CANADA

Taxation

Canadian Merger Law and Interlocking Directorships/ Minority Shareholdings

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Competition Bureau Reviewing Its Policies

The Canadian Competition Bureau ("Bureau") is currently examining its policies regarding merger reviews that involve minority shareholdings and interlocking directorships. Although this review is not complete, the Bureau recently set out some of its developing views in a report prepared for the OECD.

Preliminary Observations

A few preliminary observations are in order.

First, the Competition Act does not contain any express provision dealing with interlocking directorships. This is different from the United States, where section 8 of the Clayton Act prohibits a person from serving as a director, or a board-appointed officer, of two or more competing corporations (subject to certain materiality thresholds). In Canada, for an interlocking directorship to be subject to independent merger review, it must qualify as a "merger" as defined in the Competition Act, i.e., it must be found to result in the "acquisition or establishment, direct or indirect, by one or more persons... of control over or significant interest in the whole or part of a business of a competitor, supplier, buyer or other person." For these purposes, a "significant interest" is defined by the Bureau as "the ability to materially influence the economic behaviour of the business". Interlocking directorships may also be reviewed if they are a feature of a larger transaction that otherwise qualifies as a "merger".

The antitrust treatment of interlocking directorships/minority shareholdings has become more of an issue with the growing prominence of acquisitions involving consortiums of private equity funds.

Similarly, there is no express provision dealing with the substantive review of minority shareholdings. Minority shareholdings are examined by the Bureau as either (i) ancillary to merger transactions or (ii) as "mergers" in and of themselves, if the minority shareholding provides the acquiror with the ability to materially influence the economic behaviour of the business (i.e., represents a "significant interest" in the business).

However, unlike interlocking directorships, there are express rules governing when the acquisition of a minority shareholding may trigger a pre-merger notification requirement under Part IX of the Competition Act. Thus, assuming the other applicable thresholds are met, an acquisition of more than 20% of the voting shares of a public company, or more than 35% of the voting shares of a private company, will be subject to notification.

Recent Cases

There have been several recent cases in which the Bureau has had to deal with the implications of interlocking directorships / minority shareholdings.

In the Sogides / Quebecor case, for example, Quebecor Media Inc. acquired the French-language publishing business of Sogides Ltée. The Bureau did not have any concerns with the acquisition itself. However, its investigation disclosed that Sogides' president - Pierre Lespérance - had an interest in a bookstore chain that competed with a Quebecor-owned chain. He also was a director of this competing chain. The Bureau raised concerns that there could be improper exchanges of information between Quebecor and the competing bookstore chain through Mr. Lespérance. Accordingly, the parties agreed that Lespérance would resign from his position on the competitor's board of directors and that an independent agent would take up his position instead.

In another instance, while examining the restructuring of the Loews Cineplex movie chains, the Bureau learned that Famous Players, Canada's largest film exhibitor, had acquired an interest in a Loews Cineplex subsidiary that specialized in operating movie theatres in smaller cities. Again, although the Loews Cineplex restructuring itself did not raise issues, the Bureau was uncomfortable with the relationship between Famous Players and the Loews Cineplex subsidiary. Following discussions with the Bureau, Famous Players agreed to divest its interest in the subsidiary, cease its representation on the subsidiary's board of directors, and terminate all ancillary agreements.

The Bureau's Key Conclusions to Date

As noted, the Bureau is currently in the process of reviewing its policies regarding interlocking directorships/minority shareholdings. In its OECD paper, the Bureau offers the following "preliminary" views:

1. The Bureau will assess three main considerations when examining the competitive implications of minority interests and interlocking directorships:

— the ability to materially influence the economic behavior of the business;

— the ability to obtain confidential information; and

— changes to incentives (or the profit maximizing function).

2. In making its assessment, the Bureau will investigate the following factors:

— any attached rights to minority interest shareholdings;

— the nature of competition in the relevant market;

— dividend share of the minority interest in comparison to the equity ownership share;

— any special powers, including voting or veto rights;

— any special agreements or arrangements that could constitute a "material influence";

— the composition of the board of directors;

— board meeting attendance and voting patterns;

— the role and duty of the "interlocked" director, including the type of information to which the director has access; and

— the practical extent to which the minority shareholder can exert pressure on the company's decision-making process (e.g., if it is the largest shareholder).

3. A so-called "passive" minority shareholding may be enough to trigger concerns, provided that it confers the ability to materially influence the economic behavior of the business.

4. The Bureau believes that structural remedies are "the most effective and preferred" remedy where interlocking directorships/minority shareholdings raise issues. According to the Bureau, behavioral remedies are especially difficult to monitor in this context (it is impossible to know what goes on in a private board meeting) and would not necessarily stop an "interlocked" director from influencing the business's decisions.

Conclusion

The antitrust treatment of interlocking directorships/minority shareholdings has become more of an issue with the growing prominence of acquisitions involving consortiums of private equity funds. In 2007, for example, the FTC challenged the acquisition of interests in Kinder Morgan, Inc. by private equity funds managed by The Carlyle Group and Riverstone Holdings LLC. The FTC objected to the fact that Carlyle and Riverstone also held interests in a competitor of KMI, along with the right to board representation, the right to exercise veto power over the competitor's activities and access to non-public competitively-sensitive information. It is apparent from the Bureau's prior enforcement steps, as well as its comments in the OECD paper, that similar circumstances and arrangements could give rise to issues in Canada as well.

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