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Update

Competition Law

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Application of Canadian Competition Law to Private Equity Bidding Consortiums

Recent media reports suggest that the Antitrust Division of the United States Department of Justice is investigating the potential application of the antitrust laws to circumstances where private equity firms have agreed to join forces in bidding for corporations. With these reports, the inevitable antitrust class action suit in the U.S. was launched seeking damages for allegedly driving down the price received by shareholders in these transactions by reducing the number of independent bidders.

It is common practice for selling firms to set up an auction process in the hopes of attracting multiple bidders. Private equity firms, on the other hand, often want to share risk by seeking partners when submitting bids. Such risk sharing can encourage bids that might not otherwise be made and in that sense it would be advantageous to the target firm's shareholders. However, where the number of bidders is naturally limited by economic or regulatory circumstances, such as Canadian ownership requirements, an agreement among the bidders may lower the price the shareholders might otherwise receive. Is such activity anti-competitive under Canadian competition law?

There are two sections of the Canadian Competition Act which require analysis, the general criminal conspiracy section and the criminal bid-rigging provision.

Application of the general criminal conspiracy section of the Competition Act is problematic in these circumstances. The agreement here relates to the acquisition of a particular company, not to any goods or services that would be consumed by intermediate or final customers. It does not have any anti-competitive effect in the way that term is normally used. Prices for goods or services are not artificially increased and output is not reduced below competitive levels. It is unlikely to unduly lessen competition in a general "market" for corporate control of companies as there are many such buying opportunities. Moreover, to the extent that there is some public benefit to controlling the circumstances under which companies are bought and sold, there is already extensive regulatory oversight, at least for public companies, under securities law.

Unlike the conspiracy section, the criminal bid-rigging provision of the Competition Act does not require evidence of anti-competitive effects. All that is necessary is that there be a bid submitted that is arrived at by agreement or arrangement between or among bidders in response to a call for tenders or bids. An agreement not to submit a bid is also illegal. As a result, the bid-rigging section could potentially be applied to an auction for the sale of a corporation, even if the public policy rationale for doing so is weak.[1] However, an agreement or arrangement between bidders is not illegal if the agreement or arrangement is disclosed to the person calling for the bids at or before the time when the bid is submitted.

If an auction is conducted as a two-stage process with the first round of bids being used to select a smaller group of potential purchasers and the second round consisting of individual company negotiations, the second round of negotiations may destroy the original bid process and any undisclosed agreement with respect to the original call for bids may not be subject to the bid rigging section.[2]

[1] Bid rigging under the Competition Act is a criminal offence that carries punishment of a fine in the discretion of the court or imprisonment for term not exceeding five years or both. Persons may also sue in civil court for the recovery of damages suffered as a result of criminal conduct under the Act, including bid rigging.

[2] R. v. York-Hanover Hotels Ltd. (1986), 9 C.P.R. (3d) 440 (Ont. Prov. Ct.)

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In cases where firms have a secret "understanding" that if one firm is successful it may subsequently sell a portion of its investment to another potential bidder, it should be clear that the parties are not cooperating with respect to the original bid process, for example by not bidding independently or by agreeing not to bid. The existence of such an understanding could by itself raise questions about the independence of the bidders and it would be useful to document that that was not the case.[3]

Conclusion

Private equity bidding consortiums or "club deals" are under scrutiny in the United States, although it is far too early to say whether any liability will be found. In Canada, though it is unlikely that such arrangements could be successfully attacked under the criminal conspiracy provisions of the Competition Act, liability under that Act's bid-rigging provision is a more realistic possibility. This update examines the possible application of the Canadian Competition Act to this issue.

If you would like to know more about this subject or any other aspect of competition law, please contact Richard Annan or Daniel Gormley or any other member of Goodmans' Competition Group.

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[3] Joint bidding or informal understandings may raise other issues, such as potential liability under the terms of a non-disclosure agreement between a bidder and seller which may prevent bidders from communicating or cooperating with one another with respect to bids.