Public Comments of

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On

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Draft Merger Enforcement Guidelines
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INTRODUCTION

Thank you for inviting me to comment on the Draft Merger Enforcement Guidelines. I have only a limited understanding of Canadian competition law and enforcement policy and I hesitate to opine in any area in which I cannot claim at least reasonable expertise. The following comments are thus pitched at the level of general principles of antitrust economics and what I believe are transferable lessons from United States merger law and enforcement policy.

My comments include suggestions for strengthening the Draft Guidelines in three subject areas: (1) identification of entrenchment of existing market power as an independent theory of harm, (2) articulation of market definition principles, and (3) inference of competitive effects from market structure evidence. I order the discussion of these subject areas in this way to reflect the tendency of comments in latter subject areas to build upon comments in earlier subject areas.

ENTRENCHMENT OF MARKET POWER AS AN INDEPENDENT THEORY OF HARM

Comment 1. The Final Guidelines should stake a clear position on whether and when a merger is likely to be opposed for its tendency to entrench existing market power.

The legal recognition of entrenchment of existing market power as a theory of harm in merger review is not well settled in the United States. My own view is that U.S. merger law supports the conclusion that a merger may be found illegal on the basis of its tendency to protect and stabilize

* I submit these comments in my personal capacity. The views expressed herein do not purport to represent those of the University of Iowa or of any other organization with which I have any affiliation.

already-ongoing exercises of express or tacit collusion.[1] To the extent that Canadian competition law supports a similar conclusion, I suggest identifying that theory of harm explicitly in the Final Guidelines.

At present, different aspects of the Draft Guidelines present conflicting messages on whether and when a merger that tends to entrench market power would be opposed as illegal. In some places, possession of existing market power is described as an exacerbating factor in the evaluation of concerns about enhanced market power through merger.[2] In other places, entrenchment of existing market power appears to represent a self-contained theory of harm.[3] Elsewhere yet, the Draft Guidelines seem to limit the scope of inquiry to only those mergers that affirmatively enhance market power. An example is expression of the underlying inquiry in the following terms: whether the merger would leave the merged entity with "materially greater market power than it would have had without the merger."[4]

As I explain in more detail in my comments on market definition principles, the evaluation of mergers for their capacity to entrench competition relies on subtly different reasoning than the evaluation of mergers for their capacity to enhance future market power. An intuitive example of the difference in approach is the well-known *Cellophane Fallacy*, which applies to the definition of relevant markets in the entrenchment context, but not to the definition of relevant markets in the enhancement context.[5]

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[1] *See generally* Sean P. Sullivan, *Anticompetitive Entrenchment*, 68 U. KAN. L. REV. 1133 (2020).

[2] *E.g.*, Draft Guidelines § 3.2 ¶ 53 ("Where firms have significant market power or have entrenched their competitive position, even a merger that has a small effect on their market power may substantially harm competition.").

[3] *E.g.*, *id.* § 4.4 ¶ 153 ("We may assess whether the merger would contribute to the entrenchment of the market position of leading incumbents, including the merging parties. For example, this may occur where the merger increases barriers to entry or expansion, or otherwise harms the competitive process, such that there is a greater likelihood that leading firms will maintain the ability to individually or collectively exercise market power."); *see also* *id.* § 4.4.1.2 ¶ 192 ("[Coordinated effects concerns] also include[] cases where coordination already exists but could become more effective or extensive because of the merger.").

[4] *Id.* § 3.2 ¶ 44. The full paragraph reads: "Under section 92 of the Act, we consider two types of situations: mergers that prevent competition, and mergers that lessen competition. . . . In both cases, we assess whether the merged entity has *materially greater market power* than it would have had without the merger." (emphasis added) *Id.*

[5] *See* Sullivan, *supra* note 1, at 1153-54 ("[W]here an oligopoly is already tacitly colluding, defining markets relative to the collusive prevailing price tends to produce broad relevant markets in which competition looks stronger and less conducive to the exercise of market power than it actually is."); *see also* Sean P. Sullivan, *Market Definition*, *in* 1 RESEARCH HANDBOOK ON ABUSE OF DOMINANCE AND MONOPOLIZATION 8, 18-22 (Pinar Akman, Konstantinos Stylianou, & Or Brook eds., Edward Elgar 2023) (explaining the difference in market definition when the theory of harm is an increase in market power as opposed to the maintenance of market power).

ARTICULATION OF MARKET DEFINITION PRINCIPLES

Comment 2. The Final Guidelines should be clear and explicit about the possibility that more than one relevant market may be used to evaluate the legality of a merger.

While I appreciate that thoughtful commentators continue to believe there can be only one relevant market for every case, the illogic of that position is too obvious to ignore.[6] Most find it intuitive that multiple relevant markets should be defined when evaluating a merger in which competitive overlaps span different products and services. If the merging entities happen to overlap in their production of electric cars and computer-vision software, for example, few would insist on defining a single "cars and software" relevant market. It should be no less obvious that multiple relevant markets may be required to evaluate different theories of harm implicated by the same merger. The market that is appropriate for evaluating the coordinated-effects potential of the merger may not be the same market that is appropriate for evaluating the unilateral-effects potential of the merger, which may not be the same market that is appropriate for evaluating the non-horizontal effects potential of the merger. Relevant markets are used to evaluate the potential for specific competitive effects of a merger, and different relevant markets may be needed to evaluate different specific competitive effects.[7]

The Draft Guidelines present mixed messaging on the identification of multiple relevant markets. Footnote 25 of the Draft Guidelines provides a clear and explicit statement that I would suggest moving to the main text: "Because relevant markets are defined around a particular focal product, a single merger may affect multiple relevant markets. . . . Any properly defined relevant market may be used in our analysis."[8] I recommend describing relevant markets as being defined around theories of harm,[9] not focal products, but the multimarket implication is the same. Elsewhere, however, the Draft Guidelines make repeated reference to "*the* relevant market" in both grammatically and substantively singular terms.[10]

The Draft Guidelines specifically assert that a merger may implicate both unilateral-effects and coordinated-effects concerns, and already specifically explains that these effects could arise in

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[6] *See* David Glasner & Sean P. Sullivan, *The Logic of Market Definition*, 83 ANTITRUST L.J. 293, 326-30 (2020) (explaining and correcting this "single market fallacy").

[7] *See id.* at 330-36; *see generally* Sean P. Sullivan, *Modular Market Definition*, 55 UC DAVIS L. REV. 1091 (2021) (identifying how different tests of market definition produce relevant markets targeted to assessing different theories of harm and suggesting default tests to adopt in various contexts).

[8] Draft Guidelines, § 4.2.1.1 ¶ 77 n.25.

[9] *See* Glasner & Sullivan, *supra* note 6, at 312-24 (explaining why relevant markets should be defined around hypothesized anticompetitive effects).

[10] *E.g.*, Draft Guidelines § 4.2.1.1 ¶ 78 ("Once we have defined *the* relevant market . . . ." (emphasis added)); *id.* § 4.2.1.1 ¶ 78 n.27 ("Constraints on a firm's pricing behaviour may also come from outside *the* defined relevant market." (emphasis added)); *id.* § 4.2.1.2 ¶ 92 ("If the hypothetical monopolist would do so, the test suggests this is *the* relevant market." (emphasis added)).

different markets.[11] It would be helpful to elaborate that if a merger raised both unilateral and coordinated effect concerns, then market definition would ordinarily be performed separately for each such concern, collapsing into a single relevant market only when both market definition exercises happened to suggest the same relevant market. In the context of differentiated-goods unilateral effects predictions, it would also be helpful to note that the prediction of a significant unilateral price effect implies that a relevant market defined to include only the merging parties would constitute a relevant market under the HMT.[12]

Comment 3. The Final Guidelines should leave more room for flexibility and discretion in implementing the HMT.

The Draft Guidelines helpfully describe the HMT as an "analytical technique"[13] and "a conceptual framework"[14] for evaluating other evidence. These statements nicely capture what the HMT is (a flexible analytical framework for defining useful relevant markets) and what it is not (a rote, mechanical algorithm for producing sensible results). I suggest further committing to this flexible understanding of the HMT by qualifying or withdrawing some of the mechanical commentary on the implementation of the HMT in the current draft.

To illustrate what I mean, consider the following three statements about how the HMT is implemented and whether they may unnecessarily limit enforcement discretion:

1. "The hypothetical monopolist test defines a market as the smallest set of products, and the smallest geographic area, in which [a SSNIP would be profitable]."[15] While it may often be appropriate to focus on the smallest market in which a hypothetical monopolist would profitably impose a SSNIP, there are cases in which a broader market better serves enforcement interests. One example is where available data exist to facilitate market share and market structure analysis only for a broader definition of the market. Another example is where enforcement concerns include the possibility of tacit collusion involving firms outside the narrowest possible scoping of the relevant market.[16] I suggest describing enforcement decisions as being "typically" made with an eye to the smallest market

[11] *Id.* § 4.4.1.2 ¶ 187 ("We may assess unilateral and coordinated effects separately. . . . A merger may lead to both types of effects occurring in the same or different markets.").

[12] *See* Sullivan, *Modular Market Definition*, *supra* note 7, at 1116 ("[I]f we take the merging parties as the provisional market in the HMT, and if we take the unilateral effects prediction as evidence that the hypothetical monopolist would increase its prices by a small but significant amount, then the unilateral effects prediction would validate the merging parties as a relevant market under the very methodology of the HMT").

[13] Draft Guidelines § 4.2.1.2 ¶ 87.

[14] *Id.* ¶ 88.

[15] *Id.* ¶ 89.

[16] *See* Glasner & Sullivan, *supra* note 6, at 334-35 (explaining why leaving the choice of HMT market breadth to the enforcing authority is consistent with economic principles and obviates reliance on the narrowest market principle).

satisfying the HMT, but reserving discretion to adopt broader HMT markets when doing so better illustrates the basis for competitive concern.

2. "If we are assessing a change in price, we usually consider a five-percent price increase to be significant . . . . Market characteristics may support using a different price increase . . . as a SSNIP."[17] I recommend against describing the five percent hypothesized price increase as a measure of significance. Intuitively, it is easy to imagine how a one percent increase in the price of a large volume of trade could be more meaningful than a ten percent increase in the price of a small volume of trade. More importantly, the size of the hypothesized SSNIP should be selected on the basis of the likely competitive effect of the merger. In a market in which the largest plausible post-merger price increase would be two percent, for example, the appropriate choice of SSNIP is two percent.[18]

3. "The base price is typically the prevailing price in the relevant market."[19] The choice of base price in the HMT is a matter of substantive significance. Use of the prevailing price as the base price in the exercise is appropriate when the competitive effect of concern is enhancement of market power, here represented as an increase in price above the status quo. If the competitive effect of concern is the entrenchment of market power, the base price should be specified as an estimate of what the price would be if the relevant exercise of market power was not already ongoing.[20] The need for this flexibility in specification of the base price is more than an academic quibble. Especially where entrenchment of ongoing coordination is a concern, uncritical reliance on a prevailing price baseline will systematically bias enforcement against the identification of entrenchment concerns by defining markets that are broader than appropriate—the *Cellophane Fallacy* in a merger context.[21]

Comment 4. The Final Guidelines should connect the discussion of product and geographic evidence to the HMT.

The Draft Guidelines identify "qualitative indicators of substitutability and other evidence [relevant to definition of a relevant product market]"[22] as well as "qualitative indicators of substitutability and other evidence [relevant to definition of a relevant geographic market]."[23] The Final Guidelines should make explicit that these qualitative indicators are used to implement the

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[17] Draft Guidelines § 4.2.1.2 ¶ 91.

[18] *See* Glasner & Sullivan, *supra* note 6, at 316-19 (explaining in greater detail why the size of the SSNIP should be customized to fit the magnitude of the predicted competitive effect).

[19] Draft Guidelines § 4.2.1.2 ¶ 95.

[20] *See* Glasner & Sullivan, *supra* note 6, at 319-24.

[21] *See id.* at 319-22.

[22] Draft Guidelines § 4.2.1.3 ¶ 100.

[23] *Id.* § 4.2.1.4 ¶ 103.

HMT; they are not independent bases for identifying relevant markets that would not otherwise satisfy the HMT.

This should be made explicit to separate appropriate market definition practice from the error that the United States has long made in treating "practical indicia" of market boundaries as an independent basis for defining relevant markets.[24] While much could be said about the error of approaching market definition as an observational exercise in seeking qualitative indicia of market boundaries, a simple thought experiment suffices to show why satisfaction of the HMT is essential to subsequent market structure reasoning:

> Suppose a relevant market defined by qualitative evidence would not otherwise qualify as a relevant market under the HMT. By assumption, obtaining a 100% share of this market would not afford the post-merger entity incremental market power. This is definitional, given that we assume the market would fail the HMT. By the same reasoning, no anticompetitive effects could result from any smaller increase in the concentration of this market, and thus no shares or other concentration evidence derived from the market could plausibly support competitive effects predictions.

Qualitative evidence is essential to implementing the HMT in all but the most extreme of circumstances, and the type of evidence discussed in Draft Guidelines §§ 4.2.1.3 and 4.2.1.4 is suited to that application.

INFERENCE OF COMPETITIVE EFFECTS FROM MARKET STRUCTURE EVIDENCE

Comment 5. It would be helpful for the Final Guidelines to connect market structure analysis to the definition of relevant markets.

The Draft Guidelines state that "Under subsection 92(2) of the Act, mergers that result, or are likely to result, in a significant increase in concentration or market share are presumed to substantially harm competition."[25] From an economic perspective, the justification for inferring anything about competitive effects from market shares or other market structure evidence derives from the way in which a relevant market is defined. This is substantially the same point just made in relation to qualitative evidence of market boundaries. Relevant markets defined by the HMT are constructed in a way that invests market shares with competitive effects significance. Relevant markets defined by other methods and tests are not guaranteed to share this property.

[24] *See* Brown Shoe Co. v. United States, 370 U.S. 294, 325 (1962); Fed. Trade Comm'n and U.S. Dep't. of Justice, Merger Guidelines § 4.3 (2023).

[25] Draft Guidelines § 4.1 ¶ 65.

Comment 6. It would be helpful for the Final Guidelines to identify the ways in which market structure and market concentration evidence may inform the inference of specific types of competitive effects.

The Draft Guidelines state that "[m]arket structure is often a key indicator of market power and of the relative significance of competitors." [26] As just discussed, one immediate qualification of this assertion is that relevant markets must be defined using an appropriate methodology for market structure evidence to have this evidentiary significance. Beyond this, "market power" and "relative significance" are not abstract properties of commercial actors. As I have said in another context:

> The relevance of market structure evidence is not that it tells us how a merger influences some platonic account called "market power." The relevance of market structure evidence is that it tells us specific things about each of several specific ways that a merger might allow firms to exercise certain types of market power."[27]

If would be helpful if the Final Guidelines could indicate, even in general terms, how market structure and market concentration evidence would be used to evaluate some of the specific competitive effects that the document describes. The measurement of concentration according to the HHI and the use of HHI concentration thresholds to predict competitive consequences of mergers was, in the United States, originally envisioned as a way of identifying mergers likely to cause coordinated effects.[28] The United States merger guidelines later reoriented toward a focus on unilateral effects and other considerations, but never adequately revised articulation of the market structure inference to connect market structure evidence to these other competitive concerns.[29] Thoughtful explication of those relationships would make the Final Guidelines a model for other jurisdictions to follow.

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[26] *Id.* § 4.2.2.1 ¶ 129.

[27] Sean P. Sullivan, *The Evolution (and Devolution) of Market Structure Reasoning*, *in* THE 2023 U.S. MERGER GUIDELINES - A REVIEW 147, 152 ¶ 437 (Sean Sullivan ed., 2024).

[28] *See id.* at 157-60.

[29] *See id.* at 160-69.