Competition Act Mergers

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Maintained

This practice note discusses the Competition Bureau's Merger Enforcement Guidelines, the application of the substantial lessening or prevention of competition ("SLPC") test and possible remedies to contested mergers. It then looks at how to determine whether a proposed transaction is subject to pre-merger notification and review by the Competition Bureau pursuant to Part IX of the *Competition Act*, R.S.C. 1985, c. C-34. Specifically, the practice note identifies the types of transactions that may be subject to pre-merger notification, the pre-merger notification thresholds and how to determine the value and location of an entity's assets and revenues. Finally, this practice note discusses the timing issues triggered by a pre-merger notification under the *Competition Act* and the subsequent issuance by the Competition Bureau of a Supplemental Information Request ("SIR").

For more information on Supplemental Information Request, see Supplementary Information Request Response Checklist. For sample timelines for non-complex and complex transactions, see flowcharts: Non-Complex Transaction Merger Review Timeline (No Supplemental Information Request), Complex Transaction Merger Review Timeline (No Supplemental Information Request) and Complex Transaction Merger Review Timeline (With Supplemental Information Request).

Merger Enforcement Guidelines

The Competition Bureau: Merger Enforcement Guidelines ("MEGs") are a guidance document issued by the Competition Bureau ("Bureau") intended to provide general direction on how the Bureau will approach its analysis of merger transactions. It is an important document to reference when considering the application of the merger review provisions of the *Competition Act*, R.S.C. 1985, c. C-34 to a proposed merger and when determining what information should be provided to the Bureau to assist in its review. Topics covered in the MEGs include:

- definition of merger;
- the anti-competitive threshold;
- analytical framework;
- market definition;
- market shares and concentration;
- anti-competitive effects;
- entry;
- countervailing power;
- monopsony power;
- minority interest transactions and interlocking directorates;
- non-horizontal mergers;

- the efficiency exception; and
- failing firms and exiting assets.

The MEGs are used by the Bureau to guide its review; however, it is important to note that the MEGs are not applied rigidly and are not legally binding. In the context of certain mergers that involve big data and/or multi-sided platforms for instance, the Bureau has commented that while the traditional analytical framework will continue to apply, specific methods should not be applied rigidly. See the Bureau's report: Big Data and Innovation: Key Themes for Competition Policy in Canada (February 19, 2018).

Substantial Lessening or Prevention of Competition ("SLPC") Test

Under s. 92(1) of the *Competition Act*, the Competition Tribunal (the "Tribunal") may make a remedial order where it "finds that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially".

In assessing the likelihood of an SLPC, the Bureau's focus is on whether the merger is likely to create, maintain or enhance the ability of the merged firm to exercise market power. Although the analysis is typically focused on price, non-price effects such as a decrease in quality are also considered. The Bureau will consider both downstream and upstream effects. For example, in May 2022, the Bureau filed an application with the Tribunal seeking an order to block Rogers' proposed acquisition of Shaw and noted that the application was filed in an effort to protect Canadians from both higher prices and non-price effects such as "poorer service quality and fewer consumer choices".

The Bureau uses two broad theories of competitive harm in its analysis of competitive effects:

- **Unilateral effects.** Will the merged entity be able to profitably maintain prices above the pre-merger level for a significant period of time post-merger or will current or new competitors be likely, timely and sufficient to prevent this?
- **Coordinated effects.** Will the merger result in an increased likelihood of collusion, or a decrease in competitive vigour, among firms in the market such that higher post-merger prices are profitably sustained for a significant period of time?

In conducting its review, the Bureau's analysis generally involves four steps: (1) defining the market; (2) calculating market shares; (3) assessing competitive effects; and (4) assessing efficiencies.

Defining the Market

The Bureau defines both a relevant geographic and product market. In making its definition, the Bureau uses the hypothetical monopolist test: the smallest group of products and the smallest geographic area in which a hypothetical monopolist would impose and sustain a significant, typically 5%, and a non-transitory, typically 1 year, price increase above levels that would likely exist in absence of the merger. In practice, the Bureau will look at the following factors:

- set-up costs;
- transportation costs;
- substitution;
- switching costs;
- end use;
- price relationships;
- price levels; and
- industry views and behavior.

Calculating Market Shares

The *Competition Act* provides that market shares cannot be treated as the determinative factor in finding that a merger results in an SLPC (*Competition Act*, s. 92(2)). However, the Bureau uses market shares as an indicator of whether a merger could result in a SLPC. A merger resulting in a post-merger share of under 35% will typically not be challenged based on unilateral effects. A merger resulting in the four largest remaining firms having a market share of less than 65% or a merged entity having less than a 10% market share will typically not be challenged based on coordinated effects. Note that the Bureau focuses less on coordinated than unilateral effects.

Assessing Competitive Effects

The evaluative factors used in the Bureau's analysis of competitive effects (unilateral and coordinated) are set out in s. 93 of the *Competition Act*. The factors include:

- the extent to which foreign products or foreign competitors provide competitive discipline;
- whether the business being acquired is failing;
- the extent to which acceptable substitutes exist;
- any barriers to entry;
- the extent to which effective competition remains;
- whether a vigorous and effective competitor will be removed;
- the nature and extent of change and innovation;
- network effects within the market;
- whether the merger or proposed merger would contribute to the entrenchment of the market position of leading incumbents;
- the effect of the merger or proposed merger on price or non-price competition, including quality, choice or consumer privacy; and
- any other factor that is relevant to competition in a market that is or would be affected by the merger or proposed merger.

Note that the Bureau will be influenced by the level and degree of complaints from customers, suppliers and competitors.

Assessing Efficiencies

The *Competition Act* provides an efficiencies defence that provides that the Tribunal shall not make an order under s. 92 if the gains in efficiencies resulting from the merger will be greater than and will offset the effects of any SLPC (*Competition Act*, s. 96). To use this defence successfully, parties must establish that resulting efficiencies are likely to occur, are greater than and offset the anti-competitive effect, and would not likely be attained if a s. 92 order were made.

Remedies

In situations where the Bureau takes the view that a merger will result in a SLPC it can take remedial action to cure such effects. Upon reaching agreement on appropriate remedies, the *Competition Act* allows for a consent agreement to be filed with the Tribunal (*Competition Act*, s. 105(3)). Once registered, the consent agreement has the same force and effect as if it were a Tribunal order (*Competition Act*, s. 105(2)).

Typically, remedies are classified as either structural or behavioural in nature. Structural remedies are generally one-off remedies intended to restore the competitive structure of the market. The most common example is the divestiture of part of the business. Structural remedies are immediate and once instituted require little to no

monitoring. Alternatively, behavioural remedies are ongoing, designed to modify or constrain the behaviour of the newly merged entity on a continual basis. The Bureau has been known to use a combination of both structural and behavioral remedies interchangeably in various transactions. They have also, at times, used quasi-structural remedies. The merger remedies are classified as follows:

Structural

Typically, a structural remedy addresses the anti-competitive effects arising from a merger by directly intervening in the competitive structure of the market. As stated, divestitures are the most common form of structural remedy. Divestitures can include one (or more) standalone operating business(es) and one (or more) components of a standalone business(es).

Quasi-Structural

In some situations, the Bureau may require the merging party to take some action, either in addition to, or as an alternative to a divestiture. A quasi-structural remedy does not necessarily disturb the newly merged entity's ownership of any particular asset; however, such remedies are designed to change the structure of the marketplace. Examples of this type of remedy include the granting of access rights to networks, the removal of anti-competitive contract terms or the licensing of intellectual property.

Behavioral

A behavioral remedy is intended to address anti-competitive harm arising from a merger by modifying or constraining the behavior of the merged firm. A common behavioral remedy would be a code of conduct, which may incorporate price and service controls, or require the merged firm to implement firewalls preventing information sharing among business units.

Combination

A combination remedy refers to a structural divestiture combined with other remedial relief that is behavioral in nature. Examples of behavioral remedies that may be used to support structural remedies include:

- a short term supply arrangement to help the buyer or licensee train employees;
- a waiver by the merged entity of restrictive contract terms that lock in customers for longer periods of times; or
- codes of conduct that can be monitored and expeditiously enforced by third parties.

Interim Orders

Where the Bureau brings a s. 92 application, the Bureau may also apply to the Tribunal for an interim order (s. 104(1)). Once made, the order may be on such terms and may last for any period that the Tribunal considers necessary to meet the needs of the case (s. 104(2)). This was confirmed in February 2022, when the Federal Court of Appeal held that the Tribunal has jurisdiction to grant an injunction pending a decision on application under s. 92, and, in urgent circumstances, to temporarily block a merger pending a decision on whether to grant an injunction.

Transactions Subject to Notification

Notifiable transactions are subject to an initial waiting period of 30 days, during which, the parties to the proposed transaction are prohibited from closing, unless an advance ruling certificate ("ARC") or No Action Letter are obtained from the Commissioner of Competition (the "Commissioner") and the waiting period is terminated early or waived. An ARC indicates that the Commissioner does not have grounds on which to challenge the proposed transaction. During the waiting period, the Commissioner reviews the proposed transaction to determine whether it will result in an SLPC in any market.

Penalties for closing a notifiable transaction prior to the expiration of the applicable waiting period (unless terminated early or waived) include:

- the dissolution of the transaction;
- an administrative monetary penalty of up to $10,000 per day; and/or
- criminal liability for the officers and directors of the non-compliant corporation.

Types of Transactions That May Be Subject to Pre-Merger Notification

As a threshold issue, pre-merger notification is only required for the following types of transactions:

- an acquisition of assets;
- an acquisition of the voting shares of a corporation;
- an amalgamation of two or more corporations; and
- the establishment or acquisition of an interest in a combination carrying on business otherwise than through a corporation (*e.g.*, a partnership).

Although other types of transactions are not subject to pre-merger notification, they could still be subject to a remedial order in the event that the Competition Tribunal finds that the transaction is likely to result in an SLPC.

Exempt Classes of Transactions

The *Competition Act* also exempts certain classes of transactions from the notification and review provisions of the *Competition Act*, including the following:

- combinations that are non-corporate joint ventures whose governing agreements satisfy certain requirements; non-corporate joint ventures are exempted from the obligation to notify where three requirements are met:

  (1) the parties are party to a written agreement (or an agreement intended to be put in writing) that imposes on one or more of them the obligation to contribute assets and governs a continuing relationship between the parties;

  (2) no change of control over any party would result; and

  (3) the agreement restricts the range of activities to be carried on by the joint venture, and contains provisions allowing for its orderly termination;
- acquisitions of real property or goods in the ordinary course of business (provided that the purchaser is not acquiring all or substantially all of the assets of a business or an operating segment of a business);
- an acquisition of voting shares or interest in a combination solely for the purposes of underwriting the shares or interest;
- an acquisition of voting shares, interest in a combination, or assets that results from a gift, intestate succession, or testamentary disposition;
- an acquisition of collateral or receivables, or an acquisition resulting from a foreclosure or default or forming part of a debt-workout, by a creditor in or pursuant to a credit transaction entered into in good faith in the ordinary course of business;
- an acquisition of a Canadian resource property or voting shares in a corporation, pursuant to a written agreement, if the purchaser incurs expenses to carry out exploration or development activities on the resource property;

- transactions that all the parties to which are affiliates (affiliation is defined as a greater than 50% shareholding interest at either the subsidiary or parent level) of each other; and
- mergers of financial institutions that have been certified by the Minister of Finance as being in the public interest.

However, if a transaction or proposed transaction is designed in a manner to avoid the notifiable transaction provisions set out in Part IX, then the relevant notification and review provisions (ss. 114 to 123.1) will still apply to the substance of the transaction.

The Thresholds

If a proposed transaction is of a type that may be notifiable and not subject to any exemptions, it must be notified to the Competition Bureau (the "Bureau") in advance of its completion if two thresholds are exceeded:

- the size of parties threshold; and
- the size of transaction threshold.

Size of Parties

The size of parties' threshold is exceeded where the parties to the proposed transaction (in the case of an acquisition of shares, this includes the target corporation), collectively with their affiliates, have:

- assets in Canada; or
- gross annual revenues from sales in, from or into Canada that exceed $400 million.

Size of Transaction

The application of the size of transaction threshold depends on the type of transaction, as outlined further below. This threshold is adjusted annually.

Asset Acquisitions

Where the proposed transaction is an acquisition of the assets of an operating business (an operating business is a business undertaking in Canada to which employees employed in connection with the undertaking ordinarily work), the size of the transaction threshold will be exceeded where:

- the value of the assets in Canada being acquired; or
- the gross annual revenues from sales in or from Canada generated from those assets, exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually).

Share Acquisitions

Where the proposed transaction is an acquisition of voting shares of a corporation, the size of transaction threshold will be exceeded where the following requirements are met:

- the corporation being acquired (the "Target") carries on an operating business (either directly or indirectly);
- the aggregate value of the assets (excluding assets that are shares) in Canada owned by the Target (directly or indirectly), or the gross annual revenues from sales in or from Canada generated from those assets, exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually); and
- as a result of the proposed transaction, the purchaser or purchasers (together with their affiliates) will hold more than:
    - 20% of its voting shares if the Target is a public corporation;

- 35% of its voting shares if the Target is a private corporation; or
- 50% of the Target's voting shares if the applicable threshold is already exceeded before the transaction.

Amalgamation of Corporations

Where the proposed transaction is an amalgamation of two or more corporations, the size of transaction threshold will be exceeded where the following requirements are met:

- at least one of the amalgamating corporations carries on an operating business (either directly or indirectly);
- the aggregate value of the assets (excluding assets that are shares) in Canada owned by the amalgamated corporation (directly or indirectly), or the gross revenues from sales in or from Canada generated from those assets, exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually); and
- each of two or more of the amalgamating corporations, together with their affiliates, have assets in Canada or gross revenues from sales in, from or into Canada, that exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually).

Establishment of Combination

Where the proposed transaction is a proposed combination of two persons to carry on business otherwise than through a combination (*e.g.*, a partnership), the size of transaction threshold will be exceeded where the aggregate value of the assets in Canada that are the subject matter of the combination, or the gross revenues from sales in or from Canada generated from those assets, exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually).

Acquisition of Combination

Where the proposed transaction is the acquisition of an interest in a combination carried on otherwise than through a corporation, the size of transaction threshold will be exceeded where the following requirements are met:

- the combination carries on an operating business;
- the aggregate value of the assets in Canada, or the gross revenues from sales in or from Canada generated from those assets, exceed $93 million (**note**: this 2023 figure remains unchanged from 2022, and is adjusted annually); and
- as a result of the proposed transaction, the purchaser or purchasers (together with their affiliates) will hold:
  - an aggregate interest in the combination entitling them to more than 35% of the profits or assets (on dissolution); or
  - if this threshold is already exceeded before the transaction, an aggregate interest entitling them to more than 50% of the profits or assets (on dissolution).

Determining Values of Assets and Revenues

The value of assets and revenues of an entity are to be determined as of the last day of the period covered by its *most recent audited financial statements* in which those assets and revenues are accounted for, subject to certain timing rules set out in the regulations to the *Competition Act*.

Under the *Competition Act*, asset values are to be determined by book value (*not* fair market value or acquisition price), and the following amounts are to be deducted:

- amounts representing duplication arising from transactions between affiliates;

- amounts representing duplication arising from an ownership interest of one person in another person, whether or not those persons are affiliated; and
- amounts provided for depreciation or diminution of value.

Gross revenues from sales of a person for an annual period are to be determined by aggregating (for that period) the:

- amounts accruing from the sale or lease of goods, other than amounts that are not properly included in revenue in accordance with Generally Accepted Accounting Principles ("GAAP"); and
- amounts accruing from the rendering of services, without deducting any expenses or other amounts incurred or provided for in relation to the sale or lease of goods or the rendering of services.

In determining the gross revenues from sales, any amount representing duplication arising from transactions between affiliates is to be deducted.

If the aggregate value of assets in Canada or gross revenues from sales in or from Canada cannot reasonably be determined from audited financial statements, the value can be derived from internal records (*i.e.*, working papers). If this is necessary, the asset value must be determined as of the most recent date that the amount can reasonably be determined, subject to certain timing rules set out in the regulations to the *Competition Act*.

Determining the Location of Assets and Revenues

The Bureau has provided some draft guidance on how to determine whether assets and revenues are in Canada (see: Competition Bureau: Pre-Merger Notification Interpretation Guideline Number 15: Assets in Canada and Gross Revenues From Sales in, from or into Canada (Sections 109 and 110 of the Act)). It is important to note that these guidelines have not been finalized, and in any event, are not binding on the Bureau. This section discusses the Bureau's guidance respecting the determination of assets in Canada and gross revenues from sales in or from Canada generated from those assets. For more information about the meaning of revenues from sales "in, from or into" Canada for the purposes of the size of parties threshold, contact external competition counsel.

Assets "in" Canada

The Bureau has indicated that it considers all assets on the audited financial statements of entities incorporated in Canada (or otherwise formed pursuant to a Canadian statute) to be located "*in*" Canada, subject to the following:

- immovable tangible assets (*e.g.*, buildings or land) located outside Canada are not assets "in" Canada;
- moveable tangible assets (*e.g.*, inventory, equipment) are not assets "in" Canada if they were physically located outside Canada throughout the entire relevant fiscal period (where moveable tangible assets of a foreign entity are physically located in Canada at any time during the relevant fiscal period, parties must determine what proportion of the value of that asset is attributable to Canada, and include that amount in calculating the value of assets in Canada);
- intangible assets with rights and privileges conferred by a foreign statute (*e.g.*, copyrights, patents, trade-marks, and financial assets such as shares of a foreign-incorporated company) are not assets "in" Canada (where a group of such assets are registered in multiple jurisdictions, including Canada, and have a single value on the audited financial statements, parties must determine what proportion of that value is attributable to Canada and include it in calculating the total value of assets in Canada), whereas intangible assets that are private/contractual (i.e., not conferred by statute, such as loans or receivables) are assets in Canada; and
- the goodwill of a Canadian entity is typically considered to be an asset in Canada unless it can be demonstrated that goodwill was generated by an event occurring outside Canada.

Sales in or from Canada Generated from Assets "in" Canada

The Bureau has indicated that when calculating gross revenues for the purposes of the size of transaction threshold, only gross revenues from sales generated from those assets "in" Canada are relevant. The Bureau considers revenues to be generated from assets in Canada if *any* of the revenue-generating assets of the target business are located in Canada. Revenue-generating assets include assets that contribute in any way and at any stage (*e.g.*, manufacture, sale) to the sale of the asset.

Merger Review Timeline

This part discusses the timing issues triggered by a pre-merger notification under the *Competition Act* and the subsequent issuance by the Bureau of an Supplemental Information Request ("SIR"). Below are the key points:

- The filing of a complete pre-merger notification triggers a 30-day waiting period during which the parties are prohibited from closing the proposed transaction (the "Initial Waiting Period"). During this period, the Bureau typically makes informal requests for additional information from the parties. Although voluntary, responses to the requests may minimize the need for a SIR.
- Generally, within 5 days following the receipt of a complete notification (see Competition Act Notification Form), the Bureau will designate the transaction as either non-complex or complex. Each designation corresponds with a service standard period, within which the Bureau will endeavour to complete its review. The service standard period for non-complex transactions is 14 days. The service standard period for complex transactions (where no SIR is issued) is 45 days.
- Where the Bureau completes its review prior to the expiry of the Initial Waiting Period, it may waive the remainder of the period by issuing an ARC or by notifying the parties that the Commissioner does not intend, at that time, to make an application to the Tribunal for a remedial order on the grounds that the transaction is likely to prevent or lessen competition substantially ("No Action Letter"). Upon the issuance of an ARC or No Action Letter, the parties are permitted to close the transaction.
- If, on the other hand, the Bureau becomes concerned during the Initial Waiting Period that the transaction may result in a substantial lessening or preventing of competition, they may issue a SIR, which contains requests for records and information and triggers an additional 30-day waiting period commencing when the Commissioner has received a complete response to the SIR (the "Second Waiting Period"). Where a transaction is designated as complex and a SIR is issued, the service standard period expires on the same day that the Second Waiting Period ends.
- Where the Bureau has not completed its review before the expiry of the Initial Waiting Period, but decides not to issue a SIR, it may proceed with its review and enter into a Timing Agreement with the parties. Under Timing Agreements, parties often commit to producing additional information to the Bureau and to delay the closing of the transaction until a specified date.
- Where the Bureau has made a written request for additional information after the commencement of a service standard period, the Bureau may pause the service standard period if the requested information is not received in 3 days for non-complex transactions, and 5 days for complex transactions, from the date the request was made. The Bureau will notify the parties in writing when the service standard period has been paused and when it has been resumed, and provide a new end date for the service standard.
- In very rare cases, the Bureau may need additional time to complete the investigation following the expiry of the Second Waiting Period. In such cases, the Commissioner may apply to the Tribunal for a 30-day injunction prohibiting the parties from closing the transaction. The Tribunal must be satisfied that allowing the transaction to close would impair its ability to dissolve the merger at a later date. An injunction may be extended by an additional 30 days.

For an estimated timeline respecting the Initial Waiting Period and Second Waiting Period following the issuance of a SIR, see flowchart: Complex Transaction Merger Review Timeline (With Supplemental Information Request).

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