Goodmans LLP Update

Competition, Antitrust and Foreign Investment

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Supreme Court Decision Underscores Importance of Quantifying Efficiency Gains in Merger Reviews

The Supreme Court of Canada has provided important guidance for determining whether a merger is likely to prevent competition substantially, and for the proper application of the "efficiencies defence" under section 96 of the *Competition Act* ("**Act**").

In *Tervita Corp. v. Canada* (Commissioner of Competition) ("***Tervita***"), issued January 22, 2015, the Court upheld the finding of the Competition Tribunal ("**Tribunal**") that a merger can be blocked based on a forward-looking analysis of whether, but for the merger, competition would likely be substantially greater. This "but for" analysis can consider a range of evidence and the analysis is not entirely dependent on the parties' assets, plans and businesses at the time of the merger.

However, the Court overturned the Tribunal and Federal Court of Appeal on the correct application of the efficiencies defence. Basing its decision on principles of transparency, objectivity and fairness, the majority of the Court held that where anti-competitive effects of a merger are capable of being quantified, the Commissioner of Competition (the "**Commissioner**") bears the burden of doing so, failing which they will be assessed at "zero." The Court held that the Tribunal should then balance this against evidence led by the merging parties of any efficiencies resulting from the transaction to determine whether these efficiencies are greater than, and offset, its anti-competitive effects.

The Supreme Court relied on relatively marginal efficiencies in this case to deny the Commissioner's application to dissolve the merger.

By insisting on the strict quantification of anti-competitive effects wherever possible, and confirming the absence of any threshold amount for efficiencies that can be weighed against these anti-competitive effects as a defence, *Tervita* underscores the importance for merging parties to identify any efficiencies generated by their proposed transaction and to support such in the merger review process.

Background

Tervita involved a relatively small transaction of C$6 million, far below the current pre-merger notification review threshold for transactions. In 2010, Tervita Corp., an environmental solutions company operating hazardous waste disposal landfills in Northeastern British Columbia, acquired a company that had obtained regulatory approval to open another landfill site in the region. The Commissioner sought to block the transaction after closing, and asked the Tribunal to order the transaction be dissolved or that Tervita Corp. divest the acquisition in whole or in part.

The Tribunal is empowered under section 92 of the Act to make remedial orders, such as merger dissolution or the divestiture of shares or assets, where a merger or proposed merger substantially prevents or lessens competition, or is likely to substantially prevent or lessen competition. However, parties to a merger can invoke the so-called "efficiencies defence" under section 96 of the Act, which prohibits an order being made under section 92 if the Tribunal finds that the

merger is likely to generate efficiencies that would be "greater than" and would "offset" the merger's anti-competitive effects.

Analysis

Under section 92 of the Act, the Court upheld the Tribunal and Federal Court of Appeal's analysis of whether, "but for the merger, the acquiring firm would have entered the relevant market independently, or through the acquisition and expansion of a smaller firm, a so-called 'toe-hold' entry." The Court's analysis was not restricted to what could be discerned from the merging parties' assets, plans and business at the time of the merger (e.g., the fact that the purchased landfill site was not yet operational). The Court's forward-looking consideration of whether the merger was likely to prevent competition, was supported by its finding that "but for" the merger, the vendor would have likely entered the relevant product market (i.e., transformed the purchased site to a secure landfill so as to compete with the acquiror).

Section 96 of the Act is relatively unique, in that it is an efficiencies defence explicitly written into Canada's competition statute. As noted by the Court, this codification of the efficiencies defence reflects Parliamentary recognition that "in some cases, consolidation is more beneficial than competition" to realize economies of scale and help Canadian businesses in a relatively small domestic market to compete in international markets. (The leading authority on the efficiencies defence remains the *Superior Propane* series of cases.)

In *Tervita* the Court clarified that the Commissioner has a legal burden "to quantify by estimation all quantifiable anti-competitive effects," and if the Commissioner fails to meet this burden, "the quantifiable anti-competitive effects should be fixed at zero." The Court also overturned the Federal Court of Appeal's conclusion that a "threshold level of efficiencies" exists under the section 96 defence, which would require more than marginal efficiency gains to defend against a finding of anti-competitiveness (the merging parties, however, still bear the onus of proving the remaining elements of the section 96 defence).

This does not mean that anti-competitive effects of a transaction can never be qualitative. As the Court observed, it requires the Commissioner to at least establish estimates of quantifiable anti-competitive effects to provide the merging parties with the case they have to meet.

Practically speaking, these clarifications to the balancing test under section 96 can mean that in a case like *Tervita,* where a merger is found to be likely to prevent or lessen competition substantially, but the Commissioner fails to meet his legal burden of quantifying its anti-competitive effects, the merger will nonetheless be permitted to proceed. In short, even marginal efficiency gains will outweigh anti-competitive effects set at zero.

Conclusion

For merging parties, *Tervita* underscores the importance of developing evidence of the efficiencies generated by their proposed transaction, particularly where the proposed transaction is likely to raise competition concerns and the parties may need to rely on the efficiencies defence in addition to other submissions relating to issues of competitive effects. It can be expected, however, that where the parties intend to rely on the efficiencies defence, the Commissioner and staff at the Competition Bureau may now demand considerable evidence and more time to review a proposed transaction in order to quantify the possible anti-competitive effects of the proposed transaction. It may, therefore, be premature to assess the decision's impact on merger reviews generally, although the decision does establish a clear new burden on the Commissioner in the merger review process and any ensuing litigation.

For further information regarding the Supreme Court's decision and its potential implications, please contact any member of our Competition, Antitrust and Foreign Investment Group.

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