CT-01/009

THE COMPETITION TRIBUNAL

IN THE MATTER OF an application by the Commissioner of Competition for a consent order pursuant to sections 92 and 105 of the *Competition Act*, R.S.C. 1985, c. C-34;

AND IN THE MATTER OF the acquisition by Abitibi-Consolidated Inc. of all of the outstanding shares of Donohue Inc.;

BETWEEN:

THE COMMISSIONER OF COMPETITION

Applicant

- and -

ABITIBI-CONSOLIDATED INC.

Respondent

CONSENT ORDER IMPACT STATEMENT

I. INTRODUCTION

1. The Commissioner of Competition (the "Commissioner") files this statement pursuant to section 77 of the *Competition Tribunal Rules*. This statement describes the circumstances surrounding the Draft Consent Order ("DCO") and its anticipated effect on competition. The DCO is submitted by the Commissioner with the consent of the respondent, Abitibi-Consolidated Inc. ("ACI").

2. The respondent, ACI, does not accept all of the facts, submissions or conclusions of law contained in this Consent Order Impact Statement, but does not contest them for the purposes of this application only. Further, nothing in this Consent Order Impact Statement or in the Commissioner's application for the DCO, shall be taken as an admission by ACI of any facts, submissions or conclusions of law which would support the allegation that ACI's acquisition of all of the outstanding shares of Donohue Inc. (the "Merger") prevents or lessens, or is likely to prevent or lessen, competition substantially in any market.

II. NATURE AND PURPOSE OF PROCEEDING

3. The Commissioner files this Consent Order Impact Statement, a Notice of Application, a Statement of Grounds and Material Facts and a DCO pursuant to sections 92 and 105 of the *Competition Act*, R.S.C. 1985, c. C-34 (the "*Act*").

4. The DCO is designed to eliminate the substantial lessening or prevention of competition that, in the absence of the DCO, the Commissioner concludes would be likely to arise following the Merger in the market for the supply of newsprint in Eastern Canada, *i.e.*, all provinces located east of Manitoba, with the exception of Newfoundland (the "Relevant Market"). The Commissioner respectfully requests the Competition Tribunal's approval of the DCO pursuant to sections 92 and 105 of the *Act*, in order to provide for the appointment of an independent agent to divest the Port-Alfred newsprint mill and other related assets (as defined in the DCO) and thereby eliminate the likelihood of a substantial lessening or prevention of competition within the Relevant Market.

III. CIRCUMSTANCES GIVING RISE TO POTENTIAL IMPACT ON COMPETITION

5. Effective as of June 22, 2000, ACI acquired all of the issued and outstanding

Class “A” Subordinate Voting Shares and Class “B” Shares of Donohue Inc. (“Donohue”). As consideration, ACI paid $42 per share, payable by $12 in cash and 1.8462 ACI common shares per Donohue share, for total consideration of approximately $7.1 billion, including assumed debt.

6. Both ACI and Donohue were engaged in the manufacture and sale of newsprint, pulp, wood products and value-added papers. The Commissioner has concluded that at this time, the Merger has not resulted in a significant lessening or prevention of competition in respect of the supply of pulp, wood products and value-added papers. The Commissioner’s sole concern, as described more fully in the Statement of Grounds and Material Facts, is the effect of the Merger on competition in supply of newsprint to customers located in Eastern Canada.

7. Prior to the Merger, ACI owned and operated a total of twelve newsprint mills in North America, consisting of eight in Canada and four in the United States. Of ACI’s eight Canadian mills, four are located in Québec,[1] two in Ontario and two in Newfoundland. In the United States, ACI had mills in Steilacoom, Washington and Snowflake, Arizona, as well as 50% partnership interests in mills in Augusta, Georgia and Claiborne, Alabama. ACI also has an agreement to market all of the newsprint produced from Boise Cascade’s mill in De Ridder, Louisiana.

8. Prior to the Merger, Donohue operated a total of seven newsprint mills in North America, consisting of five in Canada and two in the United States. Of Donohue’s five Canadian mills, three were located in Québec, one in Ontario and one in British Columbia. In the United States, Donohue had two newsprint mills in Texas.

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[1] In 2000, ACI sold its interest in a paper mill located in Chandler, Québec.Also in 1999, ACI converted its newsprint mill in Thunder Bay, Ontario from newsprint production to value-added papers.

9. Of the newsprint mills currently owned by the merged entity, nine are located in the relevant market of Eastern Canada. These mills are described below:

LOCATION	**NEWSPRINT CAPACITY (metric tonnes per annum)**
Alma, QC	157,000
Iroquois Falls, ON	204,000
Kenora, ON	309,000
Port Alfred, QC	393,000
Shawinigan, QC	316,000
Amos, QC	185,000
Baie Comeau, QC	540,000
Clermont, QC	340,000
Thorold, ON	392,000
TOTAL	**3,329,000**

10. Through the mills described above, the merged entity holds 45.9% of the capacity for newsprint production within Eastern Canada.

11. As outlined in greater detail in the Statement of Grounds and Material Facts, the newsprint industry has a history of imperfect interdependence. The Merger enhances a key pre-condition to effective interdependence by increasing the level of concentration among suppliers in the Relevant Market.

12. Based upon the Commissioner's findings listed in the Statement of Grounds and Material Facts, including the merged entity's high post-Merger market share, the high level of concentration post-Merger, the presence of high barriers to entry and the increased likelihood that interdependence will be effectively acted upon, the Commissioner concludes that the Merger prevents or lessens, or is likely to prevent or lessen, competition substantially in the supply of newsprint within the Relevant Market.

III. DRAFT CONSENT ORDER

13. The DCO provides for a combination of divestiture and supply obligations by the respondent, ACI. Specifically, the DCO provides for the appointment of an independent agent to conduct the divestiture of a newsprint mill owned and operated by ACI in Ville de la Baie, Québec and other related assets (collectively, the "Port-Alfred Mill"), and to cause ACI to supply the purchaser with certain inputs required for the continued effective operation of the Port-Alfred Mill.

14. Prior to seeking the Draft Consent Order, ACI was given an opportunity to divest of the Port-Alfred Mill through a public sale process. This process was carried out pursuant to the terms of an Undertaking delivered by ACI to the Commissioner effective as of December 15, 2000.

15. Pursuant to the terms of the Undertaking, in the event that ACI was unable to

divest itself of the Port-Alfred Mill during this period, the parties agreed that a Consent Order would be sought from the Tribunal and the Mill would be divested through an independent sales agent.

16. ACI has not divested the Port-Alfred Mill. In accordance with the terms of the Undertaking, the Commissioner seeks an order with ACI's consent appointing an independent agent to carry out the divestiture of the Port-Alfred Mill under the provisions of the DCO filed.

17. The Port-Alfred Mill newsprint mill is located in Ville de la Baie, Québec and ranks among the largest newsprint mills in North America with an annual production capability approaching 400,000 tonnes. Newsprint is manufactured on four paper machines brought on stream in 1926 and modernized in the 1970s and 1980s. The Port-Alfred Mill is well maintained and to the best of ACI's knowledge, in full compliance with existing regulations governing air emissions, wastewater discharge and solid waste management. Since 1995, an average of $32.5 million of capital per year has been spent to maintain the asset base of the Mill.

18. The Port-Alfred Mill consists of a wood room, a stone groundwood pulping plant, a bisulphite chemi-mechanical pulping plant, a TMP pulping plant, a repulper for purchased kraft, four paper machines, winders, rewinders, a roll wrapping line, a warehouse, a steam plant and an effluent treatment system. The Mill purchases its electricity from Hydro-Quebec.

19. Shipments from Port Alfred are completed by three modes of transportation: ship (55%), rail (25%) and truck (20%). The mill is located on the shore of the deep

Saguenay River thereby facilitating shipments of newsprint by water. The mill currently employs approximately 672 people. The majority of employees are unionized operating under a labour contract expiring on April 30, 2001.

20. The Port-Alfred Mill is relatively efficient in comparison to other facilities of the same general age and size. Over the past several years, the Mill's cost per tonne of newsprint production has been broadly in line with the Canadian newsprint industry average.

21. In addition to the divestiture of the Port-Alfred Mill, ACI has undertaken to supply the purchaser, or cause the purchaser to be supplied, with wood fibre at fair market value in quantities no less than those in effect for the Port-Alfred Mill during the 2000 calendar year. As a portion of the wood fibre used at the Port-Alfred Mill is supplied by third parties, the DCO requires ACI to use its reasonable best efforts to secure the third party approvals necessary to continue those supply arrangements on current terms. In addition, if desired by the purchaser, the supply arrangements between ACI and the purchaser may be long-term.

22. ACI also is required to use reasonable commercial efforts to transfer to the purchaser the current customers of the Port-Alfred Mill, subject to the customers' own preferences.

23. Under the DCO, the divestiture will be conducted by an independent sales agent (the "Agent") appointed by the Commissioner. The Agent may not be a person that has a direct or indirect conflict of interest with ACI or that has been disqualified pursuant to agreement between the parties.

24. ACI is obligated under the terms of the DCO to assist the Agent in marketing the Port-Alfred Mill and to provide access to records and other information typically required by purchasers in similar circumstances.

25. The period of time within which the Agent must accomplish the sale is subject to an automatic extension where the agent receives a letter of intent, offer or similar written communication of intention to purchase the Port-Alfred Mill from a *bona fide* purchaser during the initial sale period.

26. The Agent is free to set the price and other terms upon which the Port-Alfred Mill will be divested, subject to the restriction that the price and terms the Agent sets are then most advantageous to ACI and consistent with accomplishing the sale, in the opinion of the Agent, acting reasonably and, in no event will the price and terms of an Agent sale equate to those of a “going out of business”, “fire” or liquidation sale.

27. ACI may not object to any sale by the Agent on any other grounds other than the Agent’s malfeasance, gross misconduct or breach of the DCO.

28. To ensure that concentration and, therefore, the risk of interdependent behaviour, is significantly reduced through the divestiture of the Port-Alfred Mill, the Commissioner also seeks a provision in the DCO excluding Bowater Inc. or its affiliates (“Bowater”) as potential purchasers. As outlined in the Statement of Grounds and Material Facts, Bowater is the second largest producer of newsprint in Eastern Canada with 18.5% of the capacity within the Relevant Market.

29. In addition to excluding Bowater, the DCO also provides generally that any proposed divestiture of the Port-Alfred Mill by the Agent is subject to the Commissioner's

approval. The Commissioner's discretion will be exercised to ensure that the purchaser of these assets will eliminate the likelihood of a substantial prevention or lessening of competition within the Relevant Market.

IV. ANTICIPATED IMPACT OF THE PROPOSED REMEDY

30. The divestiture of the Port-Alfred Mill will provide the purchaser with capacity to produce and supply approximately 400,000 tonnes of newsprint. The divestiture of the Port-Alfred Mill reduces ACI's share of Eastern Canadian newsprint capacity by approximately five percentage points to approximately 40%.

31. In 1999, newsprint consumption within Eastern Canada was approximately 825,000 tonnes. The capacity of the Port-Alfred Mill represents approximately 50% of the consumption of newsprint within the Relevant Market. A significant proportion of the Mill's output is currently exported to the United States. Were those exports diverted to the Relevant Market, this would put a significant downward pressure on price. In the hands of a new entrant or non-dominant incumbent, such a diversion is more likely.

32. In the event that the Port-Alfred Mill is acquired by a new entrant, this will restore the four-firm concentration ratio to its pre-merger level. Prior to the merger, the CR4 based on production capacity within the relevant market was as follows:

Firm	Market Share
ACI	27.9%

Firm	Market Share
Bowater	18.5%
Donohue	18%
Kruger	12.2%
CR4	**76.6%**

33. Following the merger, the CR4 is as follows:

Firm	Market Share
ACI-Donohue	45.9%
Bowater	18.5%
Kruger	12.2%
Daishowa	4.9%
CR4	**81.5%**

34. Following the divestiture of the Port-Alfred Mill to a new entrant purchaser, the CR4 will be as follows:

Firm	Market Share
ACI-Donohue	40.9%
Bowater	18.5%

Firm	Market Share
Kruger	12.2%
Purchaser	5.0%
CR4	**76.6%**

35. As noted in the Statement of Grounds and Material Facts, a key pre-condition to effective interdependence is concentration among suppliers within the Relevant Market. By reducing concentration within the Relevant Market through divestiture of the Port-Alfred Mill, the DCO reduces the likelihood that interdependence will be effectively acted upon by remaining suppliers within the Relevant Market. This is true whether the purchaser is a new entrant or one of the smaller incumbents (with the exception of Bowater). In either case, the likelihood of effective interdependence will be substantially reduced as a result of the reduction of ACI's post-merger market share.

36. Regardless of whether the purchaser is an incumbent producer or new entrant, the capacity obtained through the acquisition of the Port-Alfred Mill could be supplied into the Relevant Market to constrain a significant price increase by the merged entity. Given the proximity of the Port-Alfred Mill to the Relevant Market, the purchaser will have an incentive to supply newsprint into this market. As noted in the Statement of Grounds and Material Facts, newsprint producers have a cost advantage in respect of customers located in close proximity to their mills due to, *inter alia*, the decreased transportation costs and because some customers require just-in-time delivery of newsprint.

37. Under the DCO, ACI will be required to use its reasonable commercial efforts to transfer existing customers to the purchaser. The transfer of customers from ACI to the

purchaser will allow the purchaser to establish relationships with certain existing customers of the Port-Alfred Mill and ensure that a portion of the capacity of the Port-Alfred Mill be used for any current customers of the Mill which may be located in Eastern Canada.

38. The provision in the DCO requiring ACI to continue to supply wood fibre to the purchaser following the acquisition of the Port-Alfred Mill at no less than the same levels for the 2000 calendar year, subject to third party approval where required, and if desired, for a long-term, will ensure that the purchaser continues to receive the supply of fibre necessary for the operation of the Mill at fair market value and in sufficient quantities.

39. For all of the above reasons, the divestiture of the Port-Alfred Mill, with the accompanying supply obligations, reduces the likelihood that interdependence will be effectively acted upon by remaining suppliers within the Relevant Market and therefore, eliminates the likelihood of any substantial prevention or lessening of competition in respect of the supply of newsprint in the Relevant Market as a consequence of the Merger.

V. <u>ALTERNATIVE TO SETTLEMENT</u>

40. The alternative to the settlement proposed through the DCO would be to proceed with a fully contested hearing of the Commissioner's challenge to the Merger as it relates to the supply of newsprint in Eastern Canada. The Commissioner has accepted the DCO for three reasons: first, the proposed divestiture of the Port-Alfred Mill will, in the Commissioner's view, avoid the likelihood of a substantial prevention or lessening of

competition arising from the Merger; second, the DCO provides a more timely and certain outcome for Eastern Canadian newsprint customers than litigated proceedings; and third, the DCO provides a more timely and certain outcome for ACI, and allows it to proceed with the remainder of the Merger and thereby obtain whatever synergies may arise from the Merger.

VI. CONCLUSION

41. For the reasons set forth above, the Commissioner recommends the settlement found in the DCO and respectfully requests that the Tribunal approve the DCO.

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CONSENT ORDER IMPACT STATEMENT

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