Agenda and Subcommittee Reports Inside

# Deal Points

THE NEWSLETTER OF THE MERGERS AND ACQUISITIONS COMMITTEE


Michael O'Bryan
CHAIR

Rita-Anne O'Neill
VICE-CHAIR

Jessica C. Pearlman
VICE-CHAIR

Patricia O. Vella
VICE-CHAIR

Byron F. Egan
EXECUTIVE-CHAIR

Luciana Griebel
EDITOR

Janine Labusch
ASSISTANT EDITOR


**VOLUME XXIX** Issue 1, Winter 2024

# Antitrust Issues in Canadian Private Equity

By **TONY DI DOMENICO**, Partner; **CAITLIN ROSE**, Partner; **GRANT MCGLAUGHLIN**, Partner; **KAREEN ZIMMER**, Partner, and **PAUL BLYSCHAK**, Counsel, FASKEN

## Overview

Antitrust considerations are increasingly top of mind for U.S. private equity ("**PE**") firms. In September 2023, the Federal Trade Commission ("**FTC**") filed suit against a Texas PE firm alleging violations of antitrust laws associated with the firm's "*roll-up*" acquisition of multiple anesthesiology practices. In June 2023, the FTC announced expanded merger control notifications under the *Hart-Scott-Rodino Act*, including regarding minority investors, board observers and officer and director relationships. More recently, in November 2023, the Department of Justice ("**DOJ**") announced yet another investigation of a significant PE player for potential prohibited interlocking directorates among competing companies.

**Given the frequent investment by U.S. sponsors into Canada, it is prudent to query whether a similar increase in regulatory scrutiny of PE is occurring North of the border. The short answer is yes...**

Given the frequent investment by U.S. sponsors into Canada, it is prudent to query whether a similar increase in regulatory scrutiny of PE is occurring North of the border. The short answer is yes, and several examples are illustrative of this. We review these precedents for the benefit of U.S. PE considering a Canadian acquisition or minority investment. We also consider certain differences between U.S. and Canadian antitrust law, as well as the practical impacts greater regulatory oversight of PE by Canadian competition authorities is having on risk mitigation and deal dynamics.

## Canadian PE Given Express Notice

As U.S. lawyers know well, the increased scrutiny by antitrust regulators of PE over recent years has been punctuated by several much-publicized "*you've been put on notice*" comments by both the FTC and DOJ.

A similar forewarning was delivered by Canada's Commissioner of Competition in October 2023. Specifically, speaking at the Canadian Bar Association's Competition Law Conference, he cautioned:

> *"On the emerging issues front, we see clearly what's happening in terms of evolving business practices. We are wise to the risks of creeping acquisitions—including private equity roll-up strategies—and the harm they may pose to competition. We will also continue scrutinizing the conduct of gatekeeper platforms and we'll take appropriate action if it harms competition."*

This statement is only the latest and most overt instance of PE being in the cross-hairs of Canadian competition authorities.

## Post-Closing Unwinding of PE Acquisitions

An early example of Canadian competition authorities focusing on a PE acquisition is Thoma Bravo's 2019 purchase of an Alberta-based company that sold reserve reporting software to energy producers. Thoma Bravo already controlled several software companies,

CONTINUE READING ON PAGE 36

committee requires its own impartial financial and legal advisor to assist with a fairness opinion to assess transaction terms. This assists in demonstrating the board met its fiduciary duties when approving the transaction.

### 3. Litigation Risk

Litigation risks in going-private deals, especially from minority holders challenging fairness or fiduciary breaches, underscore the need for transparent processes and conflict prevention. An independent director special committee, even if not mandated, offers protection against conflicts of interest and threats from minority security holders for misrepresentations or inadequate disclosure.

### 4. Enhanced Disclosure Obligations

Depending on the transaction, MI 61-101 may impose additional disclosure obligations. For instance, related-party take-over bids must include: (i) prior two-year valuations of the target company; (ii) relevant past offers in the two years before the deal; (iii) target board and special committee review process; (iv) relied-upon exemptions from MI 61-101 valuation rules; (v) any material disagreement between the target company's board and the special committee; (vi) the number of votes that will be excluded to determine whether minority approval is obtained; and (vii) the identity of security holders who are excluded from the minority approval vote and their individual holdings.

### 5. Regulatory Matters

Foreign strategic buyers must navigate the Investment Canada Act (the "**ICA**") and its regulations on foreign investments. The ICA aims to ensure that non-Canadian investments contribute to Canadian economic growth and employment. When a foreign buyer gains control of a Canadian target, it may trigger an ICA notification or review requirement. Notifications, simpler and less costly than reviews, require the foreign buyer to submit basic transaction details within thirty days of closing. If a foreign buyer's acquisition meets financial thresholds and faces ICA review, they must prove to the Minister of Innovation, Science, and Economic Development that the investment benefits Canada. This assessment considers: (i) the impact on economic activity; (ii) the degree of Canadian involvement; (iii) the effects on productivity, technology, and innovation; (iv) the influence on industry competition; (v) policy alignment; and (vi) enhancement of Canada's global competitiveness.

## Conclusion

Going-private transactions restore operational flexibility by minimizing exposure to market volatility and regulatory constraints, but challenges persist. Foreign buyers, including PE funds, must select optimal structures carefully and manage many aspects of the transaction, including exclusivity concerns, conflicts of interest, litigation risk, disclosure, and regulatory considerations. The parties must weigh potential value creation against the complexities of transitioning to a private entity. Optimal planning and execution are crucial to harnessing the full potential of these transactions.



CONTINUED FROM PAGE 8

including a major Canadian competitor of the target; however, the Competition Bureau (the "**Bureau**") was not notified in advance of closing given the size of the transaction was below notifiable thresholds. Following closing, the Bureau sought to unwind the transaction by application to Canada's Competition Tribunal, alleging that because both the target and the competitor sold reserve reporting software specifically tailored for Canadian producers, competition from international energy service companies was insufficient to prevent a substantial lessening of competition in the domestic market.

The litigation was settled by a Consent Agreement before the Competition Tribunal, and was noteworthy in several respects. First, Thoma Bravo agreed to divest the target wholesale, rather than any subset of the target's assets acquired through the transaction. Second, the Bureau's challenge of a non-notifiable transaction[1]

[1] Transactions in Canada are subject to pre-merger notification if they meet a party-size threshold, transaction-size threshold and shareholding threshold.

reinforced its indications from earlier in 2019 that it intended to dedicate additional resources to identifying non-notifiable transactions that may nonetheless pose competition concerns. Third, the Bureau's ability (and willingness) to seek to unwind an acquisition post-closing confirmed that only minimal comfort can be taken by the absence of a pre-merger competition challenge. Indeed, anticipated upcoming amendments to Canada's competition laws are expected to increase the limitation period for non-notified mergers from one year to three years, giving the Bureau up to three years post-closing to challenge non-notifiable transactions.

### Preferred Divestiture Buyers No Longer?

Similar to the U.S., the Bureau's stance regarding PE as potential divestiture buyers has seen a markedly interventionist shift over recent years. Whereas PE funds were previously viewed as natural (or even preferred) buyers in merger-prompted divestitures, this is no longer necessarily the case. Rather, PE in Canada can now expect asset-specific, and PE-specific, interrogation in the merger divestiture context.

In 2022, the Bureau sought to block the acquisition of Canada's then-fourth largest wireless services provider (Shaw) by Canada's largest wireless services provider (Rogers). To address the Bureau's concerns, Rogers attempted a "fix-it-first" remedy. Specifically, and as noted in the judicial decision allowing the transaction to ultimately close, Rogers entered into Letters of Intent and Term Sheets with two investment firms for the divestiture of Shaw's subsidiary, Freedom Mobile ("**Freedom**").[2] However, Rogers abandoned these potential sales after the Commissioner expressed concerns regarding the planned buyers,[3] including that the "*proposed new owners*" were "*likely to provide less effective financial, managerial, technical or other support*" to Freedom's wireless operations.[4] The merger proceeded, but only after Rogers entered into an agreement with a strategic buyer to purchase Freedom on the logic that the strategic buyer was sufficiently resourced to ensure Freedom's continued competitiveness.[5]

However, the opposite result occurred after a 2022 acquisition by Domtar Corporation ("**Domtar**"), one of Canada's largest pulp and paper manufacturers. The Bureau identified competition issues related to feedstock supply, and to resolve the Bureau's concerns Domtar agreed to, post-closing, divest two pulp mills to two independent purchasers approved by the Commissioner. One of the purchasers was Atlas Holdings LLC ("**Atlas**"), a U.S. PE firm with existing pulp and paper mill operations. Among other things, Atlas was able to demonstrate to the Bureau that although it was a PE firm, it had successfully partnered with experienced leadership teams to acquire, strengthen and operate multiple pulp and paper businesses since its founding more than two decades previously, including several in Canada, establishing that Atlas would be able to maintain the divested pulp mills as competitors.

### Merger Reviews of Interlocking Directorates

Canada does not have the equivalent of *Clayton Act* section 8 prohibiting the same individual from serving simultaneously as an officer or director of two competing corporations. However, the possibility of interlocking directorates is expressly addressed in the Bureau's *Merger Enforcement Guidelines* and, similar to the U.S., regulator concerns include whether the interlocked directorate could result in less aggressive competition between the entities or increase the likelihood of the inappropriate sharing of competitive information among the entities. There are also precedents in Canada of the Bureau requiring the resignation of a director who would be interlocked as a result of a proposed merger.

One example occurred in 2005 amid the acquisition by Quebecor Media Inc. (a Quebec broadcasting, publishing and communications enterprise) of Sogides Ltée (then Quebec's largest publishing and distribution enterprise). The Bureau did not take issue with the merger itself. However, its review identified that the target's president both (1) owned an interest in a bookstore chain that competed with the acquirer's bookstores, and (2) sat on the competitor's board. The Bureau raised concerns that the president's respective roles

[2] See Rogers-Shaw - Reasons for Order and Order, 2022 CanLII 135198 (CT) at para. 22.
[3] See Rogers-Shaw - Reasons for Order and Order, 2022 CanLII 135198 (CT) at para. 22.
[4] See Notice of Application filed May 9, 2022 by the Commissioner of Competition in Commissioner of Competition v. Rogers Communications Inc. and Shaw Communications Inc. at para. 95(a).
[5] See Rogers-Shaw - Reasons for Order and Order, 2022 CanLII 135198 (CT) at paras. 1-6.

at the acquirer and its competitor could lead to anti-competitive exchanges of sensitive information. This led to a Consent Agreement among the acquirer, the target and the Bureau whereby the target's president resigned from the competitor's board and with an independent director assuming his place.

## Practical Takeaways for U.S. PE in Canada

What are the practical takeaways for U.S. PE considering a Canadian acquisition or minority investment?

Regarding risk mitigation, the age-old adage that "*an ounce of prevention is worth a pound of cure*" is apt. The starting point is appreciating that, as in the U.S., the Bureau's attitude toward PE has changed and can now carry unfounded but nonetheless negative assumptions regarding PE's business models, intentions and/or capabilities. Whether this is a temporary trend (*e.g.*, reflective of the priorities of current administrations) or of longer-term significance remains to be determined. However, so long as it persists, it should be anticipated and accounted for in transaction and transition planning.

> **"an ounce of prevention is worth a pound of cure"**

Antitrust counsel should be consulted early in transactions to evaluate potential competition risks of a PE-related nature. To minimize risks of regulatory interest and action, PE firms and their portfolio companies should also consider adopting competition-related best practices. For example, transaction documents (including Confidential Information Memoranda) should be prepared expecting they will be scrutinized by regulators. Ambiguous or inflammatory language that could be misconstrued as anti-competitive, such as "*stabilize the industry*," "*consolidate the industry*" or "*preclude competition*", should be avoided in such documentation. So too should foreshadowing future acquisitions (*e.g.*, potential "*roll-ups*") or referring to other deals currently under consideration (including to avoid confidentiality complications should the Bureau request further information regarding those deals). By contrast, PE funds should proactively look to include arguments and analyses that highlight the fund's and portfolio company's commitment to building a long-term and effective competitor.

Regarding the actual deal terms, M&A counsel should approach transaction strategy having specific regard for any PE and competition related risk identified by antitrust counsel. Examples include greater attention to and/or more bespoke drafting around (1) statutory waiting periods, (2) required regulatory approvals, (3) associated efforts undertakings, (4) the allocation of competition risk, (5) "*hell or high water*" clauses, (6) break fees and reverse break fees, and (7) applicable "*outside*" (or "*longstop*") dates. Deal dynamics may also be impacted, including consideration of who may constitute a preferred bidder in a competitive auction process.

Overall, PE in North America has entered a phase of heightened competition law scrutiny. By planning accordingly, PE firms can continue to pursue their acquisition strategies even in this more challenging antitrust environment. The task for U.S. and Canadian counsel is to demonstrate foresight, preparedness and coordination.

CONTINUED FROM PAGE 9

*"Fraud" of a party means the actual common law fraud (as determined pursuant to Delaware law) in the making of any representation or warranty set forth in Article [Seller Reps Reference] or Article [Purchaser Reps Reference], as applicable, or any certificate delivered by such party pursuant to Article [Conditions to Closing Reference]. The term "Fraud" shall not include any fraud claim based on constructive fraud, equitable fraud, negligent misrepresentation or omission or any similar theory.*

*"Willful Breach" means a material breach that is a consequence of an act or failure to act undertaken by the breaching party with actual knowledge that such party's act or failure to act would constitute a material breach of this Agreement.*