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The Use of Behavioural Remedies in Canadian Merger Law

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THE USE OF BEHAVIOURAL REMEDIES IN CANADIAN MERGER LAW

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1. INTRODUCTION

In his letter to the chairmen of the Bank of Montreal and Royal Bank of Canada regarding the proposed merger of those two banks, the Director of Investigation and Research[1] noted that "traditionally" the Competition Bureau has relied upon "remedies that focussed on structural rather than behavioural measures"[2] to resolve anti-competitive mergers. In the Director's opinion, "the most effective structural remedy is the divestiture of assets away from the merged company to others that will provide effective and sustainable competition."[3]

While divestiture has traditionally been the favourite remedy of antitrust regulators, behavioural (or non-structural) remedies are available and have been used more frequently than is generally recognised for mergers under the *Competition Act*.[4] Although often dismissed as complicated, difficult to implement and needing ongoing monitoring, we believe

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[1] On March 18, 1999, the head of the Competition Bureau, formerly the "Director of Investigation and Research", became known as the "Commissioner of Competition." The terms "Director" and "Commissioner" are used interchangeably throughout this paper.

[2] See the letter of Konrad von Finckenstein QC, to Messrs. Cleghorn and Barrett, dated December 11, 1998 at 41, available online at: <http://strategis.ic.gc.ca/pics/ct/rbceng.pdf> [hereinafter the "RBC/BMO Letter"].

[3] *Ibid*.

[4] R.S.C. 1985, c. C-34 [hereinafter the "*Act*"], ss. 92(1)(e)(iii) and (f)(iii). See also the discussion in Part 2 below.

that many of the criticisms have been overstated. Rather than simply ordering the divestiture of assets that may have played an important role in the decision to initiate a transaction[5] and may facilitate efficiency gains in the hands of the merged firm, antitrust regulators should allow the parties the opportunity to resolve competitive concerns by proposing appropriate behavioural remedies. In cases where regulators are concerned about the implementation of a behavioural order, it can be backed up with "crown jewel" divestiture provisions to motivate compliance.[6]

Mr. Justice Hugessen of the Federal Court of Appeal has reached a similar conclusion. In the *Air Canada* ("*Gemini II*")[7] case, he described the Competition Tribunal's ability to order the dissolution of a merger or the divestiture of assets as "important and even *drastic* powers" which "in the hands of either the Director or the Tribunal […] *constitute a rather blunt instrument* for the implementation of Canada's competition policy."[8] As a result, he observed that these divestiture/dissolution powers give section 92(1)(e)(iii), the behavioural remedies provision, its vitality by encouraging the parties to "engage in constructive negotiations

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[5] In the worst-case scenario, the acquiror may be required to divest *all* of the assets acquired — see, *e.g.*, the *Tree Island Industries Ltd./Davis Wire Industries Ltd.* case, discussed in: Director of Investigation and Research, *Annual Report, 1991* (Ottawa: Supply and Services Canada, 1991) at 7; and the consent order issued in the *BAT/Rothmans* merger, in which British American Tobacco agreed to divest the Rothmans International assets in Canada: *Canada (Commissioner of Competition)* v. *British American Tobacco plc.*, [1999] C.C.T.D. No. 12 (QL) (Comp. Trib), discussed further in Commissioner of Competition, *Annual Report, 2000* (Ottawa: Industry Canada, 2000) at 16.

[6] This approach has been used in several cases to ensure compliance with the behavioural orders: see, *e.g.*, *Asea Brown Boveri/Westinghouse*, *infra* note 52; *Imperial Oil/Texaco*, *infra* note 54; and *Ultramar/Coastal*, *infra* note 57.

[7] *Canada (Director of Investigation and Research)* v. *Air Canada* (1993), 49 C.P.R. (3d) 417 (F.C.A.), rev'g 49 C.P.R. (3d) 7 (Comp. Trib.) [hereinafter *Gemini II*]. (This case involved an application to vary the original consent order granted in the *Gemini I* proceedings, discussed further at note 43, *infra*.)

[8] *Ibid.* at 430 (emphasis added).

and to agree upon an order which may contain a vast range and number of fine-tuned provisions designed to satisfy the requirements both of public interest and commercial reality".[9]

This paper examines the use of behavioural remedies since Canada's current merger law was enacted in 1986. It is not intended as an indictment of divestiture orders; clearly there will be cases where an *effective* divestiture[10] is the preferred remedy. However, we review the Canadian cases involving behavioural orders in order to demonstrate the considerable range of circumstances in which such remedies have been used. We then compare the strengths and weaknesses of behavioural and divestiture remedies (including cases where divestiture did not work) and debunk some of the myths surrounding the use of behavioural orders. We conclude that a "divestiture-first" mentality is not warranted and that wider use of behavioural remedies in Canada should be considered.

2. MERGER REMEDIES UNDER THE COMPETITION ACT

Merger remedies may be implemented by either the Tribunal (where the Commissioner brings a contested merger or a consent order application for review[11]) or the Commissioner (through pre- or post-closing undertakings given by the parties to the merger).

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[9] *Ibid.* He further observed that the rationale behind the "blunt instrument" of divestiture/dissolution is that these tools are "designed to lead to the sophisticated solutions of s. 92(1)(e)(iii)": *Ibid.* at 433.

[10] See the discussion in M. Sanderson & A. Wallwork, "Divestiture Relief in Merger Cases: An Assessment of the Canadian Experience" (1993) 38 McGill L.J. 757, in particular their 3-part test for effectiveness: (1) a viable asset package; (2) an independent purchaser; and (3) timely divestiture.

[11] Recent amendments to the *Act* made by Bill C-23, now S.C. 2002, c.16 (in force as of June 21, 2002), allow merging parties and the Commissioner to avoid a Tribunal hearing to approve a draft consent order and instead to simply register a consent agreement with the Tribunal to give it immediate effect. Consent agreements so registered are enforceable in the same manner as a Tribunal order. It seems likely that the improved enforceability, greater simplicity (and reduced Tribunal scrutiny) that consent agreements offer will lead to an increase in their use, and a decrease in the Bureau's use of

(a) The Tribunal's Remedial Order Powers

The Tribunal's power to issue behavioural remedies is found primarily in sections 92(1)(e)(iii) and (f)(iii) of the *Act*.[12] In addition it has powers to include behavioural elements where they are ancillary to "structural" dissolution, divestiture or prohibition orders:[13]

- In the case of a completed merger, the Tribunal may "order any party to the merger or any person":

  (i) to dissolve the merger *in such manner as the Tribunal directs*,

  (ii) to dispose of assets or shares designated by the Tribunal *in such manner as the Tribunal directs*, or

  (iii) in addition to or in lieu of the action referred to in subparagraph (i) or (ii), with the consent of the person against whom the order is directed and the Commissioner, *to take any other action.*[14]

- In the case of a proposed merger, the Tribunal may "make an order directed against any party to the proposed merger or any other person":

  (i) ordering the person against whom the order is directed not to proceed with the merger,

  (ii) ordering the person against whom the order is directed not to proceed with a part of the merger, or

  (iii) in addition to or in lieu of the order referred to in subparagraph (ii), either or both

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undertakings to remedy anti-competitive mergers. The new procedure has already been used in the *Astral/Télémédia* case, discussed at *infra* note 68, but curiously was not used in the *Avis/Budget* case (*infra* note 71).

[12] These provisions, which became part of the *Act* during the 1986 amendments, had first been proposed by the Economic Council of Canada in its *Interim Report on Competition Policy* (Ottawa: Queen's Printer, 1969), which recommended (at 144) that, in addition to blocking a merger, the Competitive Practices Tribunal (a conceptual predecessor to the current Competition Tribunal) should have the power to allow the merger "to proceed in altered form, or subject to other conditions designed to ensure that potential disadvantages were reduced to the point where they were outweighed by potential good effects."

[13] See the Tribunal's discussions of this point in *Southam*, *infra* note 18 at 250-51 and in *Commissioner of Competition* v. *Canadian Waste Services Inc.*, [2001] C.C.T.D. No. 32 (QL) at para. 47 [hereinafter *Ridge Landfill*].

[14] *Supra* note 4 (emphasis added).

> (A) prohibiting the person against whom the order is directed, should the merger or part thereof be completed, *from doing any act or thing the prohibition of which the Tribunal determines to be necessary to ensure that the merger or part thereof does not prevent or lessen competition substantially*, or
>
> (B) with the consent of the person against whom the order is directed and the Commissioner, *ordering the person to take any other action*.[15]

In summary, unlike the behavioural remedies provided for the reviewable practice of abuse of dominance,[16] the merger provisions require the consent of both the respondent(s) and the Commissioner for the Tribunal to issue a behavioural order unless it is ancillary to a structural order.

Even if the parties consent, the Tribunal may still refuse to issue an order. The test for Tribunal approval of a merger remedy (either behavioural or structural) is whether or not it will eliminate the substantial lessening of competition caused by the merger. This standard was initially established in the *Palm Dairies* consent proceedings, in which the Tribunal described it as a "critical threshold of effectiveness, namely, that of eliminating the likely prevention or lessening substantially of competition."[17] However, in *Southam*,[18] the first contested merger proceeding to deal with the issue of remedies in a significant way,[19] the

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[15] *Ibid.* (emphasis added).

[16] *Supra* note 4, ss. 78 and 79.

[17] *Infra* note 35 at 548. The proposed order in that case was held not to meet the test.

[18] *Canada (Director of Investigation and Research)* v. *Southam Inc.* (1992), 47 C.P.R. (3d) 240. (This citation refers to the Tribunal's remedies decision; for the Tribunal's decision on the merits, see (1992), 43 C.P.R. (3d) 161.)

[19] In its first contested merger case, *Canada (Director of Investigation and Research)* v. *Hillsdown Holdings (Canada) Ltd.* (1992), 41 C.P.R. (3d) 289, the Tribunal dealt with remedies in very brief fashion, rejecting (at 345) the Director's request for a divestiture order as the transaction was not found to lessen competition *substantially*. See also the discussion in: Director of Investigation and Research, *Annual Report, 1992* (Ottawa: Supply and Services Canada, 1992) at 12; and

Tribunal referred to the *Palm Dairies* test as "a *minimum* standard" and stated that "in contested proceedings, the appropriate test is whether the proposed remedy will restore the pre-merger competitive situation in the market in question."[20] The Tribunal did not otherwise explain its distinction between contested and consent cases, other than to state that the "minimum" standard would not be "appropriate" for contested cases.

Fortunately, the Supreme Court of Canada clarified this issue on appeal. Writing for a unanimous court, Iacobucci J. noted that the Tribunal's distinction between consent and contested cases was "not a sensible one", and stated that

> [t]he evil to which the drafters of the *Competition Act* addressed themselves is substantial lessening of competition. 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.[21]

Thus, the test for the approval of a merger remedy remains as first articulated by the Tribunal in *Palm Dairies* — the remedy will be approved if it eliminates the "substantial" lessening of competition caused by the merger. As Justice Iacobucci noted, "*some* lessening of competition following a merger is tolerated, because the Act proscribes only a *substantial* lessening of competition."[22]

C.S. Goldman & J.D. Bodrug, "The *Hillsdown* and *Southam* Decisions: The First Round of Contested Mergers Under the *Competition Act*" (1993) 38 McGill L.J. 724.

[20] *Supra* note 18 at 245 (emphasis in original).

[21] *Canada (Director of Investigation and Research)* v. *Southam Inc.* (1997), 71 C.P.R. (3d) 417 at 445 (S.C.C.).

[22] *Ibid.* at 444.

Despite its apparent initial hostility towards behavioural remedies in the *Palm Dairies*[23] case, the Tribunal has subsequently accepted behavioural restraints in consent proceedings where merging parties committed to:

- seek tariff remissions and reductions;[24]
- restrict information-sharing between joint venture parties;[25]
- supply third parties on commercially acceptable terms;[26] and
- adhere to codes of conduct governing their conduct towards suppliers, customers and competitors.[27]

Each of these cases is discussed in Part 3 below.

(b) Undertakings to the Commissioner

The Commissioner's power to devise and enforce merger remedies, typically through pre-closing restructuring or post-closing undertakings by the parties, is not expressly mentioned in the *Act*. However, according to a former Commissioner, section 22 of the *Act* (which gives the Commissioner the discretion to discontinue a Bureau inquiry) provides the authority to do so.[28]

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[23] *Infra* note 35.

[24] See *Asea Brown Boveri*, *infra* note 52.

[25] See *Gemini I*, *infra* note 43.

[26] See *Imperial Oil*, *infra* note 54; and *Chapters/Indigo*, *infra* note 64. (But see also *Ultramar/Coastal*, *infra* note 57, where proposed supply commitments were rejected as ineffective and unenforceable.)

[27] See *Gemini I*, *infra* note 43; *Chapters/Indigo*, *ibid.*; and *Astral/Télémédia*, *infra* note 68.

[28] G.N. Addy, "The Bureau of Competition Policy's Compliance Approach" (1993) 38 McGill L.J. 867 at 876.

The Quebec Court of Appeal endorsed the Commissioner's implicit power to proceed by way of undertakings in the *Alex Couture* case:

> [u]ndertakings are another means of ensuring that a merger is in accordance with the Act without it being necessary to take proceedings before the tribunal. The director may obtain from parties to a proposed acquisition or merger, the undertaking that they will restructure the transaction or transfer, before or after the sale, part of the shares or assets to another purchaser.[29]

The court also noted that, "although the director must act with circumspection", his variety of powers under the *Act* indicates that "[t]he filing of an application with the Tribunal constitutes the last resort."[30]

Unlike Tribunal remedies, there is no legal test for the parties to satisfy with undertakings, since they are negotiated by the parties and enforced by the Bureau. The Commissioner has accepted undertakings in which merging parties have agreed to a wide range of behavioural remedies including:

- long-term supply conditions for customers;[31]
- guarantees of access to distribution channels for competitors;[32]
- maintenance of the acquired firm as a separate and distinct corporate entity with a separate board of directors;[33] and

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[29] *Alex Couture Inc.* v. *Canada (Attorney-General)* (1991), 38 C.P.R. (3d) 293 at 353, rev'g 30 C.P.R. (3d) 486, leave to appeal to S.C.C. ref'd (1992), 42 C.P.R. (3d) v [hereinafter *Alex Couture*].

[30] *Ibid.* at 338.

[31] See *Consumers Packaging/Domglas*, *infra* note 84.

[32] See *Molson/Elders*, *infra* note 88.

[33] See *Canada Post/Purolator*, *infra* note 82 and *Avis/Budget*, *infra* note 71.

- amendment of membership contracts in an association to reduce barriers to entry.[34]

These and other cases are discussed in greater detail in Part 3 below.

3. BEHAVIOURAL REMEDIES IN CANADIAN MERGER CASES

The following examination of cases resolved both by Tribunal consent orders and Bureau undertakings illustrates the broad potential scope of such remedies.

(a) Tribunal Cases

(i) Palm Dairies [35]

In *Palm Dairies*, the first application to the newly-established Competition Tribunal, the Director challenged the proposed acquisition of Palm Dairies (a western Canadian dairy co-operative) by a numbered company held by four of its main competitors. The parties and the Director agreed to a consent order requiring the existing management of Palm Dairies to retain a 50% interest in the company (held through a separate company), and setting out extensive voting and operational restrictions relating to the post-merger management of Palm Dairies.

Surprising all parties, the Tribunal refused to issue the consent order after observing that, *inter alia*, the behavioural restraints in the order amounted to "a perpetual mandatory injunction", and expressing concern about the "long-term enforcement of an elaborate

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[34] See *CAPAC/PROCAN*, *infra* note 89.

[35] *Director of Investigation & Research* v. *Palm Dairies Ltd.* (1986), 12 C.P.R. (3d) 540 (Comp. Trib.) [hereinafter *Palm Dairies*].

arrangement when more obvious and straightforward remedies are available."[36] By this, the Tribunal indicated that it would prefer that the case be resolved by "allowing another (completely independent) purchaser to acquire Palm Dairies".[37] In the face of the Tribunal's opposition to the draft consent order, the parties abandoned the transaction.[38]

Palm Dairies has been described by some commentators as demonstrating the Tribunal's aversion to both consent orders and behavioural remedies.[39] Certainly, Chairman Reed's repeated reference[40] to the behavioural aspects of the draft consent order as constituting "a *perpetual* mandatory injunction" and requiring "a never-ending supervisory judgement" suggest an opposition to the ongoing monitoring which behavioural remedies may entail. However, it would appear that the real motivation behind the Tribunal's hostility to the draft consent order in *Palm Dairies* was the "vagueness and imprecision"[41] in the terms of the order — the Tribunal noted that, once issued, non-compliance with the order could lead to criminal prosecution under the *Act*, and that the terms of the order were "inappropriate as descriptions of the dividing line between criminal and non-criminal conduct."[42]

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[36] *Ibid.* at 548-49.

[37] *Ibid.* at 553.

[38] C.S. Goldman, "The Merger Resolution Process Under the *Competition Act*: A Critical Time in its Development" (1990) 22 Ottawa L. Rev. 1 at 18. (The assets of Palm Dairies were ultimately sold to two purchasers in 1990. That transaction was reviewed but not challenged by the Director: see the Director's *Annual Report, 1991*, *supra* note 5 at 7.)

[39] See, Goldman, *ibid.* at 20; and W.T. Stanbury, "An Assessment of the Merger Review Process Under the *Competition Act*" (1992) 20 Can. Bus. L.J. 422 at 432.

[40] *Supra* note 35 at 548 and 549 (emphasis in original).

[41] *Ibid.* at 552.

[42] *Ibid.* at 553. This focus on the vagueness of the draft order can also be seen from the Tribunal's decision, after the initial hearing, to order further submissions and a second hearing as "some of the terms and conditions that it is proposed to impose on the parties […] are of quite a vague nature": (1986), 12 C.P.R. (3d) 425 at 425 and 429. This issue

(ii) Air Canada ("Gemini I") [43]

Almost three years passed before the next merger application to the Tribunal, notwithstanding the "unprecedented merger wave"[44] that was occurring in Canada at this time. This lull has been attributed to the reluctance of merging parties and their counsel to approach the Tribunal for a consent order in the aftermath of *Palm Dairies*.[45] However, in July of 1989 the Tribunal released a positive decision in the *Gemini I* case. Among other things, the Tribunal used *Gemini I* as an opportunity to respond to criticism that the *Palm Dairies* decision indicated an inappropriate antipathy to behavioural remedies:

> The order [in *Gemini I*] imposes behavioural constraints on the respondents. The tribunal is aware that there has been some discussion that its decision in *Director of Investigation & Research v. Palm Dairies* stands for the proposition that the tribunal is not prepared to issue behavioural type orders. *Such an interpretation is a misreading of that decision*.[46]

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reappeared more recently in the *Ridge Landfill* case (*supra* note 14 at para. 100), in which the Tribunal rejected the respondent's proposal (offered as a counter-proposal to divestiture) to provide landfill space to local competitors. The Tribunal concluded that "there is reason to doubt the effectiveness" of the agreement, as the respondent could engage in potentially discriminatory behaviour towards other firms through a variety of administrative provisions in the supply agreement.

[43] *Canada (Director of Investigation & Research)* v. *Air Canada* (1989), 27 C.P.R. (3d) 476 (Comp. Trib.) [hereinafter *Gemini I*].

[44] Goldman, *supra* note 38 at 19.

[45] Mr. Goldman, the Director of the Bureau during this period, has stated that "[i]t was my view that if we could fulfil the objectives of the legislation through the acceptance of appropriate divestiture undertakings which addressed the likely post-merger lessening of competition, in certain instances we would consider doing so. It would, of course, have been preferable to have had a smooth-operating consent order procedure which would have allowed us in certain instances to send the resolution on for a public filing before the Competition Tribunal, but that simply was not feasible in the circumstances that we faced over that two-year period": *ibid.* See also Stanbury, *supra* note 39 at 433.

[46] *Supra* note 43 at 514 (emphasis added).

The Tribunal distinguished the situation in *Gemini I* from *Palm Dairies*, particularly with respect to the vagueness of the order.[47] It further noted that:

> [t]he object of a consent order is to eliminate the substantial lessening of competition which the Director alleges will result from the merger. *If the terms of such an order are vague and therefore cannot be enforced by way of contempt proceedings*, or if the terms imposed are virtually impossible to monitor, then the order cannot meet the test of effectiveness necessary to eliminate the substantial lessening of competition which is required of it […] when those terms are essential to the creation of a post-merger competitive situation, as they were in *Palm Dairies*, then a significant degree of precision is required and the tribunal must be convinced that they can be enforced effectively.[48]

Gemini I involved a consent order application arising out of the proposed combination of the computer reservation systems ("CRS") of Air Canada and Canadian Airlines to create the Gemini CRS. Through the use of a CRS, information regarding airline fares and conditions, schedules, and seat availability is distributed to travel agents, who in turn use the system to book airline tickets and other travel services such as car rentals, hotel reservations, etc. The combined Gemini entity would account for approximately 80% of the CRS market in Canada. The Director concluded that given the overwhelming importance of Air Canada and Canadian in the domestic air travel market, any other competing CRS would require access to the Air Canada and Canadian flight information in the Gemini system in order to survive.

The detailed consent order in the *Gemini I* case consisted entirely of behavioural provisions, notwithstanding the submissions of at least one intervenor in favour of a structural

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[47] *Ibid.* at 514-15.

[48] *Ibid.* at 515 (emphasis added).

remedy.[49] It restricted the conduct of Air Canada and Canadian, as owners of Gemini, and the operation of the actual CRS itself. With respect to Air Canada and Canadian, the provisions included:

- a requirement that they provide all other CRS's operating in Canada with a direct link to the Air Canada and Canadian reservation systems, provided that the airlines which own the other CRS's offered reciprocal access to Gemini;
- an obligation to participate in all other CRS's operating in Canada on commercially reasonable terms;
- a requirement to provide complete, timely and accurate information concerning their respective schedules, fares and seat availability to all CRS's operating in Canada on the same timing and basis as such information is provided to Gemini;
- a prohibition against pressuring travel agents, through the use of commission incentives or service levels, to book tickets through Gemini instead of other CRS's; and
- a firewall precluding Air Canada and Canadian employees from sharing "commercially sensitive information" between the two airlines (in order to prevent the use of Gemini as a vehicle for coordinated behaviour).

A similarly detailed set of behavioural restrictions applied to the operations of the Gemini system. The sophistication and precision of the order is also evident in a provision which was designed to provide a "'level playing field' within the industry". It required any CRS requesting direct links to the Air Canada or Canadian reservation systems to enter into a contract incorporating all of the restrictions in the consent order relating to the daily operation of

[49] The Consumer's Association of Canada argued that "the only effective remedy is to order dissolution of the merger": *ibid.* at 501. It should be noted that the Tribunal stated on multiple occasions that the pending acquisition of one-third of Gemini by the Covia Partnership (an alliance including United Airlines, US Air, British Airways, KLM, SwissAir and Alitalia) helped it to overcome its concerns about the potential for collusive behaviour that would otherwise exist between Air Canada and Canadian: see, *e.g.*, *ibid.* at 497 and 501.

Gemini.[50] In this way, other airlines could not gain an advantage over Air Canada and Canadian by virtue of the constraints imposed on them by the consent order.

In addition to approving the use of behavioural remedies, the Tribunal in *Gemini I* declined to adopt a more demanding test for the approval of non-structural consent orders. Faced with the argument from one of the intervenors that "because there are significant regulatory [*i.e.* behavioural] aspects to the order, the Tribunal should adopt a different test" by asking "whether or not there are changes to the consent order which could be made to significantly improve its effectiveness", the Tribunal applied the traditional test for approval which requires only that the proposed remedy prevent the substantial lessening of competition.[51]

(iii) Asea Brown Boveri/Westinghouse [52]

On the heels of the successful consent order proceeding in *Gemini I*, the Director brought a consent application relating to Asea Brown Boveri's ("ABB") proposed acquisition of the electrical transmission and distribution equipment manufacturing operations of Westinghouse Canada. In the Director's view, the merger was likely to result in a substantial lessening of competition in the market for certain large power transformers, where the merged entity would have a market share of approximately 75%.

The order required ABB to petition the federal Department of Finance for tariff reductions and remissions (suspension of tariff duties for a specified period). These

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[50] *Ibid.* at 488.

[51] *Ibid.* at 513 (the submission came from American Airlines).

requirements were intended to lower the entry barriers to the Canadian market and allow foreign manufacturers to compete with ABB in Canada. In separate undertakings (curiously, not part of the consent order), ABB also agreed not to bring any anti-dumping complaints against U.S. manufacturers of transformers for five years.

In the event that ABB was unable to achieve the tariff reductions and remissions by the deadlines specified in the order, certain assets were designated for divestiture. Failure to divest those assets within a 120-day period would trigger a second, larger divestiture requirement. The divestiture condition accompanied a "hold separate" provision in the consent order, requiring ABB to maintain the Westinghouse assets as an independent, financially viable package "until either the more permanent remedies come into effect or it becomes apparent that they will not be achieved."[53]

The *ABB* case provides a valuable model for the implementation of behavioural remedies. Instead of proceeding on a divestiture-first basis, the Director gave ABB an opportunity to satisfy his concerns before imposing a sale of the acquired assets. The case may provide a compromise for critics of behavioural remedies — allow the parties an opportunity to resolve the anti-competitive concerns and, if they are unsuccessful, *then* apply the divestiture remedy. A suitably-drafted "hold separate" order can protect the viability of a divestiture (*i.e.* concerns about "unscrambling the omelette") in the event that the behavioural undertakings are not completed in a satisfactory way.

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[52] *Canada (Director of Investigation and Research)* v. *Asea Brown Boveri Inc.*, [1989] C.C.T.D. No. 35 (QL) (Comp. Trib.) [hereinafter *ABB*].

(iv) Imperial Oil/Texaco [54]

The proposed acquisition by Imperial Oil (Exxon's Canadian affiliate) of Texaco Canada involved a combination of two of the largest Canadian integrated oil companies and raised several concerns at the Competition Bureau. After months of negotiations, and being rebuffed at the Tribunal in his first attempt,[55] the Director produced a consent order which the Tribunal accepted. In addition to the divestiture of certain Texaco gas stations and terminals, the order required Imperial to guarantee unbranded gasoline supply to independent dealers in Ontario and Quebec for a seven-year period. This provision responded to concerns that Imperial's acquisition of Texaco's refineries and terminals would result in restrictions of supply to the independent dealers, reducing their effectiveness as competitors of Imperial and other integrated suppliers in concentrated retail gasoline markets. The supply guarantee provisions dealt at length with the volume and price of the product[56] to be made available to the independents, thus allaying the effectiveness and enforceability reservations expressed by the Tribunal in its interim decision on the initial draft of the order.

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[53] *Ibid.* at para. 16.

[54] For the initial reasons of November 10, 1989, see *Canada (Director of Investigation and Research)* v. *Imperial Oil Ltd.* (1989), 45 B.L.R. 1 at 7 (Comp. Trib.) [*hereinafter Imperial I*]. The Tribunal released its final decision on the merits on January 26, 1990, [1990] C.C.T.D. No. 1 (QL) [hereinafter *Imperial II*], and issued the consent order on February 6, 1990, [1990] C.C.T.D. No. 3 (QL), aff'd (1992), 41 C.P.R. (3d) 493 (F.C.A.) [hereinafter *Imperial III*].

[55] *Imperial I*, *ibid.* at 11-12. (The Tribunal rejected the first consent order on the grounds that, *inter alia*, the supply provisions did not contain precise pricing terms, did not guarantee adequate volumes, and permitted Imperial to offer lower volumes to independents based on their purchases in the previous year.)

[56] *Imperial III*, *supra* note 54 at paras 21-31.

This case demonstrates the potential for use of behavioural restraints and divestiture in tandem to craft an effective remedy. It also indicates the care with which the Tribunal will scrutinise the design of pricing and volume terms in supply commitments.

(v) Ultramar/Coastal [57]

Ultramar's proposed acquisition of Coastal Canada Petroleum's Ottawa petroleum terminal and wholesale supply business raised Bureau concerns regarding substantial lessening of competition in the markets for wholesale supply of petroleum products and the provision of terminal storage facilities in the Ottawa region. Coastal was the primary wholesale supplier of gasoline and other petroleum products as well as storage capacity to independent marketers in Ottawa. Ultramar competed with the independent marketers, and the Bureau accepted their concerns that the acquisition might provide it with the ability and incentive to disadvantage them in respect of future supplies. The remaining terminal operators (Imperial Oil, Petro-Canada and Shell Canada) were integrated oil companies that also competed with the independents.

Ultramar agreed to a draft consent order, consisting entirely of behavioural remedies but backed up by a divestiture provision which would be triggered by non-compliance with the behavioural provisions.[58] It required Ultramar to:

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[57] *Canada (Commissioner of Competition)* v. *Ultramar Ltd.*, [2000] C.C.T.D. No. 4 (QL) (Comp. Trib.) [hereinafter *Ultramar*]. One of the authors was counsel to Coastal Petroleum, the vendor of the assets that Ultramar was seeking to purchase.

[58] The version of the draft order that the Tribunal reviewed is available online, at: <http://www.ct-tc.gc.ca/english/cases/ct-2000-001/0001h.pdf>.

- maintain the Coastal terminal for a minimum of three years (this requirement was intended to, among other things, ensure that a viable asset package existed in the event that the divestiture provision was triggered);

- within two years, refurbish and re-open an adjacent Ultramar terminal which had been mothballed since 1995;

- provide uninterrupted service at the Coastal facility, in the same manner as the facility was operated pre-acquisition, until the refurbished Ultramar terminal was opened;

- maintain at least three loading arms, including at least two dedicated to blending fuel ethanol with gasoline (a major product purchased by independents), at either the Coastal or Ultramar facility;

- offer to supply a minimum amount (the average of the annual amounts sold by Ultramar and Coastal to Ottawa independents over the past three years) of refined petroleum products to independent marketers at "wholesale prices to be negotiated" (but not to exceed the monthly average of the posted Montreal rack prices plus 0.5 cents per litre); and

- offer to supply fuel ethanol to independent marketers at "wholesale prices to be negotiated". [59]

In a decision reminiscent of the *Palm Dairies* and *Imperial I* cases, the Tribunal refused to issue the consent order.[60] It criticised the supply requirements for creating "no enforceable obligation on Ultramar regarding prices at which it would have to sell to independents" other than "the obligation to negotiate in good faith".[61] It also complained that the draft order contained "no requirement to negotiate other terms of a contract such as credit terms

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[59] These behavioural provisions were subject to a number of "carve-outs" where Ultramar failed to meet its supply levels or operating/production levels at either facility due to force majeure, difficulties experienced in transitioning from the Coastal facility to the Ultramar facility or undertaking maintenance of the tankage facilities at either terminal.

[60] Ultramar subsequently abandoned the transaction and, after an unsuccessful search for an alternate buyer, Coastal shut down the facility (an outcome far less desirable for the independent marketers than the Ultramar transaction they had opposed).

[61] *Supra* note 57 at para. 40.

or delivery terms."[62] Since the volume commitment related to offers to supply, rather than actual sales, the Tribunal concluded that Ultramar could refuse to sell to independents at competitive prices. Unlike *Imperial II*, there was no "reasonable commercial terms" clause (and Ultramar declined to accept such a revision after it was suggested as a possibility in the hearing before the Tribunal). When both counsel for the Commissioner and for Ultramar pointed out that, having made major investments to acquire and refurbish these terminals, as well as a related refinery expansion and ship acquisition, Ultramar would have strong economic incentives to price competitively in order to generate sales and recoup its expenditures, the Tribunal replied that its "role in the context of consent orders is not to enforce or embrace economic theory".[63]

(vi) Chapters/Indigo [64]

In February 2001, Trilogy Retail Enterprises L.P. made a bid to acquire Chapters Inc., Canada's largest book retailer, and merge it with Indigo Books & Music Inc., a Trilogy affiliate and the only other major book store chain in Canada. Pre-merger, Chapters and Indigo dominated the book superstore business in Canada, owning 92 (77 + 15) of 96 book superstores nationwide. In the small-format bookstore business, Chapters operated 231 locations; the second

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[62] *Ibid.* at para. 38. The Tribunal also noted, with respect to the Ultramar's carve-out protections, that while it "takes no issue in principle" with such provisions, they "may go further than necessary", and that "it is notable that no such similar protection is offered to the independent marketers": see *ibid.* at para. 51.

[63] *Ibid.* at para. 47. This was a curious response for a specialized tribunal comprising an economist and a business person as well as a judge with considerable competition law background. (For a critical commentary on the decision, see J.D. Bodrug, "Competition Tribunal Dismisses Application for Consent Order for Ultramar/Coastal Canada Petroleum Merger" (Spring/Summer 2000) 20 Can. Comp. Rec. 87.)

[64] See *Canada (Commissioner of Competition)* v. *Trilogy Retail Enterprises L.P.*, [2001] C.C.T.D. No. 29 (QL) (Comp. Trib) (Reasons Regarding Consent Order) and *Canada (Commissioner of Competition)* v. *Trilogy Retail Enterprises L.P.*, [2001] C.C.T.D. No. 20 (QL) (Comp. Trib) (Consent Order). The Consent Order and Reasons for Consent Order in this case are both available online, at <http://www.ct-tc.gc.ca/english/cases/ct-2001-003/0031b.pdf> and <http://www.ct-tc.gc.ca/english/cases/ct-2001-003/0033.pdf> respectively.

largest operator had 10 locations. Chapters and Indigo also owned the only two significant online book retailers in Canada, Chapters Online and Indigo.ca.

Not surprisingly, the Competition Bureau concluded that the transaction would lessen competition substantially, in both the downstream (retail) and upstream (publishing) book markets. The parties and the Bureau eventually negotiated a draft consent order which combined structural and behavioural remedies. It imposed significant divestitures, including nine Chapters and four Indigo superstores, 10 small-format mall bookstores, Indigo's Mississauga distribution facility, the Indigo.ca online retailer, and up to three of the trade names "SmithBooks", "Classic Books" and "Prospero" (provided that no purchaser could acquire more than one of these names). It also imposed a detailed five-year code of conduct upon Chapters/Indigo, which set out constraints on terms of trade with publishers as well as additional behavioural restraints upon Chapters/Indigo in the downstream sector. The code protected publishers by limiting Chapters/Indigo's ability to demand discounts from them, setting minimum payment deadlines, and governing the timing and volume of Chapters/Indigo's book returns to publishers. In the downstream business, Chapters/Indigo was prohibited from acquiring/opening any new stores for two years or enforcing restrictive covenants against the opening of other book stores in any of its shopping centre leases. It was also required to seek Bureau approval before re-entering the wholesale book business.

While the Bureau had predicted that the consent order would "encourage expansion or new entry by other booksellers, thereby maintaining choices for consumers and competition in the book industry",[65] it failed to do so. When a buyer had not been identified by the autumn of 2001, a trustee assumed responsibility for the divestiture under the terms of the consent order. According to industry publications, the trustee approached 288 prospective purchasers without receiving "a single firm offer for any of the stores".[66] The stores ultimately reverted back to Chapters/Indigo ownership, subject to the operating restrictions outlined above. Publishers and retailers were left to rely solely on the behavioural remedies for protection against Chapters/Indigo exercising its new market power. Early reactions from publishers indicated that the code of conduct had been effective in doing so.[67]

(vii) Astral/Télémédia [68]

On September 3, 2002, the Commissioner and Astral Media Inc. agreed to a consent order regarding the latter's acquisition of several French-language radio stations owned by Télémédia Radio Inc. in Québec. The Bureau was concerned that the acquisition would result in a substantial lessening of competition in French-language radio advertising in six local markets. In addition to the divestiture of six AM radio stations (which are to be sold as a network), the consent order contains significant behavioural remedies, including a code of conduct to protect advertisers which prohibits Astral from using exclusive or long-term (*i.e.* over 12 months) advertising contracts or "meet-or-release" or "most-favoured-nation" clauses within such contracts. Astral is also required to place the Télémédia FM radio stations in four of the six

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[65] See Industry Canada, News Release, "Competition Bureau Reaches Agreement with Trilogy, Chapters and Indigo" (April 5, 2001), available online at: <http://strategis.ic.gc.ca/SSG/ct02168e.html>.

[66] "Indigo Stores Revert" *Quill & Quire* (February, 2002) at 6.

[67] *Ibid.*

local markets under the control of a trustee, to be operated as competitors to the Astral stations in those markets until the earlier of: (i) six months after the opening of a new FM station in that market; or (ii) 42 months. Astral also agreed not to acquire or seek to acquire new French-language radio stations in the six local markets for a period of three years.

(b) Cases Resolved by Undertakings

Behavioural remedies have been accepted by the Commissioner in numerous undertakings to resolve merger cases without Tribunal proceedings. While such undertakings may not be enforceable as readily as Tribunal orders,[69] cases involving their use are more common than consent orders and demonstrate the precision and flexibility which behavioural remedies can offer.

(i) Avis/Budget Rent-a-Car [70]

In November 2002, the Bureau sought and obtained undertakings from Cendant Corporation (parent of Aviscar Inc.) relating to its proposed acquisition of Budget Group, Inc.'s car and truck rental business. The proposed merger would combine two of the largest car and truck rental businesses in Canada. The undertakings, which were entirely behavioural, focussed

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[68] This case has not yet been reported, but the consent order is available online, at: <http://www.ct-tc.gc.ca/english/cases/ct-2001-010/0024b.pdf>.

[69] As noted in Part 2(b) above, there is no specific statutory basis for undertakings in the *Act*, although the Quebec Court of Appeal has endorsed them as part of the Commissioner's implicit powers to administer and enforce the *Act* (see the quotation reproduced at *supra* note 29). While undertakings arguably are enforceable in the ordinary courts as a legal contract, in practice the Bureau has overcome the enforceability issue by requiring the merging party(ies) to consent in advance to an application at any time to the Tribunal for a consent order in the same terms as the undertakings. For further discussion, see A.N. Campbell, *Merger Law and Practice: The Regulation of Mergers Under the Competition Act* (Toronto: Carswell, 1997) at 279ff.

[70] See Industry Canada, Information Notice, "Competition Bureau Obtains Undertakings to Resolve Concerns in Cendant Acquisition of Budget Rent a Car" (November 27, 2002), available online at:

on a Code of Conduct governing Cendant's interaction with the Budget licensees/franchisees, and also required Cendant to implement a compliance program to educate Avis and Budget about the relevant provisions of the *Competition Act* as well as the "special obligations" imposed on Cendant under the Code of Conduct. Annual compliance reports, certified by a director or officer of Cendant, were also required.

Cendant's "special obligations" included undertakings to:

- Not "exert control over the competitive aspects of the operations of the Budget Licensee's car rental business";
- Implement a firewall to prevent the sharing of information (other than details concerning fleet size and gross revenues) between the Budget licensees and Cendant; and
- Operate the assets of Budget "in a manner that is consistent with the promotion and growth of the Budget brand".

These undertakings appear to be an effort on the Bureau's part to preserve the competitive relationship that existed between Avis and Budget in Canada pre-merger and the independence of Budget's local licensees. They represent a particularly good example of the non-intrusive nature of behavioural remedies.

<http://strategis.ic.gc.ca/SSG/ct02464e.html>. The undertakings were not publicized on its website, but can be obtained by contacting the Bureau directly.

(ii) Air Canada/Canadian Airlines [71]

Air Canada's 1999 acquisition of rival Canadian Airlines yielded extensive undertakings governing Air Canada's future conduct in the Canadian airline industry. Although the Bureau publicly lamented the extremely high market shares (approaching 90%) the new airline would possess in Canada, Canadian Airlines' financial distress and the lack of a competitively preferable purchaser meant that Air Canada's offer represented "the best possible solution for consumers, under the circumstances".[72] While the Commissioner has been criticised by some for not obtaining more substantial remedies, the logic of a "failing firm defence"[73] is that no remedy would have been called for because the merger would not be the cause of any substantial lessening of competition.

The undertakings were aimed at reducing entry barriers to the Canadian market in the hope of inducing new entrants. They required Air Canada to:[74]

- surrender to other Canadian carriers up to 28 arrival/departure slots at Toronto's Pearson Airport during peak hours;
- permit "eligible" Canadian carriers (those with annual revenues below Cdn$250 million and no affiliations with foreign carriers) to participate in Aeroplan (Air Canada's frequent flyer program) on commercially reasonable terms, on a non-exclusive basis, for five years;

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[71] See Industry Canada, Information Notice, "Competition Bureau Announces It Will Not Oppose Acquisition of Canadian Airlines" (December 21, 1999) and accompanying Backgrounder and Undertakings, all available online at: <http:// strategis.ic.gc.ca/SSG/ct01670e.html>. See also: Commissioner of Competition, *Annual Report, 2000*, *supra* note 5 at 14-15.

[72] Information Notice, *ibid.*

[73] *Supra* note 4, s. 93(b).

[74] *Supra* note 71. Except as otherwise noted, the undertakings expire after seven years.

- enter into interlining and joint fare agreements upon request of any other Canadian carrier;

- give Canadian air carriers a right of first refusal to purchase surplus Air Canada airplanes, for a three-year period;

- assign, at the option of any new discount carrier, its facilities at Hamilton airport at cost, and refrain from establishing a discount carrier service in Eastern Canada until September 2001;

- change its travel agent commission incentive program to focus only on international flights, and to eliminate market share sales targets, for a five-year period;

- divest, at the 20 airports in which it held more than 60% of ticket counters, ticket counter positions, as well as certain gates and loading bridges at Pearson airport and Dorval airport in Montreal; and

- divest, on a "best efforts" basis, Canadian Regional Airlines Ltd. ("CRAL").

The CRAL divestiture proved a failure. Under the terms of its undertakings to the Commissioner, Air Canada offered CRAL for sale for a 60-day period during which it was required to sell the airline "to the person who offers the highest price at or above the fair market value of CRAL."[75] Air Canada never received an offer at or above fair market value (which was determined by an independent valuator) and the assets reverted back to Air Canada after the 60-day period expired. Thus, as with the *Chapters/Indigo* remedies discussed above, the behavioural provisions were the operative remedy.

[75] See Air Canada's Undertakings, *ibid.* at 15.

(iii) Lafarge Canada/Holnam [76]

In October 1998, Lafarge Corporation acquired certain assets of Holnam Inc. In Canada, the transaction resulted in Lafarge Canada's acquisition in British Columbia of a cement distribution terminal at New Westminster and a limestone quarry on Texada Island. Following the Bureau's review of the transaction, Lafarge Canada agreed to divest the New Westminster facility. It also agreed to behavioural undertakings requiring it to waive non-competition provisions in the asset purchase agreement in order to allow Holnam to supply cement into the B.C. interior from facilities in Washington and Montana that were not part of the transaction.[77] While the divestiture in this case was successful, the behavioural undertakings were not ancillary: they provided the full remedy in a separate market where competition would otherwise have been prevented by a covenant in the contract governing the transaction.[78]

(iv) SmithBooks/Coles [79]

The 1995 merger of SmithBooks and Coles combined Canada's two largest retail book chains. Despite a combined market share of over 50% (which expanded in the six years

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[76] See Industry Canada, Information Notice, "British Columbia Portland Cement Merger Settled" (October 16, 1998), available online at: <http://strategis.ic.gc.ca/SSG/ct01321e.html>; and related Information Notice, "Lafarge Completes Divestiture of Portland Cement Terminal" (March 9, 1999), available online at: <http://strategis.ic.gc.ca/SSG/ct01481e.html>. See also: *Annual Report, 2000*, *supra* note 5 at 16-17.

[77] The Bureau took a similar approach to a non-competition clause in an agreement between Petro-Canada and North Atlantic Refining regarding the latter's purchase of a refinery in Come By Chance, Newfoundland: see Industry Canada, News Release, "Competition Concerns Resolved — Restrictions Attached to Newfoundland Refinery Lifted" (January 3, 2001), available online at: <http://strategis.ic.gc.ca/SSG/ct02105e.html>.

[78] Curiously, the Bureau also noted in a public statement that "[t]he settlement is intended to return the market to its pre-merger state" — if true, this would suggest that Lafarge agreed to more onerous provisions than would otherwise be required (*i.e.* a remedy which only prevents a "substantial" lessening of competition) had the Bureau brought the matter before the Competition Tribunal: see October 16, 1998, Information Notice, *supra* note 76; and the discussion in Part 2(a) above.

leading up to Trilogy's bid to acquire the renamed Chapters[80]), the Director did not challenge the merger. Independent booksellers were regarded as providing effective competition (perhaps because this analysis pre-dated the trend towards book superstores in Canada) and barriers to entry were considered low enough to prevent the exercise of market power. However, in order to guarantee low entry barriers, the Director obtained commitments from the merging parties to waive restrictive covenants in their existing leases, not seek restrictive covenants in any future leases, and inform their landlords that they "will not take action to block access to retail sites by competing book stores."[81] This type of behavioural remedy is ideally suited to overcoming contract-based entry barriers. Not surprisingly, these types of behavioural provisions reappeared in the *Chapters/Indigo* consent order.

(v) Canada Post/Purolator [82]

Following a lengthy examination by the Bureau, the Director chose not to challenge Canada Post Corporation's ("CPC") 1993 acquisition of 75% of Purolator Courier Inc., then Canada's largest courier company and a competitor of Canada Post's "Priority Courier" business. Crucial to this decision were CPC's commitments to: refrain from subsidising Purolator with revenues from its "exclusive privilege in letter mail"; maintain Purolator as a

[79] Industry Canada, News Release (and accompanying Backgrounder), "DIR Will Not Challenge Smithbooks' Acquisition of Coles Book Stores Limited" (March 21, 1995). See also the Director's summary of the transaction in: Director of Investigation and Research, *Annual Report, 1995* (Ottawa: Supply and Services Canada, 1996) at 26-27.

[80] See the discussion in Part 3(a)(vi) above.

[81] Backgrounder, *supra* note 79 at 5.

[82] Industry Canada, News Release (and accompanying Backgrounder), "DIR Will Not Oppose Canada Post's Acquisition of Purolator" (November 26, 1993). The Bureau dismissed the "large number of complaints" about allowing a Crown corporation that was already active in the private sector to acquire a leading competitor as "not within the purview of the Act": see the Backgrounder at 5.

separate corporate entity (with a separate board of directors); and conduct any dealings between Purolator and CPC on an "arm's length commercial basis". This resolution demonstrates that even an issue as complex as cross-subsidisation can be addressed through behavioural remedies.[83]

(vi) Consumers Packaging/Domglas [84]

The proposed acquisition of Domglas Inc. by Consumers Packaging raised concerns in various inelastic segments of the rigid-wall packaging materials market (both companies produced glass containers for a wide range of applications). The Director feared that the merged entity could be positioned to exercise market power, but ultimately did not oppose the merger. Instead, following the example set in *Asea Brown Boveri/Westinghouse*,[85] he allowed the merger to proceed based on Consumers Packaging's undertaking to obtain tariff reductions under the *Free Trade Agreement* to lower entry barriers for American firms. Consumers Packaging also undertook to guarantee adequate long-term supply to vulnerable customers on "equitable terms and conditions."[86] This was a much less demanding and concrete

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[83] While the Bureau has not taken any further enforcement action with respect to the cross-subsidisation issue, more recently UPS (a major international courier competitor) has brought an investor-state arbitration under chapters 11 and 15 of *NAFTA* which is based on cross-subsidisation claims. The UPS claim was issued January 19, 2000, and is available online, at: <http://www.dfait-maeci.gc.ca/tna-nac/parcel-en.asp>. The matter is currently pending before an arbitral tribunal.

[84] Industry Canada, News Release (and accompanying Backgrounder), "DIR Decision on the Acquisition of the Assets of Domglas Inc. by Consumers Packaging Inc." (April 25, 1989). See also the comments in: Director of Investigation and Research, *Annual Report*, *1990* (Ottawa: Supply and Services Canada, 1990) at 12.

[85] *Supra* note 52.

[86] *Supra* note 81.

supply commitment than subsequently required by the Tribunal in the *Imperial II* and *Ultramar/Coastal* cases.[87]

(vii) Molson/Elders (Carling O'Keefe) [88]

The merger of Molson Companies Ltd. and Elders IXL Ltd. (the parent of Carling Breweries) attracted the Director's attention because it combined two of Canada's three largest breweries. Despite the resulting duopoly (Molson and Labatt's) with a small fringe of other competitors, he permitted the merger to proceed for various reasons including the substantial efficiency gains expected and an anticipated reduction in inter-provincial trade. However, in the Quebec market where Molson would have a particularly strong position, it was required to guarantee access to its distribution system for local and potential foreign competitors (excluding Labatt's) on a non-profit, fee-for-service basis. Here again, supply commitments were dealt with in a relatively brief and general manner.

(viii) CAPAC/PROCAN [89]

This case involved the proposed merger of the Composers, Authors, and Publishers Association of Canada Ltd. (CAPAC) and the Performing Rights Organization of Canada Ltd (PROCAN). CAPAC and PROCAN were two of only three organizations in Canada that collected performing rights fees for the public use of music. As both societies employed long-term (five-year) contracts with their members, barriers to entry for new societies were

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[87] *Supra* notes 54 and 57 respectively.

[88] Industry Canada, News Release (and accompanying Backgrounder), "Proposed Merger of the Brewing Operations of Molson and Carling O'Keefe" (July 6, 1989). See also the comments in: Director of Investigation and Research, *Annual Report, 1990, supra* note 84 at 14-15.

[89] For a summary of the case, see Director of Investigation and Research, *Annual Report, 1990*, *ibid.* at 11-12.

considered to be high. The Director allowed the merger to proceed on the strength of an undertaking from the parties to amend the terms of contracts with members from five years to three years, along with an option to terminate the contract with notice after the second year.[90] All members of both societies were to be notified of these changes.

4. BEHAVIOURAL REMEDIES VS. DIVESTITURE — A COMPARATIVE ANALYSIS

As noted at the outset of this paper, divestiture has traditionally been perceived as the preferred remedy in resolving anti-competitive mergers. Its proponents have cited simplicity, superior effectiveness and the lack of ongoing monitoring as reasons why structural remedies are preferable to behavioural remedies.[91] Divestiture addresses the likelihood that competition would otherwise be lessened substantially in two ways: (i) by reducing the size (and presumably market power) of the merged firm; and (ii) by increasing the size (and competitive strength) of a competing firm. However, divestiture orders often are not as simple as they appear or as successful as might be assumed. In order to effectively implement a divestiture remedy significant challenges must be overcome, including creating a viable asset package, finding a suitable buyer, and completing the sale in a timely fashion. Further, the often-invoked criticism that behavioural remedies require ongoing monitoring appears to be overstated, given that divestiture processes may involve monitoring for six months to two years or more before matters are concluded.

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[90] *Ibid.* at 11.

[91] See, *e.g.*, RBC/BMO Letter, *supra* note 2; Sanderson/Wallwork, *supra* note 10; Andre Lafond (Deputy Director — Civil Matters), "Notes for an Address to the Canadian Bar Association Competition Law Section, Annual Competition Law Conference", September 19, 1997, available online at: <http://strategis.ic.gc.ca/SSG/ct01098e.html>.

(a) Creating a Viable Asset Package

If a divestiture is to achieve the goal of increasing the size and competitive strength of a competing firm, it must offer an asset package with the "critical mass" and resources necessary to compete effectively with the merged firm. Where the asset package does not meet this threshold, the effectiveness of divestiture as a remedy may be jeopardized because:

- finding a buyer will be difficult, since potential buyers are usually industry competitors able to recognize the flaws in the asset package; and
- even if a buyer is found, the buyer will have difficulty competing effectively if the asset package is insufficient.

These issues are well-illustrated by the *Chapters/Indigo* case. As discussed more fully below, the fact that no willing Canadian buyers were found is likely attributable in part to an insufficient asset package. If a buyer had emerged, it is also questionable whether the acquisition would have yielded an effective competitor. Intervenors had warned the Tribunal that "a prospective purchaser does require a critical mass of stores to achieve the economies of scale necessary to compete against the new Chapters/Indigo entity" and that "the assets designated for divestiture under the DCO are 'unlikely to be sufficiently profitable to be attractive to a purchaser'."[92] Curiously, the Bureau agreed to a divestiture of only 13 book superstores in the consent order despite arguing in its "Statement of Grounds and Material Facts" that a "minimum critical mass" of 24 superstores would be needed to "support the corporate overhead associated with a national chain".[93] Given the failure of the auction, it would appear

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[92] Reasons Regarding Consent Order, *supra* note 64 at para. 29.

[93] See the Commissioner's "Statement of Grounds and Material Facts" at para. 60, available online at: <http://www.ct-tc.gc.ca/english/cases/ct-2001-003/0001b.pdf>.

that the initial estimation that 24 superstores would be required to form a viable asset package should have been followed.

The Tribunal also addressed this issue in the contested *Southam* merger application.[94] The Director sought divestiture of either the *North Shore News* or the *Real Estate Weekly*, two Southam newspapers in the lower mainland of British Columbia, to remedy the anticipated substantial lessening of competition. Southam countered that the appropriate remedy was divestiture of only the real estate supplement in the *North Shore News* rather than the entire newspaper. The Tribunal rejected Southam's submission, concluding that the real estate supplement could not compete effectively with Southam when operated as a stand-alone enterprise.[95]

(b) Finding a Suitable Buyer

The Tribunal discussed the importance of finding a single, suitable buyer in the *Imperial I* decision. When considering the proposed divestiture remedy in the draft consent order, it noted that:

> [t]here is some reason to think that the hiving off of some of the assets plus the potential sale of those remaining (if it were to several purchasers in

[94] *Supra* note 18.

[95] It noted that "the evidence points away from [the supplement] being an effective competitor", and was reluctant to accept Southam's proposal to bolster the divested supplement with supply commitments for newsprint, administrative services, delivery, *etc.* since "a remedy that depends, for its possible success, on supply contracts between the only two competitors in the market is somewhat suspect": *ibid.* at 252. In the result, the Tribunal ordered a divestiture of either of the two publications, each of which had generated only about 15% of its revenues from the overlapping relevant market of real estate advertising in the North Shore region of Vancouver. The Supreme Court ultimately upheld the Tribunal's conclusion that, where necessary to achieve an effective remedy, a divestiture which is broader than the affected relevant market may be ordered (see note 21 *supra*). While Southam's partially behavioural counter-proposal was rejected in this particular case, the flexibility of behavioural commitments may generally offer the benefits of more focussed remedies in these types of situations.

> piecemeal fashion) could so weaken the viability of the assets that the divestiture would not operate so as to prevent the substantial lessening of competition which arises as a result of the merger.[96]

Finding a single suitable buyer is sometimes difficult. The primary pool of potential buyers will usually focus on competitors in the seller's industry or in nearby product or geographic markets. However, the industry may have very few remaining competitors,[97] may lack buyers with either the interest or the financial resources to purchase the assets, or may be subject to regulatory constraints which limit the available buyers.

This occurred in the proposed *Chapters/Indigo* divestiture,[98] where neither Chapters nor the trustee was able to locate a willing buyer for the assets. There were no Canadian book sellers with the interest or financial backing to purchase the assets, and policies of the Department of Canadian Heritage which restrict foreign ownership of Canadian book retailers[99] excluded large American book sellers such as Barnes & Noble or Borders that would otherwise have been logical prospective buyers. As a result, the divestiture failed and the assets reverted back to Chapters/Indigo, leaving the behavioural provisions in the consent order as the only remedy.

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[96] *Imperial I*, *supra* note 54 at 7.

[97] This was the case in the *ABB* decision, *supra* note 52 at paras 19 and 22, where post-merger only one Canadian competitor remained in the market for "large" power transformers, and there were no remaining Canadian competitors in the market for "very large" transformers.

[98] See the discussion at note 64, s*upra*.

[99] See the Department's "Revised Foreign Investment Policy in Book Publishing and Distribution", available online at: <http://www.pch.gc.ca/progs/ac-ca/progs/eiic-csir/en_bookp.htm>.

Similar regulatory constraints, and a similar absence of remaining domestic competitors, also contributed to the failed divestiture in *Air Canada/Canadian Airlines*.[100] The ownership and other regulatory barriers facing U.S. and other foreign airlines precluded them from participating in the auction and none of the domestic regional or charter airlines were able to put together a satisfactory bid.

Even if a single buyer can be found, unless it has the resources and capabilities to be a strong competitor the divestiture may not limit an exercise of market power by the merged firm. For instance, where the merged firm is a large player in the relevant market and the divested assets are acquired by a small firm or a new entrant, particularly one with limited managerial depth or financing, the acquiror may be unable to prevent the merged firm from exercising market power. This problem will be exacerbated where the divestiture package does not have the "critical mass" necessary for the buyer to compete effectively with the merged firm.[101]

It is not always easy to determine whether a buyer is committed to competing in the business for the long-term. There is always a risk that the buyer may decide at some future point to liquidate the assets, potentially eliminating the value of the divestiture remedy. In the *Imperial Oil* case, the Tribunal required that the prospective purchaser be "someone who will maintain the viability of the divested assets."[102] In the absence of such a buyer, the Tribunal was

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[100] *Supra* note 71.

[101] See the above discussion of *Chapters/Indigo* and *Southam* on this point, *supra* notes 92 and 94 respectively.

[102] *Imperial I*, *supra* note 54 at 8.

willing to order a "crown jewels" divestiture of *all* of the Texaco assets in Atlantic Canada rather than only the Eastern Passage Refinery and certain retail service stations and terminals. As events unfolded, this concern was prescient. Ultramar acquired the refinery pursuant to a seven-year undertaking to operate the facility, subject to a "no material adverse change" clause. When Ultramar three years later sought to close the refinery in reliance on the adverse change clause, the Director reviewed the matter in detail and concluded that he had no basis for taking any further enforcement action under the *Act*.[103]

(c) Timely Implementation

Timely completion of divestitures may also pose challenges. Crampton has noted that "delay is the enemy of divestitures" because "commercial, labour and market conditions can often change rapidly" and "the economic or competitive viability of a product line or company can be quickly dissipated."[104] One early study of divestiture orders under the *Act* found that the average time taken to complete divestitures in Canada was sixteen months.[105] The authors of the

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[103] See the comments of then-Director G.N. Addy, "Notes for an Address to the 3rd Annual Competition Law Conference" (September 29, 1995), available online at: <http://strategis.ic.gc.ca/SSG/ct01409e.html>. The Director's decision was subsequently challenged in an application for judicial review by the Nova Scotia Attorney-General (acting at the behest of the local employees' union) but the Federal Court dismissed the petition: *Atlantic Oil Workers Union* v. *Canada (Director of Investigation and Research)*, [1996] F.C. 539 (F.C.T.D.). (The *Ultramar/Coastal* case, described at part 3(a)(v) above, is also an outgrowth of *Imperial Oil/Texaco*: Coastal Petroleum was the buyer of the Texaco terminal in Ottawa and a decade later decided to sell the business because of lack of critical mass and profitability in this single Canadian facility. After the Tribunal refused the proposed consent order, Coastal shut down the terminal.)

[104] P. Crampton, *Mergers and the Competition Act* (Toronto: Carswell, 1990) at 608.

[105] See Sanderson/Wallwork, *supra* note 10 at 769. Furthermore, this figure did not include the divestitures in *Imperial II* which took several years to complete.

report also cited three American studies of divestiture,[106] whose conclusions regarding timeliness of divestiture orders were more bleak than their own.

A distinguished Canadian economist offered the following observations in a 1998 study:

> [d]ivestitures have apparently been effective in some cases (*Safeway / Woodward*) and problematic in others (*A&P*). The divestiture remedy has taken a long time to take effect in some cases (*Imperial Oil*, due to environmental regulatory problems and *Southam*, due to appeals on the merits and on the remedy). *Orders guaranteeing access or requiring supply of essential inputs have apparently been more successful*.[107]

Professor McFetridge's report also notes the inherent lack of flexibility offered by structural remedies, given their permanent effects. With respect to potential banking mergers in Canada, he concluded that due to the wide range of products in the financial services industry, and the rapidly changing technology, divestiture remedies may be even more difficult to implement than in traditional manufacturing industries.[108] With their greater scope for tailored remedies, behavioural restraints may be particularly appropriate for complex sectors such as financial services, high-technology or network industries.[109]

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[106] The reports are: K. Elzinga, "The Antimerger Law: Pyrrhic Victories?" (1969) 12 J.L. & Econ. 43; M.R. Pfunder *et al*, "Compliance with divestiture orders under section 7 of the Clayton Act: An analysis of the relief obtained" (1972) 17 Antitrust Bull. 19; and R.A. Rogowsky, "The Economic Efficiencies of Section 7 Relief" (1986) 31 Antitrust Bull. 187. More recently, the FTC has released a detailed study on the its own divestiture process, which is available online, at: <www.ftc.gov/opa/1999/9908/divestreport.htm>.

[107] D.G. McFetridge, *Competition Policy Issues* (Research Paper prepared for the Task Force on the Future of the Canadian Financial Services Sector), September 1998, at 35, available online at: <http://finservtaskforce.fin.gc.ca/ research/pdf/ rr2_e.pdf> (emphasis added).

[108] *Ibid.* at 38.

[109] A leading member of the U.S. antitrust community has made similar observations. See: Mary Lou Steptoe, Acting Director, Bureau of Competition, Federal Trade Commission, "Remarks Before the Business Development Associates Inc." (March 14, 1995) (available on Westlaw at: 1995 WL 130674 F.T.C.) (Ms. Steptoe noted that "up until this decade

(d) Monitoring Concerns

During potentially lengthy pre-divestiture periods, the merged firm is usually required to submit monthly reports to the Bureau regarding the progress of the divestiture.[110] The Bureau will also normally require a hold separate order to protect the competitive viability and autonomy of the business prior to divestiture. Once a potential buyer has been found, the Bureau is again actively involved in evaluating and approving or rejecting the buyer.

Not only must the Bureau monitor the entire sale process, but one would expect it to monitor the divestiture post-closing to ensure that the remedy has been effective. In the *ABB* case, for instance, the Director monitored market conditions in the subject power transformer market for over four years.[111] When Ultramar proposed to acquire Texaco's Atlantic Canadian assets following the *Imperial II* divestiture, the total period of monitoring extended more than five years, beginning with Ultramar's undertakings in connection with the acquisition in September 1990 and then new undertakings given in 1993.[112] These cases illustrate the extent of monitoring of markets that may be required in divestiture cases. Behavioural remedies should therefore not be dismissed simply because they, too, may require monitoring.[113]

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divestiture of a plant or facility was the nearly exclusive remedy used to address section 7 violations […] However in the past few years I think we have become more sophisticated in our analysis. Part of this change is due to the fact that increasingly mergers are *technology driven*, rather than facility driven" (emphasis added).

[110] See Sanderson/Wallwork, *supra* note 10 at 772.

[111] See Director of Investigation and Research, *Annual Report, 1995*, *supra* note 79 at 24.

[112] See Director of Investigation and Research, *Annual Report, 1996* (Ottawa: Industry Canada, 1996) at 22.

[113] In many merger cases the Commissioner does not seek a remedy and instead relies only on his power to monitor the effects of a merger for three years. This practice also demonstrates the Commissioner's willingness to monitor markets when appropriate. See, *e.g.*, *Loblaws/Oshawa Group*, Commissioner of Competition, *Annual Report, 2000*, *supra* note 5 at 17; ; *PWA Corporation/Wardair*, Director of Investigation and Research, *Annual Report, 1994* (Ottawa: Supply and Services Canada, 1995) at 19; *Baxter Foods/McKay's Dairy*, *Annual Report, 1994*, *ibid.*; *Merlin Gerin/Square D Canada*

Criticism of behavioural remedies based on their monitoring requirements seems to stem from the Tribunal's strident objections to the behavioural provisions in the *Palm Dairies* consent order. As noted above, this initial hostility to behavioural remedies subsided in the three-year period between *Palm Dairies* and *Gemini I*. The *Gemini I* consent order comprised a broad and detailed array of behavioural restrictions which far exceeded those contained in the *Palm Dairies* draft order. Notwithstanding intervenors' criticisms, the Tribunal approved the *Gemini I* consent order after acknowledging that "[i]t is clear that the implementation of some of the terms of the consent order will require *the diligent and continual surveillance of the director*".[114]

Gemini I also illustrates a way in which the Bureau's monitoring efforts can be reduced. One of the provisions of the consent order required that other airlines seeking links to the Air Canada and Canadian reservation systems not only had to offer reciprocal access, but also had to enter into a contract incorporating restrictions which mirrored those imposed on Air Canada and Canadian in the order. In this way a level playing field would be created. The

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Electrical Equipment, Director of Investigation and Research, *Annual Report, 1993* (Ottawa: Supply and Services Canada, 1993) at 10; *Central Soya of Canada/Canada Packers* (certain assets), Director of Investigation and Research, *Annual Report, 1990, supra* note 84 at 12; *Institut Mérieux Canada/Connaught Bio Sciences*, *Annual Report, 1990*, *ibid*. at 13.

[114] *Supra* note 43 at 516 (emphasis added). The Tribunal also noted that "[i]t is clear that changed conditions or effective enforcement of the order may require a return to the tribunal for either changes to or interpretation of the order." However, variation applications (in both merger and non-merger settings) have been relatively infrequent and minor in scope. The one notable exception arose from the *Gemini I* order, but in fact had virtually nothing to do with problems related to competition in CRS markets or the order itself. Rather, in the face of severe financial difficulties that might result in the bankruptcy of Canadian Airlines and subsequent dominance of Air Canada in Canadian air transportation markets, the Director agreed to assist Canadian and its proposed minority equity investor, American Airlines, to extricate Canadian from the Gemini CRS (over the objections of Air Canada) so that its reservations/hosting functions could be transferred to American's competing Sabre CRS pursuant to a long-term services contract: see *Gemini II*, *supra* note 7.

Tribunal noted that such contracts would create “at least the possibility of parties to the link contracts enforcing these obligations by suing for injunctive relief or for damages.”[115]

While the reciprocal linking mechanism was highly customised for the CRS industry and the competition concerns in the *Gemini I* case, the concept of reducing enforceability and monitoring issues through contracts has significant potential application to other situations. For example, supply commitments can readily be dealt with through contracts, or at least minimum conditions that must be addressed in contracts, between the merged firm and the affected customers. Similarly, the Bureau has used codes of conduct to set post-merger boundaries that Indigo must respect in its dealings with publishers, governing Astral’s relationship with advertisers, and regulating Cendant’s conduct towards Budget licensees. In each of these cases, the codes of conduct contained arbitration clauses which permitted publishers, advertisers and licensees to initiate private arbitration proceedings to enforce the terms of the code.[116] Such arbitration regimes may provide an effective means for market participants to police the merged firm’s compliance with the behavioural restrictions placed upon it.

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[115] *Gemini I*, *ibid.* at 488.

[116] *Supra* notes 64 and 68, respectively. Arbitration clauses have been used to similar effect in several other cases — see, *e.g.*, the consent agreement reached in *Commissioner of Competition* v. *United Grain Growers Limited*, available online at: <http://www.ct-tc.gc.ca/english/cases/ct-2002-001/0105a.pdf> at para. 42ff; the undertakings given by Air Canada in the Canadian Airlines case, *supra* note 74 at no. 14ff; *Canada (Director of Investigation and Research)* v. *Canadian Waste*

5. CONCLUSIONS

The foregoing analysis is not meant to suggest that behavioural remedies are always superior to divestitures. Rather, our purpose was to examine some of the common reasons cited for the meagre use of behavioural remedies, with the intention of showing that these concerns have been over-stated and that the challenges of achieving effective divestiture remedies have been under-stated.

Our review of cases over the past decade and a half demonstrates that the Bureau has in fact been willing to entertain diverse and innovative behavioural remedies in a considerable number of cases. The Tribunal's reaction has been more mixed, but certainly there are several strong precedents supporting the use of behavioural consent orders in merger cases. This should hardly be controversial when one considers that behavioural orders are the principal remedy contemplated for the other reviewable practices in Part VIII of the *Act* and have been employed quite successfully in numerous abuse of dominance and refusal to deal cases.[117]

Services Inc., [1998] C.C.T.D. No. 10 (QL) at no. 15ff (Comp. Trib.); and *Canada (Director of Investigation and Research)* v. *ADM Agri-Industries, Ltd.*, [1997] C.C.T.D. No. 25 (QL) at no. 16ff (Comp Trib.).

[117] See, *Canada (Director of Investigation and Research)* v. *Nutrasweet Co.* (Reasons and Order) (1990), 32 C.P.R. (3d) 1 (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *Laidlaw Waste Systems Ltd.* (Reasons for Order) (1992), 40 C.P.R. (3d) 289 (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *D&B Companies of Canada* (Reasons for Order) (1995), 64 C.P.R. (3d) 216 (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *AGT Directory Ltd.* (the "CANYPS" case) (Consent Order), [1994] C.C.T.D. No. 24 (QL) (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *Bank of Montreal* (the "Interac" case) (Reasons for Consent Order) (1996), 68 C.P.R. (3d) 527 (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *Tele-Direct (Publications) Inc.* (1997), 73 C.P.R. (3d) 1 (Comp. Trib.); *Canada (Director of Investigation and Research)* v. *Chrysler Canada Ltd.* (Reasons and Order) (1989), 27 C.P.R. (3d) 1 (Comp. Trib.), aff'd (1991) 38 C.P.R. (3d) 25 (F.C.A.), leave to appeal ref'd (1992), 41 C.P.R. (3d) v (S.C.C.); and *Canada (Director of Investigation and Research)* v. *Xerox Canada Ltd.* (Reasons and Order) (1990), 33 C.P.R. (3d) 83 (Comp. Trib.).