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Bill C-59 and the Use of Structural Merger Presumptions in Canada

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Dear Chairs and Esteemed Members of the Senate and House of Commons Committees on Finance:

We, the undersigned, are scholars from the International Center for Law & Economics (ICLE) with experience in the academy, enforcement agencies, and private practice in competition law. We write to address a key aspect of proposed amendments to Canadian competition law. Specifically, we focus on clauses in Bill C-59 pertinent to mergers and acquisitions and, in particular, the Bureau of Competition's recommendation that the Bill should:

> Amend Clauses 249-250 to enact rebuttable presumptions for mergers consistent with those set out in the U.S. Merger Guidelines.[1]

The Bureau's recommendation seeks to codify in Canadian competition law the structural presumptions outlined in the 2023 U.S. Federal Trade Commission (FTC) and U.S. Justice Department (DOJ) Merger Guidelines. On balance, however, adoption of that recommendation would impede, rather than promote, fair competition and the welfare of Canadian consumers.

The cornerstone of the proposed change lies in the introduction of rebuttable presumptions of illegality for mergers that exceed specified market-share or concentration thresholds. While this approach may seem intuitive, the economic literature and U.S. enforcement experience militate against its adoption in Canadian law.

The goal of enhancing—indeed, strengthening—Canadian competition law should not be conflated with the adoption of foreign regulatory guidelines. The most recent U.S. Merger Guidelines establish new structural thresholds, based primarily on the Herfindahl-Hirschman Index (HHI) and market share, to establish presumptions of anticompetitive effects and illegality. Those structural presumptions, adopted a few short months ago, are inconsistent with established economic literature and are untested in U.S. courts. Those U.S. *guidelines* should not be codified in Canadian law without robust deliberation to ensure alignment with Canadian legal principles, on the one hand, and with economic realities and evidence, on the other.

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[1] Matthew Boswell, *Letter to the Chair and Members of the House of Commons Standing Committee on Finance*, COMPETITION BUREAU CANADA (Mar. 1, 2024), *available at* https://sencanada.ca/Content/Sen/Committee/441/NFFN/briefs/SM-C-59_CompetitionBureauofCND_e.pdf.

Three points are especially important. First, concentration measures are widely considered to be a poor proxy for the level of competition that prevails in a given market. Second, lower merger thresholds may lead to enforcement errors that discourage investment and entrepreneurial activity and allocate enforcement resources to the wrong cases. Finally, these risks are particularly acute when concentration thresholds are used not as useful indicators but, instead, as actual legal presumptions (albeit rebuttable ones). We discuss each of these points in more detail below.

What Concentration Measures Can and Cannot Tell Us About Competition

While the use of concentration measures and thresholds can provide a useful preliminary-screening mechanism to identify potentially problematic mergers, substantially lowering the thresholds to establish a presumption of illegality is inadvisable for several reasons.

First, too strong a reliance on concentration measures lacks economic foundation and is likely prone to frequent error. Economists have been studying the relationship between concentration and various potential *indicia* of anticompetitive effects—price, markup, profits, rate of return, etc.—for decades.[2] There are hundreds of empirical studies addressing this topic.[3]

The assumption that "too much" concentration is harmful assumes both that the structure of a market is what determines economic outcomes and that anyone could know what the "right" amount of concentration is. But as economists have understood since at least the 1970s (and despite an extremely vigorous, but futile, effort to show otherwise), market structure does not determine outcomes.[4]

This skepticism toward concentration measures as a guide for policy is well-supported, and is held by scholars across the political spectrum. To take one prominent, recent example, professors Fiona Scott Morton (deputy assistant U.S. attorney general for economics in the DOJ Antitrust Division under President Barack Obama, now at Yale University); Martin Gaynor (former director of the FTC Bureau of Economics under President Obama, now serving as special advisor to Assistant U.S. Attorney General Jonathan Kanter, on leave from Carnegie Mellon University), and Steven Berry (an industrial-organization economist at Yale University) surveyed the industrial-organization

[2] For a few examples from a very large body of literature, *see*, *e.g.*, Steven Berry, Martin Gaynor, & Fiona Scott Morton, *Do Increasing Markups Matter? Lessons from Empirical Industrial Organization*, 33J. ECON. PERSPECTIVES 44 (2019); Richard Schmalensee, *Inter-Industry Studies of Structure and Performance*, in 2 HANDBOOK OF INDUSTRIAL ORGANIZATION 951-1009 (Richard Schmalensee & Robert Willig, eds., 1989); William N. Evans, Luke M. Froeb, & Gregory J. Werden, *Endogeneity in the Concentration-Price Relationship: Causes, Consequences, and Cures*, 41 J. INDUS. ECON. 431 (1993); Steven Berry, *Market Structure and Competition, Redux*, FTC Micro Conference (Nov. 2017), *available at* https://www.ftc.gov/system/files/documents/public_events/1208143/22_-_steven_berry_keynote.pdf; Nathan Miller, *et al.*, *On the Misuse of Regressions of Price on the HHI in Merger Review*, 10 J. ANTITRUST ENFORCEMENT 248 (2022).

[3] *Id.*

[4] *See* Harold Demsetz, *Industry Structure, Market Rivalry, and Public Policy*, 16 J. L. & ECON. 1 (1973).

literature and found that presumptions based on measures of concentration are unlikely to provide sound guidance for public policy:

> In short, there is no well-defined "causal effect of concentration on price," but rather a set of hypotheses that can explain observed correlations of the joint outcomes of price, measured markups, market share, and concentration….
>
> Our own view, based on the well-established mainstream wisdom in the field of industrial organization for several decades, is that regressions of market outcomes on measures of industry structure like the Herfindahl-Hirschman Index should be given little weight in policy debates.[5]

As Chad Syverson recently summarized:

> Perhaps the deepest conceptual problem with concentration as a measure of market power is that it is an outcome, not an immutable core determinant of how competitive an industry or market is… As a result, concentration is worse than just a noisy barometer of market power. Instead, we cannot even generally know which way the barometer is oriented.[6]

This does not mean that concentration measures have no use in merger screening. Rather, market concentration is often unrelated to antitrust-enforcement goals because it is driven by factors that are endogenous to each industry. Enforcers should not rely too heavily on structural presumptions based on concentration measures, as these may be poor indicators of the instances in which antitrust enforcement is most beneficial to competition and consumers.

At What Level Should Thresholds Be Set?

Second, if concentration measures are to be used in some fashion, at what level or levels should they be set?

The U.S. 2010 Horizontal Merger Guidelines were "based on updated HHI thresholds that more accurately reflect actual enforcement practice."[7] These numbers were updated in 2023, but without clear justification. While the U.S. enforcement authorities cite several old cases (cases that implicated considerably higher levels of concentration than those in their 2023 guidelines), we agree with comments submitted in 2022 by now-FTC Bureau of Economics Director Aviv Nevo and colleagues, who argued against such a change. They wrote:

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[5] Berry, Gaynor, & Scott Morton, *supra* note 2.

[6] Chad Syverson, *Macroeconomics and Market Power: Context, Implications, and Open Questions* 33 J. ECON. PERSP. 23, (2019) at 26.

[7] Joseph Farrell & Carl Shapiro, *The 2010 Horizontal Merger Guidelines After 10 Years*, 58 REV. IND. ORG. 58, (2021). https://link.springer.com/article/10.1007/s11151-020-09807-6.

> Our view is that this would not be the most productive route for the agencies to pursue to successfully prevent harmful mergers, and could backfire by putting even further emphasis on market definition and structural presumptions.
>
> If the agencies were to substantially change the presumption thresholds, they would also need to persuade courts that the new thresholds were at the right level. *Is the evidence there to do so? The existing body of research on this question is, today, thin and mostly based on individual case studies in a handful of industries. Our reading of the literature is that it is not clear and persuasive enough, at this point in time, to support a substantially different threshold that will be applied across the board to all industries and market conditions.* (emphasis added) [8]

Lower merger thresholds create several risks. One is that such thresholds will lead to excessive "false positives"; that is, too many presumptions against mergers that are likely to be procompetitive or benign. This is particularly likely to occur if enforcers make it harder for parties to rebut the presumptions, *e.g.*, by requiring stronger evidence the higher the parties are above the (now-lowered) threshold. Raising barriers to establishing efficiencies and other countervailing factors makes it more likely that procompetitive mergers will be blocked. This not only risks depriving consumers of lower prices and greater innovation in specific cases, but chills beneficial merger-and-acquisition activity more broadly. The prospect of an overly stringent enforcement regime discourages investment and entrepreneurial activity. It also allocates scarce enforcement resources to the wrong cases.

Changing the Character of Structural Presumptions

Finally, the risks described above are particularly acute, given the change in the character of structural presumptions described in the U.S. Merger Guidelines. The 2023 Merger Guidelines—and only the 2023 Merger Guidelines—state that certain structural features of mergers will raise a "presumption of illegality."[9]

U.S. merger guidelines published in 1982,[10] 1992 (revised in 1997),[11] and 2010[12] all describe structural thresholds seen by the agencies as pertinent to merger screening. None of them mention

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[8] John Asker *et al*, *Comments on the January 2022 DOJ and FTC RFI on Merger Enforcement* (Apr. 20, 2022), *available at* https://www.regulations.gov/comment/FTC-2022-0003-1847 at 15-6.

[9] U.S. DEP'T JUSTICE & FED. TRADE COMM'N, *Merger Guidelines (Guideline One)* (Dec. 18, 2023), *available at* https://www.ftc.gov/system/files/ftc_gov/pdf/2023_merger_guidelines_final_12.18.2023.pdf.

[10] U.S. DEP'T JUSTICE, *1982 Merger Guidelines* (1982), https://www.justice.gov/archives/atr/1982-merger-guidelines.

[11] U.S. DEP'T JUSTICE & FED. TRADE COMM'N, *1992 Merger Guidelines* (1992), https://www.justice.gov/archives/atr/1992-merger-guidelines; U.S. DEP'T JUSTICE & FED. TRADE COMM'N, *1997 Merger Guidelines* (1997), https://www.justice.gov/archives/atr/1997-merger-guidelines.

[12] U.S. DEP'T JUSTICE & FED. TRADE COMM'N, *Horizontal Merger Guidelines* (Aug. 19, 2010), https://www.justice.gov/atr/horizontal-merger-guidelines-08192010; The U.S. antitrust agencies also issued Vertical Merger Guidelines in 2020. Although these were formally withdrawn in 2021 by the FTC, but not DOJ, they too are supplanted by the 2023 Merger Guidelines. *See* U.S. DEP'T JUSTICE & FED. TRADE COMM'N, *Vertical Merger Guidelines* (Jun. 30, 2020), *available at* https://www.ftc.gov/system/files/documents/public_statements/1580003/vertical_merger_guidelines_6-30-20.pdf.

a "presumption of illegality." In fact, as the U.S. agencies put it in the 2010 Horizontal Merger Guidelines:

> The purpose of these thresholds is not to provide a rigid screen to separate competitively benign mergers from anticompetitive ones, although high levels of concentration do raise concerns. Rather, they provide one way to identify some mergers unlikely to raise competitive concerns and some others for which it is particularly important to examine whether other competitive factors confirm, reinforce, or counteract the potentially harmful effects of increased concentration.[13]

The most worrisome category of mergers identified in the 1992 U.S. merger guidelines were said to be presumed "likely to create or enhance market power or facilitate its exercise." The 1982 guidelines did not describe "presumptions" so much as that certain mergers that may be matters of "significant competitive concern" and "likely" to be subject to challenge.

Hence, earlier editions of the U.S. merger guidelines describe the ways that structural features of mergers might inform, but not determine, internal agency analysis of those mergers. That was useful information for industry, the bar, and the courts. Equally useful were descriptions of mergers that were "unlikely to have adverse competitive effects and ordinarily require no further analysis,"[14] as well as intermediate types of mergers that "potentially raise significant competitive concerns and often warrant scrutiny."[15]

Similarly, the 1992 U.S. merger guidelines identified a tier of mergers deemed "unlikely to have adverse competitive effects and ordinarily require no further analysis," as well as intermediate categories of mergers either unlikely to have anticompetitive effects or, in the alternative, *potentially* raising significant competitive concerns, depending on various factors described elsewhere in the guidelines.[16]

By way of contrast, the new U.S. guidelines include no description of any mergers that are unlikely to have adverse competitive effects. And while the new merger guidelines do stipulate that the "presumption of illegality can be rebutted or disproved," they offer very limited means of rebuttal.

This is at odds with prior U.S. agency practice and established U.S. law. Until very recently, U.S. agency staff sought to understand proposed mergers under the totality of their circumstances, much as U.S. courts came to do. Structural features of mergers (among many others) might raise concerns of greater or lesser degrees. These might lead to additional questions in some instances; more substantial inquiries under a "second request" in a minority of instances; or, eventually, a complaint against a very small minority of proposed mergers. In the alternative, they might help staff avoid wasting scarce resources on mergers "unlikely to have anticompetitive effects."

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[13] 2010 Horizontal Merger Guidelines.

[14] *Id.*

[15] *Id.*

[16] 1992 Merger Guidelines.

Prior to a hearing or a trial on the merits, there might be strong, weak, or no appreciable assessments of likely liability, but there was no *prima facie* determination of illegality.

And while U.S. merger trials did tend to follow a burden-shifting framework for plaintiff and defendant *production*, they too looked to the "totality of the circumstances"[17] and a transaction's "probable effect on future competition"[18] to determine liability, and they looked away from strong structural presumptions. As then-U.S. Circuit Judge Clarence Thomas observed in the *Baker-Hughes* case:

> General Dynamics began a line of decisions differing markedly in emphasis from the Court's antitrust cases of the 1960s. Instead of accepting a firm's market share as virtually conclusive proof of its market power, the Court carefully analyzed defendants' rebuttal evidence.[19]

Central to the holding in *Baker Hughes*—and *contra* the 2023 U.S. merger guidelines—was that, because the government's *prima facie* burden of production was low, the defendant's rebuttal burden should not be unduly onerous.[20] As the U.S. Supreme Court had put it, defendants would not be required to clearly disprove anticompetitive effects, but rather, simply to "show that the concentration ratios, which can be unreliable indicators of actual market behavior . . . did not accurately depict the economic characteristics of the [relevant] market."[21]

Doing so would not end the matter. Rather, "the burden of producing additional evidence of anticompetitive effects shifts to the government, and merges with the ultimate burden of persuasion, which remains with the government at all times."[22]

As the U.S. Supreme Court decision in *Marine Bancorporation* underscores, even by 1974, it was well understood that concentration ratios "can be unreliable indicators" of market behavior and competitive effects.

As explained above, research and enforcement over the ensuing decades have undermined reliance on structural presumptions even further. As a consequence, the structure/conduct/performance paradigm has been largely abandoned, because it's widely recognized that market structure is not outcome–determinative.

That is not to say that high concentration cannot have any signaling value in preliminary agency screening of merger matters. But concentration metrics that have proven to be unreliable indicators

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[17] *United States v. Baker-Hughes Inc.*, 908 F.2d 981, 984 (D.C. Cir. 1990).

[18] *Id.* at 991.

[19] *Id.* at 990 (citing *Hospital Corp. of Am. v. FTC*, 807 F.2d 1381, 1386 (7th Cir.1986), cert. denied, 481 U.S. 1038, 107 S.Ct. 1975, 95 L.Ed.2d 815 (1987).

[20] *Id.* at 987, 992.

[21] *United States v. Marine Bancorporation Inc.*, 418 U.S. 602, 631 (1974) (internal citations omitted).

[22] *Baker-Hughes*, 908 F.2d at 983.

of firm behavior and competitive effects should not be enshrined in Canadian statutory law. That would be a step back, not a step forward, for merger enforcement.