

POLICY ROUNDTABLES

Competition Policy and Efficiency Claims in Horizontal Agreements

1995

Introduction

The OECD Competition Committee debated competition policy and efficiency claims in horizontal agreements in November 1995. This document includes an analytical note by Mr. John Clark of the OECD, written submissions from Canada, the European Commission, Italy, Japan, Switzerland, the United States and BIAC and an aide-memoire of the discussion.

Overview

Efficiency claims play a key role in the analysis of mergers and horizontal agreements. Static efficiencies, associated with the production and distribution of existing products, are most often considered relevant. Dynamic efficiencies, of improved processes and products, are also important, but they are inherently more difficult to estimate. Efficiencies tend to play a larger role in analysis of horizontal agreements than in analysis of mergers.

There are significant differences across countries in how efficiencies are factored into merger analysis, but there are also broad similarities. Most agencies do not reach consideration of efficiencies unless it is clear that a merger will tend to have anti-competitive effects. In such a case, the parties usually have a significant responsibility to establish that the merger should nevertheless be approved because it promises to yield significant efficiencies that cannot be obtained in less anti-competitive ways. Some countries apply a "consumer surplus" standard. Others apply a "total surplus" standard, which would approve a merger if the real resource savings will cause producers to gain more from the merger than consumers will lose from it.

Because competition authorities face an inherent informational disadvantage, efficiency claims and supporting evidence must be assessed with caution.

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COMPETITION POLICY AND EFFICIENCY CLAIMS IN HORIZONTAL AGREEMENTS

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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FOREWORD

This document comprises proceedings in the original languages of a roundtable on Efficiency Claims in Mergers and Other Horizontal Co-operation Agreements which was held by the Committee on Competition Law and Policy in November 1995. It is published as a general distribution document under the responsibility of the Secretary General of the OECD to bring information on this topic to the attention of a wider audience.

This compilation is one of several published in a series named "Competition Policy Roundtables."

PRÉFACE

Ce document rassemble la documentation, dans la langue d'origine dans laquelle elle a été soumise, relative à une table ronde sur "L'argument de l'efficience dans les fusions et accords horizontaux" qui s'est tenue en novembre 1995 dans le cadre du Comité du Droit et de la Politique de la Concurrence. Il est mis en diffusion générale sous la responsabilité du Secrétaire général de l'OCDE afin de porter à la connaissance d'un large public, les éléments d'informations qui ont été réunis à cette occasion.

Cette compilation est publiée dans la série intitulées" Les tables rondes sur le politique de la concurrence".

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BACKGROUND NOTE

(by the SECRETARIAT)

"There is general consensus that the basic objective of competition policy is to protect and preserve competition as the most appropriate means of ensuring the efficient allocation of resources - and thus efficient market outcomes - in free market economies. While countries differ somewhat in defining efficient market outcomes, there is general agreement that the concept is manifested by lower consumer prices, higher quality products and better product choice."

This principle is stated in the June 1994 OECD Interim Report on Convergence of Competition Policies[1]. The Report notes further that the competition laws of some countries encompass other objectives as well[2], but it is clear that the efficiency goal is central to competition enforcement in virtually all Member countries. One would expect, therefore, that this important objective would be translated into the rules by which competition policy is implemented in Member countries, including those rules that apply to mergers and other agreements between firms. This is indeed the case, but in surprisingly few situations involving mergers has an enforcement decision explicitly turned on the efficiency-enhancing attributes of the transaction in question. This Note will describe the outlines of the efficiency defence as commonly employed in merger matters and explore some practical aspects of applying it to specific cases, which in turn may help to explain why the defence is invoked relatively infrequently. The Note then briefly examines the treatment of efficiencies in situations involving horizontal nonmerger agreements.

The Efficiency Defence in Mergers

In most competition enforcement regimes it is recognised that a merger that may have significant anticompetitive effects should nevertheless be permitted if it also would result in improvements in efficiency that are greater than the anticompetitive effects of the transaction. That concept is articulated in, among other places, the EC Merger Regulation[3], the U.S. Horizontal Merger Guidelines[4] and the Canadian Competition Act[5]. There are certain elements of the defence that are common to most countries, although within each element there may be significant variations among countries.

Efficiencies as a Defence

In practice, efficiencies are usually relevant in merger analysis only when there is concern that the transaction is otherwise anticompetitive. Competition agencies typically conduct a straightforward analysis of competitive effects of a merger, and if anticompetitive effects are judged to be non-existent or small, there is no need to go further; the merger is approved. Only if competitive concerns are present are efficiencies evaluated as a possible offset to the anticompetitive effects, and the burden of establishing the existence and magnitude of the efficiencies usually falls upon the parties to the merger.

There are at least two reasons for this two-step approach. First, it is considered quite difficult to identify and quantify efficiencies prospectively. Competition agencies will not undertake the task unless it is necessary. Second, it is obvious that the parties to the merger, and not the competition authority, have the better access to the facts relevant to an efficiencies claim. Thus, the burden of going forward with evidence of efficiencies, if not the ultimate burden of proof, lies with the parties.

Types of Efficiencies Cognizable Under the Defence

There is general agreement that "production efficiencies", or cost savings that "permit firms to produce more output or better quality output from the same amount of input"[6] are cognizable under the defence. They include savings resulting from achieving economies of scale or scope, reduction in transportation costs, rationalisation of product mix among plants or transfer of superior production techniques, as well as savings in nonmanufacturing activities, such as distribution and research. Less well recognised under the defence are "dynamic efficiencies", such as improvements in product quality, product mix or service quality. Dynamic efficiencies benefit consumers no less than productive efficiencies, but they are inherently more difficult to measure, making their use more problematic in the trade-off analysis implicit in the defence.[7] Finally, "pecuniary" savings, such as tax savings or lower input costs resulting from improved bargaining power against suppliers, which are not considered real savings in resources, are even less favoured.[8]

Debate continues over whether broader social or industrial policy goals are properly considered as counterweights to anticompetitive effects of a merger. If economic efficiency is indeed the sole objective of competition policy, such "non-efficiency" goals are not relevant. As noted above, however, in some countries competition policy does have other objectives. The debate might then centre on the means by which those objectives can most efficiently be satisfied, whether through competition enforcement or other mechanisms, such as tax or welfare systems.[9]

The Trade-off of Efficiency Gains and Anticompetitive Effects

The trade-off of expected efficiencies against expected anticompetitive effects is universally recognised as difficult. Scholars have suggested elegant and objective methods of doing so, but there are significant difficulties in applying them.

A widely recognised model developed by Oliver Williamson[10] would permit a merger that on balance increases "total surplus", notwithstanding an increase in prices above the competitive level. That is, the cost savings resulting from efficiency gains generated by the merger must exceed the "dead-weight loss"[11] caused by the expected anticompetitive price increase. The size of the dead-weight loss is a function of the elasticity of demand for the relevant product and the anticipated price increase. Because those values cannot be precisely known, the model typically requires calculations over a range of possibilities. Nevertheless, the simple model suggests that in many cases a relatively modest gain in economies of five per cent or less would be sufficient to offset a price increase of ten or 20 percent.[12] An important aspect of the total surplus approach is that it ignores the fact that the anticompetitive price increase would cause a wealth transfer from consumers to producers, notwithstanding that total surplus will increase.[13]

An alternative to the total surplus standard is the "consumer surplus" standard, which requires that the efficiency gains be so substantial as to ensure that the merger will not result in a wealth transfer from consumers to producers. In other words, after the merger the producers will not increase prices above the premerger price, because the new efficiencies are so large as to cause their profit-maximising price to be no higher than the premerger price.[14] This standard ordinarily would require a showing of a much greater magnitude of efficiencies than the total surplus standard, and has been criticised by economists.[15] Nevertheless, the consumer surplus standard is employed in some countries. The language of the EC merger regulation indicates that consumer surplus is the operative standard there,[16] as it was in the U.S. at least prior to the 1992 U.S. Horizontal Merger Guidelines.[17] In Canada, total surplus is apparently the relevant standard.[18]

A third, or possibly complimentary, standard is one of "total welfare", in which efficiency gains from the merger that would occur in markets other than the relevant market for competition analysis are

included in the trade-off analysis.[19] The Canadian Merger Enforcement Guidelines explicitly recognise such efficiencies, to the extent that an order prohibiting the anticompetitive part of a merger would also prevent the achievement of those gains.[20] The policies of other countries are less clear in this regard.

The Absence of a Less Anticompetitive Alternative

Because the defence will operate to permit a merger that is anticompetitive, most countries require the parties to show that there are not less anticompetitive means of achieving the efficiencies. Such means could include internal expansion by one or both of the parties, other mergers that would be less anticompetitive, or interfirm contractual arrangements that fall short of complete merger.[21]

There has been some debate over the evidentiary burden that the parties should face on this issue. Must they show that absent the merger the efficiencies "could not" be achieved, that they "could not reasonably" be achieved,[22] or that they "would not likely" be achieved?[23] In practice the variance in such literal formulations may make little difference. There appears to be general agreement that the parties should not have to justify excluding every possible alternative, however remote. In particular, possible interfirm contractual arrangements should be closely scrutinised. There may be significant practical obstacles to successful, partial co-ordination between firms that are otherwise rivals. The best evidence of the feasibility of such arrangements would seem to be current industry practice in the same or similar situations.

Actual Experience With the Defence in Mergers

There appear to have been very few cases in which the efficiencies defence was given by a competition agency or court as the basis for a decision to approve a merger. There may be several reasons for this phenomenon.

The burden on the parties is indeed a difficult one. They must be prepared to articulate in detail the nature and size of the expected efficiencies, and to bear the burden of proving that achieving the efficiencies is probable and not reasonably attainable by less anticompetitive means. More often than not, parties to a merger do not reach such a detailed level of analysis in advance of their agreement, if only because it is risky to exchange during negotiations the amount of proprietary information necessary to such calculations. They are left with having to generate their efficiencies study in the course of the review by the competition agency, a situation that the authorities view with scepticism, often rightly so.

The defence is applicable only in the case of an anticompetitive merger. Parties are understandably reluctant to admit that their merger is anticompetitive and to base their entire defence on efficiencies. Thus, when they make an efficiencies defence it is in combination with a defence on competitive effects. Moreover, an efficiencies defence can be inconsistent with a competition argument, particularly one involving ease of entry. It is difficult to argue, on the one hand, that entry into the relevant market is easy, and on the other, that the claimed efficiencies cannot be achieved by internal expansion or an alternative merger.

From the perspective of the competition agency, the trade-off analysis is difficult and imprecise. Regardless of the standard that the agency employs, if indeed any is articulated, the agency will require that the demonstrated efficiencies be substantial. Practically, the efficiencies will have to comfortably exceed the agency’s estimates of the merger’s anticompetitive effects.

The paucity of decisions approving mergers on efficiency grounds does not necessarily mean that significant numbers of such beneficial mergers are being prevented, however. First, it is widely recognised that the concentration safe harbours employed by most competition authorities encompass many

efficiency-enhancing mergers. Second, many mergers that fall outside concentration safe harbours -- probably a substantial majority -- are ultimately adjudged not to be anticompetitive and are approved without the need to consider their efficiency benefits. Third, in situations where a merger is anticompetitive in one or more markets, competition agencies are increasingly willing to employ innovative forms of relief, such as partial divestiture or technology licensing, that permit the underlying transaction to go forward, thereby achieving most or all of the efficiency gains.

Finally, it is probably the case that efficiencies are an undisclosed factor, if not necessarily the deciding one, in some agency decisions approving mergers. Competition agencies are understandably reluctant to acknowledge that fact publicly, however, given the practical difficulties in applying the defence outlined above. In this regard the agencies face a challenge in providing sufficient information about their standards to the business community so that efficiency-enhancing mergers will not be unnecessarily discouraged.

Efficiencies in Horizontal Nonmerger Agreements

There is a broad range of arrangements short of merger undertaken by competitors that may be efficiency-enhancing. They include information exchanges of various types, joint production ventures, joint ventures by service providers, joint research and development ventures, joint purchasing arrangements, joint advertising arrangements, standards setting arrangements, agreements on ethical standards, specialisation agreements and technology licensing agreements. It is beyond the scope of this roundtable discussion to examine in detail how these several types of arrangements are analysed,[24] but in all cases the efficiency benefits of the particular agreement are relevant and important.

There is some difference in the way competition laws apply to what is considered traditional cartel conduct, such as price fixing, bid rigging and customer or market allocation. In the United States, a "naked" agreement to raise price or restrict output that is unrelated to any economic integration of the parties' activities is *per se* unlawful. Whether the agreement is actually harmful, or by some standard beneficial, is irrelevant. In most other countries such agreements are not *per se* unlawful; they could be permitted or granted an exemption upon a showing of some benefit as provided in the relevant law, including the generation of efficiencies. In practice such differences may be more apparent than real, however. A cartel agreement that is truly "naked", having no object or effect other than eliminating competition, is likely to be condemned whether or not it is *per se* illegal.

With respect to agreements that are not *per se* illegal, in theory there would seem to be no difference in the way efficiencies should be considered as between mergers and nonmerger agreements. In both cases the transaction should first be analysed for possible anticompetitive effects. This analysis would be done in the same way -- by defining the relevant market or markets, analysing the structure thereof and the effect of the agreement on the structure (assuming in nonmerger agreements total co-ordination between the parties for the purpose of applying the market share screen), and if the transaction falls outside the market share safe harbours, inquiring further into possible competitive effects. If the transaction is adjudged to be significantly anticompetitive, expected efficiency gains would be evaluated and compared to the anticipated anticompetitive effects.[25]

In practice, however, there do appear to be differences in the analysis of efficiencies as between the two types of transactions. Often in nonmerger agreements the parties have articulated the expected efficiencies in significant detail. The agreement is structured to achieve certain specific, allegedly procompetitive ends, which are likely to be featured prominently in presentations to the competition agency. The traditional two-step, trade-off analysis is likely to be blurred, as efficiency considerations are given prominence from the beginning. Further, some of the benefits common to nonmerger agreements, such as the creation of a new product or service or co-operation on a specific research and development project,

are a form of dynamic efficiency and are inherently difficult to quantify. A precise trade-off analysis, unlikely in most mergers as noted above, is even more improbable in this situation.

Finally, as noted above in connection with mergers, it may be appropriate to consider efficiencies generated in one market against anticompetitive effects of the transaction in another. The same could be true in nonmerger agreements, but in a slightly different sense. In a nonmerger agreement the co-operation is targeted toward benefits in a specific market or markets, but such co-operation could have "spillover" anticompetitive effects in other markets in which the parties are competitors. A joint purchasing arrangement, for example, could lower the costs of the participating firms in the input market, but facilitate collusion in the output market. The competitive analysis of such nonmerger agreements should always include the possibility of such spillover effects. In those countries in which a total welfare standard is employed, the efficiency gains in the target market would be weighed against the spillover effects in other markets.

NOTES

1. OECD/GD(94)64, at Annex, Areas of Convergence in Competition Policy and Law para. 4.

2. "There are a number of other broader objectives such as pluralism, decentralisation of decision-making, promoting small business, achieving greater fairness in market-place transactions, promoting the ability to compete in international markets and similar objectives frequently encompassed by notions of public or general interest which are present in the statutes of some, but not all, countries. Another important goal is opening up markets which are in some way sheltered from competition. These supplementary objectives may sometimes conflict with the efficiency objective. At the same time, they are often important to securing broad-based political support for the establishment of modern competition laws and institutions or for the reform of existing laws and institutions." *Id.* at para. 5.

3. Regulation No. 4064/89, Art. 2.

4. At Section 4.

5. At Section 96.

6. Canada, Merger Enforcement Guidelines, Appendix 2. See also, KWOKA, WARREN-BOULTON, "Efficiencies, Failing Firms, and Alternatives to Merger: A Policy Syntheses", *Antitrust Bulletin*, Summer 1986, 431-50.

7. The Canadian Merger Enforcement Guidelines recognise dynamic efficiencies, but they note the difficulty in measuring them (Guidelines, Appendix 2). The U.S. Horizontal Merger Guidelines do not explicitly mention dynamic efficiencies, but they note that the agencies will consider efficiencies that "do not relate to specific manufacturing, servicing, or distribution operations of the merging firms, although, as a practical matter, these types of efficiencies may be difficult to demonstrate." (Guidelines, Section 4.)

8. Canada, Competition Act, section 96(3); KWOKA, WARREN-BOULTON, *supra*.

9. See, e.g., PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", 81 *Georgetown L.J.* 195 (1992). Note, for example, that the 13th Recital of the EC Merger Regulation states that the Commission must evaluate concentrations as compatible or not with the common market in the context of the fundamental objectives stated in the EC Treaty,

including "that of strengthening the Community's economic and social cohesion...." See, WHISH, *Competition Law*, 719 (3rd ed. 1993).

10. See, Oliver E. WILLIAMSON, "Economies As An Antitrust Revisited", 125 *U. PA. L. REV.* 699 (1977).

11. After the price increase consumers collectively purchase less of the product and pay more for what they do purchase. To the extent these losses to consumers do not translate into higher profits for producers, they are a net loss to society, or "dead-weight" losses.

12. Williamson called his model "naive" because it included certain assumptions that are not found in most markets, including, for example, perfect competition premerger and achievement of the efficiency gains postmerger across the entire market and as quickly as the institution of the price increase. Giving weight to these additional factors would, on balance, increase the required cost savings. See, CRAMPTON, "Alternative Approaches to Competition Law: Consumers' Surplus, Total Surplus, Total Welfare and Non-Efficiency Goals", 17 *World Competition*, no. 3, 56 (March 1994).

13. Mergers involving multinational companies present interesting and unique issues relating to the total surplus standard. One or both of the merging companies may be foreign-owned. Under the total surplus standard the wealth transfer from consumers to producers is ordinarily ignored, but to the extent that the wealth transfer is received by the foreign owners, a competition agency charged with protecting domestic consumers may require that the cost savings be correspondingly larger, sufficient to offset both the dead-weight loss and the wealth transfer enjoyed by the foreign owners. Alternatively, some or all of the production that will benefit from the efficiencies may be located abroad, in which case the initial benefits of the efficiency gains (the freeing of assets for other productive uses) will be enjoyed abroad. The domestic competition agency could decide not to count these savings against the dead-weight loss.

14. See, STOCKUM, "The Efficiencies Defense for Horizontal Mergers: What is the Government's Standard?", 61 *Antitrust Law Journal* 829, 842-44.

15. See, CRAMPTON, *supra*; STOCKUM, *supra*.

16. "[T]he Commission shall take into account . . . the interests of the intermediate and ultimate consumers, and the development of technical and economic progress provided that it is to consumers' advantage. . . ." Regulation No. 4064/89, Art. 2, para. 1.

17. See, PITOFSKY, *supra* at 207-08. The 1992 Guidelines are silent on the issue.

18. See, CRAMPTON, "Canada's New Merger Enforcement Guidelines, a 'Nuts and Bolts' Review", 36 *Antitrust Bulletin* (1991).

19. Issues relating to mergers of multinational firms similar to those discussed above in fn. 13 could also arise under this standard.

20. Canada, Merger Enforcement Guidelines, 5.2.

21. See, KWOKA, WARREN-BOULTON, *supra*.

22. United States, Horizontal Merger Guidelines, sec. 4.

23. Canada, Competition Act, sec. 96(1).

24. The Committee considered several of these types of agreements in its roundtable discussion on horizontal agreements on 7 December 1993.

25. In fact, the same analysis would be applicable to vertical agreements as well, although the competitive effects analysis would differ according to the type of agreement.

NOTE DE RÉFÉRENCE

(par le SECRÉTARIAT)

L'argument de l'efficience dans les fusions et accords horizontaux

"Il est généralement admis que l'objectif fondamental de la politique de la concurrence est de maintenir et de favoriser le processus de concurrence afin d'assurer une utilisation efficiente des ressources. Bien qu'il existe entre les pays certaines divergences quant aux caractéristiques d'un marché efficient, on s'accorde à reconnaître que l'efficience d'un marché se traduit par des prix moins élevés à la consommation, l'amélioration de la qualité des produits et un plus large éventail de choix."

Ce principe est énoncé dans le Rapport intérimaire de l'OCDE sur la convergence des politiques de la concurrence, de juin 1994[1]. Le rapport note en outre que les règles de concurrence de certains pays visent aussi d'autres objectifs[2], mais que l'objectif d'efficience joue manifestement un rôle central dans la politique de concurrence de la quasi-totalité des pays Membres. On peut donc penser que cet objectif important se reflète dans les règles qui régissent la mise en oeuvre de la politique de concurrence dans les pays Membres, y compris celles qui s'appliquent aux fusions et autres accords entre entreprises. C'est effectivement le cas, mais il est surprenant de constater que très rares sont les fusions dans lesquelles la décision s'est expressément appuyée sur les caractéristiques présentées par l'opération considérée sur le plan de l'efficience. La présente note décrira de quelle manière l'argument de l'efficience est généralement utilisé dans le contexte des fusions et analysera certains aspects pratiques de son application à des cas particuliers, ce qui contribuera sans doute à expliquer pourquoi il est assez peu souvent invoqué. Enfin, elle examinera brièvement la question de l'efficience dans le contexte d'accords horizontaux sans fusion.

L'argument de l'efficience dans les fusions

Dans la plupart des régimes de concurrence, il est admis qu'une fusion qui risque d'avoir des effets anticoncurrentiels importants doit néanmoins être autorisée si elle se traduit par une amélioration plus importante encore de l'efficience. Cette notion est énoncée, notamment, dans le droit communautaire du contrôle des concentrations[3], les "Horizontal Merger Guidelines" des États-Unis[4] et la loi canadienne sur la concurrence[5]. Certains éléments des arguments avancés sont communs à la plupart des pays, mais on observe des différences importantes, suivant les pays, à l'intérieur de chacun de ces éléments.

L'efficience en tant qu'argument

Dans la pratique, on ne s'intéresse généralement à l'efficience, dans l'analyse d'une fusion, que si l'on craint que cette opération ait par ailleurs des effets anticoncurrentiels. Les organismes chargés de la politique de la concurrence procèdent généralement à une simple analyse des effets anticoncurrentiels d'une fusion, et s'ils estiment que ces effets sont négligeables, l'analyse n'est pas poussée plus loin, la fusion est approuvée. Il faut que des problèmes de concurrence se posent pour que l'on évalue les avantages sur le plan de l'efficience susceptibles de compenser les effets anticoncurrentiels, et c'est en principe aux entreprises qui fusionnent qu'il appartient de démontrer l'existence et l'importance des gains d'efficience attendus de la fusion.

Cette approche en deux temps s'explique par deux raisons au moins. Premièrement, on estime qu'il est assez difficile d'identifier et de chiffrer à l'avance les gains d'efficience. Les organismes chargés

de la concurrence ne veulent donc pas se charger de cette tâche si ce n'est pas indispensable. Deuxièmement, il est manifeste que ce sont les entreprises qui fusionnent, et non les autorités responsables de la concurrence, qui ont le meilleur accès aux informations de nature à justifier l'argument de l'efficience. Par conséquent, c'est à elle qu'il appartient de démontrer les gains d'efficience, voire que la charge de la preuve peut incomber.

Catégories de gains d'efficience pouvant être invoqués

Il est généralement admis que les "gains de productivité" ou les économies qui "permettent aux entreprises de produire davantage d'extrants ou des extrants de meilleure qualité avec la même quantité d'intrants"[6] peuvent être invoqués. Il peut s'agir des économies financières réalisées grâce à des économies d'échelle ou de gamme, une réduction des coûts de transport, une rationalisation des gammes de produits entre les installations ou un transfert de méthodes de production plus performantes, ainsi que des économies provenant d'activités non productives, telles que la distribution et la recherche. En revanche, il semble plus difficile d'invoquer le critère d'"efficience dynamique", résultant par exemple de l'amélioration de la qualité du produit, de sa composition ou de la qualité d'un service. L'efficience dynamique est tout aussi intéressante, pour le consommateur, que l'efficience de production, mais elle est intrinsèquement plus difficile à mesurer, si bien qu'il est moins facile d'en faire état dans une analyse[7]. Enfin, les économies "pécuniaires" telles que les économies d'impôt ou les réductions du coût des intrants résultant d'une amélioration du pouvoir de négociation vis-à-vis des fournisseurs, qui ne sont pas considérées comme de véritables économies de ressources, semblent encore plus difficilement invocables[8].

On continue de s'interroger sur la question de savoir s'il est justifié de tenir compte d'objectifs généraux relevant de la politique sociale ou de la politique industrielle pour compenser les effets anticoncurrentiels d'une fusion. Si l'on considère que l'efficience économique est le seul objectif de la politique de concurrence, de tels objectifs sans rapport avec l'efficience n'ont pas leur place dans ce contexte. Ainsi qu'on l'a noté plus haut, cependant, la politique de concurrence a, dans certains pays, d'autres objectifs. On peut donc s'interroger sur les moyens de satisfaire ces objectifs de la façon la plus efficiente possible, par l'application de règles de concurrence ou au moyen d'autres mécanismes, tels que les régimes fiscaux ou de protection sociale[9].

L'arbitrage entre gains d'efficience et effets anticoncurrentiels

L'arbitrage entre les gains d'efficience escomptés et les effets anticoncurrentiels prévisibles est universellement considéré comme difficile. Certains universitaires ont proposé des méthodes élégantes et objectives pour y parvenir, mais leur application pratique soulève de sérieuses difficultés.

D'après un modèle largement accepté, mis au point par Oliver Williamson[10], on devrait permettre les fusions qui, globalement, accroissent le "surplus total", malgré une augmentation des prix au-delà de leur niveau concurrentiel. En d'autres termes, l'économie résultant des gains d'efficience engendrés par la fusion doit être supérieure à la "perte sèche"[11] causée par l'augmentation anticoncurrentielle prévisible des prix. L'importance de cette perte sèche est fonction de l'élasticité de la demande du produit considéré et de l'augmentation de prix anticipée. Etant donné que ces valeurs ne peuvent pas être connues précisément, le modèle implique généralement l'adoption d'une série d'hypothèses. Néanmoins, ce simple modèle donne à penser que dans nombre de cas une économie relativement modérée de cinq pour cent ou moins suffirait à compenser une augmentation de prix de dix ou 20 pour cent[12].

L'un des aspects importants de cette approche est qu'elle ne tient pas compte du fait que l'augmentation anticoncurrentielle des prix provoquerait un transfert de richesse entre les consommateurs et les producteurs, nonobstant l'augmentation du surplus total[13].

Une autre méthode consiste à utiliser, au lieu du surplus total, le "surplus du consommateur", ce qui signifie que les gains d'efficience doivent être suffisants pour garantir que la fusion ne se traduira pas par un transfert de richesse entre les consommateurs et les producteurs. En d'autres termes, après la fusion, les producteurs ne devront pas augmenter leurs prix par rapport aux prix observés avant la fusion, car les gains d'efficience devront être suffisamment importants pour que les prix leur permettant de maximiser leurs profits ne soient pas plus élevés que les prix observés précédemment[14]. Suivant ce principe, il faut généralement que les gains d'efficience soient beaucoup plus substantiels que dans l'hypothèse du surplus total, et c'est là un point qui a été critiqué par un certain nombre d'économistes[15]. Néanmoins, le critère du surplus du consommateur est employé dans certains pays. Les termes du règlement communautaire sur les concentrations indiquent que c'est effectivement ce critère qui est retenu[16], comme cela était le cas dans la législation américaine, au moins avant l'adoption des Directives de 1992[17]. Au Canada, c'est le surplus total qui est apparemment l'élément d'appréciation[18].

Un troisième critère, éventuellement complémentaire, est celui du "bien-être total", dans lequel l'arbitrage tient compte des gains d'efficience provoqués par la fusion dans d'autres marchés que celui sur lequel porte l'analyse de concurrence[19]. Les lignes directrices canadiennes sur les fusionnements reconnaissent expressément l'existence de tels gains d'efficience, dans la mesure où une décision interdisant les effets anticoncurrentiels d'une fusion exclurait également la réalisation de ces gains[20].

L'absence de solutions de rechange moins anticoncurrentielles

Etant donné que l'argument de l'efficience vise à faire autoriser une fusion qui est anticoncurrentielle, la plupart des pays demandent aux parties à la fusion de démontrer qu'il n'existe pas de moyens moins anticoncurrentiels de réaliser les gains d'efficience. Il peut s'agir, par exemple, de l'expansion interne de l'une des entreprises ou des deux entreprises parties à la fusion, d'autres fusions qui seraient moins anticoncurrentielles, ou encore d'arrangements contractuels entre entreprises n'allant pas jusqu'à la fusion complète[21].

La nature des preuves que les parties doivent présenter est difficile à déterminer. Doivent-elles prouver qu'en l'absence de fusion, les gains d'efficience ne "pourraient pas" être réalisés, qu'ils ne "pourraient pas raisonnablement" être réalisés[22], ou qu'ils ne "seraient vraisemblablement pas" réalisés[23] ? Les divergences qui existent dans ces formulations n'ont sans doute pas beaucoup d'importance dans la pratique. On semble généralement s'accorder à reconnaître que les parties ne devraient pas avoir à justifier l'exclusion de toutes les possibilités envisageables, aussi éloignées qu'elles soient. En particulier, d'éventuels arrangements contractuels entre entreprises devraient être examinés de près. Il peut y avoir d'importants obstacles pratiques à une coordination efficace et partielle entre des entreprises qui sont par ailleurs rivales. La meilleure preuve de la faisabilité de tels arrangements serait sans doute à rechercher dans les pratiques actuelles des entreprises dans des conditions identiques ou similaires.

Situations dans lesquelles l'argument de l'efficience a effectivement été invoqué

Il semble qu'il y ait très peu de cas dans lesquels l'argument de l'efficience a été avancé par un organisme chargé de faire respecter la concurrence ou par un tribunal pour justifier sa décision d'approuver une fusion. Cela tient sans doute à un certain nombre de raisons.

Cela représente en effet une lourde tâche pour les parties à la fusion. Elles doivent être prêtes à décrire en détail la nature et l'importance des gains d'efficience escomptés et à prouver que la réalisation des gains d'efficience est probable, mais que des moyens moins anticoncurrentiels ne permettraient pas raisonnablement de les réaliser. Dans bien des cas, les parties à une fusion ne procèdent pas à des analyses aussi détaillées avant de conclure leur accord, ne serait-ce que parce qu'il serait risqué d'échanger pendant les négociations toutes les informations confidentielles nécessaires. Elles doivent donc étudier les gains

d'efficience escomptés une fois que leur cas est soumis à l'organisme responsable de la concurrence, situation que les autorités considèrent avec scepticisme, souvent à juste titre.

L'argument de l'efficience ne peut être invoqué qu'en cas de fusion anticoncurrentielle. On comprendra que les parties à la fusion hésitent à admettre que celle-ci est anticoncurrentielle et à fonder toutes leur défense sur les gains d'efficience escomptés. Ainsi, en même temps qu'elles invoqueront l'argument de l'efficience, elles tenteront de se défendre sur les aspects concurrentiels de la fusion. Qui plus est, l'argument de l'efficience et les aspects concurrentiels peuvent être contradictoires, en particulier en ce qui concerne la facilité d'accès au marché. Il est difficile de dire, d'une part, que l'accès au marché considéré est facile et, de l'autre, que les gains d'efficience escomptés ne peuvent pas être réalisés par une expansion interne ou une autre fusion.

Du point de vue de l'organisme responsable de la concurrence, l'arbitrage est difficile et imprécis. Quel que soit le critère éventuellement retenu par cet organisme, les entreprises devront démontrer que les gains d'efficience attendus sont substantiels. Dans la pratique, ceux-ci devront nettement l'emporter sur les effets anticoncurrentiels de la fusion tels qu'ils sont estimés par l'organisme.

La rareté des décisions d'approuver des fusions sur la base de l'argument de l'efficience ne signifie pas nécessairement qu'un grand nombre de fusions de ce type sont interdites, cependant. Premièrement, il est largement admis que les dérogations aux règles de concentration consenties par la plupart des autorités chargées de la concurrence recouvrent beaucoup de fusions de nature à améliorer l'efficience. Deuxièmement, bon nombre des fusions qui ne sont pas visées par ces dérogations (une assez forte majorité d'entre elles, probablement) sont finalement considérées comme n'étant pas anticoncurrentielles et sont approuvées sans qu'il soit nécessaire de déterminer quels avantages elles présentent sur le plan de l'efficience. Troisièmement, lorsqu'une fusion est anticoncurrentielle sur un ou plusieurs marchés, les organismes chargés de la concurrence ont de plus en plus tendance à recourir à des formes novatrices d'arrangements, tels qu'un désengagement partiel ou l'octroi de licences sur des technologies, qui permettent à la transaction de s'effectuer, et par là même à la quasi-totalité des gains d'efficience de se réaliser.

Enfin, il est probable que les gains d'efficience sont un facteur qui entre officieusement en ligne de compte, même s'il n'est pas nécessairement décisif, dans certaines approbations de fusions par des organismes chargés de la concurrence. Cependant, ces organismes sont évidemment peu enclins à reconnaître ce fait publiquement, étant donné les difficultés pratiques que pose le recours à l'argument de l'efficience, comme on l'a vu plus haut. De ce point de vue, les organismes publics sont confrontés à la nécessité de fournir suffisamment d'informations sur leurs critères aux entreprises afin d'éviter que les fusions propres à accroître l'efficience soient inutilement découragées.

L'efficience dans les accords horizontaux autres que des fusions

Il existe toute une gamme d'accords qui, sans être des fusions entre concurrents, peuvent avoir pour effet d'améliorer l'efficience. Il s'agit par exemple des échanges d'informations de divers types, des co-entreprises de production, des co-entreprises entre prestataires de services, des co-entreprises de recherche-développement, des accords en matière d'achats, des accords de publicité, des accords de normalisation, des accords de déontologie, des accords de spécialisation et des accords de licences technologiques. Un examen détaillé des méthodes d'analyse de ces différents types d'arrangements sortirait du cadre du présent débat[24], mais dans tous les cas les avantages offerts par chaque type d'accord sur le plan de l'efficience sont intéressants et importants.

Les règles de concurrence s'appliquent différemment à ce qu'on considère comme des ententes traditionnelles, telles que la fixation des prix, les soumissions concertées et la répartition de la clientèle ou du marché. Aux États-Unis, tout accord visant expressément à majorer les prix ou restreindre la production,

sans rapport avec une intégration économique des activités des parties en cause, est illégal. Que cet accord soit effectivement néfaste, ou qu'il soit au contraire avantageux à certains égards n'entre pas en ligne de compte. Dans la plupart des autres pays, de tels accords ne sont pas illégaux en tant que tels ; ils peuvent être autorisés ou faire l'objet d'une dérogation s'il est prouvé qu'ils offrent certains avantages spécifiques, y compris des gains d'efficience. Dans la pratique, cependant, la différence est parfois plus apparente que réelle. Une entente qui vise uniquement à éliminer la concurrence, sans autre objet ni effet, sera sans doute condamnée, qu'elle soit ou non illégale.

S'agissant des accords qui ne sont pas illégaux, il ne devrait pas y avoir théoriquement de différence dans la manière de traiter les gains d'efficience suivant qu'il s'agit de fusions ou d'autres catégories d'accords. Dans les deux cas, la transaction devrait tout d'abord être analysée afin de déceler d'éventuels effets anticoncurrentiels. Cette analyse serait faite de la même manière, c'est-à-dire en définissant le ou les marchés concernés, en analysant la structure de ces marchés et les effets de l'accord sur cette structure (en supposant, dans les accords autres que les fusions, une coordination totale entre les parties pour la répartition du marché) et, si la transaction n'entre pas dans le champ des dérogations possibles, en poussant plus loin l'analyse d'éventuels effets anticoncurrentiels. Si la transaction est jugée nettement anticoncurrentielle, les gains d'efficience escomptés devront être évalués et comparés aux effets anticoncurrentiels prévisibles[25].

Dans la pratique, cependant, les gains d'efficience ne sont pas analysés de la même manière suivant qu'il s'agit de l'une ou de l'autre catégorie de transaction. Souvent, dans les accords autres que les fusions, les parties en présence ont déjà analysé les gains d'efficience escomptés de façon relativement détaillée. L'accord est structuré de manière à atteindre certains objectifs spécifiques, censés promouvoir la concurrence, qui seront probablement au centre des communications présentées à l'organisme chargé de la concurrence. L'analyse traditionnelle en deux étapes sera donc probablement faussée, étant donné que l'argument de l'efficience sera invoqué dès le départ. En outre, certains des avantages communs aux accords autres que les fusions, tels que la création d'un nouveau produit ou service ou la coopération a un projet spécifique de recherche-développement, sont une forme de gain d'efficience dynamique et sont intrinsèquement difficiles à mesurer. Une analyse précise des inconvénients et avantages du projet, déjà peu probable dans la plupart des cas de fusions, comme on l'a vu plus haut, sera donc encore plus improbable dans ce cas.

Enfin, ainsi qu'on l'a noté plus haut en ce qui concerne les fusions, il peut y avoir intérêt à prendre en compte les gains d'efficience engendrés sur un marché en contrepartie des effets anticoncurrentiels de la transaction sur un autre marché. Il en va de même pour les accords autres que les fusions, mais la situation est quelque peu différente. Dans ce cas, la coopération vise à dégager des avantages sur un ou des marchés spécifiques, mais cette coopération peut avoir des "retombées" anticoncurrentielles sur d'autres marchés où les parties à ces accords sont concurrentes. Un accord d'achat en commun, par exemple, peut avoir pour effet d'abaisser les coûts des entreprises participantes sur le marché d'approvisionnement, mais faciliter la collusion sur le marché de production. L'analyse concurrentielle de tels accords devrait toujours tenir compte de la possibilité de telles retombées. Dans les pays où c'est le critère du bien-être total qui est retenu, les gains d'efficience sur le marché concerné devraient être mis en balance avec les retombées anticoncurrentielles sur les autres marchés.

NOTES

1. OCDE/GD(94)64, Annexe, Domaines de convergence dans la politique et le droit de la concurrence, para. 4.

2. "Il existe un grand nombre d'objectifs socio-politiques plus larges tels que le pluralisme, la décentralisation des décisions, l'encouragement aux petites entreprises, les mesures assurant l'équité des transactions, le développement de la compétitivité internationale et autres principes analogues englobés souvent dans les notions d'intérêt général ou d'intérêt public, qui figurent dans les législations de certains pays. Ces objectifs supplémentaires peuvent quelquefois entrer en conflit avec celui d'efficience. Pourtant, ils sont souvent essentiels si l'on veut obtenir un vaste soutien politique à la mise en oeuvre de lois et d'institutions modernes en matière de concurrence ou à la réforme des lois et institutions existantes." *Id*., para. 5.

3. Règlement N° 4064/89, Art. 2.

4. Art. 4.

5. Art. 96.

6. Canada, "Fusionnements, Lignes directrices pour l'application de la loi", Annexe 2. Voir également, KWOKA, WARREN-BOULTON, "Efficiencies, Failing Firms, and Alternatives to Merger : A Policy Synthesis", *Antitrust Bulletin*, été 1986, 431-50.

7. Les Lignes directrices canadiennes sur les fusionnements reconnaissent l'existence de gains en efficience dynamiques, mais elles précisent qu'il est difficile de les évaluer (Lignes directrices, Annexe 2). Les Directives américaines sur les fusions horizontales ne mentionnent pas expressément l'efficience dynamique, mais elles notent que les organismes devront tenir compte des gains d'efficience qui "ne sont pas liés à des opérations spécifiques de production, d'entretien ou de distribution des entreprises qui fusionnent, bien que, dans la pratique, ce type d'efficience soit sans doute difficile à démontrer" (Guidelines, article 4).

8. Canada, Loi sur la concurrence, article 96 (3) ; KWOKA, WARREN-BOULTON, *supra*.

9. Voir, par exemple, PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", 81 *Georgetown L. J.* 195 (1992). On notera par exemple que le 13ème considérant du Règlement communautaire sur les concentrations stipule que la Commission doit déterminer si les concentrations sont ou non compatibles avec le marché commun à la lumière des objectifs fondamentaux énoncés dans le Traité instituant la Communauté économique européenne, y compris celui du "renforcement de la cohésion économique et sociale de la Communauté...". Voir WHISH, *Competition Law*, 719 (3rd ed. 1993).

10. Voir Oliver E. WILLIAMSON, "Economies As An Antitrust Defense Revisited", 125 *U. PA. L. REV.* 699 (1977).

11. Une fois que les prix ont augmenté, les consommateurs achètent collectivement de moins grandes quantités du produit et paient davantage pour ce qu'ils achètent. Dans la mesure où ces pertes pour les consommateurs ne se traduisent pas par une augmentation des bénéfices des producteurs, elles constituent une perte nette ou "sèche" pour la collectivité.

12. Williamson qualifiait de "naïf" son modèle, parce qu'il comportait certaines hypothèses qui n'existent pas sur la plupart des marchés, dont par exemple une situation de concurrence parfaite avant la fusion et la réalisation de gains d'efficience après celle-ci sur l'ensemble du marché et aussi rapidement que les prix augmentent. Si l'on donnait plus de poids à ces facteurs additionnels, il faudrait globalement que les économies soient plus substantielles. Voir CRAMPTON, "Alternative Approaches to Competition Law : Consumers' Surplus, Total Surplus, Total Welfare and Non-Efficiency Goals", 17 *World Competition*, n° 3, 56 (mars 1994).

13. Les fusions faisant intervenir des entreprises multinationales soulèvent des questions intéressantes et particulières concernant le surplus total. L'une des entreprises considérées, ou les deux, peuvent appartenir à des intérêts étrangers. Normalement, le transfert de richesse entre les consommateurs et les producteurs n'est pas pris en compte dans le calcul du surplus total, mais dans la mesure où ce transfert bénéficie à des capitaux étrangers, l'organisme chargé de faire respecter la concurrence et de protéger les consommateurs dans l'autre pays peut exiger que l'économie soit plus importante, et qu'elle suffise à compenser à la fois la perte sèche et le transfert de richesse dont bénéficient les propriétaires étrangers. Ou alors, une partie ou la totalité de la production bénéficiant des gains d'efficience peut être localisée à l'étranger, auquel cas les avantages des gains d'efficience (libération d'actifs pour d'autres utilisations productives) se feront d'abord sentir à l'étranger. L'organisme chargé de la concurrence pourra alors décider de ne pas tenir compte de ces économies en contrepartie des pertes sèches.

14. Voir STOCKUM, "The Efficiencies Defense for Horizontal Mergers : What is the Government's Standard ?", 61 *Antitrust Law Journal* 829, 842-44.

15. Voir CRAMPTON, *supra* ; STOCKUM, *supra*.

16. "La Commission tient compte... des intérêts des consommateurs intermédiaires et finals ainsi que de l'évolution du progrès technique et économique pour autant que celle-ci soit à l'avantage des consommateurs..." Règlement N° 4064/89, art. 2, para. 1.

17. Voir PITOFSKY, *supra*, pp. 207-208. Les Directives de 1992 n'abordent pas cette question.

18. Voir CRAMPTON, "Canada's New Merger Enforcement Guidelines, a 'Nuts and Bolts' Review", 36 *Antitrust Bulletin* (1991).

19. Les questions concernant les fusions qui font intervenir des entreprises multinationales, évoquées dans la note 13 ci-dessus, pourraient aussi s'inscrire dans cette optique.

20. Canada, Lignes directrices sur les fusionnements, 5.2.

21. Voir KWOKA, WARREN-BOULTON, *supra*.

22. États-Unis, Horizontal Merger Guidelines, art. 4.

23. Canada, Loi sur la concurrence, art. 96(1).

24. Le Comité a examiné plusieurs de ces types d'accords lors de la réunion qu'il a eue le 7 décembre 1993 sur les accords horizontaux.

25. En fait, la même analyse pourrait être réalisée dans le cas des accords verticaux également, mais l'analyse des effets anticoncurrentiels sera différente suivant le type d'accord.

CONTRIBUTION FROM CANADA

Canada's Competition Act encompasses both criminal and civil provisions. The former are enforced by criminal courts; actions brought under the latter are reviewed by the Competition Tribunal, a body created specifically for that purpose, with a membership that combines economic and legal expertise. A number of elements of the Act potentially touch on horizontal agreements and mergers: first, conspiracy is dealt with as a criminal matter; secondly, there are civil sections that address abuse of dominance, specialisation agreements, mergers, and joint ventures.

The notion of 'efficiency' surfaces in these provisions, particularly in the civil provisions, in a variety of ways. By way of portmanteau, the purpose clause of the Act identifies efficiency prominently among other objectives. Beyond this, only the civil sections concerned with specialisation agreements and mergers speak explicitly of efficiency . However, the remaining sections too contain provisions that arguably embody specific aspects of efficiency.

Unfortunately for any discussion of these elements of the law, they have not been extensively litigated or reviewed before the courts and the Tribunal. The record before the Tribunal is particularly slim in light of the importance of the efficiency clauses for the civil portions of the Act. The treatment of efficiency in merger review offers something of an exception, and has been the subject of commentary by both the Tribunal and the Bureau of Competition Policy which bears primary responsibility for enforcement.

To begin with the criminal treatment of conspiracy, the Act groups in a list nine specific defences which could conceptually be viewed as embodying elements of efficiency. For example, one such defence is co-operation in R&D. However, it is made clear that such defences do not apply if the arrangement in question does indeed have anticompetitive effects. A separate defence for export consortia is similarly presented. Again, to be applicable there must be no domestic anticompetitive effects; the agreement must affect only exports. To date the courts have not considered a conspiracy case in which the defences and exceptions to defences have been argued.

Turning now to civil provisions of the Act, the treatment of specialisation agreements actually represents an exception to the criminal law on conspiracy. With mergers, this is one of two instances where the Act identifies efficiency, as such, as an issue. Specialisation agreements are defined as two or more parties' jointly rationalising production. Each partner agrees to discontinue producing an article. Such agreements may be presented to the Tribunal for registration and, if successful, the conspiracy section of the Act no longer applies. In deciding to register an agreement the Tribunal must conclude that the agreement is necessary for efficiencies that offset or exceed any lessening of competition that results -- that is, a trade-off. The Act goes on to specify that the Tribunal shall consider the impact on trade as a factor in assessing gains in efficiency, though it is not limited in this regard. As well, the Act states that efficiency must not be inferred only from a redistribution of income. As yet, no specialisation agreements have been presented to the Tribunal for registration. However the language dealing with efficiencies is essentially repeated for mergers which are discussed below.

Abuse of dominance is also subject to civil review by the Tribunal. Abuse is defined as anticompetitive activities practised by 'one or more persons' who substantively or completely control a class of business. However the Act requires that in establishing anticompetitiveness the Tribunal 'consider' whether the practice in question is the result of 'superior competitive performance'. As yet this rather vague provision has not been interpreted by the Tribunal.

There are two exceptions to merger review that are associated with efficiency considerations. The first is the exception granted to joint ventures. A joint venture is defined as a combination of two or

more parties which entails a commitment of assets and which undertakes a specific, time-limited project or a program of research and development. A joint venture may be anticompetitive so long as this is limited to what is necessary for the project to be effected, and the venture involves no change in control of any party. Efficiency is not explicitly at issue, but these requirements -- the manner in which the definition is framed -- suggest a trade-off between efficiency and competition. This too is a provision which has not yet been argued before the Tribunal, nor has the Bureau accepted joint-venture status for any arrangement brought to it by parties seeking advice under the Bureau's program of voluntary compliance.

The second exception -- in addition to joint ventures -- to the merger review process is explicitly directed to efficiencies. The wording in the Act repeats that used for specialisation agreements. Essentially, it calls for a trade-off between gains to efficiency and any lessening of competition where a merger is necessary for efficiency. Thus, the Act states:

> The Tribunal shall not make an order ... if it finds that the merger ... is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition ... and that the gains in efficiency would not likely be attained if the order were made.

Similar to specialisation agreements, the Act goes on to say that trade effects should be considered in assessing gains to efficiency, and that efficiency should not be inferred where only redistribution of income occurs.

The Bureau of Competition Policy has published merger enforcement guidelines (MEGs) which expand on a number of elements in this passage as follows:

-- the effects of any prevention or limiting of competition: Anticompetitive effects include deadweight or allocative losses associated with reduced production and higher prices. At least potentially, these can be quantified. Another element of anticompetitive effects consists of unquantifiable, or much less easily quantifiable, qualitative considerations like reduced quality, variety and innovation. Generally, anticompetitive effects both in the market directly at issue and in other markets within Canada are included, though other markets are unlikely to be a major issue. Transfers without consequence for resource allocation are excluded;

-- gains in efficiency: Efficiencies are limited to Canadian production, calculated on post-merger output, and they must be real, exclusive of transfers. Thus, savings in resources associated with such things as scale and transactions costs would qualify, but reductions in pecuniary costs due to increased bargaining power with suppliers or workers would not. Efficiencies may include those in other markets, where there is no anticompetitive impact, but only if they are inextricably linked to the market in question. There are two classes of potential efficiency: production and dynamic efficiencies. Dynamic efficiencies, which are associated with the development of new products and techniques, are hard to measure, and so would have only a qualitative weight. Production efficiencies would include reduced per unit operating and fixed costs as a result of lengthened production lines or the integration of new activities -- economies of scale and scope. Claimed efficiencies of this type more easily lend themselves to objective verification and should be supported by such documentation as accounting statements or engineering studies. Another type of production efficiency is the transfer of existing, but superior, know-how and technology from one organisation to another. This sort of claim is problematic both in terms of proof, and in establishing that a merger is necessary for it to occur (See the next point);

-- would not likely be attained: Claimed efficiencies only have weight if they are contingent on the merger being sustained. This, of course, raises the question of other, less anticompetitive alternatives to the merger, including internal growth, joint ventures, specialisation agreements,

licensing, or third-party mergers. Generally, in considering alternatives, the Bureau tries to minimise speculation. That is, alternative mergers are considered only if there is concrete reason for expecting them to proceed. Joint ventures, licensing or other contractual alternatives are considered only if they represent standard industry practice. The possibility of internal growth is assessed taking into account the growth of the industry, excess capacity and, thus, the possibility of incremental expansion. Parties to a merger should provide reasonable and verifiable information as to alternatives whenever possible;

-- greater than, and will offset: Consistent with the preceding discussion of efficiency and anticompetitive effects, this trade-off may have both qualitative and quantitative elements. As such there is an inevitable element of discretion in weighing the evidence. If the timing of benefits and costs differ, they should be discounted appropriately.

To date, there has not been a contested merger where the Competition Tribunal was required to weigh efficiency gains against what it held to be a substantial lessening of competition. Nor has the Bureau ever chosen, on the grounds of efficiency gains, not to challenge before the Tribunal a merger that appeared substantially to lessen competition. In this regard, it is important to note that a Tribunal order need not apply to a merger in its entirety; it can be directed against only certain assets or shares. This facilitates the separation of those elements of a merger which are clearly efficient and those which are anticompetitive, and limits the need to consider trade-offs between the two. Still, the Tribunal has chosen to comment on the question of efficiency in an obiter fashion.

This was done most extensively in the Hillsdown decision. This judgement was handed down by the Tribunal in 1992 pursuant to a merger which occurred in 1990 between two large, diversified food-processing corporations, Hillsdown Holdings and Canada Packers. As (a minor) part of this transaction, Hillsdown gained control of Orenco, a rendering company, to add to its existing operations in that field. The Bureau alleged to the Tribunal that this would result in a substantial lessening of competition in the noncaptive red meat rendering market in southern Ontario, and argued that Hillsdown should be made to divest Orenco. The Bureau had first obtained an interim order which required that Orenco be held separate from other Hillsdown operations to facilitate divestiture. Argument revolved around both the anticompetitive impact of the merger, as well as its efficiency implications, which Hillsdown suggested were sufficient to trigger the efficiency exception.

In the event, the Tribunal ruled that there would not be a substantial lessening of competition if the merger stood, though it indicated that this was a borderline case. This judgement turned on such issues as the geographic ambit of the market, unused capacity, barriers to entry, market growth and the probable independent evolution of the merged competitors should divestiture take place. Even so, the Tribunal proceeded to make additional comments on the efficiency issues that had been broached during the proceedings. In some important respects the sense of these remarks differed from the positions taken by the Bureau, both in the hearings and the MEGs.

Broadly, the Tribunal accepted the Bureau's approach to the question of production efficiencies. That is, it recognised the possibility of efficiencies of scale and scope as well as dynamic efficiencies associated with innovation, and it quoted approvingly the distinction between pecuniary and real economies. As well, the discussion placed the burden of establishing efficiencies squarely upon the respondents.

In the case at hand, Hillsdown argued that three sorts of efficiency would result from the merger: Administration, transportation, and manufacturing costs would all be reduced. The Tribunal essentially accepted all three. The Bureau had been particularly critical of the predicted savings in administration costs, suggesting that they could not be verified, and that internal growth represented an alternative means to the same end. In this regard the Tribunal felt that the Bureau was imposing too onerous a burden on the respondents in terms of establishing that the merger was necessary for the efficiencies -- that it should be sufficient to establish that efficiencies were "likely", rather than uniquely, due to the merger.

This, of course, raises the whole issue of alternative scenarios, and thus the necessity of the merger for efficiencies. This question was particularly vexed in Hillsdown. It was also central to the Tribunal's decision that the merger was not anticompetitive. Shortly before the merger, one of the rendering plants operated by Hillsdown had been expropriated and had not been replaced subsequent to the merger. Thus the question arose whether, upon divestiture, the plant would be rebuilt elsewhere -- essentially a return to the status quo ante -- or not. That answer, in turn, depended on such variables as the likely evolution of the supply of renderable meats, and increasing environmental objections to new rendering plants. The Tribunal's decision that the merger was not anticompetitive turned, inter alia, on a decision that the plant would probably not be rebuilt even with an order for divestiture. Ironically, its calculation of the efficiency gains from the merger was inconsistent in this regard as it was based on costs that existed prior to the merger and with the additional, expropriated plant still in operation.

One important point made by the Tribunal concerned the trade-off between efficiency gains and the effects of any lessening of competition. The Tribunal indicated that it was loath to engage in precise, numerical comparisons of deadweight loss and efficiencies. More importantly, however, it proceeded to question the Bureau's interpretation of the Act in this connection -- that only real, allocative costs were at issue. Rather, it suggested that the effects of any lessening of competition could also legitimately include transfers between consumers and producers associated with increased prices and reduced rivalry in the industry.

In this regard the Tribunal did not outline a specific legal test, but instead offered a series of questions for consideration. It did go so far as to suggest that a 'consumer surplus' criterion -- efficiencies great enough to lower prices to consumers -- would be sufficient, but not necessary, to meet the test for the efficiency exception in the Act. As the Tribunal did not endorse a new balancing test, the Bureau has chosen not to depart from the approach adopted in the MEGs for enforcement purposes.

CONTRIBUTION FROM ITALY

The Competition and Fair Trading Act no.287/90 ('the Act') makes it possible to take account of the efficiency defence only in relation to restrictive agreements. According to Italian legislation, the improvement in economic efficiency can be ascertained as a cost saving or, given costs, as an extension of the market (in terms of both quantity and quality of production). In order to qualify for an authorisation a restrictive agreement must benefit consumers; in other words, the increased profits resulting from such an agreement must be more than offset by the allied improvements in efficiency.

With reference to the control of mergers, any efficiency consideration forms part of the assessment of the operation only to the extent that it makes it possible to ascertain whether or not a dominant position has been created or strengthened, but it can never be deemed sufficient, in itself, to authorise a merger that would otherwise be prohibited.

Efficiency in concentrations

Section 6 of the Competition and Fair Trading Act makes no provision for trading off the creation or strengthening of a dominant position likely to appreciably restrict competition on a lasting basis against considerations relating to improved efficiency.

As a matter of fact, this section of the Act lists a number of important factors to be taken into account when assessing the effects of a merger or acquisition in terms of competition, to ascertain whether it is likely to create or strengthen a dominant position (the market position of the companies involved in the operation, the possibility to choose among different suppliers and customers, access to sources of supply or market outlets, barriers to market entry, the competitive position of the national industry, the prospects for demand or supply growth for the particular products or services involved). More specifically, reference to the market position of the companies concerned makes it possible to take into account such aspects as economies of scale and technological progress. However, these elements may only be used to assess the impact of the merger on competition, but not to trade off reduced competition against enhanced efficiency.

Legislator's intention to disallow any consideration of efficiency as a defence also emerges from the deliberate exclusion of the notion of consumer benefit among the criteria set out in section 6 of the Act, as compared with the different wording of article 2(b) of Regulation 4064/89. However, it might be argued that reference to "the competitive position of the national industry" might make it possible to take at least some account of some possible technological weakness. But this criterion has been interpreted as implying some dynamic considerations on the possible evolution of competition, more than an efficiency defence.

Efficiency in horizontal agreements

Conversely, the approach to agreements restricting competition seems to be more flexible. The general prohibition under section 2 on agreements and concerted practices or decisions taken by consortiums, associations of undertakings whose object or effect is to prevent, restrict or appreciably distort competition within the national market or within a substantial part of it, is followed by section 4, where the legislator leaves a certain amount of discretion to the Authority when deciding on the possibility of authorising otherwise prohibited agreements, though only in exceptional cases and for a limited period of time, whenever such agreements lead to an improvement in market supply conditions.

When drafting section 4 of the Act, the legislator drew on the corresponding provision of the EC Treaty, article 85(3), introducing into the Italian law a comparative test, according to which an authorisation must be granted only if the negative effects of an agreement restricting competition are more than offset by the attainment of specific requirements laid down by the law. In particular, the possibility of authorising, for a limited period of time, agreements falling within the scope of the prohibition provided by section 2 is conditional upon compliance with the following conditions: *a)* an improvement on the market supply conditions, with the effect of substantial by benefiting consumers; *b)* the absence of restrictions which are not strictly necessary for the purposes of attaining the objectives; *c)* competition is not eliminated in a substantial part of the market.

It is important to keep in mind that these conditions constrain the discretionary powers vested in the Authority. This means that the Authority may not take into account any other justification, such as safeguarding employment levels, or more general objectives of industrial policy, when conducting its assessment.

The provisions of section 4 also make it possible to use, as a criterion for authorising otherwise prohibited agreements both static and dynamic efficiencies, provided that the net gains in efficiency bring substantial benefits to consumers. This being so, it is necessary to establish whether the benefits to consumers in terms of efficiency resulting from the agreement are at all events likely to more than offset the negative effects originating from the restriction of competition. The benefit to consumers is therefore the central element in the definition of efficiency under the Act, and it is only in this sense that it can be accepted as a criterion for authorising anticompetitive agreements.

In this connection it should be emphasised that the benefit to consumers must be assessed in terms of the specific case under review, namely, the users or purchasers of the products or services forming the subject matter of the agreement.

Moreover, this condition must be objectively satisfied. Improvements in supply which remain the exclusive preserve of the parties to the agreement do not constitute a sufficient condition for granting an exemption from to the general prohibition. It was for these reasons that an agreement concluded between the leading motor-vehicle fuel manufacturers designed to restructure the distribution network by doing away with between 6 000 and 7 000 fuel retail outlets (about 23 per cent of existing service stations) over the three-year period 1992-94 was not deemed eligible to qualify for authorisation because with reduced competition between the operators it was somewhat unlikely that a substantial part of the cost reductions would be passed on to consumers (Restructuring the Fuel Distribution Network, ruling no. 1238 of 23/6/93).

However, for the efficiency argument to be accepted there must be compliance with the severe limitations laid down in the Act, namely, the fact that these restrictions are indispensable and that they must not eliminate competition.

With regard to the condition of the indispensable nature of the restrictions in order to attain the purposes set out in section 4, the benefits in terms of efficiency stemming from the agreement must be shown to be impossible to obtain by alternative and less restricting means.

Like Community law, the Act provides that the parties themselves must request exemption from the prohibition on agreements. Article 10 of the Regulation governing the examination of such cases (Presidential Decree No. 461 of 10 September 1991) provides that the request for authorisation must contain all the information deemed necessary to properly appraise the particular case. Therefore it is up to the parties to prove that the conditions laid down by the Act are met.

ANNEX

CASE STUDY

The establishment of a co-operative joint venture for the production of industrial gases (SON-IGI-SIAD/IGAT)

In February 1994, the Authority authorised the creation of a co-operative joint venture (IGAT) by three companies operating in the industrial gases sector (SON IGI and SIAD). The object of the joint venture was to build an industrial gases production plant in southern Italy. In this area there was an unmet annual demand for industrial gases (equivalent to 160 million cubic metres of liquid gas), while the annual supply was estimated at 110 million cubic metres. The unmet demand was currently being covered by gas produced from facilities located in Central and Northern Italy. The construction of the IGAT facility, whose annual production capacity was planned to be about 80 million cubic metres, would therefore make it possible to narrow the gap between supply and demand for industrial gases in southern Italy.

The planned joint venture was to operate only in the industrial gas production phase, while the parent companies would individually distribute the gases on the market.

The relevant product market was therefore the market for industrial gases (oxygen, nitrogen and argon) in the liquid state, resulting from air fractionation. The geographical extension coincided with the whole of Italian territory, in view of the sufficient similarity of competition conditions within the country.

The main undertakings operating on the national market held the following market shares: SIO (45 per cent), SIAD (15 per cent), SOL (15 per cent), IGI (11 per cent), SAPIO (7 per cent), SON (2 per cent), others (5 per cent). The parties to the joint venture therefore held a market share of 28 per cent of the national market.

The Authority found that the agreement would have restricted competition, because the joint production by the three competitor companies, implying the unification of production costs and the standardisation of the quality of the products, would have made it less easy for them to adopt independent commercial policies, leading to a co-ordination of their competitive conduct on the market.

However, the Authority ruled that the agreement was eligible for an authorisation on the basis of the following considerations:

a) It improved the conditions of supply on the market.

The production of industrial gases required substantial initial investments, estimated at about 850 billion lire in 1992. IGAT's planned annual production capacity of 80 million cubic metres of liquid gases reached a level equal to the minimum efficient scale of the operations. Moreover, the construction in southern Italy of a new production plant was likely to contribute to reducing transport costs and guarantee greater security of supply;

b) There were substantial benefits to consumers.

The availability of higher volumes of industrial gases at lower costs and the substantial reduction in transport costs would have positive effects on prices, substantially benefiting consumers;

c) There were no restrictions that were not strictly necessary to attain the objectives.

The construction and joint management of the facility was indispensable to improve the conditions of supply to such an extent that consumers would substantially benefit from it. Although the parties were able to set up individual plants for the production of industrial gases, the Authority held that they would not find sufficient incentives to do so acting independently;

d) The agreement would not enable the parties to eliminate competition on the national industrial gases market.

The presence of other leading producers, including the SIO company with a market share of 45 per cent, made it possible to guarantee a sufficient level of competition on the national market of industrial gases.

Considering the dimensions of the facility as planned, and particularly the length of time needed to guarantee an adequate rate of return, the Authority authorised the agreement for a period of ten years.

CONTRIBUTION FROM JAPAN

In order to maintain a competitive market structure in every goods and services market, the Antimonopoly Act (AMA) of Japan prohibits mergers, acquisitions of businesses,stockholdings, etc. when *(1)* such activities would substantially restrain competition in any particular "field of trade" (or market) or where *(2)* unfair trade practices have been employed in the course of such activities.

For the purpose of ensuring appropriate and efficient procedures for examining mergers etc., the Fair Trade Commission (FTC) of Japan has published "Administrative Procedure Standards for Examining Mergers, etc. by Companies" (July, 1980) and "Administrative Procedure Standards for Examining Stockholding by Companies" (September, 1981). In these administrative procedure standards, the FTC has specified standards for identifying merger cases etc., which require special scrutiny, as well as factors to be considered at the time of such scrutiny, to be used when the FTC tries to determine whether or not mergers etc. would substantially restrict competition in a particular market.

In August last year the FTC carried out a review of these standards and the revised standards were published. The purpose of the revision was not to alter the fundamental tenet of the previous administrative procedure standards, but to make them more easily understandable by inserting the meaning and purpose of each item and by adding information that was lacking.

Regarding the efficiency defense, there is no provision in the AMA itself, but the aforementioned "Administrative Procedure Standards for Examination of Mergers, etc. by Companies" provides the information given below. (The following portion was added when the guidelines were revised last August.)

A similar provision is seen in the "Administrative Procedure Standards for Examination of Stockholding by Companies". (The following paragraphs deal only with mergers, but the same applies to stockholdings.)

Efficiency was included as a factor to be considered because there are cases in which improvement in efficiency, as a result of a merger, can affect the competitive situation in a market by, for example, stimulating business activities in a way that promotes competition. However, it is also possible for increased efficiency to restrict competition, since it might contribute to an increase in the market power of the company formed by the merger. If competition in a certain market becomes restricted as a result of a merger, the benefits generated by improvement in efficiency are not normally passed on to consumers.

In this connection, it is important to distinguish between an improvement in "efficiency" in a particular company (formed by a merger), and the efficient allocation of resources in a particular industry, the latter being an almost indisputable goal of competition policy. The point is that there is no guarantee that the former will automatically contribute to the latter.

It is true that when an improvement in efficiency is realised in a merged company, the overall efficiency of the whole industry, of which the company is a part, is also increased. But the amount of increase in efficiency in the industry as a whole would barely exceed the original increase (generated by the merger) because spillover effects could not be very large. After all, merging parties may well have decided to merge because they believed they could not have obtained an efficiency increase if they had remained independent of each other. In other words, such efficiency benefits are usually unobtainable for those who remain independent. Hence, it would usually be the case that the efficiency increase resulting from a particular merger would not be particularly significant from the viewpoint of the efficiency of resource allocation in a given industry, unless the merged company’s market share is extremely high, which is not a very realistic assumption under normal merger control.

Administrative Procedure Standards for Examining Mergers

Matters to be Considered in Examining Selected Mergers

(1) .....

(2) Situation regarding competition, etc. in the relevant market where the parties concerned operate.

a. .....

b. .....

c. Overall business capabilities, etc., of the companies concerned.

The degree of effect on competition in the relevant market by:

-- the overall business capabilities of the mergering companies, such as their ability to procure raw materials, technical resources, marketing capabilities and access to credit;

-- their business situation (including the degree of poor business performance);

-- their efficiency.

(Note 3) Regarding "efficiency", attention will be paid to the effects of improvement in efficiency on competition. Efficiency may be attained through economy of scale, the integration of production facilities, the specialisation of plants, reduction in transport costs and facilitation in research and development etc. Due consideration will be given to such cases in which improvement in efficiency would promote competition (for example, if a low-ranking company, through a merger, is able to improve its cost competitiveness and promote competition).

However, the picture may be a little different when one takes into account the competition aspect. If a merged company, which remains low-ranking, realises a certain efficiency increase, it is better able to compete with leading companies. Competition in the market then becomes intensified and this normally results in more efficient resource allocation. On the other hand, if the merged company becomes dominant in the market, it can increase market power through its increased efficiency, causing the market to become restricted, and this naturally results in a less efficient resource allocation.

Accordingly, efficiency increase is just one of the factors to be considered when determining whether a certain merger would be pro- or anti-competitive, and does not by itself render the merger more acceptable from the point of view of the AMA. From such a standpoint one would wonder if it is proper to consider "efficiency" as a defense in a merger case. Hence it appears that the question of the "burden of proof" is not particularly relevant here. Also, the benefits to be accrued from improvement in efficiency should not be compared to the competition-restricting effects of the merger. Accordingly, as far as the FTC is concerned, there exists no formula for comparing efficiency benefits, on the one hand, and anti-competitive losses on the other, nor is there any formula to judge whether or not the former exceeds the latter.

CONTRIBUTION FROM NEW ZEALAND

The relevant prohibitions in the Commerce Act 1986 are:

-- s.27, which prohibits contracts, arrangements and understandings that substantially lessen competition;

-- s.30, which deems price fixing to substantially lessen competition for the purposes of s.27;

-- s.29, which prohibits collective horizontal boycotts;

-- s.47, which prohibits mergers and acquisitions that create or strengthen a dominant position in a market.

In addition, the Act includes what can be called an 'efficiencies defence', although that language is not used. Under s.58, a person who wishes to enter into or give effect to conduct that is or might be prohibited by ss.27, 29 or 30 may apply to the Commerce Commission for authorisation. Under s.67, a person who wishes to acquire assets or shares of a business may apply to the Commission for authorisation.

Although the wording of the tests for authorisation are slightly different, the tests to be applied by the Commission are the same. The Commission shall grant an authorisation if the conduct or acquisition would lead to a benefit to the public that outweighs the lessening in competition. The effect of an authorisation is to allow the conduct or acquisition to proceed without risk of challenge in the courts by way of public or private enforcement.

Application of the defence

Two issues that require discussion before moving to the specific types of benefits that can be accepted under the authorisation regime are:

-- the authorisation system in the context of a prohibition law;

-- why the New Zealand 'public benefit' defence is, essentially, an efficiencies defence.

Authorisations in the context of a prohibition law

The authorisation process does not compromise the status of the Commerce Act as a prohibition law nor its competition and efficiency objectives. There are two main reasons for this. First, authorisation cannot be obtained for past contraventions of the law. Parties to anticompetitive behaviour cannot avoid liability for past transgressions by applying for and gaining authorisation once the conduct is detected.

Secondly, there is a clear demarcation between the functions of the Commission and the courts. The Commission's role is to determine the extent that proposed conduct is likely to lessen competition and, if so, whether there is likely to be an outweighing benefit to the public. The question of whether conduct contravenes the Act (i.e. whether it substantially lessens competition) is for the courts to determine. In other words, when anticompetitive conduct is detected it is not possible to argue before the courts that it is justified on public benefit grounds.

Why the New Zealand 'public benefit' defence is, essentially, an efficiencies defence

Efficiency is the principal factor that the Commission and, on appeal, the courts take into consideration under the Act. There are two reasons for this. First, s.3A requires the Commission, when considering the extent of any benefit to the public, to have regard to any efficiencies.

Secondly, although s.3A does not preclude the consideration of other factors, the general trend in decisions made by the Commission and the courts has been to focus primarily on the efficiency arguments. The law has developed in this way because the Commission and the High Court have accepted that competition is not an end in itself and that the underlying objective of the Act is to promote economic efficiency.[12]

It took more than five years after the Act came into force in 1986 for the public benefit test to be interpreted in a consistent manner. During that period 'benefit to the public' had been applied alternatively as a one- or a two-part test.

Under the two-part test, which predominated from 1986 to 1991 (but was not always applied) it was necessary, first, to establish that there was a benefit; and secondly, that the benefit accrued to a reasonable cross-section of the public. This approach meant that the Commission had to make an assessment about the relative value of resources in the hands of different individuals. By adopting this approach the Commission was making value judgements that are, arguably, better made by governments than competition agencies.

An overall assessment of that five year period is that the approaches taken on public benefit and the weight to be attached to individual factors were inconsistent; and there was business uncertainty about what arguments they should make in support of their applications, and about the ultimate likelihood of success of their applications.

The two-part test has been abandoned. It is now established that public benefits must be net gains in economic and/or social terms. While this approach does not completely rule out the incorporation of the distributive values of New Zealand society, in practice the confirmation of the one-part test in High Court cases in 1991 and 1992 means that the public benefit test focuses very much on efficiency issues.[3] There have been no subsequent court or Commission decisions that have stated a view that a dollar is worth more to one member of society than another.

The most comprehensive decision on the interpretation of 'benefit to the public' is Telecom Corporation of NZ Ltd v Commerce Commission.[4] In that case the High Court adopted what had been stated by the Australian Trade Practices Tribunal in re Rural Traders Co-op (WA) Ltd:[5]

> It is undesirable to attempt to fix in advance the limits of what the concept of 'benefit to the public' encompasses or to exclude, in advance, from its ambit any contribution to the legitimate aims pursued by society. In the context of [competition] legislation, the encouragement of competition and competitive behaviour within relevant markets and the achievement of the economic goals of efficiency and progress will commonly be paramount . . .[6]

The High Court went on to say that:

> The approach of the [Australian] Tribunal embodies the values of Australian society, values that are not necessarily shared in New Zealand. Plainly, the New Zealand Commission and Court must have regard . . . to any contribution to the legitimate aims pursued by New Zealand society. That said, it is relevant that the Australian Tribunal has always proceeded on the basis that the term 'benefit to the public' draws attention

to the possibility that business conduct, that would otherwise infringe the Act, may have social value. Hence, it would not be in the public interest to rely exclusively upon the functioning of competitive markets to deliver everything 'of value to the community generally' There is the possibility of market failure, using that term to refer not only to 'market failure' in the economist's technical sense (stemming from economies of scale and scope, externalities and public goods) but also to some wider inadequacy of market functioning in the specific case to address the values of society.[7]

Commerce Commission guidelines on public benefit

The Commerce Commission has produced guidelines that outline its approach to the analysis of detriments and benefits when considering applications for authorisation.[8] The key principles appearing in the guidelines are as follows:

(a) The 'public' is the public of New Zealand.

(b) The comparison is 'with' and 'without' the matter under consideration rather than 'before' and 'after'.

(c) The detriments from a loss of competition include losses of economic efficiency, incentives to innovate and incentives to avoid waste.

(d) The gain must be shown to be dependent on the proposed acquisition or conduct.

(e) Gains are considered in net terms, not in terms of changes to specific inputs and outputs.

(f) Gains which may contribute to a benefit to the public include:

-- tangible benefits such as economies of scope and scale; better use of existing capacity; cost reductions due to reduced labour costs, greater specialisation of production, lower working capital and reduced transaction costs; and

-- intangible benefits such as environmental improvements and health improvements.

(g) Double counting of gains are excluded.

(h) Generally, no extra weighting is given to:

-- increased employment unless national employment is increased;

-- export compared with domestic earnings; or

-- redistribution of activity to particular regions.

(i) Transfers of wealth *per se* are not treated as net gains.

(j) The distribution of gains and losses is, *per se*, irrelevant to their inclusion in the process of weighing benefits and detriments.

The approach adopted by the Commission is illustrated in the Health Waikato/Midland Health case study appended to this report.

The treatment of economies of scale and scope in a small economy

A common attitude in some larger economies is that economies of scope and scale will be achieved over time through normal market processes. Our view is that this approach does not always apply in small economies, like New Zealand's. The much higher concentration of markets means that some potential efficiencies might only be achieved by allowing mergers that have an anticompetitive effect. Hence, it is essential to avoid both an overly permissive policy that entrenches market power and an overly aggressive approach that prevents efficiency-creating acquisitions. The Commission has given weight to economies of scale and scope in a number of cases.

Benefits that accrue to or are at the expense of foreigners

An issue that has arisen occasionally is how to treat acquisitions and conduct where some or all the relevant firms have foreign shareholders. The position as it applies in New Zealand was described by the High Court in the Telecom case as follows:

We reject any view that profits earned by overseas investment in this country are necessarily to be regarded as a drain on New Zealand. New Zealand seeks to be a member of a liberal multilateral trading and investment community. Consistent with this stance, we observe that improvements in international efficiency create gains from trade and investment which, from a long run perspective, benefit the New Zealand public.

On the other hand, if there are circumstances in which the exercise of market power gives rise to functionless monopoly rents, supranormal profits that arise either from cost savings or innovation, and which accrue to overseas shareholders, we think it right to regard these as exploitation of the New Zealand community and to be counted as a detriment to the public.[9]

The burden of proof/standards for comparing efficiency benefits with the anticompetitive effects

The onus of proof lies upon the applicant to provide sufficient and credible evidence to support its public benefit claims. The burden of proof the applicant must meet is the 'balance of probability'. The 'balance of probability' is the most appropriate test because of the need to weigh incommensurable predictive economic evidence of anticompetitive effects on the one hand and various elements of public benefit on the other.

This comparison is, inevitably, largely a qualitative judgement although both the Commission and courts have encouraged quantification where that is possible. The danger in this approach is to place excessive weighting on the quantifiable factors such as short term productive efficiency gains at the expense of the hard-to-measure allocative and dynamic efficiency factors such as reduced incentives to innovate and reduced incentives to control costs. Over reliance on quantitative data creates a dilemma because dynamic efficiency, which is the least quantifiable form of efficiency, is almost always the most economically significant component of total efficiency.

Summary

A defence is available for the full range of mergers and horizontal agreements in New Zealand. It allows parties to a proposed acquisition or proposed conduct that does or might contravene the Act to argue that there is a benefit to the public that outweighs the anticompetitive detriment. However, that defence can be accepted by the Commerce Commission only, and only in the context of an application for

authorisation. It is not possible to argue an efficiencies defence before the courts in a public or private enforcement case.[10]

The New Zealand public benefit defence is, essentially, an efficiencies defence. While the test does not completely rule out the incorporation of distributive values of New Zealand society, all decisions made in the last four years have squarely focused on efficiency issues. This approach has created business certainty about the scope of the defence and has produced outcomes that accord with the achievable objectives of competition legislation.

NOTES

1. When moving the introduction of the Commerce Bill at its second reading, the Hon. David Caygill stated '[The Bill] will promote competition in the New Zealand marketplace. In tandem with other changes, the Bill increases efficiency in the New Zealand economy.' [1986] NZ Parliamentary Debates 506.

2. *E.g.*, in Tru Tone Ltd v Festival Records Retail Marketing Ltd [1988] 2 NZLR 352, RICHARDSON J concluded (at 358) 'In terms of the long title, the Commerce Act is an Act to promote competition in markets in New Zealand. It is based on the premise that society's resources are best allocated in a competitive market where rivalry between firms ensures maximum efficiency in the use of resources.'

3. See, *e.g.*, Telecom Corporation of NZ Ltd v Commerce Commission [1992] NZAR 193 where JEFFRIES J concluded that 'Economic efficiencies are real and of benefit to the public in terms of overall resource allocation and economic welfare even if little or none of the benefit directly accrues to others than the owners of the business.'

4. 4 TCLR 473.

5. [1979] ATPR 40-110 at 18,123.

6. at p. 527.

7. at pp. 529-530.

8. Commerce Commission, 'Guidelines to the Analysis of Public Benefits and Detriments in the Context of the Commerce Act', October 1994.

9. at p. 531.

10. What is or isn't a public benefit is not always clear. *E.g.*, the courts are yet to consider a case where an agreement that would normally be regarded as price fixing is defended on the grounds that the market would not exist but for the agreement. The courts could either conclude that it is not price fixing because it is a procompetitive agreement; or that it is price fixing because the words of s.30 of the Act are plain. The different interpretations have significant implications for the parties in terms of whether it would have been prudent to have sought advance authorization from the Commission.

ANNEX

CASE STUDY

Health Waikato LTD/Midland Health
(Decision No. 275, 1 August 1995)

The facts

Midland Regional Health Authority ('Midland Health') is the monopsony purchaser of publicly funded health care and disability services and manages contracts with the service providers in the central North Island region. Health Waikato is a Crown health enterprise operating the main 24-hour acute/intensive tertiary and secondary general hospital in Hamilton (the major population centre of the region), and an outdated medium and minimum secure mental health facility at Tokanui.

The parties sought authorisation for certain provisions in two contracts between Midland Health and Health Waikato which provide that:

-- Midland Health would purchase access for ten years to a new and secure mental health facility (capable of meeting all the relevant mental health service needs in the Midland Health region) to be built by Health Waikato as a precondition to Health Waikato setting up that facility. The contract would, among other things, grant Health Waikato a first right to negotiate and include a guaranteed access fee of NZ$ three million a year; and

-- The two parties would agree to negotiate a service contract for the provision of forensic mental health services; intensive patient care and acute/intensive care services; rehabilitation services; and other health or disability services, if any, to be provided at the facility.

The counterfactual

The Commission considered the most plausible 'without' scenarios to be:

(a) a ten year heads of agreement, with rights of access to the developed facility, and with shorter term contracts for delivered mental health services being put out to tender; or

(b) a reduction in the term of the heads of agreement from ten to five years.

Of the two, option (b) was considered to be the more likely. Although Midland Health did not favour a shorter contract, Health Waikato stated that it would be happy with a five year contract term, provided the cost of the facilities was funded over that period. Option (a) was also accepted as a possible counterfactual. However, the need for patients to be treated by the same clinicians when they moved between different levels of mental health services suggested that it would be less likely.

Competitive impact

The Commission concluded that:

-- Due to the complimentary nature of the delivered mental health services and the facilities contract, Health Waikato's advantageous position would be likely to be retained for the duration of the ten year facilities contract.

-- The contracts would create a substantial barrier to entry for existing or potential providers in the markets for inpatient mental health facilities, forensic mental health services and acute/intensive mental health services. When considered in conjunction with the tying effects of a longer term contract, there would be a lessening of competition compared to more contestable contractual arrangements.

-- There would be no lessening of competition in the markets for rehabilitation and continuing care mental health facilities and services markets.

Competitive detriments

The Commission concluded that the detriments were as follows:

(a) Absence of competitive tendering for facilities: There would be scope for uncompetitive pricing given that the contract for facilities was not put out for tender. However, this scope is likely to be small because of various approvals processes, and scrutiny by independent accountants employed by both parties to determine the costs to be capitalised at the time of the commissioning of the facility.

(b) Absence of competitive tendering for services: The contracts would greatly limit the opportunity for other providers to supply mental health services through it. This would have adverse effects on:

-- prices. However, given inelastic demand for mental health services, the loss of allocative efficiency would be relatively small.

-- service quality. However, various safeguards would exist including review conditions in the services contract, and various statutory responsibilities.

-- static efficiency. The absence of competition would be likely to reduce incentives for Health Waikato's management to deliver mental health services more efficiently, especially if the services contract price were a favourable one.

-- dynamic efficiency. The proposed contract would be likely to hinder Midland Health in negotiating, from time to time, for the delivery of mental health services from other more efficient providers.

The Commission concluded that as it would take some time for competition to emerge, the identified detriments were unlikely to be felt for three to five years. Allowing for the time value of money, and for uncertainties implicit in forecasting, the aggregate size of the detriment is likely to be substantially reduced. Nevertheless, these expected competitive detriments were regarded as significant.

Public benefits

The Commission's comments on the claimed benefits were as follows:

(a) Upgrading of facilities: The Commission accepted that improved facilities would lead to improved mental health care, but that these would also accrue in each of the 'without' scenarios.

(b) Overcoming investment risk: The applicants stated that Health Waikato would be exposed to significant risk in building the facility. Once the facility was built, the balance of negotiating power would shift to the monopsony. The contract would transfer the risk to the monopsony. The Commission stated that the investment risk could be overcome in either of the 'without' scenarios.

(c) Economies of scale: The applicants stated that there are substantial economies of scale from having a single integrated forensic unit, rather than a number of smaller units scattered in the Midland Health region. Similar comments were made in relation to the acute/intensive levels of general mental health facilities and services, which also require highly trained personnel and specialised in-patient facilities. The Commission stated that a competitive market would be expected to drive providers to operate facilities of optimal scale, so that any advantages from economies of scale would be expected to accrue anyway.

(d) Economies of scope: Various economies of scope were claimed relating to the integration of mental health and general hospital facilities on one site. The Commission accepted that these economies could be generated but that they would accrue to a similar facility built in more competitive circumstances.

(e) Locational advantages: It was claimed that mental health is fostered when patients are close to rehabilitation programmes, and when there is ready access for patients to their families and to community support, vocational and recreational services. These objectives may be maximised in a single mental health facility located in the major population centre of the region. The Commission stated that it would expect the facility to be built in Hamilton under either 'without' scenario. However, a new entrant would probably have less developed links and there might be some loss of benefit in the short term.

(f) Community well-being: Various community benefits were claimed, all of which the Commission considered would occur under either 'without' scenario.

Weighing of benefits and detriments

The Commission stated that it believed that the most probable outcome in the absence of the proposed contracts is that the proposed facility would be built on the Waikato Hospital campus under different contractual terms. Hence, no benefits arose solely from the proposal and there were significant competitive detriments. Accordingly, the application for authorisation was declined.

CONTRIBUTION DE LA SUISSE

La nouvelle loi suisse

Le droit suisse de la concurrence connaît actuellement une phase de transition. Le Parlement vient d'adopter une nouvelle loi fédérale sur la concurrence, qui devrait entrer en vigueur dans le courant de l'année prochaine.

La nouvelle loi aura des retombées décisives sur la politique suisse de la concurrence. En effet alors que la loi actuelle fait intervenir un large éventail de critères (notamment de politique économique et de politique générale) pour des restrictions à la concurrence, la nouvelle érige la concurrence efficace en critère central d'évaluation. Cette nouvelle orientation confère à la notion d'efficacité économique un tout autre contenu.

Occultée par un grand nombre de critères l'efficacité économique n'aura joue tout au plus qu'un rôle marginal dans le régime actuel. La nouvelle loi en fait par contre, pour ainsi dire, partie intégrante de la concurrence efficace.

La notion d'efficacité dans la nouvelle loi

En présence d'une restriction à la concurrence, il faudra, sous la nouvelle loi, d'abord examiner si la restriction élimine la concurrence efficace ("effective competition"). Axée sur cette dernière, la politique de la concurrence devra permettre aux fonctions statiques et dynamiques généralement attendues de la concurrence de s'exprimer dans une mesure suffisante. Aussi longtemps que ces fonctions essentielles ne souffrent d'aucune atteinte significative sur un marché déterminé, la concurrence peut être qualifiée d'efficace.

Les restrictions à la concurrence qui n'éliminent pas la concurrence efficace (les accords dits de coopération, par exemple) sont considérées comme licites lorsqu'elles sont justifiées par des motifs d'efficacité économique. Un accord en matière de concurrence est économiquement efficace lorsque les conditions suivantes sont remplies :

-- L'accord est nécessaire pour réduire les coûts de fabrication ou de distribution, pour améliorer des produits ou des procédés de fabrication, pour promouvoir la recherche ou la diffusion de connaissances techniques ou pour exploiter plus rationnellement des ressources[1]).

-- La situation en matière de concurrence garantit que cet accord ne permettra en aucune façon aux entreprises concernées de supprimer la concurrence efficace[2]).

Avec cette deuxième condition, des avantages recherchés dans le seul intérêt des entreprises parties à l'accord ne pourront à eux seuls constituer une justification. L'efficacité doit avant tout être comprise d'un point de vue économique global ; les gains d'efficacité obtenus sur un marché devront toujours être répercutés, au moins partiellement, sur d'autres échelons du marché. Il en résulte que la justification par des motifs d'efficacité économique est exclue pour des restrictions à la concurrence qui éliminent la concurrence efficace (les justifier ne serait pas compatible avec la notion d'efficacité au sens économique global). On pense ici en premier lieu aux accords horizontaux sur prix, les quantités ou la répartition géographique.

Afin de rendre la nouvelle loi plus facilement applicable, le législateur l'a assortie de deux dispositions qui méritent d'être mentionnées. Celles-ci prévoient:

-- la présomption légale que les accords horizontaux sur les prix, les quantités ou la répartition géographique éliminent la concurrence efficace[3];

-- la compétence de l'autorité de concurrence de fixer, dans des actes législatifs d'exécution, les conditions auxquelles certains types de restrictions pourront être considérés comme économiquement efficaces[4]). Il faut s'attendre à voir ces textes d'exécution s'inspirer largement des exemptions par catégories du droit de l'UE, même si, juridiquement, ils ne leur sont pas vraiment comparables (droit suisse ne connaît pas d'interdiction à des cartels).

Réponses aux questions du Secrétariat

La nature de l'argument d'efficacité

Lors de l'évaluation des avantages liés à l'efficacité d'une restriction à la concurrence, on ne peut, formellement ou matériellement, parler de "défense". Au sens de la nouvelle loi, les aspects d'efficacité interviennent déjà lors de l'examen du comportement d'une entreprise quant à ses effets de restriction à la concurrence. Cette appréciation fonde sur la concurrence efficace ; les aspects de politique générale ne peuvent être retenus.

La promotion des exportations comme argument d'efficacité

Les aspects dont la nouvelle loi demande la prise compte découlent des conditions mentionnées plus haut. Le renforcement de la compétitivité sur le marché d'exportation ne suffit pas à justifier, en raison du surcroît d'efficacité, une restriction à la concurrence sur le marche national. Il convient cependant de relever dans ce contexte que, lors de la délimitation du marché en cause, il ne sera pas seulement tenu compte de la situation des entreprises concernées sur le marché national, mais aussi, le cas échéant, de leur position dans la concurrence internationale.

La charge de la preuve

Il résulte de la nature de l'examen de l'efficacité inscrit dans la nouvelle loi qu'il n'appartient pas aux entreprises concernées de fournir la preuve stricte de l'amélioration de l'efficacité économique. L'évaluation d'une restriction à la concurrence sous l'angle de l'efficacité relève essentiellement de l'application du droit matériel, tâche incombant à la Commission de la concurrence.

Où les avantages doivent-ils se manifester?

Dans la nouvelle loi, les avantages obtenus sur le plan de l'efficacité doivent atteindre, au moins partiellement, d'autres échelons du marché en cause. Cette répercussion devrait être garantie par la concurrence efficace.

La proportionnalité

Dans le cadre de l'examen de la proportionnalité, il faudra se demander si la restriction à la concurrence est effectivement nécessaire a l'amélioration de l'efficacité. Il sera alors, selon la loi, décisif

de savoir si la restriction affecte de manière significative la concurrence efficace ; dans la négative, l'examen de la proportionnalité ne revêtira pas de signification prioritaire, étant donné que d'autres critères d'examen permettraient d'aboutir dans la quasi-totalité des cas à appréciation à peu près semblable des effets sur la concurrence. Si, par contre, on se trouve en face d'une atteinte significative à la concurrence efficace, le critère de la nécessite devra, lors de l'examen de la proportionnalité, contribuer à réduire l'importance des dommages de l'atteinte.

Les accords en matière de prix, de quantités ou répartition géographique

Il ressort de l'exposé général de la notion à la base de la nouvelle loi qu'il est quasiment exclu d'invoquer une amélioration de l'efficacité économique pour justifier des accords horizontaux en matière de prix, de quantités ou de géographique (voir sous point 2, i.f., la présomption légale).

NOTES

1. Article 5, 2ème alinéa, lettre a, de la nouvelle loi.

2. Article 5, 2ème alinéa, lettre b, de la nouvelle loi.

3. Article 5, 3ème alinéa de la nouvelle loi.

4. Article 6 de la nouvelle loi.

CONTRIBUTION FROM UNITED STATES

The role of efficiencies in US antitrust analysis of mergers and horizontal agreements is not set forth in a single law or policy but rather requires examination of relevant case law and enforcement policy statements. Under US antitrust law, efficiency claims are not recognised as an absolute defence to an otherwise anticompetitive agreement but rather constitute a factor that in some circumstances may be weighed in the determination of the net competitive effects. This paper will discuss how efficiencies are taken into account in determining the legality of a merger or horizontal agreement. Section I will address the treatment of efficiencies in merger analysis and section II that of horizontal agreements. Section III will briefly note the ongoing dialogue on whether modifications in the current treatment of efficiencies in US antitrust analysis is necessary.

Efficiencies and Merger Analysis

During the 1960's and early 1970's, the Supreme Court indicated that efficiencies may not be relied upon to uphold an otherwise anticompetitive merger. The most direct statement is found in the l967 case of FTC v. Proctor and Gamble Co.,[1] in which the Court said: "Possible economies cannot be used as a defence against illegality. Congress was aware that some mergers which lessen competition may also result in economies but it struck the balance in favour of protecting competition."[2]

The Supreme Court has not spoken on this issue in the intervening years. Courts and academics have differing interpretations of this precedent. Some infer that the Supreme Court has rejected the use of efficiency evidence to justify a merger; others opine that the Court rejected only efficiencies defences that were based on insufficient or speculative evidence.[3] The Federal Trade Commission ("FTC") in a l984 decision examined the relevant Supreme Court cases and concluded that "the Supreme Court has stated, in dicta only, a bias against assertions of the efficiencies justification in Section 7 cases, and those statements do not appear in the context of an efficiencies defence."[4]

The decisions of lower federal courts exhibit no established trend. Some have rejected consideration of efficiencies, relying on their reading of Supreme Court precedent, though most of these are older cases.[5] However, in recent years, several federal courts have considered efficiency claims. For example, in its 1991 decision in FTC v. University Health, Inc.,[6] the Eleventh Circuit Court of Appeals stated that "evidence that a proposed acquisition would create significant efficiencies benefiting consumers is useful in evaluating the ultimate issue--the acquisition's overall effect on competition."[7] The court went on to say: "We think, therefore that an efficiency defence to the government's prima facie case in section 7 challenges is appropriate in certain circumstances."[8] However, while it referred to the consideration of efficiencies as a "defence," the Court also stated: "Of course, once it is determined that a merger would substantially lessen competition, expected economies, however greater, will not insulate the merger from a section 7 challenge." [9] To date, no federal court has upheld an otherwise anticompetitive merger on the basis of efficiencies.[10]

The administrative decisions of the FTC also consider efficiencies as a factor in the analysis of likely competitive effects but do not recognise them as a legal defence. In American Medical International Inc.,[11] the Commission weighed the arguments for and against an efficiency defence, and without ruling whether such a defence was legally cognizable, rejected the claims on evidentiary grounds. Recently in Honickman,[12] the Commission approved an application for prior approval of a proposed acquisition in New Jersey and rejected another proposal in New York. It found that anticompetitive risks of the New Jersey acquisition were "smaller" and the likelihood of resulting net efficiencies greater than in New York. In rejecting the New York acquisition, the Commission concluded that "only an extremely strong showing

of net efficiencies" (which the proponent failed to make) would outweigh the competitive risks of a transaction that presented "a high risk to competition."[13] Some have characterised the Commission standard in Honickman as suggesting a "sliding scale" between efficiencies and anticompetitive threats.[14]

The federal court and FTC decisions provide insight on the type of efficiency claims that will be considered in litigation and the evidentiary requirements. The types of efficiencies that have been considered have been those resulting from operating economies, such as production or plant economies, and research and development.[15] Following Supreme Court precedent,[16] some courts have required that the claimed efficiencies must be achieved in the relevant product market rather than other markets.[17] Some court and FTC cases have expressly imposed a requirement that the resulting economies be passed on to consumers or benefit competition and, hence, consumers.[18] Courts and the FTC generally have rejected efficiency claims where the economies can be obtained by less anticompetitive means other than the merger.[19] All have placed the burden of proof of efficiency claims on the proponents of the merger and require substantial and convincing proof of significant economies.[20]

The framework for analysis of efficiencies by the federal enforcement agencies in exercising their prosecutorial discretion is set forth in the 1992 joint Horizontal Merger Guidelines.[21] The 1992 Merger Guidelines, like earlier versions, provide that the presumption of anticompetitive effects, which is triggered by specified concentration levels, may be overcome by other factors. After determining that the merger would significantly increase concentration and result in a concentrated market, the agencies assess whether the merger, in light of market concentration and other factors that characterise the market, raises concerns about potential adverse competitive effects. If so, an assessment is made as to whether entry would be timely, likely and sufficient either to deter or to counteract the anticompetitive effects. If that analysis discloses a significant likelihood of anticompetitive effects, the next step is to look at efficiency gains that reasonably cannot be achieved through other means.

Section 4 of the 1992 Merger Guidelines states that the agencies will evaluate any claim that significant net efficiencies should save from challenge an anticompetitive merger. The section then describes the elements of a persuasive efficiencies argument by the proponents of the proposed merger.[22] The Guidelines confine the analysis to an examination of "significant net efficiencies." This means that the authorities weigh not only potential cost savings or other benefits but also offsetting cost increases or quantity or quality decreases. The net efficiencies requirement, for example, would preclude consideration of cost reductions achieved simply by reducing the quantity or quality of services provided to consumers or economies of scale that are offset by the capital costs involved in bringing the merged entity to that scale.

The Guidelines provide examples of the types of efficiencies that will be considered:

> Cognizable efficiencies include, but are not limited to, achieving economies of scale, better integration of production facilities, plant specialisation, lower transportation costs, and similar efficiencies relating to specific manufacturing, servicing, or distribution operations of the merging firms. The Agency may also consider claimed efficiencies resulting from reductions in general selling, administrative, and overhead expenses, or that otherwise do not relate to specific manufacturing, servicing, or distribution operations of the merging firms, although as a practical matter, these types of efficiencies may be difficult to demonstrate.[23]

The second requirement is that the efficiencies must be merger-specific; that is, realisable only through the proposed merger. This means that the efficiency claims will be rejected "if equivalent or comparable savings can reasonably be achieved by the parties through other means"[24] without the merger's potential adverse competitive effects. The analysis begins by identifying major alternative means by which

an efficiency may be accomplished, such as internal expansion or joint ventures with other competitors or firms in a related industry.

Third, "the expected net efficiencies must be greater the more significant are the competitive risks" created by the proposed merger.[25] While efficiencies have influenced agency decisions not to challenge a merger, efficiency arguments are "much tougher to sell when the merger in question would clearly create a monopoly or otherwise seriously endanger competition."[26]

Fourth, the Guidelines implicitly require that the claimed efficiencies be passed on to consumers, rather than only benefiting the parties to the merger.[27] In cases where the efficiencies take the form of improved service and quality, the direct benefit is clearest.[28]

For purposes of the round table discussion, which requests an illustrative case, attached is an excerpt of the discussion of efficiencies from the Eleventh Circuit's aforementioned decision in FTC v. University Health Inc.

Efficiencies and Nonmerger Horizontal Agreements

Efficiency considerations are a key element of antitrust analysis of nonmerger, horizontal restraints i.e., horizontal agreements that do not involve an acquisition of stocks or assets. At the outset, efficiencies play a key role in answering the threshold question of whether the *per se* rule or the "rule of reason" applies. Where the rule of reason is the appropriate standard, an evaluation of efficiencies is important in determining whether an agreement is anticompetitive and therefore legal.[29]

To determine whether a horizontal agreement is given *per se* or rule of reason treatment, both the courts and enforcement agencies assess whether the restraint in question can be expected to contribute to an efficiency-enhancing integration of economic activity. Where there is no efficiency-enhancing integration of economic activity and the restraint falls within the traditional categories of *per se* offences, such as price-fixing, the *per se* rule will apply. Otherwise the rule of reason standard is used.[30]

The role of efficiencies in deciding whether the *per se* rule applies is illustrated in Broadcast Music, Inc. v. Columbia Broadcasting System ("BMI"),[31] where the Supreme Court, based on a finding of integrative efficiencies, remanded for a rule of reason analysis a blanket licensing arrangement among composers by which they delegated pricing on a collective basis to two clearinghouses. The Court found that the agreement had been mischaracterized as *per se* illegal price fixing, because the blanket license was not a naked restraint of trade but rather was "designed to 'increase economic efficiency and render markets more, rather than less competitive.'"[32] It pointed to the accompanying "integration of sales, monitoring, and enforcement against unauthorised copyright use," which resulted in a "substantial lowering of costs" and enhancement in service and consumer choice.[33] The Court went on to find that the blanket-license fee was essential to the production of a new product, the blanket license, which no individual copyright owner could produce alone.

In contrast, in Arizona v. Maricopa County Medical Society, [34] the Supreme Court declined to apply a rule of reason standard to a maximum fee schedule by doctors participating in a "foundation" to provide physician services as an alternative to existing insurance programs. Central to its decision was the Court's finding of the absence of any integrative efficiencies or any offering of a new product:

> The foundations are not analogous to partnerships or other joint arrangements in which persons who would otherwise be competitors pool their capital and share the risks of loss as well as the opportunities for profit. . . . The agreement under attack is an agreement among hundreds of competing doctors concerning the price at which each will offer his own services to a substantial amount of consumers. . . . If a clinic offered

> complete medical coverage for a flat fee, the co-operating doctors would have the type of partnership arrangement in which a price-fixing agreement among the doctors would be perfectly proper. But the fee agreements disclosed by the record in this case are among independent competing entrepreneurs.[35]

As these cases illustrate, integrative efficiencies involve some form of economic integration of the parties that goes beyond the mere co-ordination of the parties' decisions on price and output and include efficiencies that would enable the parties to the agreement to increase output or lower cost, or to produce new products or services that would not otherwise be produced by a single firm.[36] Such efficiencies typically arise from the realisation of significant economies of scale and the integration of existing complementary research and development, production and marketing capabilities.[37] These are the same broad types of efficiencies that are considered in merger cases.

A determination that a horizontal agreement has the potential to create efficiencies through economic integration precludes a finding of *per se* illegality but does not end the legal analysis. The legality of the agreement will depend on whether depend on whether under the rule of reason standard it is on balance anticompetitive. The rule of reason approach entails an assessment as to whether the restraint is likely to have anticompetitive effects, and if so, whether the restraint is reasonably necessary to achieve procompetitive efficiencies that outweigh those anticompetitive effects.[38] In National Collegiate Athletic Ass'n ("NCAA") v. Board of Regents of the University of Oklahoma,[39] for example, the Supreme Court applied a rule of reason analysis to the NCAA's jointly-marketed broadcast plan that limited output of live telecast of college football games. The Court condemned the plan because on its face it was anticompetitive, and there was no support for the NCAA's assertions that the restraints produced any valid, procompetitive efficiencies.[40]

Application of the rule of reason generally requires a comprehensive analysis of market conditions. However, in certain circumstances the courts truncate that analysis.[41] Under the truncated or "quick look" rule of reason analysis, efficiencies can play a determinative role where a restraint on its face would always or almost always tend to reduce output or increase price. If such a restraint is not reasonably related to efficiencies, it may be held unlawful without a comprehensive analysis of market conditions.[42] However, where there are valid and plausible efficiency justifications, a full-scale rule of reason analysis is necessary. Both enforcement agencies use a truncated analysis in their prosecutorial decisions.[43] The Federal Trade Commission utilised such an approach in its decisions in American Medical Ass'n,[44] and more recently in Massachusetts Board of Registration in Optometry[45] and Detroit Auto Dealers Ass'n.[46]

The Ongoing Debate

As noted, for example, by the Eleventh Circuit Court of Appeals in University Health, there has been considerable dialogue among antitrust scholars on the proper scope of an efficiencies defence, particularly in merger analysis.[47] Some advocate an absolute defence, others a partial defence limited to certain types of efficiencies, while still others suggest that the enforcement agencies and not the courts consider efficiencies.[48]

The Federal Trade Commission is holding public hearings this Fall on whether antitrust enforcement requires adjustments in order to account for changing competitive circumstances prompted by the development of a global economy and of innovation-based competition. One of the issues to be examined is whether current US antitrust analysis adequately takes into account efficiencies in merger and nonmerger analysis. The specific issues to be addressed are set forth in the attached agenda. Following the hearings, the Commission intends to issue a report that may indicate changes it intends to adopt or areas for further study or co-ordinated action with the Department of Justice.

NOTES

1. 386 U.S. 568, 580 (1967).

2. See also Brown Shoe v. United States, 370 US 294, 344 (1962) ("Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favour of decentralisation."); United States v. Philadelphia Nat'l Bank, 374 US 321, 371 (l963) ("...a merger the effect of which may be 'substantially to lessen competition' is not saved because, on some ultimate reckoning of social and economic debits and credits, it may be deemed beneficial.").

   Even when the courts were most hostile to considering efficiencies in merger cases, they did consider efficiencies in joint venture cases. See, *e.g.*, United States v. Penn-Olin Chemical Co., 378 US 158 (l964). As discussed in section II, integrative efficiencies are considered in determining whether a purported joint venture is in fact a cartel, as well as in deciding, under a rule of reason analysis, whether a valid joint venture is on balance procompetitive.

3. For a discussion of some of the differing views, see, *e.g.*, FTC v. University Health, Inc., 938 F.2d 1206, 1222-1223 (11th Cir. l991).

4. American Medical Int'l Inc., 104 FTC 1, 217 (1984). The FTC also pointed to statements in other Supreme Court and lower federal court decisions and found that they suggest "that efficiencies should be considered in antitrust analysis, in general, and under Section 7, in particular." *Id.*

5. See, *e.g.*, ITT v. GTE, 518 F.2d 913, 936 (9th Cir. 1975); RSR Corp. v. FTC, 602 F.2d 1317, 1325 (9th Cir. 1979), cert. denied, 445 US 927 (1980). See also American Bar Association Antitrust Section, 1 *Antitrust Developments* 319 (3d.ed. 1992) (hereinafter "ABA").

6. 938 F.2d at 1222.

7. See also United States v. Rockford Memorial Corp., 717 F. Supp 1251, 1289-91 (N.D. Ill. l989), aff'd, 898 F.2d 1278 (7th Cir.), cert. denied, 498 US 920 (1990); United States v. Country Lake Foods, Inc., 754 F. Supp 669, 680 (l990). See generally ABA, *supra* note 5, at 320; PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", 81 *GEO.L.J.* 195, 212-213 (1992).

8. 938 F.2d at 1222.

9. *Id*. at 1222 n. 29.

10. See PITOFSKY, *supra* note 7, at 213; STOCKUM, "The Efficiencies Defence for Horizontal Mergers: What is the Government Standard?", 61 *Antitrust L.J.* 829-30 (l993); ABA, *supra* note 5, at 320.

11. 104 FTC at 219-220.

12. Harold A. HONICKMAN, 5 *Trade Reg. Rep* (CCH) ¶ 23,286 at 22,965-66(1992).

13. *Id*. at 22,964-65.

14. See STOCKUM, *supra* note 10, at 838; KATTAN, "Efficiencies and Merger Analysis", 62 *Antitrust L.J.* 513, 519 (l994).

15. See, *e.g.*, ABA, *supra* note 5, at 320.

16. In Philadelphia Nat'l Bank, 374 US at 370, the Supreme Court also stated that anticompetitive effects in one market cannot be offset by proof of efficiencies in other markets.

17. See, *e.g.*, RSR Corp., 602 F.2d at 1325 ; United States v. Ivaco, Inc., 704 F.Supp. 1409, 1427 (W.D. Mich. l989) (joint venture).

18. See, *e.g.*, University Health, 938 F.2d at 1223; United States v. United Tote, Inc., 768 F. Supp. l064, 1084-85 (D. Del. l991); FTC v. Imo Indus., Inc., 1992 Trade Cas. ¶ 69,943 at 68,559-560 (l992); American Medical Int'l. Inc., 104 FTC at 219-220; Honickman, 5 Trade Reg. Rep. at 22,963, 22,965 n.26.

19. See, *e.g.*, Rockford Memorial Corp., 717 F. Supp. at 1289-91; Ivaco, 704 F.Supp at 1425-27; Honickman, 5 Trade Reg. Rep. at 22, 964-65. In Ivaco, for example, the court noted that there was no evidence that the joint ventures seriously considered the less anticompetitive alternatives nor attempted to explain why the alternatives were impractical or even unattractive.

20. See, *e.g.*, University Health, 938 F.2d at 1223; Rockford Memorial, 717 F. Supp at 1289-1291; American Medical Int'l, 104 FTC at 219-20. See also ABA, *supra* note 5, at 320; PITOFSKY, *supra* note 7, at 213 n. 64.

21. See US Department of Justice and Federal Trade commission, Horizontal Merger Guidelines § 4 (April 2, l992), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104 (hereinafter "1992 Merger Guidelines"). FTC staff has argued that efficiencies may be considered in the Commission's prosecutorial decision but cannot be asserted as a defence. See Brief for the Federal Trade Commission in FTC v. University Health, Inc., No. 91-8308 at 32 (11th Cir. filed Apr. 24 1991).

22. The burden of proof with respect to efficiencies resides with the proponents of the merger. *Id*. § 0.1 n.5.

23. *Id*. § 4. While the Guidelines provide no further guidance on the relative merits of these various types of efficiencies, some commentators have discussed this subject. See, *e.g.*, PITOFSKY, *supra* note 7, at 216-218.

24. 1992 Merger Guidelines, *supra* note 21, § 4.

25. *Id*. The Merger Guidelines presume that most mergers will achieve a certain level of efficiencies, and, therefore, efficiency claims are only pertinent where the parties can show they exceed what is normally expected from a merger. See, *e.g.*, Mary Lou Steptoe, "Efficiency Justifications for Hospital Mergers," Address before Practising Law Inst. 9 (July 20, l994).

26. Steptoe, *supra* note 25, at 9.

27. *Id*.

28. *Id*.

29. In addition to the Supreme Court and FTC cases discussed *infra*, for the most recent statement of enforcement policy of the FTC and Department of Justice, see US Department of Justice and Federal Trade Commission, Antitrust Guidelines for the Licensing of Intellectual Property

("Intellectual Property Guidelines") §§ 3.4, 5.1 (1995), reprinted in Special Supplement to Antitrust & Trade Reg. Rep. (BNA) No. 1708 (April 13, l995).

30. See, *e.g.*, *id*. § 3.4.

31. 441 US 1 (l979).

32. *Id*. at 19-20.

33. *Id*. at 20-21.

34. 457 US 332 (1982).

35. *Id*. at 295.

36. See also ARQUIT and KATTAN, "Efficiency Considerations and Horizontal Restraints", 36 *Antitrust Bull.* 717, 721 (l991).

37. See, *e.g.*, Intellectual Property Guidelines, *supra* note 29, § 5.1. For other cases illustrating cognizable efficiencies, see ARQUIT and KATTAN, *supra* note 36, at 722-725.

38. See, *e.g.*, FTC v. Indiana Federation of Dentists, 476 US 447 (l986); National Collegiate Athletic Ass'n ("NCAA") v. Board of Regents of the Univ. of Okla., 468 US 85 (l984).

39. 468 US 85 (l984).

40. *Id*. at 113-117.

41. See, *e.g.*, Nat'l Society of Professional Engineers v. United States, 435 US at 692; NCAA, 468 US at 109-110; Indiana Federation of Dentists, 476 US at 460-461; Chicago Professional Sports Ltd. Partnership v. National Basketball Ass'n, 961 F.2d 667, 674 (7th Cir.), cert. denied, 113 S.Ct 409 (1992); United States v. Brown University, 5 Fed.3d 658, 669 (1993).

42. For a general discussion of the development of the truncated rule of reason, see LANGENFELD, SILVIA, and WINSLOW, "Nonprice Horizontal Restraints in Antitrust Laws and Trade Regulation", Ch. 19 (J. VON KALINOWSKI, ed. l995).

43. See Intellectual Property Guidelines, *supra* note 29, §§ 3.4, 5.1.

44. 94 FTC 701, aff'd sub nom. American Medical Ass'n v. FTC, 638 F.2d 443 (2d Cir. l980), aff'd by an equally divided Court, 455 US 676 (l982).

45. 110 FTC 549 (l988).

46. 111 FTC 417 (l989), aff'd in part and remanded sub. nom. Detroit Auto Dealers Ass'n, Inc. v. FTC, 955 F.2d 457 (l992).

47. See University Health, 938 F.2d at 1222 n. 30.

48. *Id*. See also PITOFSKY, *supra* note 8, at 218-221.

ANNEX

F.T.C. v. UNIVERSITY HEALTH, INC.
Cite at 938 1206 (11th Cir. 1991)

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[16,17] The appellees argue that the proposed acquisition would generate significant efficiencies and, therefore, would not substantially lessen competition. The FTC responds that the law recognizes no such efficiency defense in any form. We conclude that in certain circumstances, a defendant may rebut the government's prima facie case with evidence showing that the intended merger would create significant efficiencies in the relevant market. Here, however, the appellees have failed to introduce sufficient evidence to demonstrate that their transaction would yield any efficiencies, and the district court's factual finding to the contrary is clearly erroneous. Accordingly, the appellees may not rely on an efficiency defense.

The Supreme Court stated in FTC v. Procter & Gamble Co., 886 U.S. 568, 87 S.Ct. 1224, 18 L.Ed.2d 303 (1967)(Clorox), that '[p]ossible economies cannot be used as a defense to illegality" in section 7 merger cases. *Id.* at 579, 87 S.Ct. at 1224; see also Philadelphia Nat'l Bank, 374 U.S. at 371, 83 S.Ct. at 1745 ('We are clear...that a merger the effect of which 'may be substantially to lessen competition' is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial.'); Brown Shoe Co. v. United States, 370 U.S. 294, 344.82 S.Ct. 1502, 1534, 8 L.Ed.2d 510 (1962). Courts and scholars have debated the meaning of this precedent. Some argue that the Court completely rejected the use of efficiency evidence by defendants in section 7 cases. *See RSR Corp. v. FTC.* 602 F.2d 1317, 1325 (9th Cir.1979) ('RSR argues that the merger can be justified because it allows greater efficiency of operation. This argument has been rejected repeatedly.'), cert. denied, 445 U.S. 927, 100 S.Ct. 1313, 63 L.Ed.2d 760 (1980); Fisher & Lande, Efficiency Considerations in Merger Enforcement, 71 Calif. L.Rev. 1580, 1595 (1983). Others posit that the Court merely rejected the use of insufficient or speculative evidence to demonstrate efficiencies; a limited efficiency defense to the government's prima facie case, they argue, remains available. See P. Areeda & D. Turner, *supra* p.22 ¶ 941b. at 154 ("To reject an economies defense based on mere possibilities does not mean that one should reject such a defense based on more convincing proof.'); Murris, The Efficiency Defense Under Section 7 of the Clayton Act, 30 Case W. Res.L.Rev. 381, 412-13 (1990).

It is clear that whether an acquisition would yield significant efficiencies in the relevant market is an important consideration in predicting whether the acquisition would substantially lessen competition[1]. Market share statistics, which the government uses to make out a prima facie case under section 7, are not an end in themselves; rather, they are used to estimate the effect an intended transaction would have on competition. Thus, evidence that a proposed acquisition would create significant efficiencies benefiting consumers is useful in evaluating the ultimate issue - the acquisition's overall effect on competition. We think, therefore, that an efficiency defense to the government's prima facie case in section 7 challenges is appropriate in certain circumstances[2].

[18] We recognize, however, that it is difficult to measure the efficiencies proposed transaction would yield and the extent to which these efficiencies would be passed on to consumers. See R. Bork, *supra* note 30, at 127; R. Posner, *supra* note 30, at 112 ('The measurement of efficiency...[is] an intractable subject for litigation.'); Fisher & Lande, *supra* p. 26, 1670-77; see also U.S. Dep't of Justice, Merger Guidelines § V.A., 4 Trade Reg. Rep. (CCH) ¶ 13,102, at 20,542 (1982) (claims about expected efficiency gains are 'easier to allege than to prove'); cf. L. Sullivan, *supra* note 30, § 204, at 631. Moreover, it is difficult to

calculate the anticompetitive costs of an acquisition against which to compare the gains realized through greater efficiency; such a comparison is necessary, though, to evaluate the acquisition's total competitive effect. Because of these difficulties, we hold that a defendant who seeks to overcome a presumption that a proposed acquisition would substantially lessen competition must demonstrate that the intended acquisition would result in significant economies and that these economies ultimately would benefit competition and, hence, consumers.[3] As Justice Harlan, concurring in Clorox, explained: 'Economies cannot be premised solely on dollar figures, lest accounting controversies dominate § 7 proceedings. Economies employed in defense of a merger must be shown in what economists label 'real' terms.' 386 U.S. at 604, 87 S.Ct. at 1243. To hold otherwise would permit a defendant to overcome a presumption of illegality based solely on speculative, self-serving assertions.

[19] The appellees here have not presented sufficient evidence to support their claim that the intended acquisition would generate efficiencies benefiting consumers. The district court, in finding that the proposed acquisition would result in a 'number of efficiencies,' admitted that its finding was based on the appellees' 'speculation.' The appellees simply concluded that the intended acquisition would reduce 'unnecessary duplication' between University Hospital and St. Joseph; they then approximated, in dollars, the savings these efficiencies would produce. They did not specifically explain, however, how these efficiencies would be created and maintained. In the end, the court concede that 'on one can tell at this point what all of [the efficiencies] are or are not.' Clearly, the district court's conclusion is not well grounded in fact; while the proposed acquisition may produce significant economies, the appellees simply failed to demonstrate this[4]. Therefore, although we hold that an efficiency defense (the scope of which we do not discuss here, see *supra* note 30) may be used in certain cases to rebut the government's prima facie showing in a section 7 challenge, the appellees may not rely on this defense because they failed to demonstrate that their proposed acquisition would not yield significant economies.

NOTES

1. Of course, once it is determined that a merger would substantially lessen competition, expected economies, however great, will not insulate the merger from a section 7 challenge. See Clorox, 386 U.S. at 579, 87 S.Ct. at 1231 ("Congress was aware [when it enacted section 7] that some mergers which lessen competition may also result in economies but it struck the balance in favor of protecting competition."); Philadelphia Nat'l Bank, 374 U.S. at 371, 83 S.Ct. at 1745-46 ("Congress determined to preserve out traditionally competitive economy. It therefore proscribed anticompetitive mergers, the benign and the malignant alike, fully aware, we must assume, that some price might have to be paid.").

2. It is unnecessary for us to define the parameters of this defense now; as we explain *infra*, the appellees failed to demonstrate that the proposed acquisition would generate significant efficiencies. We note, however, that it may further the goals of antitrust law to limit the availability of an efficiency defense, even when a defendant can demonstrate that its proposed acquisition would produce significant efficiencies. For example, it might be proper to require proof that the efficiencies to be gained by the acquisition cannot be secured by means that inflict less damage to competition, such as internal expansion or merger with smaller firms. For various suggestions on the proper scope of an efficiency defense, see MURRIS, *supra* p.26,426-31 (advocating absolute efficiency defense); P. AREEDA & D. TURNER, *supra* p. 1221, ¶ ¶ 939-62 (advocating partial defense limited to types of efficiencies); L. SULLIVAN, *Handbook of the Law of Antitrust* § 204, at 631 (1977) (advocating partial defense limited only by evidentiary standard); ROGERS, *The Limited Case for an Efficiency Defense in Horizontal Mergers*, 58 *Tul.L.Rev.*503, 521-25, 528 (1983) (advocating partial defense for merger between two small firms in market dominated by large firms). Some scholars advocate placing the efficiency issue before enforcement agencies rather than courts. See, *e.g.*, WILLIAMSON, "Economies as an Antitrust

Defense Revisited", 125 *U.Pa.L.Rev.* 699, 729-31 (1977) (proposing that the Justice Department and the FTC consider efficiencies but not the courts). Others have suggested that enforcement 2.agencies simply take efficiencies into account by increasing the level of market concentration at which a merger is challenged, rather than engaging in case-by-case weighing of efficiencies. Fisher & Lande, *supra* p. 1222, at 1670-77; R. BORK, *The Antitrust Paradox: A Policy at War with Itself* 129 (1978); R. POSNER, *Antitrust Law: An Economic Perspective* 112-13 (1976).

3. The Department of Justice and the FTC, in deciding whether to challenge a merger, require the same threshold showing. See Merger Guidelines, *supra* note 12, § 3.5, ¶ 13,103, at 20,564.

4. Nor did the appellees compare the benefits they expect to realize from the alleged efficiencies with the costs the intended acquisition may exact on competition. It is difficult, then, to conclude with any reliability that the acquisition ultimately would aid, rather than hinder, competition and consumers.

ANNEX 2

Federal Trade Commission Hearings
on Global and Innovation-Based Competition

Day 9 (Nov. 2) (Thurs.)

Efficiencies (General)

AM: What Efficiencies Matter Most to Various Industries? Up to What Point Can Firms Benefit From Economies of Scale or Scope (9:30 am - 12:00 pm)

* Alliance for Managed Care
David Pitts (Pitts Management Associates)

PM: Should Antitrust Enforcers View Certain Efficiencies as More Important Than Others in Promoting Market Competition? Are Some Efficiencies too Difficult to Measure or Subject to Manipulation by Private Parties? Should Enforcers Seek to Ensure That Efficiencies From a Merger Are Passed On to Consumers? (1:30 pm - 3:00 pm)

W. Dale Collins (Shearman & Sterling)
James Egan (Rogers & Wells)
Ann Jones (Blecher & Collins)
Professor Steven Salop (Georgetown University)

PM: What Can We Learn From Foreign Competition Regimes About the Extent To Which Enforcers Should Weigh -- or Can Measure -- Efficiencies or Other Public Benefits, Particularly in Mergers? (3:00 pm - 4:30 pm)

Francine Matte (Senior Deputy Director, Bureau of Competition Policy, Canada)
Margaret Sanderson (Bureau of Competition Policy, Canada)
Mexican representative, Federal Competition Commission
* Professor Eleanor Fox (NYU)

Day 10 (Nov. 7) (Tues.)

Efficiencies in Light of Global Competition and Innovation

AM: How Businesses Value and Achieve Efficiencies; Whether Antitrust Law Impedes Businesses' Efforts to Obtain Efficiencies (9:30 am - 11:30 am)

Richard Scott (President, HCA Healthcare Corp.)
* Norman R. Augustine (President, Lockheed/Martin Corp.)
* Ronald Stern (General Electric Co.)
Grocery Manufacturers Association

PM: Whether Antitrust Enforcers Should Adjust Current Enforcement Policy Regarding Efficiencies; Whether a More Skeptical Approach is Warranted if Claimed Efficiencies Are Difficult to Measure; What is Required to Show That Comparable Savings Can Reasonably Be Achieved Through Other Means? (1:30 pm - 4:30 pm)

Kevin Arquit (Rogers & Wells)
Terry Calvani (Pillsbury, Madison & Sutro)
Professor Harvey Goldschmid (Columbia University)
Joseph Kattan (Morgan, Lewis & Bockius)
Professor Robert Lande (Univ. of Baltimore)
Professor Timothy Muris (George Mason Univ.)
Kevin O'Connor (Ass't Att'y General, Wisconsin, chair, NAAG Multistate Task Force)

CONTRIBUTION FROM THE EUROPEAN COMMUNITY

Efficiency issues occur in two areas of the European Commission's competition cases. Article 85 of the Treaty of Rome covers co-operative agreements - including co-operative joint ventures typically where the parent companies remain on the market in which the joint venture operates. Concentrations - which include concentrative joint ventures where the parents withdraw from the joint venture's market as well as true mergers and acquisitions - are considered under the Merger Regulation. The treatment of efficiency differs between these legal instruments.

The prohibition of anticompetitive agreements and concerted practices in Article 85(1) is tempered by Article 85(3), i.e. the possibility of an exemption where the agreements also bring about economic benefits, such as to contribute to improving the production or distribution of goods or to promoting technical or economic progress. The benefits must outweigh the reduction in competition in order to qualify for an exemption. Thus, in the context of cooperative agreements the Treaty clearly provides for an efficiency defence. The criteria mentioned in Article 85(3), i.e. improving production/distribution or promoting technical/ economic progress, can be summarised as efficiency gains and, taking into account that the burden of proof is with the companies, the term "defence" is appropriate. The efficiency defence of 85(3) finds its explanation in the prohibition principle which does not allow for a rule of reason within Article 85(1) itself.

However, there is a clear limit for the efficiency defence: the elimination of competition. Therefore, even if the parties can prove that an agreement would bring about high efficiency gains, these efficiencies are not able to justify an elimination of competition. Basically, 85(3) provides for a kind of a "sliding scale": the more competition is restricted by means of a cooperative agreement the higher the efficiency gains have to be in order to qualify for an exemption - up to the limit where effective competition is eliminated (or a substantial part of the products concerned).

This general rule is an implementation of the basic principles of the treaty, mainly Article 2 and 3 (and newly introduced Article 3a). Thus, one of the means of attaining the goals and tasks of the Community mentioned in Article 2 is "a system ensuring that competition in the internal market is not distorted" (Article 3g). The Court has ruled that these basic principles in Articles 2 and 3 are merely given concrete expression in Articles 85 and 86. The Court furthermore ruled that the competition rules are designed to maintain "effective competition". Consequently, maintaining effective competition is the decisive criterion. The requirement that competition must remain effective is of such an essential nature that without it many provisions of the Treaty would become pointless.

This basic philosophy does not only apply within the context of 85(3), it is also the reason for the dominance test under the Merger Regulation. This test within the Merger Regulation for the prohibition of a concentration is the creation or strengthening of a dominant position, a test which requires a very high burden of proof as is shown by the one per cent prohibition rate amongst cases considered under the Merger Regulation. There is no real legal possibility of justifying an efficiency defence under the Merger Regulation. Efficiencies are assumed for all mergers up to the limit of dominance - the "concentration privilege". Any efficiency issues are considered in the overall assessment to determine whether dominance has been created or strengthened and not to justify or mitigate that dominance in order to clear a concentration which would otherwise be prohibited.

Article 86 has a dominance-test governing the abusive behaviour of firms. Although concerning behavioural control and therefore serving a different purpose than merger control, Article 86 is also based on the philosophy described above. If dominance is already existent on a market, i.e. competition is already very fragile, the aim is to preserve at least the little degree of remaining competition. Therefore, the abuse

of a dominant position is not tolerable, even if efficiency gains could be demonstrated. There is thus no efficiency defence to an abuse committed by a dominant firm.

Elimination of competition as the threshold of Article 85(3) amounts to dominance. Dominance is the absolute limit. Since the upper limit is dominance which is a strong possibility from a market share of about 40-45 per cent, the Commission is unlikely to grant exemption in cases that approach these market shares.

As already mentioned, restrictions which do not eliminate competition can be outweighed by efficiency gains. These efficiency gains have to be shown, statements or mere claims are not sufficient. The more restrictive agreements are, the higher is the requirement for efficiency gains. Price and quota fixing as well as market sharing agreements hardly bring about any efficiencies. However, even if the companies could - theoretically - demonstrate some efficiencies like cost savings, this would not normally be sufficient to outweigh these severe forms of competition restrictions.

In conclusion, therefore, it can be said that though efficiency considerations are taken into account under European competition law, their application is clearly constrained. Under Article 85, any agreement which restricts competition will have to demonstrate efficiency benefits in direct proportion to the degree of competition which is restricted. Under cases brought under Article 86 and those notified under the Merger Regulation, by contrast, the Commission has a dominance test and efficiency gains will not justify the abuse of a dominant position (Article 86) and may not justify the creation or strengthening of a dominant position as a result of which effective competition would be significantly impeded (Article 2(2) Merger Regulation).

ANNEX

CASE STUDIES

MERGER REGULATION

Aerospatiale-Alenia/de Havilland[1] (1991)

This case concerned the proposed acquisition by Aerospatiale and Alenia (who had combined their regional aircraft activities into a joint venture ATR) of the de Havilland division of Boeing. De Havilland produced turboprop aircraft. The parties in the de Havilland case claimed an efficiency defence as a justification for the merger. This was rejected by the Commission in its prohibition decision.

The Commission argued that the cost savings (of about 0.5 per cent of the turnover of combined operations of ATR and de Havilland) were insufficient to contribute to the development of technical and economic progress within the meaning of Article 2(1)b of the Merger Regulation. Furthermore, even if there was such progress, the Commission did not judge that it would be to the consumer's advantage. The analysis did offset the static efficiency gains to the parties against both the loss of consumer welfare and the longer term possibilities for technical progress which would have been afforded by the merger.

MSG Media Service (1994)

In MSG Media Service[2] the parties claimed (unquantified) gains from the operation. The operation involved the creation of a joint venture company to handle the technical, business and administrative handling of digital pay TV services. The three parent companies were Bertelsmann and Kirch, both of which are major German media groups and Deutsche Telekom, the monopoly telecommunications provider in Germany. Each of the parents had activities upstream of those of the joint venture.

The Commission rejected the parties' arguments saying that even if the operation were to contribute to technical and economic progress, Article 2(1)(b) goes on to state that no obstacle must be formed to competition. This was clearly not so in this case as the joint venture would seal off the market for technical and administrative services. The Commission went on to say that the hindering of competition in this case made even the achievement of technical and economic progress questionable because of the deterrent effect of the operation to future entrants into the market.

Nordic Satellite Distribution[3] (1995)

Nordic Satellite Distribution (NSD) concerned the distribution of satellite TV to the Nordic area. NSD was envisaged as a joint venture between TeleDanmark, the public Danish telecom operator, Telenor, the public Norwegian telecom operator, and Kinnevik, a Swedish industrial group with large interest in media and in possession of some of the most popular TV programmes in the Nordic countries.

The operation would have created a highly vertically integrated structure ranging from programme provision via satellite capacity to cable TV networks. NSD would undoubtedly have involved significant efficiencies. However, it would also have resulted in the parties achieving or strengthening dominant

positions on several markets. The Commission in the end decided to prohibit the operation, since the anti-competitive effects of the operation were not deemed necessary for the achievement of the efficiencies.

Article 85

BT/MCI (1994)

This strategic alliance in the telecom area concerned among others the acquisition of a stake of 20 per cent in MCI by British Telecom and the creation of a joint venture in the field of value added services. The joint venture was found to come under 85(1) because the parent companies were assessed to be competitors, but got an individual exemption.

It was considered that the joint venture would offer new global services more quickly and of a more advanced nature than either BT or MCI alone. Furthermore, cost reductions were taken into account. There was no risk of elimination of effective competition. In this context the Commission took particular account of the evolving nature of the telecommunications market due to technical progress and the process of liberalisation.

Exxon/Shell (1994)

This case concerned a joint production company in the petrochemical industry. Because the parent companies were competitors and remained active as independent producers and sellers of the same or similar products, the joint venture was caught by Article 85(1). However, it could be exempted due to the fact that the technology used by the joint venture provided a high degree of flexibility and efficiency. Customers would be encouraged to convert ageing extrusion equipment and to take advantage of the superiority of linear polyethylene over conventional polyethylene. It was assessed that the agreement did not afford the parties the possibility to eliminate competition due to an overall market share of the parties of about 22 per cent with regard to the products concerned.

Ford/Volkswagen (1992)

The joint venture of Ford and Volkswagen for the development and production of a "multi purpose vehicle" was caught by Article 85(1) because the parties were potential competitors and the exchange and sharing of know how could affect the competitive behaviour of the two partners in neighbouring markets. Main reason for the exemption was that the cooperation allowed the partners to complement one another as to their engineering resources and technical expertise which would rationalise production and promote technical progress. Because of the strong position of Renault ("Espace") and foreseeable further penetration of this segment by Japanese producers there was no risk of elimination of competition.

Optical fibres (1986)

This case concerned various agreements and joint ventures between Corning, the inventor of optical fibres for telecommunication, and several cable producers (eg. BICC, Siemens). The parallel existence of joint ventures with Corning as a partner and the common technology source in an oligopolistic market was seen as a restriction of competition. However, the agreements were exempted because the advanced technology made a quick conversion to this technology possible and would increase the global competitiveness of European industry. Due to competitive pressure from inside and outside the Community the agreements did not bring about the elimination of competition.

NOTES

1. Case IV/M.053 in OJ L 334 of 5.12.91.

2. Case No. IV/M.469 - OJ L 364 of 31.12.94.

3. Case No. IV/M.490, decision of 19.07.1995, in print.

CONTRIBUTION FROM BIAC

The Treatment of Efficiency Gains in Canadian Merger Analysis[1]

This report briefly summarizes the treatment of efficiency gains in Canadian merger analysis. Section 96 of the Competition Act (Canada) (the "Act") is unique among competition/antitrust statutes around the world, in that it provides parties to an anti-competitive merger with the ability to avoid the issuance of an order (*e.g.*, for divestiture or dissolution) by establishing that the efficiency gains likely to result from the merger will be greater than, and will offset, the effects of any prevention or lessening of competition resulting from the merger. As the Canadian Merger Enforcement Guidelines ("MEGs") explain in considerable detail,[2] the Director of Investigation and Research (the "Director") under the Act views section 96 as contemplating a "total welfare" balancing process. However, this interpretation has been questioned in non-binding comments of the (now former) Chairperson of the Competition Tribunal, whose observations suggest sympathy for a "consumer welfare" approach to section 96.[3]

While the differences between the two approaches are substantial in theory,[4] the experience with section 96 has, for all intents and purposes, deprived the ongoing debate of any practical significance. To date, not a single merger in the ten-year history of section 96 has been permitted to proceed by virtue of having met the requirements of that provision. This makes it difficult to recommend, without qualification, that other jurisdictions whole-heartedly embrace a similar statutory exception.

The difficulties encountered with section 96 to date may have more to do with the evidentiary burden than with the statutory language *per se*. Merging parties bear the responsibility of establishing, on the balance of probabilities: *(i)* that the various claimed efficiency gains are likely to result from the merger; and *(ii)* that those efficiency gains would not likely be achieved in an alternative way if an order were made in respect of the merger. This has proven to be an exceedingly difficult burden to meet at the pre-merger stage. In Part III of this report, several reasons for adopting a lower evidentiary burden in respect of efficiencies, where the objective is to maximize total welfare, are identified. The adoption of a lower evidentiary burden, similar to that which has been adopted in Australia and New Zealand, would likely breathe significant life into section 96 and make it much more relevant to merger review in Canada. Similarly, the adoption of the suggested evidentiary threshold by other jurisdictions contemplating the adoption of an approach similar to Canada's would help to ensure that any new statutory provision that may be adopted will have more relevance than section 96 has had to date.

Where the goal of maximizing total welfare is rejected in favour of the alternative objective of maximizing consumer welfare, the U.S. approach to efficiencies in merger review is superior to the approach suggested in the Competition Tribunal's non-binding remarks, (i.e., adjusting the Canadian trade-off approach by incorporating wealth transfers into the analysis).[5]

The choice between the total welfare and consumer welfare frameworks not only has important implications for the broad approach to efficiencies, but also for the manner in which several key issues arising in the context of merger review are treated.

The Canadian Approach to Efficiencies

When a determination has been made by the Competition Tribunal that a merger is likely to prevent or lessen competition substantially, merging parties can avoid being subjected to an order for

dissolution, divestiture or other relief by meeting the requirements of the efficiency "exception" set forth in section 96 of the Act. Section 96 provides:

> 96.(1) The Tribunal shall not make an order under section 92 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.
>
> 96.(2) In considering whether a merger or proposed merger is likely to bring about gains in efficiency described in subsection (1), the Tribunal shall consider whether such gains will result in
>
> *(a)* a significant increase in the real value of exports; or
>
> *(b)* a significant substitution of domestic products for imported products.
>
> 96.(3) For the purposes of this section, the Tribunal shall not find that a merger or proposed merger has brought about or is likely to bring about gains in efficiency by reason only of a redistribution of income between two or more persons.

The Director interprets section 96 as contemplating a balancing process that resembles, in very general terms, Williamson's "naive" trade-off model.[6] Generally speaking, as described in considerable detail in the MEGs, the Director and his staff at the Bureau of Competition Policy (the "Bureau") estimate the likely increase in producers' surplus resulting from anticipated efficiency gains and then balance that estimate against the estimated "deadweight loss" to the Canadian economy that is expected to result from the price increase and corresponding output reduction that is believed will be brought about by the merger.[7] The likely wealth transfer from buyers (or sellers) to the merged entity is treated as a wash, (i.e., is not given any weight in the analysis), and efficiencies do not have to be passed on to consumers.

This approach occupies the middle ground between the approach of jurisdictions such as the E.U., where, it appears, merging parties are invited "to claim some efficiencies so that the Merger Task Force will have a more friendly attitude towards their merger",[8] and the approach of the U.S. Department of Justice ("DOJ"), which appears to require efficiency gains to be so great that prices will not rise as a result of the merger (i.e., because the merged entity's profit maximizing level of output will correspond to a price that is at or below the pre-merger price).[9]

In the EEC and certain other jurisdictions[10] in which efficiencies may be given weight, there does not seem to be any balancing of detailed estimates of efficiencies and anti-competitive effects. Instead, efficiencies appear to be considered either in broad terms together with other factors in deciding whether a given merger should be challenged, or in the exercise of enforcement discretion. In the U.S., there does not appear to be any formal trade-off analysis, because efficiencies have to be so great that there are no material anti-competitive effects of the merger. (However, statements by former senior antitrust officials, such as former Assistant Attorney General James Rill and former FTC Bureau of Competition Director Kevin Arquit, suggest that the DOJ and FTC will consider tolerating a short-run price increase if there is sufficient evidence that prices will fall in the longer run to below the pre-merger level.)[11] There does not appear to be anything on the public record which indicates that there have been any otherwise anti-competitive mergers which have been permitted to proceed solely on this basis.[12]

Whereas section 96 of the Act clearly subordinates the policy objective of competitive prices to the goal of enhanced efficiency (where the effects of increased prices on total welfare are likely to be outweighed by the efficiency gains likely to be brought about by the merger),[13] it appears that the

paramount policy goal underlying U.S. merger policy is the prevention of wealth transfers, i.e., the maximization of consumers' surplus (also sometimes referred to as consumer welfare). For this reason, there is no need for a trade-off between efficiencies and anti-competitive effects in U.S. merger policy.

The efficiency gains assessed by the Bureau pursuant to section 96 fall into two broad classes: production efficiencies and dynamic efficiencies. These are described Appendix 2 of the MEGs.

Subsection 96(3) and the last clause in subsection 96(1) eliminate two broad classes of gains from consideration in the balancing assessment:

(i) gains that would likely be brought about by reason only of a redistribution of income between two or more persons; and

(ii) gains that would likely be attained even if the order that would be required to remedy the anti-competitive effects of the merger were made.

With respect to *(i)*, these gains are excluded on the basis that they are mere pecuniary gains that do not represent a real saving in resources. The MEGs indicate that the following classes of gains are generally excluded from consideration on this basis: tax-related gains; savings that flow from a reduction in output, quality or variety; revenues resulting from a price increase; and gains resulting from the exercise of increased bargaining leverage. However, gains that can be expected to be realized as a result of the fact that a supplier or distributor will pass resource savings (attributable to increased order size, etc.) on to the merged entity will not be excluded from consideration.

With respect to the second category of gains excluded from the trade-off analysis, as suggested by the language at *(ii)* above, it is not necessary for the merging parties to establish that claimed efficiencies could not be attained in any other way. All that must be established is that the efficiencies would not likely be realized if the order in question (*e.g.*, to block all or part of the merger) were made. Where only part of a merger raises significant antitrust issues, any order sought will likely be confined to the relevant market in which those issues are raised. If the rest of the merger proceeds, efficiencies in the markets not targeted by the order are unlikely to be prevented by the order, unless they are economies of scope or other sources of savings that are inextricably related to the efficiencies in the relevant market that will be blocked by the making of the order. If efficiencies expected to arise in other markets would not likely be prevented by the order, they are not considered by the Director in the section 96 balancing process,[14] as they would not represent a "cost" to society of making the order.

The MEGs also state that efficiency gains that would likely be attained through alternative means if the order is made cannot be attributed to the merger and cannot be considered to represent a "cost" to society of making the order. The alternative means typically canvassed by the Bureau include internal growth (within the reasonably foreseeable future), a merger with a competitively preferable third party which has expressed a serious interest in merging with the seller, a joint venture, a specialization agreement, or a licensing, lease or other contractual arrangement.[15]

Given that efficiency gains are only included in the balancing process if they "would not likely be attained if the order were made", the commercial realities of the relevant market are considered in evaluating whether one or both of the merging parties would likely pursue the attainment of all or some of the claimed efficiencies if the merger were challenged and an order were made. Unlike the approach that the DOJ took in the Archer-Daniels-Midland case,[16] and that appears to be reflected in statements by the FTC,[17] efficiencies are not excluded from the section 96 trade-off assessment on the basis that they could be attained in some other way, *e.g.*, on the basis that there might be "other plausible efficiency enhancing transactions".[18] The MEGs make it clear that the Director will not go on a fishing expedition in search of other possible or even plausible ways of attaining efficiencies, and that efficiencies will only be excluded from the balancing process where they can reasonably be expected to be attained in an

alternative way. Accordingly, "[i]f the common industry practice is such that the alternative in question would not likely be resorted to if an order were made, the efficiencies in question will ordinarily be included in the balancing process".[19] However, the onus will be on the merging parties to provide "a reasonable and objectively verifiable explanation of why efficiencies that are available would not likely be sought if the order were made".[20]

Once a determination has been made of what gains should or should not be considered in the trade-off analysis, the balancing process can begin. Subsection 96(1) requires a finding that the gains "will be greater than, and will offset, the effects of any prevention or lessening of competition" that is likely to result from the merger. The Director's position is that "effects" means resource allocation effects. Accordingly, it is not the value of the price increase multiplied by the number of units sold (area C on Diagram 1, at Appendix 1) that is the measure of anti-competitive "effects" resulting from the merger, but rather the negative resource allocation effect (area D on Diagram 1) that is attributable to the price increase and the corresponding output reduction. This effect is generally referred to as the deadweight loss to the economy as a whole, because it is lost to consumers and gained by no one. (As noted earlier, the wealth transfer from consumers to producers is not included among the anticompetitive effects of the merger, because it is neutral from a total welfare perspective.)

Before resigning as chairperson of the Tribunal, Madame Justice Reed indicated in *obiter dictum* remarks in the Hillsdown case that she had "difficulty accepting" the Director's position with respect to wealth transfers, although she did not endorse any particular alternative approach.[21] This position, together with certain other comments in the decision, reflect a consumer-oriented view of section 96.[22] For example, the Tribunal observed that "[t]o the extent that the efficiency gains would likely lead to lower prices for consumers this would likely be determinative".[23] In response, the Director observed: "... if Parliament's desire had been to deny the possibility of any price impact on consumers by giving consideration to the wealth transfer effects of a merger, then this presumably would have been specified in the language of the section."[24] Goldman and Bodrug have added:

> [I]t is difficult to imagine circumstances in which a merger which is likely to lead to lower prices could be considered likely to lessen competition substantially in the first place, and if there is no likely substantial lessening of competition, then resort to the efficiency exception would not be necessary.[25]

One of the arguments in support of the Director's interpretation of section 96 is that Parliament clearly intended section 96 to play an important role in Canadian merger policy,[26] and that if section 96 were interpreted to contemplate the inclusion of wealth transfer effects against a merger it there would rarely, if ever, be a meaningful role for section 96 to play. This is because it would be virtually impossible for merging parties to meet the requirements of section 96. The combined effect of the deadweight loss and the wealth transfer typically far exceeds in order of magnitude any efficiencies which may be brought about by a merger. The Tribunal responded to this argument by stating: "Whether this is the case or not is not a matter which can be determined on the evidence given in this case."[27] The Director responded by stating that he was not aware of any merger that would have generated efficiencies sufficient to outweigh the sum of the likely wealth transfer and deadweight loss of the merger, and that he did not believe that such a merger will likely present itself in the future.[28] He also noted that since the Tribunal's treatment of efficiencies was *obiter dictum* (non-binding), "there appears to be no requirement to revise the Guidelines at this time".[29]

The MEGs acknowledge that the calculation of the likely anti-competitive effects of mergers is generally very difficult to make, particularly with respect to the measurement of losses related to a reduction in service, quality, variety, innovation and other non-price dimensions of competition. As a result "several trade-off assessments are ordinarily performed over a range of price increases and market demand elasticities". For example, the analysis might be performed with respect to price increases of 3 per cent, 5 per cent and 10 per cent, assuming demand elasticities of 0.5, 1, 1.5 and 2. If the trade-off is only likely

to be unfavourable for the merging parties where the price increase and the demand elasticity are both at the upper extremes of these ranges, and if this scenario is unlikely, it would be surprising if the merger were challenged.

The provision in subsection 96(2) that requires account to be taken of whether the gains in efficiency discussed above ["gains in efficiency described in subsection (1)"] will result in:

(a) significant increase in the real value of exports; or

(b) a significant substitution of domestic products for imported products

is not considered to add anything significant to the analysis. From a legal perspective, the words "gains in efficiency described in section 1" seem to indicate that the subsection does not contemplate an expansion of the class of gains to be considered in the balancing process. Apparently, there was never any intention on the part of the drafters of subsection 96(2) that this provision have any significant role in the trade-off assessment. The MEGs provide that this provision:

> ...is simply considered to draw attention to the fact that, in calculating the merged entity's total output for the purpose of arriving at the sum of unit and other savings brought about by the merger, the output that will likely displace imports, and any increased output that is sold abroad, must be taken into account.[30]

The Canadian Experience - Lessons Learned

Notwithstanding the fact that the Canadian approach (as interpreted in the MEGs) is much more advantageous to merging parties than what appears to be the approach of the DOJ and the FTC, it appears that only one merger reviewed by the Director since 1986 has satisfied the total welfare test contemplated by section 96.[31] However, after the trade-off analysis was performed, and before the Director's final decision, new information came to light which led to the conclusion that the merger would not likely result in a substantial lessening of competition. As a result, there still has not been a single case in the decade since section 96 came into existence where that provision has had a role to play in Canadian merger policy.[32] This experience makes it difficult to recommend that the Canadian model be embraced without reservation by other jurisdictions.

The Canadian experience with a total welfare-oriented statutory efficiency exception may have been better if the requirement that efficiencies be proved on the balance of probabilities had not been strictly enforced.[33] It is typically very difficult to prove that efficiencies will likely materialize (let alone that they clearly and convincingly will be attained). CEOs and other decision-makers often pursue a merger initiative on the basis of a general sense of the synergies likely to be attained, and of the "fit" between the two firms, without ever having completed a detailed assessment of all or even most of the potential sources of efficiency gains and of the extent to which they are more or less probable. Even when such studies have been performed, there may be other factors that will affect the probability that particular efficiencies will be attained.

If one is truly interested in maximizing total welfare, it is inappropriate to require that efficiencies be strictly proved on the balance of probabilities. This is because: *(i)* efficiencies are ordinarily the principal source of any increase in total welfare that may be brought about by a merger, *(ii)* they are inherently uncertain in nature and, most importantly, *(iii)* over time they are likely to dwarf any static losses in consumers' surplus that may result from the merger (particularly where the efficiencies have a reasonable chance of increasing innovation).[34] Rather, the standard that has been adopted in New Zealand would appear to be better. There, all that must be established is "a tendency or real probability", rather than it being "more probable than not" that claimed public benefits will materialize.[35] In short, it is recommended

that if the Canadian model is embraced by other jurisdictions, it should be adjusted to reflect this lower evidentiary threshold. (It may be noted that if the policy objective is to maximize consumers' surplus, it is much more defensible to require proof on the balance of probabilities, rather than some lower burden, that efficiencies will likely be attained.)

A second alternative that arguably can be accommodated within the total welfare approach would be to require that the merging parties establish that there is a real probability that the merger will result in "substantial" efficiencies. The principal benefit of this approach would be that it would avoid the need to engage in a full-blown trade-off analysis. However, the downside would be that it would confer upon the enforcement authority and ultimately the tribunal or court considerable discretion to decide in any particular case whether the claimed efficiencies are "substantial". This would considerably increase the uncertainty for merging parties, to the point that they likely would not be prepared to incur the substantial costs associated with putting the matter before a tribunal or a court, on efficiency grounds alone.

Where the goal of maximizing total welfare is rejected in favour the alternative objective of maximizing consumer welfare, the U.S. approach to efficiencies in merger review is superior to the approach suggested in the Competition Tribunal's non-binding remarks, i.e., adjusting the Canadian trade-off approach by incorporating wealth transfers into the analysis.[36] Such an approach would be an odd-hybrid of the approaches adopted in the MEGs and the U.S., and would maximize neither total welfare nor consumer welfare.

Ultimate Policy Objective Constrains Choice of Alternatives

The choice between the total welfare and consumer welfare frameworks not only has important implications for the broad approach that is adopted to efficiencies, but also for the manner in which several key issues that arise in the context of merger review are treated.[37] These include the treatment of: (i) efficiency gains that would likely be attained through other means if the merger did not proceed in whole or in part; *(ii)* efficiencies that are redistributive in nature; *(iii)* efficiencies that will ultimately pass through to foreign shareholders; and *(iv)* efficiencies resulting from reductions in fixed, versus variable, costs.

In addition to the various substantive differences in approach that are warranted under the total welfare and consumer welfare models, respectively, it should be recognized that the choice between these two orientations can have very important implications for the way in which enforcement authorities and the courts view competition, exercise discretion, define markets, approach the issue of entry and evaluate efficiencies.[38]

Conclusions

When section 96 was inserted into the Act in 1986, the government of the day had high hopes that it would play a significant role in facilitating efficient restructuring in Canada.[39] These hopes were shared by the Bureau.[40] Unfortunately, the record has been disappointing. As noted earlier, not a single merger in the ten-year history of section 96 has been permitted to proceed by virtue of having met the requirements of that provision. This is no doubt attributable, at least in part, to the chilling effect of the Hillsdown decision on parties contemplating mergers which would have resulted in substantial efficiencies, had they proceeded. In any event, the Canadian record makes it difficult to recommend, without qualification, that other jurisdictions whole-heartedly embrace a similar statutory exception.

It is submitted that if the evidentiary burden that merging parties are required to meet with respect to claimed efficiency gains is changed from "the balance of probabilities" to the lower test adopted in New

Zealand, i.e., that there be a "tendency or real probability" that the efficiencies will be attained, the total welfare approach can have significantly more practical utility than it has had to date in Canada.

A second alternative that arguably can be accommodated within the total welfare approach would be to simply require that the merging parties establish that there is a real probability that the merger will result in "substantial" efficiencies. The significant downside associated with this approach would be that it would create a significant degree of uncertainty, because the meaning of "substantial" is inherently subjective.

Where the goal of maximizing total welfare is rejected in favour of the alternative objective of maximizing consumer welfare, the U.S. approach to efficiencies in merger review is arguably the most appropriate.

The choice between the total welfare framework and the consumer welfare framework not only has important implications for the broad approach to efficiencies, but also for the manner in which several key issues that arise in the context of merger review are treated.

NOTES

1. Prepared for the Competition Law & Policy Committee of the Business and Industry Advisory Committee to the OECD by Paul S. CRAMPTON, Partner at Davies, Ward & Beck (Toronto).

2. Department of Supply and Services Canada, 1991.

3. Canada (Director of Investigation and Research) v. Hillsdown Holdings (Canada) Ltd. (1992), 41 C.P.R. (3d) 289 at 337-43. For a detailed discussion of this aspect of the Hillsdown decision, see Crampton, "The Efficiency Exception for Mergers: An Assessment of Early Signals from the Competition Tribunal", 21 *Can. Bus. L.J.* 371 (1993). See also Goldman and Bodrug, "The Hillsdown and Southam Decisions: The First Round of Contested Mergers Under the Competition Act", *38 McGill L.J.* 724 at 735-39.

4. See CRAMPTON, "Alternative Approaches to Competition Law - Consumers' Surplus, Total Surplus, Total Welfare and Non-Efficiency Goals", 17 *World Competition* 55 (1994).

5. See *infra*, note 20, and corresponding discussion in text.

6. *Cf.* WILLIAMSON, "Economies as an Antitrust Defense: The Welfare Tradeoffs", 58 *Am. Econ. Rev.* 18-36 (1968) (hereafter "WILLIAMSON I"); WILLIAMSON, "Economies as an Antitrust Defense: Correction and Reply", 58 *Am. Econ. Rev.* 1372-1376 (1968); O. WILLIAMSON, "Allocative Efficiency and the Limits of Antitrust", *Am. Econ. Rev. Papers & Proc.* 105-118 (May 1969) (hereafter "WILLIAMSON II"); WILLIAMSON, "Economies as an Antitrust Defense: Reply", 59 *Am. Econ. Rev.* 954-959 (Dec. 1969); and WILLIAMSON, "Economies as an Antitrust Defense Revisited", 125 *Univ. Penn. L.R.* 699-736 (1977) (hereafter "WILLIAMSON III").

7. See *supra*, note 1, at §§5.4 and 5.5. See also CRAMPTON, "Canada's New Merger Enforcement Guidelines: a 'Nuts and Bolts' Review", 36 *Antit. Bull.* 883 at 955-70 (1991). For a discussion of the underlying rationale of the Director's approach, see CRAMPTON, "Mergers and the Competition Act", Toronto: *Carswell Legal Publications*, 1990, at 515-54.

8. See remarks of Colin Overbury, former head of the Merger Task Force of the European Commission, in International Merger Law, March 1991, p. 8. *Cf. Council Regulation* (EEC) No

4064/89 of 21 December 1989, Article 2(1)(b). Note, however, Frederic Jenny's observation that "not only is there no 'efficiency defence' in the EEC merger regulation but ... there can be cases of 'efficiency attack'". JENNY, "EEC Merger Control: Economies as an Antitrust Defence or an Antitrust Attack?", Nineteenth Annual Fordham Corporate Law Institute, International Antitrust Law and Policy, (October 22-23, 1992) 367 at 374.

9. See, for example, U.S. v. Archer-Daniels-Midland Company and Nabisco Brands, Inc. (Memorandum in Support of Plaintiff's Motion in Limine Relating to Efficiencies), reproduced in Practising Law Institute, *Federal Antitrust Enforcement in the 90's (Vol. 1)* (Course Handbook Series Number 708), 409 at 415; and WHALLEY, "After the Herfindahls are Counted: Assessment of Entry and Efficiencies in Merger Enforcement by the Department of Justice", reproduced in Practising Law Institute, *ibid*., 237 at 256. The FTC appears to take the same approach. See ARGUIT, Remarks before the Cleveland Chapter of the Federal Bar Association, Cleveland, Ohio, December 14, 1989, at 5. Reproduced in Practising Law Institute, 21st Annual Advanced Antitrust Workshop, 1991 (Course Handbook Series Number 726) at 123; DEYAK and LANGENFELD, "Efficiencies in U.S. Merger Analysis" (1992 unpublished), pp. 10-11. (Mr. Langenfeld is a former Director for Antitrust, U.S. Federal Trade Commission ("FTC"). Mr. Deyak was his assistant); and CALKINS and WARREN-BOULTON, "'Kinder, Gentler' Antitrust" (to be published in forthcoming publication of 1991 CATO Institute proceedings), at 27-28. See also CRAMPTON (1990), *supra*, note 6, at 517-19, and 541-43.

10. See references to the approach taken in the U.K. and Australia in Crampton (1990), *supra*, note 6, at 498. A similar approach has been adopted in New Zealand.

11. Deyak and Langenfeld, *supra*, note 8, at 15.

12. *Cf.* CALKINS and WARREN-BOULTON, *supra*, note 8, at 28; and FISHER, JOHNSON and LANDE, "Price Effects of Horizontal Mergers" (1989), 77 *Cal. L.R.* 777, at 791 n. 51. However, DEYAK and LANGENFELD, *supra*, note 8 at 21, state: "[W]e believe that efficiencies have been one of several factors in the decisions [of federal enforcement agencies] not to challenge some mergers."

13. The purpose clause in section 1.1 of the Act makes it clear that competition is not desired as an end in itself, but in order to facilitate the attainment of other objectives, including "to promote the efficiency and adaptability of the Canadian economy".

14. *Supra*, note 1, at §5.2.

15. *Ibid*.

16. *Supra*, note 8, at 417 ("it is also necessary for the merging parties to prove that the (transaction is) uniquely capable of producing those efficiencies"). See also WHALLEY, *supra*, note 8, at 258-59 ("the only efficiency claims that we will recognize are those unachievable by means that are more pro-competitive than the merger in question..... Unless efficiencies achieved by a merger ... are unique to that particular transaction, they will not be considered in assessing the competitive impact of the merger"). *Cf.* KWOKA, and WARREN-BOULTON, "Efficiencies, Failing Firms, and Alternatives to Merger: A Policy Synthesis", 31 *Antit. Bull.* 434-35 (1986).

17. See for example, Arquit, *supra*, note 8, at 135 ("Comparable cost reductions that could be achieved in other ways ... are not cognizable efficiencies"). See also the report of the FTC's opinion letter in respect of the proposal by Harold A. Honickman to acquire the Seven-Up soft drink franchises of New York Seven-Up Bottling Company Inc., at (CCH) FTC Complaints and Orders (1992), 22,957 at 22,964 ("If there are several plausible transactions that produce almost

the same efficiencies, the net efficiencies would be only those efficiencies that are unique to the transaction").

18. Honickman opinion, *ibid.*, at 22,965. Compare this with the approach articulated in §5.2 of the MEGs, *supra*, note 1.

19. *Supra*, note 1, at §5.2.

20. *Ibid*.

21. *Supra*, note 2, at 337-43.

22. The (now former) Director has drawn a similar conclusion from the Tribunal's comments. See WETSTON, "Decisions and Developments: Competition Law and Policy", Remarks Delivered to The Canadian Institute, Toronto, June 8, 1992 (Consumer and Corporate Affairs Canada speech #S-10728\92-07) at 7.

23. *Supra*, note 2, at 343.

24. WETSTON, Developments and Emerging Challenges in Canadian Competition Law, paper delivered at Fordham Corporate Law Institute (New York, New York), October 22, 1992, at 16.

25. *Supra*, note 2, at 738.

26. See *infra*, notes 38 and 39.

27. Supra, note 2, at 343.

28. These comments were made by the Howard I. Wetston at a conference on Competition Law and Competitive Business Practices, organized by The Canadian Institute and held in Toronto at the Four Seasons Hotel on June 8, 1992.

29. *Supra*, note 21, at 8. The Tribunal did not need to address the issue of efficiencies in that case because it concluded that the merger would not prevent or lessen competition substantially. The Tribunal did not state that it was addressing the issue of efficiencies in the event that its conclusion in this regard was overturned on appeal. There was no dispute between the Director and counsel for Hillsdown with respect to this matter.

30. *Supra*, note 1, at §5.6.

31. The author was involved in the review of this case while working in the Bureau. This aspect of the case was never made public.

32. However, there have been a few cases that would have come close to satisfying this test, given certain reasonable assumptions regarding the elasticity of demand for the relevant product and the extent of the price increase likely to result from the merger. It may also be noted that other provisions in the Act, relating to specialization agreements, contain a similar efficiency gains test which has not been met by anyone to date.

33. Note that in the Hillsdown case, the Tribunal agreed with the Director that "the respondents have the onus of proving the existence of the efficiencies claimed, or the likelihood of their existence ... on the balance of probabilities in the normal way". See *supra*, note 2, at 335.

34. Brodley has observed: " ... while estimates vary, there is perhaps a consensus that the loss from monopolistic pricing is considerably less than one percent of the gross national product - a fraction of the welfare at stake in technological progress and productive efficiency." He adds: "The social trade-off is desirable because the loss of consumer benefit is temporary, but the achievement of production efficiencies frequently has a multiplier effect on the growth of social wealth." BRODLEY, "The Economic Goals of Antitrust: Efficiency, Consumer Welfare, and Technological Progress", 62 *N.R. Univ. L.R.* 1020 at 1027 and 1039 (1987). In this regard, Easterbrook adds: "In the long run, a continuous rate of change, compounded, swamps static losses." EASTERBROOK, "Ignorance and Antitrust", in Jorde and Teece, (ed), *Antitrust, Innovation and Competitiveness*, (New York: Oxford Univ. Press, 1992), at 122-23. Michael Porter, who has studied a wide range of industries in a wide range of nations, has concluded: "When faced with tradeoffs, we should weigh progressiveness higher than static efficiency or a snapshot of price-cost margins", because "innovativeness is by far the most important source of economic growth and welfare, greatly outweighing price-cost margins (allocative efficiency), or even static efficiency". M. PORTER, *The Competitive Advantage of Nations*, (New York: The Free Press, 1990), at 5.

35. Re Weddel Crown Corporation Ltd. and Ors (1987), 1 NZBLC 104,200 at 104,213 (Com). Note that in that case the Commerce Commission accepted that private benefits have an element of public benefit even where they are not directly passed on to consumers. See also Fisher and Paykel Ltd. v. Commerce Commission, [1990] 2 NZLR 731 at 767 (H. Ct.).

36. See CRAMPTON, *supra*, note 2, at 388-89; and CRAMPTON (1990), *supra*, note 6, at 527-29.

37. For a more detailed discussion, see CRAMPTON, *supra*, note 3, at 69-75.

38. See *ibid.*, at 60-63.

39. For example, in the Guide that accompanies the proposals which eventually became the 1986 amendments to the Act, it was observed:

> The new merger law will also provide a defence in situations where the gains in efficiency that would result from the merger would more than offset the costs due to the lessening of competition. It is important for the performance of the economy that significant cost savings brought about by mergers, for example, through scale economies or other efficiencies, be allowed.

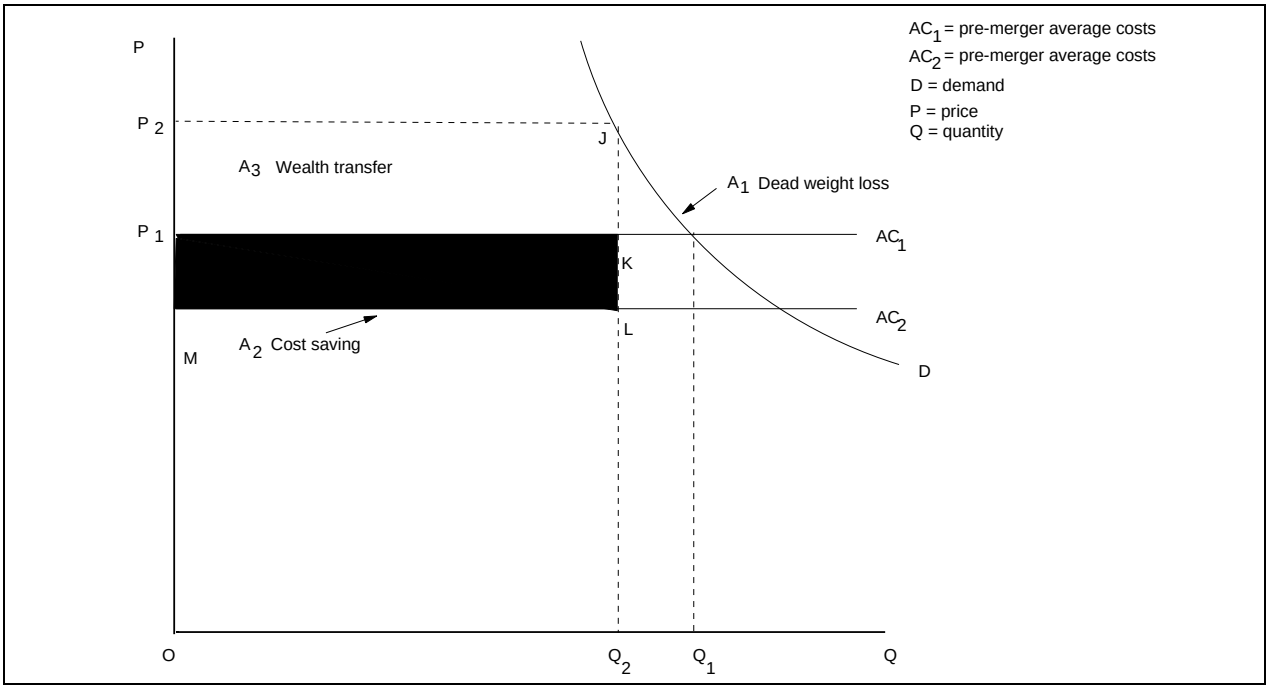
Consumer and Corporate Affairs Canada, Competition Law Amendments - A Guide, (December 1995) at 17.

40. See, for example, GOLDMAN, "Mergers, Efficiency and the Competition Act", Notes for an address to the Consumer and Commercial Law Workshop, Faculty of Law, McGill University, Montreal, November 15, 1988, at 8 (Speech # S-1-170); and Goldman, Notes for an Address to the Gordon Group Conference on the Competition Act, Toronto, March 31, 1987, at 13-14.

APPENDIX

The trade-off approach contemplated in sections 86 and 96 of the Act has its roots in a series of articles by Oliver Williamson.[41] Williamson articulated his analytical framework by reference to the following diagram:

Diagram 1



Williamson explained the diagram as follows:[42]

> The horizontal line labelled AC_1 represents the level of average costs of each duopolist before combination, while AC_2 shows the level of average costs after the merger. The price before the merger is given by P_1 and is equal to AC_1. The price after the merger is given by P_2 and is assumed to exceed P_1; if it were less than P_1 the immediate economic effects of the merger would be strictly positive.
>
> The net welfare effects of the merger are represented by the two shaded areas in the Figure. The area designated A_1 is the familiar deadweight loss that would result if price were increased from P_1 to P_2, assuming that costs remain constant. But because average costs are actually reduced by the merger, the area designated A_2, which represents cost savings, must also be taken into account. Geometrically, the net allocative-efficiency effect of the price increase and cost reduction resulting from the merger (judged in naive terms) is positive if the area represented by A_2 is greater than the area represented by A_1 ...

In short, Williamson's model suggested that "a relatively modest cost reduction is sufficient to offset relatively large price increases even if the elasticity of demand is as high as 2, which for most commodities is probably a reasonable upper bound".[43] Williamson characterized his model as "naive" because it made various assumptions which do not fully reflect commercial realities.[44] For example, if

the model's assumption of pre-merger pure competition is altered to reflect the levels of market power and demand elasticities "normally found in our economy, very large cost reductions would be necessary".[45] Additional cost reductions typically become necessary to outweigh the deadweight loss[46] resulting from a merger where the merged entity does not account for the entire market as a result of the merger. The smaller the share of the market held by the merged entity, the greater the reduction in its costs required to outweigh the deadweight loss. Similarly, as the elasticity of demand for the relevant product increases, "the efficiencies necessary to compensate for possible market power effects would increase dramatically".[47]

Moreover, the comparative statics framework of the model does not capture the fact that the absolute value of the stream of estimated future efficiency gains attributed to a merger is often discounted by much more than the absolute value of the stream of estimated future anti-competitive effects attributed to the merger. This is because the latter will ordinarily commence shortly after the consummation of an anti-competitive merger, whereas the efficiency gains are often delayed by up to several years.

Thus, demonstrating that a merger is likely to bring about greater efficiencies than the deadweight loss believed to result from the merger will be much more difficult than suggested by Williamson's "naive" model.

Parenthetically, Williamson did not make even passing mention of Area A_3 (on Diagram 1) in his trade-off analysis because "the transfer of benefits from one form (consumer surplus) to another (profit) is treated as a wash under the conventional welfare economics model".[48] In short, "[w]hen a dollar is transferred from a buyer to a seller, it cannot be determined *a priori* who is more deserving, or in whose hands it has a greater value".[49] As Charles F. Rule observed when he was Assistant Attorney General, Antitrust Division, DOJ: "It is not clear ... that policy should be skewed toward consumers of luxury items such as Cadillacs and against 'producers' of the product, who may, in the final analysis, be the proverbial widows and orphans whose only source of income is the dividends from the 'producers' stock." In 1992, the Director added:[50]

> Economists have advocated treating the wealth transfer effects of mergers neutrally owing to the difficulty of assigning weights *a priori* on who is more deserving of a dollar. Even considering that some system of weighting could be articulated, the practical implications of this are likely insurmountable -- for, who is losing and who is receiving the transfer?

One need only consider the substantial presence of pension funds in today's capital markets to gain a sense of the perverse effects that could result from including the wealth transfer in the trade-off analysis to facilitate redistribution objectives. In any event, competition law is generally considered to be a poor policy tool for advancing wealth distribution objectives.[51]

NOTES

41. See *supra*, note 5.

42. WILLIAMSON III, *ibid.*, at 707-708. Area A_3 has been added to Williamson's diagram to facilitate the discussion in this paper.

43. *Ibid.*, at 709.

44. These are summarized below and discussed in greater detail in CRAMPTON (1990), *supra*, note 6, at 499 *et seq*.

45. DEPRANO and NUGENT, "Economies as an Antitrust Defense: Comment", 59 *Am. Econ. Rev.* 947, at 951 (1969). See also FISHER and LANDE, "Efficiency Considerations in Merger Enforcement" (1983), *Cal. L.R.* 1580 at 1643.

46. The loss represented by Area A_1 on Figure 1 is commonly characterized as a "deadweight loss" because it is something that is lost by buyers but not gained by sellers. It is a measure of the amount by which society as a whole is worse off by virtue of the fact that persons who continue to buy the product at a higher price have less money left over to buy other products, and persons who no longer buy the product because its price has increased allocate the money that they would otherwise have spent on the product to less-valued products.

47. FISHER and LANDE, *supra*, note 44, at 1643. These authors suggest that demand elasticities in the 2.5 to 5 range are common for successful brands of consumer products. A 1988 survey of 42 published studies that in aggregate reported 367 estimates of price elasticities for 220 different brands or markets found the average price elasticity to be 1.76. See TELLIS, "The Price Elasticity of Selective Demand: A Meta-Analysis of Econometric Models of Sales", *XXV Journ. Marketing Research* 331 at 337 (Nov. 1988).

48. WILLIAMSON III, *supra*, note 5, at 711.

49. MEGs, *supra*, note 1, at 49 n.57. See also SCHERER, "Antitrust, Efficiency and Progress", 62 *N.Y. Univ. L.R.* 998 at 998-99 (1987).

50. *Supra*, note 27.

51. WILLIAMSON II, *supra*, note 5, at 108. Williamson observes: "Macroeconomic policy instruments (taxes, transfers, expenditures) with which to correct distributional conditions are not only available but are superior to the use of antitrust for this purpose." See also WARREN-BOULTON, "Implications of U.S. Experience with Horizontal Mergers and Takeovers for Canadian Competition Policy", in Mathewson, Trebilcock and Walker (eds.), *The Law and Economics of Competition Policy*, (Vancouver: The Fraser Institute, 1990) 337 at 340:

> Since we have no way to determine which individuals are more deserving than others, since any general principle for income redistribution would necessitate a unique set of weights for each merger, and since any such principle could be more efficiently implemented through other policy instruments, the obvious approach is to treat everyone equally and simply maximize total welfare.

CONTRIBUTION FROM BIAC

Here's to a More Significant Role for Efficiences in U.S. Merger Analysis[1]

The United States has an extensive array of antitrust laws, including the Sherman Act,[2] the Clayton Act[3] and the Federal Trade Commission Act.[4] These laws are designed to help preserve and enhance competition, leading to lower prices and greater product innovation and selection for consumers.

There is a clear and stable consensus that, in the past, the U.S. antitrust laws and the competition they engendered have been an important factor in forcing U.S. industry to perform in an innovative and cost-effective manner, thus helping to produce one of the most affluent societies in the world.[5] Effective antitrust enforcement therefore is a widely shared bi-partisan goal. It benefits both U.S. consumers, who have been provided better products at more affordable prices, and the nation's businesses, which have been driven to efficiency and, ultimately, greater profitability by the competitive forces of the marketplace. As a result, U.S. companies have been better situated for the increased competition flowing from growing integration of the global economy.

On the other hand, while the focus of the antitrust laws is to preserve a sufficiently unconcentrated market so that companies are forced to compete and offer new or improved products at prices approximating their own costs (with some level of appropriate return on capital, effort and other opportunities foregone), regulation that prohibits transactions and commercial practices that are efficiency enhancing may lead both to increased prices for consumers and a loss of competitive advantage for U.S. industries. The higher the costs of production or development borne by U.S. producers, the higher the prices passed on to their customers. And, if the antitrust enforcement regimes in other countries allow efficiency enhancing mergers, acquisitions or joint ventures that would be blocked in the United States, firms in those other countries may well be rewarded with lower cost structures, elimination of duplicative operations, a pooling of talent, and the like that would leave U.S. firms at a competitive disadvantage. Accordingly, the U.S. antitrust laws must be enforced in a manner that permits U.S. companies to be competitive with their counterparts operating primarily under the antitrust enforcement regimes of our major trading partners.

What is called for, therefore, from an enforcement standpoint, is an ongoing examination of the way in which antitrust principles should be applied to new market circumstances, including, most importantly, the increasing globalization of markets and the emergence of new and capital-intensive technologies. The FTC is currently undertaking such a study under the leadership of Chairman Pitofsky. This paper will examine this subject with specific reference to the role for efficiencies in U.S. merger analysis.

Discussion

The United States antitrust regulators apply a "rule of reason" to assess the permissibility of many forms of concerted activity, as well as to evaluate changes in market concentration from mergers, acquisitions, and joint ventures. Such analyses typically weigh the potential benefits of a cooperative activity or combination of independent actors against the potential costs to the economy caused by a loss of competition.

A major point of departure between the U.S. antitrust regime and the regulatory focus of many of our major trading partners is the period of time over which a combination's potential effects should be

assessed. The U.S. typically focuses on a relatively short period of time. For example, the 1992 Merger Guidelines state that where a merger or acquisition may create potentially troublesome levels of market concentration, only market entry that will drive down prices within two years will be deemed timely.[6] By contrast, the antitrust regimes of many of the United States' trading partners take into account the existence of efficiencies that may be realized over significantly longer periods of time, thus permitting companies falling within their primary jurisdictions to engage in transactions or combinations designed to achieve long-term pro-competitive benefits that may not be immediately manifested in the economy. We believe the time has come for U.S. antitrust enforcement to move toward a longer-term focus, taking efficiencies more fully into account than is currently the case.

Under the 1992 Merger Guidelines, the antitrust enforcement agencies will consider cognizable efficiencies resulting from a merger when conducting their analysis of the legality of the merger. Efficiencies that might result from a merger typically include economies of scale, which allow a firm to spread its fixed costs of operation over a larger volume of goods and to drive down per-unit costs. Similarly, economies of scope may be realized when a producer is able to expand its product line, so that its investment in one type of product may be carried over to benefit operations in a related product or field. Other efficiencies typically include better integration of production facilities, which allow firms to optimize their operating rates and to eliminate excess capacity, and plant specialization.

Under established antitrust analysis, the more significant the competitive risks posed by a combination or cooperative activity, the greater these efficiencies must be to permit a transaction to proceed. While efficiency arguments may help a proposal of "borderline" permissibility survive antitrust scrutiny, they alone cannot save a transaction raising substantial anticompetitive concerns. This is, on balance, normally as it should be. However, in today's world, with the increased globalization of markets and the increasing expense of innovation and research and development in high technology industries, we believe that the Department of Justice and FTC need to give efficiencies greater consideration when analyzing transactions than is their current practice.

The 1992 Merger Guidelines recognize that most mergers are competitively beneficial (i.e. efficient) or neutral,[7] and any merger falling below the general concentration thresholds of the Guidelines is assumed to come within that category. On the other hand, the Guidelines provide that any mergers exceeding the standard concentration thresholds are presumptively anti- competitive.[8]

The current concentration thresholds were established by the 1982 Department of Justice Merger Guidelines. Those guidelines introduced the use of the Herfindahl-Hirschman Index ("HHI"), which closely approximated the four-firm concentration test and market share standards contained in the Department's 1968 Merger Guidelines. However, there is no economically compelling basis for viewing the current HHI thresholds of the Merger Guidelines as sacrosanct, or to regard transactions which exceed these thresholds as presumptive "Guidelines violations." Rather, modern economic scholarship indicates that markets may function efficiently with substantially higher levels of concentration, depending on the vast plethora of factors that influence economic performance.[9] The 1992 Merger Guidelines were designed to create a five-step analytical framework, with each step necessary, but not individually sufficient, to conclude that a merger is likely to have an anticompetitive effect. The structuralist presumptions contained in the Guidelines do no more than indicate that concentrative transactions or activity merits some further scrutiny in light of the other market conditions influencing competitive performance. However, the need carefully to consider these other factors (such as efficiencies) does not diminish with the level of concentration; there should be no sliding scale of analysis.

Efficiencies are given much more weight by the antitrust enforcement regimes of our major trading partners than by the U.S. agencies. This in and of itself may significantly disadvantage U.S. industry. The European Union, for example, often permits concentrative agreements that afford significant economic efficiencies, while the same agreements might well be *per se* illegal in the United States. Under EU law, for example, producers are permitted to cooperate under "specialization" or other forms of

agreement to address market conditions (such as chronic overcapacity) that are preventing them from operating in a profitable or economically viable manner. The United States, by contrast, prohibits many collaborative industry efforts addressing systemic market conditions (*e.g.*, to avoid "ruinous" competition), regardless of whether the restraint or its economic effect is reasonable.[10]

The European Commission's Merger Control Regulation,[11] likewise, is much more lenient than that of the Merger Guidelines with respect to industry concentration thresholds. Generally speaking, the focus of EU competition law, insofar as it regulates market structure, is on the prohibition of transactions that would create a dominant firm or a duopoly. For example, when Nestle acquired Perrier, the European Commission entered a consent decree that permitted an acquisition resulting in the top two firms having a combined 75 per cent market share. Under that decree, the parties agreed to divest certain operations to a firm already in the market with the aim of creating a significant "third force." While this may have afforded some degree of protection, it is unlikely that such a decree would have been accepted by U.S. antitrust regulators, since the level of concentration created in the market in and of itself would have been deemed unacceptable (regardless of the creation of some "countervailing power" in a third party).

The Commission's approach in the EU may be more consistent with the available empirical studies. These studies indicate that mergers should be of concern only when they involve the first or second leading firms in the market where the two firm concentration ratio exceeds 35 per cent.[12] Such a standard could be one way of according efficiencies greater significance than previously has been the case.[13]

The role of efficiencies in U.S. antitrust analysis has been evolving over time, and should continue to evolve in order to promote economically sound and pro-competitive decision making. The 1968 Department of Justice Merger Guidelines were written so narrowly as to be virtually hostile to efficiencies. They stated that, in general, the Department would not accept an efficiency justification for a merger for three reasons: *(1)* attainment of economies of scale is exhausted at such low levels that they do not justify long-term structural changes in the market; *(2)* potential efficiencies can be realized through means other than merger; and *(3)* efficiencies are difficult to assess.[14] The validity of each of these propositions was seriously challenged over time. Indeed, although there is no consensus that mergers are always efficient, it would be difficult to quarrel with the notion that many mergers do provide substantial efficiencies, and that scale economies often are not exhausted at extremely low levels.[15]

Considerable progress was made in this area when the Department of Justice released its 1984 Merger Guidelines. Those Guidelines specifically acknowledged that mergers and acquisitions can yield substantial efficiencies, but required that such efficiencies be demonstrated by "clear and convincing" evidence. Even then, the 1984 Guidelines provided only that the Department would consider such evidence in its analysis; there was no suggestion that efficiencies could save a transaction that might otherwise be deemed unlawful under an analysis of market concentration levels and other, more traditional factors. The government tended to view evidence that the transaction would yield economic efficiencies merely as an indication that the parties might have economically valid (pro-competitive) motives for the transaction, rather than as a factor actually mitigating demonstrable risks that a transaction could create significant anticompetitive effects.

In 1992, the Department of Justice and Federal Trade Commission issued yet another set of Horizontal Merger Guidelines. In these, the requirement that efficiencies be proved by "clear and convincing" evidence was removed. This change was made to allay concerns that the government was not according sufficient recognition to the efficiencies afforded by various combinations, and to make clear that efficiencies would be accorded the same significance as other elements of the regulators' analysis. Again, however, there was no express confirmation that efficiencies could justify an otherwise unlawful merger, and no articulation as to how exactly efficiencies would be factored into the analysis. Although the Department had stated in independent fora that an otherwise unlawful merger might be justified by a demonstration that efficiencies would result in lower prices and increased output,[16] this was not carried

forward into the Guidelines, and no similar suggestion was voiced by any Commission official. Thus, even under the 1992 Guidelines, commentators continue to view the task of proving that efficiencies could outweigh potential anticompetitive effects as an imposing one.[17]

With three years' experience under the most recent Merger Guidelines behind us, we now have a basis on which to accelerate the evolution of U.S. antitrust regulation toward a greater recognition of efficiencies, particularly in light of several very significant macroeconomic trends.

First, and perhaps most important, is the increasing globalization of markets and escalating competition between companies around the world. The 1992 Merger Guidelines specify that antitrust analysis should be fully informed by the existence of global market forces, and that market shares should be assigned to foreign firms on the same basis as domestic firms.[18] However, while the agencies will argue that they examine a global market when relevant, the reality is that they often also perform an independent analysis of the potential anticompetitive effects of a transaction in a "U.S. submarket."

The government's (stated or implicit) reason for its focus on the domestic market often is an inbred concern that offshore supply responses are too unreliable to form a meaningful constraint on potential anticompetitive conduct within the United States. For example, foreign suppliers are subject to the vagaries of currency exchange rates, and currency fluctuations can have the same effect as a price increase in the United States (so that imports which are competitive at the time the regulators perform their analysis may not be able to constrain supra-competitive price increases caused by a merger). Similarly, offshore producers may be subject to onerous trade actions that increase their costs and make effective competitive responses uncertain. Moreover, foreign suppliers typically favor home market demand, so the ability to divert supplies to the U.S. may be subject to complex supply-and-demand conditions in other countries that are difficult for U.S. regulators to assess.

These arguments, however, fail to take into account that no supplier (domestic or foreign) is insulated from world market conditions; in many cases both domestic and foreign firms acquire inputs from worldwide markets that are likewise affected by changes in the dollar. Moreover, foreign firms increasingly have been establishing production facilities in the U.S. that assure their ability to compete effectively there on an ongoing basis. Accordingly, the reticence of U.S. regulators to take foreign supply capabilities and responses fully into account may well impose unrealistic constraints on how competition in a market should properly be assessed.

One answer to the reticence of U.S. regulators to give full recognition to global industry participants and structures is to enhance the significance afforded the potential economic efficiencies from a combination. To compete on this larger scale requires that firms have increased capital and other resources, and be able to obtain such maximum production and development efficiency from their workers and facilities. Such benefits help to ensure that any potential anticompetitive effects from a transaction may be balanced by cost savings that flow through to the market.

Similarly, efficiencies derived from mergers or joint ventures in the United States increase the ability of U.S. companies to compete on a larger, global scale. Often, however, these efficiencies are rationalized over the long term. As a result, prices in the United States may not go down in the short term, but as these companies compete more effectively around the world, prices eventually may decrease in the United States.

The second trend that calls for an increasing recognition of efficiencies in antitrust analysis is the dramatically increasing pace of innovation in numerous industries, which forces companies to expend unprecedented amounts on further development. Such development -- like the invention of microprocessors, development of enhanced television and communications technologies, and creation of new software programs and interoperable computer capabilities -- benefit consumers enormously, and should be

encouraged. Yet many companies find such investment to be beyond their reach, leading, potentially, to a *de facto* surrender of emerging markets to large incumbent firms.

Mergers or joint ventures allow competitors to pool knowledge to develop a product that can better compete against large incumbents or consortia in other countries. They often allow companies to eliminate duplication of efforts, increasing the resources available to conduct research or bring a new product to market. In addition, synergies between unique skills and technologies often can lead to the development of a better product than either company independently could produce. One notable example is the development of semiconductors and other new technologies in the consumer electronics industry, which requires vast expenditures and investments from which positive results may not be seen for years. It is in high tech areas such as these that globalization is so important, with the country that develops the best product the quickest often dominating the market for that product around the world.

U.S. antitrust law does take into consideration the potential benefits of joint research and development ventures between a number of competitors in an industry, such as the conglomeration of U.S. companies in the semiconductor industry known as Sematech, examining such ventures under a rule of reason analysis. The National Cooperative Research Act of 1984[19] ("NCRA") specifically states that a joint research and development venture will "be judged on the basis of its reasonableness, taking into account all relevant factors affecting competition."[20] However, aside from limiting antitrust exposure of parents of the joint venture to actual costs and attorney's fees, the NCRA does little more than the law previously permitted. Indeed, many have argued that the principle benefit of the law is simply to publicize the standards already being applied by regulators to this type of activity. Thus, efficiencies still are not accorded the appropriate weight due them, especially when competition in high tech industries of the future often occurs with foreign companies backed and encouraged by their governments. Yet it is in these areas where efficiencies should play a stronger role, allowing companies to better invest for the future so that they may be able to compete effectively in the industries of the future.

There is support for the notion that even mergers in concentrated markets will enhance welfare as long as they are accompanied by modest cost reductions.[21] Thus, our failure to adequately address efficiencies could be a costly error, and it is, therefore, an excellent time to re-evaluate their role in merger analysis.

One impediment to full and proper consideration of efficiencies is the requirement that companies prove they will pass on the benefit of economic efficiencies to consumers in the short term. Serious consideration should be given to adopting an analysis that would not require such proof. Although a more lenient standard could imply reliance to an extent on a general welfare standard, there are several good reasons for such a change, which could be consistent with the direction of the 1992 Merger Guidelines' indication that a pass on of efficiency benefits to consumers could occur "over time."

First, as discussed above, the antitrust regimes of the U.S.'s major trading partners appear to give efficiencies much greater consideration than is given here, which could have the effect of disadvantaging domestic companies in a more global economy. Second, objections to the societal welfare standard were largely based on issues of equity in the distribution of stock holdings. The stock of publicly traded companies had been held, for the most part, by a fairly small segment of the population. As a result, the benefits of cost savings from mergers that were not passed on to consumers would have been reaped in the past by that small, affluent segment of the nation possessing the majority of stock holdings, while the costs of price increases would have been borne by the rest of the country. Today, however, the dramatic growth of pension and mutual funds has spread the ownership of publicly traded companies much more widely and severely reduced concerns of distributional equity. Third, although efficiencies are hard to measure, we should provide an incentive to improve the means of doing so. When the market definition standard of the 1982 Merger Guidelines was introduced, the common lament was that it was not applicable in practice. Those concerns may have been well founded at the time, but the Guidelines asked the right question and

helped develop the means to provide the answers, which has been done to a significant degree over the last decade. Similar improvements should be anticipated for efficiency analysis.[22]

Finally, in this connection, the agencies should become more hospitable to the types of efficiencies that may be considered. Efficiencies related to long-term production capabilities should certainly be taken into account, and the 1992 Merger Guidelines do acknowledge the existence and relevance of economies of scale. There does not, moreover, appear to be a compelling case for the utter disregard of talent, managerial, and administrative efficiencies where they are real and substantial.

Conclusion

The Sherman, Federal Trade Commission, and Clayton Acts effectively create a federal common law concerning unfair competition that has broad-based applicability and is inherently flexible. There is nothing fundamentally incompatible between these laws and the efficient operation of American business. As a result, the temptation to propose piecemeal legislation, such as the NCRA, carving out specific exceptions to the antitrust laws should be avoided. Under-enforcement of the antitrust laws will make domestic markets less competitive and harm consumers in the short run and the efficiency of businesses in the long run.

On the other hand, overreaching enforcement of the antitrust laws would also be problematic. It could deny efficiencies to domestic industry that are permitted to foreign firms, with obvious consequences in this increasingly global economy. Thus, the enforcement agencies must continue to be vigilant, yet at the same time be more willing to expand their view of relevant geographic markets, taking into account the importance of efficiencies in today's global economy and refining the manner in which those efficiencies are measured.

NOTES

1. By James F. RILL and A. Paul VICTOR. Mr. Rill is a partner in Collier, Shannon, Rill & Scott, Washington, D.C., and Mr. Victor is a partner in Weil, Gotshal & Manges, New York, N.Y. The authors are grateful to Douglas A. Nave and Marc Brotman of Weil, Gotshal & Manges, and Joseph J. Simons of Collier, Shannon, Rill & Scott, for their assistance in the preparation of this paper.

2. 15 U.S.C. §§ 1 et seq. Section 1 of the Sherman Act prohibits contracts, combinations or conspiracies in restraint of trade. Section 2 prohibits unilateral monopolization and attempted monopolization, as well as conspiracies to monopolize.

3. 15 U.S.C. §§ 12 et seq. The Clayton Act, among other things, prohibits mergers and acquisitions the effect of which may be to substantially lessen competition or create a monopoly in any line of commerce. 15 U.S.C. § 18. This section of the Clayton Act is the primary statute governing the Department of Justice's and Federal Trade Commission's authority over and review of mergers and acquisitions.

4. 15 U.S.C. § 41. The FTC Act prohibits unfair methods of competition and unfair or deceptive acts or practices.

5. See generally M. PORTER, *The Competitive Advantage of Nations* 662-64 (1990); R. PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", 81 *Georgetown L. J.* 195, 198 (1992).

6. 1992 Merger Guidelines § 3.2.

7. 1992 Department of Justice and Federal Trade Commission Horizontal Merger Guidelines at § 0.1.

8. *Id.* at § 1.51.

9. See P. PAUTLER, "A Review of the Economic Basis for Broad-Based Horizontal Merger Policy", 28 *Antitrust Bulletin* 571(1983); W. BLUMENTHAL, *Horizontal Merger: Law and Policy* 184-89, 195 (1986).

10. One particularly notorious example in this regard is United States v. Trenton Potteries Co., 273 U.S. 392 (1927). But see, *e.g.,* Nat'l Soc'y of Professional Engineers v. United States, 435 U.S. 679 (1978).

11. Council Regulation No. 4064/89 of 21 December 1989 on the control of concentrations between undertakings, 1990 O.J.(4L 257)14.

12. P. PAUTLER, "A Review of the Economic Basis for Broad-Based Horizontal Merger Policy", 28 *Antitrust Bulletin* 571, 636 (1983).

13. See R. PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", *supra* note 1, at 218 (proposing a defense for production efficiencies where the combined firm would have less than a 35 per cent market share, but requiring that concentration be moderate).

14. Department of Justice 1968 Merger Guidelines ¶ 10, reprinted in 4 *Trade Reg. Rep.* (CCH) ¶ 13,101, at 20,524.

15. See PITOFSKY, "Proposals for Revised United States Merger Enforcement in a Global Economy", *supra* note 1, at 208; D. CARLTON and J. PERLOFF, *Modern Industrial Organization* 171 (1990); F. SCHERER and D. ROSS, *Industrial Market Structure and Economic Performance* 111-41, 162-174 (1990).

16. J. WHALLEY, "After the Herfindahls are Counted; Assessment of Entry and Efficiencies in Merger Enforcement by the Department of Justice", Address Before the 29th Annual Antitrust Seminar, Practicing Law Institute 36-37 (1989).

17. See, *e.g.*, PITOFSKY, "Proposals for Revised United States Meager Enforcement in a Global Economy", *supra* note 1, at 206 ("the Guidelines have been interpreted by Administration officials to include a killer qualification.").

18. 1992 Merger Guidelines § 1.43.

19. 15 U.S.C.A.§ 4301-05 (1991 Supp.).

20. 15 U.S.C. § 4302.

21. T. MURIS, "The Efficiency Defense Under Section 7 of the Clayton Act", 30 *Case West. Res. L.R.* 384-88.

22. T. MURIS, "The Efficiency Defense Under Section 7 of the Clayton Act", *supra* note 10, at 425.

AIDE-MEMOIRE of DISCUSSION

(by the SECRETARIAT)

The Chairman (Mr. Jenny) introduced the topic. He noted that the papers that were submitted by delegations raised three broad issues, which he proposed discussing in turn: *(1)* The status of efficiency considerations in the laws of Member countries, in particular whether claimed efficiencies are relevant only as a defence in an otherwise anticompetitive transaction or are relevant in the competitive analysis itself; *(2)* the standards for considering efficiencies, including the relevance of various types of efficiency claims and the standard of proof; and *(3)* the difference, if any, in treatment of efficiency claims in mergers and in nonmerger agreements.

The European Commission stated that its standards do differ as between mergers and restrictive practice cases. The Council Merger Regulation sets forth criteria for consideration of mergers, of which efficiencies are one, but if the merger is found on balance to be anticompetitive -- the creation or strengthening of a dominant position which results in a significant limitation of competition -- efficiencies are not a defence. The Nordic Satellite case was such a case, in which the transaction could have generated significant efficiencies, but it was found to create or strengthen a dominant position on several markets, and was prohibited.

Japan stated that the Japanese Antimonopoly Act does not explicitly recognise efficiencies, but administrative procedures for merger control do provide for consideration of efficiencies as a relevant factor. They are not considered separately, but in the overall assessment of the effect of the transaction on competition. Thus, a merger that improves the efficiency of smaller firms in a market can strengthen competition. On the other hand, efficiency gains through merger by a dominant firm could contribute to the likelihood of the exercise of market power in the relevant market. The relevant question is the effect of the merger on competition in the market as a whole, and not the benefits that it might bring solely to the merged company.

In New Zealand efficiencies are treated identically in evaluation of merger and restrictive practices transactions. Efficiencies are relevant in applications to the Commerce Commission for advance authorisation of a transaction or conduct, but may not be considered in enforcement actions in the courts. The Commission shall grant the application if the transaction would generate a "benefit to the public" that outweighs the anticompetitive effects, if any. "Benefit to the public" is construed to include only economic efficiencies, and not social benefits. That standard was articulated by the High Court in the Telecom Corporation of NZ case. The Commerce Commission Guidelines on Public Benefit elaborate on the test. The comparison is "with" and "without" the transaction, and the efficiency gain must be dependent upon the transaction. In the Health Waikato /Midland Health case the proposed transaction was denied because it was not shown that the benefits would arise solely from the proposal. The Commission can consider matters other than productive efficiencies accruing to the applicant firms, such as environmental and health benefits. These other benefits seldom are determinative, however, and have not been considered by the Commission in recent cases.

The Chairman introduced the next issue, relevant standards in considering efficiency benefits. He noted that standards do appear to vary among countries. For example, Canada appears to give principal weight to efficiencies accruing to Canadian firms, while New Zealand appears to take into account efficiencies also occurring abroad. Where a trade-off analysis is employed, some countries seem to apply the "total surplus" test, while others employ the "consumer surplus" test.

The United States stated that currently there is some controversy surrounding the efficiencies defence in the U.S. Efficiencies are more readily considered by competition agencies and courts in integrative joint ventures than in mergers. In mergers, the agencies are more willing than the courts to entertain efficiency claims, but some lower courts also have evaluated efficiency claims by the parties. Such a case was the University Health case, in which the court considered the efficiency claims of the parties but found them inadequate to outweigh the anticompetitive effects of the merger. Indeed, in no decided merger case has efficiency claims determined the result. All efficiencies relating to the competitive process, such as improvement in unit costs (as opposed to more general claims, for example, relating to creation of jobs or benefits to the environment), are relevant, but their achievement must be specific to the merger. The view is generally held in the U.S. that the parties must show that their efficiency benefits will be passed on to consumers, though there continues to be debate on that issue. The Federal Trade Commission is currently conducting hearings on a number of important competition issues, including the proper role of the efficiency claims. Questions under consideration include: *(1)* the need for reconciliation of the treatment of efficiencies as between mergers and integrative joint ventures and as between the competition agencies and the courts; *(2)* clarification of the relevance of different types of efficiencies and the weight to be given them; *(3)* whether it must be shown that efficiency benefits will be passed on to consumers; and *(4)* the appropriateness of a sliding scale in efficiency analysis, in which efficiencies of a greater magnitude would be given correspondingly greater weight in evaluating the net effect of the transaction.

Canada stated that its Competition Act contains an explicit recognition of an efficiencies defence in merger analysis, which is unique among OECD countries. An anticompetitive merger is to be approved if the efficiency gains from the transaction will be greater than and will offset the expected anticompetitive affects of the merger. It must be shown that the gains would not likely be attained if an order against the transaction were made. Relevant to the efficiency analysis is the effect of the transaction on increase in exports or substitution of domestically-produced goods for imported ones. The relevant standard for comparing efficiency gains to anticompetitive effects in Canada is total welfare. Wealth transfers from consumers to producers are neutral in this analysis. Canada is a relatively small, open economy characterised by high concentration in many markets; Canadian firms may not be operating at minimum efficient scale, which causes efficiency issues to be particularly important. To date, however, no case has explicitly turned on efficiencies, either in the Competition Tribunal or the Bureau of Competition Policy. In the Hillsdown case considered by the Tribunal, the defence was raised by the parties, but the Tribunal ultimately ruled that the transaction was not significantly anticompetitive. The Tribunal did consider the efficiency claims, however. In some respects it accepted the Bureau's position on the issue, but in others it differed. The Tribunal would have imposed a lesser burden on the parties to show the probability of achieving the claimed efficiencies, and it displayed a reluctance to articulate a precise test for the trade-off analysis.

The European Commission discussed the Aerospatiale-Alenia/de Havilland case, which is outlined in the EC's Note. The claimed efficiencies of 0.5 per cent of the total turnover of the combined parties were considered by the Commission, but even if the benefits were judged to sufficiently contribute to the development of technical and economic progress within the meaning of Article 2 of the Merger Regulation, the Commission concluded that consumers would not have sufficiently benefited from these gains. This analysis, moreover, was conducted in the context of the overall assessment of whether the merger would significantly eliminate competition through the creation or strengthening of a dominant position.

The Chairman introduced the third issue for discussion, the extent of differences in treatment of efficiencies as between mergers and horizontal agreements.

Italy stated that the standard for evaluation of efficiencies does differ as between mergers and horizontal agreements, because the competition standards differ. For mergers the standard is creation or enhancement of a dominant position, while for restrictive agreements the standard is substantial elimination of competition. In these respects Italy resembles the EU. An anticompetitive merger under this standard

is likely to have serious anticompetitive effects, while on the other hand projected efficiency gains are prospective and difficult to quantify. In the context of restrictive agreements, it must be shown that the net gains will benefit consumers and that the restrictions on competition are necessary to achieve the efficiency gains. In the IGAT case described in the Note, which involved a production joint venture, these criteria were satisfied and the transaction was approved. Also, in that case there remained outside the joint venture a sufficient number of competitors to prevent the exercise of market power by the joint venture.

The Chairman invited general discussion on the subject, also noting that a Note written by Switzerland was available for the delegates.

Germany described its policies relating to efficiencies in lieu of a written presentation. The merger control regulation, adopted in 1974, does not provide for an efficiency defence. The competitive effects test is dominance; mergers that fall short of that threshold are presumed to achieve efficiencies, but at the level of dominance efficiencies cannot offset the anticompetitive effects, with one exception. Pursuant to the so-called "Minister's authorisation" the Minister may approve a merger that has been denied by the Bundeskartellamt if the anticompetitive effects are outweighed by advantages to the entire economy or it is justified by a predominant public interest. Relevant consideration include not just economic efficiencies, but wider interests such as national employment or energy policies, or enhancement of international competitiveness. Only 15 applications for this authorisation have been made, however, and of these only six have been granted in whole or in part. With respect to restrictive agreements, efficiency considerations may outweigh anticompetitive effects of such agreements, but as with mergers, if the agreement results in dominance the efficiency considerations are not relevant.

A BIAC representative from the United States [see Note, "Here's to a More Significant Role for Efficiencies in U.S. Merger Analysis", by James F. Rill and A. Paul Victor] stated that in the U.S. the efficiencies defence continues to be applied more strictly than in many other countries, but there is an encouraging trend toward liberalisation. Consideration should be given to employing higher market share screens to give greater effect to efficiency gains. Longer time frames should be employed in the analysis and all types of efficiencies, including savings in fixed costs, should be cognizable. The total welfare standard, not consumer welfare, should be employed.

A BIAC representative from Canada [see Note, "The Treatment of Efficiency Gains in Canadian Merger Analysis", by Paul S. Crampton] noted that the incorporation of a statutory efficiency defence into Canadian law created high expectations, but they have not been met, in that as noted by the Canadian delegation no case has yet turned on the defence. In his view this is primarily because the defence is "all or nothing", requiring full compliance with rigorous economic standards that govern the defence. Business executives do not operate in those terms, and are unable to effectively mount a convincing case when necessary. Preferable would be a "sliding scale" approach, in addition to the current standard, in which efficiencies would be part of the evaluation of the overall anticompetitive effects.

A BIAC representative from the EU urged that dynamic efficiencies should be fully considered in efficiency analyses. They are especially important in innovative, rapidly evolving markets, and they also present difficult analytical problems relating to market definition, dominance and enjoyment of such benefits by consumers. He also noted that structural joint ventures and mergers are comparable types of transactions and should not be subject to differing standards relating to efficiencies.

Australia noted that efficiency-generating mergers can be of two types: procompetitive transactions creating new stimulus to competition through efficiencies, and transactions creating efficiencies that themselves are not necessarily procompetitive, and may be anticompetitive if achieved by a dominant firm. The first type is relatively straightforward and is easily dealt with. The second is more problematic, and is subject to different approaches in OECD countries, ranging from being considered irrelevant to integration into the overall competitive assessment. Another possible approach for consideration of the issue is to place such claims in a separate process: a separate procedure would be formally invoked at the

request of the proponent; the procedure would be public, and the proponent would have a heavy burden of persuasion. The result could be that the issue could be more directly considered, perhaps creating a greater willingness by merging parties to raise it, but it would remain a difficult defence to sustain.

The Netherlands stated that a new competition law which has been prepared for submission to Parliament in 1996 contains a merger control provision but an efficiencies defence is not included. It appears that in those countries that do have such a defence very few transactions have been approved specifically on the basis of efficiencies. If this is so, the justification for the defence is not readily apparent. Why bother? On the other hand, the new law does recognise efficiencies in analysis of restrictive agreements, as in Article 85(3) of the Treaty of Rome. Such agreements are created for one or more specific purposes, which may directly involve efficiency considerations. Also, exemptions for restrictive agreements are limited in time and scope, as are the agreements themselves. Mergers, on the other hand, are permanent, and defences should therefore be more narrowly construed.

New Zealand questioned the rationale for the consumer surplus standard in the trade-off analysis. If the merger in question results in an increase in price above the competitive level, it is difficult to see how the efficiency gains will be passed on to consumers, at least in the short run. In the longer run that could happen, if the supracompetitive price attracts new entry and prices fall.

Canada noted that while efficiency considerations have not been determinative in a case in Canada, they have been considered in several cases. It also appears to be true, however, that many if not most mergers are proposed for reasons -- legitimate ones -- other than efficiencies, such as product diversification, accessing a new market, etc. Also, the point raised by New Zealand regarding the difficulties associated with the consumer surplus standard is consistent with the position of the Bureau of Competition Policy that the relevant standard should be total surplus, not consumer surplus.

The United Kingdom noted that there seems to be some variation in the way efficiencies are considered in merger analysis in different countries, although some countries, notably the U.S. and Canada, there are efforts to bring efficiency considerations into play more often. A related procedural point may be relevant: the usual short period within which decisions on mergers must be made can preclude consideration of efficiencies, which is a time consuming exercise.

The United States responded to the question of "why bother?" While efficiencies have seldom been determinative in a formal sense, it is certain that the issue has been relevant to enforcement agencies in decisions not to challenge mergers as a matter of prosecutorial discretion. Also, efficiencies are clearly important in joint venture analysis. As to the question regarding the application of the consumer surplus standard, if the efficiency defence is limited to close cases, for example in a market where the merger reduces the number of sellers from five to four, there will be the certainty of achieving the efficiency gains, but prices may not rise as a result of the merger, particularly where the efficiencies are significant.

Ireland responded to the point made by New Zealand on the consumer surplus standard. If the price increase does indeed induce new entry that forces the price back down, then in fact the merger may not have been anticompetitive, and application of the efficiency defence would not have been necessary.

The EC elaborated on the efficiency analysis under Article 85(3). It operates to authorise transactions that would otherwise be prohibited under 85(1), and in that sense is a defence, but the competitive analysis also can be likened to a sliding scale. The upper bound of the scale is the elimination of competition in respect of a substantial part of the market. No transaction, regardless of efficiencies, that has such an effect can be permitted.

The Chairman thanked all participants for their contributions to the discussion. He shared the feelings expressed by several delegates that the discussion warranted additional time, and hoped that the Committee might someday return to one or more aspects of the subject.

AIDE-MÉMOIRE de la DISCUSSION

Le Président (M. Jenny) a présenté le sujet. Il a observé que les documents évoquent trois grandes questions qu'il propose d'examiner l'une après l'autre : *(1)* l'argument de l'efficience dans les lois des pays Membres, en particulier la question de savoir si les efficiences alléguées ne valent qu'à titre de moyen de défense dans une transaction qui, sans cela, serait anticoncurrentielle, ou si elles valent pour l'analyse de la concurrence proprement dite ; *(2)* les normes appliquées lors de l'examen des efficiences, notamment l'admissibilité des divers types d'arguments d'efficience et le critère de preuve ; et *(3)* la façon, éventuellement différente, dont est traité l'argument de l'efficience dans les fusions et dans les accords autres que les fusions.

La Commission européenne a déclaré que ces normes diffèrent incontestablement selon qu'il s'agit de cas de fusions ou de pratiques restrictives. Le Règlement du Conseil sur les fusions définit les critères à utiliser lors de l'examen des fusions, critères parmi lesquels figurent les efficiences, mais si la fusion est en définitive jugée comme étant anticoncurrentielle -- création ou renforcement d'une position dominante qui entraîne une limitation sensible de la concurrence -- les efficiences ne constituent pas un moyen de défense. On citera à cet égard l'affaire Nordic Satellite dans laquelle la transaction aurait suscité des efficiences importantes, mais dont on a estimé qu'elle créait ou renforçait une position dominante sur plusieurs marchés, ce qui l'a fait interdire.

Le Japon a indiqué que sa loi Anti-monopole ne reconnaît pas expressément la notion d'efficience mais les procédures administratives appliquées pour le contrôle des fusions tiennent compte des efficiences. Celles-ci ne sont pas examinées séparément mais à l'occasion de l'évaluation globale des effets de la transaction sur la concurrence. Ainsi, une fusion qui accroît l'efficience des petites entreprises sur le marché peut renforcer la concurrence. En revanche, les gains d'efficience résultant de la fusion réalisée par une entreprise dominante pourraient incliner à penser qu'il y a pouvoir de marché sur le marché considéré. La question qu'il faut se poser est de savoir quel est l'effet de la fusion sur la concurrence qui s'exerce sur le marché dans son ensemble, et non quels sont les avantages qu'elle pourrait apporter uniquement à l'entreprise faisant l'objet de la fusion.

En Nouvelle-Zélande, les efficiences sont traitées de façon identique, que l'évaluation porte sur une fusion ou sur des pratiques restrictives. Les efficiences sont prises en compte dans les demandes d'autorisation préalable introduites auprès de la Commission du Commerce pour une transaction ou un comportement donné, mais ne peuvent être prises en considération dans les actions d'exécution engagées devant les tribunaux. La Commission fera droit à la demande si la transaction entraîne un "avantage pour le public" avantage qui compense les éventuels effets anticoncurrentiels. Par "avantage pour le public", on entend uniquement les efficiences économiques, et non les avantages pour sociaux. Ce critère a été énoncé par la High Court dans l'affaire Telecom Corporation de NZ. La Commission du Commerce l'a précisé dans ses lignes directrices sur l'avantage pour le public (Guidelines on Public Benefit). Il s'agit de comparer la situation "avec" et "sans" la transaction, et le gain d'efficience doit dépendre de ladite transaction. Dans l'affaire Health Waikato/Midland Health, le projet de transaction a été interdit car il n'avait pas été démontré que les avantages résulteraient uniquement du projet. La Commission peut examiner d'autres éléments que les efficiences dont bénéficient les entreprises demanderesses au stade de la production, et notamment les avantages pour l'environnement et la santé. Toutefois, ces autres avantages sont rarement déterminants, et dans des affaires récentes, la Commission ne les a pas pris en considération.

Le Président a présenté ensuite la question suivante, à savoir les normes à prendre en considération lorsqu'on examine les avantages en termes d'efficience. Il a observé que les normes paraissent en fait varier d'un pays à l'autre. Le Canada semble, par exemple, attribuer la place principale aux efficiences qui en résultent pour les entreprises canadiennes, alors que la Nouvelle-Zélande semble tenir compte également

des efficiences qui en résultent à l'étranger. Lorsqu'ils procèdent à un arbitrage entre gains d'efficience et effets anticoncurrentiels, certains pays paraissent appliquer le critère du "surplus" total alors que d'autres emploient le critère du "surplus des consommateurs".

Les États-Unis ont déclaré que l'argument de l'efficience est actuellement assez controversé. Les instances chargées des questions de concurrence ainsi que les tribunaux prennent plus volontiers en considération les efficiences dans les entreprises communes visant à une intégration que lorsqu'il s'agit de fusions. Dans les cas de fusions, les instances chargées de la concurrence sont davantage disposées que les tribunaux à faire droit à l'argument de l'efficience, mais certaines juridictions inférieures ont également évalué les gains d'efficience escomptés par les parties. Cela a été le cas dans l'affaire University Health dans laquelle le tribunal a examiné les gains d'efficience invoqués par les parties et les a jugés insuffisants pour compenser les effets anticoncurrentiels de la fusion. De fait, dans aucune affaire jugée, les arguments d'efficience n'ont influé sur la décision. Tous les gains d'efficience liés au processus de concurrence, par exemple une amélioration des coûts unitaires (par opposition à des arguments de caractère plus général, par exemple création d'emplois ou avantages pour l'environnement), seront à considérer, mais ils doivent dépendre expressément de la fusion. On considère généralement aux États-Unis, mais ce point reste débattu, que les parties doivent montrer que les gains d'efficience seront répercutés sur les consommateurs. La Federal Trade Commission procède actuellement à des auditions sur un certain nombre de problèmes importants de concurrence, notamment sur le rôle exact des gains d'efficience. Parmi les questions examinées, on citera : *(1)* la nécessité de concilier les régimes don font l'objet les efficiences selon qu'il s'agit de fusions ou d'entreprises communes visant une intégration, et selon qu'il s'agit d'instances chargées de la concurrence ou de tribunaux ; *(2)* la nécessité de préciser quels sont les différents types d'efficience et l'importance qu'il faut leur donner ; *(3)* faut-il prouver que les efficiences réalisées seront répercutées sur les consommateurs ; et *(4)* l'opportunité de définir pour l'analyse de l'efficience un barème, barème dans lequel les gains d'efficiences de plus grande ampleur se verraient attribuer une plus grande importance dans l'évaluation de l'effet net de l'opération.

Le Canada a indiqué que sa Loi sur la concurrence reconnaît expressément l'argument de l'efficience dans l'analyse des fusions, ce qui est un cas unique dans les pays de l'OCDE. Une fusion anticoncurrentielle sera approuvée si les gains d'efficience résultant de la transaction sont supérieurs aux effets anticoncurrentiels escomptés de la fusion et qu'ils compenseront ces effets. Il faut prouver que les gains ne seraient probablement pas obtenus si la transaction faisait l'objet d'une ordonnance d'interdiction. L'effet de la transaction sur l'augmentation des exportations ou sur le remplacement de produits fabriqués dans le pays par des produits importés est à prendre en compte dans l'analyse des efficiences. Le critère appliqué pour comparer les gains d'efficience est celui des effets anticoncurrentiels au Canada. Dans cette analyse, les transferts de richesse des consommateurs aux producteurs sont neutres. Le Canada est une petite économie ouverte, sont fortement concentrés où bon nombre de marchés ; les entreprises canadiennes risquent de ne pas opérer au niveau d'efficience minimal, ce qui explique que les problèmes d'efficience sont particulièrement importants. Mais jusqu'à présent, aucune affaire n'a expressément porté sur les efficiences, que ce soit devant le Tribunal de la concurrence ou devant le Bureau de la politique de la concurrence. Dans l'affaire Hillsdown dont avait saisi le Tribunal, ce moyen de défense a été invoqué par les parties, mais le Tribunal a, en fin de compte, jugé que la transaction n'avait pas d'effets anticoncurrentiels sensibles. Il a toutefois examiné les gains d'efficience. Il a fait droit sur certains points à la position adoptée par la question sur le Bureau mais il s'est écarté sur d'autres. Le Tribunal n'aurait pas obligé les parties à prouver que les gains d'efficience allégués seraient probablement réalisés, preuve qu'il leur aurait été difficile d'administrer et il s'est montré peu disposé à énoncer un critère précis à appliquer dans l'arbitrage entre gains d'efficience et effets anticoncurrentiels.

La Commission européenne a examiné l'affaire Aérospatiale-Alenia/de Havilland, présentée dans sa note. La Commission a pris en considération les gains d'efficience de 0.5 pour cent du chiffre d'affaires global, qu'invoqueraient les parties mais même si elle a jugé que les avantages contribuaient suffisamment au développement du progrès technique et économique au sens de l'article 2 du Règlement sur les fusions, elle a conclu que les consommateurs n'en auraient pas suffisamment profité. En outre, cette analyse a été

réalisée dans le cadre de l'évaluation globale tendant à déterminer si la fusion supprimerait sensiblement la concurrence du fait de la création ou du renforcement d'une position dominante.

Le Président a présenté la troisième question soumise à examen, à savoir l'importance des différences dans l'évaluation des efficiences suivant qu'il s'agit de fusions ou d'accords horizontaux.

L'Italie a déclaré que si la norme d'évaluation des efficiences diffère, selon qu'il s'agit de fusion ou d'accords horizontaux, c'est parce que les normes de concurrence elles-mêmes diffèrent. Pour les fusions, le critère est la création ou le renforcement d'une position dominante, alors que pour les accords restrictifs, le critère est l'élimination substantielle de la concurrence. Sur ces points, l'Italie se rapproche de l'UE. Une fusion anticoncurrentielle au regard de ce critère aura probablement des effets anticoncurrentiels sérieux, alors que de l'autre côté, les gains d'efficience escomptés sont prospectifs et difficiles à chiffrer. Lorsqu'il s'agit d'accords restrictifs, il faut prouver que les gains nets bénéficieront aux consommateurs et que pour réaliser les gains d'efficience, il est nécessaire de limiter la concurrence. Dans l'affaire IGAT décrite dans la note, qui visait une entreprise commune de production, il avait été satisfait à ces critères et l'opération a été approuvée. Par ailleurs, dans ladite affaire, il subsistait en dehors de l'entreprise commune un nombre de concurrents suffisant pour l'empêcher d'exercer un pouvoir de marché.

Le Président a ouvert ensuite un débat général sur la question en indiquant aux délégués que la Suisse avait elle aussi soumis une note par écrit.

L'Allemagne, qui n'a pas adressé de communication écrite, a exposé les politiques qu'elle applique dans ce domaine. Le règlement sur le contrôle des fusions, adopté en 1974, ne prévoit pas de moyens excipant de l'efficience. Le critère concernant les effets sur la concurrence est la domination du marché ; les fusions qui ne répondent pas à ce critère sont présumées réaliser des gains d'efficience, mais lorsqu'il y a domination, ces gains ne peuvent compenser les effets anticoncurrentiels, à une exception près. Conformément à la disposition qui prévoit l'autorisation dite "du Ministre", celui-ci peut approuver une fusion rejetée par la Bundeskartellamt si les effets anticoncurrentiels sont compensés par des avantages pour l'ensemble de l'économie, ou si la fusion est justifiée par l'intérêt général. Il ne s'agit pas seulement de prendre en considération des efficiences économiques, mais des intérêts élargis tels que l'emploi national ou les politiques énergétiques, ou encore un renforcement de la compétitivité internationale. Toutefois, cette autorisation n'a fait l'objet que de 15 demandes, et elle a été accordée pour la totalité ou une partie dans six cas seulement. S'agissant des accords restrictifs, les considérations d'efficience peuvent compenser les effets anticoncurrentiels de ce type d'accords, mais comme pour les fusions, elles ne sont pas prises en compte si l'accord aboutit à une domination du marché.

Un membre du BIAC représentant les États-Unis, [voir note "Here's to a More Significant Role for Efficiencies in U.S. Merger Analysis" (Plaidoyer en faveur d'un rôle plus important à donner aux efficiences dans l'analyse des fusions aux États-Unis), par James F. Rill et de A. Paul Victor] a indiqué qu'aux États-Unis, l'argument de l'efficience reste appliqué de façon plus stricte que dans plusieurs autres pays, mais que l'on y observe une tendance encourageante à la libéralisation. Il s'agirait d'appliquer des critères plus rigoureux en ce qui concerne la part de marché afin de donner davantage d'effet aux gains d'efficience. Il conviendrait de faire porter l'analyse sur des périodes plus longues et tous les types d'efficiences, notamment les économies de coûts fixes, devraient pouvoir être connus. Il conviendrait d'appliquer le critère du bien-être global, non celui du bien-être des consommateurs.

Un membre du BIAC représentant le Canada [voir note "The Treatment of Efficiency Gains in Canadian Merger Analysis" (les gains d'efficience dans l'analyse canadienne des fusions) de Paul S. Crampton] a noté que l'on espérait beaucoup de l'incorporation, dans la loi canadienne, de l'argument de l'efficience, mais ces espoirs ont été déçus car, comme l'a noté la délégation du Canada, cet argument n'a été invoqué dans aucune affaire. A son avis, la principale raison en est que cet argument est celui du "tout ou rien", qui exige que les critères économiques rigoureux régissant ce moyen de défense doivent être pleinement respectés. Ce n'est pas ainsi qu'opèrent les chefs d'entreprise qui ne sont pas en

mesure d'élaborer effectivement une argumentation convaincante lorsqu'il le faut. Il serait préférable d'ajouter à la norme actuelle un système "d'échelle mobile", dans lequel les gains d'efficience entreraient dans l'évaluation des effets anticoncurrentiels globaux.

Un membre du BIAC représentant de l'UE a demandé que les efficiences dynamiques soient pleinement prises en compte dans les analyses de l'efficience. Ces efficiences sont surtout importantes sur les marchés novateurs et en rapide évolution ; elles présentent aussi des problèmes d'analyse difficiles à résoudre, qui visent la définition du marché, la domination du marché et le fait que les consommateurs puissent jouir de ces avantages. Il a également noté que les entreprises communes structurelles et les fusions sont des types d'opérations comparables et qu'il ne devrait pas leur être appliqué des normes différentes en matière d'efficience.

L'Australie a fait observer que les fusions génératrices d'efficience peuvent être de deux types : les opérations pro-concurrentielles qui relancent la concurrence par le biais des efficiences et les transactions créant des efficiences qui elles-mêmes ne sont pas nécessairement pro-concurrentielles, et qui peuvent être anticoncurrentielles si elles sont réalisées par une entreprise dominante. La première catégorie est relativement bien circonscrite et facile à gérer. La seconde soulève davantage de problèmes, et il fait l'objet d'approches différentes d'un pays de l'OCDE à l'autre, selon qu'elle est jugée sans intérêt pour l'intégration, ou qu'elle est comprise dans l'évaluation de la concurrence. Autre approche possible : replacer ces arguments dans une procédure distincte : cette procédure serait officiellement invoquée sur requête du demandeur ; elle serait publique et les preuves seraient principalement à la charge du demandeur. La question pourrait alors être examinée de façon plus directe, les parties procédant à la fusion pouvant peut-être alors être davantage disposées à invoquer, mais ce moyen de défense qui resterait pourtant difficile à faire valoir.

Les Pays-Bas ont fait état d'une nouvelle loi sur la concurrence dont le texte devrait être soumis au Parlement en 1996 ; cette loi contient une disposition sur le contrôle des fusions mais elle ne prévoit pas de moyen excipant de l'efficience. Il semble que dans les pays où ce moyen existe, les transactions approuvées expressément sur la base de l'efficience ont été très peu nombreuses. Dans ce cas, ce moyen ne paraît pas vraiment justifié. Pourquoi s'en préoccuper ? En revanche, le nouveau texte reconnaît bien les efficiences dans l'analyse des accords restrictifs, comme c'est le cas dans l'article 85(3) du Traité de Rome. Ces accords sont conclus en vue d'un ou de plusieurs objectifs spécifiques qui peuvent directement mettre en cause des considérations d'efficience. Par ailleurs, les exemptions concernant les accords restrictifs sont limitées dans le temps et dans leur ampleur, comme le sont les accords eux-mêmes. Par contre, les fusions ont un caractère permanent et les moyens de défense devraient donc être interprétés de façon plus étroite.

La Nouvelle-Zélande s'est interrogée sur les raisons pour lesquelles l'arbitrage entre les gains d'efficience et les effets anticoncurrentiels devrait s'appuyer sur le critère du "surplus du consommateur". Si la fusion en cause entraîne une hausse des prix supérieurs aux prix de concurrence, on voit mal comment les gains d'efficience seront répercutés sur les consommateurs, du moins à court terme. A plus long terme, ils pourraient l'être si le prix supérieur au prix de la concurrence attire de nouveaux entrants, ce qui se traduit par une baisse des prix.

Le Canada a noté que les considérations d'efficience n'ont pas été déterminantes dans aucune affaire précise, mais qu'elles ont été prises en compte dans plusieurs affaires. Toutefois, il semble vrai que bon nombre de fusions, sinon la plupart d'entre elles, sont envisagées pour des raisons -- légitimes -- autres que les gains d'efficience, notamment une diversification de la production, l'accès à un nouveau marché, etc. Par ailleurs, l'observation de la Nouvelle-Zélande concernant les difficultés que soulève le critère du surplus du consommateur concorde avec la position du Bureau de la politique de la concurrence selon lequel la norme à considérer devrait être le surplus total et non le surplus du consommateur.

Pour le Royaume-Uni, il semble que la façon dont l'efficience est prise en compte dans l'analyse des fusions varie quelque peu d'un pays à l'autre, bien que certains, notamment les États-Unis et le Canada, s'efforcent de faire appel plus souvent aux considérations d'efficience. Un point de procédure pourrait entrer en ligne de compte : la période durant laquelle doivent être prises les décisions sur les fusions, étant généralement brève, il peut être impossible de procéder à l'examen des efficiences, pour lequel il faut du temps.

Les États-Unis ont répondu à la question des Pays-Bas, à savoir "Pourquoi s'en préoccuper ?". Si l'efficience a rarement été déterminante au sens formel du terme, la question ne s'en est pas moins posée aux instances d'exécution lorsqu'elles ont décidé de ne pas attaquer les fusions, décisions laissées à la discrétion des juges. Par ailleurs, les efficiences jouent à l'évidence un rôle important dans l'analyse des entreprises communes. Quant à la question concernant l'application du critère du surplus du consommateur, si l'argument de l'efficience est limité à des cas très proches, par exemple, un marché où la fusion réduit de cinq à quatre le nombre de vendeurs, il est à peu près certain que les gains d'efficience seront réalisés, mais les prix risquent de monter du fait de la fusion, surtout lorsque ces gains sont importants.

L'Irlande a répondu à la remarque de la Nouvelle-Zélande concernant le critère du surplus du consommateur. Si la hausse des prix attire sur le marché de nouveaux entrants qui font retomber les prix, la fusion peut, en fait, ne pas avoir été contraire à la concurrence et il n'aurait pas été nécessaire de recourir à l'argument de l'efficience.

La CE a donné des précisions sur l'analyse de l'efficience au regard de l'article 85(3). Cet article vise à autoriser les transactions qui, sans cela, seraient interdites au titre de l'alinéa 1, et en ce sens, il s'agit d'un moyen de défense, mais l'analyse de la concurrence peut également être assimilée à une échelle mobile. La limite supérieure correspond à l'élimination de la concurrence sur une partie substantielle du marché. Aucune transaction ayant un effet de ce genre ne peut être autorisée, quels que soient les gains d'efficience.

Le Président a remercié tous les participants pour leurs contributions. Il a déclaré partager les points de vue formulés par plusieurs délégués, à savoir que le débat méritait davantage de temps, et il a exprimé l'espoir que le Comité puisse revenir un jour ou l'autre sur un ou plusieurs aspects de la question.