>perspective

Canadian Competition Bureau Clears RONA Acquisition But Requires Post-Merger Monitoring

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On August 14, 2006, the Canadian Competition Bureau released a "Technical Backgrounder" with respect to the acquisition by RONA Inc. ("RONA") of a 51% interest in the operating business of Matériaux Coupal Inc. ("Coupal"). RONA is a leading Canadian distributor and retailer of hardware, renovation and gardening products. Coupal operates retail outlets for lumber and building supplies in the Province of Quebec and also manufactures structural products, such as roof trusses and joints.

Although the Bureau had concerns with certain aspects of the acquisition, it did not seek to prevent the merger from closing. Instead, the Bureau imposed more active than usual post-merger monitoring requirements to track the merger's effects. Another unusual aspect of the Bureau's review process was its agreement to delay contacting industry participants to obtain their views about the acquisition. Market contacts are a key part of the Bureau's merger analysis and it is usually reluctant to limit its ability to speak to third parties about a transaction.

These aspects of the Bureau's review are discussed in more detail below.

The Bureau's Assessment

The Bureau focussed its analysis on the downstream market for retail sales of lumber and building materials to home building contractors and on the upstream market for the supply of these materials to retailers.

With respect to retail sales, the Bureau found that that a combined RONA/Coupal would have a post-merger market share of between 30%-35% in all but one of the areas of Québec in which Coupal retail outlets overlapped with RONA outlets. Based on the Bureau's *Merger Enforcement Guidelines*, market shares at this level are not usually sufficient to give rise to concerns. Moreover, the Bureau also found that there would be sufficient competition remaining in these markets to prevent RONA from exercising market power (i.e., between 2-4 remaining competitors).

The Bureau identified one market, however (the city of Granby), in which RONA/Coupal would account for approximately 50% of total retail sales of lumber and building materials to home building contractors. As well, there would be only one remaining competitor to the merged entity following the acquisition. In addition, many customers interviewed by the Bureau in Granby said that they feared that prices would rise due to a lack of competition resulting from the transaction.

Weighed against the foregoing, however, was the Bureau's finding that some competitors might consider expanding their businesses to Granby in the event of a post-merger price increase by RONA, despite what the Bureau found to be "moderate" barriers to entry (such as the need to make major investments in logistics; the time required to earn customer confidence; and excess capacity in the industry). These "indications of a real potential for expansion by competitors" were sufficient to "significantly reduce" the Bureau's concerns about the merger's possible impact, notwithstanding a market share of 50% and doubts about the effectiveness of existing competition.

On the upstream side, certain suppliers had expressed concerns about RONA's buying power post-merger. This, in turn, caused the Bureau to consider whether the acquisition would enable RONA to obtain preferential treatment from suppliers resulting in the exclusion of retail competitors. However, as with the retail market, the Bureau was not satisfied that these concerns were sufficiently crystallized to prevent the transaction from proceeding.

Post-Merger Monitoring

Although not sufficient to justify challenging RONA's acquisition, the Bureau decided that its lingering concerns about the merger's possible effects (particularly in the upstream supply market) meant that active post-merger monitoring would be necessary.

Under the *Competition Act*, the Bureau may challenge a merger within three years of completion (unless it has granted an "advance ruling certificate" which generally has the effect of precluding such a challenge). It is not unusual for the Bureau to decide to permit a merger to proceed while reserving its right to subsequently challenge the transaction within the three-year period allowed under the *Competition Act.* However, the Bureau does not typically accompany this with any form of monitoring mechanism. In this instance, however, the Bureau secured RONA's agreement to cooperate in providing the Bureau with the information required to track the competitive effects of the merger going forward.

Market Contacts

Another unusual aspect of the Bureau's review process was its agreement to delay market contacts for approximately five months after it was first advised by RONA about the merger. Market contacts are an important aspect of the Bureau's merger analysis (and, as seen above, ultimately proved to be a key element of the Bureau's analysis in this case as well). However, the Bureau was prepared in this instance to take what it characterized as the "exceptional" step of acquiescing to RONA's request, subject to an undertaking that RONA would not complete the merger without giving the Bureau six weeks advance notice. The Bureau eventually commenced its market contacts once the acquisition was made public.

It is apparent from subsequent consultations with the Canadian competition bar (although not in the specific context of the RONA merger), that the Bureau is keen to avoid parties routinely requesting limitations on market contacts. Representatives of the Bureau have asserted that they will not look favourably upon requests to refrain from making market contacts and that they will not agree to limits on their ability to speak to third parties except in "extraordinary circumstances". Parties should also be aware that any delays requested in the Bureau contacting market participants (e.g., until the transaction is made public) will trigger corresponding delays in receiving the Bureau's response with regard to their merger and in the closing of the transaction.

If you have any questions regarding the foregoing, please contact George Addy, John Bodrug or Mark Katz in the Toronto office (416.863.0900) and Hillel Rosen in the Montréal office (514.841.6400).

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