**494** Subparagraph 96(1) of the Act provides that:

> 96.(1) The Tribunal shall not make an order under section 92 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.
>
> (2) In considering whether a merger or proposed merger is likely to bring about gains in efficiency described in subsection (1), the Tribunal shall consider whether such gains will result in
>
> (a) a significant increase in the real value of exports; or (b) a significant substitution of domestic products for imported products.
>
> (3) For the purposes of this section, the Tribunal shall not find that a merger or proposed merger has brought about or is likely to bring about gains in efficiency by reason only of a redistribution of income between two or more persons. (emphasis added)

**495** While the Commissioner bears the onus of proving the effects of any prevention or lessening of competition resulting from the merger on a balance of probabilities, it is the respondents' burden to prove all the elements of their defence in order to be successful. These elements are: the existence of the claimed efficiencies, the likelihood that they will be brought about by the merger (realized post-merger through their actual implementation), the fact that they would not likely be attained if the order for total divestiture were made and that they are not pecuniary in nature. Once a determination has been made of what gains (both quantitative and qualitative) should be considered in the trade-off analysis, then the balancing process can take place.

**496** Indeed, section 96 limits the efficiency gains that can be considered in the trade-off analysis to those that would not likely be attained if the order were made and to those that do not constitute a redistribution of income between two or more persons. While I agree with the majority that only efficiencies that constitute "real" resource savings must be considered and not those that are pecuniary in nature, I disagree with their appreciation of the requirement set out in subparagraph 96(1) and that the gains in efficiency would not likely be attained if the order were made.

**497** This requirement of subparagraph 96(1) that they would not likely be attained if the order were made leads to this question: would the gains in efficiency likely be realized if the order for total divestiture were made? In other words, if the order for total divestiture were made, would the two companies independently likely realize gains in efficiency in some other way? The burden of proving this element also falls on the respondents and, in my view, has not been met on a balance of probabilities.

**498** Indeed, only those gains which would not likely be attained if the order were made can be claimed by the respondents. This requirement is to ensure that gains that would likely be obtained absent the merger for instance as a result of internal growth, merger or joint venture with a third party, restructuring, or contractual arrangements (e.g., specialization agreement) are excluded from efficiencies claimed. Therefore, it appears that the merging parties had the onus of providing a reasonable explanation as to why efficiencies would not likely be sought through an alternative mean if the order for total divestiture were made.

**499** In this case, the respondents have not, in my view, proved that the claimed efficiencies would not likely be attained if the order for total divestiture were made. Cole-Kearney's mandate was to provide an opinion as to the value of efficiencies that were likely to result from a merger of Superior and ICG. Their report states that alternative means were explored within the context of common industry practice such as internal growth, merger or joint venture with a third party or specialization agreement or licensing lease or other contractual arrangements. On that basis, they concluded that the merger is the only means by which to achieve efficiencies. No comparative evidence was provided on the results arising from the value of efficiencies from alternative means to assure the Tribunal that a merger was the only means by which to achieve the efficiencies. Surprisingly, restructuring was not mentioned by the experts.

**500** Further, no evidence in support of their conclusions was provided to the Tribunal nor any explanation as to why measures such as restructuring would not likely be undertaken by Superior to reduce its costs in order to achieve efficiencies in some other way, absent the merger. Indeed, while evidence was provided regarding ICG's transformation process (a process that led to efficiencies which were properly not claimed by the experts), no evidence was provided as to what Superior would or would not likely undertake to achieve efficiency gains if the order were made. The Tribunal does not have evidence to conclude that Superior, on its own, had already "cut-out the fat" within its organization before undertaking the merger with ICG. Consequently, the efficiencies claimed by the respondents could include cost savings that Superior would likely achieve on its own, absent the merger. Such efficiencies resulting from Superior's own restructuring would have been discounted from the efficiencies claimed. Indeed, as stated in the MEG's, cited above at paragraph [57], where some or all of the claimed efficiency gains would likely be attained through other means if the order were made, they cannot be attributed to the merger and hence, must not be considered in the section 96 trade-off analysis. For these reasons, I am of the view that the respondents failed to prove that the gains in efficiency would not likely be attained if the order were made.

## D. ISSUES REGARDING THE TRADE-OFF ANALYSIS

**501** As stated above, the respondents argue that the test to be met under section 96 of the Act is that the efficiencies must be greater than and offset any substantial lessening of competition and that the effects of such are measured by the deadweight loss to the economy and exclude wealth transfers between producers and consumers which are neutral to the economy.

**502** The Commissioner submits that in conducting the trade-off analysis set out in section 96, the Tribunal has a statutory responsibility to exercise its judgment as to the weight to be accorded to the transfer from consumers to producers. Hence, he submits that applying a standard with a fixed predetermined weight would be contrary to section 96. Further, the Commissioner submits that the efficiency gains do not offset, i.e., "neutralize" or "compensate for", the anti-competitive effects caused to the economy as a whole by this merger.

**503** The majority accepted that $29.2 million of efficiencies per annum is likely to be realized and is satisfied that

the gains in efficiency are greater than and offset the effects of any prevention or lessening of competition that is likely to result from the merger. In their view, these quantitative efficiencies are greater than and offset the deadweight loss to the economy evaluated at $3 million per annum and the qualitative effects of any prevention or lessening of competition.

**504** I agree with the majority that the trade-off analysis must be conducted through a single test where quantitative (productive) and qualitative (dynamic) efficiency gains together must be greater than and offset the quantitative (deadweight loss) and qualitative (e.g., reduction in non-price dimensions of competition) effects of any prevention or lessening of competition resulting from the merger. While I agree with the single test approach (i.e., as opposed to two tests, one quantitative and one qualitative), I disagree with their interpretation of the word "offset" in subsection 96(1) and with the weight that they attach to the effects of this merger.

**505** It is clear to me that Parliament intended the members of the Tribunal to exercise their judgment when assessing the trade-off set out in section 96 of the Act. During the proceedings of the Legislative Committee on Bill C-91, there were several references to the fact that the terms used in that section should not be so precise as to restrict the Tribunal's interpretation and discretion. Rather, there was an agreement that the Tribunal should have the jurisdiction to exercise its discretion based on the merits of a specific case. It appears that the legislator intended that the Tribunal should not become so rigid when applying the law as to prevent some mergers that would benefit the economy and conversely allowing others that would clearly not benefit the economy. Therefore, the legislator decided not to provide a specific list of factors in addition to those already stated in subsection 96(2); the increase in the real value of exports and substitution of domestic products for imported products. Instead, the legislator preferred to rely on the discretion of the Tribunal members who have expertise to hear competition law matters.

**506** While I recognize that efficiencies are given special consideration under section 96 and may constitute a defence to an otherwise anti-competitive merger, it appears to me that section 96 is an exception to the application of section 92 of the Act and not an exception to the Act itself. As Parliament stated, the trade-off set out in section 96 involves a balancing process and does not constitute, in my view, an absolute defence where the effects of the anti-competitive merger ought to be ignored. By that, I mean while the section 96 trade-off gives precedence to the gains in efficiency likely to result from the merger, this section must be interpreted in accordance with the objective and goals of the Act. This objective is to maintain and encourage competition in Canada in order to achieve the goals of the Act (i.e., the promotion of the efficiency and adaptability of the Canadian economy, the expansion of opportunities for Canadian participation in world markets, the equitable opportunity for small and medium-sized enterprises to participate in the Canadian economy and the provision of competitive prices and product choices to consumers). Therefore, it appears to me that the effects of any prevention or lessening of competition, which are contrary to the goals stated in the purpose clause of the Act, ought to be considered (for instance, the reduction or loss of consumer choice) in the trade-off analysis in order to determine whether the gains in efficiency are greater than and offset those effects.

**507** In my view, if the analysis under section 96 were so simplistic as to only require the comparison between quantitative efficiency gains and the deadweight loss to the economy, this could lead to distorted outcomes. For instance, such a narrow interpretation would mean that an anti-competitive merger would more easily meet the test set out in the section as the demand for the relevant product becomes less elastic (i.e., less price-sensitive). This perverse result arises from the fact that the calculated deadweight loss is proportional to the elasticity of demand. Therefore, following the interpretation of the majority, smaller gains in efficiency are required to outweigh and offset the deadweight loss to the economy when the demand is inelastic. In my view, there is no obvious reason to explain why Parliament would have written section 96 to give preference to anti-competitive mergers involving products for which demand is relatively inelastic (e.g., commodities).

**508** Consequently, I am of the view that the qualitative effects must be given appropriate consideration in the trade-off analysis. Indeed, while the deadweight loss can simply be depicted on a matrix and quantified, a matrix does not take into account the peculiar effects of the merger under review. As it is recognized by authorities in the field and by the MEG's, cited above at paragraph [57], some effects of a merger cannot be valued in dollar terms, for

instance reduction in service, quality, variety, innovation and other non-dimensions of competition. Therefore, these effects must receive a weight that is qualitative in nature. Accordingly, as certain effects in this merger cannot be quantified, I am of the view that they must be considered as qualitative and given an appropriate weight in the trade-off analysis.

**509** As I explained earlier, I do not accept the quantum of efficiencies as adopted by the majority. However, I will use that amount in table 2 (contained in paragraph [512]) simply for the purpose of illustration. As seen in table 2, which compares the efficiency gains claimed in this merger to the effects of any prevention or lessening of competition, the respondents have not claimed any qualitative effects that will benefit society as a whole. For instance, they do not claim any dynamic efficiencies or that the efficiencies will result in a significant increase in the real value of exports as stated at subsection 96(2) of the Act. Therefore, I cannot conclude that this merger will generate qualitative gains in efficiency that will benefit the economy as a whole.

**510** As to the qualitative effects of any prevention or lessening of competition, I have identified some that have not been given, in my view, sufficient weight in the analysis conducted by the majority. These effects are the loss of a vigorous competitor, which reduces consumer choice generally, particularly for national account customers and the absence of choice due to the elimination of competition in 16 markets. Further, the merged entity will have the ability to exercise market power which may result in the imposition of unilateral price increases and/or a reduction or elimination of programs such as the Cap-It and Auto-fill offered to customers. Conversely, the merged entity could use its market power to reduce prices for a period of time in order to squeeze competitors out of the market. This latter effect would be contrary to one of the goals stated at section 1.1 of the Act which seeks to provide an equitable opportunity for small and medium businesses to participate in the Canadian economy.

**511** Finally, I am of the opinion that consideration must be given to the significant wealth transfer from consumers to producers that will result from a price increase. Controversy surrounds the issue as to whether the wealth transfer is an effect that should be considered in the analysis stated at section 96. While a wealth transfer resulting from a merger is deemed to be neutral from a pure economic standpoint, it is not neutral in the context of the purpose clause of the Act which states that the objective is to promote and encourage competition in order to, among other goals, provide consumers with competitive prices and product choices. I am of the view that if Parliament's intention were that gains resulting from higher profits (due to a reduction in competition) and achieved at the expense of consumers should be viewed as neutral, surely it would have stated so in the Act. Indeed, if this had been the intention of the legislator, no references would have been made to consumers in section 1.1 and further, the term "effects" in section 96 would have been defined as to exclude any consideration of that nature. Therefore, I agree with the obiter dictum of Reed J. in Hillsdown, cited above at paragraph [127], at page 337, that the word "effects" should not be given such a restrictive interpretation as to exclude the transfer from consumers to producers.

**512** I am of the opinion that the wealth transfer from consumers to producers should not be viewed as a quantitative effect. There are no provisions in the Act suggesting that the effects must be quantified. It is my opinion that the transfer should be given qualitative consideration in the balancing process, which requires an exercise in judgment. A qualitative consideration allows for flexibility in the evaluation of each individual case under review.

TABLE 2: Trade-off Analysis

| | Quantitative | Qualitative |
|---|---|---|

| | | |
|---|---|---|
| Positive | $29.2 million as accepted by the majority (see my dissenting opinion above) | The respondents provided no evidence of any qualitative "positive" effects. |
| Negative | $3 million (deadweight loss) | Loss of a vigorous competitor which reduces consumer choices.<br><br>Absence of choice for consumers in 16 markets and for national account customers.<br><br>Ability to exercise market power that may result in:<br>- the imposition of a unilateral price increase or price decrease ("to squeeze competitors out" of the market);<br>- the reduction or elimination of programs offered to customers (i.e., Cap-It, Auto-fill, etc.);<br>- the reduction or elimination of services (e.g., delivery services in certain areas); and<br>- significant wealth transfer from consumers to producers. |

**513** I am of the view that when assessing the gains in efficiency against the effects of any prevention or lessening of competition, the claimed efficiencies are not greater than and do not offset these effects.

**514** As stated by the Commissioner, I am of the view that in order for the defence to be successful, the respondents must demonstrate that the efficiencies will be greater than and will offset (i.e., compensate for) the effects of a merger. The respondents provided no evidence that the efficiencies claimed will compensate for the detrimental effects that will result from the merger. For example, the respondents could have claimed that the merger is likely to bring about dynamic efficiencies arising from innovation that will benefit the Canadian economy. Such qualitative efficiency gains could have been assessed in the trade-off analysis as ways to compensate for the detrimental effects caused to the economy as a whole. However, the respondents did not even attempt to present any such beneficial effect to the economy that will result from the merger.

## E. CONCLUSION

**515** In light of my dissenting reasons, I conclude that the respondents have not met their burden of proof of demonstrating, on a balance of probabilities, that the merger has brought about or is likely to bring about gains in efficiency that will be greater than and will offset the effects of any prevention or lessening of competition. Therefore, the Tribunal should make the order for total divestiture by Superior of all of ICG's shares and assets (including those of the previously integrated branches thereof) formulated pursuant to section 92 of the Act.

## VIII. ORDER

**516** The Tribunal hereby orders that the Commissioner's application for an order under section 92 of the Act is denied.

DATED at Ottawa, this 30th day of August, 2000.

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

(s) Marc Nadon

* * * * *

GUIDE TO ACRONYMS

| | |
|---|---|
| 2SLS | two-stage least squares |
| cpl | cents per litre |
| EBITDA | earnings before interest, taxes, depreciation and amortization |
| IOL | Imperial Oil Limited |
| mbpd | million barrels per day |
| MEG's | Merger Enforcement Guidelines |
| OLS | ordinary least squares |
| SMS | Superior Management Services Limited Partnership |

# Nadeau Poultry Farm Ltd. v. Groupe Westco Inc., [2009] C.C.T.D. No. 6

Canada Competition Tribunal Decisions

Canada Competition Tribunal

Ottawa, Ontario

Before: Blanchard J. (Presiding), H. Lanctôt and P.A. Gervais

Heard: November 17-21, 24-28 and December 2-3, 2008.

Decision: June 8, 2009.

File No.: CT-2008-004

Registry Document No.: 0532

**[2009] C.C.T.D. No. 6** | *[2009] D.T.C.C. no 6* | *2009 Comp. Trib. 6*

Reasons for Order and Order IN THE MATTER of the Competition Act, R.S.C. 1985, c. C-34, as amended; AND IN THE MATTER of an Application by Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited for an Order pursuant to section 75 of the Competition Act; AND IN THE MATTER of an Application by Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited for an Interim Order pursuant to section 104 of the Competition Act Between Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited (applicant), and Groupe Westco Inc. and Groupe Dynaco, Coopérative Agroalimentaire, and Volailles Acadia S.E.C. and Volailles Acadia Inc./Acadia Poultry Inc. (respondents)

(484 paras.)

## Appearances

For the applicant: Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited: Leah Price, Ron Folkes, Andrea McCrae, Joshua Freeman.

For the respondents: Groupe Westco Inc.: Eric C. Lefebvre, Martha Healey, Denis Gascon, Alexandre Bourbonnais, Geoffrey Conrad.

Groupe Dynaco, Coopérative Agroalimentaire: Olivier Tousignant.

Volailles Acadia S.E.C. and Volailles Acadia Inc./Acadia Poultry Inc.: Valérie Belle-Isle.

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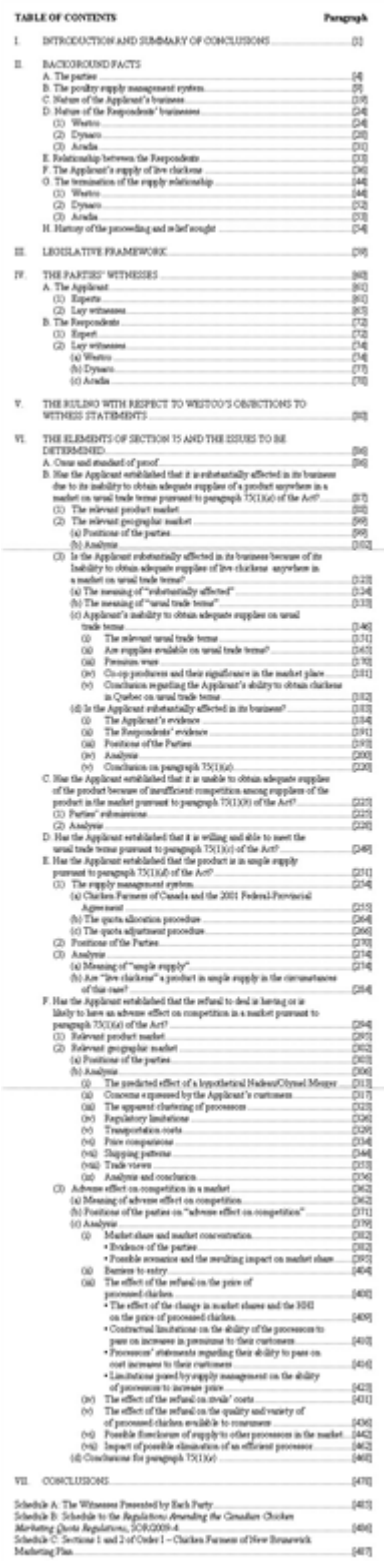
**REASONS FOR ORDER AND ORDER**



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## I. INTRODUCTION AND SUMMARY OF CONCLUSIONS

**1** Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited (the "Applicant" or "Nadeau") brings an application for an order directing the Respondents to accept Nadeau as a customer and to supply live chickens to Nadeau on the usual trade terms. The application is made pursuant to section 75 of the *Competition Act*, *R.S.C. 1985, c. C-34* (the "Act").

**2** In the reasons that follow, we[1] find that:

(a) The Applicant has established that it is substantially affected in its business due to its inability to obtain adequate supplies of a product anywhere in a market on usual trade terms;

(b) The Applicant has failed to establish that it is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market;

(c) The Applicant has established that it is willing and able to meet the usual trade terms of the suppliers of the product;

(d) The Applicant has not established that the product is in ample supply; and

(e) The Applicant has not established that the refusal to deal is having or is likely to have an adverse effect on competition in a market.

**3** Since the Act requires that all of the requirements of subsection 75(1) be met for an order to issue, it follows that the application will be dismissed.

## II. BACKGROUND FACTS

### A. **The parties**

**4** The Applicant, Nadeau Ferme Avicole Limitée/Nadeau Poultry Farm Limited, is a corporation incorporated under the laws of the Province of New Brunswick and is a wholly-owned subsidiary of Maple Lodge Holding Corporation ("Maple Lodge"), which is one of Canada's largest chicken processors.

**5** Maple Lodge employs about 2,300 people and owns 100% of the shares of two chicken processing facilities in Canada, one in Norval, Ontario, which is operated by Maple Lodge Farms Ltd. ("Maple Lodge Farms"), and one in St-François de Madawaska, New Brunswick (the "St-François Plant"). The St-François Plant is operated by the Applicant.

**6** The Respondent Groupe Westco Inc. ("Westco") is a corporation incorporated under the laws of the Province of New Brunswick. Westco is highly integrated in the chicken industry. It owns or controls egg hatching production quota, farms, chicken production quota and chicken production farms. Through its subsidiaries, Westco owns or controls around 50.9% of New Brunswick's chicken production.

**7** The Respondent Groupe Dynaco, Coopérative Agroalimentaire ("Dynaco"), is a co-operative registered in the Province of Quebec. Dynaco has interests in certain chicken production facilities in the Province of New Brunswick. Dynaco is highly integrated in a number of industries, including the chicken industry. Dynaco is the [TRANSLATION] "fifth most significant co-operative in the Province of Quebec".

**8** The Respondent Volailles Acadia S.E.C., created under the laws of the Province of Quebec, is registered as an extra-provincial limited partnership in the Province of New Brunswick, and the Respondent Volailles Acadia Inc./Acadia Poultry Inc., incorporated under the laws of Canada, is registered as an extra-provincial corporation in the Province of New Brunswick (collectively, "Acadia"). Acadia's main activity is the production of chicken and turkey.

### B. **The poultry supply management system**

**9** The events underlying this proceeding occurred in the context of Canada's poultry supply management system. It is therefore useful to understand the workings of that system.

**10** Under Canada's supply management system, the typical set of market-determined economic arrangements is replaced with a detailed and complex set of regulations, akin to a centrally planned economic system. It has been described as being, in effect, a state-mandated cartel arrangement.

**11** Supply management in the poultry sector evolved as a policy response to the interprovincial competition in chicken and egg marketing; also known as the "chicken and egg wars". The policy regime originated in the early to mid-1970s and replaced open, and at times aggressive, competition with mandated market shares enforced by provincial and producer marketing quotas. As a result, the poultry sector is likely the most highly regulated industry in the Canadian economy.

**12** Supply management is commonly said to rest on three pillars, namely production control, price control and import control. We will briefly deal with each of these in turn.

**13** Chicken farmers or producers are limited to producing their quota amounts, which are measured in kilograms of live weight. A producer receives a single quota applicable to all of his or her production regardless of the intended destination. Non-compliance can give rise to penalties. National quotas are set by a federal marketing agency, the Chicken Farmers of Canada (the "CFC"). Its prime responsibility is to ensure that Canadian chicken producers supply a sufficient quantity of product to ensure that the domestic market meets consumer demand. The CFC then allocates provincial quotas of chicken to the provinces. In turn, the provincial marketing boards set individual quotas for producers. Unlike some other provinces, New Brunswick currently does not have regulations requiring producers to direct their live chicken supply to any particular processor. Since 1995, the national quota or the quantities of chicken required have been determined at the provincial level through a process known as the "bottom-up" approach. Under this approach, provincial processors negotiate with provincial marketing boards to determine provincial quota requirements. The provincial requirements are then aggregated and adjusted, if necessary, by the CFC. The national quota is thus the aggregate of provincial requirements and is set periodically, "every 6 or 7 weeks depending on the year of production" according to the expert evidence adduced.

**14** While there is no legislation preventing the interprovincial trade of chickens, the evidence indicates that relatively few chickens move across provincial borders. In 2005, interprovincial trade in chickens involved only 4% of total Canadian production. A producer wishing to export chickens to another province must obtain a license from the CFC. The license is issued by the CFC as long as the producer is in compliance with statutory regulations.

**15** Farmers may buy and sell their quotas, but certain restrictions apply. One such restriction is that owners themselves must be engaged in the production of chickens. New entrants have little option but to purchase quota from existing farmers, which can prove costly. The cost of quota for an average-size chicken farm in 2007 climbed to $2.25 million. In certain provinces new quotas are reserved for new entrants at no cost, but these quotas are limited. In most jurisdictions, free entry involves a very long wait and is not a realistic option for new entrants. The more realistic approach has been for new entrants to purchase existing quotas from producers. Most new quota allocations are issued to existing producers.

**16** The minimum price at which chickens may be sold in respective provinces is set by provincial marketing boards. Under law, the provincial boards are charged with the task of restricting production so that farmers can earn a reasonable margin, but at the same time they must prevent prices from rising so high that demand is choked off. The evidence would suggest that the boards have been successful, since chicken production in Canada has risen by 77% in the last 15 years. Certain provinces have used the price negotiated in Ontario as the benchmark price for their own negotiations. Since May 2003, the price in Ontario is established by a formula which includes taking into account market conditions, input costs based on a cost-of-production formula, and prices set in neighbouring provinces.

**17** Protection from imports from other countries is also an important feature of the supply management scheme. To import chickens into Canada, a special permit is required. Import quotas, also known as "tariff rate quotas" ("TRQs"), specify the quantity of imports that are allowed, and are allotted annually and not permanently. These

quotas are managed by the federal Department of Foreign Affairs and International Trade, whose role it is to allocate the TRQs to individual firms and set and maintain the rules by which they are administered. The TRQs are automatically set at 7.5% of the previous year's production. Allocation procedures vary by commodity and are affected by increases or decreases in demand of the commodity in question and other factors. For the most part, quota holders are likely to have their import quota allotment renewed or re-allocated in subsequent years.

**18** Given the significance of the supply management system and its impact on this case, we shall conduct a comprehensive review of the legislative and regulatory framework of the system later on in these reasons and particularly in those parts relating to paragraphs 75(1)(*b*) and (*d*) of the Act.

C. **Nature of the Applicant's business**

**19** The Applicant is a primary processor that slaughters live chickens and sells them (in whole or in parts) to further processors and other customers. The Applicant's only business is the St-François Plant, which was acquired in 1989. At the time of the acquisition, the former owner was insolvent. The Applicant has invested millions of dollars over the years to improve and maintain the St-François Plant. It has been the only chicken processing plant in New Brunswick since 1992 and has been slaughtering all of the chickens produced in New Brunswick since 1998.

**20** In February 2002, the St-François Plant was damaged by a fire that resulted in the closure of operations. It was rebuilt as a "broiler plant" and was up and running again in November 2002. During the rebuilding period, the Applicant continued to purchase all of New Brunswick's live chicken production and arranged to have the chickens slaughtered at other processing plants. According to the Applicant, the newly rebuilt St-François Plant is the most modern and efficient chicken processing facility in Canada.

**21** The Applicant currently has about 375 employees. It is the largest employer in the St-François community. At present, it runs one production line with two shifts, averaging sixty hours a week, five days a week.

**22** The Applicant states that it requires a full range of birds within certain weight tolerances in order to meet its customers' specifications. The Applicant offers both air-chilled and water-chilled chicken. Air-chilled chickens, which are considered to be "premium" chickens, are cooled after being eviscerated by using cold air, rather than water. This method prevents the absorption of water thus reducing the amount of moisture in the chicken. Having both systems at the St-François Plant gives the Applicant increased flexibility to satisfy its customers' needs.

**23** The majority of the Applicant's arrangements with its customers are verbal agreements that are entered into by way of a "handshake deal". The only written contract between the Applicant and any of its customers is a **[CONFIDENTIAL]** contract between the Applicant and **[CONFIDENTIAL]** relating to the sale of chicken by **[CONFIDENTIAL]** to **[CONFIDENTIAL]**. The Applicant also has written agreements with **[CONFIDENTIAL]** and **[CONFIDENTIAL]** with regard to their respective specifications and pricing requirements.

D. **Nature of the Respondents' businesses**

(1) **Westco**

**24** Westco is a group of chicken and turkey producers. Westco's head office is located in St-François de Madawaska. Through its subsidiaries, it currently owns or controls 50.9% of New Brunswick's quota, which represents an annual volume of 19,367,920 kg of live chickens. Westco presently has approximately 200 employees.

**25** Westco (formerly called Fermes Waska) was created in 1984 by the consolidation of a dozen New Brunswick chicken producers who wanted to increase their buying and negotiating power vis-à-vis egg and meal producers, chick breeders, carriers and processors. A further consolidation of production quotas occurred during the 1990s, mainly between 1994 and 1998, resulting in an increase in Westco's quota. The consolidation was encouraged by Maple Lodge in order to bring production quota closer to the St-François Plant.

**26** In the early 1990s, Westco started to pursue a project of vertical integration. Westco's vertical integration started gradually, beginning with the purchase of trucks making it possible to transport chips and meal and continuing with the consolidation of meal purchasing to facilitate negotiations for its fabrication and price. Westco then constructed hatcheries, reproduction farms and transport facilities. During Westco's vertical integration, the size of farms also dramatically increased.

**27** Westco is now involved in almost all phases of the production of live chickens including the organic production of manure, the purchase of wholesale grains, egg production, the manufacture of meal, fecundation, chick production, poultry production and transportation. According to Westco, the only phases in which it is not involved are the processing of live chickens and distribution of processed chicken to the retail market.

(2) **Dynaco**

**28** Dynaco is an agricultural co-operative with over 1,500 members, 655 of which are agricultural producers. It is involved in other fields such as home renovation centers, the sale of petroleum products and transportation.

**29** Dynaco's poultry production represents 1.6% of its total sales figure and Dynaco owns 6.22 % of New Brunswick's chicken production quota.

**30** Dynaco holds 100% of the shares of Les Fermes J.J.C. Bolduc inc. and Les Fermes avicoles Bolduc ("Fermes Bolduc") and also owns 25% of the shares of Cormico Inc. ("Cormico"). Cormico's other shares are owned by La Coop Fédérée ("Coop Fédérée") (25%) and the Cormier family (50%). Its chicken production quota represents 4.98% of New Brunswick's supply. Coop Fédérée is Canada's largest firm in the chicken sector: with revenues of $2.9 billion, this poultry co-operative ranks second amongst all co-operatives. The quota held by Fermes Bolduc is, however, the only New Brunswick production quota over which Dynaco has control with respect to the slaughtering destination.

(3) **Acadia**

**31** Acadia was created in 2006 to acquire poultry and pig production facilities. Acadia's main activity is chicken and turkey production. It operates four chicken production sites in New Brunswick. Its pig production has been abandoned.

**32** Acadia currently owns or controls 16% of New Brunswick's chicken production quota. Since 2006, Acadia has also been producing the quota for Slipp Farms, a New Brunswick chicken producer, under a leasing agreement. Its quota represents 1.01% of New Brunswick's supply or about 3,679 chickens per week. Acadia does not exert any control over where Slipp Farms' production is processed.

E. **Relationship between the Respondents**

**33** Westco owns one of Dynaco's 734 shares. Dynaco is a member of Coop Fédérée. Dynaco is also indirectly related to Olymel S.E.C. ("Olymel"), given that Coop Fédérée owns 60% of Olymel. Olymel is a limited partnership formed under the laws of Quebec. It is a primary and secondary chicken processor and is the Applicant's primary competitor in Quebec and the eastern provinces. Olymel currently owns two chicken processing plants, one in Berthierville and another in St-Damase, Quebec. On average, the aforementioned plants process approximately 1.3 million chickens per week. Olymel also owns 50% of Volaille Giannone inc., which operates a chicken processing plant in St-Cuthbert, Quebec.

**34** The shareholders of Volailles Acadia Inc./Acadia Poultry Inc. are the same as the limited partners of Volailles Acadia S.E.C. Acadia is jointly owned by Coop Fédérée (30%), Dynaco (30%), Purdel Coopérative Agro-

Alimentaire ("Purdel") (15%) and Westco (25%). Purdel is also a member of Coop Fédérée. Acadia is thus also indirectly affiliated with Olymel, as three of its four co-owners are related to Coop Fédérée.

**35** Rémi Faucher, who testified on behalf of both Acadia and Dynaco in these proceedings, has worked for each of these Respondents. Mr. Faucher was president and administrator of Acadia from May 2006 to July 2008 and was also president and general manager of Dynaco from September 1998 to February 2008.

F. **The Applicant's supply of live chickens**

**36** When the St-François Plant was acquired in 1989, the birds in the province were split between northern and southern New Brunswick (50/50). At that time, there was another processing plant in Sussex, New Brunswick, which was processing birds from southern New-Brunswick, while the St-François Plant was processing birds from the province's northern part. In 1989, the St-François Plant was in financial difficulty as a result of problems between the previous owners and producers. Consequently, many producers from northern New Brunswick were shipping their birds to Quebec and Ontario for processing.

**37** In or about June 1990, the Applicant entered into negotiations with New Brunswick producers that were shipping their production out-of-province. The Applicant wanted to bring the New Brunswick birds back to New Brunswick to be processed at the St-François Plant. The Applicant agreed to pay the producers $0.065 over the Ontario price instead of the price set by the New Brunswick chicken marketing board, which was about $0.04 over the Ontario board price. The negotiations thus raised the New Brunswick board price (the "NB Board Price") by $0.025.

**38** The Sussex plant closed in 1992, making the St-François Plant the only chicken processing plant in New Brunswick. In late 1995, as a result of poor markets and the suggestion of the then Deputy Minister of Agriculture, the Applicant introduced a "relocation bonus" whereby it split its transportation costs for transporting birds from southern New Brunswick to northern New Brunswick with producers from the north who bought quota from the south. The agreement was that the Applicant would pay $0.03/kg for three years from the date the producer purchased the quota. Payments under the program started in about 1996 and the last of the quota was purchased in 1998. Accordingly, the program was completed by 2001. As of 1998, the Applicant was processing the totality of the New Brunswick production.

**39** The Applicant began receiving supply from the Respondents in 1990 and was processing the totality of their production at the time the Applicant filed its Notice of Application with the Tribunal on March 17, 2008. The Respondents' production facilities are currently all located within 30 km of the St-François Plant. The Applicant does not have any written contracts with New Brunswick producers, including the Respondents, specifying the number and size of chickens that are to be supplied by those producers to Nadeau. There are also no contractual arrangements between the parties specifying a term for supply.

**40** From 1990 to January 2007, the Applicant always paid its producers the NB Board Price for their chickens, which is $0.065 above the regulated Ontario minimum price. In January 2007, the Applicant developed a market-based incentive plan for producers in New Brunswick (the "Incentive Plan").The Incentive Plan cost the Applicant $**[CONFIDENTIAL]** in 2007, of which $**[CONFIDENTIAL]** went to the Respondents collectively. Westco gained $**[CONFIDENTIAL]** from the Incentive Plan that year.

**41** Prior to May 2007, the Applicant obtained all of its live chickens from New Brunswick producers, with almost 75% being supplied by the Respondents or their quota-holding predecessors. Due to a plant closure in Nova Scotia in May 2007, the Applicant began to obtain supply from Nova Scotia and Prince Edward Island. When the Notice of Application in this case was filed, the St-François Plant was processing on average about 565,800 chickens per week from the following sources:

| | |
|---|---|
| Westco | 186,230 |
| Acadia | 58,670 |
| Dynaco | 26,450 |
| New Brunswick, other | 94,450 |
| Prince Edward Island | 40,000 |
| Nova Scotia | 160,000 |

**42** The Applicant began receiving an additional 25,000 birds per week from Nova Scotia in June 2008 and another 6,250 birds per week in September 2008.

**43** In order to accommodate the surplus of birds coming from Nova Scotia and Prince Edward Island, the Applicant started a second shift, which required it to hire approximately 130 new employees. In order to offset the additional costs incurred by running a second shift, the Applicant needed some assurance that it would receive the Nova Scotia birds for a reasonable time period. The Applicant therefore made a "handshake deal" with certain Nova Scotia producers under which they would send Nadeau their chickens for a period of three years. This "handshake deal" was entered into in May 2007.

## G. **The termination of the supply relationship**

### (1) **Westco**

**44** In January 2007, Westco advised the Applicant of its interest in buying or investing in the St-François Plant. Westco submits that the only way to ensure its future in the poultry industry is to proceed with a complete vertical integration of its operations, which requires Westco to acquire an existing slaughterhouse or to build a new one. During a meeting which was held in Atlanta on January 25, 2007, Anthony Tavares, the president and CEO of Maple Lodge at the time, informed Westco that Maple Lodge's shareholders would likely not be interested in selling the St-François Plant. Mr. Tavares further stated that a structure that would result in Westco owning a percentage of the St-François Plant and retaining 100% of its live production assets would result in non-aligned shareholder interests and would likely eventually lead to conflicts.

**45** Shortly after the meeting in Atlanta, Mr. Tavares met with the Board of Directors of Maple Lodge, which decided that it was not interested in selling to Westco. The Board, however, indicated that it would be prepared to look at an ownership structure in which Nadeau and Westco assets would be pooled and Westco and Maple Lodge would each own a part of the combined operations. This proposal was communicated to Westco, but there was no agreement.

**46** Westco approached Olymel in March 2007 in order to develop a partnership so as to complete its strategy of vertical integration. As mentioned above, Olymel is a chicken processor in Quebec and competes with the Applicant in Quebec and the eastern provinces. The purpose of the partnership was to acquire the assets or shares of the Applicant or to acquire property and construct, start up, own and operate a new chicken processing plant. Westco and Olymel thus worked out a business plan envisaging the acquisition of the St-François Plant or, in the event that negotiations failed with the Applicant, the construction of a new processing plant in New Brunswick. The partnership between Olymel and Westco is the Sunnymel Limited Partnership ("Sunnymel") which was created pursuant to the New Brunswick *Limited Partnership Act*, *S.N.B. 1984, c. L-9.1*.

**47** Thomas Soucy, Chief Executive Officer of Westco, contacted Mr. Tavares in mid-August 2007 and said that he wanted Mr. Tavares to meet with him and Réjean Nadeau, President and Chief Executive Officer of Olymel. At the meeting, Mr. Tavares was advised that Westco and Olymel wanted to buy the St-François Plant. He was told that if the Applicant was not willing to sell the St-François Plant, all of the chickens produced by Westco would be diverted to Quebec and Sunnymel would then build its own plant in New Brunswick.

**48** Mr. Tavares met with Westco representatives again on September 6, 2007. During the meeting, Mr. Tavares told Westco's representatives that he was shocked by their decision to partner with Olymel and also stated that he was of the opinion that it was a poor business decision. Westco's representatives did not reconsider.

**49** Following the September 6, 2007, meeting, Mr. Tavares advised Mr. Soucy that although its first choice was to maintain the status quo, Maple Lodge's Board of Directors had, given the circumstances, instructed him to assemble a negotiating team.

**50** On November 6, 2007, the parties started negotiations for the sale of the St-François Plant. The purchase price offered by Sunnymel was less than 25% of the value attributed to the St-François Plant by the Applicant. The negotiations therefore broke down and, on January 17, 2008, Westco gave written notice that it would cease supplying its live chickens to the Applicant, effective July 20, 2008, and that its chickens would be diverted to Olymel in Quebec pending Sunnymel's construction of a new slaughterhouse in New Brunswick.

**51** During the negotiations, the Applicant filed complaints with the New Brunswick Minister of Agriculture and Aquaculture and with Chicken Farmers of New Brunswick (sometimes "CFNB").

(2) **Dynaco**

**52** The Applicant submits that during the negotiations for the acquisition of the St-François Plant, Mr. Soucy affirmed that he had the authority to speak on behalf of Dynaco and that that is why Dynaco was referenced in the Applicant's correspondence with the Minister of Agriculture and Aquaculture. Dynaco states that Mr. Soucy never had the authority to speak on its behalf. Notwithstanding an apology by the Applicant for the mistaken reference to Dynaco in the letter to the Minister, Dynaco confirmed by two letters dated March 6, 2008, that its chickens would cease arriving at Nadeau, effective September 15, 2008.

(3) **Acadia**

**53** By letter dated February 28, 2008, Acadia gave the Applicant formal notice that it would cease supplying it with live chickens, effective September 15, 2008. Acadia submits that this was a business decision and states that its decision to cease supplying the Applicant was not influenced by the negotiations that took place between the Applicant and Westco regarding the acquisition of the St-François Plant.

## H. **History of the proceeding and relief sought**

**54** This proceeding is brought pursuant to the Tribunal's order of May 12, 2008, which granted the Applicant leave to apply for an order under section 75 of the Act. The Applicant seeks an order requiring the Respondents to continue supplying the Applicant with live chickens on the usual trade terms and in the numbers previously provided by the Respondents.

**55** On June 26, 2008, the Tribunal granted the Applicant's request for interim relief pursuant to section 104.1 of the Act (the "Interim Supply Order"). The Respondents were ordered to continue to supply the Applicant with live chickens on usual trade terms at the level of weekly supply that was in place at that time, namely 271,350 live chickens, pending the hearing of the main application.

**56** On November 4, 2008, the Applicant filed a motion for an order requiring the Respondents to show cause why they should not be held in contempt of the Interim Supply Order ("Show Cause Motion"). The Applicant alleged that the Respondents breached and are continuing to breach the Interim Supply Order, as the Applicant has been and will continue to be significantly short on deliveries of chicken.

**57** On November 6, 2008, Westco filed a motion for an order or direction regarding the interpretation of the Interim

Supply Order. Westco seeks an order to confirm its view that the weekly number of chickens ordered to be delivered to the Applicant is a notional figure based on a hypothetical average weight of 2 kg and that the volume of live chickens to be supplied to the Applicant by the Respondents will :

i. be decreased by the volume of replacement chickens obtained by the Applicant;

ii. vary proportionally and in accordance with the periodic fluctuation of the Respondents' production quotas; and

iii. reflect the Respondents' production schedules.

**58** On February 26, 2009, the Tribunal dismissed the Show Cause Motion with respect to Acadia and Dynaco. It granted the motion with respect to Westco and ordered a show cause hearing. The show cause hearing has not yet taken place and the matter is still outstanding before the Tribunal. Westco's motion for an order or direction regarding the interpretation of the Interim Supply Order will be argued at the show cause hearing.

**III. LEGISLATIVE FRAMEWORK**

**59** The refusal to deal provision is contained in section 75 of the Act. It reads as follows:

> **75.** (1) Where, on application by the Commissioner or a person granted leave under section 103.1, the Tribunal finds that
>
> (*a*) a person is substantially affected in his business or is precluded from carrying on business due to his inability to obtain adequate supplies of a product anywhere in a market on usual trade terms,
>
> (*b*) the person referred to in paragraph (*a*) is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market,
>
> (*c*) the person referred to in paragraph (*a*) is willing and able to meet the usual trade terms of the supplier or suppliers of the product,
>
> (*d*) the product is in ample supply, and
>
> (*e*) the refusal to deal is having or is likely to have an adverse effect on competition in a market,
>
> the Tribunal may order that one or more suppliers of the product in the market accept the person as a customer within a specified time on usual trade terms unless, within the specified time, in the case of an article, any customs duties on the article are removed, reduced or remitted and the effect of the removal, reduction or remission is to place the person on an equal footing with other persons who are able to obtain adequate supplies of the article in Canada.
>
> (2) For the purposes of this section, an article is not a separate product in a market only because it is differentiated from other articles in its class by a trade-mark, proprietary name or the like, unless the article so differentiated occupies such a dominant position in that market as to substantially affect the ability of a person to carry on business in that class of articles unless that person has access to the article so differentiated.
>
> (3) For the purposes of this section, the expression "trade terms" means terms in respect of payment, units of purchase and reasonable technical and servicing requirements.
>
> (4) In considering an application by a person granted leave under section 103.1, the Tribunal may not draw any inference from the fact that the Commissioner has or has not taken any action in respect of the matter raised by the application.

* * *

**75**. (1) Lorsque, à la demande du commissaire ou d'une personne autorisée en vertu de l'article 103.1, le Tribunal conclut :

*a*) qu'une personne est sensiblement gênée dans son entreprise ou ne peut exploiter une entreprise du fait qu'elle est incapable de se procurer un produit de façon suffisante, où que ce soit sur un marché, aux conditions de commerce normales;

*b*) que la personne mentionnée à l'alinéa *a*) est incapable de se procurer le produit de façon suffisante en raison de l'insuffisance de la concurrence entre les fournisseurs de ce produit sur ce marché;

*c*) que la personne mentionnée à l'alinéa *a*) accepte et est en mesure de respecter les conditions de commerce normales imposées par le ou les fournisseurs de ce produit;

*d*) que le produit est disponible en quantité amplement suffisante;

*e*) que le refus de vendre a ou aura vraisemblablement pour effet de nuire à la concurrence dans un marché,

le Tribunal peut ordonner qu'un ou plusieurs fournisseurs de ce produit sur le marché en question acceptent cette personne comme client dans un délai déterminé aux conditions de commerce normales à moins que, au cours de ce délai, dans le cas d'un article, les droits de douane qui lui sont applicables ne soient supprimés, réduits ou remis de façon à mettre cette personne sur un pied d'égalité avec d'autres personnes qui sont capables de se procurer l'article en quantité suffisante au Canada.

(2) Pour l'application du présent article, n'est pas un produit distinct sur un marché donné l'article qui se distingue des autres articles de sa catégorie en raison uniquement de sa marque de commerce, de son nom de propriétaire ou d'une semblable particularité à moins que la position de cet article sur ce marché ne soit à ce point dominante qu'elle nuise sensiblement à la faculté d'une personne à exploiter une entreprise se rapportant à cette catégorie d'articles si elle n'a pas accès à l'article en question.

(3) Pour l'application du présent article, "conditions de commerce" s'entend des conditions relatives au paiement, aux quantités unitaires d'achat et aux exigences raisonnables d'ordre technique ou d'entretien.

(4) Le Tribunal saisi d'une demande présentée par une personne autorisée en vertu de l'article 103.1 ne peut tirer quelque conclusion que ce soit du fait que le commissaire a accompli un geste ou non à l'égard de l'objet de la demande.

## IV. THE PARTIES' WITNESSES

**60** Before turning to the analysis of the merits of the application before us, it is important to identify all the witnesses who appeared before the Tribunal. A detailed description of their testimony appears in Schedule A to these reasons.

### A. **The Applicant**

#### (1) **Experts**

**61** Dr. Richard Barichello, Dr. Roger Ware and Mr. Grant Robinson filed expert reports and testified as experts on behalf of the Applicant.

**62** Dr. Richard Barichello is an associate professor at the University of British Columbia where he teaches in the areas of agricultural policy, food markets and international agricultural development. The Tribunal found that he was qualified as an expert in the field of agricultural economics with a specialization in regulated markets, especially supply management, quota markets, trade policy and the analysis of government policy. The Respondents did not take issue with Dr. Barichello's qualifications to give an expert opinion on these matters.

**63** Dr. Roger Ware is a professor of economics at Queen's University. With the parties' agreement, the Tribunal

recognized Dr. Roger Ware as an expert in the areas of economics, competition policy and industrial organization, including market definition and the competitive behaviour of firms.

**64** Grant C. Robinson is a chartered accountant who has worked as an outsource chief financial officer for Maple Lodge. The Tribunal found that he was qualified to give evidence as an accountant, including his expert opinion on the area of the chicken processing industry.

(2) **Lay witnesses**

**65** Seventeen other individuals appeared on behalf of the Applicant.

**66** Two members of the Applicant's management team testified. The Applicant called Yves Landry, the Applicant's general manager, and Denise Boucher, its office manager.

**67** Anthony Tavares, the former president of the Applicant and Chief Executive Officer of Maple Lodge, and John Feenstra, the former general manager of the Applicant, also gave evidence.

**68** The Applicant called three members of its procurement team to testify about the Applicant's efforts to procure chickens from Quebec. Those members were Tina Ouellette, Léonard Viel and Réjean Plourde.

**69** Further processors of chickens and other customers of the Applicant also appeared before the Tribunal. They are:

(i) Guy Chevalier, President, Service Alimentaire Desco Inc. ("Desco"). Desco is a further processor and distributor of chicken;

(ii) Terry Ellis, President, Sunchef Farms Inc. ("Sunchef"). Sunchef is a further processor of chicken;

(iii) Lyndsay Gazzard, Senior Purchasing Manager responsible for poultry purchases for the Unified Purchasing Group of Canada ("UPGC"). UPGC operates as the purchasing agent for YUM! Restaurants International Canada Ltd.;

(iv) Corey Goodman, General Manager, UPGC, and Chief Purchasing Officer, Priszm;

(v) Debbie Goodz, President and CEO, Poulets Riverview Inc. ("Riverview"). Riverview is a further processor and distributor of chicken; and

(vi) Jeffrey Lloyd McHaffie, the *de facto* vice-president of Puddy Bros. Limited ("Puddy"), in charge of sales and the purchase of poultry products. Puddy is a further processor of chicken.

**70** Kevin Thompson, Executive Director, Association of Ontario Chicken Processors, and Bruce McCullagh, Senior Vice President and General Manager, Poultry Operations, Maple Leaf Consumer Foods ("Maple Leaf"), also testified on behalf of the Applicant. Maple Leaf is a large poultry processing company located in Ontario.

**71** Finally, Andre Merks, a Nova Scotia chicken farmer, and Michael Donahue, Vice-President, Agri Stats, Inc. ("Agri Stats"), were called by the Applicant. Agri Stats is a statistical research and analysis firm that offers benchmarking services for the poultry industry across North America.

B. **The Respondents**

(1) **Expert**

**72** Margaret Sanderson was called as an expert by the Respondent Westco. Ms. Sanderson has held a number of positions with the Competition Bureau including the position of Assistant Deputy Director of Investigation and Research for the Bureau's Economics and International Affairs Branch. The Tribunal accepted Ms. Sanderson as

an expert in the area of economics, competition policy and industrial organization, including market definition and the competitive behaviour of firms. The Applicant consented to Ms. Sanderson's expertise.

**73** Ms. Sanderson was the only expert to testify on behalf of the Respondent Westco. Dynaco and Acadia did not call any experts.

(2) **Lay witnesses**

(a) Westco

**74** Five lay witnesses appeared on behalf of Westco. Westco called two individuals who testified about its operations. They were Thomas Soucy, Westco's Chief Executive Officer and President, and Bertin Cyr, a member of Westco's Board of Directors.

**75** Westco also called two Olymel employees. The vice-president of Olymel's chicken procurement division, Yvan Brodeur, and another Olymel employee, Julie Desroches, gave evidence.

**76** Richard Wittenberg was the last lay witness to testify for Westco. He is a Nova Scotia chicken farmer.

(b) Dynaco

**77** Gilles Lapointe and Rémi Faucher testified on behalf of Dynaco. Gilles Lapointe is Dynaco's chief financial officer and Rémi Faucher is Dynaco's former chief executive officer.

(c) Acadia

**78** As stated above, Rémi Faucher also testified for Acadia as he acted as Acadia's president from 2006 until 2008. He was the only witness called by Acadia.

**79** Before turning to the elements of section 75 and the issues to be determined, we dispose of an outstanding matter: the ruling with respect to objections made by Westco to certain paragraphs found in certain witness statements.

## V. THE RULING WITH RESPECT TO WESTCO'S OBJECTIONS TO WITNESS STATEMENTS

**80** Prior to the hearing of the Application, the parties filed witness statements setting out the lay witnesses' evidence in chief in full pursuant to the *Competition Tribunal Rules*, *SOR/2008-141* (Rules 68-70). The parties were provided with an opportunity to raise objections with respect to the admissibility of the witnesses' statements or parts thereof. Both the Applicant and Westco raised such objections. In its order dated October 31, 2008, the Tribunal dealt with some of the objections raised by the parties but it reserved its ruling on three of Westco's objections until the final reasons. What follows is the ruling on those objections.

**81** Westco argued that certain statements made in the witness statements of Yves Landry (paras. 74-79), Réjean Plourde (paras. 7-9) and Lyndsay Gazzard (paras. 9-12) (the "Contested Statements") consisted of hearsay evidence and were consequently inadmissible. Westco further stated that the individuals mentioned in the Contested Statements were not identified as witnesses scheduled to appear during the hearing.

**82** The Applicant indicated that the Contested Statements did not consist of hearsay as they were not put into evidence for the purpose of proving the truth of their contents. The Applicant argued that the Contested Statements were rather offered as proof that the assertions were made to these witnesses. The Applicant submitted that the assertions were fact evidence that could be given orally by the witnesses during the hearing and stated that there

was no requirement that persons named in a witness statement appear on a party's witness list. The Applicant further argued that the Contested Statements were relevant to the issues in the litigation and had probative value.

**83** With respect to paragraph 77 of the statement of Mr. Landry, the Applicant argued that it did not constitute hearsay evidence as Mr. Landry was providing his own testimony as to the identity of Mr. Morin.

**84** Hearsay is testimony or written evidence of a statement made to a witness by a person who is not called as a witness, the statement being offered to show the truth of the matter stated therein. The main concern underlying the admissibility of hearsay lies in the inability to test the truth of the statement or assertion through cross-examination. Therefore, written or oral statements "are inadmissible, if such statements [...] are tendered either as proof of their truth or as proof of assertions implicit therein." (John Sopinka, Sidney N. Lederman & Alan W. Bryant, *The Law of Evidence in Canada*, 2d ed. (Markham: Butterworths, 1999) at 173).

**85** Upon reviewing the Contested Statements and considering the arguments of the parties, we admit the statements for the purpose of establishing the fact that they were indeed made and not to prove the truth of their contents. To that end, the Contested Statements are not hearsay. We now turn to the elements of section 75.

## VI. THE ELEMENTS OF SECTION 75 AND THE ISSUES TO BE DETERMINED

### A. Onus and standard of proof

**86** The burden of proof rests on the Applicant who must establish each constituent element contained in paragraphs (*a*) through (*e*) of subsection 75(1) of the Act on the balance of probabilities.

### B. Has the Applicant established that it is substantially affected in its business due to its inability to obtain adequate supplies of a product anywhere in a market on usual trade terms pursuant to paragraph 75(1)(*a*) of the Act?

**87** Market definition is the first issue. This question will be assessed from two perspectives: the product market and the geographic market where the Applicant might reasonably be expected to look for supplies of live chickens. We will deal with each in turn.

#### (1) The relevant product market

**88** In its Notice of Application, the Applicant seeks an order "directing the Respondents to accept Nadeau as a customer and to supply live chickens to Nadeau on the usual trade terms, in the numbers previously provided to Nadeau by the Respondents." In its Notice of Application and Reply (the "Pleadings"), the Applicant deals only with numbers of live chickens and does not mention that the chickens must be within a given weight range. However, in its submissions, the Applicant takes the position that the "product" for the purposes of paragraph 75(1)(*a*) is live broiler chickens, in a full range of sizes from a minimum of 1.71 kg to a maximum of 2.4 kg.

**89** The Respondents are of the view that the "product" is clearly live chickens since this is the product described in the Applicant's Pleadings. Further, the Respondents contend that this is the product that meets the test for determining the product market articulated in *B-Filer Inc. et al. v. The Bank of Nova Scotia*, *2006 Comp. Trib. 42*.

**90** In *B-Filer*, the Tribunal adopted the approach to the definition of product market in the context of paragraph 75(1)(*a*) set out in *Canada (Director of Investigation and Research) v. Chrysler Canada Ltd.* *(1989), 27 C.P.R. (3d) 1*, aff'd *(1991), 38 C.P.R. (3d) 25*; *[1991] F.C.J. No. 943* (QL) (F.C.A.), where it is stated that the ultimate test concerns the effect on the business of the person refused supplies. In *B-Filer*, the Tribunal restated the test in the following terms at paragraphs 79 and 80 of its reasons:

> [79] For purposes of clarity, we articulate the "*Chrysler* test" as follows: For the purposes of 75(1)(*a*), products are substitutes, and so are included in the same market, if a person is not substantially affected in his business (or if the person is not precluded from carrying on business) as result of switching to these other products.
>
> [80] In regard to the meaning of "substantially" as used in paragraph 75(1)(*a*), as noted by the Tribunal in *Chrysler* at page 23, "[t]he Tribunal agrees that 'substantial' should be given its ordinary meaning, which means more than something just beyond *de minimis*. While terms such as 'important' are acceptable synonyms, further clarification can only be provided through evaluations of actual situations." In our view, for example, a person would be considered substantially affected in his business or precluded from carrying on business if switching to other products resulted in the person's business moving out of the market in which it currently participates.

**91** It is noteworthy that the Tribunal in *B-Filer* took into consideration whether the addition of paragraph 75(1)(*e*) had changed the context and purpose of section 75. The Tribunal ruled that the market of concern in 75(1)(*e*) need not be the market of concern in paragraphs 75(1)(*a*) and 75(1)(*b*), and therefore the addition of 75(1)(*e*) did not change the ultimate concern of 75(1)(*a*). We are also of that view.

**92** The Tribunal finds that the proper test for determining the product market is the above-stated test articulated in *B-Filer*, which is based on the substitutability of products. The application of that test to the evidence leads us to the conclusion that the relevant product market here is live chickens without regard for weight. Our reasons for this conclusion now follow.

**93** The evidence indicates that a number of the Applicant's customers require chickens that meet certain specifications particularly in respect to size. **[CONFIDENTIAL]**.

**94** Since its reconstruction after the 2002 fire, the St-François Plant has been producing only "broiler chickens". Mr. Feenstra's evidence, on cross-examination at the hearing, is that broiler chickens range in size between 1.7 and 2.4 kg live weight. We note that a "broiler" is defined under Order II of the New Brunswick Chicken Marketing Board as a chicken which is not more than 2.65 kg live weight.

**95** The above evidence is of little assistance in determining whether chickens in the Applicant's stated size range, namely a minimum of 1.71 kg and a maximum of 2.4 kg, can be substituted by smaller or larger chickens without substantially affecting the Applicant's business. The Applicant has not established the impact of losing supply of live chickens within the stated size range on its business. For instance, we do not know if the Applicant had the option of processing and marketing larger or smaller birds in the event that it lost its supply of all chickens in the stated size range. The Applicant's evidence focuses essentially on the loss of live chickens, not live chickens of a given size.

**96** While there is some evidence relating to the Applicant's size requirements, the Applicant's expert, Dr. Ware, made no case for a narrower market. Dr. Ware does not explicitly refer to the size of chickens. In discussing the product market under paragraph 75(1)(*a*), he refers only to the "market for selling live chicken". At paragraph 35 of his report, he acknowledges the difficulty in obtaining birds that meet the size and quality requirements of the Applicant's customers, but no further discussion on the issue is found in his report. Ms. Sanderson, in her expert report, expresses the view that "the relevant product market is not in dispute here, it is live chicken". We find there is insufficient evidence to establish that chickens in a range of sizes from a minimum of 1.71 kg to a maximum of 2.4 kg cannot be substituted by other chickens.

**97** Further, the Applicant's Pleadings do not specify that the live chickens at issue are chickens in a range of sizes from a minimum of 1.71 kg to a maximum of 2.4 kg. As stated above, the Notice of Application deals with a broader product market, live chickens. It would have been open to the Applicant to move to amend its Pleadings, but it did not. In the absence of such an amendment, it is our view that it would be unfair for the Respondents to be required to address the issue of a narrower product market without notice.

**98** The Applicant has therefore failed to establish that the product market is defined more narrowly to include only those birds in the stated size range. In this respect, the Applicant has failed to meet its onus. We therefore find the product market for the purposes of paragraph 75(1)(*a*) of the Act to be "live chickens".

**(2) The relevant geographic market**

(a) Positions of the parties

**99** There is no agreement between the parties as to the definition of the relevant geographic market.

**100** It is the Applicant's position that the relevant market is limited to the Province of New Brunswick. The Applicant argues, in the alternative, that even assuming replacement supply can be obtained from Quebec producers, this supply cannot be obtained on usual trade terms. The Applicant's expert, Dr. Ware, expresses the opinion that, because of high transportation costs and high premiums to attract Quebec farmers already bound by contracts with Quebec processors, it is "neither economic nor efficient" for the Applicant to replace the Respondents' supply with supply from locations farther away in Quebec. In reaching this conclusion, Dr. Ware points to the level of interprovincial trade. He notes that, at present, between 4% and 5% of Quebec-grown chickens are shipped outside the province and that this level will reach 14% if the Respondents' supply is replaced with supply from Quebec. In Dr. Ware's view, it is unlikely that such a level of export would be permitted by the Quebec governmental agencies in the long run.

**101** The Respondents contend that the relevant geographic market includes New Brunswick, Quebec, Nova Scotia and Prince Edward Island, and submit that the Applicant can source live chickens from producers in Quebec without being substantially affected. Ms. Sanderson is of the opinion that Quebec producers can provide a ready alternative to replace the Respondents' supply and, in support of her conclusion, points to the following factors:

(i) The Applicant's current live chicken shipments include shipments from more distant locations, such as Nova Scotia and Prince Edward Island;

(ii) A substantial volume of chickens is produced in regions that are located within a reasonable distance from the St-François Plant such as the Quebec City, Beauce and Central Quebec regions;

(iii) There are no regulatory restraints preventing the Applicant from sourcing chickens in Quebec;

(iv) The Applicant's survey indicates that Quebec producers are willing to supply Nadeau live chickens at a reasonable cost; and

(v) The costs associated with Quebec supply such as shrinkage, transportation and birds that are dead on arrival at the processing plant ("DOAs") are not so high as to make it uneconomic for the Applicant to source chickens from Quebec.

(b) Analysis

**102** There is no dispute that New Brunswick forms part of the geographic market. However, at the outset, we reject the contention that the geographic market in the instant case is confined to New Brunswick. At a minimum, the market would include Prince Edward Island since Nadeau has obtained and expects to continue to obtain supply from that province. Both Mr. Feenstra and Mr. Tavares testified that the Applicant will continue to process these chickens. The undisputed evidence is that Prince Edward Island is a long term supplier.

**103** It is useful to discuss the approach we adopt in order to define the geographic market. The Tribunal acknowledged in *Chrysler* that, because of the language used in paragraph 75(1)(*a*), the market definition analysis under that paragraph would be different from the analysis usually performed under other sections of the Act. The Tribunal held at page 10 as follows:

> Products and markets can only be meaningfully defined in a particular context and for a particular purpose. The approach to defining these terms may be entirely different where, as in the case of a merger, the ultimate test is whether the merger will substantially lessen competition and the definition must be consistent with the attempt to determine whether the merger will result in an increase in prices or in other effects consistent with a lessening of competition. In the case of paragraph 75(l)(*a*), the ultimate test concerns the effect on the business of the person refused supplies.

**104** As stated above, the Tribunal relied, in *B-Filer*, on the above paragraph in *Chrysler* and developed the "*Chrysler* test" to determine the relevant product market under paragraph 75(1)(*a*). While the Tribunal was not required to consider the geographic market definition, it nevertheless noted that the "correct test for defining markets" (our emphasis) for the purposes of paragraph 75(1)(*a*) is the *Chrysler* test which it articulated as follows:

> For the purposes of 75(l)(*a*), products are substitutes, and so are included in the same market, if a person is not substantially affected in his business (or if the person is not precluded from carrying on business) as result of switching to these other products.

**105** In *Chrysler,* the Tribunal did not explicitly allude to the proper test for defining the relevant geographic market. It based its conclusion on the geographic market on functional indicators, in particular, the existence of different price lists from Chrysler, the only supplier for Canada and the United States. The existence of price differences is one of the functional indicators referred to in the Competition Bureau's *Merger Enforcement Guidelines*. Therefore, the test in *Chrysler* for defining the geographic market essentially consisted of the simple application of these functional indicators.

**106** In the instant case, there is evidence of functional indicators which support the contention that parts of Quebec should be included in the geographic market. These indicators are those summarized from the evidence of Ms. Sanderson at paragraph 101 above and which essentially consist of the location of current suppliers; the relative proximity of potential Quebec suppliers to the St-François Plant based on the Applicant's survey; significant volumes of chickens in Quebec being located at a reasonable distance, around 500 km, from the St-François Plant; and the absence of regulatory restraints preventing the Applicant from sourcing chickens in Quebec.

**107** We are of the view that consideration of these functional indicators is the preferred approach to defining the geographic market in the instant case. These indicators will be comprehensively dealt with below. As will be seen, they clearly support including that part of Quebec within 500 km from the St-François Plant as part of the geographic market. We find support for our position in the results obtained in the procurement survey conducted by the Applicant, which indicate that numerous Quebec suppliers within 500 km of the St-François Plant are willing to supply chickens to the Applicant. Indeed this radius was acknowledged in Ms. Sanderson's report; she states that "... chicken from Quebec (at the very least from within 500 km of St. Francois) should comprise part of the relevant geographic market for Nadeau's live chicken volumes."

**108** In the circumstances of this case, the proper approach is to consider the above-mentioned functional indicators discussed in Ms. Sanderson's evidence. We find support for our approach to defining the geographic market in the expert evidence adduced before us.

**109** Neither Ms. Sanderson nor Dr. Ware expressed a formal opinion as to the limits of the relevant geographic market for the purposes of paragraph 75(1)(*a*). Nor did they explicitly set out the test that should be applied to determine the market. While they were silent on the exact parameters of the relevant geographic market, both experts did address the question of whether the Applicant can obtain supplies in Quebec.

**110** Dr. Ware testified that the determination of the relevant geographic market in this case poses some difficulties:

> But the important point here is, especially with respect to the geographic market, is that it really is a construct; that we--it's not actually the case that necessarily a supplier who is just outside that boundary

plays no role in this market at all. Neither is it the case that every supplier that's inside that boundary plays an equal role in competition.

**111** To the extent that geographic market definition is a pre-condition for analysis under paragraph 75(1)(*a*), it is to suggest a definition that includes a geographic area within which an applicant might reasonably be expected to look for supplies following a refusal to deal. This geographic market may include areas from which supplies of live chickens are currently obtained by the Applicant and could, in this case, therefore include New Brunswick, Prince Edward Island and Nova Scotia. Further, the geographic market could also include areas where an applicant might reasonably be expected to seek supplies and may therefore include, pursuant to the evidence adduced, geographic areas that are similarly placed in relation to an applicant's existing sources of supply. This method reflects the approach adopted by the experts who gave their opinions before the Tribunal.

**112** We are of the view that, in this case, the geographic market also includes parts of Quebec. Both Dr. Ware and Ms. Sanderson turned to that province to determine whether obtaining supplies from that province is a reasonable possibility for the Applicant. Mr. Robinson, an expert who testified on behalf of the Applicant, based one of his four scenarios on the assumption that the Applicant can replace the Respondents' supply with Quebec-grown chickens and examined the effect of such replacement supply on the Applicant's business.

**113** We agree that the geographic market includes parts of Quebec where the Applicant might reasonably be expected to look for supplies of live chickens. The evidence adduced shows that many producers in Quebec located within 500 km of the St-François Plant are no farther than the distance between the Applicant's current suppliers and its St-François Plant. For example, the Applicant processes chickens from Prince Edward Island producers, and the distance between these producers and the St-François Plant is approximately 650 km. As explained above, both Mr. Feenstra and Mr. Tavares testified that the Applicant will continue to process these chickens.

**114** Further, as stated above, there are no regulatory impediments to interprovincial shipments. A producer must obtain a license from the CFC pursuant to the *Canadian Chicken Licensing Regulations*, *SOR/2002-22*. After having obtained such a license, the producer can export chickens in accordance with the conditions set out in the *Canadian Chicken Licensing Regulations*.

**115** Dr. Ware, however, expressed the opinion that, if the Applicant were to replace the Respondents' supply with Quebec-grown chickens, an intervention by Quebec governmental agencies would be likely. In his view, the resulting increase in interprovincial trade will have a direct impact on Quebec's VAG ("volume d'approvisionnement garanti"). The Quebec Chicken Marketing Board, under the VAG, fills interprovincial demands of processors located outside the province, before allocating live chicken supply to Quebec processors under the Quebec processor allocation system. Therefore, the greater the volume of supply sold to processors located outside Quebec is, the smaller the volume available to Quebec-based processors will be. In Dr. Ware's view, it is unlikely that a high level of interprovincial trade, around 14%, would be permitted by the Quebec governmental agencies in the long run.

**116** To support his view, Dr. Ware refers to the Applicant's submissions in an application brought before the Chicken Farmers of New Brunswick in which it stated that "... the industries in Ontario and Quebec undertook negotiations because interprovincial trade reaching 5 to 7% of total production was considered a crisis situation." In his examination in chief, he admitted that he was not an expert in this particular field.

**117** After a careful review of the evidence, we conclude that it is insufficient to support Dr. Ware's hypothesis. The evidence establishes that provincial processing associations have expressed concerns about interprovincial trade. Mr. McCullagh testified that the Quebec and Ontario processing associations have approached their respective governments to advise them "that interprovincial trade has the jeopardy of creating an unsustainable premium war". According to Mr. Brodeur, over the last few years, attempts have been made to address these concerns, but, up until now, no solution has been found. Mr. Robinson, the Applicant's expert who was recognized by this Tribunal as having expertise in the chicken processing industry, stated that the increase in interprovincial trade would have a

significant impact on the competitive price to acquire live supply, but he did not confirm the evidence adduced by Dr. Ware according to which Quebec stakeholders would intervene to limit such trade.

**118** We find that there are no regulatory impediments to interprovincial trade and that while processing associations have expressed concerns about interprovincial trade, the evidence is insufficient to conclude, on the balance of probabilities, that an increase in interprovincial trade between Quebec and New Brunswick would induce a drastic intervention by Quebec governmental agencies.

**119** In summary, given the absence of regulatory restrictions and the proximity of many Quebec producers to the Applicant's St-François Plant, we agree that parts of Quebec should be included in the geographic market for the purposes of the analysis performed under paragraph 75(1)(*a*).

**120** Regarding Nova Scotia chickens currently processed by the Applicant at its St-François Plant, apart from the three-year arrangement involving the delivery of 160,000 chickens per week, there is evidence of limited supply being sourced from Nova Scotia. In June and September 2008, the Applicant sourced an additional 31,250 chickens per week from Nova Scotia. While there is a paucity of evidence regarding Nova Scotia supply, we nevertheless conclude that Nova Scotia is part of the geographic market because chickens are currently being sourced from there and because the evidence also indicates that the Applicant is not processing these chickens at a loss.

**121** The geographic market will therefore comprise New Brunswick, Prince Edward Island, parts of Quebec which extend to a radius of 500 km of the St-François Plant and Nova Scotia. The parties did not suggest that any other geographic areas be considered.

**122** We now turn to the analysis under paragraph 75(1)(*a*) and consider the following question.

> **(3) Is the Applicant substantially affected in its business because of its inability to obtain adequate supplies of live chickens anywhere in a market on usual trade terms?**

**123** The analysis under paragraph 75(1)(*a*) sets out a number of components that require definition, in particular the phrases "substantially affected" and "usual trade terms".

(a) The meaning of "substantially affected"

**124** We turn first to the meaning of "substantially affected". The Tribunal dealt with the expression in the *Chrysler* case, and concluded that the ordinary dictionary meaning should be given to the word "substantially", and that it required showing "more than something just beyond *de minimis*". The Tribunal, in that case, went on to state that, "[w]hile terms such as 'important' are acceptable synonyms, further clarification can only be provided through evaluations of actual situations" (*Chrysler*, at p. 23). In *Sears Canada Inc. v. Parfums Christian Dior Canada Inc. and Parfums Givenchy Canada Ltd.*, *2007 Comp. Trib. 6*, the Tribunal also held that the term "substantial" in respect to the expression "substantially affected" carries meanings such as "important" and "significant" (*Sears*, at para. 31).

**125** The parties disagree on the meaning to be given to this phrase. The Applicant submits that terms such as "large, significant, important and substantial" capture the concept of a substantial effect on a business. In support of its argument, the Applicant points to the *Chrysler* case.

**126** The Respondent Westco adopts a different approach. In its submissions, it argues that the Tribunal has never really dealt with or specifically defined "substantially affected" or any of the various components of paragraph 75(1)(*a*) and invites the Tribunal to do so in this case.

**127** The Respondent Westco argues that paragraph 75(1)(*a*) contemplates two circumstances: first, that the

refusal substantially affects the Applicant in "his business" ("son entreprise"), and second, that it precludes "a person" from "carrying on business" ("ne peut exploiter une entreprise"). In the latter case, the Respondent contends that this could only mean that the refusal would effectively preclude a new entrant from entering the market because no reference is made to the Applicant's existing business ("his business"). In the Respondent's view, the rules of statutory interpretation require that the terms "substantially affected" and "precluded from carrying on business" be read together. The Respondent contends that this approach is consistent with the case law, since the term "substantially affected" would be given its usual and ordinary meaning in accordance with the case law (*Chrysler* and *Sears*), but would be qualified by the expression "precluded from carrying on business". Consequently, the required magnitude of the "substantial effect" would be such that it would approach an applicant being unable to continue in business. The Respondent therefore submits that an enterprise that is not affected to the point of it being unable to carry on business does not meet the test of "substantially affected" for the purposes of paragraph 75(1)(*a*).

**128** With respect, and for the reasons that follow, we reject the Respondent's above interpretation of "substantially affected" in paragraph 75(1)(*a*).

**129** The applicable principle of statutory interpretation, also known as "the modern approach to interpretation", was endorsed by the Supreme Court of Canada in *Rizzo & Rizzo Shoes Ltd. (Re)*, *[1998] 1 S.C.R. 27*. At paragraph 21 of that decision, Mr. Justice Iacobucci wrote:

> Although much has been written about the interpretation of legislation (see, e.g., Ruth Sullivan, *Statutory Interpretation* (1997); Ruth Sullivan, *Driedger on the Construction of Statutes* (3rd ed. 1994) (hereinafter "*Construction of Statutes*"); Pierre-André Coté, *The Interpretation of Legislation in Canada* (2nd ed. 1991)); Elmer Driedger in *Construction of Statutes* (2nd ed. 1983) best encapsulates the approach upon which I prefer to rely. He recognizes that statutory interpretation cannot be founded on the wording of the legislation alone. At p. 87 he states:
>
> > Today there is only one principle or approach; namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

**130** In accordance with this approach to statutory interpretation, we will first consider the words of paragraph 75(1)(*a*), and in particular the following words which are at issue: "a person is substantially affected in his business or is precluded from carrying on business". The sole issue here is whether the two circumstances contemplated in the provision should be read together as suggested by the Respondent. In our view, the above-cited words, read in their grammatical and ordinary sense, contemplate two separate circumstances. The phrase "substantially affected in his business" is not qualified by the phrase "or is precluded from carrying on business" (emphasis added). Had Parliament intended this to be so, it would have used the word "and" and not "or" in linking the two phrases. Support for the proposition that Parliament intended two separate scenarios by the provision is found in the 1975 House of Commons committee debates. The Minister responsible for the legislation, in response to questions from committee members, indicated that the purpose of the clause was to protect someone who was in business from being put out of business and to allow the entry of others in the market. We reproduce below the relevant passages from the transcripts of the committee debates.

> **Mr. Clarke** (Vancouver Quadra): What was the intent of the clause then?
>
> **Mr. Ouellet**: Well, under certain conditions to make sure that the refusal to deal could become a reprehensible action.
>
> **Mr. Clarke** (Vancouver Quadra): But was it the purpose of that clause to protect someone who was in business from being put out of business?
>
> **Mr. Ouellet**: Yes. But we would like to allow the entry of others, because if we add too many conditions the refusal to deal will never become a reprehensible activity.

**Mr**. **Clarke** (Vancouver Quadra) Did the Minister say, Mr. Chairman, that they did want to prevent the entry of others or they did not want to prevent the entry of others?

**Mr**. **Ouellet**: To facilitate the entry of others.

**Mr**. **Clarke** (Vancouver Quadra): That is what I thought. But the way I read the recommendations from the Senate Committee they are suggesting the present wording would discriminate against someone who wanted to enter that field and their recommendation was designed, in their description, to facilitate the entry of someone into the field. Their criticism is - and I will see how it is worded here. It says:

> The Committee does not consider that the reviewable practice jurisdiction should be available to someone who has never been in business.

And it recommends the deletion of the words "or is precluded from carrying on business".

**Mr. Ouellet**: The way the proposal made by the Senate has to be understood is that they want to deal with people that are already in the business. We feel it would be too restrictive.

**Mr. Clarke** (Vancouver Quadra): Do you mean that the Senate recommendation is the opposite of what I have been saying?

**Mr. Ouellet**: As suggested by the Senate, it will narrow the protection that we are giving, and we do not want to go that far.

**Mr. Clarke** (Vancouver Quadra): Perhaps the definition hangs on the word "precluded" -- precluded from carrying on business, and the way you are reading that is, "or is prevented from entering business,"? Is that the idea?

**Mr. Ouellet**: Yes.

(Canada, House of Commons, *Minutes of Proceedings and Evidence of the Standing Committee on Finance, Trade and Economic Affairs*, 30th Parl. 1st Sess., No. 46 (May 12 1975) at 46:14 - 46:15).

**131** In this case, the Applicant is already in the business of processing chickens and is not seeking to enter the market. In order to meet the test of "substantially affected" for the purposes of paragraph 75(1)(*a*), the Applicant need not demonstrate that it is affected by the refusal to the point of it being unable to carry on business. Rather, it is required to establish on a balance of probabilities that it is affected in an important or significant way. This interpretation is in accordance with the above-cited principle of statutory interpretation and with the case law of the Tribunal.

**132** Having defined "substantially affected", we now turn to the meaning of "usual trade terms".

(b) The meaning of "usual trade terms"

**133** "Usual trade terms" is relevant to section 75 in three ways. First, under paragraph 75(1)(*a*), it must be established that an applicant is unable to obtain adequate supplies on the usual trade terms; second, an applicant must be willing under paragraph 75(1)(*c*) to meet those trade terms as a condition of supply; and third, any order issued under section 75 must be based on the usual trade terms. We turn now to the paragraph 75(1)(*a*) requirement.

**134** Subsection 75(3) of the Act defines trade terms as follows:

> **75(3)** For the purposes of this section, the expression "trade terms" means terms in respect of payment, units of purchase and reasonable technical and servicing requirements.

* * *

> **75(3)** Pour l'application du présent article, "conditions de commerce" s'entend des conditions relatives au paiement, aux quantités unitaires d'achat et aux exigences raisonnables d'ordre technique ou d'entretien.

**135** Paragraph 75(1)(*a*) speaks of supply of a product on "usual" trade terms. Reference to the dictionary definition of "usual" is helpful. The *Canadian Oxford Dictionary* (2004) defines "usual" as follows: "such as commonly occurs or is observed or done, customary, habitual ...". *Webster's Ninth New Collegiate Dictionary* (1986) provides the following definition: "Normal; commonly or ordinarily used; found in ordinary practice or in the ordinary course of events".

**136** The term "usual" qualifies the statutorily defined expression "trade terms" in paragraph 75(1)(*a*). Applying the ordinary meaning to the term, we are left with trade terms that are ordinarily used or found in ordinary practice in a market. The specific terms which are ordinarily used will, of course, vary and depend on the circumstances in each case. Further, there may be a need to interpret the words and phrases used in the definition of "trade terms" found in subsection 75(3), in particular, for our purposes: "terms in respect of payment".

**137** The parties disagree on the elements to be included in defining "usual trade terms". In reference to the statutory definition in subsection 75(3), the Applicant argues the term "usual trade terms" must have a correlative meaning and therefore refers to the practice that had been in place between the contending parties in terms of price, units, etc. before the refusal to supply. It is the Applicant's contention that the "usual trade terms" in place between each of the Respondents and the Applicant entailed the following elements:

(a) delivery of chickens in a full range of broiler sizes, namely, from 1.71 kg to 2.4 kg;

(b) the CFNB regulated price, which equates to the Ontario base price plus $0.065/kg, plus applicable CFNB size premiums, where applicable;

(c) delivery of chickens grown within 30 km of the St-François Plant, thus resulting in minimal transportation costs, minimal DOAs, and minimal shrink;

(d) payment pursuant to the Marketing Orders of the CFNB, namely net 7 days; and

(e) delivery each and every week of chickens in numbers averaging about:

  (i) from Westco, 186,230 chickens per week;

  (ii) from Acadia, 58,670 chickens per week; and

  (iii) from Dynaco, 26,450 chickens per week,

for a total supply from the Respondents of about 271,350 chickens per week.

**138** The Respondents argue that subsection 75(3) provides a complete definition of "trade terms" and as such can only refer to "terms in respect of payment, units of purchase and reasonable technical and servicing requirements". The Respondents contend that the definition does not include price or volume and that, had Parliament wanted price to be included in "trade terms", it would have said so expressly and not used the phrase "terms in respect of payment" in its definition. Further, the Respondents argue that since paragraph 75(1)(*d*) requires that the product be in ample supply, it was not contemplated that volume be a concern. It is consequently argued that the Tribunal would not have the jurisdiction to grant the Applicant's request and order the Respondents to continue to supply "in the numbers previously provided to Nadeau by the Respondents". It is also argued that since the product market is live chicken, and not chickens of a specified weight, there is no basis here to support size or weight of the chickens as a usual trade term.

**139** We are of the view that "usual trade terms" must be determined in relation to a defined market at a particular time. The applicable time frame in this case is generally at about the time the Respondents gave notice of their refusal to continue to supply. For the purposes of this application, we have also determined above that the product is live chickens and that the geographic market includes parts of the Province of Quebec as well as New Brunswick, Nova Scotia and Prince Edward Island.

**140** What then are the applicable "usual trade terms" that are ordinarily used or found in ordinary practice in the geographic areas? We do not accept the Applicant's submission that the applicable terms are those which reflect the very agreements, in terms of price, units supplied etc., that prevailed between the Respondents and the Applicant prior to the refusal. Parliament did not provide that the Applicant need only establish its inability to obtain supply on the "same" trade terms, for the purposes of paragraph 75(1)(*a*). Had it intended this, it would have expressly provided so, as it did elsewhere in the Act. See section 80 of the Act where reference is made to "same" trade terms.

**141** In our view, the plain reading of the provision leaves no doubt that the trade terms are not those specific to the parties, but rather those that are viewed from the perspective of all processors competing for live chickens in the defined market generally. In such a market, the usual trade terms are identified and customarily come to be expected by suppliers of live chickens.

**142** Price is clearly the most important element influencing trade in chickens. It is a commodity product and is sold largely on the basis of price. In the context of supply management, if price were not important, the marketing board would have felt no need to set a minimum price. It is difficult therefore to divorce trade terms from price. The issue here is whether the expression "terms in respect of payment" is to be interpreted to include price and, in particular, premiums. We respectfully reject the Respondents' position on the question and, for the reasons that follow, find that "terms in respect of payment" must be interpreted to include price in the circumstances.

**143** We acknowledge that the issue has never been dealt with before by the Tribunal. In *Chrysler*, the Tribunal ordered Chrysler Canada to accept the complainant as a customer for the supply of Chrysler parts "on trade terms usual and customary to its relationship with [the complainant] as the said terms existed prior to [the date that the complainant was first refused supply]" (at p. 28). In that case, there was but one supplier and one customer. The Tribunal has not yet identified the "usual" trade terms involving a business with multiple suppliers and customers. If "terms in respect of payment" includes price, it could be argued that the Tribunal's order in *Chrysler* prevented Chrysler Canada from ever raising its price to the complainant. Since the Tribunal recognized the regular fluctuation in Chrysler Canada's prices, this would appear not to have been the Tribunal's intention. If price, however, is not to be included as a usual trade term, there would be nothing to prevent a supplier, even one subject to a section 75 order, from raising its prices to a person to the point that this person can no longer afford to purchase from the supplier. This would render the provision ineffective, particularly in cases where a complainant was the sole purchaser in a market.

**144** While there is no dispute that "terms in respect of payment" includes credit terms and acceptable methods of payments, in the context of paragraph 75(1)(*a*), we are of the view that price is also included. Otherwise, a complainant who is unable to obtain adequate supplies in a market because prices are higher than the usual price would have no possibility of relief under the provision, simply because other usual terms of payment are in place. For example, in the instant case, it would matter little if the credit terms and the methods of payment available in the market for processors were the usual terms prevailing in that market, if the amount to be paid in order to obtain live chickens was increased by suppliers to an amount higher than the usual price paid for live chickens in that same market. In essence, the only term of payment that really matters in the circumstances here is price.

**145** Under supply management, price is essentially the principal trade term. As discussed above, the minimum price is set by the respective provincial marketing boards. Whether this minimum price set by the marketing board translates into a usual trade term will depend on the circumstances. In this case, the ultimate price paid by chicken processors in the market may be higher than the minimum price. This will depend on a number of factors, not the least of which is the premium paid to producers. A premium is an amount over the board price paid by processors to producers. Therefore, the notion of price as a "usual trade term" is best expressed, for our purposes, in terms of a range of prices. This approach recognizes the dynamic reality of a competitive market and would be particularly helpful in the event that the Tribunal were to issue an order to continue supply on "usual trade terms", since it would allow for flexibility by not binding the parties to a fixed price. The range of prices for our purposes would include minimum board prices set by the provincial marketing boards from time to time, plus the applicable premium, which

would likely also vary by reason of competitive market forces.

(c) Applicant's inability to obtain adequate supplies on usual trade terms

**146** Having determined the meaning of "substantially affected" and "usual trade terms", we will now turn to the question of whether the Applicant has established that it is substantially affected in its business because of its inability to obtain adequate supplies anywhere in a market on usual trade terms.

**147** The parties disagree markedly on whether the suppliers are likely to provide adequate replacement supplies on usual trade terms. Quebec is important in the instant case because it is the most likely source of replacement chickens for the Applicant.

**148** The Applicant, at the time it filed its application, processed around 94,450 chickens from southern New Brunswick, 40,000 chickens from Prince Edward Island, and 160,000 chickens from Nova Scotia. On the evidence, there is no dispute that it is unlikely the Applicant can obtain the required additional volumes of chickens to replace the Respondents' chickens from southern New Brunswick or Prince Edward Island. In respect to New Brunswick and Prince Edward Island, the evidence shows that the Applicant currently processes all of the New Brunswick and Prince Edward Island supply.

**149** The 160,000 chickens from Nova Scotia were to be made available for a period of three years, and there is little evidence to indicate whether this volume of chicken would be available in the long term. Since the Interim Supply Order, the Applicant has secured an additional supply of around 31,250 chickens per week from Nova Scotia. However, we do not know the terms, if any, on which the Nova Scotia producers that are continuing to supply ACA Co-Operative Ltd. ("ACA"), the only Nova Scotia processor, would be willing to switch to the Applicant. No survey of Nova Scotia producers was conducted by the Applicant in order to ascertain the availability and terms of supply from Nova Scotia, as was done in Quebec. Nor did the experts address this issue. As a consequence, we are unable to make a finding regarding the terms on which additional supply could be acquired from Nova Scotia.

**150** This leaves Quebec as the only source of additional supply about which we actually know the possible terms of supply. Therefore, producers located in parts of Quebec are the most likely source of replacement supply for the Applicant. In order to determine whether the Applicant can obtain supplies from these producers on the usual trade terms, it is useful to define the relevant usual trade terms that are applicable to live chickens in Quebec.

(i) The relevant usual trade terms

**151** In order to determine whether the Applicant has met its burden in establishing that it is unable to obtain adequate supplies of live chickens anywhere in the market on "usual trade terms", it is necessary to clearly define the usual trade terms in this case. By definition, "trade terms" includes "terms in respect of payment", which we have interpreted to include price. It also includes "units of purchase" and "reasonable technical and servicing requirements". No issues regarding technical and servicing requirements are raised in this case. The only issue in respect to trade terms is the price of the replacement chicken.

**152** In order to assess whether the Applicant is able to obtain adequate supplies "on usual trade terms", the usual price for live chickens in the market must be determined. As stated above, in the circumstances, that price will consist of a range of prices. In order to determine the usual range of prices, we turn to the evidence adduced and in particular the evidence regarding premiums.

**153** Determining the range of prices for live chickens in those relevant parts of Quebec will indicate the "usual trade terms" for those chickens. The price usually paid by the Applicant is not necessarily the applicable "usual trade term". It is rather the usual price for live chickens paid by processors in the market. For our purposes, these processors are mostly Quebec-based processors and, as indicated in our earlier analysis on the geographic market, these processors would be competing in the area where the Applicant is likely to find its replacement

chickens. They are paying the Quebec board price set by the Quebec marketing board, Les Éleveurs de volailles du Québec, which is $0.065 below the NB Board Price, plus a premium. Significant evidence was adduced regarding premiums. Premiums currently being paid by Quebec processors will afford the best evidence of the usual prices being paid by processors in the market and are the best indicator of usual trade terms.

**154** The evidence on premiums stems principally from efforts made by the Applicant's procurement team following the Tribunal's Interim Supply Order dated June 26, 2008. The Applicant's management team instructed the procurement team to begin making efforts to inquire about the availability of chickens from Quebec producers. Initially, calls were made to a list prepared by the Fédération des producteurs de volailles du Québec in the year 2000 containing the names of 700 Quebec producers. In total, attempts were made to contact 454 producers. Many could not be contacted by reason of incorrect phone numbers, phone line disconnection and number changes. This comes as no surprise, given that the list of names and contact information was over eight years old. Many producers did not respond to the initial telephone message, and of those that did, only 67 requested a meeting with a procurement agent of the Applicant. Call logs were kept and turned over to the Applicant's procurement agents for follow-up. These call logs were eventually filed in evidence.

**155** The Respondents contend that the Applicant's procurement effort or survey of Quebec producers was essentially undertaken as a result of the Tribunal's Interim Supply Order and was not a serious effort to obtain replacement chickens in Quebec. In its Interim Supply Order, the Tribunal found that there was a duty to mitigate damages. At paragraph 37 of its reasons it wrote:

> I reject the Applicant's contention that it had no duty to mitigate. It could not sit idly by and make no attempt to secure additional live chickens when faced with the loss of about half of its supply. However, what is adequate mitigation will turn on the circumstances of each case.

**156** The Respondents point to a number of deficiencies in the Applicant's procurement effort. They argue that the Applicant's procurement team did not have a mandate to close a deal or sign contracts for supply with any of the Quebec producers called. They point to Mr. Feenstra's testimony, where he attests that the procurement team was "[t]o gauge what the opportunities are to procure chickens in Quebec". He also asserted on examination for discovery that he was not hopeful of the outcome of the procurement survey and that he would not initiate negotiations with Quebec producers who were not willing to sell their supply of live chickens at a price that is equal to or lower than the NB Board Price. They point to the testimony of Ms. Ouellette, where she attests that Mr. Landry had ordered her to end her calls to Quebec producers even though 196 producers had yet to be contacted by the Applicant's procurement team.

**157** There is evidence, essentially uncontested, to support a finding that the Applicant's procurement effort was not designed with the objective of securing sufficient live chickens from Quebec to replace all the chickens lost as a result of the Respondents' refusal to supply. However, whether or not the Applicant's efforts were genuinely motivated by a desire to obtain replacement chickens from Quebec is essentially not material to the question of whether replacement chickens are actually available on usual trade terms from Quebec. While the procurement effort is not a perfect gauge of the opportunities available in Quebec, it does provide evidence to assist in answering the question. The call logs reflect information obtained as a result of the procurement efforts. While this information has been interpreted differently by the experts, it is essentially unchallenged. Further, the members of the procurement team consisting of Ms. Ouellette, Mr. Plourde and Mr. Viel gave testimony regarding the procurement efforts. In our view, they did so in a forthright manner, and we find their testimony to be credible.

**158** Ms. Ouellette was tasked with placing the initial call to producers in Quebec for the purpose of inquiring as to whether they were interested in meeting with the Applicant to discuss the possibility of supplying chickens. In determining which producer to call, Ms. Ouellette attests that she considered the geographic location of each producer *vis-à-vis* the location of the St-François Plant. She stated that the majority of the calls were placed to producers that were located east of Montreal. Ms. Ouellette kept call logs for each call placed. Of the producers with whom she spoke, 67 requested a meeting with a "Nadeau procurement agent". She then gave the call logs

containing the contact information of each interested producer to either Mr. Plourde or Mr. Viel, who were responsible for the follow-up.

**159** Mr. Plourde eventually met with 39 producers between July 14 and September 19, 2008. During these meetings, he made detailed notes which were annexed to the call logs. Mr. Plourde attests that the Quebec producers he met demanded the following pricing arrangements before they would agree to moving their production to the Applicant, namely **[CONFIDENTIAL]**; and payment of premiums in addition to the Quebec board price, ranging from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]**/kg.

**160** Mr. Viel, who is the Applicant's manager of sales and transportation, assisted the procurement team when Mr. Plourde was on vacation. He met with 11 Quebec producers in the week of July 21, 2008, and also made detailed notes during these meetings, which notes he attached to the call logs provided by Ms. Ouellette. Mr. Viel attests that the producers he met with indicated they would consider moving their production to the Applicant on pricing arrangements which would include **[CONFIDENTIAL]** and premiums ranging from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]**/kg. Mr. Viel further stated that each producer would be able to supply between **[CONFIDENTIAL]** and **[CONFIDENTIAL]** heads per eight-week quota period.

**161** As indicated above, in order to determine the usual trade terms for live chicken in Quebec, it is helpful to examine evidence of the "usual" premium paid by processors in that geographic area. The survey of the Applicant's procurement team tabulated data of premiums actually paid by Quebec processors to producers in that province. This evidence was considered by the experts. Ms. Sanderson attested that among all of the producers who offered the Applicant supply at a requested premium of $**[CONFIDENTIAL]**/kg, the highest premium that the producer receives from its current Quebec customer is $**[CONFIDENTIAL]** above the Quebec board price. Based on the procurement surveys conducted by the Applicant, Ms. Sanderson aggregated the premiums that are currently received from Quebec processors and divided these by the total number of kilograms offered. She found that the weighted average premium that is currently received by the surveyed producers from processors is $**[CONFIDENTIAL]**/kg above the Quebec board price. The evidence indicates that the survey conducted by the Applicant's procurement team covered less than **[CONFIDENTIAL]**% of the Quebec quota owned by producers located within 500 km of the Applicant's plant in St-François. The producers surveyed that did not specify a premium and those that indicated that they would not supply the Applicant represented **[CONFIDENTIAL]**% of the total quota within 500 km of the St-François Plant.

**162** While it is difficult to determine from the above evidence what premium would be sought by those producers that were not surveyed, the evidence provides a good indication of the premiums currently being paid by Quebec processors to producers in the relevant area of Quebec. Further, the evidence adduced in respect to the "Projet Westco" (the "Projet Westco Report"), a 2007 report prepared by Olymel regarding a possible partnership with Westco, indicates that the premiums paid by Olymel for its Quebec live supply in 2006 is $**[CONFIDENTIAL]**/kg above the Quebec board price. Mr. Brodeur's witness statement confirms that Olymel's current premium is in the order of $**[CONFIDENTIAL]**/kg above the Quebec board price.

**163** The above evidence in respect to premiums paid by Quebec processors is not speculative, nor is it contested. It represents direct evidence of premiums that are actually being paid by processors in the relevant areas of Quebec. While the survey does not tabulate the premiums paid by all processors in Quebec, the data is sufficiently complete to allow us to determine a range of premiums that are usually paid by processors in that part of the Quebec market covered by the Applicant's procurement survey, which includes that area within 500 km of the St-François Plant. We find that premiums range from $**[CONFIDENTIAL]** and $**[CONFIDENTIAL]** over the Quebec board price. It follows that usual trade terms for Quebec chickens, in this instance, would include prices within that stated range of premiums above the Quebec board price.

**164** We note that Quebec prices including the premiums are very close to the NB Board Price. As mentioned above, both the Quebec board price and Ontario board price are $0.065 below the NB Board Price. The Serecon Report, a consultant's report on the assessment of the broiler chicken industry in Nova Scotia published in July 2008, indicates that "there is no real historical pattern of a consistent spread in price between Nova Scotia and

Ontario" and that "[f]or the past few periods (about the past year), the spread has been somewhat consistently 6.5 cents". We also know that the Applicant pays Nova Scotia producers the NB Board Price. Mr. Wittenberg testified that the Nova Scotia board price was "somewhat higher" than the NB Board Price, but he did not know the exact board price. Mr. Merks testified that "historically", the Nova Scotia board price was $0.02 below the NB Board Price. We are satisfied on the evidence that the Nova Scotia and New Brunswick board prices are very close.

(ii) Are supplies available on usual trade terms?

**165** We now turn to considering whether the Applicant is able to obtain supplies of chickens in Quebec on usual trade terms or within the stated price range. Both Mr. Robinson and Ms. Sanderson considered the data obtained from the Applicant's procurement survey.

**166** In his expert report on behalf of the Applicant, Mr. Robinson made certain assumptions in respect to the replacement of the Respondents' birds with birds from Quebec. He assumed this chicken could be obtained in Quebec, but that premiums would have to be paid to entice them away from their current processor; that the Applicant would be responsible for DOAs, transportation cost and shrink; and that the appropriate chickens can be found for the sizes necessary for the customers. Mr. Robinson assumed, based on conversations the Applicant's management team had with Quebec producers, that a minimum premium of $**[CONFIDENTIAL]**/kg over the Quebec board price would have to be paid.

**167** Ms. Sanderson stated that because of the assumptions adopted in both the Ware and Robinson reports, these reports overstate the potential impact that the loss of the Respondents' supply of live chickens would have on the Applicant. She stated that the assumed premium is far above the premiums currently and historically paid in Quebec. She first estimated the premium needed to obtain chickens from Quebec producers to be in the area of $**[CONFIDENTIAL]**/kg. After corrections were made in the affidavits of Ms. Boucher, Mr. Viel and Mr. Plourde, and based on additional testimony, Ms. Sanderson revisited her opinion on the premiums that the Applicant would have to pay above the Quebec board price in order to obtain chickens from Quebec. Her revised opinion was that that premium would be in the area of $**[CONFIDENTIAL]**/kg. She explained that in coming to this opinion, she assumed that the producers in Quebec that the procurement team did not meet or contact would respond in the manner as those that were contacted. In other words, the premiums requested by the producers that did respond were extrapolated and applied for the purpose of her analysis to all producers from Quebec in the market.

**168** The parties therefore take different approaches in reviewing the data obtained from the Applicant's procurement survey. On premiums, each of the two experts disputes the appropriateness of the different assumptions made by the other. In the end, we note that neither expert takes issue with the accuracy of the data collected. It is not disputed that, at a minimum, a premium of at least $**[CONFIDENTIAL]**/kg would have to be paid, which is higher than the premiums we have determined to be within the usual trade terms (i.e. $**[CONFIDENTIAL]**/kg -$**[CONFIDENTIAL]**/kg).

**169** The Applicant contends that two other factors bear on the question of whether the Applicant can obtain chickens in Quebec on usual trade terms. First, the concerns expressed by a number of witnesses regarding interprovincial trade and premium wars; second the specific characteristics of co-op producers and their significance in the market place. It is useful to review the evidence adduced in respect to these factors.

(iii) Premium wars

**170** There is significant evidence adduced, essentially on behalf of the Applicant, regarding concerns in respect to growing interprovincial trade in live chickens. Mr. McCullagh, the vice-president of Maple Leaf, expresses the view that increased interprovincial trade is "a jeopardy to processing companies". He says that the supply management system affords protection to Canadian chicken producers and allows for sustainable farm earnings. He attests that the system further insulates chicken farmers from competition by reason of the national quotas which are allocated to provinces based upon a market share system and governed by an interprovincial agreement.

**171** Mr. McCullagh expresses the view that any attempts by the Applicant to source chickens from Quebec would be very expensive and that such a strategy is highly unlikely to succeed. If, however, the strategy were successful, he attests that Quebec processors who lose supply to the Applicant would seek to regain chickens by offering premiums to producers in other provinces, such as Ontario. According to Mr. McCullagh, the outcome would be that downstream processors, retailers, food service operators and consumers would incur greater costs, and chicken producers would receive an unfair financial benefit by leveraging power allotted to them through the quasi-monopoly afforded to them through supply management regulations.

**172** At the hearing, Mr. McCullagh testified that Maple Leaf was extremely concerned with the developments in interprovincial trade because of the tremendous risk that premiums will be driven to unsustainable levels for the industry. **[CONFIDENTIAL]**. He also expressed the view that this premium war had the potential, by reason of the limited supply of chickens owing to quotas, to escalate to encompass the entire industry.

**173** The executive director of the Association of Ontario Chicken Processors, Mr. Thompson, expressed similar views in regard to premium wars. He explained that under supply management, no province is able to increase its share of national chicken production beyond its historical market share. Processors that lose supply to an interprovincial competitor have little choice but to retaliate by providing increased premium incentives to induce local producers to return to processors within their own province, if they wish to stay in business.

**174** Mr. Thompson expresses the view that the interprovincial movement of chicken is a weakness in the regulated supply system. He attests that the provincial percentage share of national production is effectively fixed. He argues that because of this, the only avenue outside of consolidation where processors may seek additional supply is by "raiding" the producers selling to their competitor in neighbouring provinces.

**175** This aspect of interprovincial trade in chicken is also acknowledged by Mr. Brodeur, who testified on behalf of the Respondent Westco. In his testimony, he attests that the pressure from Ontario processors attempting to source chickens from Quebec is now very strong and growing. He recognized that this could have an upward effect on premiums. He also testified that it was essentially smaller processors that were involved in Quebec-Ontario interprovincial trade of chickens and that the "big players" were essentially not involved. He considered Olymel, Exceldor, Maple Leaf and Maple Lodge to be the big players. He testified that Maple Lodge and Exceldor did trade but only for smaller volumes.

**176** Both Mr. Tavares and Mr. Feenstra testified to the effect that increased interprovincial trade in chickens would spark a price war that would increase costs for any processor and would further erode profits. They expressed the general reluctance of major processors to become involved in interprovincial trade of chickens for this reason. Mr. Feenstra stated that he had been involved in premium wars in the past and that the net effect of a premium war is a huge hit on the processing sector because if they want supply, processors have no choice but to pay the premiums demanded by the producers.

**177** Professor Barichello stated in his report that relatively little interprovincial trade in chickens takes place in Canada. The bulk of this movement is between Ontario and Quebec. He reported that in 2005, interprovincial trade in chickens involved only 4% of total Canadian production. He is of the opinion that because the quantity of output is fixed under supply management, producers can only increase their margin by demanding a higher price from the processor, or by making their operations more efficient, or both.

**178** Dr. Ware, in examination in chief, explained that even if the Applicant were able to source all of the Respondents' chickens from Quebec, this would represent an increase in demand for supply of chicken from Quebec by about 10%. He says that in a supply management system where the total amount of chicken produced in Quebec is regulated and cannot be expanded, this could only occur by bidding supply away from other chicken processors. This would cause price increases in the form of escalating premiums.

**179** While there are no regulatory restrictions on interprovincial trade in chickens, **[CONFIDENTIAL].** We know that

under supply management, supply is limited. In these circumstances, it is understandable that to attract supply away from other processors, a higher price would have to be offered.

**180** We are prepared to accept that the evidence supports the contention that circumstances surrounding interprovincial trade in live chickens and premiums could lead to upward pressure on the price of live chickens in the market. In our view, however, this is no more than the result of competition between processors in a market where the aggregate supply of live chickens remains unchanged. The underlying theme of the evidence of processors and their representatives cited above is that processors should not have to compete for live chickens because such competition would result in higher prices and a "premium war" amongst processors. This evidence is self-serving. It should come as no surprise that in a market where supply is limited, competition for that supply usually results in higher prices. In the instant case, the issue is not about "premium wars", but rather the supply of live chickens. The issue of the supply of live chickens will be comprehensively dealt with below when we consider the "ample supply" requirement under paragraph 75(1)(*d*) of the Act.

(iv) Co-op producers and their significance in the market place

**181** The evidence indicates that the Exceldor co-op is an important processor with approximately 47% of the Quebec slaughter. This is similar to Olymel's share. The Exceldor co-op is made up of and owned by 260 member suppliers or producers. The Exceldor producers receive a dividend based on the Co-op's performance at the year's end. In his report, Mr. Robinson expresses the view that Exceldor's status as a co-op represents yet another barrier to the Applicant in its effort to source chickens from Quebec. He refers to the philosophy of co-op members that would favour having their product processed in a plant they own so that they may benefit from year-end dividends. Apart from making up these dividends, the Applicant would have to overcome this different philosophy of co-op members who favour the co-op business model over the Applicant's for-profit model. Mr. Robinson expresses the view that it may not be possible to entice any significant number of producers or chickens from Exceldor members no matter what price is paid by the Applicant. Given the significance of Exceldor's share of Quebec slaughter, this represents another significant hurdle for the Applicant.

(v) Conclusion regarding the Applicant's ability to obtain chickens in Quebec on usual trade terms

**182** The evidence reviewed above indicates that even if the Applicant were able to access the necessary volume of chickens to replace the Respondents' from Quebec producers, it would only be able to do so at premiums that exceed those considered within the range of usual trade terms. Ms. Sanderson conceded that the Applicant would have to pay a premium of $**[CONFIDENTIAL]** above the Quebec board price to obtain replacement supplies, whereas we have found the usual trade terms in that market regarding premiums to be between $**[CONFIDENTIAL]** and $**[CONFIDENTIAL]** above the Quebec board price. In all of the circumstances, we find that the Applicant is unable to obtain adequate supplies of live chickens anywhere in the market on usual trade terms.

(d) Is the Applicant substantially affected in its business?

**183** We now turn to the question of whether the Applicant is substantially affected in its business due to its inability to find adequate supplies of live chickens anywhere in the market on usual trade terms. We will first review the evidence adduced by the parties, in particular the expert reports.

(i) The Applicant's evidence

**184** The reports of Mr. Robinson and Dr. Ware deal directly with the elements of paragraph 75(1)(*a*). We turn first to the evidence of Dr. Ware.

**185** Dr. Ware notes that the Respondents supply almost one half of the chickens processed by the Applicant and that if this supply were redirected to rival processing facilities, the Applicant would lose over half its revenue. Dr.

Ware indicates that "[t]here is no economically feasible source of supply whereby Nadeau can make up this shortfall in supplies of live chicken". He further states that replacing such a volume would take at least months if not years and that the only economically comparable replacement would have to come from New Brunswick. With respect to the market for selling live chickens, Dr. Ware is of the opinion that the Applicant would not be able to bid supply away from producers outside New Brunswick because those producers are already contractually committed to other processors; that not all producers raise chickens that meet the Applicant's size and quality requirements; and that very high premiums would have to be paid to producers in Quebec to attract them away from current processors. Dr. Ware relies on the affidavit evidence of Mr. Tavares in support of these claims. He also indicates that because of high transportation costs "it is neither economic nor efficient for [the Applicant] to replace the large amount of supply from the respondents with supply from greater distances."

**186** With respect to the market for purchasing live chickens, Dr. Ware's observations are not based on any independent analysis. He does not seek to quantify the costs the Applicant would incur to replace the Respondents' live chicken supply.

**187** Mr. Robinson gave evidence with respect to projected earnings of the Applicant. He was asked to review the Applicant's operations to assess the impact of the withdrawal of the Respondents' birds, namely 271,350 birds per week. Mr. Robinson approached his task by developing the following four different scenarios involving:

1. the loss of the Respondents' chickens;
2. replacement of the Respondents' birds with birds from Quebec;
3. the loss of the Respondents' birds and Nova Scotia birds; and
4. replacement of the Respondents' birds with birds from Quebec and loss of Nova Scotia birds.

**188** In developing the four models, Mr. Robinson used the 12-month period ending June 30, 2008, as the base period for his analysis (the "Base Period"). This period included supply from the Respondents as well as Nova Scotia and Prince Edward Island. Mr. Robinson reasoned that this period represented an appropriate base since it not only represented the current operations of the Applicant but was also representative of the performance the Applicant could achieve "on a long term basis" through good and poor periods. In his testimony, Mr. Robinson refers to very strong prices in the poultry market for the first six months of the Base Period ending December 31, 2007, and a very weak market for the remainder of the period.

**189** Mr. Robinson made certain assumptions in respect to the replacement of the Respondents' birds with birds from Quebec. He assumed that these chickens could be obtained in Quebec, but that premiums would have to be paid to entice them away from their current processor; that the Applicant would be responsible for DOAs, transportation costs and shrink; and that the appropriate chicken could be contracted for the sizes necessary for the customers. As stated above, Mr. Robinson assumed, based on conversations the Applicant's management team had with Quebec producers, that a minimum premium of $**[CONFIDENTIAL]**/kg would have to be paid on the Quebec board price. He also assumed that, as a result of having to haul the birds up to six hours, the Applicant would have to compensate producers for higher DOAs, higher transportation costs and higher shrink. This would amount to an additional $**[CONFIDENTIAL]**/kg on top of the live price premium.

**190** Mr. Robinson concluded that in all four scenarios, the Applicant's operations are negatively impacted to a significant degree.

(ii) The Respondents' evidence

**191** Ms. Sanderson acknowledges that certain costs are higher when sourcing live chicken from Quebec rather than from New Brunswick, such as transportation costs, shrink and mortality. She notes that the regulated minimum board price paid to Quebec producers is $0.065/kg lower than that paid to New Brunswick producers. Ms. Sanderson factors in the additional costs to the Applicant to purchase replacement chickens for volumes lost

because of increased mortality and shrink for more distant shipments. She is of the opinion that the Applicant would be able to replace all of the Respondents' chickens with chickens from Quebec at an additional cost of approximately $**[CONFIDENTIAL]**. This would cover additional costs associated with premiums, shrink, DOAs and transportation. In Ms. Sanderson's view, this would still leave the Applicant with operational earnings of approximately $**[CONFIDENTIAL]**, which is more than **[CONFIDENTIAL]**% over the Applicant's average earnings from operations between 1998 and 2007.

**192** Ms. Sanderson expresses the opinion that, because of the assumptions essentially about the size of the premiums in the Robinson and Ware reports, their estimate of the potential impact on the Applicant from the Respondents' shifting their supply of live chickens from the Applicant to Sunnymel is overstated.

(iii) Positions of the parties

**193** It is the Applicant's position that it is substantially affected by the refusal and relies on the evidence of Mr. Robinson. Mr. Robinson testified that without the Respondents' supply, the Applicant's earnings from operations would drop by $**[CONFIDENTIAL]** from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]** using the Base Period as a comparator. He testified that, assuming that the Applicant incurred additional costs for transportation and for DOAs and shrink, and assuming that the Applicant would be required to pay a premium of $**[CONFIDENTIAL]** over the Quebec board price to access replacement chickens in Quebec, the Applicant's earnings from operations would drop by $**[CONFIDENTIAL]** from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]**.

**194** The Respondents argue that the Applicant is not substantially affected by the refusal. They contend that the evidence supports their submission that the Applicant would be able to replace the Respondents' chickens with chickens from Quebec and in doing so would be able to maintain historic levels of processing which would result in earnings that would allow it not only to survive but also to be viable.

**195** The Respondents point to the Applicant's own procurement initiative, which concluded that within a 600 km radius of the Applicant's plant in St-François, a significant volume of live chickens is available from Quebec producers upon payment of certain premiums over the Quebec board price.

**196** The Respondents also rely on the opinion of the Applicant's expert, Mr. Robinson, who testified using the same approach as that used by Ms. Sanderson, that the Applicant would incur additional costs of $**[CONFIDENTIAL]** in order to procure replacement chickens from Quebec and would be left with earnings of over $**[CONFIDENTIAL]**. The Respondents argue that even earnings of this magnitude approach the Applicant's average yearly earnings prior to the arrival of the Nova Scotia and Prince Edward Island chickens, and that the Applicant therefore cannot be "substantially affected" by their refusal even if the Applicant had to replace all the Respondents' chickens with chickens from Quebec producers.

**197** The Respondents essentially argue that chickens are available in the market to replace the chickens currently supplied by the Respondents in sufficient quantities and on trade terms that would allow the Applicant not only to survive but to be viable based on the survival and viability thresholds set by Mr. Tavares in his testimony. Mr. Tavares attested that the Applicant "requires a guarantee of 350,000 chickens per week to stay viable", but later stated that a weekly supply of 300,000 live chickens would allow the Applicant to get by, that "getting by" referred to "viability in the long term" and that "[d]epending on the markets, it could mean losing a lot of money".

**198** Further, the Respondents contend that even if the Applicant failed to replace any of the Respondents' chickens, its current supply from Nova Scotia and Prince Edward Island and other producers in New Brunswick would allow the Applicant to maintain processing such that it would achieve 108.5% and 93.05% of its self-declared survival ("getting by") and viability thresholds respectively. In the Respondents' view, given the above considerations, the Applicant cannot be substantially affected in its business by reason of the refusal.

**199** The Respondents Dynaco and Acadia argue that their respective refusals cannot substantially affect the

Applicant's business because of their small numbers.

(iv) Analysis

**200** Earnings are a meaningful indicator of the performance of an enterprise. In order to assess the impact of the refusal at issue on the Applicant's business, it is therefore useful to consider the Applicant's earnings over time. The projected impact on future earnings by the refusal will be a helpful guide in determining whether the Applicant's business is substantially affected by the refusal.

**201** The evidence of both Mr. Robinson and Ms. Sanderson addresses the question of projected earnings of the Applicant. As discussed above, various models were developed by Mr. Robinson and reviewed by Ms. Sanderson. We review below certain relevant aspects of this evidence.

**202** Mr. Robinson's first scenario involved the loss of the Respondents' chickens. He concluded that without those chickens, the Applicant's earnings would drop by $**[CONFIDENTIAL]** from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]** using the Base Period as a comparator. Ms. Sanderson assumed that the Applicant would be able to replace the Respondents' chickens with Quebec-sourced chickens, and she did not provide an estimate of the Applicant's earnings if it could not obtain supply on usual trade terms. She is of the opinion that the Applicant would incur an additional cost of almost $**[CONFIDENTIAL]** if it were to replace the Respondents' chickens with Quebec-sourced chickens.

**203** Of the four scenarios considered by Mr. Robinson, the one that least affects the Applicant's business is the second scenario, which assumes that the Respondents' birds are replaced with Quebec birds and that the Nova Scotia and Prince Edward Island birds continue to be processed by the Applicant. If the Applicant can demonstrate that under this scenario its business is substantially affected by the refusal, there will be no need to consider the other scenarios developed by Mr. Robinson, including his first scenario in which the Applicant's earnings will drop to $**[CONFIDENTIAL]**.

**204** In the second scenario, Mr. Robinson makes the following assumptions: that chicken could be obtained in Quebec but that premiums would have to be paid to Quebec producers to entice them away from their current processor; that the Applicant would be responsible for DOAs, transportation costs and shrink; that the appropriate chickens could be contracted for the sizes necessary for the Applicant's customers. As mentioned above, Mr. Robinson assumed a premium of $**[CONFIDENTIAL]**/kg of live chicken based on conversations between the Applicant's management and Quebec producers.

**205** As a result of this analysis, Mr. Robinson identified that the earnings from operations would drop by $**[CONFIDENTIAL]** from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]** and that the St-François Plant would continue to operate **[CONFIDENTIAL]**. In Mr. Robinson's opinion, under this scenario, as with the other three he developed, the removal of the Respondents' chickens would have a significant impact on the profitability of the operations and, by extension, on the viability of one of the "most efficient processing plants in Canada".

**206** Ms. Sanderson disagreed with the size of the premium that Mr. Robinson assumed would have to be paid by the Applicant to Quebec producers. Initially, she was of the view that a more realistic premium would be $**[CONFIDENTIAL]** over the Quebec board price. Ms. Sanderson was of the opinion that after taking into account the differences in board prices, premiums and transportation costs, and the cost of purchasing additional chickens to replace the lost volumes from increased mortality and shrink, the total incremental cost to the Applicant to source live chickens from Quebec instead of the Respondents is $**[CONFIDENTIAL]**/kg of live weight, which represents **[CONFIDENTIAL]**% of the Applicant's total cost of sales for the 12-month period ending June 2008. In Ms. Sanderson's opinion, this would leave the Applicant with earnings of $**[CONFIDENTIAL]** for the period, as opposed to over $**[CONFIDENTIAL]** estimated by Mr. Robinson.

**207** As discussed earlier, these figures were revised by Ms. Sanderson as a result of corrected data adduced

during the trial. As explained above, her estimate of earnings for the period was revised to $**[CONFIDENTIAL]** after corrections were made to affidavits and additional evidence was provided. This now represents a drop of approximately $**[CONFIDENTIAL]** from estimated earnings of $**[CONFIDENTIAL]**. Her revised opinion was that the premium would be in the area of $**[CONFIDENTIAL]**.

**208** On cross-examination, Ms. Sanderson agreed that a reduction in earnings of "**[CONFIDENTIAL]**" is in an order of magnitude of **[CONFIDENTIAL]** %. She acknowledged that **[CONFIDENTIAL]** % is "a large number" (the actual reduction is in the order of **[CONFIDENTIAL]** %). She nevertheless went on to express the opinion that the Applicant would not be substantially affected or precluded from carrying on business by reason of the refusal, because its earnings from operations would be comparable with historical levels.

**209** Ms. Sanderson stated her opinion as follows on examination in chief at the hearing:

> Yes. So -- given I find that they're going to be able to earn profits -- earnings from operations that are in the range of **[CONFIDENTIAL]**, which is **[CONFIDENTIAL]** percent higher than the average over '98 through to 2007 and about, if you exclude the year of the fire. So given that their earnings are within the range of historical levels, they're certainly not precluded from carrying on business if they get replacement supply.
>
> And I would also conclude that they're not substantially affected given their earnings are comparable to historical levels.

**210** It is noteworthy that Mr. Robinson's assessment regarding the Applicant's reduction in earnings relative to the Base Period is in the order of a **[CONFIDENTIAL]** % reduction.

**211** In terms of transportation costs, Ms. Sanderson compared the live-haul cost of chickens from Quebec with the Applicant's average live-haul cost for all of New Brunswick. Mr. Robinson accepts Ms. Sanderson's live-haul cost of $**[CONFIDENTIAL]**/kg for Quebec chickens, but argues that she should have compared that cost with the live-haul cost for the Respondents' chickens. Had this been done by Ms. Sanderson, Mr. Robinson maintains that the result of her analysis would have essentially been the same as his. If the analysis undertaken by both experts assessed the incremental costs of replacing the Respondents' chickens with Quebec chickens, then the approach advocated by Mr. Robinson would necessarily produce a more accurate result in terms of incremental costs, as it relates to the replacing of the Respondents' birds.

**212** While we agree with Mr. Robinson's approach, we disagree with his estimate ($**[CONFIDENTIAL]**) of the live-haul cost for the Respondents' chickens. We agree with Ms. Sanderson that this estimate must be incorrect because Mr. Landry testified that the cost of transporting live chickens from southern New Brunswick to the St-François Plant varies between $**[CONFIDENTIAL]** and $**[CONFIDENTIAL]**, and that 15% of the Applicant's New Brunswick supply comes from southern New Brunswick. He added that the Applicant's average transportation cost for New Brunswick chickens is around $**[CONFIDENTIAL]**/kg. The freight costs associated with the Respondents' live chickens must therefore be approximately $**[CONFIDENTIAL]**/kg, since the Respondents' supply represents 85% of the Applicant's New Brunswick supply. The incremental transportation costs of supplying the replacement birds, approximately $**[CONFIDENTIAL]**/kg, are therefore part of the additional costs of replacing the Respondents' birds, and these costs, together with premiums, constitute the main factors affecting the cost of live chickens to be obtained from Quebec. Premiums also represent the main area of disagreement between the two experts.

**213** It is not disputed that Nadeau will incur additional costs when sourcing chicken in Quebec because of DOAs and shrinkage. With respect to DOAs, Mr. Landry testified that if a load arrives at the St-François Plant with a DOA rate of 1% or more, the Canadian Food Inspection Agency will conduct an investigation. If this rate is 3% or higher, the Agency will impose a fine.

**214** There is general agreement between Mr. Robinson and Ms. Sanderson in respect of DOA/shrink costs. Mr. Robinson finds that Nadeau's shrink and DOA percentages would be **[CONFIDENTIAL]**%. There is, however, a

different approach in respect to losses associated with replacing DOAs and shrink. Ms. Sanderson does not factor in lost profits, since these chickens are replaced with new purchases.

**215** Both experts agree that, as a result of the Applicant having to replace all of the Respondents' chickens with chickens from Quebec, earning from operations will drop, relative to the Base Period, to a range from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]**. Ms. Sanderson's opinion acknowledges this reduction in earnings but reasons that the Applicant is not substantially affected or precluded from carrying on business as a result, because this range of earnings is comparable with historic levels. Historic levels are defined by Ms. Sanderson as the average earnings between 1998 and 2007, excluding the year of the fire.

**216** The Tribunal accepts that the approach taken by both parties regarding the Applicant's earnings is the correct one for assessing the projected earnings of the Applicant as a result of the refusal. With respect, however, we reject Ms. Sanderson's conclusion on "substantial effect" for the reasons that follow.

**217** On cross-examination, Ms. Sanderson agreed that a **[CONFIDENTIAL]**% reduction in earnings is "a large number" but was of the opinion that the Applicant was not substantially affected. Her opinion is based on the choice of a different comparator period. In her analysis, Ms. Sanderson adopts the period 1998-2007 in support of her conclusion. In her view, excluding the year of the fire, this period reflects the historic performance of the Applicant in terms of earnings. Her analysis consequently fails to take into account the subsequent period, when earnings from operations were significantly higher as a result of the arrival of additional chickens from Nova Scotia and Prince Edward Island. In our view, this approach does not fairly reflect the Applicant's circumstances. It is an approach that would purport to measure the impact of the refusal on the basis of the Applicant's historic performance and not its current circumstances. Such an approach would not allow for consideration of growth and dynamic expansion of an enterprise in assessing the effect of a refusal to deal under paragraph 75(1)(*a*). We agree, however, that current earnings should not be considered if they reflect unusual or non-recurring circumstances.

**218** Here, for reasons that are particular to this case, the Applicant saw its processing capacity increase significantly for a three-year period as a result of certain agreements with Nova Scotia and Prince Edward Island producers. A second shift had to be set up at the Applicant's plant and additional employees had to be hired. In many ways, this was a planned expansion of production, although potentially not for an indefinite period. This is not comparable with an exceptional event such as a fire or other act of God, which arguably would not be reflective of normal operations.

**219** While the Applicant's earnings from operations since 2007 indicate a significant increase in earnings over prior years, they are nevertheless earnings that resulted from business decisions which were made in the context of an expansion of operations owing to particular circumstances. The substantial effect on the Applicant's business by reason of the Respondents' refusal must, in our view, be considered in the context of this increased capacity and, by extension, the Applicant's increased earnings, because this is the Applicant's current business situation. To conclude otherwise would be inconsistent with the provision which requires that the Applicant be substantially affected in "his business". The fact that the Applicant's earnings are above its historic average is of no consequence. What matters, for the purpose of paragraph 75(1)(*a*), is the effect of the refusal on the Applicant's current business. In our view, it is therefore appropriate to consider the Applicant's recent increase in earnings in assessing the effect of the refusal on the Applicant's business.

(v) Conclusion on paragraph 75(1)(*a*)

**220** In summary, we agree with Mr. Robinson that the Base Period is the appropriate comparator period in the circumstances. The increase in earnings over the historic average, reflected in the selected Base Period, is representative of the Applicant's current business earnings and is therefore a proper basis upon which to consider the effect on the Applicant's business that may be caused by reason of the Respondents' refusal to supply.

**221** In the result, we find that a reduction in earnings of **[CONFIDENTIAL]**% relative to the Base Period is

significant and important in the circumstances of this case. We therefore find that, on the basis of the evidence and arguments adduced, replacing the Respondents' chickens with Quebec chickens will have a substantial impact on the Applicant's business. Given our above determinations, we find that the Applicant has established that it is substantially affected in its business due to its inability to obtain adequate supplies anywhere in a market on usual trade terms. Because of the effect of the refusal on earnings explained above, we are of the view that our conclusion would have been the same under any of the Robinson scenarios. Therefore, by reason of the projected impact on the Applicant's earnings, the Applicant would be substantially affected in its business.

**222** Certain other options in terms of supply, which are potentially plausible, were simply not argued before the Tribunal: for instance, the possibility of replacing one half of the Respondents' supply from Quebec producers, as opposed to all of it. The impact on the Applicant's business was not considered by the experts, nor did the parties advance arguments on such a scenario and, in these circumstances, we decline to speculate on its effect on the Applicant's profits.

**223** On the evidence, and upon consideration of the arguments advanced by the parties, for the above reasons, we are satisfied that the Applicant has met its burden under paragraph 75(1)(*a*) of the Act.

**224** We now turn to consideration of the requirement under paragraph 75(1)(*b*).

### C. Has the Applicant established that it is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market pursuant to paragraph 75(1)(*b*) of the Act?

#### (1) Parties' Submissions

**225** The Applicant contends that it is unable to obtain adequate supplies of live chickens because of insufficient competition among suppliers in the market. It submits that as a result of the supply management scheme, chicken producers are completely insulated from competition. The Applicant states that it is in fact the processors who fight among themselves to offer ever-increasing prices to producers.

**226** The Respondent Westco contends that the insufficient competition referred to in paragraph 75(1)(*b*) must be assessed in light of the overall context of the Act and can only refer to situations in which a competitor or competitors have a dominant position or a monopoly, or in which there is a lack of competition as a result of any kind of collusion. It submits that there are a considerable number of suppliers in the relevant market and that there is no evidence of collusion among them, which indicates that there is no issue of insufficient competition. Westco further states that not only are there several competitors, but the evidence also shows that chicken producers are indeed willing to compete and supply the Applicant with their production upon payment of premiums over and above the board price set by regulatory authorities. The Respondents Dynaco and Acadia also submit that there are enough producers in the relevant market to conclude that there is sufficient competition.

**227** In the alternative, the Respondents contend that the evidence in the Tribunal's record shows that the cause of any inability on the Applicant's part to obtain replacement birds has nothing to do with a lack of competition among suppliers of live chickens. It is rather because of the following three factors that came to light during the hearing, namely, the Respondents' objectively justifiable business reasons for the refusal, the workings of the supply management system and the level of competition among processors.

#### (2) Analysis

**228** Pursuant to paragraph 75(1)(*b*) of the Act, the refused party must demonstrate that it is unable to obtain adequate supplies of the product because of insufficient competition among suppliers in the market. As was set out in *B-Filer*, paragraph 75(1)(*b*) of the Act contains two requirements. First, there must be insufficient competition among suppliers in the relevant market. Second, the inability of the refused party to obtain adequate supplies of the product must be by reason of that insufficient competition. The Tribunal, in *Canada (Director of Investigation and*

*Research) v. Xerox Canada Inc.* *(1990), 33 C.P.R. (3d) 83*, considered the causal requirement of the provision and concluded as follows, at page 116:

> In addition, the refusal to supply must occur "*because* of insufficient competition among suppliers of the product". That is, the overriding reason that adequate supplies are unavailable must be the competitive conditions in the product market.
>
> (emphasis added)

**229** The Tribunal must therefore determine whether the Applicant has established that insufficient competition among suppliers in the market is the overriding reason why it is unable to obtain adequate supplies of the product in the market. The product and geographic markets, for the purposes of paragraph 75(1)(*b*), are the same as those which have been defined pursuant to paragraph 75(1)(*a*). The relevant geographic market therefore consists of New Brunswick, Prince Edward Island, parts of Quebec within a 500 km radius of the St-François Plant, and Nova Scotia.

**230** The Tribunal has not yet had an opportunity to determine the meaning of "insufficient competition". In *Xerox* and *Chrysler*, the Tribunal defined the relevant product market in a very narrow manner, and it was therefore not difficult for the Tribunal to conclude that there was insufficient competition among suppliers in the market. The Tribunal noted that the level of competition among suppliers will depend on the facts of the particular case. The Tribunal also stated the following in *Xerox*, at page 116:

> Clearly a market composed of numerous suppliers acting independently would not qualify. (It is also very difficult to conceive of a case before the tribunal where so many of a multitude of suppliers would refuse to supply an individual that his business could be "substantially affected". One would postulate that if one supplier did not want the business, another would be more than happy to earn the extra revenue.)

**231** We now turn to an assessment of the competitive conditions in the market. The evidence on the record shows that there are many suppliers in the relevant market. Data provided by the Chicken Farmers of New Brunswick indicate that in 2007 there were 38 chicken producers in New Brunswick, 82 producers in Nova Scotia, 7 producers in Prince Edward Island and 760 producers in Quebec. Statistics from Les Éleveurs de volailles du Québec indicate that in 2006 there were 85 producers in the Beauce region, 62 producers in the Québec region and 22 producers in the Côte-du-Sud region, all of which are located in Quebec within 400 km of the St-François Plant. From this data, the Tribunal can conclude that there are, in fact, numerous producers located in the relevant geographic market.

**232** The evidence adduced at the hearing shows that over the last few years a number of chicken producers have consolidated their quotas and that some producers have formed alliances to reap financial benefits. Further, the evidence demonstrates that some producers are related, as they are members of the same co-operatives. The evidence does suggest some lack of independence among producers in the New Brunswick market. In fact, Mr. Feenstra has indicated that only eight nominal quota holders in New Brunswick are independent from the Respondents. The Respondents together produce almost 75% of New Brunswick's live chickens. Mr. Feenstra, however, also acknowledged that he is not aware of that degree of concentration in any other Canadian province. In fact, no evidence was adduced regarding such concentrations in Nova Scotia, Prince Edward Island or parts of Quebec. Furthermore, evidence adduced by the Applicant concerning its efforts to seek replacement supply of live chickens in Quebec clearly demonstrates that producers are acting independently. Results from the Applicant's survey show that producers were in fact offering live chickens to the Applicant at different prices above the board price. Under these circumstances, there is insufficient evidence to conclude that there is either collusion or a lack of independence amongst producers in the market as a whole.

**233** Normally, the presence of numerous suppliers acting independently is a strong indicator of sufficient competition. However, the parties in this matter are operating within the supply management system, which is governed by a detailed and complex set of regulations. We must therefore consider the impact, if any, of the supply management system on competition among suppliers in the market.

**234** As discussed above, under supply management, the minimum price for which chicken may be sold in respective provinces is set by the provincial marketing boards. Production is also restricted to quota holders and limited by a producer's quota allocation.

**235** The Applicant asserts that as a result of the supply management system, chicken producers do not compete amongst themselves. Mr. McCullagh indicated that the supply management system has been a "quasi-monopoly for chicken producers" and Dr. Ware indicated that "[w]hatever the merits of such a system, there is no doubt that competition is restricted by it, as entry is precluded completely and the competitive battles for market share which create benefits for consumers and foster incentives for innovation are also completely absent".

**236** The purpose or objects of the acts and regulations governing the supply management system are not intended to limit competition. The CFC was created in 1978 by order in council pursuant to section 16 of the *Farm Products Agencies Act* ("FPAA"), *R.S.C. 1985, c. F-4*. Section 21 of the FPAA identifies the objects of a farm product agency:

> **21.** The objects of an agency are
>
> (a) to promote a strong, efficient and competitive production and marketing industry for the regulated product or products in relation to which it may exercise its powers; and
>
> (b) to have due regard to the interests of producers and consumers of the regulated product or products.
>
> (emphasis added)
>
> * * *
>
> **21.** Un office a pour mission :
>
> a) de promouvoir la production et la commercialisation du ou des produits réglementés pour lesquels il est compétent, de façon à en accroître l'efficacité et la compétitivité;
>
> b) de veiller aux intérêts tant des producteurs que des consommateurs du ou des produits réglementés.
>
> (nos soulignements)

**237** As an agency created under Part II of the FPAA, the CFC has the power to implement a marketing plan for chicken pursuant to the terms of the proclamation establishing it (see s. 22(1) FPAA). Some of the terms of that plan are found in the 2001 Federal Provincial Agreement for Chicken. The purpose and objectives of that agreement are as follows :

> **1.01** This Agreement provides for an orderly marketing system for chicken coordinated in a flexible and market responsive manner having appropriate safeguards so as to provide consistency, predictability and stability in accordance with the following objectives:
>
> (a) to optimize sustainable economic activity in the chicken industry;
>
> (b) to pursue opportunities in both domestic and international markets;
>
> (c) to enhance competitiveness and efficiency in the chicken industry; and

(d) to work in the balanced interest of producers, industry stakeholders and consumers.

(emphasis added)

* * *

**1.01** Le présent Accord établit un système de commercialisation ordonnée du poulet coordonné de façon flexible et axée sur le marché, comportant les mesures de protection nécessaires pour assurer l'uniformité, la prévisibilité et la stabilité en conformité avec les objectifs suivants :

(a) optimiser l'activité économique durable dans l'industrie du poulet;

(b) rechercher des débouchés tant sur le marché national que sur le marché international;

(c) améliorer la compétitivité et l'efficacité dans l'industrie du poulet;

(d) travailler dans l'intérêt mutuel des producteurs, des intervenants de l'industrie et des consommateurs.

(nos soulignements)

**238** The Applicant's expert, Dr. Barichello, has indicated that competition, within the context of the supply management system, can exist among producers in the provinces in which premiums are paid, albeit not below the minimum price established by the board:

> **Ms. Healey**: So to the extent -- so there's that range, minimum price and up; that's an area in which producers could engage in competition?
>
> **Dr. Barichello:** That's correct.
>
> **Ms. Healey:** You want 6 cents for your birds; I'll agree to 4.5?
>
> **Dr. Barichello**: Right.

**239** However, Dr. Barichello also stated that there was a relatively modest scope for competition within the market, as the margin within which producers could compete was limited. He also added that "[n]ormal competitive pressure would be when you would be able to also lower your required price such as below the minimum price".

**240** The Tribunal accepts that the margin in excess of the regulated minimum price that Quebec producers receive is relatively small. In our view, however, it is competition among individual producers that keeps this margin relatively small. What matters is that the price received by producers (including the margin in excess of the regulated minimum price) is determined by competition among producers. As for Dr. Barichello's contention that the minimum price set by the provincial board restricts competition, we are of the view that the regulated minimum price does not itself limit a producer's ability to compete effectively unless the aggregate market supply set by the marketing board exceeds demand at the regulated minimum price. In that case, the regulated minimum price would prevent the competitive price adjustment required to clear the market. There is no evidence that competition in the relevant market is currently inhibited in this way.

**241** Significant evidence was adduced to the effect that prices received by producers in Quebec exceed the minimum price set by the marketing board. Such evidence was outlined under the paragraph 75(1)(*a*) analysis and will not be repeated here. Suffice it to say that the Tribunal is satisfied that prices received by producers in Quebec

generally include a premium above the regulated base. As Dr. Barichello has conceded, this premium and thus the price received by each producer can be determined by competition among individual producers.

**242** Furthermore, some Quebec producers canvassed during the Applicant's procurement survey indicated that they were seeking the same price as other producers were getting. This is consistent with price-taking behaviour and supports the finding that an individual producer cannot set the price and that the price ultimately paid is set by the competitive forces in the market.

**243** The restrictions on entry and expansion established by the supply management system have an impact on competition, but inelastic market supply does not itself imply that there is insufficient competition among suppliers in the market.

**244** In our view, while supply management restricts the available aggregate supply and makes it less price-responsive, it does not give any one producer any price-setting power. The inability of the Applicant to obtain adequate supplies on the usual trade terms is not the result of insufficient competition among individual producers. The existence of inelastic market supply is not incompatible with the market price being set by competition among individual producers in the market.

**245** Apart from producers in Quebec, there is very little evidence regarding the prices producers in Nova Scotia and Prince Edward Island are receiving relative to their respective regulated minimum prices. We know that in New Brunswick, there is an Incentive Plan in place. We are unable, therefore, to make a conclusive finding as to whether and how the regulated minimum prices in those provinces might have affected competition among producers.

**246** To conclude, we are of the opinion that the Applicant has failed to establish that there is insufficient competition among suppliers in the relevant market for the following reasons: the number of producers in the market; the absence of any evidence that producers, except for the Respondents, are not acting independently; and our conclusion that supply management in and of itself does not establish that there is insufficient competition among individual producers.

**247** Even if there were a finding of insufficient competition among suppliers, we would nevertheless still be of the view that the Applicant has not met its burden under paragraph 75(1)*(b*) of the Act. There is inadequate evidence to establish that the competitive conditions of the market are the overriding reason why the Applicant is unable to obtain adequate supplies of the product. The overwhelming evidence indicates that the limit on aggregate supply which results from the supply management system is essentially the reason why the Applicant is unable to obtain adequate supplies of live chickens. As will become evident from our discussion of ample supply for the purposes of paragraph 75(1)*(d*) later in these reasons, the limit on aggregate supply has a very significant impact on the question of whether the Applicant is able to obtain adequate supplies of chickens in the market.

**248** Therefore, for the purposes of paragraph 75(1)(*b*), we conclude that the Applicant has not established that it is unable to obtain adequate supplies of chickens because of insufficient competition among suppliers in the market.

### D. **Has the Applicant established that it is willing and able to meet the usual trade terms pursuant to paragraph 75(1)(*c*) of the Act?**

**249** The Applicant contends that it has always met the usual and customary terms of trade. The testimony of the Applicant's representatives, Mr. Feenstra, Mr. Landry, and Mr. Plourde, indicates that the Applicant is willing to meet the usual trade terms with respect to Quebec supply. There appears to be no dispute that the Applicant is willing and able to meet the usual trade terms.

**250** On the evidence, we are satisfied that the Applicant is willing and able to meet the usual trade terms of the suppliers of live chickens.

E. **Has the Applicant established that the product is in ample supply pursuant to paragraph 75(1)(*d*) of the Act?**

**251** The Tribunal has dealt with this element of the provision only once. *Quinlan's of Huntsville Inc. v. Fred Deeley Imports Ltd.*, *2004 Comp. Trib. 28*, is the only case in which the Tribunal has made a determination in respect to ample supply. It decided that the product, Harley-Davidson motorcycles, was not in ample supply and consequently declined to grant an interim order. The Tribunal held, at paragraph 19, that "section 75, and, therefore, interim orders under section 75, are meant to deal with situations in which the product is readily available and unencumbered in the sense that it has not been sold or promised to another purchaser."

**252** In *Quinlan's*, the Tribunal acknowledged that the product was in ample supply some months of the year, but found that it was not appropriate to order interim supply, in the circumstances, because the product was not in ample supply at the time the order to supply was sought.

**253** In the circumstances of this case, the supply of the product, live chickens, is regulated under the supply management system. The system strictly controls the supply of live chickens in Canada through a quota system. Under supply management, each producer may only produce live chickens in accordance with its quota in a given period. A producer faces a significant penalty if it exceeds its quota. The system does provide for adjustments in the total supply of live chickens. This adjustment is fixed at each production period through a complex adjustment formula designed to strike a balance between chicken production and consumer demand. The issue here is whether, under these circumstances, live chickens can be said to be in ample supply for the purposes of paragraph 75(1)(*d*).

(1) **The supply management system**

**254** Before proceeding further, it is useful to fully understand the complex supply management system in place for the production of live chickens in Canada and to appreciate how that system functions. To that end, we will review below the various statutory and regulatory provisions which underlie the system, applicable federal-provincial agreements and certain orders issued by provincial marketing boards which are material to the issues in this case.

(a) Chicken Farmers of Canada and the 2001 Federal- Provincial Agreement

**255** As mentioned above, the Chicken Farmers of Canada was created in 1978 by order in council and implements a marketing plan pursuant to the terms of the 2001 Federal-Provincial Agreement for Chicken (the "FPA"). Schedule A to the FPA is known as the *Chicken Farmers of Canada Proclamation*, *SOR/79-158*. This document establishes the CFC and the quota system. Under section 6 of the Proclamation, the CFC shall establish a quota system for the signatory provinces by which quotas are allotted to chicken producers in each province to which quotas are allotted by the appropriate board. The CFC Board of Directors is comprised of the following persons:

(i) ten members representing the producers of each provincial marketing board;

(ii) two persons appointed by the Canadian Poultry and Egg Processors Council;

(iii) one person appointed by the Canadian Restaurant and Food Service Association;

(iv) one person appointed by the Further Poultry Processors Association of Canada; and

(v) one national chairperson elected from among the chairs of the provincial marketing boards.

**256** Under section 3.01 of the FPA, each Provincial Commodity Board agrees to limit chicken production pursuant to the quotas:

**3.01** In the fulfillment of their obligations under section 2.05, the Provincial Commodity Boards each agree:

(a) to limit the total quantity of chicken produced in their respective provinces, and marketed, to the quota allocation as determined from time to time by reference to this Agreement;

(b) to establish the minimum prices at which live chicken may be sold in their respective provinces; and

(c) in conjunction with CFC, to implement and maintain a coordinated system of quota allotment that is auditable by CFC, where the basic effects as between provinces are similar.

(emphasis added)

* * *

**3.01** Dans le cadre de la réalisation de leurs obligations en vertu de l'article 2.05, chaque office de commercialisation provincial convient :

(a) de limiter la quantité totale de poulet produite et commercialisée dans leur province respective à l'allocation de contingents déterminée, de temps à autre, conformément au présent Accord;

(b) d'établir des prix minimums de vente du poulet vivant dans leur province respective;

(c) de mettre en oeuvre et de maintenir, en collaboration avec les PPC, un système coordonné d'allocation de contingents qui peut être vérifié par les PPC lorsque les effets de base entre les provinces sont similaires.

(nos soulignements)

**257** Schedule B to the FPA is known as the Operating Agreement and its purpose is to set out the fundamentals of the operation of the marketing system for chickens.

**258** Schedule B distinguishes "federal quota" from "provincial quota". It defines "federal quota" as "the quantity of chicken expressed in live weight that a producer is entitled to market in interprovincial and export trade in a period, and is allotted to the producer by the Provincial Commodity Board on behalf of CFC". This is different from the "provincial quota" defined as "the quantity of chicken expressed in live weight that a producer is entitled to market in intraprovincial trade in a period, and is allotted to the producer by the Provincial Commodity Board."

**259** It appears, however, that the provinces adopt as the provincial quota the exact share assigned by the CFC. Justice Abella, in *Fédération des producteurs de volailles du Québec v. Pelland*, 2005 SCC 20; [2005] 1 S.C.R. 292, acknowledged that this is the accepted practice in the industry. She states at paragraph 8 that "[e]ach provincial body ... adopts as its intraprovincial production quota the exact share federally assigned to it."

**260** It is also accepted that the system provides for a granting of authority in respect of allotting federal quotas and administering them in accordance with the *Canadian Chicken Marketing Quota Regulations*, SOR/2002-36 (see subsection 2(1) of the *Chicken Farmers of Canada Delegation of Authority Order*, SOR/2003-274). This was recognized by Justice Abella in *Pelland*, where she wrote at paragraph 9 of the Court's decision that "[i]n order to facilitate the integration of production and marketing quotas, the federal body delegates its authority to regulate the marketing of chickens in interprovincial and export trade to the provincial body".

**261** This regulatory scheme provides strict limitations on quotas. Section 9 of the *Canadian Chicken Marketing*

*Quota Regulations* provides the following limits:

> **9.** The Provincial Commodity Board of a province must allot federal quotas to producers in the province in such manner that the aggregate of the following numbers of kilograms of chicken that is produced in the province, and authorized to be marketed, during the period referred to in the schedule will not exceed the applicable number of kilograms of chicken set out in column 2 of the schedule in respect of the province for that period:
>
> (a) the number of kilograms of chicken authorized to be marketed by producers in interprovincial or export trade under federal quotas allotted on behalf of CFC by the Provincial Commodity Board;
>
> (b) the number of kilograms of chicken authorized to be marketed by producers in intraprovincial trade under provincial quotas allotted by the Provincial Commodity Board; and
>
> (c) the number of kilograms of chicken anticipated to be marketed by producers under quota exemptions authorized by the Provincial Commodity Board.
>
> (emphasis added)
>
> * * *
>
> **9.** L'Office de commercialisation d'une province doit allouer des contingents fédéraux aux producteurs de cette province de manière que la somme des nombres de kilogrammes de poulet ci-après, exprimés en poids vif, qui sont produits dans une province et dont la commercialisation est autorisée au cours de la période visée à l'annexe, n'excède pas le nombre de kilogrammes de poulet, exprimé en poids vif, visé à l'annexe pour cette province, pour la période en cause :
>
> a) le nombre de kilogrammes de poulet que les producteurs sont autorisés à commercialiser sur le marché interprovincial ou d'exportation, au titre des contingents fédéraux alloués au nom des PPC par l'Office de commercialisation de la province;
>
> b) le nombre de kilogrammes de poulet que les producteurs sont autorisés à commercialiser sur le marché intraprovincial, au titre des contingents alloués par l'Office de commercialisation de la province;
>
> c) le nombre de kilogrammes de poulet que les producteurs prévoient de commercialiser en vertu des exemptions de contingents autorisées par l'Office de commercialisation de la province.
>
> (nos soulignements)

**262** The schedule referred to in the above provision sets the quota allocation for an eight-week production period. The system provides for periodic adjustments to the schedule. We reproduce in Schedule B to these reasons a recent schedule issued covering the quota period of January 4, 2009, to February 28, 2009.

**263** The FPA also provides for a specific quota allocation procedure (see sections 3.01 to 3.10 of the FPA) (the "quota allocation procedure") and for subsequent adjustments to the quotas set in the initial procedure (see sections 4.01 to 4.11 of the FPA) (the "quota adjustment procedure"). We will briefly review these two regulatory procedures.

(b) The quota allocation procedure

**264** Section 3.02 of the FPA provides that, for six periods at a time, the CFC will establish the initial base for each province pursuant to a formula which takes into account the previous year's level. Each provincial commodity board may make a request to adjust the initial base allocation for one or more of the six periods provided that the adjustments for any period do not exceed 5% and the total of the bases for the six periods does not change (s. 3.03).

**265** Further, prior to each period, each provincial commodity board also makes a written quota allocation request to the CFC in the following manner:

> **3.05**...
>
> (a) in accordance with the procedures, if any, established pursuant to section 5.01 below, the Provincial Commodity Board will consult with its processors using a "bottom up approach and, having regard to the market requirements proposed by those processors will arrive at the estimated provincial market requirements prior to the submission of the quota allocation request for the period to CFC;
>
> (b) in accordance with the procedures, if any, established pursuant to section 5.02 below, Provincial Commodity Boards in each region shall consider discussing market conditions and estimated market requirements in the region prior to the submission of the quota allocation request by each Provincial Commodity Board to CFC; and
>
> (c) in submitting its quota allocation request to CFC for a period, each Provincial Commodity Board will provide to CFC the rationale for the request which will enable CFC to fulfill its obligations under the *Farm Products Agencies Act*, including those in section 23(2).
>
> (emphasis added)

* * *

> **3.05** [...]
>
> (a) l'office de commercialisation provincial consulte ses transformateurs, conformément à la procédure, s'il y en a une, qui est établie en vertu de l'article 5.01, en utilisant une approche "ascendante" et, après avoir examiné les besoins de marché proposés par ces transformateurs, estime les besoins du marché provincial avant de soumettre aux PPC la demande d'allocation de contingents pour la période;
>
> (b) les offices de commercialisation provinciaux de chaque région envisagent de discuter, conformément à la procédure, s'il y en a une, qui est établie en vertu de l'article 5.02 ci-dessous, des conditions de marché et des estimations des besoins du marché dans la région avant de présenter la demande d'allocation de contingents aux PPC;
>
> (c) lorsqu'il présente sa demande d'allocation de contingents aux PPC pour une période, chaque office de commercialisation provincial fournit aux PPC la justification de la demande, ce qui permet aux PPC de s'acquitter de leurs obligations en vertu de la Loi sur les offices des produits agricoles, y compris celles qui sont prévues au paragraphe 23(2).
>
> (nos soulignements)

(c) The quota adjustment procedure

**266** The Operating Agreement also sets out certain rules regarding adjustments to the quota allocation. Temporary changes to the regional range are possible in certain circumstances (see s. 4.02). For provinces in a region ("region" is defined in section 2.01 of the Operating Agreement), the regional range shall allow for quota allocation changes of up to 5%. An adjustment to the regional range, which is not temporary and which establishes a new regional range requires a special vote of the CFC (s. 4.01).

**267** Further, section 4.07 provides that a provincial board may request a quota allocation that exceeds the provincial range for one or more periods to accommodate exceptional circumstances ("provincial range" means the percentage change from the base for a province for a period). Section 4.06 provides that "[f]or a province, the provincial range shall allow for quota allocation changes of up to eight (8) percent" and "[a]n adjustment to the provincial range, other than pursuant to section 4.07, requires a special vote" of the CFC.

**268** What emerges from the above provisions of the FPA is that any adjustments to quotas are made provincially and/or regionally. The system provides for adjustments to be made on a "macro" level, that is, for all producers within a province or a region.

**269** The evidence adduced before the Tribunal does not contradict the above summary of the supply management system. We note, in particular, the evidence of Mr. Feenstra in his reply affidavit, wherein he confirms that the "bottom-up" approach was implemented across Canada in or about January 1995. He further attests that during the period leading up to the new approach, processors had experienced shortages of chickens for so long and thought they could sell a lot more chicken. According to Mr. Feenstra, this shortage led to a recommendation to increase volumes and prices substantially. Mr. Feenstra further testified that the market could not handle the increase and that a significant oversupply of chickens resulted across Canada.

**(2) Positions of the parties**

**270** The Applicant argues that the product here is in ample supply. It takes the position that the Respondents can and do raise enough chickens and just want to deprive the Applicant of them. It is argued that the purpose of paragraph 75(1)(*d*) is to ascertain whether the supplier, through no fault of its own, is unable to supply the Applicant with the product. Alternatively, the Applicant argues that the purpose of the supply management system as a whole is to ensure a match between supply and demand or, in other words, to ensure ample supply to meet consumer needs. The Applicant also relies on a statement made by Mr. Brodeur, who stated at the hearing that there is too much supply ("Il y a trop d'approvisionnement").

**271** The Respondents argue that the product is not in ample supply. It is argued that ample supply must be assessed not in relation to the Applicant's need, but rather in relation to what is available in the relevant market or from the supplier from whom an obligation to supply is sought. The focus must be on the suppliers' capacity to offer product in the relevant market. The Respondents contend that live chickens are not generally a product in ample supply because the supply management system regulating the chicken industry expressly limits the quantities that may be supplied by producers in a given period. In the Respondents' view, this is the primary reason chickens are not available in ample supply.

**272** Further, the Respondents argue that section 75 is not intended to apply to situations where a supplier's particular production capacity is limited, nor is it intended to oblige the Tribunal to arbitrate an agreement between customers who are seeking access to a limited supply of products. It is argued that the section provides for only one remedy, namely acceptance of the customer on usual trade terms. If the product were in ample supply, there would be no need for an order stipulating a volume or to allocate supply, since the suppliers in the market would have available capacity to meet the needs of the person who has been refused supply. Conversely, the Respondents maintain that if, in order to accomplish its purpose, an order should need to specify a volume to ensure supply to a

customer at the expense of another, the product then would not be in ample supply, and the conditions of section 75 would not have been met.

**273** Finally, the Respondents maintain that it does not matter whether the product is no longer available because it is reserved for an innocent third party, as in *Quinlan's*; or whether it is no longer available by reason of a business decision by the Respondent Westco to vertically integrate its operations. The supplier simply does not have "ample supply" of the product because there is no excess capacity available to meet the demand.

(3) **Analysis**

(a) Meaning of "ample supply"

**274** Defining "ample supply/quantité amplement suffisante" in the context of paragraph 75(1)(*d*) is essentially a question of legal interpretation. It is now accepted law that "the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act and the intention of Parliament" (see *Rizzo & Rizzo Shoes Ltd. (Re)*, *[1998] 1 S.C.R. 27*).

**275** The word "ample" is defined by both the *Canadian Oxford Dictionary* (2004) and *Webster's Encyclopedic Dictionary of the English Language* as plentiful, abundant, extensive and more than enough. *Le Petit Robert de la langue française* (2006) defines "amplement" as "abondamment" and "en allant au-delà du nécessaire". This is to be contrasted with the word "adequate" found in paragraph 75(1)(*a*), which is defined by the *Canadian Oxford Dictionary* as sufficient, satisfactory, and barely sufficient. The *Webster's Encyclopedic Dictionary of the English Language* defines "adequate" as equal to or sufficient for a special requirement.

**276** A different meaning of "supply" was therefore intended in each paragraph. In its grammatical and ordinary sense, ample therefore means more than a sufficient or adequate supply. It means supply available in abundance or to the point that it is considered to be excessive. Ample or abundant supply must then be considered in the context of the object and scheme of the Act, the object of the particular provision, and the intention of Parliament.

**277** The purpose of the Act is set out in section 1.1. It essentially provides that the purpose of the Act is to maintain and encourage competition in Canada. It includes, among other objectives, doing so in order to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy, and in order to provide consumers with competitive prices and product choices.

**278** In *Xerox*, the Tribunal had occasion to consider the constitutionality of section 75 of the Act. In finding the provision to be within Parliament's legislative authority and constitutionally valid, it commented on the purpose of the provision. At page 78 of its decision, the Tribunal wrote:

> Section 75 can certainly be characterized as ancillary to the main purpose of the legislative scheme as well as having an intimate connection thereto. The immediate effect of an order to supply is to open up channels of distribution and free competitive forces hindered by lack of access to supplies. The section's objective is to promote or preserve competition. Section 75 operates within the same regulatory parameters as do the other provisions of Part VI.

**279** We agree with the above characterization of the objective of the provision. The goal of promoting and maintaining competition is also reflected in the scheme of the Act. The scheme under section 75 of the Act provides for certain conditions which, when met, render a refusal to deal, an otherwise legal act, a reviewable practice. Two of these conditions make express reference to competition being affected. In paragraph 75(1)(*b*), it must be established that there is insufficient competition among suppliers in the market, and paragraph 75(1)(*e*) requires that it be shown that the refusal to deal is having or is likely to have an adverse effect on competition in the market. Therefore, a refusal's impact on competition is a central focus of the provision. Once it is established that competitive forces are hindered by the refusal or the lack of access to supplies, the Tribunal may, pursuant to section 75 of the Act, order that one or more suppliers of a product in a market accept the Applicant as a customer

on usual trade terms. As stated by the Tribunal in *Xerox*, the effect of the remedy under section 75 is to open up channels of distribution and free competitive forces hindered by lack of access to supplies.

**280** The term "ample supply" must be interpreted harmoniously with the above discussed purpose of the Act and scheme. Supply is not ample when suppliers generally would be inhibited from growing or even changing the nature of their business, or be forced to ration supplies between current and potential future customers because supply is limited. A product is in ample supply when its availability is not in issue when a supplier considers whether to develop its business by seeking new customers and/or new distribution channels, such as involvement in the downstream processing market.

**281** A remedy under section 75 would not be available in circumstances where a refusal to supply was caused by reason of a shortage of supply in general as a result of a strike, scarcity of raw materials, or by reason of an upstream supplier going out of business. In such circumstances, supply is constrained by reason of factors beyond anyone's control. As a consequence, a supplier is unable to meet demand in the market, by reason of supply being limited. It follows that the product is therefore not in ample supply. This view finds support in the 1974 transcripts of committee proceedings before the House of Commons when Bill C-7 (*An Act to amend the Combines Investigation Act and the Bank Act and to repeal an Act to amend an Act to amend the Combines Investigation Act and the Criminal Code*, 2nd Sess., 29th Parl.) was being debated. The issue being debated was a refusal where the product was in short supply. The following question was put to the minister responsible, followed by his response:

> **Mr. Frank**: Mr. Chairman, Mr. Minister, unfortunately I do not have the legal mind that most members of this committee apparently have and this disturbs me to some degree, to the effect that, when this bill gets passed, if it ever does, just what in actual fact may happen.
>
> To clarify one particular area, which, no doubt, you can adjust to suit other areas: in the fertilizer business back in the winter, there was some degree of concern at the lack of products for dealers to sell. As a specific example, a company that supplied dealers went out of business and the dealers that were supplied by them naturally could not have the product unless they were able to acquire it from other manufacturers.
>
> At that particular time, the other manufacturers felt that they wanted to protect their dealers and make sure that they were not shorting them. Consequently, they refused to sell to these dealers that had unfortunately found themselves ex-customers of this other company. Now, would this particular area here change that particular picture? In other words, would it make it necessary for these manufacturers to sell to dealers that they had not supplied before?
>
> **Mr. Gray**: No, because in the situation you have outlined it would appear that the product in question was not in ample supply, and in order for the Commission to make an order requiring a supplier to supply somebody, it would have to find that the product was in ample supply.
>
> (Canada, House of Commons, *Minutes of Proceedings and Evidence of the Standing Committee on Finance, Trade and Economic Affairs*, 29th Parl. 2nd Sess., No. 9 (April 30, 1974) at 9:34)

**282** Bill C-7 died on the order paper, but the provision at issue was eventually brought back under a different bill. The above exchange is therefore relevant and would appear to support an intention by the minister to have the provision apply only where there is evidence of ample supply of the product in the market. What is also suggested is that in cases where product is in short supply, a supplier would not be required to ration limited supplies of a product in a manner that prevents existing customers from obtaining the quantities they wish to purchase.

**283** The above factors support a definition of "ample supply" consistent with that articulated by the Tribunal in *Quinlan's*. The words "ample supply", read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act and the intention of Parliament, are meant to deal with situations in which the product is in ample supply, in the sense that suppliers are not obliged to choose between serving new customers and continuing to supply historic quantities to existing customers.

(b) Are "live chickens" a product in ample supply in the circumstances of this case?

**284** As can be observed from the above review of the supply management system for live chickens in Canada, the system as structured does provide for adjustments in the total supply of live chickens. This adjustment is fixed at each production period through a complex adjustment mechanism designed to strike a balance between chicken production and consumer demand. Essentially quotas are adjusted by the CFC when consumer demand for chicken increases or decreases. This is measured by what industry participants refer to as a "bottom-up" process which starts when processors gauge changes in consumer demand for chicken. According to Mr. Brodeur, any increase in demand translates into a corresponding increase in what is known as the "meat margin". The "meat margin" measures the difference between the minimum board prices for live chickens set by the provincial marketing board and the aggregate of the prices paid for processed chickens at both the primary and secondary stages of transformation. These prices are not regulated and are set by market forces. Therefore, when the prices for processed chickens either rise or fall, the "meat margin" increases or decreases. This reflects an increase or decrease in consumer demand. It is when the "meat margin" exceeds historic levels that the CFC is led to conclude that supply and demand for chickens in Canada is not in equilibrium, and as a result there is a need to increase production quotas in order to satisfy increased consumer demand. The evidence indicates that, historically, such an adjustment has served to reduce prices at both the wholesale and retail levels. The converse is also true. When the "meat margin" is below historic levels, quotas may be reduced. As seen above, such adjustments in quotas, if any, can only occur at the end of an eight-week production period.

**285** We are satisfied that the above review of the supply management system in Canada as it relates to chickens properly reflects the system under which the parties to this application are operating and were operating at the time of the filing of the application. It is a system that does not allow for an immediate or timely response to changes in market conditions as would be the case in an unregulated market.

**286** The system in place provides for supply to be adjusted at the "macro" level. Quotas may be increased nationally and even on a provincial level as a result of increased consumer demand. However, under the system, there is no assurance that a particular supplier who wishes to increase production can obtain the increased quota that it needs to meet its business plan. Indeed the evidence of Mr. Feenstra indicates that adjustments in the system are made across the system and that an increased quota over a previous period is divided up on a pro-rata basis between each existing producer. That is of little assistance to individual producers who wish to accommodate additional customers.

**287** Under the system, aggregate supply is maintained at adequate levels to meet consumer demand. The level of supply is essentially fixed for any given period. Increases in quotas are made only after the market data is computed and assessed at various levels of administration in the system for a given period. When quotas are adjusted, they are adjusted on an aggregate basis and distributed on a pro-rata basis among existing producers. This takes time, and in the meantime, a producer is unable to increase production to meet increased demand. A producer can only supply more if it acquires production quotas from another producer, and processors can only increase capacity and grow in the market by obtaining additional supply by accessing supply that is destined for another processor, since total supply is limited by the system.

**288** As can be seen from the above review of the supply management system, the main focus has been to ensure stability and a reasonable rate of return for producers and an adequate supply for consumers. Indeed, on the latter point, the Marketing Plan issued under Order I of the Chicken Farmers of New Brunswick (see Schedule C) uses such language. The plan provides that one of its objects is to ensure that there is "adequate supply of New Brunswick grown chicken available to the consumer". Under the supply system as discussed above, the product cannot be said to be in ample supply, in the sense that it is available on a timely basis to individuals wishing to expand or develop their businesses. This is a consequence, in particular, of the time lag required for an adjustment in aggregate supply and of the apportioning of any adjustment among all suppliers.

**289** In accordance with the definition of "ample supply" set out earlier in these reasons, and in the circumstances of this case, its follows that the product, live chickens, cannot be said to be in ample supply as that term is understood for the purposes of paragraph 75(1)(*d*) of the Act.

**290** The Applicant further argues that "(s)ubsection 75(1)(d) cannot be interpreted so as to permit the malefactors to profit from their own misconduct". The Applicant maintains that the Respondents "embarked on a deliberate and conspiratorial course of conduct, as far back as August 2006, whose sole purpose and object was to attempt to force an improvident sale of the Nadeau Plant". In support of its argument, the Applicant relies on evidence adduced by different witnesses which indicates that the Respondents were strategizing to acquire the St-François Plant at below market value by threatening to cut off supply to the Applicant if it was not prepared to sell. A number of e-mails and other correspondence were adduced in evidence, including exchanges between the Respondents and their respective officials that support elements of the Applicant's allegation.

**291** As stated earlier, the Respondents argue that the prime reason that motivated their decision to refuse supply to the Applicant is their decision to have their birds processed by Sunnymel. This would allow for continued vertical integration of Westco's enterprise. In essence, the Respondents say that it was no more than a business decision.

**292** We are of the view that we need not decide whether the Respondents' conduct, which led to its decision to terminate supply to the Applicant, is misconduct, as alleged by the Applicant, or tough negotiations motivated by a business decision, as argued by the Respondents. In our view a determination is not necessary in the circumstances because of our above finding that there is not "ample supply" of chickens in the market. In the context of a section 75 application, for a remedy to be available, all the requirements in subsection 75(1) must be met.

**293** We now turn to the final requirement under subsection 75(1) and consider whether the refusal is having or is likely to have an adverse effect on competition in a market.

### F. Has the Applicant established that the refusal to deal is having or is likely to have an adverse effect on competition in a market pursuant to paragraph 75(1)(*e*) of the Act?

**294** Under paragraph 75(1)(*e*), the market of concern is different from the market defined for the purposes of paragraph 75(1)(*a*). Our analysis will involve the "downstream market". We will begin by defining this market, which includes defining the relevant product market and the relevant geographic market.

#### (1) Relevant product market

**295** Neither party disputes that the product market includes processed chicken. The only question is whether "further processed chicken" and "air-chilled chicken" constitute separate and distinct product markets. The parties adopt different approaches to this question.

**296** In its Pleadings, the Applicant states that the refusal to deal is likely to have an adverse effect on competition "at various levels of the market for chicken". The Applicant's final submissions also refer to "sub-markets". Dr. Ware refers to both the market for "processed chicken" and the "market for further processed chicken" in his reports. In his examination in chief, Dr. Ware stated that there can be subcategories within the broad category of processed chicken such as air-chilled chicken, but said that he "didn't have even close to adequate data" that would allow him to make that identification. He also stated, however, that the market for further processing of chicken constituted another product market in this case.

**297** The Respondents assert that the relevant product market is processed chicken. Ms. Sanderson's report also refers to "processed chicken". In cross-examination, when asked whether air-chilled products are different from water-chilled products, Ms. Sanderson stated the following:

> They may be different products, but they may be part of the same relevant product market. So for example, because this happens with differentiated products, it may be the case that you're unable to increase the price of an air-chill product by a substantial amount, because if you were to do that, customers will

> substitute to water-chill products. If there's sufficient substitution possibilities between those products at a market level, then they might be part of the same relevant product market even though they're distinguished from each other.

**298** With regards to air-chilled chicken and water-chilled chicken, we acknowledge, as did Dr. Ware, that they may well be "subcategories for processed chicken". However, there is insufficient evidence on the record to support a conclusion that they are separate product markets.

**299** We come to the same conclusion with respect to further processed chickens. There is a paucity of evidence on this issue. Counsel for the Applicant acknowledged that stakeholders do not always agree on the definition of "further processing". This disagreement may lie in the fact that there are different types of further processing operations such as boning, cutting, and cooking. Mr. Donahue referred to different "grades of further processing" and responded as follows in cross-examination when asked about the Applicant's processing operations: **[CONFIDENTIAL]**

**300** Dr. Ware described the product market for further processed chicken as "basically anything that happens to the chicken after it's been killed and possibly cut up". However, without further evidence, we are unable to conclude on the record before us that further processed chicken constitutes a separate product market.

**301** We therefore find that the product market for the purpose of paragraph 75(1)(*e*) is processed chicken. We agree that further processed chicken forms part of the same relevant product market in the circumstances.

### (2) Relevant geographic market

**302** The parties disagree on the definition of the relevant geographic market. The dispute turns on whether Ontario or parts of Ontario should be included in the geographic market.

#### (a) Positions of the parties

**303** In its Pleadings, the Applicant submits that the relevant geographic market for the purposes of paragraph 75(1)(*e*) is Quebec and the Maritimes. In its submissions, however, the Applicant takes the position that provincial boundaries are artificial boundaries and distances itself from a formal definition of the geographic market. When asked about the Applicant's submissions concerning the relevant geographic market, counsel for the Applicant stated:

> All right. In my argument I don't look at geographic. I think if you remember Dr. Ware said, he said provincial boundaries are somewhat artificial lines that are drawn and they may not be relevant for the purpose of the market analysis. Because the real question is, is what is the market that's affected?
>
> ...
>
> My point though is that in trying to draw --I submit that it's somewhat artificial to use geography as the defining characteristics of the behaviour of a market where the element that is concern is the impact, wherever it may fall, of the particular behaviour. We have to look at the impact of the behaviour wherever it may fall, and if it falls within three miles of Toronto, fine, but if it falls 1,000 miles away it's still relevant for the purpose of the 75(1)(e) analysis.

**304** Dr. Ware did express the view that relevant markets need not necessarily coincide with provincial borders. Using provincial boundaries, however, he found that the "best definition" of the geographic market is one that consists of Quebec, New Brunswick, Nova Scotia and Prince Edward Island.

**305** The Respondents are of the view that the relevant geographic market is the region comprising Ontario,

Quebec and the Maritimes.

(b) Analysis

**306** Dr. Ware is of the opinion that the hypothetical monopolist test should be used to define the relevant geographic market, but expresses the view that the data are insufficient to determine the precise boundaries of the market pursuant to such a test:

> My conclusion was, and is, that the geographic market for processed chicken is likely -- well, let me put it this way, well described by the boundary of Quebec, New Brunswick and the maritime provinces, not including Newfoundland, but it's certainly smaller than the boundary of those same provinces and the Province of Ontario. That's my conclusion. The reason -- so my reasoning that I have used in reaching this conclusion is indirect. It's indirect because, as I said, I don't have the ability -- I mean, what I need to do to make a formal precise conclusion of that kind is I need to -- I need to actually estimate the ability of a hypothetical monopolist who controlled the supply within Quebec, New Brunswick and the other maritime provinces too if they were to act as one to increase the price. That would give me the answer. That would give me a precise answer, but I don't have the ability to do that. I need a lot of data on demand elasticities and supply, behaviour of all the relevant producers. I don't have that information, but I do have indirect information and there are various indirect indicators that one can use to assess whether or not the geographic market is, in a sense, broad or relatively narrow. And, again, I do stress that because this is both a spatially and a product differentiated market, that geographic market definition is going to be a rather fuzzy sort of concept because if you have -- you know, clearly these producers are separated by space. We're talking about a lot of territory here.

**307** Instead, Dr. Ware therefore relies on indirect indicators, namely (1) the predicted effect of a hypothetical Nadeau/Olymel merger on the price of Nadeau's products; (2) concerns expressed by Nadeau's customers regarding its possible exit from the market; (3) the apparent clustering of processors; (4) transportation costs; (5) price relationships between different geographic areas as described in the *Merger Enforcement Guidelines*; and (6) the regulatory limitation of the aggregate supply of chickens available to the market.

**308** Ms. Sanderson is not explicit about the test she uses to define the geographic market. The evidence on which she relies includes (1) Nadeau's and Olymel's historic shipping patterns; (2) shipping distances; (3) transportation costs; and (4) price comparisons.

**309** While the usual approach to market definition under paragraph 75(1)(*a*) is based on the ability of the applicant to substitute in favour of alternative service or material inputs without being substantially affected, the Tribunal clarified in *B-Filer*, as mentioned earlier in these reasons, that the approach need not be the same under paragraph 75(1)(*e*):

> [78] In our view, while the addition of paragraph 75(l)(*e*) changes the context and purpose of section 75 to the extent that there is now a focus on determining whether refusals to deal result in adverse effects on competition, this amendment does not change the ultimate concern of 75(l)(*a*). That concern, as stated in *Chrysler*, is the effect on the business of the person refused supply. Since the market of concern under 75(l)(*e*) need not be the market of concern in paragraphs 75(l)(*a*) and 75(l)(*b*), the market that best suits the particular context and purpose of 75(l)(*e*) can be separately considered when considering that paragraph of the Act.

**310** Therefore, the conventional hypothetical monopolist approach to market definition which, in essence, relies on the practical indicia suggested in the *Merger Enforcement Guidelines*, can be used under paragraph 75(1)(*e*).

**311** Both the Applicant and the Respondents ultimately make use of the practical indicia suggested in the *Merger Enforcement Guidelines* and commonly used in connection with geographic market definition in merger cases to

support their proposed market definitions. Practical indicia include transportation costs, price relationships, shipping patterns and trade views.

**312** Our approach to determining the relevant geographic market will involve considering the above-mentioned practical indicia as well as the following indicators suggested by Dr. Ware: (1) the predicted effect of a hypothetical Nadeau/Olymel merger on the price of the Applicant's products; (2) concerns expressed by the Applicant's customers regarding the Applicant's possible exit from the market; (3) the apparent clustering of processors; and (4) the regulatory limitation of the aggregate supply of chickens available to the market. We will consider each of these indicators in turn.

(i) The predicted effect of a hypothetical Nadeau/Olymel merger

**313** Dr. Ware is of the opinion that an Olymel/Nadeau merger would result in an increase of approximately **[CONFIDENTIAL]**% in the price of processed chicken. **[CONFIDENTIAL].** On the assumption that the geographic market would consist of Ontario, Quebec and the Maritimes, Nadeau would hold a 7% market share in such a market. Dr. Ware reasons that a "7% market share" is not sufficient to produce a price increase of nearly 2% and concludes that these data point to a narrower geographic market.

**314** Ms. Sanderson notes that the **[CONFIDENTIAL]**. She adds that Dr. Ware did not question the Nadeau management team's belief or provide any analysis to support the **[CONFIDENTIAL]**% price increase upon which he founded his opinion. She also notes that Olymel's managers, "who are in a more informed position to assess Olymel's ability to raise prices to Olymel customers should the Partnership acquire the St. François facility", did "not identify price increases as part of their internal valuation of the acquisition".

**315** We note that the Projet Westco Report indicates that **[CONFIDENTIAL]**. While this may represent Olymel's view, this does not necessarily imply either higher prices in general or a **[CONFIDENTIAL]**% price increase in particular.

**316** We are also of the view that Dr. Ware's opinion regarding the effect of a hypothetical merger on the price of processed chicken is of little assistance in determining the geographic market. Dr. Ware's market share analysis is incomplete in its own terms in that it does not appear to take into account the combined market share of the merging parties. Further, apart from the belief of the Applicant's management team reflected in the Robinson Report, there is simply no explanation to support the conclusion that the merger would result in a **[CONFIDENTIAL]**% price increase.

(ii) Concerns expressed by the Applicant's customers

**317** As a second indicator, Dr. Ware cites the concerns of some of the Applicant's customers that prices would increase and service would deteriorate if the Applicant were to cease to be a competitor. He points, for example, to a letter written by Ms. Goodz, the president of Riverview, who wrote that "[i]f the Nadeau plant were to shut down, or even if it were to be acquired by a competitor, I would definitely foresee that prices would definitely rise, and supply problems would occur". Dr. Ware is of the opinion that these customers would not be concerned if the geographic market were broader, that is, if it included Ontario processors; the fact that these customers expect prices to rise and supplies to be restricted indicates that the geographic market is significantly smaller.

**318** In her report, Ms. Sanderson closely examines each of the letters cited by Dr. Ware and notes that in many cases, alternative sources of supply exist.

**319** Complaints by customers will be dealt with more comprehensively later in these reasons when we consider the adverse effect on competition. In the absence of further corroborating evidence to support complaining customers' concerns about price increases and supply shortages, very little can be concluded in terms of their impact on geographic market definition.

**320** First, as pointed out by Ms. Sanderson, many of the complaining customers did not investigate alternative sources of supply in the event the Applicant is unable to continue supplying chickens. This was the case of the general manager of UPGC, also Priszm's chief purchasing officer, who admitted in cross-examination that he had not sought out other sources of supply.

**321** Second, there is no evidence to establish the relative importance of these complaints in respect to the geographic definition of the market. For instance, Puddy, one of the largest complaining customers, is located in the Greater Toronto Area and is closer to Ontario processors and Quebec processors than it is to the Applicant. Consequently, Puddy's complaint does not point to a narrower geographic market.

**322** On the evidence, it is difficult to assess the relative importance of customers' complaints and concerns. Many of the complaints are not based on the geographic proximity of competing suppliers. For these reasons we find this indicator to be of little utility in determining the geographic market and consequently conclude that no inference can be drawn for defining the geographic market.

(iii) The apparent clustering of processors

**323** Also regarded as being instructive by Dr. Ware is a map of Eastern Canada (Figure 1 in his Expert Report) that appears to show that there is a cluster of processors around the Toronto area. Dr. Ware testified that :

> ...there are two distinct clusters of poultry processing plants in Eastern Canada.
>
> Given the significance of transportation costs, the cluster of processing plants west of Toronto are unlikely to be part of the same market as those in Quebec, New Brunswick and Nova Scotia (the plant in Newfoundland is supplied by, and supplies to, only Newfoundland).

**324** While admitting that this was not a "super scientific approach", he stated that these clusters illustrate "a kind of density of economic activity that they are more likely - the ones close together - are more likely to be in the same geographic area than the ones that are further away".

**325** While Dr. Ware's definition of clustering is somewhat vague, we accept the general proposition that plants that are close together are more likely to be in the same geographic market than plants that are further away from each other. There are, however, many factors (such as the availability of the requisite inputs) that bear on the location of plants. Whether plants in different locations are in the same geographic market depends on the characteristics of the product concerned, in particular, the distance over which it can be shipped economically. Looking at plant locations is simply the starting point of the analysis required to determine the boundaries of the geographic market. In the circumstances, this indicator is of little assistance in defining the geographic market.

(iv) Regulatory limitations

**326** At paragraph 23 of his first report, Dr. Ware also suggests that another reason why geographic markets for processed chicken are smaller than might be expected from their basic manufacturing characteristics is because the supply elasticities for live chickens are kept low by supply management policies. If the price of processed chicken rises in one area, potential importers will have to bid chicken away from consumers in other areas.

**327** Ms. Sanderson responds that the inelasticity of the supply of live chickens is common throughout Canada and that there is no reason to believe that it is possible to distinguish Quebec and the Maritimes from Ontario or the rest of Canada on this basis.

**328** It is true that under the marketing board regime, additional chickens can be shipped to one geographic area only by diverting them from another, but this is also true within individual provinces. We therefore agree with Ms.

Sanderson that there is no reason to distinguish Quebec and the Maritimes from Ontario on this basis.

(v) Transportation costs

**329** In his first report, Dr. Ware relies on the Projet Westco Report to conclude that the Applicant's transportation cost for processed chicken is $**[CONFIDENTIAL]**/kg. In her expert report, Ms. Sanderson states that if the transportation cost is $**[CONFIDENTIAL]**/kg, it is less than **[CONFIDENTIAL]**% of the average price of processed chicken; she therefore notes that large shipments of processed chicken can be made over substantial distances because of low transportation costs. In this regard, she testified that the analysis should focus on the cost to ship processed chicken relative to the price, rather than the cost of processed chicken.

**330** At paragraph 20 of his reply report, Dr. Ware points to data on sales for quota period A-76 to conclude that the average transportation cost as a proportion of the sale price is not **[CONFIDENTIAL]**%, but rather **[CONFIDENTIAL]**%. Prior to the hearing, Westco objected to paragraph 20 and other paragraphs of Dr. Ware's reply report on the basis that it failed to constitute a proper reply to Ms. Sanderson's report. In an order dated November 7, 2008, the Tribunal held that the evidence would be admitted; Westco was granted the latitude to address this issue at the hearing (see *Nadeau Poultry Farm Limited v. Groupe Westco Inc. et al.,* 2008 Comp. Trib. 31).

**331** Dr. Ware testified that transportation costs matter because customers say they matter and because the figure of **[CONFIDENTIAL]**% is significant. He failed, however, to explain the significance of **[CONFIDENTIAL]**% or to point to any customer who stated that transportation costs matter *per se*.

**332** In her examination in chief, Ms. Sanderson testified that the figure of **[CONFIDENTIAL]**% is incorrect, as it is the result of an error in the sales data on which Dr. Ware relied. She found that transportation costs for Nadeau averaged **[CONFIDENTIAL]**% of its sales revenue of 2007. Ms. Sanderson testified that it is significant that transportation costs are less than 5% of the price of the product because this would allow competitors to undercut a 5% price increase by a hypothetical monopolist.

**333** We agree with Ms. Sanderson that Nadeau's average transportation cost was **[CONFIDENTIAL]**% of the average price of its products in 2007. As an average, however, it does not tell us what the fixed component (loading and unloading) of transportation costs is and how the variable component of transportation costs increases with distance. As a consequence, it does not speak conclusively to the boundaries of the geographic market. Nevertheless, Nadeau's average transportation cost does reflect the cost of relatively large shipments in excess of 1,000 km because we know that one of the Applicant's largest customers, **[CONFIDENTIAL]**, is located in Mississauga, Ontario. The evidence that the Applicant's transportation costs for processed chicken averaged **[CONFIDENTIAL]**% of the price of its products certainly implies that transportation costs are not prohibitive even over significant distances. It could also imply that transportation costs would not prevent an Ontario processor from undercutting a 5% price increase by a New Brunswick or Quebec producer and vice versa. The stated 5% price increase refers to the hypothetical monopolist test as articulated in the *Merger Enforcement Guidelines*[2].

(vi) Price comparisons

**334** The expert economists make a variety of price comparisons, none of which are entirely satisfactory.

**335** At paragraph 21 of his initial report, Dr. Ware refers to paragraph 3.25 of the *Merger Enforcement Guidelines*, which states that "[e]vidence that prices in a distant area have historically either exceeded or have been lower than prices in the candidate geographic market by more than transportation costs may indicate that the two areas are in separate relevant markets, for reasons that go beyond transportation costs". He then compares retail prices for various cuts of processed chicken in Ontario, Quebec and New Brunswick because wholesale price data are sparse. Dr. Ware finds that retail prices of processed chicken are higher in New Brunswick than in Ontario and assumes that this implies that wholesale prices are also higher.

**336** In her report, Ms. Sanderson notes that a review of the retail price data for the products set out in Dr. Ware's report shows that the average retail price for those products is $**[CONFIDENTIAL]** in Ontario, $**[CONFIDENTIAL]** in Quebec, and $**[CONFIDENTIAL]** in New Brunswick, making average prices 17% lower in Ontario and 20% lower in Quebec than in New Brunswick. At first glance, this would mean that Quebec is not in the same market as New Brunswick and that therefore Quebec-based Olymel does not compete with the Applicant. Ms. Sanderson finds that such a conclusion is nonsensical and that conclusions of this type cannot be drawn from retail price comparisons. **[CONFIDENTIAL]**.

**337** In his reply report, Dr. Ware uses another source of data to construct average wholesale prices for the Applicant's sales by province. Dr. Ware conducts an analysis of Nadeau's 2007 sales and finds that when the analysis is confined to products sold in all three provinces, the weighted average wholesale price was $**[CONFIDENTIAL]** in Ontario, $**[CONFIDENTIAL]** in Quebec and $**[CONFIDENTIAL]** in New Brunswick. **[CONFIDENTIAL]**.

**338** At the hearing, Ms. Sanderson produced a price comparison of the average Ontario, Quebec and New Brunswick prices of the Applicant's five biggest-selling products in Ontario. Ms. Sanderson testified that these top five products represent **[CONFIDENTIAL]**% of the Applicant's sales in Ontario. Her bar graph is reproduced as Table 1 below.

Table 1

**[CONFIDENTIAL]**

**339** Ms. Sanderson stated that this comparison shows that the prices are basically the same. **[CONFIDENTIAL]**.

**340** During her cross-examination, Ms. Sanderson agreed that **[CONFIDENTIAL]** of the **[CONFIDENTIAL]** products sold in all three provinces were priced higher in New Brunswick than in Ontario. Further, **[CONFIDENTIAL]** of the **[CONFIDENTIAL]** products were priced higher in New Brunswick than in both Quebec and Ontario. Ms. Sanderson stated that this was consistent with the weighted average price being **[CONFIDENTIAL]** in New Brunswick than in Ontario.

**341** Both experts agreed that a comparison of the Applicant's weighted average wholesale prices of products sold in all three provinces, Ontario, Quebec and New Brunswick, in 2007 was the most informative. As mentioned above, the comparison was confined to **[CONFIDENTIAL]** products sold in all three provinces. The results were as follows: Ontario, $**[CONFIDENTIAL]**/kg; Quebec, $**[CONFIDENTIAL]**/kg; and New Brunswick, $**[CONFIDENTIAL]**/kg. The Applicant's weighted average price in Ontario was **[CONFIDENTIAL]** and its price in Quebec **[CONFIDENTIAL]** than in New Brunswick during 2007.

**342** The extent to which the observed differences in the weighted average prices are due to differences in the mix of products sold in each province and to the average size of the customers in each province is unclear. The same is true of the extent to which these averages might vary from year to year. The above data support the contention that differences amongst the three provinces are relatively small. There is no expert evidence on price differentials that would allow for any inference to be drawn with respect to the relationship between prices in Prince Edward Island and Nova Scotia and the remainder of the market.

**343** With respect to the differences between New Brunswick and Quebec prices, the Applicant has already defined New Brunswick and Quebec as being in the same geographic market. The observation of price differences between New Brunswick and Quebec merely serves to emphasize that there is a certain amount of underlying price variability within a geographic market.

(vii) Shipping Patterns

**344** In Ms. Sanderson's view, processed chicken can be shipped economically for considerable distances. She notes that the Applicant's revenues from sales in Ontario account for **[CONFIDENTIAL]**% of the Applicant's sales revenues whereas the Applicant's revenues from sales in New Brunswick and Nova Scotia account for **[CONFIDENTIAL]**% and **[CONFIDENTIAL]**% respectively of the Applicant's sales revenue. She states that the Applicant's furthest Ontario customer is located **[CONFIDENTIAL]** km from the St-François Plant. Relying on the Applicant's customer data for quota period **[CONFIDENTIAL]**, she concluded that the Applicant makes frequent and large shipments of processed chicken every day to very distant customers, including customers based in Ontario. In her opinion, the fact that the Applicant can profitably ship processed chicken to Ontario is clear evidence that Quebec and Ontario processors can profitably ship to customers located in New Brunswick and Nova Scotia.

**345** Ms. Sanderson also finds that the Applicant's customers based in Quebec and Ontario have access to alternative nearby processors and that in many instances, the closest processing facility is not the Applicant's plant.

**346** She adds that Olymel makes **[CONFIDENTIAL]**% of its sales in Ontario and that over **[CONFIDENTIAL]**% of those sales are made to customers located in the Greater Toronto Area. Ms. Sanderson concludes that, given that Olymel can profitably ship processed chicken 475 km to Toronto, Ontario processors could profitably ship their products the same distance in the other direction:

> ... it is self-evident that Ontario-based processors in the GTA can also profitably ship product to Montreal and throughout Quebec, which they do. Consequently, the prices that Olymel charges to its Quebec customers are influenced by competition from Ontario processors and as a result, Nadeau's prices to its Quebec customers are also influenced by Ontario processors given the competition that exists between Nadeau and Olymel for sales in Quebec.

**347** In cross-examination, Ms. Sanderson conceded that she had no direct evidence of Ontario processors' shipping their products to customers in New Brunswick. She also agreed that Olymel does not have significant sales in New Brunswick. In her report, Ms. Sanderson stated that Olymel makes more sales to customers in the western provinces than it does to customers in the Maritimes.

**348** We find the fact that Olymel sells only a small amount of processed chicken in New Brunswick does not support the position that Ontario is not part of the relevant market. Dr. Ware has defined the relevant market to include both New Brunswick and Quebec so that the lack of sales by Olymel (a Quebec-based processor) in New Brunswick merely emphasizes that a producer in a relevant geographic market need not have sales in every part of it at all times.

**349** It is not disputed that the Applicant ships processed chicken to Quebec and Ontario and that Olymel also does so. There is some evidence that processed chicken is shipped from Ontario to Quebec and the Maritimes. Mr. McHaffie testified that Ontario-based Puddy delivers to **[CONFIDENTIAL]**.

**350** The Brodeur affidavit states that Olymel buys 210,000 birds per week from other primary processors but that the great majority of these purchases are from Exceldor. Mr. Brodeur states that Olymel has purchased chicken for further processing from Ontario processors such as Maple Leaf and from the United States. Ms. Goodz testified that **[CONFIDENTIAL]**.

**351** Mr. Brodeur testified that McDonald's chicken nuggets are all made in Ontario and that Costco in Ontario is supplied by Exceldor.

**352** Based on the above evidence, we find that processed chicken can be and is shipped profitably for fairly long distances, over 1,000 km in one major instance. A considerable fraction of Nadeau's and Olymel's sales are in Ontario's Toronto area. Olymel ships some processed chicken products further still. While there is no reason to believe that processed chicken could not be shipped equivalent distances to customers east of Ontario, there is

less evidence of such shipments.

(viii) Trade views

**353** In her expert report, Ms. Sanderson relies on the Serecon Report to the effect that Nova Scotia must compete in a national chicken market despite being located in a high-cost region. The Serecon Report refers to the fact that current production in Nova Scotia exceeds consumption within the province and that this is why "NS chicken has to compete with production from outside the region not only in NS but also in Quebec and Ontario".

**354** In cross-examination, Mr. Feenstra agreed that the Applicant competes with Ontario and Quebec processors for its business in the Greater Toronto Area and that it competes with Ontario processors that want to sell into Quebec for the Quebec business. During his examination for discovery, he stated that "[p]rocessed product travels across the country back and forth all the time".

**355** A number of witnesses testified that they consider Ontario and Quebec to be in the same market. Mr. McHaffie stated that "Ontario processors can sell into Quebec at their whim and Quebec processors can sell here at their whim". Mr. Brodeur expressed the view that Quebec and Ontario constitute a single market. Mr. Ellis stated that Sunchef competes with processors in Ontario and Quebec.

(ix) Analysis and conclusion

**356** It is not disputed that Quebec and Ontario are in the same geographic market. Counsel for the Applicant conceded this:

> We have not suggested that Ontario and Quebec are not in the same market with each other. There's no question that there's competition between Ontario and Quebec. And you heard Mr. Lefebvre talk about a central Canada market. That's right through the evidence, not just of our witnesses but of all of them. Ontario and Quebec compete with each other.
>
> The issue, in my respectful submission, for this Tribunal is not that at all, not this issue, but rather the issue as to whether there is competition between Ontario and New Brunswick, because the question was whether the scope of the geographic market -- we, as I told you at the outset, accept that it's New Brunswick and Quebec. The question is does it extend as far as Ontario?

**357** As mentioned above, Dr. Ware finds that the relevant geographic market consists of Quebec, New Brunswick, Nova Scotia and Prince Edward Island. Ms. Sanderson is of the opinion that the relevant market consists of Ontario, Quebec and the Maritimes. The experts thus agree that New Brunswick and Quebec are in the same market. Further, the Applicant concedes that Quebec and Ontario are in the same market. If Ontario and the Maritimes are both in the same market as Quebec, it is difficult to escape the conclusion that they are in the same market as each other. The implication is that Ontario, Quebec, New Brunswick, Nova Scotia and Prince Edward Island are part of the same geographic market.

**358** Put another way, Quebec processors compete with Ontario-based processors as well as with New Brunswick and Nova Scotia-based processors. Quebec processors discipline and are disciplined by both Ontario and Maritime-based processors.

**359** Put yet another way, according to the Applicant's argument, even if Nadeau were to disappear, Olymel would continue to be disciplined by competition from Ontario processors as well as from Exceldor and ACA on the **[CONFIDENTIAL]**% of its sales that are in Quebec and Ontario. There is nothing on the record to indicate that this competitive discipline would not apply to any sales that Olymel or any other competitor might make to customers located in New Brunswick in the event that Nadeau disappears.

**360** In our view, the evidence relating to both the practical indicia suggested in the *Merger Enforcement*

*Guidelines*, including transportation costs, price relationships, shipping patterns and trade views, and the indicators relied on by Dr. Ware support the argument that the Ontario processors should be included in the relevant geographic market. The relevant geographic market is therefore defined to include processors in New Brunswick, Nova Scotia, Prince Edward Island, Quebec and Ontario.

**361** Having defined the relevant product and geographic market for the purposes of paragraph 75(1)(*e*), we now turn to the requirement that the refusal to deal is having or is likely to have an adverse effect on competition in a market.

### (3) Adverse effect on competition in a market

#### (a) Meaning of adverse effect on competition

**362** We first consider what is meant by "an adverse effect on competition in a market". We begin with the position advanced by the parties.

**363** The Applicant submits that by deliberately omitting the word "substantial" and using the word "adverse", "Parliament must be taken to have accepted that a remedy should be granted at the suit of a private litigant on a showing of *any* non-trivial adverse effect on *any* market" (emphasis in original).

**364** The Respondent Westco submits that adverse effect, while a lower threshold than substantial effect, must still incorporate a notion of market power or dominant market position; it cannot just be a trivial reduction in competition. Westco contends that the test established in *B-Filer* does not admit a finding of adverse effect on competition if only one competitor is affected and notes that protecting competition cannot be reduced to protecting competitors or a select handful of them.

**365** In *B-Filer,* beginning at paragraph 195, the Tribunal had occasion to consider the final element of subsection 75(1) of the Act. It conducted a comprehensive review of the case law in interpreting the phrase "competition in a market". It was guided by prior decisions that dealt with how paragraph 79(1)(*c*) of the abuse of dominance provision of the Act had been interpreted. The Tribunal in *B-Filer* agreed that paragraph 75(1)(*e*) demands a relative and comparative assessment of the market in two time frames, namely with the refusal to deal and without the refusal to deal. It concluded as follows at paragraph 200 of its decision:

> Thus, we conclude that paragraph 75(1)(*e*) of the Act similarly requires an assessment of the competitiveness or likely competitiveness of a market with, and without, the refusal to deal.

**366** The Tribunal went on to consider what is meant by "competitiveness". It considered the case law on the issue under the abuse and merger provisions of the Act. The Tribunal noted that adverse effects in a market are generally likely to manifest themselves in the form of an increase in price, the preservation of a price that would otherwise have been lower, a decrease in the quality of products sold in the market or a decrease in the variety of products made available to buyers. The Tribunal noted that these and other competitive factors can only be adversely affected by the exercise of market power. The Tribunal applied this reasoning to the refusal to deal provision and concluded:

> Consequently, in our view, for a refusal to deal to have an adverse effect on a market, the remaining market participants must be placed in a position, as result of the refusal, of created, enhanced or preserved market power.

**367** The Tribunal then distinguished between the term "substantial" found in other provisions of the Act and the term "adverse" used in section 75. It found that the difference lies in the degree of the effect and that "adverse", according to its plain meaning, is a lower threshold than "substantial".

**368** Regarding the requirement that the refusal to deal "is likely to have" such adverse effect, based on earlier case

law, the Tribunal found the requirement to establish the likelihood of an adverse effect requires proof that such an event is "probable" and not merely possible.

**369** We agree with and adopt the approach articulated in *B-Filer*, above, regarding the meaning of adverse effect on a market. Consequently, our analysis under paragraph 75(1)(*e*) will require consideration of whether the refusal creates, enhances or preserves the market power of the remaining market participants. In *Canada (Director of Investigation and Research) v. NutraSweet Co.* *(1990), 32 C.P.R. (3d) 1*, the Tribunal noted that "[m]arket power is generally accepted to mean an ability to set prices above competitive levels for a considerable period". In that case, the Tribunal recognized that this valid conceptual approach is not one that can be readily applied. It held that the factors that need be considered in evaluating market power will vary from case to case but ordinarily include indicators such as market share and entry barriers. As indicated above in *B-Filer*, the impact on indicators such as price, quality and variety of the product must also be considered in assessing adverse effect. It is also understood that without market power there can be no adverse effect in a market. Our analysis under paragraph 75(1)(*e*) will therefore lead us to consider the following indicators in the circumstances of this case:

1. Market share and market concentration;
2. Barriers to entry;
3. Impact on prices;
4. The effect of the refusal on rivals' costs;
5. Impact on quality and variety of the product;
6. Possible foreclosure of supply to other processors in the market; and
7. Impact of possible elimination of an efficient processor.

**370** Before proceeding to our analysis of the above indicators, it is useful to first set out the respective positions of the parties on adverse effect under paragraph 75(1)(*e*) of the Act.

(b) Positions of the parties on "adverse effect on competition"

**371** The Applicant submits that the evidence adduced establishes the likelihood of many scenarios involving adverse effects on competition in various markets and sub-markets. In its written submissions, the Applicant states that these adverse effects include the following:

(a) the adverse effect on competition entailed by the increase in "live price" caused by a "premium war";

(b) the adverse effect on competition resulting from the "raising of a rival's costs", in that it is admitted that Nadeau is a rival of Olymel's (the Partnership) and the refusal to deal will admittedly (at a minimum) raise its costs;

(c) the adverse effect on non-price dimensions of competition, namely product quality, product choice and service;

(d) the adverse effects on the price (money) dimension of competition, given the likelihood that the live cost increases caused by a premium war, if these cannot be passed on by Nadeau and other processors to their customers;

(e) the likelihood that the elimination of Nadeau would create market power for Olymel in the Maritimes, where it previously had none ("un percée sur le marché des Maritimes");

(f) the "raising of rival's costs" among Nadeau's customers who are competitors of Olymel's at the further processing levels of the market;

(g) Olymel's enhanced market power *vis-à-vis* the other players in the market, even assuming that the geographic dimensions of the market encompass Ontario; and

(h) the possible elimination of the most efficient chicken processing plant in Canada.

**372** In the Applicant's argument, any of the adverse effects listed above would flow from the Respondents' refusal to supply. We summarize below the Applicant's explanation of the alleged adverse effects.

**373** The Applicant contends that the resulting premium war amongst processors will lead to an increase in the cost of price of live chickens which will generate "severe repercussions on the price of chicken at the retail level". The Applicant submits that raising its costs has an anti-competitive effect because it would weaken the Applicant to the benefit of Olymel. It is further argued that the Respondents' refusal to supply will threaten the Applicant's very viability and that its elimination will have an immediate effect on product quality and availability throughout the Maritimes. The Applicant states that many of its customers are also further processors that compete directly with Olymel. It is argued that the weakening or elimination of the Applicant would prohibitively increase its costs, even if it is able to obtain supply, and thus imperil its businesses. Finally, the Applicant contends that it "operates the most modern and efficient processing plant in Canada" and that for this reason alone, its elimination would have an adverse effect on competition in the market.

**374** In oral argument, counsel for the Applicant argued that except for (g) listed above, which provides for a market power analysis, none of the alleged adverse effects require an exercise of market power by Olymel. It is argued, for instance, that the disappearance of a processor that is unable to remain viable has nothing to do with Olymel's market power but is nonetheless an adverse effect on competition.

**375** In his report, Dr. Ware relies largely on the possible shift in market share from Nadeau to Olymel to support his inference that the alleged refusal to deal would have an adverse effect on competition. He argues that if Olymel were to experience the same increase in market share as a result of a merger or acquisition, the Competition Bureau would deem the merger or acquisition concerned as likely to lessen competition substantially and would challenge it.

**376** The Respondent Westco submits that the guidelines on mergers and abuse of dominant position state that there is no market power where market share is below a threshold of 35%. It argues that Westco's refusal will not create, maintain, or enhance the market power of Westco or any other entity in the relevant market because no entity will have a sufficient market share as a result of the refusal to supply, even if Nadeau ceased its operations. Westco further submits that the evidence shows that the other indicia of market power, be they direct or indirect, have not been met in this case.

**377** Ms. Sanderson focuses on the question of whether Olymel would gain market power or enhance it as a result of the refusal. To answer this question, Ms. Sanderson suggests the following analytical steps: (1) define the relevant market; (2) examine the position of the firm concerned with that of other firms in the market (using market share and concentration); (3) examine the ability of customers to switch suppliers; and (4) examine the ability of rivals to expand their supply. In her view, the inference of an adverse effect cannot be drawn on the basis of market share and concentration evidence alone.

**378** In his reply report, Dr. Ware states that the increase in Olymel's market share coupled with what he calls the degradation in product quality and disruption in supply to certain customers resulting from Nadeau's possible inability to continue to supply them constitutes an adverse effect on competition. Dr. Ware relies on affidavits filed by certain customers of the Applicant to support his conclusion that the refusal will decrease quality and disrupt supply. In support of his conclusion, Dr. Ware points to the Projet Westco Report wherein it is stated that **[CONFIDENTIAL]**.

(c) Analysis

**379** As stated earlier, we adopt the approach set out in *B-Filer*, which provides that for a refusal to deal to have an adverse effect on a market, the remaining market participants must, as a result of the refusal, be placed in a position of created, enhanced or preserved market power. As a consequence we necessarily reject the Applicant's submission that the exercise of market power need not be established for there to be an adverse effect on competition in a market.

**380** We acknowledge that neither Westco, nor any of the Respondents for that matter, are involved in the slaughter of chickens or the sale of processed chicken. Strictly speaking, the Respondents have no market share in this downstream market. However, the arrangement under which Olymel will process the Respondents' chickens is a **[CONFIDENTIAL]** partnership. While the interests of this Sunnymel partnership are not fully aligned with those of Olymel, it is reasonable to treat the Sunnymel partnership and Olymel as a single entity for purposes of the analysis of the competitiveness of the Ontario-Quebec-Maritimes market for processed chicken. We therefore accept that adverse effect under paragraph 75(1)(*e*) may be analysed by measuring the impact on the market power of the said partnership.

**381** We now turn to the above-mentioned indicators which we will consider in our evaluation of market power.

(i) Market share and market concentration

- *Evidence of the parties*

**382** Having defined the geographic market for processed chicken as Quebec, New Brunswick, Nova Scotia and Prince Edward Island, Dr. Ware calculates the market shares of the processors in Table 4 of his expert report as follows:

Nadeau **[CONFIDENTIAL]**%

Olymel **[CONFIDENTIAL]**%

Exceldor **[CONFIDENTIAL]**%

ACA Co-op **[CONFIDENTIAL]**%

Other (Quebec) **[CONFIDENTIAL]**%

**383** The Herfindahl-Hirschman Index ("HHI") is a common measure of industry concentration that takes into account all participants in a relevant market and gives proportionately greater weight to the market shares of larger firms. The HHI is defined as the sum of the squares of the respective market shares of each competitor in the market.

**384** Dr. Ware calculates the HHI for this market to be 3062. He also describes Olymel as "the dominant processor" in that market. Ms. Sanderson correctly points out that the market shares Dr. Ware reports do not support the characterization of Olymel as dominant given Exceldor's market share of **[CONFIDENTIAL]**%.

**385** We have concluded that the geographic market is broader than the one defined by Dr. Ware and that it should include Ontario-based processors. This has the effect of reducing both the market shares of the processors listed in Dr. Ware's Table 4 and the market concentration.

**386** We note, however, that even according to his own definition of the geographic market, Dr. Ware's estimates of market share and market concentration are imperfect. The market shares Dr. Ware reports are based on *slaughter* (number of chickens slaughtered) rather than sales of processed chicken to customers in the relevant market. However, slaughter data were the only data available to the experts and the Tribunal.

**387** It is known that **[CONFIDENTIAL]**% of Olymel's total sales are to customers in Ontario. According to Dr. Ware's definition of the relevant geographic market, these would be "exports". Similarly, the Applicant "exports"

**[CONFIDENTIAL]**% of its sales to Ontario. There is little evidence regarding Exceldor's sales outside the market as defined by Dr. Ware. It is also the case that Olymel, Exceldor, the Applicant and ACA are not the only processors competing in the geographic market as Dr. Ware defines it. There is some evidence that Ontario processors compete in this market. For example, Mr. Feenstra testified that it is safe to assume that the Applicant competes with the Ontario processors that want to sell into Quebec. In addition to excluding the "export" sales of Olymel, Exceldor, the Applicant and ACA, a proper market share calculation would include the share of "imports" from Ontario and elsewhere.

**388** Dr. Ware conceded in cross-examination that including only the sales that were made within the relevant market "might be a better way to do it". He stated, however, that he did not have the necessary data to make those calculations:

> **Ms. Healey**: Right. Okay. So back to the issue of assessing shares of sales in Quebec and the Maritimes: You would only include the sales that were made within those provinces; correct?
>
> **Dr. Ware**: I would -- I think I would like to have done that. Of course, I didn't have those data.
>
> **Ms. Healey**: Fair enough, Dr. Ware. I'm not-- I'm not suggesting that you did.
>
> **Dr. Ware**: But I -- I think I would have preferred that, yes.

**389** We have found that the relevant geographic market for the purposes of paragraph 75(1)(*e*) includes Ontario processors. Ms. Sanderson examines the market shares in this broader geographic market, but these shares are also based on slaughter and therefore include sales that are made outside the relevant market and ignore sales of chickens that are slaughtered outside the relevant market (imports). However, we find that the misstatement of market shares is likely to be less serious than was the case with the more narrowly defined market advocated by Dr. Ware because exports from and imports to the broader market are absolutely and proportionately smaller. In particular, Olymel makes **[CONFIDENTIAL]**% of its sales outside of Quebec and the Maritime provinces but only **[CONFIDENTIAL]**% of its sales outside of Ontario, Quebec and the Maritime provinces. Similarly, Nadeau makes **[CONFIDENTIAL]**% of its sales outside Quebec and the Maritime provinces but only **[CONFIDENTIAL]**% of its sales outside of Ontario, Quebec, New Brunswick and Nova Scotia.

**390** Maple Lodge Farms is among the Ontario processors in the relevant geographic market. The Applicant and Maple Lodge Farms are wholly-owned subsidiaries of Maple Lodge. It is clear that as a wholly-owned subsidiary, the Applicant's interests are fully aligned with those of Maple Lodge. It is therefore sensible to assume that Maple Lodge Farms and the Applicant conduct themselves with an eye to their joint profitability and to treat them as a single entity (Maple Lodge) for the purpose of analyzing the state of competition in this market.

**391** The processors' market shares (based on weekly slaughter) in the relevant geographic market in 2007 are found in Exhibit A to Mr. Soucy's affidavit of May 29, 2008. While they have their defects, we accept these data to be an adequate reflection of the market shares of processors in the market for that period. Based on these data, the shares are as follows[3]:

| | |
|---|---|
| Maple Lodge Farms/Nadeau | 22.6% |
| Maple Leaf | 17.9% |
| Olymel | 17.9% |
| Exceldor | 18.5% |
| ACA | 5.1% |
| Cargill | 5.1% |
| Port Colborne | 3.8% |
| Grand River | 2.6% |

| | |
|---|---|
| Other Ontario | 3.8% |
| Other Quebec | 2.6% |

(Total 99.9%)

**392** The HHI in the relevant geographic market in 2007 was 1579.[4] Maple Lodge Farms/Nadeau had the largest market share (over 22%) with Maple Leaf, Exceldor and Olymel all grouped at around 18%. For purposes of comparison, taken by itself, the Applicant's share of this market would have been 7.2%.

**393** As stated above, the Applicant advances a number of scenarios where there would be an adverse effect on competition. Some of these assume that the Applicant will remain a market participant, although with higher costs as a result of the refusal; in other scenarios it is no longer a participant. Dr. Ware acknowledged these scenarios:

> And as I say, there are sort of a number of possible scenarios here. One, ranging -- and we already went through this. I don't want to -- perhaps you don't want to spend a lot of time on this, but ranging from Nadeau, ceasing to process -- ceasing to replace, not being able to replace the chicken that it's currently getting from New Brunswick. Two, it being able to -- possibly being able to replace after a delay perhaps but at a significantly higher price. So both those cases, it seems to me, would amount to an adverse effect on competition.

**394** In its analysis, the Tribunal decided that it would be helpful to develop the scenarios described by the Applicant and Dr. Ware to determine the likely impact on market shares and, where possible, on market concentration if the scenarios played out.

*- Possible scenarios and the resulting impact on market share*

**395** We agree that a number of scenarios are possible. The Respondents' refusal to supply takes place against an uncertain backdrop. The Sunnymel partnership has stated its intention to build a processing plant in New Brunswick, but it has not commenced construction, and the Applicant argues that it will not do so. According to the evidence adduced, the Sunnymel partnership is proceeding with certain tests, such as testing the groundwater, to determine the best location for a new processing plant. Witnesses have also testified that ACA may expand its Nova Scotia plant and that Maple Lodge may participate in that expansion. There is also considerable disagreement regarding the success that the Applicant is likely to have in replacing the Respondents' birds, both in terms of the price premium to be paid and the number of birds it will succeed in obtaining. Also in dispute is the point (in terms of weekly slaughter) at which the Applicant's St-François Plant would cease to be a viable operation.

**396** The suggested implication of the foregoing is that the refusal could impact market shares and market concentration in a variety of ways. We agree that a number of scenarios are possible and some are more likely than others. It is therefore useful to consider a number of these scenarios and the resulting impact on market share for each. In considering these alternatives, an analysis of market share and market concentration (as measured by the HHI) is helpful in assessing the market power implications of each scenario.

*Scenario 1*

**397** One possible scenario is that the Applicant is able to replace all of the Respondents' birds from sources in Quebec. Given the operation of the Quebec supply guarantee (VAG), the net effect of this would be to leave Maple Lodge Farms/Nadeau's market share unchanged while increasing Olymel's market share at the expense of Exceldor and other Quebec processors. In this scenario, given the increase in exports from Quebec to New Brunswick, the VAG allocated to each Quebec processor, including Olymel's allocated share, would be reduced. In this regard, it is difficult to understand the basis for Dr. Ware's assertion at paragraph 14 of his reply report, that "[t]here is every reason to believe that Olymel's production of processed chicken would increase by the volume of redirected chicken". On cross-examination, Dr. Ware acknowledged that he had not taken the VAG into consideration. He also stated that Olymel's market share would, however, increase in this scenario and added that

he was not qualified to predict the effect of the VAG on concentration and market shares. We are unable to compute the HHI for this circumstance because of insufficient data.

*Scenario 2*

**398** Another possibility is that the Applicant is able to replace approximately half of the Respondents' birds from sources in Quebec. **[CONFIDENTIAL]**. Dr. Ware is of the opinion that 136,000 birds per week is the "absolute maximum" Nadeau would be able to obtain in Quebec. The net effect of this would be to reduce Exceldor's and Maple Lodge Farms/Nadeau's respective market shares and increase Olymel's. Here, too, the data available do not make it possible to compute the HHI.

*Scenario 3*

**399** Yet another possibility is that the Applicant is unable to replace any of the Respondents' birds but is able to retain the balance of the New Brunswick birds as well as the Prince Edward Island and Nova Scotia birds it is presently processing. According to Mr. Robinson, the Applicant would remain profitable under these circumstances; in his view, the Applicant's earnings would drop from $**[CONFIDENTIAL]** to $**[CONFIDENTIAL]**. In this case, Olymel would slaughter the Respondents' 271,350 chickens and, as a result, its market share would go up by 3.5 percentage points to 21.4% and Maple Lodge Farms/Nadeau's share would go down to 19.1%. The HHI would decline from 1579 to 1570. That is, by the well-known market concentration measure used by Dr. Ware, the market would become *less* concentrated. The reason for this is that a processor with a smaller market share (Olymel) is increasing its share at the expense of a processor with a larger market share (Maple Lodge Farms/Nadeau). This reduces the share inequality in the market and, in turn, reduces the HHI.

**400** In his discussion of this scenario at paragraph 16 of his reply report, Dr. Ware states that an increase of Olymel's market share by 3.5 percentage points, coupled with evidence on quality degradation and supply disruption, would satisfy the threshold requirement for an adverse effect on competition. Keeping aside the issues of supply disruption and quality degradation for the moment, it does not appear analytically sound to infer an adverse effect on competition on the basis of an increase in the market share of *one firm*, when the *overall* measure of market concentration (the HHI) is decreasing, if only by a small amount.

*Scenario 4*

**401** Another possibility is that the Applicant is unable to source any birds from Quebec and that it ultimately loses the Prince Edward Island and Nova Scotia birds to ACA. In this event, the St-François Plant would likely be closed and the remaining New Brunswick birds might go to either ACA or Olymel. In this scenario, we assume that the remaining New Brunswick birds go to ACA. In this event, as explained above, Olymel's market share would go up to 21.4%, Maple Lodge Farms/ Nadeau's share would go down to 15.4% and ACA's share would go up to 8.8%. The HHI would fall to 1494. If ACA gets the Prince Edward Island and Nova Scotia birds, but the remaining New Brunswick birds go to Olymel, ACA's market share would be 7.7% and Olymel's 22.5%, and the HHI would be 1524.

*Scenario 5*

**402** Another possibility is that the Applicant is unable to source any birds from Quebec and ultimately loses its Prince Edward Island and Nova Scotia birds and remaining New Brunswick birds to Olymel. We are of the view that, on a balance of probabilities, this scenario is not likely. The Applicant is more likely to be able to obtain supply to replace at least some of the Respondents' chickens. In this scenario, Olymel's market share would go up to 25.1%, Maple Lodge Farms/Nadeau's share would be 15.4%, and ACA's would remain unchanged. The HHI would be 1615. This could be regarded as the worst-case scenario from a competition perspective. In this scenario, the refusal would result in an increase in the HHI, implying a more concentrated market. The HHI would increase from 1579 to 1615 or 36 points. In their expert reports, both Dr. Ware and Ms. Sanderson referred to thresholds at which mergers can be challenged or blocked. In this case, to provide a frame of reference, a merger of two firms each of

which had a market share of 4.25% would increase the HHI by 36 points. A merger of this nature would be within the safe harbours stated in the *Merger Enforcement Guidelines*[5]. We fully appreciate, however, that the experts' reference to safe harbours is in the context of mergers and that a different threshold applies; namely a "substantial" lessening or prevention of competition and not an "adverse effect" pursuant to paragraph 75(1)(*e*).

*Conclusion*

**403** Based on the above, we find that the refusal to supply will likely not have a significant impact on market shares of processors or market concentration. Even the worst case scenario, scenario 5, results in only a very small increase in the HHI.

(ii) Barriers to entry

**404** The assessment of barriers to entry is usually part of the assessment of market power. None of the experts discussed barriers to entry directly. Neither Dr. Ware nor Ms. Sanderson incorporated considerations on barriers to entry into their market power analyses.

**405** There is very little evidence of the kind usually used in the assessment of barriers to entry on the record. We have no systematic information on the historic entry-and-exit pattern, although there are statements to the effect that the chicken processing industry has become more consolidated over time. For instance, in a document prepared by Agriculture and Agri-Food Canada on the Canadian chicken industry, one can read that "the poultry industry has become concentrated over the years" and that "[w]hile the concentration ratio has stabilized in the recent years, concentration in the industry might continue to occur in the future".

**406** Concerns about cost-related barriers to entry normally center on diseconomies of small scale and sunk costs (specialized investments required for entry). We have very little information on these factors, although Dr. Barichello does state that "[c]learly, a processing plant represents a considerable capital investment and therefore business risk". With respect to regulatory barriers to entry, we have some information: given that the supply of live chickens is fixed by the marketing boards, a new entrant abattoir would have to bid against incumbents for live birds. Although some chicken producers may have relationships with co-ops, having to bid against incumbents for birds does not necessarily place an entrant at a disadvantage. The problem for new abattoirs comes with the provincial allocation systems in place in Ontario and Quebec, which allocate incumbents their historic share of provincial slaughter. These allocation schemes provide for some exceptions. Dr. Barichello stated that there is an "open sign-up pool"[6] in Ontario. Also, new entrants can bid inter-provincially. The impression remains, however, that the provincial allocation schemes make new entry into processing at the abattoir level difficult. Entry into further processing would not be subject to the same regulatory barrier. While there is evidence that there are barriers to entry in primary processing, there is little to indicate that the refusal would increase them or prevent them from eroding.

**407** While it is clear that barriers to entry do exist, they are one of many factors to be considered in assessing market power. In our view, the existence of barriers to entry is not in itself determinative.

(iii) The effect of the refusal on the price of processed chicken

**408** With respect to the link between the Respondents' refusal to supply and the price of processed chicken paid by consumers, four issues are raised in argument, namely (1) the price increase that is implied by the change in Olymel's market share and in the HHI; (2) contractual provisions bearing on the ability of processors to pass premiums along to customers; (3) statements by processors regarding their ability to pass price increases along; and (4) the implications of supply management for processors' ability to raise the price of processed chicken. We will deal with each of these in turn.

- *The effect of the change in market shares and the HHI on the price of processed chicken*

**409** Dr. Ware testified that he did not model the effect of the change in market concentration on the price of processed chicken. He explained that he had not been asked to undertake such an analysis and that he did not have enough data to do so. He explained that "because...we have a standard of the adverse effect on competition rather than a substantial lessening on competition ... any lessening or any change in market structure in the direction of increasing concentration would constitute an adverse effect on competition" and that "if you add that to the increasing costs arising from an increase in premiums and an increase in live transport costs plus the effect on the further processing market, then that would amount to an adverse effect on competition". The first statement would appear to require some qualification. An increase in concentration could be the result of pro-competitive forces at work. For example, an increase in concentration may occur if a more efficient firm attracts customers from a less efficient rival. In any event, as stated above, the refusal in this case could well decrease concentration. In the worst-case scenario, it would increase concentration by a very small amount.

*- Contractual limitations on the ability of processors to pass on increases in premiums to their customers*

**410** Dr. Ware contends that if the Applicant attempted to replace the Respondents' birds by acquiring birds in Quebec, the result would be an increase in premiums paid by the Applicant and other processors, and these premiums would be passed on to consumers. Dr. Ware believes that some of the Applicant's contracts with its customers "are of a cost plus form in which their cost -- Nadeau's cost increase would automatically be represented in their prices to the customers". During her cross-examination of Dr. Ware, counsel for the Respondent Westco made reference to several cost-plus contracts. According to Westco, these contracts do not allow the Applicant to pass on its premiums to its customers. Below, we review the provisions in a number of these contracts.

**411** Clauses **[CONFIDENTIAL]** of the Applicant's contract with **[CONFIDENTIAL]** stipulate the following:**[CONFIDENTIAL]**.

**412** **[CONFIDENTIAL]**.

**413** On this evidence, while **[CONFIDENTIAL]** may be able to pass an increase in the NB Board Price on to **[CONFIDENTIAL]**, it is unclear if any other increase can be passed on.

**414** The Applicant's contract with **[CONFIDENTIAL]** sets out the following pricing formula: **[CONFIDENTIAL]**.

**415** We have limited evidence to explain how the contracts described above work in practice. On the whole, they appear to provide for prices to be fixed at least for a set time period. It is unclear as to how and when cost increases can be passed on, if at all. There is simply insufficient evidence to determine, based on these contracts, how increases in cost to the Applicant, caused by "premium wars", could be passed on to customers.

*- Processors' statements regarding their ability to pass on cost increases to their customers*

**416** At paragraph 101 of her report, Ms. Sanderson stated that "[t]he record is filled with statements from processors indicating that they have no ability to raise prices to customers". In that regard, she referred to the statements made by Mr. Feenstra and two of the Applicant's customers. Cara, a full-service restaurant operator, indicated in a letter that its business is very price-sensitive and that there is "virtually no room to increase prices to our customers". In a letter addressed to the Applicant, the following concerns are expressed on behalf of La Préférence, another customer:

> Eliminating Nadeau from the supply chain, by way of shut down or purchase from a competitor of there's [sic] will only tighten the supply of fresh raw products, and ultimately I foresee an increase in the price of poultry.

> An increase in the price of poultry will hurt La Preference's bottom line. Our clients will not pay for the increase in price for simply having fostered a controlled supply.

**417** In her testimony, Ms. Sanderson stated that the fact that costs were going up did not necessarily mean that prices of processed chicken would go up. She expressed the opinion that processors were worried about a premium war because they could not pass the higher premiums on to their customers.

**418** Mr. Brodeur stated that it would be very difficult for a processor to pass these costs on to customers and consumers. In his evidence, he gave three reasons to explain his view. He said:

> 7.16. À la connaissance du Témoin, advenant une augmentation des coûts d'approvisionnement en poulets vivants causés par une hausse des primes versées aux éleveurs, il serait très difficile pour un transformateur ou un surtransformateur d'exiger un prix plus élevé de la part de ses clients et ultimement, des consommateurs. Cela s'explique par les trois raisons suivantes :
>
> 1ère raison: produits substituts
>
> 7.16.1. Il existe une "concurrence croisée" entre le poulet et les autres viandes telles que le boeuf et le porc. Le Témoin a pu constater, au fil de ses années d'expérience dans l'industrie, que lorsque les prix des Produits transformés et surtransformés augmentent, les consommateurs se tournent vers le porc ou le boeuf, ce qui a résulté en une baisse de la demande des clients d'Olymel pour ses Produits transformés et surtransformés. Cette réalité a aussi été constatée dans le rapport des PPC, joint à la présente déclaration à la pièce YB-16, à la page 41. En effet, chez les Canadiens, la consommation d'un type de viande se fait naturellement au détriment d'un autre type.
>
> 2e raison: coûts des inventaires
>
> 7.16.2. Les coûts associés à la conservation en inventaire des Produits transformés et des Produits surtransformés sont élevés et motivent les abatteurs, transformateurs et surtransformateurs à vendre leurs produits rapidement. De plus, une fois congelé, le produit perd de sa valeur en raison des frais qui devront être encourus pour le décongeler et des limitations concernant l'utilisation de cette viande.
>
> 3e raison: augmentation prévisible des contingents
>
> 7.16.3. Advenant une hausse des prix de vente, les contingents de production des poulets vivants sont rapidement ajustés à la hausse afin de ramener les "marges viande" des transformateurs à leur niveau historique.
>
> 7.16.4. Il faut savoir que les données produites par la firme Express Markets Inc. (EMI), dont les résultats sont utilisés par les organismes de réglementation dans leur évaluation des besoins en poulets de la population canadienne, ne tiennent pas compte des primes payées aux éleveurs dans le calcul de la "marge viande" des transformateurs. Dans les calculs effectués par ces organismes de réglementation, la "marge viande" des transformateurs correspond à l'écart entre les prix de gros moyens (données EMI) et prix de référence du poulet vivant en Ontario.
>
> 7.16.5. Or, lorsque cette marge augmente au-delà d'une moyenne historique, ceci peut laisser présager un manque de viande sur le marché domestique et les contingents de production de poulets vivants seront normalement ajustés à la hausse, ce qui aura pour effet d'augmenter la quantité de produit disponible pour les abatteurs et, par le fait même, de réduire les primes versées aux éleveurs.
>
> 7.17. Selon l'expérience du Témoin, il n'y a pas de relation directe entre les primes payées aux éleveurs pour les poulets vivants et les prix de vente en gros et au détail des Produits transformés et surtransformés. En effet, la variation des prix de ces produits est principalement causée par les fluctuations de l'offre et de la demande et par les variations de prix des autres viandes transformées. Quant aux primes payées aux éleveurs, celles-ci dépendent notamment de la concurrence entre les abatteurs et de la rentabilité relative de l'industrie.

**419** Some processors stated, however, that they would attempt to pass on the increased costs to their customers.

In a letter addressed to the New Brunswick Farm Products Commission, Kevin Thompson, on behalf of the Association of Ontario Chicken Processors, stated that processors would "attempt to [pass] the additional costs on to their customers causing increases in the price of chicken at the retail meat counter and an adverse impact on consumption which will in turn lead to lower production for all chicken farmers". In his view, "...consumers who already pay higher prices in Canada to support supply management will unjustly pay even more".

**420** Mr. McCullagh, at paragraph 14 of his affidavit, states that processors will look to and need to pass on the costs to their retail and foodservice customers, who, in turn, will seek to increase prices to consumers.

**421** However, Mr. Feenstra testified that it is very difficult for processors to pass on the costs of a "premium war" to the end consumer as consumers are willing to pay only so much for their chicken. In cross-examination, Dr. Ware responded to Mr. Feenstra's testimony as follows:

> **Ms. Healey**: If Mr. Feenstra were to advise the Tribunal that it is very difficult to pass along the cost of a premium to a consumer or consumers are only willing to pay so much for chicken, would you have any reason to doubt Mr. Feenstra's comments in that regard?
>
> **Dr. Ware**: Yes, I would because it is possible that economists take a bit more of a detached view of how markets work than people who are embroiled in the everyday decision-making and, as I said, these premiums are not just going up to Nadeau. These premiums are going to go up way across Quebec and if that were to happen, that would be, you know, a market-wide increase in costs and it's hard for me to imagine that a market-wide increase in costs would not be reflected in the price of chicken.

**422** Dr. Ware is distinguishing between the ability of the Applicant or that of any other individual competitor to pass on cost increases that they may have incurred and the ability of processors as a group to pass on a market-wide increase in the premiums they pay for live chicken. Competitive pressure normally limits the ability of individual competitors to pass on cost increases that they have incurred. In the absence of supply management, a market-wide increase in costs is more likely to be passed on as Dr. Ware has stated. It is the Tribunal's view, however, that supply management itself limits processors' ability to pass on even a widespread increase in the premiums they pay for live birds. We will now turn to that issue.

*- Limitations posed by supply management on the ability of processors to increase price*

**423** Supply management reduces the ability of processors to raise the price of processed chicken and also attenuates any link between price and concentration that might otherwise exist. The supply of live chickens in Canada is determined by producer-controlled provincial marketing boards coordinated by a national marketing board, the CFC. Dr. Barichello explains the regulatory process by which the supply of live chickens is determined:

1. Processors calculate their requirements for production.
2. Each province's marketing board aggregates processors' requirements within their province.
3. Provincial marketing boards send their aggregates to the CFC.
4. The CFC makes any necessary adjustments and then authorizes a total production for each province.

**424** According to Dr. Barichello, national chicken quota is set by the CFC for a six- to seven- week production period, and farmers cannot deviate materially from their quota. Thus, there is a continuous flow of live chickens coming to market. The quantity is determined by regulation, and the birds must be processed and sold to consumers. It is normally not possible to sustain a price increase in a market if supply and demand conditions remain unchanged. In the case at hand, it would appear very difficult to raise the price of processed chicken without simultaneously restricting the amount offered on the market. The weekly flow of chicken into the market is not under the control of any one processor.

**425** The evidence also points to a recent instance in which processors jointly lobbied the CFC for a reduction in the national quota and were successful; the CFC reduced the allocation for period A-87. Mr. Landry testified as follows with respect to the request made by the processors:

> **Mr. Lefebvre**: Une des dernières questions que j'ai pour vous. Pourquoi tant vouloir baisser la production de poulets?
>
> **Mr. Landry**: C'est comme je t'ai expliqué, c'est que le prix de vente, c'est un marché contrôlé, c'est là qu'est la demande. Puis quand le prix vivant du poulet vient trop élevé--
>
> **Mr Lefebvre**: Oui.
>
> **Mr. Landry**: --- pour le prix de vente que les abattoirs peuvent faire, les retours sont pas bons. Donc, c'est une des raisons pourquoi que le système est révisé à toutes les huit semaines.

**426** The limited information provided about this one incident is insufficient to support the inference that processors exercise the kind of control over supply management that would be necessary for them to increase the price of processed chicken as and when they wish. This is particularly so given the complex nature of quota adjustments provided for in the supply management system.

**427** As indicated in our earlier review of the supply management system, a "bottom-up approach" is contemplated in order to determine if quota adjustments are required. The mechanism is designed to strike a balance between chicken production and consumer demand. In essence, quotas are adjusted as a result of changes in that demand.

**428** We find that it would normally not be possible to sustain a price increase in a market if supply and demand conditions remain unchanged. In the absence of an increase in consumer demand or a reduction in supply, there is no reason to believe that prices will rise.

**429** The Applicant contends, in essence, that the price increases caused by "premium wars" will be passed on to customers and consumers. In the event that the Applicant is able to obtain all of its replacement birds from Quebec, the concern is that this would result in "premium wars" that would squeeze processor margins. It is argued that processors would then attempt to pass on premium increases to customers. It is our view that other factors, such as consumer preferences, being equal, an increase in the price of processed chicken cannot be sustained in the absence of a further restriction in supply by the marketing boards. Here, any "premium war" would be the result of excess processor demand for live chickens. There is little evidence to suggest that the marketing boards would respond to excess processor demand for chickens by reducing quotas and thus further restricting supply. This would only make things worse, because processors would then be competing for an even smaller supply of chickens. It is our view that it would be more logical for marketing boards to attempt to mitigate any premium increase by increasing quotas to ensure that there would be sufficient chickens for all processors. In that case, prices would fall.

**430** For the above reasons, we find that the price increases to processors caused by "premium wars" are not likely to be passed on to customers or consumers without an accommodating reduction in supply by the marketing boards. We also question whether a further restriction of supply would remedy or even be seen as a remedy for a deterioration of processor margins caused by "premium wars".

(iv) The effect of the refusal on rivals' costs

**431** The Applicant further argues that to the extent that processors cannot pass on the increased live costs caused by a "premium war", their viability will be threatened. It also argues that the refusal will substantially raise the Applicant's costs and that the raising of these costs would have an anti-competitive effect because it would weaken the Applicant to the benefit of Olymel. Dr. Ware states as follows in his examination in chief:

**Ms. Price:** Can I just stop you there for a minute and ask a question arising from what you said? This concept of raising rivals' costs, I believe that there's been a fair bit of evidence that Nadeau and Olymel do compete in the primary processing market. Does that concept that you've just described apply not only to the further processors whose costs might be raised as you've described but also to Nadeau itself in the event it has to go into Quebec?

**Dr. Ware:** It could, yes. Yes, it could. We don't know -- you're basically saying does it apply to the processing market, the primary processing market?

**Ms. Price:** As well.

**Dr. Ware:** Yes. Well, it certainly could. We don't know -- and I didn't really directly address this, but we don't know how much premiums will be bid up in Quebec to other processors as a result of them being bid up to Nadeau.

**Ms. Price:** Right.

**Dr. Ware:** But they certainly will be bid up to some extent because as I was saying before the break, if Nadeau is going to bid 10 percent of the supply of Quebec chicken out of Quebec, it's going to do that by raising the price, and you raise the price -- when you raise the price that they pay, that's going to increase the price to everyone else too.

**432** "Raising rivals' costs" is a term described in section 4.2 of the Competition Bureau's *Enforcement Guidelines on the Abuse of Dominance Provisions* and can be described as a set of anti-competitive strategies that a dominant incumbent firm might use to inhibit the expansion of smaller competitors or the entry of new competitors, thereby entrenching its dominance. The Guidelines note that in order for the raising of rivals' costs to be a profitable strategy for the dominant firm, the burden of the cost increase concerned must fall more heavily on the rivals of the dominant firm than on the dominant firm itself.

**433** The Tribunal has found that, for the purposes of paragraph 75(1)(*a*), if the Applicant replaced the Respondents' birds with birds from Quebec, its costs would increase and it would be substantially affected as a consequence. The question here is whether the evidence supports that the raising of rivals' costs would be the result of the refusal and, if it does, whether this implies that competition in the Ontario-Quebec-Maritimes market for processed chicken would be adversely affected. The answer is that it does not. The reasons are as follows.

**434** First, the conditions for the successful pursuit of a strategy of raising rivals' costs do not appear to exist in the relevant market. Olymel, the recipient of the Respondents' birds, is not dominant in the relevant market, and the receipt and retention of the Respondents' birds would not come close to making it so. Indeed, there is no dominant firm in the relevant market. There are several other large, if not larger, competitors (Maple Leaf, Maple Lodge, Exceldor) and numerous smaller ones. Second, there is little in the evidence to indicate that a price war for live chickens would be less burdensome to Olymel than to other processors. In his testimony, Dr. Ware refers to a market-wide increase in processors' costs that is the result of their bidding more aggressively for live birds.

**435** To the extent that cost increases resulting from the refusal are confined to the Applicant, it is unlikely that any cost increases experienced by the Applicant could be passed on to consumers in the form of higher prices. Indeed, it is central to the Tribunal's determination under paragraph 75(1)(*a*) that the Applicant would be substantially affected by the refusal, that it could not simply pass the higher cost of acquiring replacement birds in Quebec on to its customers. The evidence relating to the possibility that costs increases experienced by the Applicant could be passed on to consumers is summarized above. Further, Mr. Robinson assumed that the price at which the Applicant sells processed chicken would remain unchanged in scenario 2, where the Applicant is able to replace the Respondents' chickens with birds from Quebec. The ultimate limitation on the ability of the Applicant or other processors to increase the price of processed chicken is that they do not control the supply of chickens to the market. Control of supply lies with the marketing boards.

(v) The effect of the refusal on the quality and variety of processed chicken available to consumers

**436** Dr. Ware states as follows at paragraph 25 of his reply report:

> There are compelling reasons also to believe that the refusal to deal will lead to severe declines in quality in some cases, which are sufficient in themselves to constitute an adverse effect on competition.

**437** Dr. Ware cites an example of what he sees as a decline in quality, the evidence of **[CONFIDENTIAL]**, which is that if the Applicant were to close, **[CONFIDENTIAL]** would lose a source of **[CONFIDENTIAL]**, and replacement sources would be further away and more costly. **[CONFIDENTIAL]**.

**438** Ms. Sanderson responds that if the Applicant were able to replace the Respondents' birds, there is no issue. If the Applicant were unable to replace the Respondents' birds, **[CONFIDENTIAL]** would still have a variety of realistic alternatives. One possibility is that Sunnymel builds a plant in New Brunswick. Exceldor and ACA could also supply **[CONFIDENTIAL]** without greatly increasing the shipping distance.

**439** Ms. Gazzard stated in her affidavit that UPGC and Olymel have been in negotiations to replace the Applicant as a source of supply. Olymel has apparently stated that it has the capability of filling UPGC's requirements but has not quoted a price. She stated that they had also approached Exceldor about replacing the lost Nadeau volume. Exceldor believed, however, that their price would not be commercially viable to UPGC.

**440** There is evidence of complaints by certain customers of the Applicant, in particular Puddy, relating to their inability to obtain chickens of the required quality and variety should they no longer be supplied by the Applicant. Mr. McHaffie stated as follows:

> By contrast, our purchases from Olymel have declined significantly since 2006. This is because of quality and service problems. The quality problems have included bruising, cuts, neck skin left on, missing parts, (such as wings), and the like. Service problems include late delivery and short delivery. Olymel, for reasons unknown, has been unresponsive to our requests for improvement. As we are unable, in our view, to obtain sufficient supplies to meet our needs from elsewhere in Québec, it has been a major advantage for us to have Nadeau as an alternative source of fresh killed chicken.

**441** Given the distances processed chicken is routinely shipped, a need to find a new (possibly more distant) source of supply does not necessarily qualify as a decline in quality. There are several post-refusal scenarios under which Priszm and Puddy would not experience any need to change suppliers, for instance, if the Applicant were to replace some or all of its lost supply. In the event that they have to change suppliers, there are several other options open to Priszm and Puddy whereby they need not go much further afield for supply. Nor is it necessarily the case that the need to change suppliers qualifies as an adverse effect on competition. Changing suppliers is part of the normal process of competition. Given the consolidation that has occurred among chicken processors, customers have presumably changed suppliers in the past although there is not much in the way of evidence on this point.

(vi) Possible foreclosure of supply to other processors in the market

**442** Dr. Ware also cites a possible lessening of competition in what he calls the "market for further processed chicken" as another manifestation of the adverse effect on competition flowing from the refusal. He cites the affidavit of Ms. Goodz of Riverview and the affidavit of Mr. Ellis of Sunchef. Both Ms. Goodz and Mr. Ellis express the concern that, as a competitor, Olymel would not supply them or would not supply them on reasonable terms. Also, at paragraph 28 of his report, Dr. Ware cites the affidavit of Mr. McHaffie of Puddy. Mr. McHaffie explains that Puddy has had quality and service problems with Olymel and that Olymel has been unresponsive to its request for

improvement. We now turn to the evidence of some of the Applicant's customers in that respect.

*Riverview*

**443** Ms. Goodz testified that both Olymel and Exceldor have refused to supply Riverview. She stated as follows at paragraph 17 of her affidavit:

> My ability to continue to supply my specialized product at an acceptable price depends on my ability to obtain supplies from Nadeau. Should Nadeau go out of business, reduce its business, or be acquired by Olymel, I foresee that our supplies will be reduced or cut off, and we will no longer be able to continue in this business.

**444** Ms. Sanderson responds to these concerns at paragraph 77 of her report. She states that Ms. Goodz' concerns would not arise if the Applicant is able to replace the Respondents' birds. She states that alternate suppliers such as Exceldor, Abattoir Agri and Lilydale are closer to Riverview than Nadeau is and that Maple Lodge Farms and Maple Leaf are not much further away. Lilydale is no longer an alternative for Riverview as it is going out of business, and Exceldor is questionable as Ms. Goodz has testified that it has refused to supply her. Ms. Goodz also stated that some suppliers cannot meet her size requirements. Ms. Goodz conceded under cross-examination that **[CONFIDENTIAL]**. Ms. Sanderson further stated that even if Riverview were forced out of business, it is small enough that there would be no adverse effect on the market for processed chicken.

*Sunchef*

**445** Sunchef is a further processor of chicken located in Montreal. **[CONFIDENTIAL]**

**446** Mr. Ellis states at paragraph 16 of his affidavit that if the Applicant's supplies are cut off or curtailed, its ability to compete with Exceldor and Olymel would be reduced or eliminated:

> This would have a major adverse effect at our level of the market. It would permit Olymel to increase its dominance and market power, at the expense of other businesses like ours.

**447** At paragraph 15 of his affidavit, Mr. Ellis makes the same claim as Ms. Goodz as to the crucial role that continued supply from Nadeau at the same level plays with respect to the future of his business:

> Should Nadeau go out of business, reduce its business, or be acquired by Olymel, I foresee that our supplies will be reduced or cut off and that we will no longer be able to continue in this business.

*Puddy Brothers*

**448** Puddy is a further processor located in Mississauga, Ontario. According to Mr. McHaffie, it currently purchases whole birds from Exceldor (**[CONFIDENTIAL]**%), Nadeau (**[CONFIDENTIAL]**%) and Olymel (**[CONFIDENTIAL]**%). According to paragraph 9 of Mr. McHaffie's affidavit, Puddy has been in business since 1884 and began purchasing from the Applicant in about 2004 or 2005. Since 2006, it has reduced its purchases from Olymel because it has not been satisfied with its service. Mr. McHaffie states that Puddy cannot buy from Ontario primary processors, which are much closer than Nadeau, because they are also engaged in further processing, and the requirements of Ontario processors exceed the Ontario slaughter.

**449** Mr. McHaffie states that if the Applicant were unable to continue as a viable business, Puddy would be forced to buy more from Olymel, and its service might be worse. He concludes that if the Applicant were to close or be taken over by Olymel, competition in the market would definitely be hurt. He admitted under cross-examination, however, that he had not taken his concerns regarding inadequate supply up with the CFC.

*Desco*

**450** Mr. Chevalier testifies that Desco competes directly with Olymel and Exceldor and that they have refused to supply Desco at reasonable prices. At paragraph 7 of his affidavit, he states that if the Applicant's supplies of live chicken were reduced or cut off, Desco's ability to compete effectively against Olymel would be reduced.

**451** Ms. Sanderson responds to Mr. Chevalier at paragraph 78 of her report. She states that there would be no issue if the Applicant is able to replace the Respondents' birds. Ms. Sanderson also calculates that Desco's purchases from Nadeau account for **[CONFIDENTIAL]**% of its annual chicken purchases, indicating to her that Desco has many other suppliers available to it. She states that Desco currently obtains fresh-killed chickens within 72 hours from the United States and that the Ontario processors as well as ACA could provide chicken within the same delivery time. Ms. Sanderson also states that if Desco were to go out of business, this does not mean that prices for processed chicken would rise.

**452** In cross-examination, Mr. Chevalier conceded that the Applicant's supply accounts for a small percentage of Desco's supply.

*Analysis*

**453** We earlier determined that further processed chicken is not a separate product market. We have little evidence regarding the respective market shares of the stated further processors Riverview, Sunchef, Puddy and Desco. We note that Mr. McHaffie stated in cross-examination that further processors are numerous. When questioned on the matter, he stated that he thought that there are more than 50 further processors in Ontario and 5 to 15 in Quebec.

**454** Both Riverview and Sunchef maintain that any diminution of their supply of chicken from the Applicant would be disastrous. Puddy concludes that it would be forced to return to a longstanding supplier, Olymel, with whom it has recently become disenchanted. This assumes, of course, that the Applicant is put out of business. There are many possible scenarios short of the worst-case scenario in which the St-François Plant closes and all the Applicant's birds go to Olymel. In the event of the worst-case scenario where the St-François Plant closes and Riverview and Sunchef are denied chicken from all other sources and are obliged to close, there is insufficient evidence to infer that this would have an adverse effect on competition in the relevant market which is the Ontario, Quebec and Maritimes market for processed chicken. This is essentially because of the size of that market, the apparent number of further processors in the market, the marketing boards' ultimate control of supply in the market and the paucity of evidence to show that complaining further processors cannot obtain supply elsewhere.

**455** We further note that there are several reasons why customer complaints might not be given significant weight in the determination of whether the probable effect of the refusal competition in the market is or is likely to be adverse. First, some of the complaints appear to have been orchestrated. For example, as explained above, some of the letters sent to the Applicant by some of its customers regarding the Respondents' refusal contain paragraphs that are virtually identical to those found in a draft letter prepared by the Applicant. This letter, which was apparently provided to Riverview and Cara, includes the following two paragraphs:

> Our business is a "pennies" business. There is virtually no room to increase prices to our customers. Accordingly, any increase in raw price or transportation costs would have an immediate adverse effect on our bottom line.
>
> If the Nadeau plant were to shut down, or even if it were to be acquired by a competitor, I would foresee that prices would rise, and supply problems would occur. We are therefore opposed to any reduced competition.

**456** The evidence adduced shows that similar paragraphs are found in letters sent to the Applicant by Riverview and Cara:

> [Riveriew]

> If the Nadeau plant were to shut down, or even if it were to be acquired by a competitor, I would definitely foresee that prices would definitely rise, and supply problems would occur. We are therefore strongly opposed to any reduced competition in this market.
>
> [Cara]
>
> Our business is very price sensitive. There is virtually no room to increase prices to our customers. Accordingly, any increase in raw price or transportation costs would have an immediate adverse effect on our bottom line.
>
> If the Nadeau plant were to shut down, or even if it were to be acquired by a competitor, I would foresee that prices could rise, and supply problems could occur. We are therefore extremely concerned with any reduced competition.

**457** Second, notwithstanding the evidence adduced on behalf of certain customers, in particular Sunchef and Riverview, that they would be put out of business should the Applicant cease operations, we are not persuaded that this result is likely. Some complaining customers have not attempted to investigate alternate sources of supply and have simply asserted that it would be either unavailable or too costly. While the complaining customers assert that specific suppliers approached were either unwilling or unable to supply chickens to required specifications, there is insufficient evidence to establish that these further processors were unable to obtain the chickens they require from other suppliers in the market. Further, at this time, no one appears to have complained about the situation to the CFC, the regulatory body responsible for determining the supply of chickens available to processors as well as being the most capable of remedying their perceived supply problems.

**458** Third, many customer complaints focus on a limited set of scenarios, to wit, the possibility of the Applicant's closing or being acquired by Olymel. There are many other possible scenarios. A likely scenario is that the Applicant will be able to replace some but not all the Respondents' birds from Quebec sources. It could be business as usual or business on a reduced scale. This reduced scale could be quite consistent with the Applicant's historic supply of chickens, before it added an extra shift to accommodate the Nova Scotia and Prince Edward Island birds. In the event that the Applicant were to operate at a reduced scale, it might well arrange to continue to supply those customers who rely most on it and allow customers that are less concerned about their alternatives to seek supply elsewhere. This could also be true of some complaining customers who have only recently entered into contracts with the Applicant or increased their purchases from the Applicant.

**459** The quality degradation issue appears to be overblown to the extent that it is related to incremental shipping distances. In many cases, complaining customers have alternate sources of supply that are closer than the Applicant. The most common source of concern appears to be the tension between the abattoirs and the further processors rather than distance. This issue is market-wide and cannot turn on the actions of the St-François Plant. The Applicant itself engages in some further processing (Kentucky Fried Chicken birds) and its sister, Maple Lodge Farms, is also integrated into further processing. There are apparently 50 further processors in Ontario, even though the major abattoirs in Ontario (Maple Lodge Farms and Maple Leaf) are integrated into further processing. It appears that there are market opportunities for specialists in further processing and that these opportunities will not depend on the conduct of or the scale of operations at the St-François Plant.

**460** A need to change suppliers does not necessarily equate with a supply disruption. The aggregate supply of chickens coming to market remains the same regardless of where the Respondents send their birds. The capacity to process chickens would remain the same unless the St-François Plant actually closes. Even then, the Sunnymel partnership may build a new plant, and/or ACA may expand, perhaps with the participation of Maple Lodge. It appears that some of the customers who have submitted evidence in this proceeding have changed their mix of suppliers in the past, some quite recently. This is a normal part of doing business, and it is not clear that any special significance should be attached to the fact that some of the Applicant's current customers are obliged to make further changes in their mix of suppliers.

**461** In the event that the worst-case scenario prevails and some of the Applicant's current customers are adversely affected, the question remaining is whether this can be regarded as an adverse effect on competition in the market.

There is no evidence of concern among purchasers of processed chicken who are not current Nadeau customers. Nor is there much in the way of evidence regarding the portion of the market accounted for by Nadeau's complaining customers. Given the limited likelihood of the worst-case scenario prevailing and the lack of evidence regarding the portion of the market that would be affected if it did prevail, the complaints of the Applicant's customers are not sufficient to support an inference that the Respondents' refusal is likely to have an adverse effect on competition in the market.

(vii) Impact of possible elimination of an efficient processor

**462** The Applicant argues that it operates the most modern and efficient processing plant in Canada and that for this reason alone, its elimination would have an adverse effect on competition in the market. In this regard, the Applicant relies on the statistics compiled by Mr. Donahue and the affidavit of Mr. Robinson.

**463** Mr. Donahue, as explained above, works for Agri Stats, a statistical research and analysis firm that offers benchmarking services for the poultry industry across North America. At the Applicant's request, he prepared a report about the St-François Plant. He testified that the Applicant's wage rates **[CONFIDENTIAL]** and that the Applicant **[CONFIDENTIAL]**.

**464** According to Dr. Ware, **[CONFIDENTIAL]** are an example of the greater efficiencies obtained by the Applicant. He is of the opinion that any adverse effect on competition will be quantitatively more severe if processing at the St-François Plant were replaced by the processing of chickens at a less efficient plant.

**465** Mr. Robinson, at paragraph 6 of his affidavit, states that **[CONFIDENTIAL]**.

**466** The evidence adduced does not establish that the Applicant operates the most efficient processing plant in Canada. When asked about the findings of his report, Mr. Donahue simply stated that **[CONFIDENTIAL]**.

**467** Further, given the paucity of evidence regarding the efficiency of other processing plants in the relevant market, we cannot agree with Dr. Ware that any adverse effect would be quantitatively more severe if another processing plant processed the Respondents' chickens. As stated earlier, we find it unlikely that the Applicant would close. However, if it were to close, any new plant built by Sunnymel could benefit from the same sources of efficiency **[CONFIDENTIAL]**.

(d) Conclusions for paragraph 75(1)(*e*)

**468** As stated above, for a refusal to deal to have an adverse effect on a market, the remaining market participants must, as a result of the refusal, be placed in a position of created, enhanced or preserved market power. This analysis requires a relative and comparative assessment of the market with the refusal to deal and that same market without the refusal to deal. The level of competitiveness in the presence of the refusal to deal must be compared with the level that would exist in the absence of the refusal. It must then be determined whether the effect on competition, if any, is "adverse". In *B-Filer*, the Tribunal found that "adverse" is a lower threshold than "substantial".

**469** Paragraph 75(1)(*e*) refers to two time frames: the present and the future. In the instant case, because of the Interim Supply Order, the refusal to deal is not having an adverse effect on competition at present because the Respondents have not yet ceased supply. Indeed, in their arguments, the parties referred to the likely effects of the refusal to deal.

**470** We are satisfied that neither Olymel nor any other processor in the market currently exercises market power. For comparative purposes, the market we consider at the outset, without the refusal, is a market consisting of numerous processors; many small processors and a number of larger ones including Maple Lodge, Maple Leaf, Exceldor and Olymel. We will now summarize the results of our above analysis of the effect of the refusal to deal.

**471** We have considered a number of different scenarios of the Applicant's circumstances resulting from the refusal. We have compared the effect of the refusal on market shares under five different scenarios and found that the results of this comparison are normally not associated with any concern about enhanced market power. We recognize, however, that the market shares upon which these calculations or other estimates of market concentration are based are not entirely accurate because they are based on slaughter rather than sales of processed chicken to customers in the relevant market. The parties failed to adduce any other evidence regarding market shares.

**472** In assessing market power, we have also considered a number of other factors. The first factor considered is barriers to entry. We find that while barriers to entry into processing at the abattoir level exist, there is little to indicate that the refusal increases them or keeps them from decreasing. The next factor considered is the likelihood of an increase in the price of processed chicken. We find that there are good reasons to doubt that any increase in costs incurred by processors as a result of increased competition for birds can be readily passed on to consumers. Given the level of demand, it is impossible to sustain an increase in the price of a product without decreasing the quantity of the product offered in the market. Processors can only indirectly influence the supply of chickens through the regulatory process in which they constitute only one group of stakeholders.

**473** With respect to the effect of the refusal to deal on further processors, we find that this does not constitute an adverse effect on competition. If the Applicant is able to replace the Respondents' birds, these processors will not be affected by the refusal. If the Applicant is obliged to reduce the amount it supplies to some further processors, alternative sources of supply exist. In this regard, it is important to re-emphasize that the refusal does not restrict the supply of chickens coming to market. Only the marketing boards can do that. In the event that some of the complaining further processors were to suffer some form of competitive disadvantage, there remains the question of the significance of this to the market as a whole. The Applicant failed to adduce evidence regarding the competitive significance of the complaining further processors. Given the absence of evidence regarding the significance of these market participants from the perspective of competition in the market, we cannot draw the inference that harm suffered by them constitutes an adverse effect on competition in the market.

**474** The Applicant has failed to establish that it is likely that its customers will experience a disruption in supply and a reduction in quality. There are several plausible scenarios in which there are no adverse effects on complaining customers as a result of the refusal. In the event that some of the Applicant's customers actually do experience a decline in the quality of service or a disruption of service that is beyond the adaptation that is part of the normal competitive process, this effect would be confined to a very small fraction of the market and, because of the paucity of evidence in this regard, would not mean that the effect on competition could be qualified as "adverse" from the perspective of the market as a whole.

**475** Based on the above comparative assessment of the market with the refusal to deal and that same market without the refusal to deal, we find that the Applicant has failed to establish that the refusal to deal is having or is likely to have an adverse effect on competition in the market. None of the factors discussed above, taken individually, support a conclusion that the Respondents' refusal is having or is likely to have an adverse effect on competition in the market. We are also of the view that, taken together, these factors lead to the same result. We find that, as a result of the refusal to deal, Olymel would not be placed in a position of created, enhanced or preserved market power. Instead the post-refusal market situation would be fluid, with the potential for a range of possible shifts in market share and changes in market concentration that are ambiguous in their implied effect on competition and, in any case, so small that they would normally pass without notice.

**476** We note that earlier in these reasons, we developed a number of different scenarios to assist us in our analysis under paragraph 75(1)(*e*). We have found that, in all cases, there would be no adverse effect on competition. It is therefore unnecessary to determine which of the scenarios is most likely. The evidence on many material factors is not conclusive. For instance, we do not know if the ACA plant in Nova Scotia will expand and if it does, whether Maple Lodge will be involved. Nor do we know whether or when the Sunnymel partnership will build its proposed New Brunswick plant. We would be speculating on such matters. We are, however, as stated earlier,

satisfied on the whole of the evidence that the Applicant will likely succeed in obtaining supply to replace at least some of the Respondents' chickens. Therefore to the extent that a finding of a likely scenario is required, we are of the view that the scenarios which provide for the Applicant's being able to replace some of the Respondents' chickens are, on a balance of probabilities, more likely.

**477** Finally, we agree with the Respondents' contention and with the evidence of Ms. Sanderson who is of the opinion that, while the refusal does not have or is not likely to have an adverse effect on competition in the relevant market, a remedial order might have such an effect. The processor allocation systems maintained by provincial marketing boards limit intra-provincial competition for live birds. The allocation systems have the effect of fixing the share of the provincial slaughter accounted for by each abattoir in the province. This reduces the ability of one abattoir to attract business from another. A way around this is for an abattoir to purchase live birds from another province, but processors have generally been reluctant to do this on a significant scale. The tacit arrangement to avoid interprovincial competition for live birds has been justified, as arrangements of this nature so often are, by the argument that interprovincial competition for live birds would raise their price and this would be ruinous to processors. In our view, an attempt by the Applicant to acquire live birds in Quebec can be viewed as a departure from the tacit arrangement not to compete interprovincially for live birds. From this perspective, a remedial order that ties the Respondents' birds to the Applicant and to New Brunswick would be anti-competitive in all of the circumstances.

## VII. CONCLUSIONS

**478** For the above reasons, we find that:

(a) The Applicant has established that it is substantially affected in its business due to its inability to obtain adequate supplies of a product anywhere in a market on usual trade terms;

(b) The Applicant has failed to establish that it is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market;

(c) The Applicant has established that it is willing and able to meet the usual trade terms of the suppliers of the product;

(d) The Applicant has not established that the product is in ample supply; and

(e) The Applicant has not established that the refusal to deal is having or is likely to have an adverse effect on competition in a market.

**479** As a consequence, the application will be dismissed.

**480** These reasons are confidential. To enable the Tribunal to issue a public version of these reasons, the parties shall meet and endeavour to reach agreement upon the redactions that must be made to these confidential reasons in order to protect properly confidential evidence. The parties are to jointly correspond with the Tribunal by no later than the close of the Registry on Friday, July 10, 2009 setting out their agreement and any areas of disagreement concerning the redaction of these confidential reasons.

**481** The issue of costs is reserved. The parties are to meet and endeavour to reach agreement with respect to costs. On or before Monday, July 20, 2009, they should communicate with the Registry in order to advise as to whether they require any further time in order to attempt to agree on costs. If there is no agreement, the Tribunal will receive written submissions as to costs, as it will more particularly direct.

**FOR THESE REASONS, THE TRIBUNAL ORDERS THAT:**

**482** The application is dismissed.

**483** The issue of costs is reserved. On or before Monday, July 20, 2009, the parties shall communicate with the Registry in order to advise as to whether they require any further time in order to attempt to agree on costs.

**484** On or before Friday, July 10, 2009, the parties are to jointly correspond with the Tribunal setting out their agreement and any areas of disagreement concerning the redaction of these confidential reasons.

DATED at Ottawa, this 8th day of June 2009

SIGNED on behalf of the Tribunal by the panel members

(s) Edmond P. Blanchard

(s) Henri Lanctôt

(s) P. André Gervais

* * * * *

**SCHEDULE A**

The Applicant's Experts

*Dr. Richard Barichello*

Dr. Richard Barichello is an associate professor at the University of British Columbia where he teaches in the areas of agricultural policy, food markets and international agricultural development. He was qualified as an expert in the field of agricultural economics with a specialization in regulated markets, especially supply management, quota markets, trade policy and the analysis of government policy. Dr. Barichello testified about the origins and purpose of supply management in the poultry industry and gave his view that the underlying motivation of the supply management system was the protection of the producer. He described the regulations governing the supply management system and described the workings of that system including quota setting and allocation, import control, and price control. He spoke about the barriers to entry in chicken production and he provided his view that competition among producers was limited. He also testified with respect to premiums and the importance of assured continued supply for chicken processors.

*Dr. Roger Ware*

Dr. Roger Ware is a professor of economics at Queen's University. He was qualified as an expert in the areas of economics, competition policy and industrial organization, including market definition and competitive behaviour of firms. Dr. Ware opined on the product market and geographic market for both the 75(1)(*a*) analysis and the 75(1)(*e*) analysis. In respect of paragraph 75(1)(*a*) of the Act, he referred to the product as being live chickens. Dr. Ware acknowledged the difficulty in obtaining birds that would meet the size and quality requirements of the Applicant's customers. As for the geographic market under paragraph 75(1)(*a*), Dr. Ware gave his opinion that because of high transportation costs and high premiums to attract Quebec farmers already bound by contracts with Quebec processors, it was neither economic nor efficient for the Applicant to replace the Respondents' supply with supply from greater distances in Quebec.

In respect of paragraph 75(1)(*e*), Dr. Ware was of the opinion that the product market was processed chickens and that the geographic market consisted of the Maritimes and Quebec. Dr. Ware also testified with respect to the magnitude and dimensions of adverse effects on competition as a result of the refusal to deal. Dr. Ware opined that the increase in market power of Olymel in the processed chicken market would inevitably lead to higher prices and worsening conditions in other dimensions for customers.

*Grant Robinson*

Mr. Grant Robinson is a chartered accountant who has worked as an outsource chief financial officer for Maple Lodge. He was qualified to give evidence as an accountant, including his expert opinion on the area of the chicken processing industry. Mr. Robinson developed the following four scenarios to assist the Tribunal in understanding the impact of the removal of the Respondents' birds on the Applicant's operations:

i. loss of the Respondents' chickens;

ii. replacement of the Respondents' birds with birds from Quebec;

iii. loss of the Respondents' birds and Nova Scotia birds; and

iv. replacement of the Respondents' birds and loss of Nova Scotia birds.

He provided his view that the Applicant would be substantially affected in its business in all of the abovementioned scenarios. In order to develop his scenarios, Mr. Robinson made assumptions regarding transportation costs, shrink, DOAs and premiums which would have to be paid by the Applicant to source replacement supply in Quebec.

**The Applicant's Lay Witnesses**

*Yves Landry*

Yves Landry is the general manager of the St-François Plant. He testified about the plant's operations, the requirements of Nadeau's customers and Nadeau's arrangements with its customers. He talked about the range of birds supplied by the Respondents to Nadeau and their refusal to deal. He stated that Nadeau began to receive 25,000 additional birds per week from Nova Scotia in early June 2008 and that on September 15, 2008, Nadeau began to receive 6,250 additional chickens per week from Nova Scotia. He testified that one of the reasons why Nadeau had not made extensive efforts to procure supply in Quebec was the concern that those efforts would lead to a premium war. He also testified about Nadeau's efforts to procure chickens from Quebec. He spoke about Nadeau's transportation costs and DOAs.

*Denise Boucher*

Denise Boucher is the office manager at the St-François Plant. She is responsible for assembling financial data and is familiar with the records and the operations of the St-François Plant. Ms. Boucher's evidence consisted of adducing a number of financial documents into the record.

*Anthony Tavares*

Anthony Tavares is the former chief executive officer of Maple Lodge and former president of Nadeau. Mr. Tavares described the supply management system and Nadeau's operations in New Brunswick. He spoke about New Brunswick producers and chicken production in New Brunswick. Mr. Tavares also testified with respect to the Respondents' threat of the removal of their birds from the Applicant and of the Respondents' termination of supply. Mr. Tavares referred to the substantial detrimental effect the refusal to deal would have on the Applicant and to the difficulty the Applicant would have in replacing the Respondents' chickens. Mr. Tavares spoke about the current situation and indicated that the Applicant was willing to continue to meet all of the usual trade terms and to pay fair market price to the Respondents for the continuation of supply of live chickens.

*John Feenstra*

John Feenstra was the general manager of Nadeau from 1989 to 2006. He talked about Nadeau's initial attempts to obtain supply from New Brunswick producers in the early 1990s, the chicken industry including the legislative

scheme in place in New Brunswick and the operations of the St-François Plant. He testified about Nadeau's negotiations with Westco regarding the purchase of the St-François Plant and the effect on Nadeau's business of the Respondents' refusal to supply. Mr. Feenstra explained that an "all-out premium war" would be created if Nadeau were required to purchase chickens from Quebec.

*Tina Ouellette*

Tina Ouellette is part of the procurement team at the St-François Plant. She testified about her role in the procurement effort to source live chickens from Quebec. She indicated that she was charged with making the initial telephone calls to Quebec producers for the purpose of inquiring as to whether or not they would be interested in meeting with a representative from Nadeau to discuss the possibility of supplying the St-François Plant with live chickens. Ms. Ouellette described the procedure she followed when making the calls to producers. She stated that she contacted 454 producers and that 67 producers were interested in meeting with a Nadeau procurement representative. Ms. Ouellette also indicated that a number of producers could not be reached for a variety of reasons and that others could not supply the Applicant because they produced other types of poultry or had sold their quota.

*Léonard Viel*

Léonard Viel is the manager of sales, transportation and the garage at the St-François Plant. He stated that he was asked to assist the procurement team to attempt to source chickens from Quebec when another member of the procurement team was on vacation. He testified with respect to his part of the procurement effort, which was to meet with producers who had indicated to Ms. Ouellette that they may be interested in supplying Nadeau with live chickens. He also outlined the pricing arrangements sought by potential Quebec producers before they would consider moving their production to the St-François Plant and the volume of live chickens they were willing to supply the Applicant.

*Réjean Plourde*

Réjean Plourde is part of the procurement team at Nadeau. He testified with respect to his part of the procurement effort, which was to meet with producers who had indicated to Ms. Ouellette that they may be interested in supplying the Applicant with live chickens. He also testified with respect to the instructions he received from Mr. Landry regarding his task to seek replacement supply in Quebec and stated that he did not have the authority to sign contracts. He indicated that he had met with 39 producers and that he had made detailed notes of these meetings. He testified about the pricing arrangements sought by Quebec producers before they would consider moving their production to the St-François Plant. He also testified with respect to the procedure he followed when meeting with Quebec producers.

*Guy Chevalier*

Guy Chevalier is the president of Desco, a further processor and distributor of chickens. He stated that Desco competes directly with Olymel and Exceldor in the Quebec market and that as a result it cannot purchase fresh-killed chickens from them at reasonable prices. He further stated that Desco has no difficulty obtaining supply at reasonable prices from Nadeau. Mr. Chevalier indicated that he purchased processed chickens from the United States by purchasing importation quotas from processors that did not utilize them. He further testified about the procedure applicable to processors seeking to obtain supplementary importation quotas from the CFC.

*Terry Ellis*

Terry Ellis is the president and a major shareholder of Sunchef, a further processor located in Quebec. He described the nature of Sunchef's business and the contractual relationship between Sunchef and Nadeau. He stated that Sunchef entered into a contractual relationship with Nadeau in 2007 in order to ensure sufficient supply for its biggest customer. He further stated that, since their arrangement came into effect, the birds supplied by

Nadeau had been of high quality and of the type and size requested. Mr. Ellis also indicated that Olymel was unwilling to supply fresh-killed chickens to Sunchef at a reasonable price and that although he currently purchased processed chickens from Exceldor, it could not meet all of its needs. Mr. Ellis stated that Nadeau had always been an effective competitor to Exceldor and Olymel and said that if Nadeau's supplies of live chickens were cut off or curtailed, its ability to compete with Exceldor and Olymel would be reduced or eliminated. According to Mr. Ellis, this would have a major adverse effect at Sunchef's level of the market. He further stated that should Nadeau go out of business or be acquired by Olymel, he foresaw that Sunchef's supplies would be reduced or cut off and that he would no longer be able to continue in that business.

*Lyndsay Gazzard*

Lyndsay Gazzard is the senior purchasing manager of UPGC. She testified about UPGC's long and mutually beneficial relationship with Nadeau. She stated that Nadeau had for a long time supplied all of the fresh chickens used in KFC restaurants in New Brunswick, and, in the last two years, supplied 98% of KFC restaurants in Nova Scotia and Prince Edward Island. She further stated that UPGC had no difficulty obtaining all of its requirements for Atlantic Canada from Nadeau at a reasonable price. She testified about UPGC's purchasing requirements and trends, including procurement from Olymel and Exceldor. She also testified about the problems arising from Westco's change in production size. Lastly, she indicated that she remained concerned about UPGC's ability to obtain birds of the required size and specifications in the event that live chicken supply to Nadeau was disrupted.

*Corey Goodman*

Corey Goodman is the chief purchasing officer for Priszm LP and the general manager of UPGC. Priszm operates about 45 KFC restaurants in New Brunswick and Nova Scotia, and UPGC is a non-profit association that operates as the purchasing agent for all KFC restaurants in Canada. Mr. Goodman stated that he was concerned about the impact of any reduction in the supply of live chickens to Nadeau, as it would result in increased costs, reduced freshness and operational complexities with respect to obtaining replacement supply. He further stated that Olymel and Exceldor were already very powerful players in the market and that with Nadeau weakened or gone, there would be even less competition.

*Debbie Goodz*

Debbie Goodz is the president and CEO of Riverview which is a further processor located in Ste-Sophie, Quebec. Ms. Goodz described Riverview's business and its supply requirements and specifications. She indicated that Riverview purchased the vast majority of its supplies from the Applicant and that it had always been content with the Applicant's service, quality and price. Ms. Goodz stated that her ability to continue to supply her specialized product at an acceptable price depended on her ability to continue to obtain supplies from the Applicant. She indicated that she was unable to obtain chickens from Olymel and that she could not obtain alternative supplies from elsewhere because of transportation issues, price concerns and size requirements. Ms. Goodz also indicated that she had never complained to the CFC regarding the unavailability of supplies. Ms. Goodz expressed her view regarding the current state of competition and stated that if the Applicant's supplies of live chickens were cut off or curtailed, its ability to compete with Olymel would be reduced or eliminated, thus causing a major adverse effect at Riverview's level of the market.

*Jeffrey Lloyd McHaffie*

Jeffrey Lloyd McHaffie is a consultant to Puddy and its *de facto* vice president, in charge of sales and purchases of poultry products. He has over 20 years' experience in the poultry industry. Puddy is a further processor of fresh-killed chickens, specializing in "case-ready" chicken for the retail supermarket. Mr. McHaffie testified about Puddy's strict specifications for its incoming supplies of chickens and stated that Nadeau has consistently been able to meet its exacting quality and freshness requirements. He also testified about Puddy's difficulties in obtaining supply from Ontario and western Canada and he discussed the service and quality problems associated with Olymel's products.

*Kevin Thompson*

Kevin Thompson is the executive director of the Association of Ontario Chicken Processors ("AOCP"). He has been involved with the Ontario chicken industry since 1978. He stated that maintaining a supply of live chicken was essential for a processor as without supply, processors become less competitive and less able to meet the needs of their customers. He described the plant supply allocation systems in place in Ontario and Quebec and the supply management system in place in Canada. He stated that it was disconcerting to the AOCP that Nadeau's only alternative may be to enter into an interprovincial premium war to try to replace 50% of its live supply if the Respondents were able to unilaterally withdraw their live chicken production from Nadeau. He testified on the detrimental effects of interprovincial trade via premium wars and concluded that the consequences of a premium war for the processor community as a whole, its customers and for consumers were all negative. He indicated that the interprovincial movement of live chickens is really a weakness in the regulated supply system and one that must ultimately be addressed if supply management is to be sustained. He further stated that if Nadeau elected not to source chickens from Quebec or if it decided to close or to sell to one of the other processors in the region, there would be a substantial adverse effect on competition in the marketplace in Quebec and eastern Canada.

*Bruce McCullagh*

Bruce McCullagh is the senior vice president and general manager of poultry operations at Maple Leaf. He has over 12 years' experience in the poultry industry. He described the nature of the supply management system including the manner in which the system shields chicken producers from competition. He also testified about the plant supply allocation systems in place in Ontario and Quebec. Mr. McCullagh discussed the detrimental effects of interprovincial trade including the creation of unsustainable premium wars. He stated that interprovincial trade is a systemic problem in the poultry industry and that the government needs to look at possible amendments to the current regulatory regime to address this issue. Mr. McCullagh also testified about Maple Leaf's involvement in the interprovincial procurement of live chickens.

*Andre Merks*

Andre Merks is a Nova Scotia producer. He has been farming broiler chicken, turkeys and layer eggs for over thirty years. Mr. Merks spoke of the "handshake deal" he entered into with the Applicant following the closure of the Maple Leaf plant in Nova Scotia. He discussed the reasons why he had decided to send his production to the Applicant instead of ACA. Mr. Merks spoke of the concerns expressed by Nova Scotia producers with respect to the chicken industry in Nova Scotia. He also testified with respect to a meeting that took place in October of 2008 between Nova Scotia producers and Maple Lodge concerning Maple Lodge's possible involvement in the modernization of the ACA plant.

*Michael Donahue*

Michael Donahue is the vice-president of Agri Stats, a company that offers benchmarking services for the poultry industry across North America. He described the procedure used by Agri Stats to collect and analyze data. Mr. Donahue explained the report that he had generated for the St-François Plant and indicated that, in the areas he had examined the St-François Plant would be competitive with the Canadian industry.

**Westco's Expert**

*Dr. Margaret Sanderson*

Margaret Sanderson has held a number of positions with the Competition Bureau including the position of Assistant Deputy Director of Investigation and Research for the Bureau's Economics and International Affairs Branch. Ms. Sanderson was qualified as an expert in the area of economics, competition policy and industrial organization, including market definition and the competitive behaviour of firms. Ms. Sanderson testified with respect to

paragraphs 75(1)(*a*) and 75(1)(*e*) of the Act. With respect to paragraph 75(1)(*a*), Ms. Sanderson expressed the opinion that the issue was not in dispute and that the product market was live chickens. To determine whether or not the Applicant would be substantially affected in its business, Ms. Sanderson looked at the cost of replacing the Respondents' birds with birds from Quebec. She was of the opinion that the Applicant could source live chickens from producers in Quebec without being substantially affected and thus concluded that Quebec-based chickens were substitutes for the live chickens supplied by the Respondents.

In respect of paragraph 75(1)(*e*), Ms. Sanderson was of the opinion that the relevant geographic market for determining whether there was an adverse effect on competition was at least as large as Ontario, Quebec and the Maritimes. She examined Nadeau's and Olymel's historic shipping patterns, shipping distances, transportation costs and prices to make this determination. In Ms. Sanderson's view, the refusal would not provide Olymel with market power and would not cause an adverse effect on competition.

**Westco's Lay Witnesses**

*Thomas Soucy*

Thomas Soucy is the president and chief executive officer of Westco. He testified about Westco's activities and operations. He discussed the consolidation of production quota in New Brunswick and Westco's plans for complete vertical integration. He testified about Westco's business relationship with the Applicant and provided his view that the Applicant had abused its monopoly power in New Brunswick. Mr. Soucy described the conception of Sunnymel and discussed Sunnymel's plan to acquire or construct a new processing plant in New Brunswick. He also testified about Westco's negotiations with the Applicant regarding the purchase of the St-François Plant and with respect to the Applicant's ability to obtain replacement supply of live chickens in Quebec.

*Bertin Cyr*

Bertin Cyr is a Westco shareholder and has been chairman of Westco's Board of Directors since 2003. He testified about the history of the corporation as well as its plans for complete vertical integration. Mr. Cyr described the steps toward vertical integration that had been taken by Westco in the past and he provided his view that complete vertical integration, by acquiring an existing processing plant or by building a new one, was Westco's only way to ensure its long term survival in the poultry industry. Mr. Cyr testified about Westco's business relationship with the Applicant and indicated that Westco's desire to vertically integrate was also motivated by the fact that the Applicant had abused its position. Mr. Cyr also spoke of Westco's past attempts to enter into a partnership with the Applicant.

*Yvan Brodeur*

Yvan Brodeur is vice-president of procurement at Olymel. He described the nature of Olymel's business including its processing and procurement activities. He described the supply allocation system in place in Quebec and he discussed interprovincial trade of live chickens. Mr. Brodeur also spoke about the conditions of purchase of both live and processed chickens. He discussed transportation costs associated with transporting live chickens as well as transportation costs associated with transporting processed chickens. Mr. Brodeur also testified about Olymel's clients and their location from Olymel's processing plants.

*Julie Desroches*

Julie Desroches is an environmental project officer at Olymel. She testified about her involvement in Sunnymel's project to build a new slaughterhouse in New Brunswick and the steps that had been taken to date in the construction project. She also spoke of the circumstances which had led to the project being delayed and she discussed Sunnymel's future construction plans for the new slaughterhouse in New Brunswick.

*Richard Wittenberg*

Richard Wittenberg is a chicken producer in Nova Scotia. He testified on the closure of the Maple Leaf plant in Nova Scotia and spoke of the "handshake" agreement he entered into with the Applicant following the closure of that plant. He also testified with respect to a meeting that took place on October 15, 2008, between Nova Scotia producers and Maple Lodge concerning Maple Lodge's possible involvement in the modernization of the ACA plant.

**Dynaco's Lay Witnesses**

*Gilles Lapointe*

Gilles Lapointe is the director of finance for Dynaco. He testified with respect to Dynaco's corporate structure and the nature of its business. He described Dynaco's production quota and indicated that it consisted of 6.22% of New Brunswick's total production quota. Mr. Lapointe testified about Dynaco's decision to cease supplying the Applicant with live chickens. He also described how co-operatives operate and why it was beneficial for Dynaco to send its production to Sunnymel.

*Rémi Faucher*

Rémi Faucher is the general manager of Dynaco. He testified about Dynaco's corporate structure and the nature of its business and chicken production. He spoke of the reason why Dynaco decided to cease supplying the Applicant with live chickens and stated that it was essentially based on the deterioration of its business relationship with the Applicant and on the business opportunities offered by Sunnymel.

**Acadia's Lay Witnesses**

*Rémi Faucher*

Rémi Faucher is the former president and director of Acadia. He testified about Acadia's corporate structure and the nature of Acadia's business. Mr. Faucher spoke of Acadia's quota and indicated that it consisted of 16% of New Brunswick's total production quota. He also testified about Acadia's decision to cease supplying the Applicant with live chickens and indicated that it was a business decision. He also spoke about the financial advantages involved in sending Acadia's production to a processing facility owned by Olymel.

**SCHEDULE B**

Schedule to the *Regulations Amending the Canadian Chicken Marketing Quota Regulations*, SOR/2009-4

SCHEDULE *(Sections 1, 5 and 7 to 10)*

LIMITS FOR PRODUCTION AND MARKETING OF CHICKEN

FOR THE PERIOD BEGINNING ON JANUARY 4, 2009

AND ENDING ON FEBRUARY 28, 2009

| Item. | Column 1<br>Province | Column 2<br>Production Subject to Federal and Provincial Quotas (in live weight) (kg) | Column 3<br>Production Subject to Federal and Provincial Market Development Quotas (in live weight) (kg) |
|---|---|---|---|
| 1. | Ont. | 65,725,554 | 2,920,000 |
| 2. | Que. | 53,105,045 | 5,400,000 |
| 3. | N.S. | 7,014,256 | 0 |
| 4. | N.B | 5,716,109 | 0 |
| 5. | Man. | 8,390,996 | 394,950 |
| 6. | B.C | 29,212,807 | 4,089,793 |
| 7. | P.E.I | 754,057 | 0 |
| 8. | Sask. | 7,015,829 | 982,216 |
| 9. | Alta. | 18,430,359 | 400,00 |
| 10. | Nfld. and Lab. | 2,825,158 | 0 |
| Total | | 198,190,170 | 14,186,959 |

ANNEXE *(articles 1, 5 et 7 à 10)*

LIMITES DE PRODUCTION ET DE COMMERCIALISATION DU POULET

POUR LA PÉRIODE COMMENÇANT LE 4 JANVIER 2009

ET SE TERMINANT LE 28 FÉVRIER 2009

| Article | Colonne 1<br>Province | Colonne 2<br>Production assujettie aux contingents fédéraux et provinciaux (en poids vif) (kg) | Colonne 3<br>Production assujettie aux contingents fédéraux et provinciaux d'expansion du marché (en poids vif) (kg) |
|---|---|---|---|
| 1. | Ont. | 65 725 554 | 2 920 000 |
| 2. | Qc | 53 105 045 | 5 400 000 |
| 3. | N.-É. | 7 014 256 | 0 |
| 4. | N.-B | 5 716 109 | 0 |
| 5. | Man. | 8 390 996 | 394 950 |
| 6. | C.-B | 29 212 807 | 4 089 793 |
| 7. | Î.-P.-É | 754 057 | 0 |
| 8. | Sask. | 7 015 829 | 982 216 |
| 9. | Alb. | 18 430 359 | 400 00 |
| 10. | T.-N.-L. | 2 825 158 | 0 |
| Total | | 198,190,170 | 14 186 959 |

**SCHEDULE C**

Sections 1 and 2 of Order I - Chicken Farmers of New Brunswick Marketing Plan

1. The object of the marketing plan is to control the number of chickens raised for marketing within the province, in such a manner:

   (a) As to ensure there is an adequate supply of New Brunswick grown chicken available to the consumer.

   (b) To provide an opportunity for the maximum number of residents in New Brunswick to earn a living in the marketing of chicken.

   (c) To ensure a reasonable rate of return from the sale of chicken and to ensure a continuity of supply.

   (d) To avoid the development of monopolies which could result in excessive cost to the consumers of chicken.

   (e) To avoid a curtailment of the overall supply in the event one or more producers cease to market chicken.

2. There shall be established a periodic marketing limit being the number of kilograms of chicken live weight which can be raised for marketing within the Province in conformity with the objectives of the plan.

* * *

1. Le but du plan de commercialisation est de réglementer l'élevage du poulet destiné à la commercialisation dans la province, de façon à :

   a) assurer au consommateur un approvisionnement adéquat de poulets produits au Nouveau-Brunswick,

   b) offrir à un nombre maximum de résidents du Nouveau-Brunswick l'occasion de gagner leur vie dans la commercialisation du poulet,

   c) assurer un profit raisonnable de la vente de poulets et assurer un approvisionnement continuel.

   d) éviter la réalisation de monopoles qui pourraient entraîner un coût excessif au consommateur, et

   e) éviter une réduction de l'approvisionnement global advenant le retrait d'un ou de plusieurs producteurs de la commercialisation du poulet.

2. Une limite de commercialisation périodique est établie, correspondant au nombre de kilogrammes (poids vif) de poulets pouvant être élevés à des fins de commercialisation dans la province, conformément aux objectifs du plan.

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1 We note that, where the words "Tribunal" or "we" are used and the decision relates to a matter of law alone, that decision has been made solely by the presiding judicial member.

2 Sections 3.5 and 3.6 of the *Merger Enforcement Guidelines* state as follows:

> **3.5** The market definition analysis begins by postulating a candidate market for each product of the merging parties. For each candidate market, the analysis proceeds by determining whether a hypothetical monopolist controlling the group of products in that candidate market would be able to impose a five per cent price increase assuming the terms of sale of all other products remained constant. If the price increase would likely cause buyers to switch their purchases to other products in sufficient quantity to render the price increase unprofitable, the postulated candidate market is not the relevant market, and the next-best substitute is added to the candidate market. The analysis then repeats by determining whether a hypothetical monopolist controlling the set of products in the expanded candidate market would be able to profitably impose a five per cent price increase. This process continues until the point at which the hypothetical monopolist would impose and sustain the price increase for at least one product of the merging parties in the candidate market. The

smallest set of products in which the price increase can be sustained is defined as the relevant product market.

**3.6** The same general approach applies to assessing the geographic scope of the market. In this case, an initial candidate market is proposed for each location where the merging parties produce or sell the relevant products. As above, if buyers are likely to switch their purchases to sellers in more distant locations in sufficient quantities to render a five per cent price increase by a hypothetical monopolist unprofitable, the location that is the next-best substitute is added to the candidate market. This process continues until the smallest set of areas over which a hypothetical monopolist would impose and sustain the price increase is identified.

(emphasis added)

**3** Both Ms. Sanderson and Dr. Ware used market shares based on slaughter; shares of further processors are therefore not included in their calculations.

**4** For purposes of calculating the HHI, the "Other Quebec" processors are treated as one. If there is more than one, this results in a slight overstatement of the HHI. "Other Ontario" processors are treated as three equal sized processors. The reason for this is that the smallest Ontario processor that is identified (Grand River) processes 200,000 birds per week. Unidentified Ontario processors slaughter a total of 300,000 birds per week. It is reasonable to assume that the largest unidentified processor is smaller than Grand River. Given this, the total slaughter by unidentified Ontario processors could be allocated in a variety of ways. The assumption made here is that three unidentified Ontario processors are each slaughtering 100,000 birds per week. Given the very small portion of the market involved, the assumption made regarding the composition of the unidentified segment of the market makes very little difference to the value of the HHI.

**5** See s. 4.12 of the *Merger Enforcement Guidelines*.

**6** He explained that the pool "...provides some flexibility for producers to choose the processor with whom they wish to do business as well as allowing some differential growth among processors" and that there "...is no long-term requirement for a producer to continue to sell to the same processor."

**End of Document**

# R. v. Bradshaw, [2017] 1 S.C.R. 865

Supreme Court Reports

Supreme Court of Canada

Present: McLachlin C.J. and Abella, Moldaver, Karakatsanis, Wagner, Côté and Brown JJ.

Heard: November 3, 2016;

Judgment: June 29, 2017.

File No.: 36537.

**[2017] 1 S.C.R. 865** | [2017] 1 R.C.S. 865 | [2017] S.C.J. No. 35 | [2017] A.C.S. no 35 | 2017 SCC 35

Her Majesty The Queen Appellant; v. Robert David Nicholas Bradshaw Respondent, and Attorney General of Ontario, British Columbia Civil Liberties Association and Criminal Lawyers' Association of Ontario Interveners

(188 paras.)

**Appeal From:**

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

## Case Summary

**Catchwords:**

**Criminal law — Evidence — Hearsay — Admissibility — Principled exception to hearsay rule — Trial judge admitting co-accused's hearsay statement into evidence — When can trial judge rely on corroborative evidence to conclude that threshold reliability of hearsay statement is established.**

**Summary:**

Two people were shot to death. Suspected by police, T became the target of a Mr. Big investigation, during which he told an undercover officer that he shot both victims. He then told Mr. Big that he had shot one victim and that B had shot the other. T was arrested. When he later re-enacted the murders for police, he implicated B in both. T and B were charged with two counts of first degree murder and T pled guilty to second degree murder. Because T refused to give sworn testimony at B's trial, the Crown sought to admit into evidence T's re-enactment, which had been video-recorded. Following a *voir dire*, the trial judge admitted the re-enactment, under the principled exception to the hearsay rule. A jury convicted B on two counts of first degree murder. The Court of Appeal allowed the appeal, set aside B's convictions and ordered a new trial.

[page866]

*Held* (Moldaver and Côté JJ. dissenting): The appeal should be dismissed.

*Per* McLachlin C.J. and Abella, Karakatsanis, Wagner and Brown JJ.: Hearsay evidence is presumptively inadmissible because it is often difficult for the trier of fact to assess its truth. However, it can be admitted under the principled exception if the criteria of necessity and threshold reliability are met on a balance of probabilities.

In this case, the necessity of the hearsay evidence is established because T refused to testify. Thus, its admissibility rests on whether threshold reliability is met. Threshold reliability is established when the hearsay is

sufficiently reliable to overcome the dangers arising from the difficulty of testing it. The hearsay dangers relate to the difficulties of assessing the declarant's perception, memory, narration or sincerity. These dangers can be overcome by showing that (1) there are adequate substitutes for testing truth and accuracy (procedural reliability) or (2) that there are sufficient circumstantial or evidentiary guarantees that the statement is inherently trustworthy (substantive reliability). Substantive reliability is established when the statement is unlikely to change under cross-examination. To determine whether substantive reliability is established, the trial judge can consider the circumstances in which the statement was made and evidence (if any) that corroborates or conflicts with the statement.

A trial judge can only rely on corroborative evidence to establish substantive reliability if it shows, when considered as a whole and in the circumstances of the case, that the only likely explanation for the hearsay statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement.

First, corroborative evidence must go to the truthfulness or accuracy of the material aspects of the hearsay statement. Since hearsay is tendered for the truth of its contents, corroborative evidence must go to the truthfulness or accuracy of the content of the statement that the moving party seeks to rely on.

Second, corroborative evidence must assist in overcoming the specific hearsay dangers raised by the tendered statement. Corroborative evidence does so if its combined effect, when considered in the circumstances of the case, shows that the only likely explanation for the hearsay statement is the declarant's truthfulness about, [page867] or the accuracy of, the material aspects of the statement. Otherwise, alternative explanations for the statement that could have been elicited or probed through cross-examination, and the hearsay dangers, persist. Corroborative evidence is of assistance in establishing substantive reliability if it shows that alternative explanations for the statement are unavailable. In contrast, corroborative evidence that is equally consistent with the truthfulness and accuracy of the statement as well as another hypothesis is of no assistance. To be relied on for the purpose of rejecting alternative hypotheses, corroborative evidence must itself be trustworthy.

In sum, to determine whether corroborative evidence is of assistance in the substantive reliability inquiry, a trial judge should: (1) identify the material aspects of the hearsay statement that are tendered for their truth; (2) identify the specific hearsay dangers raised by those aspects of the statement in the particular circumstances of the case; (3) based on the circumstances and these dangers, consider alternative, even speculative, explanations for the statement; and (4) determine whether, given the circumstances of the case, the corroborative evidence led at the *voir dire* rules out these alternative explanations such that the only remaining likely explanation for the statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement.

The trial judge erred in relying significantly on corroborative evidence that was of no assistance in establishing substantive reliability to deem the re-enactment statement admissible. The material aspect of the statement was T's assertion that B participated in the murders. The specific danger raised by T's statement was the inability of the trier of fact to assess whether T lied about B's participation in the murders. T gave inconsistent statements about B's participation. He also had a significant motive to lie to reduce his own culpability. Furthermore, T was a *Vetrovec* witness, a witness who cannot be trusted due to his unsavoury character. Given the hearsay dangers presented by the re-enactment statement, an alternative explanation is that T lied about B's participation in the murders. Therefore, corroborative evidence will only assist in establishing the substantive reliability of the re-enactment statement if it shows, when considered in the circumstances of the case, that the only likely explanation is that T was truthful about B's participation. Considered as a whole, the corroborative evidence relied on by the trial judge did not meet this standard. For example, while the weather evidence and forensic evidence showed that T accurately described the [page868] way the murders unfolded and the weather on the nights of the murders, this evidence does not mitigate the danger that T lied about B's participation. Furthermore, while there are recordings of B admitting that he participated in the murders, there are concerns about the trustworthiness of these admissions. Much of the corroborative evidence relied on by the trial judge was probative of B's guilt, and thus could be considered by the trier of fact in the trial on the merits, but none of it was of assistance in establishing the threshold reliability of the re-enactment statement.

The threshold reliability of the hearsay statement is not otherwise established. Jury warnings about the dangers of hearsay evidence or *Vetrovec* testimony do not provide a satisfactory basis for the trier of fact to rationally

evaluate the truth and accuracy of the hearsay statement. Instructing a jury on how to evaluate a statement that it lacks the means to evaluate does not address the hearsay dangers that underlie the exclusionary rule. Given that the trier of fact could not adequately test the trustworthiness of T's statement, and there were no circumstances or corroborative evidence showing that this statement was inherently trustworthy, it should not have been admitted into evidence.

*Per* Moldaver and Côté JJ. (dissenting): The trial judge did not err in admitting T's re-enactment. His ruling was amply supported by the record and is entitled to deference.

The principled approach to hearsay recognizes that threshold reliability can be met in three ways: (1) where a statement has sufficient features of substantive reliability; (2) where the statement has adequate features of procedural reliability; or (3) where the statement does not satisfy either of the first two ways, but incorporates features of both which, in combination, justify its admission. Under this third way, where a statement has a sufficient level of trustworthiness, relative to the strength of the procedural safeguards for the trier of fact to evaluate its ultimate reliability, the statement is safe to admit.

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In this case, T's re-enactment was admissible under the third way of establishing threshold reliability. The hearsay dangers at issue -- sincerity along with memory and perception -- were sufficiently overcome by powerful corroborative evidence indicating the statement's trustworthiness and a number of procedural safeguards that provided the jury with the tools it needed to evaluate its truth and accuracy.

In reaching a different conclusion, the majority has departed from the functional approach to threshold reliability by unduly restricting the extrinsic evidence that a court can consider when assessing a statement's substantive reliability and by adopting a narrow view of the procedural safeguards available at trial that can equip the jury with the tools it needs to assess the ultimate reliability of a statement.

The functional approach emphasizes that there is no bright-line distinction between factors that inform threshold and ultimate reliability. For extrinsic evidence, the inquiry is focused on whether the evidence addresses hearsay dangers by providing information about whether the statement is trustworthy. The majority's approach instead creates a threshold test within the threshold test, which unnecessarily complicates the analysis and discards extrinsic evidence that can be crucial for evaluating threshold reliability. Trial judges should be trusted to limit the scope of extrinsic evidence that can be considered in a hearsay *voir dire* on a case-by-case basis to ensure that the proceedings are not derailed.

In this unusual case, the corroborative evidence included surreptitiously recorded conversations in which B admitted his involvement in the murders, telephone records as circumstantial evidence implicating B in the murders and forensic evidence from the crime scenes confirming T's account of the details of the murders. Considered cumulatively, this evidence provides powerful support for the trustworthiness of T's re-enactment. There was also circumstantial indicia of trustworthiness, including: the fact that the re-enactment was voluntary and free flowing; that it was contrary to T's interest, in that he did not attempt to shift blame to B but instead implicated himself in two counts of first degree murder; and that T's alleged motivation to fabricate was rebutted by his prior consistent statement to Mr. Big. There is no evidence of any inducements or assurances made by the [page870] police prior to T's re-enactment, nor is there any information to suggest that T's plea to second degree murder had anything to do with his participation in the re-enactment.

As for procedural reliability, there is no principled distinction between safeguards in place at the time the hearsay statement was made and safeguards available at trial. Both enhance the ability of the trier of fact to critically evaluate the evidence. As in this case, the latter may include jury cautions, the limited admission of prior inconsistent statements that contradict the hearsay statement, requiring the Crown to call the police officers who took prior inconsistent statements as witnesses so that they can be cross-examined by defence counsel, and permitting enhanced leeway for defence counsel during closing submissions. The trial judge is uniquely positioned to adapt and implement these measures based on the specific circumstances of the case.

The majority's unwillingness to consider these various procedural safeguards relied upon by the trial judge in this case leads it to skirt the third way of establishing threshold reliability -- the one applied by the trial judge in this case -- in which features of substantive and procedural reliability may, in conjunction, justify the admission of a

hearsay statement.

In conjunction, the re-enactment's features of substantive and procedural reliability were capable of satisfying the test for threshold reliability. The trial judge made a difficult call in a close case. He was in the best position to make that call based on his assessment of the trustworthiness of the evidence and the jury's ability to evaluate it. And his analysis discloses no legal error. As a result, his ruling is entitled to deference. It is not the role of the Court to second guess the trial judge's reasonably exercised judgment from a position far removed from the trial setting. Doing so betrays both the deference owed to trial judges and the trust and confidence placed in juries to follow instructions and use their common sense and reason to evaluate evidence.

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The trial judge's refusal to admit T's prior inconsistent statement given on May 15, 2010, for the truth of its contents is also entitled to deference. The trial judge applied the correct test and considered the relevant factors in finding this statement to be inadmissible. This included the fact that the statement was not video-recorded, that it was contradicted by extrinsic evidence and that T had a strong incentive to exaggerate his involvement in the murders.

Ultimately, there is no reason to send this case back for a second trial. B had a fair trial before a properly instructed jury that was well positioned to critically evaluate the reliability of the re-enactment. Accordingly, his two convictions for first degree murder should be restored.

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By Karakatsanis J.

**Applied:** *R. v. Khelawon*, 2006 SCC 57, [2006] 2 S.C.R. 787; **referred to:** *Vetrovec v. The Queen*, [1982] 1 S.C.R. 811; *R. v. Hart*, 2014 SCC 52, [2014] 2 S.C.R. 544; *R. v. B. (K.G.)*, [1993] 1 S.C.R. 740; *R. v. Baldree*, 2013 SCC 35, [2013] 2 S.C.R. 520; *R. v. Youvarajah*, 2013 SCC 41, [2013] 2 S.C.R. 720; *R. v. Hawkins*, [1996] 3 S.C.R. 1043; *R. v. U. (F.J.)*, [1995] 3 S.C.R. 764; *R. v. Couture*, 2007 SCC 28, [2007] 2 S.C.R. 517; *R. v. Smith*, [1992] 2 S.C.R. 915; *R. v. Blackman*, 2008 SCC 37, [2008] 2 S.C.R. 298; *R. v. Starr*, 2000 SCC 40, [2000] 2 S.C.R. 144; *R. v. R. (D.)*, [1996] 2 S.C.R. 291; *R. v. Khan*, [1990] 2 S.C.R. 531; *R. v. Khela*, 2009 SCC 4, [2009] 1 S.C.R. 104; *R. v. Smith*, 2009 SCC 5, [2009] 1 S.C.R. 146; *R. v. Salah*, 2015 ONCA 23, 319 C.C.C. (3d) 373.

By Moldaver J. (dissenting)

*R. v. Baldree*, 2013 SCC 35, [2013] 2 S.C.R. 520; *R. v. Khelawon*, 2006 SCC 57, [2006] 2 S.C.R. 787; *R. v. Devine*, 2008 SCC 36, [2008] 2 S.C.R. 283; *R. v. Blackman*, 2008 SCC 37, [2008] 2 S.C.R. 298, aff'g (2006), 84 O.R. (3d) 292; *R. v. Youvarajah*, 2013 SCC 41, [2013] 2 S.C.R. 720; *R. v. Couture*, 2007 SCC 28, [2007] 2 S.C.R. 517; *R. v. Khan*, [1990] 2 S.C.R. 531; *R. v. Hawkins*, [1996] 3 S.C.R. 1043; *R. v. B. (K.G.)*, [1993] 1 S.C.R. 740; *R. v. Hamilton*, 2011 ONCA 399, 271 C.C.C. (3d) 208; *R. v. U. (F.J.)*, [1995] 3 S.C.R. 764; *R. v. Hart*, 2014 SCC 52, [2014] 2 S.C.R. 544; *R. v. Abbey*, 2009 ONCA 624, 246 C.C.C. (3d) 301; *R. v. Carroll*, 2014 ONCA 2, [page872] 304 C.C.C. (3d) 252; *R. v. McNamara (No. 1)* (1981), 56 C.C.C. (2d) 193; *R. v. R. (T.)*, 2007 ONCA 374, 85 O.R. (3d) 481; *R. v. Lowe*, 2009 BCCA 338, 274 B.C.A.C. 92; *R. v. Goodstoney*, 2007 ABCA 88, 218 C.C.C. (3d) 270; *R. v. Smith*, 2009 SCC 5, [2009] 1 S.C.R. 146; *R. v. Adjei*, 2013 ONCA 512, 309 O.A.C. 328; *R. v. Stirling*, 2008 SCC 10, [2008] 1 S.C.R. 272; *R. v. Corbett*, [1988] 1 S.C.R. 670; *R. v. Carroll*, 1999 BCCA 65, 118 B.C.A.C. 219; *R. v. Noel*, 2002 SCC 67, [2002] 3 S.C.R. 433; *R. v. S. (S.)*, 2008 ONCA 140, 232 C.C.C. (3d) 158; *R. v. Post*, 2007 BCCA 123, 217 C.C.C. (3d) 225; *R. v. Tash*, 2013 ONCA 380, 306 O.A.C. 173; *R. v. Kimberley* (2001), 56 O.R. (3d) 18.

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**History and Disposition:**

APPEAL from a judgment of the British Columbia Court of Appeal (Neilson, Bennett and Garson JJ.A.), *2015 BCCA 195*, *323 C.C.C. (3d) 475*, *372 B.C.A.C. 77*, 640 W.A.C. 77, *20 C.R. (7th) 398*, *[2015] B.C.J. No. 884* (QL), *2015 CarswellBC 1168* (WL Can.), setting aside the accused's convictions for first degree murder and ordering a new trial. Appeal dismissed, Moldaver and Côté JJ. dissenting.

## Counsel

*Margaret A. Mereigh* and *David Layton*, for the appellant.

*Richard S. Fowler*, *Q.C.*, *Eric Purtzki* and *Karin Blok*, for the respondent.

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*Greg J. Allen*, for the intervener the British Columbia Civil Liberties Association.

*Louis P. Strezos* and *Samuel Walker*, for the intervener the Criminal Lawyers' Association of Ontario.

The judgment of McLachlin C.J. and Abella, Karakatsanis, Wagner and Brown JJ. was delivered by

## KARAKATSANIS J.

## I. Introduction

**1** Hearsay is an out-of-court statement tendered for the truth of its contents. It is presumptively inadmissible because - in the absence of the opportunity to cross-examine the declarant at the time the statement is made - it is often difficult for the trier of fact to assess its truth. Thus hearsay can threaten the integrity of the trial's truth-seeking process and trial fairness. However, hearsay may exceptionally be admitted into evidence under the principled exception when it meets the criteria of necessity and threshold reliability.

**2** In this case, the Crown tendered hearsay from Roy Thielen, an accomplice, implicating Robert Bradshaw, the accused, in two murders. The trial judge ruled that this hearsay statement was admissible. The Court of Appeal allowed the appeal and ordered a new trial.

**3** The following issue arises in this appeal: When can a trial judge rely on corroborative evidence to conclude that the threshold reliability of a hearsay statement is established?

**4** In my view, corroborative evidence may be used to assess threshold reliability if it overcomes the specific hearsay dangers presented by the statement. These dangers may be overcome on the basis of corroborative evidence if it shows, when considered as a whole and in the circumstances of the [page874] case, that the only likely explanation for the hearsay statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement. The material aspects are those relied on by the moving party for the truth of their contents.

**5** Here, the hearsay statement was tendered for the truth of Thielen's claim that Bradshaw participated in the murders. The specific hearsay danger raised by Thielen's statement was the inability of the trier of fact to assess whether Thielen lied about Bradshaw's participation in the murders. In addition to the reliability dangers that are inherent in all hearsay statements, there are specific reasons to be concerned that Thielen lied. Thielen had a motive to lie to shift the blame to Bradshaw. Thielen previously said that he had shot both victims, and had not implicated Bradshaw. Furthermore, Thielen was a *Vetrovec* witness, a witness who cannot be trusted to tell the truth due to his unsavoury character (*Vetrovec v. The Queen*, *[1982] 1 S.C.R. 811*).

**6** The trial judge relied significantly on the existence of corroborative evidence to deem Thielen's statement admissible. However, the evidence he relied on did not, when considered in the circumstances of the case, show that the only likely explanation was that Thielen was truthful about Bradshaw's involvement in the murders. It did not substantially negate the possibility that Thielen lied about Bradshaw's participation in the murders. While this corroborative evidence may increase the probative value of the re-enactment statement if admitted, it is of no assistance in assessing the statement's threshold reliability. The trial judge therefore erred in relying on this corroborative evidence.

**7** Given that the trier of fact could not adequately test the trustworthiness of Thielen's statement, and there were no circumstances or corroborative evidence showing that this statement was inherently [page875] trustworthy, it should not have been admitted into evidence.

**8** For the reasons that follow, I would dismiss the appeal.

## II. Background

**9** Laura Lamoureux and Marc Bontkes were killed in March 2009, five days apart. The police suspected that Thielen was involved in both murders. They ran a Mr. Big operation targeting Thielen. In a Mr. Big operation, undercover officers recruit a suspect into a fictitious criminal organization for the purpose of eliciting a confession from him (*R. v. Hart*, *2014 SCC 52*, *[2014] 2 S.C.R. 544*, at para. 85). The officers befriend the suspect and demonstrate that membership in the criminal organization provides rewards and friendship. The suspect discovers that his membership is conditional on a confession to the crime boss, Mr. Big (*Hart*, at paras. 1-2).

**10** As part of the Mr. Big operation, Thielen went on a road trip with Cst. B., an undercover agent, in May 2010. During the road trip, Thielen told Cst. B. that he had shot both Lamoureux and Bontkes.

**11** In July 2010, Thielen met an undercover agent posing as the crime boss. During this meeting, Thielen said that he had shot Lamoureux but that "Paulie" and Michelle Motola had shot Bontkes. "Paulie" was Bradshaw's nickname.

**12** Later that day, Thielen and Bradshaw met up at the Best Western Hotel. Their conversation was recorded, but only the latter part is audible. Bradshaw said that he had shot Bontkes and had participated in both murders.

**13** Two days later, Thielen and Bradshaw met at Bothwell Park. Bradshaw discussed an unsuccessful attempt to kill Bontkes, which preceded Bontkes's actual murder in March 2009.

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**14** Thielen was arrested on July 30, 2010. He initially denied his involvement in both murders. However, when the police told Thielen that he had been the target of a Mr. Big operation, he then described the murders and identified unnamed participants. The next day, he made another statement to the police in which he described the murders and directly named Bradshaw. A few days later, Thielen re-enacted the murders for the police officers and implicated Bradshaw in both murders. This re-enactment was recorded in a roughly six-hour video.

**15** Thielen and Bradshaw were initially charged together with two counts of first degree murder. However, Thielen pled guilty to second degree murder before the trial started. Thielen was called as a Crown witness in Bradshaw's trial, but refused to be sworn to give testimony. As a result, he was held in contempt of court. The Crown sought to admit part of the re-enactment video - a hearsay statement - into evidence.

## III. Decisions Below

**16** Following a *voir dire*, Greyell J. admitted the re-enactment video into evidence ( *2012 BCSC 2025*). He found that this hearsay statement was necessary and sufficiently reliable to be admitted. In finding that the statement was sufficiently reliable, he noted that the re-enactment was voluntary, incriminating, and was made after Thielen received legal advice. The statement was also corroborated by extrinsic evidence. However, given Thielen's unsavoury character, the trial judge determined that a strong *Vetrovec* warning regarding the re-enactment video was required.

**17** The British Columbia Court of Appeal held that the trial judge erred in admitting the re-enactment video because it was not sufficiently reliable. The court noted that the trial judge relied significantly [page877] on evidence that did not implicate Bradshaw in the murders as corroboration. Furthermore, in the recorded conversations at the Best Western Hotel and Bothwell Park, Bradshaw did not implicate himself in the murders to the degree that Thielen implicated Bradshaw in the re-enactment. The British Columbia Court of Appeal concluded that the trial judge erred in finding that threshold reliability was established. It allowed the appeal, set aside the guilty verdicts, and ordered a new trial ( *2015 BCCA 195*, *323 C.C.C. (3d) 475*).

## IV. Analysis

### A. *Legal Principles*

**18** Hearsay can exceptionally be admitted into evidence if it is necessary and sufficiently reliable. This appeal raises the following question: When can a trial judge rely on corroborative evidence to conclude that the threshold reliability of a hearsay statement is established? To answer, I turn to the rationale for the rule against hearsay and for the principled exception to this rule.

(1) The Principled Exception to the Hearsay Rule

**19** The truth-seeking process of a trial is predicated on the presentation of evidence in court. Litigants make their case by presenting real evidence and *viva voce* testimony to the trier of fact. In court, witnesses give testimony under oath or solemn affirmation. The trier of fact directly observes the real evidence and hears the testimony, so there is no concern that the evidence was recorded inaccurately. This process gives the trier of fact robust tools for testing the truthfulness of evidence and assessing its value. To determine whether a witness is telling the truth, the trier of fact can observe the witness's demeanor and assess whether the testimony withstands testing through cross-examination (*R. v. Khelawon*, 2006 SCC 57, [2006] 2 S.C.R. 787, at para. 35).

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**20** Hearsay is an out-of-court statement tendered for the truth of its contents. Because hearsay is declared outside of court, it is often difficult for the trier of fact to assess whether it is trustworthy. Generally, hearsay is not taken under oath, the trier of fact cannot observe the declarant's demeanor as she makes the statement, and hearsay is not tested through cross-examination (*R. v. B. (K.G.)*, [1993] 1 S.C.R. 740, at p. 764). Allowing a trier of fact to consider hearsay can therefore compromise trial fairness and the trial's truth-seeking process. The hearsay statement may be inaccurately recorded, and the trier of fact cannot easily investigate the declarant's perception, memory, narration, or sincerity (*Khelawon*, at para. 2). As Fish J. explains in *R. v. Baldree*, 2013 SCC 35, [2013] 2 S.C.R. 520:

> First, the declarant may have *misperceived* the facts to which the hearsay statement relates; second, even if correctly perceived, the relevant facts may have been *wrongly remembered*; third, the declarant may have narrated the relevant facts in an *unintentionally misleading manner*; and finally, the declarant may have *knowingly made a false assertion*. The opportunity to fully probe these potential sources of error arises only if the declarant is present in court and subject to cross-examination. [Emphasis in original; para. 32.]

**21** Given the dangers that hearsay evidence presents, "[t]he fear is that untested hearsay evidence may be afforded more weight than it deserves" (*Khelawon*, at para. 35). Therefore, while all relevant evidence is generally admissible, hearsay is presumptively inadmissible (*Khelawon*, at paras. 2-3).

**22** However, some hearsay evidence "presents minimal dangers and its *exclusion*, rather than its admission, would impede accurate fact finding" (*Khelawon*, at para. 2 (emphasis in original)). Thus, categorical exceptions to the rule excluding hearsay developed through the common law over time. These traditional exceptions are based on admitting types of hearsay statements that were considered [page879] necessary and reliable, such as dying declarations (*Khelawon*, at para. 42; *R. v. Youvarajah*, 2013 SCC 41, [2013] 2 S.C.R. 720, at para. 20; J. H. Wigmore, *Evidence in Trials at Common Law* (2nd ed. 1923), vol. III, at p. 152).

**23** Eventually, a more flexible approach to hearsay developed through the jurisprudence. Under the principled exception, hearsay can exceptionally be admitted into evidence when the party tendering it demonstrates that the twin criteria of necessity and threshold reliability are met on a balance of probabilities (*Khelawon*, at para. 47).

**24** By only admitting necessary and sufficiently reliable hearsay, the trial judge acts as an evidentiary gatekeeper. She protects trial fairness and the integrity of the truth-seeking process (*Youvarajah*, at paras. 23 and 25). In criminal proceedings, the threshold reliability analysis has a constitutional dimension because the difficulties of testing hearsay evidence can threaten the accused's right to a fair trial (*Khelawon*, at paras. 3 and 47). Even when the trial judge is satisfied that the hearsay is necessary and sufficiently reliable, she has discretion to exclude this evidence if its prejudicial effect outweighs its probative value (*Khelawon*, at para. 49).

**25** In this case, the necessity of the re-enactment evidence is established because Thielen refused to testify. Thus, its admissibility rests on whether threshold reliability is met.

(2) Threshold Reliability

**26** To determine whether a hearsay statement is admissible, the trial judge assesses the statement's *threshold* reliability. Threshold reliability is established when the hearsay "is sufficiently reliable to overcome the dangers arising from the difficulty of testing it" (*Khelawon*, at para. 49). These dangers arise notably due to the absence of contemporaneous [page880] cross-examination of the hearsay declarant before the trier of fact (*Khelawon*, at paras. 35 and 48). In assessing threshold reliability, the trial judge must identify the specific hearsay dangers presented by the statement and consider any means of overcoming them (*Khelawon*, at paras. 4 and 49; *R. v. Hawkins*, [1996] 3 S.C.R. 1043, at para. 75). The dangers relate to the difficulties of assessing the declarant's perception, memory, narration, or sincerity, and should be defined with precision to permit a realistic evaluation of whether they have been overcome.

**27** The hearsay dangers can be overcome and threshold reliability can be established by showing that (1) there are adequate substitutes for testing truth and accuracy (procedural reliability) or (2) there are sufficient circumstantial or evidentiary guarantees that the statement is inherently trustworthy (substantive reliability) (*Khelawon*, at paras. 61-63; *Youvarajah*, at para. 30).

**28** *Procedural* reliability is established when "there are adequate substitutes for testing the evidence", given that the declarant has not "state[d] the evidence in court, under oath, and under the scrutiny of contemporaneous cross-examination" (*Khelawon*, at para. 63). These substitutes must provide a satisfactory basis for the trier of fact to rationally evaluate the truth and accuracy of the hearsay statement (*Khelawon*, at para. 76; *Hawkins*, at para. 75; *Youvarajah*, at para. 36). Substitutes for traditional safeguards include a video recording of the statement, the presence of an oath, and a warning about the consequences of lying (*B. (K.G.)*, at pp. 795-96). However, some form of cross-examination of the declarant, such as preliminary inquiry testimony (*Hawkins*) or cross-examination of a recanting witness at trial (*B. (K.G.)*; *R. v. U. (F.J.)*, [1995] 3 S.C.R. 764), is usually required (*R. v. Couture*, 2007 SCC 28, [2007] 2 S.C.R. 517, at paras. 92 and 95). In this respect, I disagree with the Court of Appeal's categorical assertion that safeguards relevant to assessing procedural reliability are only "those in place when the statement is taken" (para. 30). Some safeguards imposed at trial, such as cross-examination of a [page881] recanting witness before the trier of fact, may provide a satisfactory basis for testing the evidence.

**29** However, jury warnings about the dangers of hearsay evidence or *Vetrovec* testimony do not provide adequate substitutes for traditional safeguards. Instructing a jury on *how* to evaluate a statement that it lacks the *means* to evaluate does not address the hearsay dangers that underlie the exclusionary rule. Furthermore, *Vetrovec* warnings are designed to address concerns about a witness who is inherently untrustworthy, despite the opportunity to cross-examine in court. They are not tools for assessing the truth and accuracy of a hearsay statement in the absence of contemporaneous cross-examination.

**30** A hearsay statement is also admissible if *substantive* reliability is established, that is, if the statement is inherently trustworthy (*Youvarajah*, at para. 30; *R. v. Smith*, [1992] 2 S.C.R. 915, at p. 929). To determine whether the statement is inherently trustworthy, the trial judge can consider the circumstances in which it was made and evidence (if any) that corroborates or conflicts with the statement (*Khelawon*, at paras. 4, 62 and 94-100; *R. v. Blackman*, 2008 SCC 37, [2008] 2 S.C.R. 298, at para. 55).

**31** While the standard for substantive reliability is high, guarantee "as the word is used in the phrase 'circumstantial guarantee of trustworthiness', does not require that reliability be established with absolute certainty" (*Smith*, at p. 930). Rather, the trial judge must be satisfied that the statement is "so reliable that contemporaneous cross-examination of the declarant would add little if anything to the process" (*Khelawon*, at para. 49). The level of certainty required has been articulated in different ways throughout this Court's jurisprudence. Substantive [page882] reliability is established when the statement "is made under circumstances which substantially negate the possibility that the declarant was untruthful or mistaken" (*Smith*, at p. 933); "under such circumstances that even a sceptical caution would look upon it as trustworthy" (*Khelawon*, at para. 62, citing Wigmore, at p. 154); when the statement is so reliable that it is "unlikely to change under cross-examination" (*Khelawon*, at para. 107; *Smith*, at p. 937); when "there is no real concern about whether the statement is true or not because of the circumstances in

which it came about" (*Khelawon*, at para. 62); when the only likely explanation is that the statement is true (*U. (F.J.)*, at para. 40).

**32** These two approaches to establishing threshold reliability may work in tandem. Procedural reliability and substantive reliability are not mutually exclusive (*Khelawon*, at para. 65) and "factors relevant to one can complement the other" (*Couture*, at para. 80). That said, the threshold reliability standard always remains high - the statement must be sufficiently reliable to overcome the specific hearsay dangers it presents (*Khelawon*, at para. 49). For example, in *U. (F.J.)*, where the Court drew on elements of substantive and procedural reliability to justify the admission of a hearsay statement, both cross-examination of the recanting witness and corroborative evidence were required to meet threshold reliability, though neither on its own would have sufficed (see also *Blackman*, at paras. 37-52). I know of no other example from this Court's jurisprudence of substantive and procedural reliability complementing each other to justify the admission of a hearsay statement. Great care must be taken to ensure that this combined approach does not lead to the admission of statements despite insufficient procedural safeguards and guarantees of inherent trustworthiness to overcome the hearsay dangers.

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(3) Corroborative Evidence and Substantive Reliability

**33** With these principles in mind, I turn to the issue at the heart of this appeal: When and how can a trial judge rely on corroborative evidence to conclude that substantive reliability is established?

**34** The Crown submits that threshold reliability involves a consideration of all the corroborative evidence that supports the truthfulness of a statement, including evidence that does not implicate the accused, or directly confirm the disputed aspect of the statement. The Crown explains that this approach to corroboration is aligned with other areas of the law, including corroboration when assessing the ultimate reliability of hearsay statements, the ultimate reliability of unsavoury witness statements, and the threshold reliability of Mr. Big statements.

**35** In contrast, the respondent Bradshaw submits that the trial judge can only consider evidence that corroborates the *purpose* for which a hearsay statement is tendered, and notes that the re-enactment statement was tendered to implicate him in the murders.

**36** In my view, the Crown's position that "a uniform definition of confirmatory evidence" should be employed "at both the threshold and ultimate reliability stages" is untenable because it misconstrues the relationship between threshold and ultimate reliability (A.F., at para. 96). It also misconstrues the relationship between threshold reliability and probative value.

**37** In *R. v. Starr*, *2000 SCC 40*, *[2000] 2 S.C.R. 144*, this Court held that corroborative evidence could not be considered in assessing the threshold reliability of hearsay. This bright-line rule was created to ensure that the trial judge did not invade the [page884] province of the trier of fact by pre-determining a hearsay statement's ultimate reliability (para. 217).[1]

**38** *Khelawon* overturned *Starr* on this point. Charron J. explained that, in appropriate cases, corroborative or conflicting evidence can be considered in assessing threshold reliability (paras. 93-100). *Khelawon* established that "an item of evidence [that] goes to the trustworthiness of the statement ... should no longer be excluded simply on the basis that it is corroborative in nature" (*Blackman*, at para. 55 (emphasis added)). But "[i]t is important to emphasize that *Khelawon* did not broaden the scope of the admissibility inquiry; it merely refocused it" (*Blackman*, at para. 54). While *Khelawon* overturned the prohibition on considering corroborative evidence in the admissibility inquiry, it reaffirmed the distinction between threshold and ultimate reliability (para. 50; *Blackman*, at para. 56).

**39** The distinction between threshold and ultimate reliability, while "a source of confusion", is crucial (*Khelawon*, at para. 50). Threshold reliability concerns admissibility, whereas ultimate reliability concerns reliance (*Khelawon*, at para. 3). When threshold reliability is based on the inherent trustworthiness of the statement, the trial judge and the

trier of fact may both assess the trustworthiness of the hearsay statement. However, they do so for different purposes (*Khelawon*, at paras. 3 and 50). In assessing ultimate reliability, the trier of fact determines whether, and to what degree, the statement should be believed, and thus relied on to decide issues in the case (*Khelawon*, at para. 50; D. M. Paciocco and L. Stuesser, *The Law of Evidence* (7th ed. 2015), at pp. 35-36). This determination is made "in the context of the entirety of the evidence" including [page885] evidence that corroborates the accused's guilt or the declarant's overall credibility (*Khelawon*, at para. 3).

**40** In contrast, in assessing threshold reliability, the trial judge's preoccupation is whether in-court, contemporaneous cross-examination of the hearsay declarant would add anything to the trial process (*Khelawon*, at para. 49; see also H. Stewart, "*Khelawon*: The Principled Approach to Hearsay Revisited" (2008), 12 *Can. Crim. L.R.* 95, at p. 106). At the threshold stage, the trial judge must decide on the *availability* of competing explanations (substantive reliability) and whether the trier of fact will be in a position to choose between them by means of adequate substitutes for contemporaneous cross-examination (procedural reliability). For this reason, where procedural reliability is concerned with whether there is a satisfactory basis to rationally *evaluate* the statement, substantive reliability is concerned with whether the circumstances, and any corroborative evidence, provide a rational basis to *reject* alternative explanations for the statement, other than the declarant's truthfulness or accuracy.

**41** In short, in the hearsay context, the difference between threshold and ultimate reliability is qualitative, and not a matter of degree, because the trial judge's inquiry serves a distinct purpose. In assessing substantive reliability, the trial judge does not usurp the trier of fact's role. Only the trier of fact assesses whether the hearsay statement should ultimately be relied on and its probative value.

**42** To preserve the distinction between threshold and ultimate reliability and to prevent the *voir dire* from overtaking the trial, "[t]here must be a distinction between evidence that is admissible on the *voir dire* to determine necessity and reliability, and the evidence that is admissible in the main trial" [page886] (Stewart, at p. 111; see also L. Lacelle, "The Role of Corroborating Evidence in Assessing the Reliability of Hearsay Statements for Substantive Purposes" (1999), 19 C.R. (5th) 376; *Blackman*, at paras. 54-57). As Charron J. explained in *Khelawon*, "the trial judge must remain mindful of the limited role that he or she plays in determining admissibility - it is crucial to the integrity of the fact-finding process that the question of ultimate reliability not be pre-determined on the admissibility *voir dire*" (para. 93). Similarly, she noted in *Blackman*: "The admissibility *voir dire* must remain focused on the hearsay evidence in question. It is not intended, and cannot be allowed by trial judges, to become a full trial on the merits" (para. 57). Limiting the use of corroborative evidence as a basis for admitting hearsay also mitigates the risk that inculpatory hearsay will be admitted simply because evidence of the accused's guilt is strong. The stronger the case against the accused, the easier it would be to admit flawed and unreliable hearsay against him. The limited inquiry into corroborative evidence flows from the fact that, at the threshold reliability stage, corroborative evidence is used in a manner that is qualitatively distinct from the manner in which the trier of fact uses it to assess the statement's ultimate reliability. As Lederman, Bryant and Fuerst explain, at the threshold reliability stage,

> [t]he use of corroborative evidence should be directed to the reliability of the hearsay. Certain items of evidence can take on a corroborative character and be supportive of the Crown's theory when considered in the context of the evidence as a whole. Such evidence relates to the merits of the case rather than to the limited focus of the *voir dire* in assessing the trustworthiness of the statement and is properly left to the ultimate trier of fact.

(S. N. Lederman, A. W. Bryant and M. K. Fuerst, *The Law of Evidence in Canada* (4th ed. 2014), at s.6.140)

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**43** Thus, the Crown's argument that the approach to corroboration when assessing the ultimate reliability of *Vetrovec* testimony is analogous to the approach for assessing the threshold reliability of hearsay is also fundamentally flawed. Further, an unsavoury witness, unlike a hearsay declarant, is a witness at trial and can be cross-examined. The particular dangers posed by the absence of cross-examination make it necessary to

distinguish between the *Vetrovec* and hearsay approaches to corroborative evidence. As a result, I do not accept the Crown's submissions in this regard.

**44** In my view, the rationale for the rule against hearsay and the jurisprudence of this Court make clear that not all evidence that corroborates the declarant's credibility, the accused's guilt, or one party's theory of the case, is of assistance in assessing threshold reliability. A trial judge can only rely on corroborative evidence to establish threshold reliability if it shows, when considered as a whole and in the circumstances of the case, that the only likely explanation for the hearsay statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement. If the hearsay danger relates to the declarant's sincerity, truthfulness will be the issue. If the hearsay danger is memory, narration, or perception, accuracy will be the issue.

**45** First, corroborative evidence must go to the truthfulness or accuracy of the *material aspects* of the hearsay statement (see *Couture*, at paras. 83-84; *Blackman*, at para. 57). Hearsay is tendered for the truth of its contents and corroborative evidence must go to the truthfulness or accuracy of the content of the hearsay statement that the moving party seeks to rely on. Because threshold reliability is about admissibility of evidence, the focus must be on the aspect [page888] of the statement that is tendered for its truth.[2] The function of corroborative evidence at the threshold reliability stage is to mitigate the need for cross-examination, not generally, but *on the point* that the hearsay is tendered to prove.

**46** A similar approach was taken in restricting the type of corroborative evidence that can be relied on to establish the threshold reliability of Mr. Big statements. In *Hart*, Moldaver J. (writing for the majority) concluded that there was a "complete lack of confirmatory evidence" (para. 143), disregarding corroborative evidence that merely confirmed the accused's presence at the scene of the crime when it took place, because the Mr. Big statement was tendered to show that the accused killed his daughters, not that he was present at the scene of the crime. As Moldaver J. explained:

> The issue has always been whether the respondent's daughters drowned accidentally or were murdered. There was never any question that the respondent was present when his daughters entered the water. All of the objectively verifiable details of the respondent's confession (e.g., his knowledge of the location of the drowning) flow from his acknowledged presence at the time the drowning occurred. [para. 143]

Thus, in assessing the threshold reliability of Mr. Big statements, the trial judge considers only corroborative evidence that goes to the truthfulness or accuracy of the material aspects of the statement.

**47** Second, at the threshold reliability stage, corroborative evidence must work in conjunction with [page889] the circumstances to overcome the *specific hearsay dangers* raised by the tendered statement. When assessing the admissibility of hearsay evidence, "the scope of the inquiry must be tailored to the particular dangers presented by the evidence and limited to determining the evidentiary question of admissibility" (*Khelawon*, at para. 4). Thus, to overcome the hearsay dangers and establish substantive reliability, corroborative evidence must show that the material aspects of the statement are unlikely to change under cross-examination (*Khelawon*, at para. 107; *Smith*, at p. 937). Corroborative evidence does so if its combined effect, when considered in the circumstances of the case, shows that the *only likely explanation* for the hearsay statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement (see *U. (F.J.)*, at para. 40). Otherwise, alternative explanations for the statement that could have been elicited or probed through cross-examination, and the hearsay dangers, persist.

**48** In assessing substantive reliability, the trial judge must therefore identify alternative, even speculative, explanations for the hearsay statement (*Smith*, at pp. 936-37). Corroborative evidence is of assistance in establishing substantive reliability if it shows that these alternative explanations are unavailable, if it "eliminate[s] the hypotheses that cause suspicion" (S. Akhtar, "Hearsay: The Denial of Confirmation" (2005), 26 C.R. (6th) 46, at p. 56 (emphasis deleted)). In contrast, corroborative evidence that is "equally consistent" with the truthfulness and accuracy of the statement as well as another hypothesis is of no assistance (*R. v. R. (D.)*, [1996] 2 S.C.R. 291, at

paras. 34-35). Adding evidence that is supportive of the truth of the statement, but that is also consistent with alternative explanations, does not add to the statement's inherent trustworthiness.

**49** While the declarant's truthfulness or accuracy must be more likely than any of the alternative explanations, this is not sufficient. Rather, the fact that the threshold reliability analysis takes place on a balance of probabilities means that, based on the circumstances and any evidence led on *voir dire*, the [page890] trial judge must be able to rule out any plausible alternative explanations on a balance of probabilities.

**50** To be relied on for the purpose of rejecting alternative hypotheses for the statement, corroborative evidence must itself be trustworthy. Untrustworthy corroborative evidence is therefore not relevant to the substantive reliability inquiry (see *Khelawon*, at para. 108). Trustworthiness concerns are particularly acute when the corroborative evidence is a statement, rather than physical evidence (see Lacelle, at p. 390).

**51** The jurisprudence of this Court provides two examples of corroborative evidence that could be relied on to establish threshold reliability.

**52** In *R. v. Khan*, *[1990] 2 S.C.R. 531*, this Court held that a hearsay statement from a child regarding a sexual assault was admissible, notably because it was corroborated by a semen stain on the child's clothes (p. 548). The child alleged that she had been sexually assaulted at the doctor's office. She was only alone in the office for a brief period and "did not come into contact with any other male person during [that] period" (p. 534). Given the semen stain and the circumstances of the case, the only likely hypothesis was that the child had not lied about or misperceived the assault. The semen stain directly responded to the hearsay dangers.

**53** *Khan* can be contrasted with *R. (D.)*, where this Court held that a child's hearsay regarding a sexual assault by her father was inadmissible, although there was evidence that supported her statement: bloodstained underpants. This corroborative evidence was consistent with more than one hypothesis, both the possibility that her brother had assaulted her and the possibility that her father had assaulted her, and thus was of no assistance in assessing threshold reliability (paras. 34-35).

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**54** In *U. (F.J.)*, a hearsay statement was admissible in part because it was corroborated by a strikingly similar statement. The strikingly similar statement was capable of supporting the threshold reliability of the hearsay statement because the Court was able to rule out the possibilities that the similarity was purely coincidental, that the second declarant had heard the first statement and modeled her statement off of it, and that either statement was the result of collusion or outside influence. Importantly, Lamer C.J. was concerned with rejecting, not the hypothesis that the second statement was *in fact* based on the first, but the possibility that it *could have been* based on the first. He concluded that the only likely explanation for the similarity between the two statements was the truthfulness of the hearsay declarant (*U. (F.J.)*, at paras. 40 and 53).

**55** In contrast, the corroborative evidence in *Khelawon*, bruises and garbage bags filled with clothes, was not capable of bolstering the threshold reliability of a hearsay statement regarding an assault. Charron J. explained that the bruises on the complainant's body could have been caused by a fall rather than an assault. And while the complainant had alleged that the accused had put his clothes in garbage bags, Charron J. reasoned that the complainant "could have filled those bags himself" (para. 107). Given that the corroborative evidence was consistent with many hypotheses, it did not show that the only likely explanation was the declarant's truthfulness about the assault.

**56** Clarifying when corroborative evidence can be relied on to establish substantive reliability is not a departure from the functional approach to the admissibility of hearsay. There is no bright-line rule restricting the type of corroborative evidence that a trial judge can rely on to determine that substantive reliability is established. In all cases, the trial judge must consider the specific hearsay dangers raised by the statement, the corroborative evidence as a whole, and the circumstances of the case, to determine whether the corroborative evidence (if any)

can be relied on to establish substantive reliability.

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**57** In sum, to determine whether corroborative evidence is of assistance in the substantive reliability inquiry, a trial judge should

1. identify the material aspects of the hearsay statement that are tendered for their truth;
2. identify the specific hearsay dangers raised by those aspects of the statement in the particular circumstances of the case;
3. based on the circumstances and these dangers, consider alternative, even speculative, explanations for the statement; and
4. determine whether, given the circumstances of the case, the corroborative evidence led at the *voir dire* rules out these alternative explanations such that the only remaining likely explanation for the statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement.

**58** With these principles in mind, I now turn to the trial judge's assessment of the threshold reliability of the re-enactment statement.

B. *Application*

**59** In concluding that the threshold reliability of the re-enactment statement was established, the trial judge relied on the fact that the statement was: (1) voluntary; (2) incriminating; (3) made after Thielen received legal advice; (4) a detailed, free-flowing narrative; and (5) corroborated by extrinsic evidence. As a result, he was satisfied that threshold reliability was established.

**60** I conclude that the trial judge erred in relying significantly on corroborative evidence that did not show, in the circumstances of the case, that the only likely explanation was Thielen's truthfulness about the material aspect of the re-enactment statement. Given this error, the trial judge's admissibility ruling is not entitled to deference. This Court [page893] must therefore determine whether the hearsay re-enactment statement meets the reliability threshold. I conclude that it does not.

(1) The Trial Judge's Reliance on Corroborative Evidence

**61** The trial judge relied significantly on the existence of corroborative evidence to find that the re-enactment statement was admissible. In particular, he relied on

* forensic evidence that corroborated Thielen's detailed description of the murders (para. 45);
* Thielen's accurate description of the weather on the nights of the murders (para. 46);
* evidence of a conversation between Bontkes and Motola on the night Bontkes died (para. 47) (Motola was a third accomplice in Bontkes's death and pled guilty to manslaughter in separate proceedings.);
* evidence that Bradshaw may have been present when Motola and Thielen discussed their plan to kill Bontkes (para. 52);
* call records between one of the murder victims and Bradshaw on the night of one of the murders, and between Thielen and Bradshaw on the night of the other murder (para. 51); and

* Bradshaw's admissions at the Best Western and Bothwell Park (paras. 48-49).

**62** As I shall explain, this corroborative evidence is of no assistance in the threshold reliability inquiry.

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**63** The first step in assessing the substantive reliability of a hearsay statement is identifying the material aspects of the statement. The re-enactment statement was tendered for the truth of Thielen's claim that Bradshaw participated in the murders. Given the purpose for which the statement was tendered, the material aspect of the statement was Thielen's assertion that Bradshaw participated in the murders.

**64** As to the specific hearsay dangers presented by the statement, a number of common hearsay dangers were not in play in this case. The accuracy of the statement is not at issue because it was video-recorded. While the difficulties of investigating a hearsay declarant's perception and memory are often dangers associated with hearsay evidence, these dangers are minimal in this case because the statement was not tendered to provide details of how the murders unfolded, but rather to prove that Bradshaw participated in the murders. It is hardly plausible that Thielen would have been mistaken - or wrongly remembered - whether Bradshaw participated in the murders.

**65** Therefore, the specific hearsay danger presented by the re-enactment statement is the difficulty of testing Thielen's sincerity with regards to Bradshaw's participation in the murders. This danger is inherent in all hearsay statements due to the inability to test for and detect the hearsay declarant's insincerity through contemporaneous, in-court cross-examination. Additionally, in this case, there are serious reasons to be concerned that Thielen lied about Bradshaw's participation in the murders.

**66** First, Thielen gave inconsistent statements about Bradshaw's participation in the murders. In May 2010, Thielen told Cst. B. that he shot Lamoureux and Bontkes, and he did not implicate Bradshaw. When he met with the crime boss in July, Thielen implicated Bradshaw in the murders. [page895] When he was arrested, Thielen initially denied his own involvement in both murders. After the police told Thielen that he had been the target of a Mr. Big operation, he admitted that he had been involved in the murders and he implicated Bradshaw.

**67** Second, Thielen had a significant motive to lie about Bradshaw's participation in the murders. Like the hearsay declarant in *Youvarajah*, Thielen "had a strong incentive to minimize his role in the crime and to shift responsibility" to his accomplice (para. 33). Thielen had a motive to implicate Bradshaw to reduce his own culpability, particularly given his admissions to Cst. B. Although Thielen was charged with the first degree murder of Lamoureux and Bontkes, he ultimately pled guilty to second degree murder. Thielen's motive to lie is relevant in assessing the reliability of his hearsay statement (*Blackman*, at para. 42).

**68** Third, Thielen was a *Vetrovec* witness. In the trial judge's words:

> ... there is already considerable evidence of Mr. Thielen's unsavoury character before the jury. He has been described by a number of witnesses as a drug dealer, a thug, an enforcer and a murderer. He is clearly a person about whom a strong *Vetrovec* warning is appropriate. [para. 60 (CanLII)]

**69** Given that a *Vetrovec* witness cannot be trusted to tell the truth, even under oath (*R. v. Khela*, *2009 SCC 4*, *[2009] 1 S.C.R. 104*, at para. 3), establishing that hearsay evidence from a *Vetrovec* witness is inherently trustworthy will be extremely challenging. However, there is no blanket prohibition on admitting hearsay from *Vetrovec* witnesses. In all cases, the trial judge must assess whether the hearsay dangers have been overcome. That said, the strong *Vetrovec* warning indicates that the dangers presented by the hearsay statement here are particularly severe.

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**70** The third step in assessing a hearsay statement's substantive reliability is considering alternative explanations

for the hearsay statement that arise from the particular circumstances of the case. Given the hearsay dangers presented by the re-enactment statement, an alternative explanation is that Thielen lied about Bradshaw's participation in the murders.

**71** With this in mind, corroborative evidence will only assist in establishing the substantive reliability of the re-enactment statement if it shows, when considered in the circumstances of the case, that the only likely explanation is that Thielen was truthful about Bradshaw's involvement in the murders. When the hearsay danger is sincerity, substantive reliability is only established when the circumstances and corroborative evidence show that the possibility that the declarant lied is substantially negated, that "even a sceptical caution would look upon [the statement] as trustworthy" (Wigmore, at p. 154; *Khelawon*, at para. 62; *Couture*, at para. 101). Corroborative evidence or circumstances showing that the statement is inherently trustworthy are required to rebut the presumption of inadmissibility.

**72** The forensic evidence, weather evidence, and evidence of a conversation between Bontkes and Motola did not implicate Bradshaw in the murders. This evidence is of no assistance in determining whether Thielen was being truthful about Bradshaw's involvement in the murders. The fact that Thielen accurately described the way the murders unfolded and the weather on the nights of the murders does not mitigate the danger that he lied about Bradshaw's participation. As an accomplice, Thielen was present at the scenes of the crimes and was well positioned to fabricate a story implicating Bradshaw (see *R. v. Smith*, *2009 SCC 5*, *[2009] 1 S.C.R. 146*, at para. 15; *R. v. Salah*, *2015 ONCA 23*, *319 C.C.C. (3d) 373*, at para. 116).

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**73** The remaining corroborative evidence relied on by the trial judge was probative of Bradshaw's involvement in the murders. It will be for the trier of fact to determine whether or not this evidence increases the likelihood that Bradshaw is guilty. The call records show that Bradshaw may have spoken to Lamoureux and Thielen on the evenings in question, and the evidence of Bradshaw's presence when the plan to kill Bontkes was discussed shows that Bradshaw may have been aware of this plan. However, this evidence, viewed in the circumstances, did not assist in effectively ruling out the alternative explanation for the re-enactment statement - the danger that Thielen lied about Bradshaw's involvement in the murders.

**74** Finally, the recorded conversations at the Best Western Hotel and Bothwell Park provide direct evidence of Bradshaw's involvement in the murders. However, as I shall explain, there are concerns about the trustworthiness of these statements. As mentioned above, corroborative evidence must itself be trustworthy to be relied on to establish the threshold reliability of a hearsay statement (see *Khelawon*, at para. 108).

**75** When Thielen was the target of a Mr. Big operation, undercover officers encouraged him to meet up with Bradshaw to clarify their respective roles in the murders. On July 21, 2010, Thielen and Bradshaw met in a room at the Best Western Hotel. Their conversation was recorded. The first eight minutes of the recorded conversation are inaudible because Bradshaw and Thielen were in the bathroom, while the tap was running. Cst. B. called Thielen to get him to leave the bathroom so the conversation could be captured. Once Bradshaw and Thielen moved into the main room, Bradshaw said that he had shot Bontkes and participated in both murders.

**76** A few days later, Thielen and Bradshaw met at Bothwell Park. Their conversation was recorded again. During their meeting, Bradshaw discussed [page898] their unsuccessful attempt to kill Bontkes, before Bontkes was actually murdered in March 2009.

**77** While this evidence provides some evidence of guilt, it does not assist, for several reasons, in effectively ruling out the possibility that Thielen lied about Bradshaw's involvement in the murders.

**78** The Best Western and Bothwell Park evidence was collected in a Mr. Big operation. Undercover officers were orchestrating the circumstances to obtain an admission from Thielen and then from Bradshaw. As the trial judge explained, the Best Western and Bothwell Park "meetings were set up by Constable B. with Mr. Thielen's

cooperation, during the course of the Mr. Big operation, in an endeavour to elicit evidence of Mr. Bradshaw's possible participation in the murders of Ms. Lamoureux and Mr. Bontkes" (para. 43). Indeed, Cst. B. explained that he "wanted Mr. Thielen to get ... the truth from Mr. Bradshaw" (examination in chief, A.R., vol. V, at p. 134) and that he gave Thielen instructions on what was required during his conversation with Bradshaw at the Best Western Hotel.

**79** In Mr. Big operations, parties believe they are dealing with a criminal organization. They are often induced and threatened. As this Court noted in *Hart*: "Suspects confess to Mr. Big during pointed interrogations in the face of powerful inducements and sometimes veiled threats - and this raises the spectre of unreliable confessions" (para. 5). The Mr. Big operation raises concerns about Thielen's motivation and role in these conversations, and the trustworthiness of Bradshaw's statements at the Best Western and Bothwell Park.

**80** As well, the initial part of the Best Western conversation was inaudible because Thielen and Bradshaw were in the bathroom and a tap was running. This raises questions about what followed. [page899] As I have said, the trial judge is required to consider alternative, even speculative, explanations that could account for the hearsay statement (*Smith* (1992), at pp. 936-37). Indeed, while this evidence was not before the trial judge at the time of his ruling, Bradshaw subsequently testified that, while the tap was running, Thielen asked him to lie and say that he had been involved in Lamoureux and Bontkes's murders.

**81** Furthermore, in the Bothwell Park conversation, Bradshaw primarily implicated himself in the attempted murder of Bontkes, rather than in Bontkes's actual murder.

**82** Of course, as the accused's admissions, the recording of Bradshaw's own words are admissible against him quite independently of whether Thielen's re-enactment video is admitted. Indeed, Bradshaw's admissions at the Best Western and Bothwell Park were admitted into evidence for the jury's consideration. That is not challenged on appeal.

**83** However, these admissions are not of such a nature to justify the admission of Thielen's highly suspect hearsay statements implicating Bradshaw. They do not, when considered in the circumstances and with the other evidence led at the *voir dire*, "substantially negate the possibility that the [hearsay] declarant was untruthful" about Bradshaw's involvement in the murders (*Smith* (1992), at p. 933). Bradshaw's Best Western admission does not, in the circumstances, demonstrate that Thielen's statement would be unlikely to change under cross-examination (*Khelawon*, at para. 107; *Smith* (1992), at p. 937).

**84** In *U. (F.J.)*, this Court held that "instances of statements so strikingly similar as to bolster their reliability will be rare" (para. 45). Lamer C.J. explained that a similar statement cannot bolster the reliability of a hearsay statement unless it is unlikely that "[t]he second declarant knew of [page900] the contents of the first statement, and based his or her statement in whole or in part on this knowledge" and unlikely that the similarity is due to outside influence (para. 40). Thielen was present for Bradshaw's Best Western and Bothwell Park admissions, and could have based his re-enactment statement on this knowledge. Furthermore, outside influence cannot be rejected as a possible explanation for Bradshaw's Best Western and Bothwell Park admissions. Indeed, according to Cst. B.'s testimony, he played a role in orchestrating the admissions. The Best Western and Bothwell Park statements were therefore of no assistance in establishing the inherent trustworthiness of the re-enactment statement.

**85** The evidence led at the admissibility *voir dire* as corroborative of Thielen's statement is unlike the semen stain in *Khan*, or the strikingly similar statement in *U. (F.J.)*. When considered in the circumstances of the case, this evidence does not show that the only likely explanation for the statement was Thielen's truthfulness about Bradshaw's involvement in the murders. Taken as a whole, this evidence therefore did not assist in establishing threshold reliability. While much of the evidence relied on by the trial judge was probative of Bradshaw's guilt, and thus could be considered by the trier of fact in the trial on the merits, none of it was of assistance in establishing the threshold reliability of the re-enactment statement. Furthermore, as noted above, the evidence and circumstances here showed that there were serious reasons to be concerned that Thielen lied.

(2) Threshold Reliability of the Re-enactment Statement

**86** Given the trial judge's flawed approach to corroborative evidence, this Court must determine whether the threshold reliability of the hearsay re-enactment statement is nonetheless established. Are [page901] the serious hearsay dangers presented by the re-enactment statement overcome?

**87** To respect the role of the trier of fact in assessing trustworthiness, I consider first the statement's procedural reliability (*Khelawon*, at para. 92). There were few means for the trier of fact to determine whether Thielen lied about Bradshaw's participation in the murders. While the accuracy of the reporting of the statement is not at issue in this case because it was video-taped, Thielen was not cross-examined at the time the statement was taken or subsequently. Thielen's statement was not taken under oath and he was not warned of the consequences of lying before the statement was taken. Most importantly, he was not available to be cross-examined at trial. The trier of fact evidently did not possess a "sufficient substitute basis for testing the evidence" in the absence of cross-examination (*Khelawon*, at para. 105).

**88** The trial judge considered "possible safeguards that [could] be put in place by the Crown and the court to overcome [the hearsay] dangers" (para. 19). He explained that Thielen's inconsistencies could be put into evidence and that the Crown had agreed to call the police officers to whom Thielen gave the different statements, in order to allow the defence to cross-examine them on these inconsistencies (para. 59). He also noted that a strong *Vetrovec* warning would be given (para. 60).

**89** Putting Thielen's inconsistencies into evidence did not provide the jury with a sufficient substitute basis for evaluating the truth of the re-enactment statement. And while cross-examining the *recipient* of a hearsay statement may be helpful if there are concerns about the recipient's credibility or reliability (*Blackman*, at para. 50), there were no such concerns in this case. As the Criminal Lawyers' Association of Ontario (an intervener) notes, "where there is no doubt about what was actually said or under what circumstances - if the [page902] statement is video-taped, for instance - then cross-examination of the recipient does nothing to help assess whether the *content* of the hearsay is true" (I.F., at para. 32 (emphasis in original)). Furthermore, as explained above, jury warnings about the dangers of hearsay evidence and *Vetrovec* testimony do little to support the statement's procedural reliability. Jury warnings do not provide an adequate substitute for the traditional safeguards. They are no substitute for other conditions of admissibility. Rules of evidence, such as the rule against hearsay, protect trial fairness and the integrity of the trial process by deeming certain types of evidence presumptively inadmissible.

**90** Because there were few tools available for testing the truth and accuracy of the re-enactment statement, it could only be admitted if the circumstances in which it was made and corroborative evidence, if any, "substantially negate[d] the possibility that the declarant was untruthful" (*Smith* (1992), at p. 933).

**91** The trial judge found that the statement was reliable because it was voluntary, made after Thielen had received legal advice, and was a "free-flowing narrativ[e]". He also relied on the fact that it was incriminating. He reasoned that Thielen put himself at risk, even in the prison system, by implicating himself and others in the murders (para. 40).

**92** However, these circumstances "while relevant, in essence simply point to an absence of factors that, if present, would detract from an otherwise trustworthy statement" (*Couture*, at para. 101). They do not provide a circumstantial guarantee of trustworthiness. Furthermore, while Thielen incriminated himself in the murders in the re-enactment video, he had already done so in his statements to police following his arrest, and during the Mr. Big operation. And while he may have put himself at risk in the prison system by implicating Bradshaw, he nonetheless [page903] benefited from the opportunity of reduced criminal liability: he pled guilty to the lesser charge of second degree murder. Thielen clearly had a significant motive to lie about Bradshaw's involvement in the murders. The Court of Appeal rightfully noted that "[t]he [trial] judge did not sufficiently address the issues that would detract from the truthfulness of Mr. Thielen's statements, including his considerable motive to lie to extricate himself from his admissions to Cst. B. that he committed first degree murder, not once, but twice" (para. 37).

**93** Finally, as discussed above, the corroborative evidence relied on by the trial judge was of no assistance in establishing threshold reliability.

**94** The hearsay danger raised by the re-enactment evidence, namely the inability to investigate Thielen's sincerity about Bradshaw's participation, is particularly difficult to overcome in this case. Thielen had a motive to lie about Bradshaw's involvement in the murders and he initially did not implicate Bradshaw in the murders. Thielen is also a *Vetrovec* witness, a witness who cannot be trusted due to his unsavoury character. There are few tools available to the trier of fact to test Thielen's sincerity. The circumstances in which the statement came about, and the evidence led at the *voir dire*, do not substantially negate the possibility that Thielen lied about Bradshaw's participation in the murders.

**95** This is not a case where the hearsay "presents minimal dangers and its *exclusion*, rather than its admission, would impede accurate fact finding" (*Khelawon*, at para. 2 (emphasis in original)). Rather, admitting the re-enactment statement would undermine the truth-seeking process and trial fairness. Hearsay is presumptively *inadmissible* and the trial judge erred in finding that this presumption was rebutted.

[page904]

V. Conclusion

**96** I conclude that the trial judge erred in admitting the re-enactment statement into evidence. The Crown failed to establish the threshold reliability of this statement on a balance of probabilities.

**97** I would dismiss the appeal. I agree with the British Columbia Court of Appeal that the convictions be set aside and a new trial ordered.

The reasons of Moldaver and Côté JJ. were delivered by

## MOLDAVER J. (dissenting)

I. Overview

**98** At issue in this appeal is the admissibility of a video re-enactment[3] of the events surrounding the murders of Laura Lamoureux and Marc Bontkes in March 2009. In the re-enactment, which occurred in August 2010, some 17 months after the murders, Roy Thielen describes for the police how he and the respondent, Robert Bradshaw, carried out the murders together. After Mr. Thielen refused to testify at Mr. Bradshaw's trial, the trial judge admitted the re-enactment under the principled approach to hearsay evidence.

**99** My colleague, Karakatsanis J., concludes that the trial judge erred in doing so. She reaches this conclusion on the basis of a restrictive new test that departs from the functional approach to threshold reliability which this Court has endorsed in its modern jurisprudence.

**100** With respect, I disagree with my colleague's approach and her conclusion. I acknowledge that [page905] Mr. Thielen's re-enactment was not problem-free and that hearsay dangers are generally more pronounced when a declarant is not available to be cross-examined. However, this was an unusual case, in that there was exceptionally powerful corroborative evidence, including surreptitiously recorded conversations in which Mr. Bradshaw admitted his involvement in the two murders. In addition, the trial judge adopted a number of procedural safeguards which placed the jury in a position to critically evaluate the impugned evidence. These included the limited admission of prior inconsistent statements taken by police officers along with the opportunity to cross-examine them, strict

cautionary instructions to the jury and wide latitude given to defence counsel to canvass the same points in his closing submissions that he would have canvassed had he been able to cross-examine Mr. Thielen.

**101** In conjunction, these factors - powerful corroborative evidence and procedural safeguards - were capable of satisfying the test for threshold reliability. The principled approach to hearsay should not stand in the way of the truth-seeking function of a trial where the impugned evidence is shown to be trustworthy and the jury has the tools it needs to critically evaluate its ultimate reliability. This was the conclusion of the trial judge, who was uniquely positioned to make this determination. In my view, his ruling admitting the video re-enactment was amply supported by the record and error-free. I see no basis in fact or law to interfere with it.

**102** The trial judge's decision to reject a defence application to tender another hearsay statement by Mr. Thielen which did not implicate Mr. Bradshaw is also entitled to deference. I would uphold it.

**103** Accordingly, I would allow the appeal, set aside the judgment of the British Columbia [page906] Court of Appeal ordering a new trial and restore Mr. Bradshaw's convictions for the first degree murders of Ms. Lamoureux and Mr. Bontkes.

## II. Analysis

**104** The modern approach governing the admissibility of hearsay evidence is the principled approach. Under this approach, hearsay evidence can be admitted where it is necessary and where it meets the test for threshold reliability. It is uncontested that Mr. Thielen's refusal to testify at trial satisfies the necessity criterion. The focus of this appeal is on whether Mr. Thielen's re-enactment meets the test for threshold reliability.

*The Test for Threshold Reliability*

**105** Hearsay evidence is presumptively inadmissible primarily because of the difficulty in testing its reliability. There is always a risk that a witness may misperceive the facts, wrongly remember them, narrate events in a misleading or incomplete manner, or make an intentionally false assertion. When a statement is made in court, traditional safeguards - such as the presence of the declarant in the courtroom and cross-examination - protect against the danger of falsehoods or inaccuracies going undetected by the trier of fact. Without the declarant being present in court and subjected to contemporaneous cross-examination, the trier of fact may be unable to detect mistakes, exaggerations or deliberate falsehoods: *R. v. Baldree*, 2013 SCC 35, [2013] 2 S.C.R. 520, at paras. 31-32; *R. v. Khelawon*, 2006 SCC 57, [2006] 2 S.C.R. 787, at para. 2.

**106** The extent to which the reliability of hearsay evidence may be difficult to assess varies according to context. In certain circumstances, the challenges in assessing the declarant's perception, memory, narration or sincerity and the dangers arising from this will be sufficiently overcome to [page907] meet the test for threshold reliability: *R. v. Devine*, 2008 SCC 36, [2008] 2 S.C.R. 283, at para. 22; *R. v. Blackman*, 2008 SCC 37, [2008] 2 S.C.R. 298, at para. 35; *Khelawon*, at para. 61.

**107** The principled approach to hearsay recognizes that threshold reliability can be met in three ways: (1) where the statement has sufficient features of substantive reliability; (2) where the statement has adequate features of procedural reliability; or (3) where the statement does not satisfy either of the first two ways, but incorporates features of both which, in combination, justify its admission. As I will explain, this case engages the third way and provides this Court with an opportunity to clarify its operation for the first time.

**108** First, substantive reliability in this context refers to a statement's degree of trustworthiness. Features of substantive reliability include the circumstances in which the statement was made and the existence of extrinsic evidence capable of corroborating or contradicting it: *R. v. Youvarajah*, 2013 SCC 41, [2013] 2 S.C.R. 720, at para. 30; *Khelawon*, at para. 62; *Blackman*, at para. 35; *R. v. Couture*, 2007 SCC 28, [2007] 2 S.C.R. 517, at para. 80. In the absence of procedural safeguards, these features of substantive reliability will, on their own, satisfy the

threshold reliability requirement where they show that there is "no real concern about a statement's truth and accuracy": *Couture*, at paras. 98 and 100; *Devine*, at para. 22; *Khelawon*, at para. 62.[4] For example, in *R. v. Khan*, [1990] 2 S.C.R. 531, features of substantive reliability justified the admission of a three-and-a-half-year-old child's hearsay statement describing a sexual act, in that the statement was made spontaneously and was powerfully corroborated by a semen stain found on her clothing.

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**109** Second, threshold reliability may be established where there are adequate features of procedural reliability, namely, procedural safeguards in place when the statement is made or at trial that permit the trier of fact to assess the statement's ultimate reliability: *Youvarajah*, at para. 30; *Khelawon*, at para. 63; *Blackman*, at para. 35; *Couture*, at para. 80. In the absence of features of substantive reliability indicating a statement's trustworthiness, threshold reliability will be satisfied if these procedural safeguards, on their own, demonstrate that without contemporaneous cross-examination of a witness in court, a hearsay statement's "truth and accuracy can nonetheless be sufficiently tested" by the trier of fact: *Khelawon*, at para. 63; *Devine*, at para. 22; *Couture*, at para. 80. Where features of procedural reliability *alone* are relied on, some form of cross-examination of the declarant has generally been required to satisfy the test for threshold reliability. For example, courts have held that adequate substitutes for testing truth and accuracy are present in preliminary hearing testimony (see *R. v. Hawkins*, [1996] 3 S.C.R. 1043) and prior inconsistent statements that are video-taped and taken under oath where the declarant has recanted but remains available to be cross-examined at trial (see *R. v. B. (K.G.)*, [1993] 1 S.C.R. 740).

**110** As Charron J. explained in *Khelawon*, characterizing these procedural safeguards as factors which indicate a statement's threshold *reliability* is "somewhat of a misnomer" (para. 80). These tools for testing hearsay evidence do not enhance the reliability of the statement, but rather ensure that the trier of fact is sufficiently equipped to evaluate the ultimate reliability of the statement: see also D. M. Paciocco and L. Stuesser, *The Law of Evidence* (7th ed. 2015), at p. 138.

**111** Finally, threshold reliability may be established where the statement has adequate features of *both* substantive and procedural reliability. [page909] These two categories that inform threshold reliability are not mutually exclusive: *Youvarajah*, at para. 30; *Khelawon*, at para. 66; *Devine*, at para. 22; *Blackman*, at para. 35; *Couture*, at paras. 80 and 99. Rather, features of procedural reliability and substantive reliability may, in combination, satisfy threshold reliability: *Couture*, at para. 99; *R. v. Hamilton*, 2011 ONCA 399, 271 C.C.C. (3d) 208, at para. 156. In *R. v. U. (F.J.)*, [1995] 3 S.C.R. 764, the Court applied this approach, drawing on features of both substantive and procedural reliability to justify the admission of a hearsay statement (para. 53).

**112** Thus, a statement that is not admissible under the first two principal ways of establishing threshold reliability may still be admitted under this third way. Where a statement has a sufficient level of trustworthiness, relative to the strength of the procedural safeguards for the trier of fact to evaluate its ultimate reliability, the statement is safe to admit. Put another way, "[s]o long as [the hearsay statement] can be assessed and accepted by a reasonable trier of fact, then the evidence should be admitted": Paciocco and Stuesser, at p. 134.

**113** It is important to keep in mind that threshold reliability is distinct from ultimate reliability. The trial judge does not need to be satisfied that the hearsay statement is true for it to meet the threshold reliability requirement under any of the three ways set out above. As with the common law tests for Mr. Big statements and expert evidence, the reliability of a hearsay statement need not be established *to a point of certainty* before it can be admitted: *R. v. Hart*, 2014 SCC 52, [2014] 2 S.C.R. 544, at para. 98; *R. v. Abbey*, 2009 ONCA 624, 246 C.C.C. (3d) 301, at para. 89. Otherwise, the trier of fact's role of determining the ultimate reliability of a hearsay statement will have been usurped.

**114** On several occasions, this Court has discussed the danger of conflating threshold and [page910] ultimate reliability. In *Khelawon*, Charron J. stated, at para. 50:

> It is important that the trier of fact's domain not be encroached upon at the admissibility stage. If the trial is before a judge and jury, it is crucial that questions of ultimate reliability be left for the jury - in a criminal trial, it is constitutionally imperative. If the judge sits without a jury, it is equally important that he or she not prejudge the ultimate reliability of the evidence before having heard all of the evidence in the case. Hence, a distinction must be made between "ultimate reliability" and "threshold reliability". Only the latter is inquired into on the admissibility *voir dire*. [Emphasis added.]

This cautionary note was echoed in *Blackman*, at para. 56: "It is essential to the integrity of the fact-finding process that the question of ultimate reliability not be pre-determined on the admissibility *voir dire*: see *Khelawon*, at para. 93."

**115** In this regard, I agree with the observations of Watt J.A. in *R. v. Carroll*, *2014 ONCA 2*, *304 C.C.C. (3d) 252*, at para. 111, that the party tendering hearsay

> need not eliminate all possible sources of doubt about the perception, memory or sincerity of the declarant. All that was required in this case was that the circumstances in which the statements were made and any relevant extrinsic evidence provided the trier of fact with the means to critically evaluate the honesty and accuracy of the declarant ... . [Citations omitted.]

**116** In other words, as with expert evidence and Mr. Big confessions, the trial judge is simply tasked with deciding "the threshold question of 'whether the evidence is worthy of being heard by the jury'": *Hart*, at para. 98, quoting *Abbey*, at para. 89.

**117** I am satisfied that the re-enactment in the present case was admissible under the third way of establishing threshold reliability. As I will explain, there was powerful corroborative evidence indicating the statement's trustworthiness and a number of [page911] procedural safeguards that provided the jury with the tools it needed to evaluate its truth and accuracy. With respect, I believe that in reaching a different conclusion, my colleague has departed from the functional approach to threshold reliability by: (1) unduly restricting the extrinsic evidence that a court can consider when assessing a statement's substantive reliability; and (2) adopting a narrow view of the procedural safeguards available at trial that can equip the jury with the tools it needs to assess the ultimate reliability of a statement.

(1) The Extrinsic Evidence That a Court Can Consider When Assessing Substantive Reliability

**118** My colleague maintains that "at the threshold reliability stage, corroborative evidence is used in a manner that is qualitatively distinct from the manner in which the trier of fact uses it to assess the statement's ultimate reliability" (para. 42). In her view, "[a] trial judge can only rely on corroborative evidence to establish threshold reliability if it shows, when considered as a whole and in the circumstances of the case, that the only likely explanation for the hearsay statement is the declarant's truthfulness about, or the accuracy of, the material aspects of the statement" (para. 44).

**119** Respectfully, my colleague's test gives rise to two difficulties. First, her test would replace the functional approach that this Court has repeatedly endorsed, with a restrictive test that unnecessarily complicates the analysis and discards crucial information for evaluating threshold reliability. The functional approach emphasizes that there is no bright-line distinction between factors that inform threshold and ultimate reliability. Rather, the inquiry is focused on whether the extrinsic evidence addresses hearsay dangers by providing information about whether the statement is trustworthy:

> In each case, the scope of the inquiry must be tailored to the particular dangers presented by the evidence and limited to determining the evidentiary question of admissibility.
>
> [page912]
>
> ...

> ... Relevant factors should not be categorized in terms of threshold and ultimate reliability. Rather, the court should adopt a more functional approach ... and focus on the particular dangers raised by the hearsay evidence sought to be introduced and on those attributes or circumstances relied upon by the proponent to overcome those dangers.

(*Khelawon*, at paras. 4 and 93; see also para. 55.)

**120** My colleague's approach instead creates a "threshold test within the threshold test", which is

> subject to the same criticisms which arise from the [absolute] exclusion of corroborating or conflicting evidence. The categorizing or labelling of evidence that is suitable for including in the *decision-making process* of hearsay admissibility is neither necessary nor desirable. [Emphasis in original.]

(S. Akhtar, "Hearsay: The Denial of Confirmation" (2005), 26 C.R. (6th) 46, at p. 60)

**121** Second, in applying her approach, my colleague parses the analysis by examining whether each individual piece of corroborative evidence demonstrates that the "only likely explanation" is the declarant's truthfulness. This ignores the reality that even if an individual piece of extrinsic evidence does not satisfy my colleague's requirement on its own, it may nonetheless work in conjunction with other extrinsic evidence or features of substantive reliability to satisfy the test for threshold reliability (see *R. v. McNamara (No. 1)* *(1981), 56 C.C.C. (2d) 193* (Ont. C.A.), at pp. 278-79, points 4 and 5, on the nature of corroborative evidence in general). Yet according to her test, for a piece of corroborative evidence to make its way onto the evidentiary scale for threshold reliability purposes, it must effectively be independently capable of tipping the scale. This restrictive test fails to look at the picture as a whole and discards corroborative evidence that could play an important role in satisfying threshold reliability.

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**122** That said, I acknowledge that it may be necessary for the trial judge to limit the scope of extrinsic evidence that can be considered in a hearsay *voir dire*. As Paciocco and Stuesser note (at p. 134): "There is concern, however, that the *voir dire* on the admissibility of the hearsay evidence could well overtake the trial... . The difficulty is where to draw the line and the reality [is] that there is no fixed line" (emphasis added). I agree that such concerns must be addressed on a case-by-case basis, which is consistent with the functional approach to the admissibility of hearsay endorsed in *Khelawon*: see *R. v. R. (T.)*, *2007 ONCA 374*, *85 O.R. (3d) 481*, at para. 19; *R. v. Lowe*, *2009 BCCA 338*, *274 B.C.A.C. 92*, at para. 78. In my opinion, the line should be drawn where the trial judge is of the view that the probative value of certain corroborative evidence is tenuous and outweighed by its prejudicial effect in prolonging and complicating the proceedings - in other words, where the bang is not worth the buck. Trial judges should be trusted to make this determination and exercise restraint when considering extrinsic evidence to ensure the trial proceedings are not derailed by the *voir dire*: *Blackman*, at para. 57.

### (2) The Role of Safeguards Implemented at Trial in Establishing Procedural Reliability

**123** As Charron J. held in *Khelawon*, "the optimal way of testing evidence adopted by our adversarial system is to have the declarant state the evidence in court, under oath, and under the scrutiny of contemporaneous cross-examination" (para. 63). It follows that where no meaningful cross-examination is possible, trial judges should be particularly cautious when determining the admissibility of a hearsay statement. However, where there are adequate substitutes for these traditional safeguards, "common sense tells us that we should not lose the benefit of the evidence": *Khelawon*, at para. 63. A trial judge may have procedural safeguards at his or her disposal that can provide the trier of fact with the tools needed to evaluate the ultimate reliability of hearsay evidence.

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**124** In this case, the Court of Appeal held that the trial judge erred in considering procedural safeguards that were

implemented at trial in evaluating the threshold reliability of the re-enactment. According to the Court of Appeal, only safeguards in existence at the time of the statement could be considered:

> The guarantee of trustworthiness and accuracy at the threshold test does not arise as a result of anything a judge or the Crown at trial can do. Safeguards are those in place when the statement is taken, for example, placing the person under oath, warning them of the consequences of lying under oath and so on, but that is not the situation here. The judge looked at safeguards that could be imposed at trial, which do not assist in ascertaining threshold reliability. [Emphasis added; para. 30.]

**125** I agree with the Crown that safeguards that support procedural reliability include those which can be implemented at trial. In my view, there is no principled distinction between safeguards in place at the time the hearsay statement was made and safeguards available at trial. Both enhance the ability of the trier of fact to critically evaluate the evidence.

**126** This is well established in the jurisprudence. For example, where a recanting declarant is available to be cross-examined at trial on a prior statement, this significantly enhances the trier of fact's ability to evaluate its reliability: *Khelawon*, at para. 66; *Devine*, at para. 19; *Couture*, at para. 92; *B. (K.G.)*, at pp. 795-96. In addition, the cross-examination of a third party who witnessed the declarant's demeanour may provide an added procedural safeguard implemented at trial: *U. (F.J.)*, at para. 32; *B. (K.G.)*, at p. 792.

**127** There are also other tools that can be implemented at trial to assist the jury in evaluating a hearsay statement. As this case illustrates, jury cautions, the limited admission of prior inconsistent statements that contradict the hearsay statement, requiring the Crown to call the police officers who took prior inconsistent statements as witnesses so that they can be cross-examined by defence counsel, [page915] and permitting enhanced leeway for defence counsel during closing submissions may also enable the trier of fact to test a statement's truthfulness and accuracy. The trial judge is uniquely positioned to adapt and implement these measures based on the specific circumstances of the case.

**128** My colleague does not consider or address several safeguards referred to above upon which the trial judge relied. In particular, she rejects the viability of jury instructions as a procedural safeguard, asserting that "[i]nstructing a jury on *how* to evaluate a statement that it [the jury] lacks the *means* to evaluate does not address the hearsay dangers that underlie the exclusionary rule" (para. 29 (emphasis in original)). In my respectful view, this statement oversimplifies the issue.

**129** Jury instructions can be a *means* of assisting the jury with the evaluation of a hearsay statement. Like cross-examination, instructions can draw a jury's attention to evidentiary concerns, which ameliorates hearsay dangers by helping the jury assess the reliability of a statement: see *R. v. Goodstoney*, *2007 ABCA 88*, *218 C.C.C. (3d) 270*, at paras. 58 and 92; *R. v. Blackman* *(2006), 84 O.R. (3d) 292* (C.A.), at paras. 81-87, aff'd *2008 SCC 37*, *[2008] 2 S.C.R. 298*. For example, an instruction cautioning a jury about a declarant's motive to fabricate and a suggestion of a motive to fabricate put to a witness in cross-examination can both alert a jury to a concern regarding sincerity, which helps it assess whether the statement is reliable. Further, jury instructions include a caution to resolve any doubt in favour of the accused.

**130** It goes without saying that cross-examination is a superior means of testing evidence because it allows the jury to observe how a witness responds - be it a denial, an admission or an explanation. However, in setting out the potential dangers of a [page916] hearsay statement, jury instructions are capable of enhancing, to a limited extent, the procedural reliability of the statement. In this case, to be clear, the instructions were only one feature of a package of safeguards adopted by the trial judge to put the jury in a position whereby it could critically evaluate the ultimate reliability of the re-enactment.

**131** Ultimately, my colleague's unwillingness to consider the various procedural safeguards relied upon by the trial judge in this case leads her to conclude that, because the hearsay statement does not have sufficient features of substantive reliability, it cannot be admitted. With respect, this skirts the third way of establishing threshold reliability

- the one applied by the trial judge in this case - in which features of substantive and procedural reliability may, in conjunction, justify the admission of a hearsay statement.

**132** I now turn to the issue of whether the trial judge erred in admitting the re-enactment under this third way.

## III. Application to the August 2, 2010 Re-enactment

### A. *The Hearsay Dangers Raised by the Re-enactment*

**133** In this case, the primary hearsay danger raised by the re-enactment was the possibility that Mr. Thielen was lying about Mr. Bradshaw's involvement in the murders. Mr. Thielen made prior inconsistent statements and he was an accomplice in both murders. The concern that the jury could not assess Mr. Thielen's sincerity was therefore a particularly acute hearsay danger.

**134** The challenges of testing Mr. Thielen's memory and perception also created hearsay dangers, given his drug abuse at the time of the events and the nearly 17 months that had elapsed between the murders and the re-enactment. My colleague suggests that Mr. Thielen's sincerity was the sole [page917] danger in issue, dismissing Mr. Thielen's memory and perception concerns as "minimal" (para. 64). In my view, this is not supported by the record. During oral submissions on the *voir dire*, defence counsel specifically referred to memory and perception concerns that he said detracted from the re-enactment's reliability. In doing so, he did not characterize these as weak or minimal. Rather, he stated:

> Now, I also want to highlight to you some of the other overriding factors that you have to consider in assessing threshold reliability, and those are that Mr. Thielen has a long-term substance abuse problem. His statement are replete with references to being foggy, to having no recollection, all of which he attributes to drug use and, I might say, the fact is that he's giving this video re-enactment 17 months after the fact. [Emphasis added.]

(A.R., vol. VII, at p. 147)

In my view, Mr. Bradshaw's trial counsel was in a better position than this Court to assess whether it was "plausible" that Mr. Thielen's memory of Mr. Bradshaw's role in the killings was inaccurate. In light of defence counsel having raised these concerns, the trial judge can hardly be faulted for responding to them.

**135** As I will explain, however, these hearsay dangers - sincerity along with memory and perception - were sufficiently overcome by features of both substantive and procedural reliability that permitted the trier of fact to evaluate the reliability of the re-enactment.

### B. *The Substantive Reliability of the Re-enactment*

**136** The substantive reliability of the re-enactment was significantly enhanced by both powerful extrinsic evidence that corroborated its content and the circumstances in which it took place. I acknowledge that these features of substantive reliability, on their own, were insufficient to justify the admission [page918] of the re-enactment under the first way of meeting threshold reliability. That said, they went a long way toward establishing the trustworthiness of the re-enactment. In my view, this attenuated the importance of cross-examination and the relative strength of the procedural safeguards needed to meet the third way of establishing threshold reliability.

#### (1) The Powerful Corroborative Evidence

**137** Mr. Thielen's re-enactment was corroborated by three separate groups of evidence: (a) surreptitiously recorded conversations with Mr. Bradshaw, in which Mr. Bradshaw admitted his involvement in the murders; (b) circumstantial evidence implicating Mr. Bradshaw in the murders; and (c) forensic evidence from the crime scenes

confirming Mr. Thielen's account of the details of the murders. As stated, this corroborative evidence must be examined as a whole, not assessed on a piecemeal basis. Considered cumulatively, this evidence provides powerful support for the trustworthiness of Mr. Thielen's re-enactment.

(a) *The Recorded Conversations*

**138** This case is unusual, in that the most compelling corroborative evidence comes from Mr. Bradshaw's own admissions. As noted by my colleague, two surreptitiously recorded conversations with Mr. Thielen "provide direct evidence of Bradshaw's involvement in the murders" (para. 74).

(i) The July 21, 2010 Conversation

**139** The first recorded conversation took place approximately 16 months after the two murders at a local hotel on July 21, 2010. It followed Mr. Thielen's meeting earlier that day with "Mr. Big", during which Mr. Thielen implicated both himself and Mr. Bradshaw in the two murders. In [page919] the meeting with Mr. Big, Mr. Thielen was told by undercover officers posing as members of a criminal organization to discuss the murders with Mr. Bradshaw in order to ensure there were no loose ends that needed to be brought to Mr. Big's attention.

**140** The first eight minutes or so of the conversation between Mr. Thielen and Mr. Bradshaw at the hotel were not captured because they were in a washroom together and their discussion was muffled by the sound of running water. After an undercover officer called Mr. Thielen on his phone, Mr. Bradshaw and Mr. Thielen left the washroom and the conversation continued in the hotel room where it could be heard. Neither Mr. Thielen nor Mr. Bradshaw knew they were being recorded. During this conversation, Mr. Bradshaw admitted to being present during the murder of Ms. Lamoureux (who went by the moniker "Double 'D'"):

Thielen: 'Kay, remember like my first one, Double 'D'?

Bradshaw: Uh-hm.

Thielen: Right? When you parked, right. Is there anybody that could have seen me?

Bradshaw: Houses.

Thielen: What?

Bradshaw: The houses around us.

Thielen: Right.

Bradshaw: And they said they saw a white Acura leaving.

Thielen: Exactly.

Bradshaw: Cobalt. Right, we were in the black

Thielen: right? ... there's nothing I touched,

Bradshaw: No, that's a tactic.

[page920]

Thielen: That's a tactic?

Bradshaw: Yeah. That's what I think. My personal opinion. 'Cause if they had anything fuckin', (knocking sound) [video shows Bradshaw knocking on wooden table] like that -

Thielen: Yeah.

Bradshaw: -pff-

Thielen: added.] There's nothing man. [Emphasis

(A.R., vol. XII, at pp. 51-52)

**141** Later, Mr. Bradshaw seemingly agreed that he and Mr. Thielen did not have a plan for murdering Ms. Lamoureux. He described how Ms. Lamoureux called him to purchase drugs and he picked up Mr. Thielen before the murder:

Bradshaw: ... Before I picked you up. I think you were just getting ready weren't you?

Thielen: Yeah, well we didn't-

Bradshaw: ...

Thielen: -really hatch a plan.

Bradshaw: ...

Thielen: We didn't really have that one planned did we? It was just kinda on a whim remember?

Bradshaw: Maybe-

Thielen: ou went-

Bradshaw: -and she called me-

Thielen: -you went, you went and sold her dope and then she wanted to trade it back.

Bradshaw: Yeah.

[page921]

Thielen: And then, 'cause I wasn't with you went and met her and you picked me up from somewhere out in the area.

Bradshaw: Okay. [Emphasis added.]

(A.R., vol. XII, at pp. 60-61)

This was consistent with Mr. Thielen's re-enactment. It was also corroborated by logs on Ms. Lamoureux's phone, which was recovered from the crime scene and showed several calls with Mr. Bradshaw immediately prior to the murder.

**142** Mr. Bradshaw implicated himself in the murder of Mr. Bontkes as well. He described how he and Mr. Thielen had worn gloves and waited for Michelle Motola (Mr. Bradshaw's then girlfriend) to drive up with Mr. Bontkes, which corresponds with Mr. Thielen's re-enactment. He also told Mr. Thielen that Ms. Motola did not see who shot Mr. Bontkes. Ms. Motola thought the shooter was Mr. Thielen, when it fact it was Mr. Bradshaw:

Thielen: the van? On the second one, did we touch

Bradshaw: time. No, we had gloves on the whole

Thielen: 'Kay.

Bradshaw: As soon as got out of the car,
gloves. And then we pulled the piece
out. Cleaned all the shells off. Put
everything back together and waited.
And then there's fuckin' ...

Thielen: ... did she? But Michelle didn't do the last

Bradshaw: She was there, but she didn't see
shit. She didn't see what
happened, she thought it was you. She
didn't even know it was me.

Thielen: Okay.

[page922]

Bradshaw: So, she's fuckin', even if she wanted to, she couldn't even tell it straight, because of that advantage because she was (smacking sound) we were over here, right? She's sitting her like this and this ... everything's going on over here. She doesn't know. She doesn't know anything for sure. [Emphasis added.]

(A.R., vol. XII, at pp. 52-53)

**143** Mr. Bradshaw also discussed their actions after the murders:

Thielen: Where were we before that? Where were we after that?

Bradshaw: My house.

Thielen: And before, at your house, right?

Bradshaw: All my house.

Thielen: Both times?

Bradshaw: Both. Before and after. We stashed the thing in my house, took all the shit, you fuckin' left with it. You walked over to the fuckin' ...

Thielen: later. And then I came back and got it

Bradshaw: Yeah.

Thielen: ... got rid of it, right?

Bradshaw: ... the pieces that were missing were my shoes and I burned them personally. [Emphasis added.]

(A.R., vol. XII, at p. 53)

**144** Finally, the two discussed the investigations and potential sources of evidence regarding the two murders:

Thielen: it? Have you talked to anybody about

[page923]

Bradshaw: Nah.

Thielen: Nobody?

Bradshaw: Nothing.

Thielen: Just absolutely nobody, so if-

Bradshaw: No.

Thielen: -it's anybody yapping their gums it's Michelle?

Bradshaw: That's it. But people have been saying that I killed Double 'D' since it happened.

Thielen: I know, I know, I've been-

Bradshaw: ...

Thielen: -hearing so many things, I heard-

Bradshaw: ...

Thielen: -stories about it in jail.

Bradshaw: -about me, blah, blah, blah. Fuckin' everybody's saying ... whatever, that's hearsay. That doesn't make a fuckin' difference ... to nothing ... anyone that even has a half fuckin' I know, is Michelle. The only one. Because she knows for a fact who was there, that's it. And it can only be one or the other.

Thielen: On the one, on the one, that's it.

Bradshaw: Yeah, only on that one. Right? She doesn't know shit about the first one.

Thielen: And so after both of them we went to your house?

Bradshaw: Uh-hm. No, not after the first one.

Thielen: Where'd we go?

Bradshaw: I think we went to your house after the first one.

Thielen: And you just dropped me off? And you kept goin' on right?

[page924]

Bradshaw: I think I was working.

Thielen: Yeah.

Bradshaw: Yeah.

Thielen: Okay. So, we're not gonna say nothing about this? Not gonna talk to nobody about this?

Bradshaw: I'm not sweating it to be honest. [Emphasis added.]

(A.R., vol. XII, at pp. 55-56)

(ii) The July 23, 2010 Conversation

**145** The second conversation took place two days later at Bothwell Park on July 23, 2010. Undercover officers posing as members of a criminal organization again instructed Mr. Thielen that he needed to speak to Mr. Bradshaw about the murders, particularly with respect to a "dry run" that had preceded the murder of Mr. Bontkes. This dry run involved Ms. Motola picking up Mr. Bontkes and taking him for a drive, while Mr. Bradshaw pretended to be unconscious in the back seat and Mr. Thielen hid under a jacket across the back seat floor with a firearm. The plan to kill Mr. Bontkes on that occasion failed because, in Mr. Bradshaw's words, "[i]t was my fault 'cause I was supposed to string him up and then you were supposed to put the bitch on him ... . And I didn't do that" (the "bitch" being the gun they had at the time) (A.R., vol. XII, at p. 76).

**146** Because this conversation centres more on the dry run of the murder of Mr. Bontkes, it is somewhat less compelling in corroborating Mr. Bradshaw's involvement in the actual murders than the hotel conversation. Nevertheless, Mr. Bradshaw's admitted participation in the dry run strongly supports his motive for the killing of Mr. Bontkes. In addition, Mr. Bradshaw did refer to the murders themselves, mentioning the ongoing police investigation and suggesting that if the police had any evidence, they would have already acted:

[page925]

Thielen: So, I just, I'm trying to go through everything because how much dope I was on back then, I'm so fuzzy with a lot of shit, man. I thought I was-

Bradshaw: Even better.

Thielen: No, it's not even better because I-

Bradshaw: Why?

Thielen: -I'm goin' through stuff ... trying to figure out what the hell needs to be fixed here. So we don't get popped, right.

Bradshaw: You could fly through a polygraph on that. If you don't know ...

Thielen: Yeah, I would never, I would never do a polygraph in my life, obviously I'm uh, I'm just trying to figure what is missing and what can be put against us, right, so that we-

Bradshaw: Honestly, like I said I think as long as ... I think the, the rest of it is fuckin' snap shut tight. I think if there was anything left it would have already been done immediately. They wouldn't have waited so long, they're, they're playing the drum, that's all they're doin'. [Emphasis added.]

(A.R., vol. XII, at p. 80)

**147** Mr. Bradshaw later added that no one would have seen Ms. Motola pick up Mr. Bontkes prior to the murder and the only witnesses who could have seen them on the night of Mr. Bontkes's murder was a construction crew they drove past after the murder took place:

Bradshaw: And when she went to go see him, it was just her and then you, so ... no [page926] other eyeballs on that one, the only other thing, the only other people that saw us together was a construction crew.

Thielen: What construction crew?

Bradshaw: Construction crew ... remember that? You went south on 192, down to 32.

Thielen: And there was a construction crew there?

Bradshaw: There was a construction worker on 32. We came across 32, hit 176, came up 176 and the car died. Remember?

Thielen: On that day?

Bradshaw: ... that was that night.

Thielen: No that was the night it all went down. We left and ... phone call ... someone ... sources ... fuck off. Um ...

Bradshaw: Personally, I think, like I said, I think it's fuckin' smooth. You know if I didn't even know you guys at that time, you know, we met at the bar talking maybe a month or so later, whatever. You know, everybody's fuzzy enough ... no one can say for sure, right. That's what I'm talking about. (Chuckles) You know, especially with her.
[Emphasis added.]

(A.R., vol. XII, at p. 82)

It is apparent that "her" referred to Ms. Motola - who was also present for the killing of Mr. Bontkes - as the two went

on to discuss how the police had approached her. The police investigation also confirmed that a construction crew was working in the area at the relevant time.

**148** Reading these two conversations in their entirety, there can be no doubt that Mr. Thielen and Mr. Bradshaw were implicitly - and at times [page927] overtly - discussing their joint involvement in the two murders. This provides powerful corroborative evidence that significantly enhances the substantive reliability of the re-enactment by alleviating concerns about Mr. Thielen's sincerity.

**149** For my colleague, however, these conversations provide "no assistance" in establishing substantive reliability (para. 84) - a remarkable proposition that no one advanced in the proceedings below or before this Court. In her view, Mr. Thielen's truthfulness is not the only likely explanation for the conversations - a conclusion which rests squarely on her second-guessing the trial judge's factual assessment of the conversations and speculating about "outside influence" as a "possible explanation" for them (para. 84).

**150** My colleague makes two points in this regard. First, she maintains that the trial judge did not account for the reduced reliability of Mr. Bradshaw's statements because they were "collected in a Mr. Big operation" (para. 78). With respect, calling these "Mr. Big" statements is a misnomer. Mr. Bradshaw was not the subject of the Mr. Big operation. He believed he was speaking to an accomplice, not to a member of a criminal organization in circumstances involving the type of inducements or implied threats that characterize Mr. Big operations: *Hart*, at paras. 5 and 58-60. The rationales for exercising special caution with Mr. Big confessions therefore simply do not apply. On the contrary, I agree with the trial judge that the fact that these conversations were surreptitiously recorded while both Mr. Thielen and Mr. Bradshaw believed they were privately discussing the details of the murders, as accomplices, significantly enhanced their reliability (ruling on *voir dire* No. 1, *2012 BCSC 2025*, at para. 44 (CanLII)). Any motive for Mr. Bradshaw to falsely implicate himself in such circumstances is mere fancy.

[page928]

**151** Second, my colleague expresses concern that "the initial part [the first eight minutes] of the Best Western conversation was inaudible because Thielen and Bradshaw were in the bathroom and a tap was running" (para. 80). In her opinion, this raises questions about the trustworthiness of the recording.

**152** I disagree. Neither individual knew that they were being recorded. It stretches the bounds of credulity and common sense to think that this initial part of the conversation could explain away the incriminating admissions made by Mr. Bradshaw in the audible part of the conversation. How one could reasonably infer that during these eight minutes, Mr. Bradshaw may have been influenced and prepared to falsely recite his participation in the two murders escapes me. It is clear from the transcript that Mr. Bradshaw was, at times, leading the conversation and volunteering details about the murders without any prompting on Mr. Thielen's part. Unlike my colleague, I do not believe it is appropriate to consider Mr. Bradshaw's trial testimony - that, during these eight minutes, Mr. Thielen asked him to pretend that he had been involved in the murders - in assessing the substantive reliability of the re-enactment. Mr. Bradshaw testified after the re-enactment was admitted and therefore his testimony was not before the trial judge at the time of his ruling. Furthermore, the jury clearly rejected Mr. Bradshaw's testimony that he was lying about his involvement in the murders at Mr. Thielen's request.

**153** If these conversations do not qualify as corroborative evidence supporting a hearsay statement's substantive reliability, then I am at a loss to know what would. Even on the basis of my colleague's restrictive test, they clearly qualify. The only plausible - and certainly the "only likely" - explanation for Mr. Bradshaw's admissions was that he participated in the two murders. It follows, in my view, that the trial judge did not err in relying on Mr. Bradshaw's admissions as powerful corroboration of the truthfulness of Mr. Thielen's re-enactment.

[page929]

(b) *The Circumstantial Evidence Implicating Mr. Bradshaw in the Murders*

**154** The Crown also led circumstantial evidence implicating Mr. Bradshaw in the murders.

**155** Indeed, there are telephone records that connect Mr. Bradshaw to both murders on the nights in question. These records establish a number of calls between Mr. Bradshaw and Ms. Lamoureux on the night she was murdered. Several of these calls took place immediately prior to the murder. This corroborates Mr. Thielen's account of Mr. Bradshaw luring her into a set-up under the ruse of a drug transaction before Mr. Thielen shot her.

**156** Similarly, on the night Mr. Bontkes was killed, telephone records show a number of calls between Mr. Bradshaw and Mr. Thielen, Mr. Thielen and Ms. Motola, and Ms. Motola and Mr. Bontkes - which was the last call registered on Mr. Bontkes's cell phone. This is consistent with Mr. Thielen's account that all three of them participated in the killing.

(c) *The Forensic Evidence From the Crime Scenes Investigation*

**157** In my view, forensic evidence from the crime scenes investigation, which corroborates the details of Mr. Thielen's description of the murders, provides additional support for the trustworthiness of the re-enactment. The trial judge noted that this forensic evidence included: "... where and how the shootings occurred, the number of shots fired, the fact the same gun was used, the positioning of the bodies of Ms. Lamoureux and Mr. Bontkes, the presence and position of the van at High Knoll Park ..." (ruling on *voir dire* No. 1, at para 45).

**158** This evidence responds to the memory and perception concerns raised by defence counsel. It [page930] alleviated the risk that Mr. Thielen's drug abuse and/or the passage of time made his account inaccurate.

**159** In my view, this evidence also addressed Mr. Thielen's overall sincerity. Assessing a declarant's sincerity in a hearsay statement, like assessing the credibility of a witness, is not a mathematical exercise. Where extrinsic evidence corroborates or contradicts the contents of a statement, this affects the statement's overall reliability. If the details of Mr. Thielen's account were belied by the forensic evidence, this would cast further doubt on his sincerity. On the other hand, the corroboration of the details of his account by forensic evidence enhances the substantive reliability of the re-enactment.

**160** I acknowledge that in view of Mr. Thielen's status as an accomplice, the forensic evidence is not as compelling in this case as the corroborative evidence which directly implicated Mr. Bradshaw in the murders: see *Youvarajah*, at para. 62; *R. v. Smith*, *2009 SCC 5*, *[2009] 1 S.C.R. 146*, at para. 15. However, I agree with counsel for the intervener British Columbia Civil Liberties Association that this forensic evidence is relevant and should not be taken off the table.

(2) The Circumstances of the Re-enactment

**161** Beyond the powerful corroborative evidence, there are also other features of the re-enactment that enhance its substantive reliability. The statement was voluntary and detailed, and it was provided after Mr. Thielen received legal advice. It was also delivered in a free-flowing narrative, without any leading questions from the police (ruling on *voir dire* No. 1, at paras. 40-41). Although not under oath, it was made to police officers while Mr. Thielen was under arrest in circumstances which, viewed objectively, would have underscored the importance of telling the truth: *B. (K.G.)*, at p. 792; *R. v. Adjei*, *2013 ONCA 512*, *309 O.A.C. 328*, at para. 45.

[page931]

**162** In addition, Mr. Thielen's motives for participating in the re-enactment with police were important to consider because of the concerns regarding his sincerity. As recognized by this Court in *Blackman*, at para. 42:

> There is no doubt that the presence or absence of a motive to lie is a relevant consideration in assessing whether the circumstances in which the statements came about provide sufficient comfort in their truth and accuracy to warrant admission. It is important to keep in mind, however, that motive is but one factor to consider in the determining of threshold reliability, albeit one which may be significant depending on the circumstances. The focus of the admissibility inquiry in all cases must be, not on the presence or absence of motive, but on the particular dangers arising from the hearsay nature of the evidence. [Emphasis added.]

**163** In my view, the fact that Mr. Thielen's re-enactment went against his own interests is significant in this regard. It directly implicated him in both murders and could be used to incriminate him. It also implicated Ms. Motola, whom he considered to be a "sister". Moreover, he was aware that, in re-enacting the two murders for the police, he was putting himself at risk in the prison system: "... what I'm asked to do here is take the biggest step of my life and bring down a whole bunch of people and you know what else, that's gonna put me at risk for the rest of my life" (A.R., vol. XV, at p. 169). Given the unlikelihood that Mr. Thielen would willingly make a false statement prejudicial to his own interests, this provides further support that the re-enactment is trustworthy.

**164** My colleague takes a different view of Mr. Thielen's motivations for re-enacting the murders. She asserts that Mr. Thielen's statement was not actually made against his interests because he had previously incriminated himself to police and in the Mr. Big operation. She also takes the position that Mr. Thielen had a "significant motive to lie" to gain "the opportunity of reduced criminal liability", citing the fact that he pled guilty to two counts of second degree murder (para. 92).

[page932]

**165** I disagree with both of these assertions. First, the fact that Mr. Thielen had previously implicated himself in both murders to police does not change the fact that the re-enactment was made against his interests. The police clearly wanted to collect as much information as possible from Mr. Thielen and the re-enactment provided detailed and cogent evidence that could be used against him.

**166** Second, the suggestion that Mr. Thielen was seeking leniency is purely speculative. There is no evidence of any inducements or assurances made by the police prior to Mr. Thielen's re-enactment. Indeed, the police rejected Mr. Thielen's requests to see his girlfriend, receive a name change, and be incarcerated in a faraway prison. The fact that Mr. Thielen ultimately pled guilty to second degree murder does not detract from the reliability of his previously made statement. We have no information to suggest that the plea offer had anything to do with his participation in the re-enactment. Indeed, we do not know if the same plea offer was made to Mr. Bradshaw before his trial.

**167** Furthermore, the theory that Mr. Thielen fabricated Mr. Bradshaw's involvement to shift responsibility away from himself is belied by the facts. Mr. Thielen did not minimize his own role in the killings or shift the primary responsibility to Mr. Bradshaw for the murder of Ms. Lamoureux. Instead, he admitted to pulling the trigger himself. Additionally, in my view, Mr. Thielen's prior statement to Mr. Big on July 21, 2010, in which he implicated Mr. Bradshaw in the murders, rebuts any purported motive on Mr. Thielen's part to fabricate Mr. Bradshaw's involvement during the re-enactment. Mr. Thielen had no motive to lie about Mr. Bradshaw's involvement to Mr. Big. Rather, it was against Mr. Thielen's interest to implicate Mr. Bradshaw when speaking to Mr. Big. At that time, Mr. Thielen believed his role in the organization was in jeopardy because of the ongoing police investigation. This jeopardy was only enhanced by [page933] implicating another person in the murders, which could further complicate matters for Mr. Big. Mr. Big repeatedly emphasized that Mr. Thielen had to be honest about the murders to maintain his role in the organization, telling him:

> ... lie to everybody else, but we don't lie to each other here. And uh, and guys that get found out for lying or fuckin' uh, screwing me around are gone... .
>
> ...

> ... if I find out at anytime as we go along that anything you tell me right now is wrong or it's bullshit or it's a lie, and again I'm not sayin' that it is ... but I want to be up front ... then I'm washing my hands of you.

(A.R., vol. XVIII, at pp. 66 and 88-89)

**168** The fact that Mr. Thielen told Mr. Big about Mr. Bradshaw's involvement well before he had any motive to fabricate indicates that he was telling the truth when he re-enacted the two murders for police: see *R. v. Stirling*, *2008 SCC 10*, *[2008] 1 S.C.R. 272*, at para. 5; *Couture*, at paras. 83 and 127-28; *Goodstoney*, at paras. 69-71.

**169** In sum, the substantive reliability of the re-enactment was significantly enhanced by a combination of:

(1) Extrinsic corroborative evidence, including: surreptitiously recorded conversations of Mr. Bradshaw admitting to his involvement in the two murders; circumstantial evidence implicating Mr. Bradshaw in the murders; and forensic evidence from the crime scenes confirming the details of the murders as described by Mr. Thielen.

(2) Circumstantial indicia of trustworthiness, including: the fact that the re-enactment was [page934] voluntary and free flowing; that it was contrary to Mr. Thielen's interest, in that he did not attempt to shift blame to Mr. Bradshaw but instead implicated himself in two counts of first degree murder; and that Mr. Thielen's alleged motivation to fabricate was rebutted by his prior consistent statement to Mr. Big.

C. *The Procedural Reliability of the Re-enactment*

**170** In this case, the jury had the benefit of several substitutes for the traditional safeguards relied on for testing evidence. As my colleague acknowledges, the fact the re-enactment was video-taped ensures an accurate record of the statement and enhances the ability of the jury to observe and evaluate it. In addition, the trial judge took a number of steps to ensure the jury was in a position where it could assess and weigh the reliability of the hearsay statement. These safeguards included the following: requiring the Crown to call officers who were present for the re-enactment and prior inconsistent statements so that defence counsel could cross-examine them on any inconsistencies and any reduced plea offers or inducements made to Mr. Thielen; the limited admission of prior inconsistent statements made by Mr. Thielen to help assess his credibility; and wide latitude for defence counsel to discuss Mr. Thielen's possible motives and challenge the ultimate reliability of the re-enactment in closing submissions.

**171** Further, the trial judge provided detailed cautions to help the jury identify and evaluate the strengths and weaknesses of the re-enactment. Before the video re-enactment was played for the jury, the trial judge provided a mid-trial instruction that told the jury the following:

> That evidence is hearsay evidence, and is not usually permitted as evidence in a court of law. The reason it is [page935] not permitted is because the individual who is offering the evidence is not appearing in the witness box, and testifying and subjecting himself to cross-examination, cross-examination which might reveal lies, inconsistencies, motive for making up a story and so forth. So you will need to consider the weight ultimately that you are going to attach to the evidence that you are about to hear this morning.
>
> Now, that is particularly important because in this case, the person who is offering that evidence is subject to a special warning, and you will hear more about this from me in my final instructions to you on the law. Mr. Thielen, you have heard other witnesses testify, is not only an unsavoury character, having regard to his background in drugs and the drug culture in Langley and Surrey. He has been described as an enforcer. He is certainly of unsavoury character in that regard. You have also and will hear -- I think you have heard that he pled guilty to the second degree murder of Ms. Lamoureux and Mr. Bontkes.

> You will recall when I gave you some opening instructions, I set out some things you should consider when you decide whether or not to believe a witness. Well, you should consider those things when you assess what Mr. Thielen is about to say. But in addition, I must warn you that you should be extremely cautious in accepting Mr. Thielen's testimony. I must caution you it is dangerous to rely on that testimony alone. The reasons are Mr. Thielen has admitted to participation in the commission of the offence. As I've said, he has an unsavoury reputation. He's admitted and pled guilty to a criminal conviction. Mr. Thielen may well have some motive other than the pursuit of truth. All of these things you will need to consider. [Emphasis added.]

(A.R., vol. VIII, at pp. 2-3)

**172** In the jury charge at the close of trial, the trial judge thoroughly and repeatedly cautioned the jurors about Mr. Thielen's re-enactment and instructed them on how to evaluate it. This included the following key excerpts:

> As I explained during in the trial, this evidence [Thielen's re-enactment] was placed before you without the usual testing of evidence by cross-examination, and that you [page936] must therefore be very cautious in determining the reliability of the evidence.
>
> ...
>
> In this case Mr. McMurray was not able to cross-examine Mr. Thielen on the things he said or did in the enactment. He was unable to test Mr. Thielen's memory, credibility, motive of or for the things said and done during the re-enactment. You did not have the opportunity to observe the demeanour of Mr. Thielen in the witness box as he gave his evidence.
>
> Furthermore, the statements Mr. Thielen gave to [Cst. D.] were not given under oath. As a result of all that you should not place the statement of Mr. Thielen on the same footing as the statement of a witness who testifies under oath in the courtroom. You should treat Mr. Thielen's out-of-court statement with special care and, after considering it with all the evidence in this case, give it the weight you think it deserves.
>
> ...
>
> ... In addition, however, I must warn you that you should be extremely cautious in accepting some or any of his testimony. It is dangerous for you to rely on his evidence alone. There are a number of grounds upon which you may question whether his evidence is reliable: Thielen admitted he participated in the commission of the two offences with which Mr. Bradshaw is charged. He plead guilty to second degree murder of Ms. Lamoureux and Mr. Bontkes.
>
> Thielen admitted to an extensive history of criminal conduct, including the attempted murder of Sigurdson. He has an unsavoury reputation. He has given prior inconsistent statements, that is, in his statement particularly to [Cpl. G.] on March the 18th, when he said he had not seen Lamoureux for two months; and to [Cst. B.] on the drive from Edmonton to Calgary. Mr. Thielen might have some motive other than the pursuit of truth in giving his testimony.
>
> The last and most important ground is that of course Mr. Thielen's evidence was not tested by cross-examination. A person who participated in the [page937] commission of an offence would be in a particularly good position to concoct a story that falsely implicates the accused. All that person would need to do is tell a truthful story that could be confirmed easily, and falsely add to it an allegation the accused was also a participant.
>
> ...
>
> ... In this case Thielen made statements to the police that tend to show Mr. Bradshaw was involved in committing the offences you are trying. You should consider those statements with particular care because Thielen may have been more concerned about protecting himself than about telling the truth. [Emphasis added.]

(A.R., vol. I, at pp. 73, 82-83, 85-86 and 96)

**173** In my view, the opportunity to observe Mr. Thielen in the re-enactment video and the numerous procedural safeguards adopted by the trial judge, including these instructions, placed the jury in a position to identify and critically evaluate each of the frailties of the re-enactment that my colleague identifies. To assume that the jury was incapable of following these instructions and appreciating the frailties of this evidence betrays the time-honoured trust and confidence our justice system places in juries. In *R. v. Corbett*, [1988] 1 S.C.R. 670, this Court emphasized the need to "trust the good sense of the jury" in determining what evidence it may hear (p. 691). This point was put succinctly by Donald J.A. in *R. v. Carroll*, 1999 BCCA 65, 118 B.C.A.C. 219, at para. 41:

> Juries are often required to find facts from a melange of evidence. It is not uncommon for cross-examination to use prior statements of several kinds: police statements, testimony given in a previous trial, an inquest or a preliminary inquiry. We have to trust juries to use their common sense in sifting the evidence and to follow the guidance offered by the trial judge. [Emphasis added.]

**174** I share the sentiment expressed by L'Heureux-Dubé J. in dissent in *R. v. Noel*, 2002 SCC 67, [2002] 3 S.C.R. 433, at para. 145, that [page938] courts should trust juries to make proper use of admissible evidence or risk "demean[ing] the jury by suggesting that they are incapable of properly dealing with [the] evidence. Our faith in the jury system is a hollow one if such an attitude is allowed to prevail."

D. *Final Balancing*

**175** In this case, I am satisfied and agree with the trial judge that the re-enactment met the test for threshold reliability on the basis of strong features of substantive reliability, supplemented by sufficient features of procedural reliability. The trial judge was uniquely positioned to make this determination. And, contrary to my colleague's assertions, his analysis discloses no legal error. As a result, his ruling is entitled to deference.

**176** In *Youvarajah*, Karakatsanis J. explained the rationale for this deference (at para. 31):

> The admissibility of hearsay evidence, such as the prior inconsistent statement in this case, is a question of law. Of course, the factual findings that go into that determination are entitled to deference and are not challenged in this case. As well, a trial judge is well placed to assess the hearsay dangers in a particular case and the effectiveness of any safeguards to assist in overcoming them. Thus, absent an error in principle, the trial judge's determination of threshold reliability is entitled to deference: [*Couture* ], at para. 81. [Emphasis added.]

**177** In *Blackman*, Charron J. made a similar observation (at para. 36):

> The trial judge is well placed to determine the extent to which the hearsay dangers of a particular case are of concern and whether they can be sufficiently alleviated. Accordingly, the trial judge's ruling on admissibility, if informed by correct principles of law, is entitled to deference.
>
> [page939]

**178** Ultimately, the trial judge made a difficult call in a close case. It must be emphasized that he was in the best position to make that call based on his assessment of the trustworthiness of the evidence and the jury's ability to evaluate it. Contrary to my colleague's assertions, the trial judge's reasons for admitting the re-enactment were free from error and, as I have endeavoured to demonstrate, were well supported by the record. Indeed, he followed the functional approach that has been repeatedly endorsed by this Court.

**179** I agree with the comments of the Court of Appeal for Ontario in *R. v. S. (S.)*, 2008 ONCA 140, 232 C.C.C. (3d)

158, at paras. 29-30:

> Trial judges cannot consult rules akin to mathematical formulas to tell them how much weight to give to each of the factors. The assessment is case-specific. Different judges will reasonably assign more or less weight to each of the particular factors in any given case.
>
> As long as the trial judge addressed the factors germane to the reliability of the hearsay statement, did not fall into any material misapprehension of the evidence relevant to those factors, and made a reasonable assessment of the weight to be assigned to those factors, this court should not redo the weighing process, but should defer to the trial judge's weighing of those factors. [Emphasis added.]

**180** Respectfully, in my view, it is not the role of this Court to second guess the trial judge's reasonably exercised judgment from a position far removed from the trial setting. Doing so betrays both the deference owed to trial judges and the trust and confidence placed in juries to follow instructions and use their common sense and reason to evaluate evidence. As a result, I would uphold the trial judge's ruling that the re-enactment was admissible.

## IV. Application to the May 15, 2010 Statement

**181** Since I have concluded that the re-enactment was admissible, I must address Mr. [page940] Bradshaw's alternative argument that the trial judge erred in refusing to admit a prior statement by Mr. Thielen given on May 15, 2010, for the truth of its contents.

**182** That statement occurred during a road trip from Edmonton to Calgary that Mr. Thielen took with an undercover office as part of the Mr. Big operation. Their conversation in the car was audio-recorded. During the trip, Mr. Thielen told the undercover officer that he killed Ms. Lamoureux by himself and killed Mr. Bontkes with the assistance of Ms. Motola. He made no mention of any involvement by Mr. Bradshaw.

**183** The May 15, 2010 statement shares the same hearsay dangers as the re-enactment. However, as I will explain, this statement has a number of distinguishing features that add to its frailties and support the trial judge's decision to refuse to admit it for the truth of its contents.

**184** First, it is significant that the statement was not video-recorded. This prevents the jury from observing Mr. Thielen's demeanour and reduces its ability to assess his credibility.

**185** Second, Mr. Thielen's motives were entirely different in this context. He had a strong incentive to exaggerate his individual involvement and responsibility for the murders in order to impress his perceived peer in the criminal underworld: *Hart*, at paras. 68-69. Moreover, the statement cannot be characterized as being against his interests because Mr. Thielen admitted his involvement to an associate, not to the police. Unlike the re-enactment, these circumstances of the May 15, 2010 statement cast doubt over Mr. Thielen's sincerity.

**186** Third, this May 15, 2010 statement was strongly contradicted by extrinsic evidence which suggests that it was untruthful. For example, Mr. Thielen stated that after he shot Mr. Bontkes in [page941] the head and body, Ms. Motola shot him again in the groin area. This version of events was directly contradicted by forensic evidence which showed Mr. Bontkes was not shot in his groin area. Mr. Thielen's omission of any mention of Mr. Bradshaw is also directly contradicted by Mr. Bradshaw's own admissions of involvement in his recorded conversations with Mr. Thielen described above.

**187** The trial judge considered the relevant factors and applied the correct test in finding this statement to be inadmissible for its truth. As indicated, his ruling is entitled to deference. Accordingly, I would not interfere. I say this mindful of the fact that the trial judge may relax the rules of evidence for hearsay tendered by the accused in order to prevent a miscarriage of justice: *R. v. Post*, 2007 BCCA 123, 217 C.C.C. (3d) 225, at paras. 89-90; *R. v. Tash*, 2013 ONCA 380, 306 O.A.C. 173, at para. 89; *R. v. Kimberley* (2001), 56 O.R. (3d) 18 (C.A.), at para. 80. Accepting this principle, I note that this statement was put before the jury as a prior inconsistent statement for the

purpose of evaluating Mr. Thielen's credibility in the re-enactment. Indeed, defence counsel made reference to it in his closing address and submitted to the jury that it was true. As a result, even if the trial judge did err in refusing to admit it for the truth of its contents, I do not think it caused significant prejudice or resulted in a miscarriage of justice that would warrant appellate intervention.

## V. Conclusion

**188** For these reasons, I conclude the trial judge did not err in admitting Mr. Thielen's re-enactment and refusing to admit his May 15, 2010 statement for the truth of its contents. In my respectful view, there is no reason to send this case back for a second trial. Mr. Bradshaw had a fair trial before a properly instructed jury that was well positioned to critically evaluate the reliability of the re-enactment. Accordingly, I would allow the appeal and restore [page942] Mr. Bradshaw's two convictions for first degree murder.

*Appeal dismissed,* MOLDAVER *and* CÔTÉ JJ. *dissenting.*

**Solicitors:**

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*Solicitors for the respondent: Fowler and Smith Law, Vancouver.*

*Solicitor for the intervener the Attorney General of Ontario: Attorney General of Ontario, Toronto.*

*Solicitors for the intervener the British Columbia Civil Liberties Association: Hunter Litigation Chambers, Vancouver.*

*Solicitors for the intervener the Criminal Lawyers' Association of Ontario: Louis P. Strezos & Associate, Toronto; Henein Hutchison, Toronto.*

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1 This rule was criticized for being antithetical to the flexible nature of the principled exception to hearsay (H. Stewart, "*Khelawon*: The Principled Approach to Hearsay Revisited" (2008), 12 *Can. Crim. L.R.* 95, at p. 105) and for leading to the exclusion of manifestly reliable hearsay evidence (S. Akhtar, "Hearsay: The Denial of Confirmation" (2005), 26 C.R. (6th) 46).

2 Ensuring that corroborative evidence goes to the truthfulness or accuracy of the material aspects of the hearsay statement is particularly important when the hearsay statement is lengthy. In this case, for example, a 200-page transcript from the re-enactment video was given to the jury. If the trial judge were entitled to consider any evidence that corroborated *any* part of this statement in assessing its admissibility, the *voir dire* could become a trial within a trial (*Blackman*, at para. 57).

3 In these reasons, Mr. Thielen's hearsay re-enactment refers to both the visual demonstrations and verbal statements he made in the video to describe how the murders and related events took place.

4 While this is clearly a high standard, it does not require the trial judge to be convinced to a point of certainty that the statement is true, otherwise the difference between threshold and ultimate reliability, which this Court has consistently maintained, would be lost (see paras. 113-16 below).

**CT-2019-005**

**THE COMPETITION TRIBUNAL**

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

**AND IN THE MATTER OF** the acquisition by Parrish & Heimbecker, Limited of certain grain elevators and related assets from Louis Dreyfus Company Canada ULC;

**AND IN THE MATTER OF** an application by the Commissioner of Competition for one or more orders pursuant to section 92 of the *Competition Act*.

**BETWEEN:**

**THE COMMISSIONER OF COMPETITION**

**Applicant**

**– and –**

**PARRISH & HEIMBECKER, LIMITED**

**Respondent**

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**COMMISSIONER'S BOOK OF AUTHORITIES CHALLENGING THE ADMISSIBILITY OF CERTAIN PROPOSED EVIDENCE FROM JOHN HEIMBECKER**

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