COMPETITION TRIBUNAL
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CT-2021-002

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 proposed acquisition of Tervita Corporation by Secure Energy Services Inc.;

AND IN THE MATTER OF an Application by the Commissioner of Competition for an order pursuant to 92 of the *Competition Act*;

AND IN THE MATTER OF an Application by the Commissioner of Competition for an interim order pursuant to section 104 of the *Competition Act*;

B E T W E E N:

COMMISSIONER OF COMPETITION

Applicant

- and -

SECURE ENERGY SERVICES INC.

TERVITA CORPORATION

Respondents

AFFIDAVIT OF NATHAN H. MILLER
(AFFIRMED JULY 19, 2021)

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1. My name is Nathan H. Miller. I am the Saleh Romeih Associate Professor at the McDonough School of Business at Georgetown University in Washington, DC.

2. I have been asked by the Commissioner of Competition to provide an economic assessment of the competitive implications of the proposed merger between Secure Energy Services Inc. and Tervita Corporation.

3. I attach as Exhibit "A" to this affidavit my report setting out my opinion.

Affirmed remotely by Nathan H. Miller at the City of Washington in the District of Columbia, before me on July 19, 2021 in accordance with O. Reg. 431/20, Administering Oath or Declaration Remotely.

Commissioner for Taking Affidavits
Mallory Kelly

NATHAN H. MILLER

A Commissioner, etc., Province of Ontario
Commissaire, etc., Province de l'Ontario
Mallory Christina Kelly
exp.: February 27, 2022
exp.: 27 février 2022
for the Government of Canada, Department of Justice
au service du gouvernement du Canada, ministère de la Justice

This is Exhibit A to the Affidavit of
Nathan H. Miller
Affirmed on July 19, 2021

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EXPERT REPLY REPORT OF NATHAN H. MILLER, PH.D.

July 19, 2021

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1. ASSIGNMENT

1. I was asked by the Competition Bureau ("Bureau") to provide an economic assessment of the competitive implications of the proposed merger between Secure Energy Services Inc. ("Secure") and Tervita Corp. ("Tervita"). In my affidavit dated June 29, 2021 ("Miller Initial Affidavit"), I described the economic analyses I conducted to assess the competitive impact of the merger based on the Parties' transaction-level data, locations of the Waste Service facilities and the Parties' customers, documents produced for the merger investigation, and other documents.

2. The Bureau also asked me to review the Affidavit of David Engel, Affidavit of Andrew Harington, and Secure's response to the Commissioner's Section 104 application,[1] and explain if they alter my opinions.

2. SUMMARY OF OPINIONS

3. After reviewing the affidavits and Secure's response to the Commissioner's Section 104 application, my conclusions explained in my Initial Affidavit remain the same. Specifically, the merger will:

- eliminate competition among the two largest suppliers of Waste Services;[2]
- lead to greater market concentration in many local markets, exceeding the Safe Harbour specified by in the *Guidelines*; and[3, 4]
- increase the prices of Waste Services. [5]

[1] The Commissioner of Competition and Secure Energy Services, Inc., Response of Secure Energy Services Inc. to the Commissioner's Application for an Interim Order, CT-2021-002, July 14, 2021; The Commissioner of Competition and Secure Energy Services, Inc., Affidavit of David Engel, CT-2021-002, affirmed July 14, 2021 ("Engel Affidavit"); The Commissioner of Competition and Secure Energy Services, Inc., Affidavit of Harington, CT-2021-002, affirmed July 14, 2021 ("Harington Affidavit").

[2] Miller Initial Affidavit, Section 6.1.

[3] The *Guidelines* state that a merger is unlikely to have anti-competitive consequences due to unilateral exercise of market power if the post-transaction market share of the merged firm would be less than 35 percent. The Competition Bureau, "Merger Enforcement Guidelines," October 6, 2011, ("Merger Enforcement Guidelines") ¶ 5.8.

[4] Miller Initial Affidavit, ¶ 75.

[5] Miller Initial Affidavit, Section 6.3.

4. I note that the Parties have not presented any economic analyses of competitive effects that contradict my opinion. In this Affidavit, I further consider and provide opinions on the following issues:

- Mr. Engel's claim that the efficiencies discussed in Mr. Harington's report will benefit consumers.
- Mr. Engel's assertion regarding the implication of reduced drilling and completion activity for the Parties.
- Mr. Engel's claim that "there exist many third-party competitors across FST, landfill, and water disposal facilities."[6]

3. PARTIES' CLAIMED EFFICIENCIES ARE UNLIKELY TO BENEFIT CONSUMERS

5. Mr. Engel and Mr. Harington claim that the merger will lead to various efficiencies such as those stemming from TRD and landfill facility closures,[7] reductions in corporate and field-office redundancy, including a reduction in field personnel,[8] and others. Mr. Engel's affidavit appears to claim that the savings will be passed on to Waste Service customers in the form of lower prices.[9]

6. Assessing whether these efficiencies are cognizable and merger specific is beyond the scope of my assignment. I further understand that the law under Section 96 does not evaluate the merits of efficiencies based on its effect on consumers, but instead weighs such efficiencies to examine any potential dead-weight loss.[10] My opinions below are limited to rebutting Mr. Engel's assertion that efficiencies will benefit customers.

7. Mr. Engel has not established that any of the cost-savings claimed by Mr. Harington will be "passed through" to consumers. It is not enough to show that efficiencies will result from the merger. There must also be an incentive for the merged entity to pass on those efficiencies to consumers. As a matter of

[6] Engel Affidavit, p. 25.

[7] Harington Affidavit, pp. 9-11, 34-40. Mr. Engel describes savings in capital expenditures due to the closings. See Engel Affidavit, p. 36.

[8] Engel Affidavit, p. 38, 43-44; Harington Affidavit, p. 41.

[9] Engel Affidavit, p. 11. ("… provide better services at lower prices through achieving synergies/efficiencies").

[10] Competition Act (R.S.C. (Revised Statutes of Canada) , 1985, c. C-34), Section 96 ("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.").

economics, fixed or sunk costs matter in a firm's decision to run a business, but they do not matter in a firm's pricing decisions.[11] Therefore, efficiencies resulting from fixed or sunk costs do not change a firm's pricing calculus and are unlikely to be passed through to consumers.[12] A significant part of the efficiencies claimed by Mr. Harington relate to such fixed costs, including facility closures and reductions in back-office personnel.[13] Further, when one considers variable cost savings from the closure of a facility, one should also consider the increased costs at other facilities that may experience higher volume as a result of receiving the customers from the closed facility. Mr. Harington does not present any analysis showing that increased volume at absorbing facilities would not increase costs at these plants.

8. Even if there are efficiencies that stem from non-fixed costs, the incentive to pass on these savings to customers depends on the level of competition in the market.[14] In my Initial Affidavit, I find that many local markets will face monopolies or a high concentration of Waste Service providers because of the transaction and thus will have little competition.[15] In these markets (and others not explicitly analyzed in my Initial Affidavit), the Parties will not have strong incentives to pass on the cost savings to customers.

9. Notwithstanding the issue that a large part of Parties' claimed efficiencies are unlikely to put downward pressure on prices, when a merger also lessens competition, one must weigh any cost-savings that may be passed on to customers against other merger-related incentives to increase prices. Mr. Engel has not conducted such an analysis.[16]

[11] Dennis Carlton and Jeffry Perloff, Modern Industrial Organization, Fourth Edition, 2005, p. 29.

[12] In particular, the pass-through rate refers to the rate at which marginal cost reductions are passed on to consumers in the form of lower prices.

[13] See fn. 7, 8.

[14] Miller, Nathan H., Matthew Osborne, and Gloria Sheu. "Pass - through in a concentrated industry: empirical evidence and regulatory implications." *The RAND Journal of Economics* 48, no. 1 (2017): 69-93.

[15] Miller Initial Affidavit, Section 6.1.

[16] Indeed, to conduct such analysis, one must calculate the amount of marginal cost savings and have a measure of pass-through. Pass-through in concentrated markets, such as the Waste Service markets I examine, tend to be low. MacKay, Alexander, Nathan H. Miller, Marc Remer, and Gloria Sheu. "Bias in reduced-form estimates of pass-through." *Economics Letters* 123, no. 2 (2014): 200-202; Weyl, E. Glen, and Michal Fabinger. "Pass-through as an economic tool: Principles of incidence under imperfect competition." *Journal of Political Economy* 121, no. 3 (2013): 528-583.

4. REDUCTIONS IN DRILLING AND COMPLETION ACTIVITY AND IMPLICATIONS FOR WASTE SERVICE PROVIDERS

10. Mr. Engel states that the oil and gas sector has been in decline since 2014, which has also affected Secure's Waste Service business.[17] Even if there had been a decline in demand for Waste Services, it does not change my opinion that the merger is anticompetitive.

11. First, a decrease in demand does not immediately imply that economics dictate the closure of existing facilities. In fact, Mr. Engel himself states that "most SECURE and former Tervita facilities are profitable on a standalone operational basis and have low operating costs on a go-forward basis, with most costs being incurred to initially establish the facilities."[18] Similarly, Mr. Harington explains that "Tervita has positive cash flow and operating profits," and if Secure divests any businesses, these businesses will be financially strong, viable, and effective competitors.[19] Facilities that have undertaken sunk "start-up" costs but have low operating costs can continue to be economically profitable as long as they are able to cover their variable costs.

12. Further, any reorganization necessitated by changing market conditions can be achieved through market forces rather than a merger. Ultimately, market forces would result in the survival of some facilities that provide better services to customers more efficiently and the closure of other facilities, which would achieve the same type of facility closure related cost reductions Mr. Harington identifies.[20]

5. THIRD-PARTY COMPETITORS, SELF SUPPLY, AND THE CLAIMED COUNTERVAILING MARKET POWER DO NOT SUFFICIENTLY CONSTRAIN THE ADVERSE IMPACT OF THE MERGER

13. Mr. Engel suggests that the merged firm would face several sources of competitive pressure and these sources would restrain price increases post-transaction—namely, other third-party competitors, self-supplying oil and gas

[17] Engel Affidavit, pp. 9, 13-15.

[18] Engel Affidavit, p. 60. Mr. Engel further claims that if the Tribunal requires Secure to divest part or all of former Tervita's facilities, these assets would be viable and effective competitors. Mr. Engel's claim implies that these facilities can be operated profitably under current economic conditions.

[19] Harington Affidavit, pp. 9, 15, 24.

[20] Moreover, Mr. Harington explains that the type of facility closures ("cold shut ins") contemplated by Secure "occurs in the ordinary course within the company on a regular basis." Harington Affidavit, Exhibit C, p. 22. Notably, Mr. Harington's analysis evaluates the efficiencies realized from planned facility closures, absent the merger, that can proceed sooner because of the merger. See Harington Affidavit, Exhibit C, p. 24.

producers, and/or countervailing bargaining power of oil and gas producers.[21] Mr. Engel fails to substantiate his claims with economic analyses. Indeed, the analyses in my Initial Affidavit shows that Mr. Engel's claims are flawed.

14. Mr. Engel claims that many existing third-party competitors across FST, landfill, and water disposal facilities would constrain prices,[22] and "if SECURE even attempted to increase prices post-Transaction, such an increase would result in lost volumes to third-party competitors."[23] However, he does not present any analyses to substantiate his claims. He does not present any analysis of local markets that accounts for the locations of third party facilities, their proximity to Secure and Tervita facilities, or the facility draw areas. In my Initial Affidavit, I considered all of this information and found that third-party competitors would likely not constrain Waste Services prices post-transaction in many markets. Specifically,[24]

- I reviewed documentary evidence from the Parties and found that Secure and Tervita consider each other their primary competitors in many local markets and more generally.[25]
- I analyzed Secure and Tervita's transaction data and precise facility locations of the Parties' and competitors' TRD, landfill, and water disposal facilities.[26] Based on this analysis, I find that Secure and Tervita are often each other's closest competitors in terms of the services offered and the location of its facilities.[27]
- The transaction will lead to the merged firm's market share well above the safe harbour level in many locally-defined markets.[28]
- The transaction creates monopolies and reduces competition from three firms to two firm in many local markets.[29]

[21] Engel Affidavit, pp. 25-30.

[22] Engel Affidavit, p. 25.

[23] Engel Affidavit, p. 25.

[24] As I noted in my Initial Affidavit, the Bureau identified additional facilities shortly before I submitted my affidavit. The additional facilities identified by the Parties would not change the overall findings because many these facilities would not provide competition for many of the customer-based markets identified in my Initial Affidavit, either because of their location, services they provide, or their size.[25] Miller Initial Affidavit, Section 6.2.

[25] Miller Initial Affidavit, Section 6.2.

[26] Miller Initial Affidavit, Section 6.1.

[27] Miller Initial Affidavit, Section 6.2.

[28] Merger Enforcement Guidelines, ¶ 5.8.

[29] Miller Initial Affidavit, Section 6.1.

- Additionally, the transaction increases the market concentration significantly on other markets.[30]

15. Second, Mr. Engel claims that oil and gas producers are a competitive threat because they are able to self-supply Waste Services.[31] As described in my Initial Affidavit, oil and gas producers are not likely to constrain prices through self-supply, particularly for services that require TRDs, landfills, or excess waste water that result from well-completion activities.[32] I also understand that the regulatory process to approve landfills for disposal is regional and extensive. Even in instances where an oil and gas producer is approved to dispose of its own waste, there are additional regulatory requirements to take in waste from other producers, limiting its ability to compete with and constrain third-party Waste Service suppliers.[33]

16. In sum, neither third-party facilities nor self-supply of waste stream services can constrained the prices of the Parties since they are not a viable substitute to the services offered by the Parties in many markets. Indeed, Mr. Engel and Mr. Harington acknowledge in their affidavits that the parties are each other's closest substitute, not third-party facilities nor the option of self-supplying. Specifically, in describing its plans to fully or partially shutter many facilities post-transaction, they note that Secure selected these facilities because they "provide the same or similar services, [and] are in close geography proximity."[34] Put differently, the Parties appear to have identified facilities that are located in regions where the Parties face little threat that closure will lead them to lose waste volume business, even if some of the customers are required to travel farther to reach the remaining facility. I note that many of the facilities Secure has identified for potential closure correspond to the facilities in markets that

[30] Note that my competition analysis is also conservative on several dimensions. The revenue-based market shares assume that any third-party competitor is of a comparable size to the maximum of the average nearby Secure or Tervita facility, even for municipal landfills. The market shares are also calculated using 90-percent overlapping draw areas based on driving distances, and many of the draw areas are larger than the markets proposed by the Parties. Miller Initial Affidavit, Section 5.2.1, fn. 123.

[31] Engel Affidavit, p. 26 ("Second, many of SECURE's customers are large, sophisticated oil and gas producers … their ability to punish any attempted price increases across multiple product lines and geographies by diverting volumes either to third-party competitors or through self-supply.").

[32] Miller Initial Affidavit, ¶ 47.

[33] Miller Initial Affidavit, ¶¶ 47-48, fn. 103.

[34] Harington Affidavit, Exhibit C, p. 17 ("SECURE identified 20 facility 'integration groupings' within which the facilities provide the same or similar services, are in close geographic proximity, and where one or more closures are likely to occur as a result of the Proposed Transaction."). See also Harington Affidavit, Exhibit C, p. 16.

would be a monopoly or face a decline from three to two competitors according to the analysis in my Initial Affidavit.[35]

17. Mr. Harington's assumptions and analysis also support my finding that many Secure and Tervita facilities are close competitors. In particular, Mr. Harington assumes that when the merged firm closes a facility, its volume will be absorbed by the remaining merged firm facility.[36] This assumption indicates that Mr. Harington also views that the diversion rate between many close-by Secure and Tervita facilities are high. As I explained in my Initial Affidavit, the incentive to raise prices after a merger is greater, the greater is the diversion rate between merging facilities.[37]

18. Finally, Mr. Engel claims that prices will be constrained by the counter-veiling market power from oil and gas producers that can leverage better disposal prices based on the volume of waste they produce or the threat to self-supply Waste Services.[38] Setting aside the fact that Mr. Engel has not provided sufficient economic evidence to demonstrate the presence of countervailing market power, Mr. Engel fails to acknowledge that this merger will ultimately weaken the producer's bargaining leverage, which is precisely the core competitive concern in this matter and in negotiated markets.[39]

19. Indeed, prior to the merger, a source of the oil and gas producer's bargaining leverage is the ability to turn to one of the merging Parties if it fails to negotiate favorable terms with one of them. After the merger, a Secure customer can no longer use its ability to ship its waste to a Tervita facility as leverage, which significantly weakens the customer's bargaining position given that Secure and Tervita facilities are each other's closest substitutes. Put differently, the merger will combine two of the largest Waste Service providers

[35] See Harington Affidavit, Exhibit C, p. 19-20, Table 7, Table 8; Miller Initial Affidavit, Exhibit 13, Exhibit 14, Appendix 7.3. The following list includes some of the Secure-Tervita facilities the Parties list among the "integration groupings" and that appear as customer-based markets that become monopoly markets with the transaction or for which customers are limited to only two competitors (instead of three) because of it. For example, Fox Creek (Secure), Fox Creek East (Tervita) TRDs; Obed (Secure), West Edson (Tervita) TRDs; Judy Creek (Secure), Judy Creek (Tervita) TRDs; Brazeau (Secure), Brazeau (Tervita) TRDs; Rocky Mountain House (Secure), Stauffer (Tervita) TRDs; Kindersley (Secure), Kindersley (Tervita) TRDs; Saddle Hills (Secure), Sprit River (Tervita) landfills; Fox Creek (Secure), Fox Creek (Tervita) landfills; South Grand Prairie (Secure), South Wapiti (Tervita) landfills; Wonowon (Secure), Mile 103 (Tervita) water wells.

[36] Harington Affidavit, Exhibit C, pp. 7-8, 16.

[37] Miller Initial Affidavit, ¶ 31.

[38] Engel Affidavit, p. 26.

[39] See, for example, Gowrisankaran, Gautam, Aviv Nevo, and Robert Town. "Mergers when prices are negotiated: Evidence from the hospital industry." *American Economic Review* 105.1 (2015): 172-203 for a discussion of why a customer's bargaining leverage weakens in mergers of two close substitutes.

in the region, which will necessarily increase the combined entity's bargaining power in negotiations with oil and gas producers located in many of the local markets as defined by analyses in my Initial Affidavit.[40]

Nathan Miller

Nathan Miller, Ph.D.
July 19, 2021

[40] Miller Initial Affidavit, Exhibit 13, Exhibit 14, Appendix 7.3.

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