Canadian Regulation of Big Tech: The Short and the Long Arm of the Law

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The Short and the Long Arm of the Law

COMPETITION ACT

INVESTMENT CANADA ACT

The Competition Act – Antitrust and Consumer Protection

- **The *Competition Act* ("Act") is a single statute that governs antitrust law in Canada.**
- **It also contains a number of consumer protection laws.**
- **Unlike in the US, there are no provincial (i.e. state) antitrust enforcers – all antitrust laws and enforcement are federal**
  - This is a major headache-saving distinction.

The Competition Act – Antitrust and Consumer Protection

- **The Act contains a number of provisions similar to those familiar under US antitrust and consumer protection law, including:**
  - Cartel provisions – criminal price-fixing
  - Prohibition on false and misleading representations related to the promotion of a product
  - Abuse of dominance – similar to monopolization in the US
  - Refusal to deal, tied selling, exclusive dealing
  - Resale price maintenance
  - Merger control

The Investment Canada Act – Two (or Three?) Foreign Investment Review Schemes in One

- **There are technically two separate foreign investment review schemes under the federal *Investment Canada Act* ("ICA")**
  - "Net Benefit Review" requires that acquisitions of control of businesses carried on in Canada that exceed certain thresholds be reviewed and found to be "likely of net benefit to Canada"
  - "National Security Review" allows any investment in Canada, whether controlling or not, to be reviewed to determine whether it could be injurious to national security
    - This is similar to the CFIUS process in the US
- **Additionally (scheme #3), acquisitions of control of "Cultural" businesses carried on in Canada – those involved in publishing, film, music or broadcasting – above certain (much lower) thresholds, are reviewed for whether they are "likely to be of net benefit to Canada" by a different government department (Canadian Heritage) using different standards**
- **More on these later…**

The Short Arm of the Law…

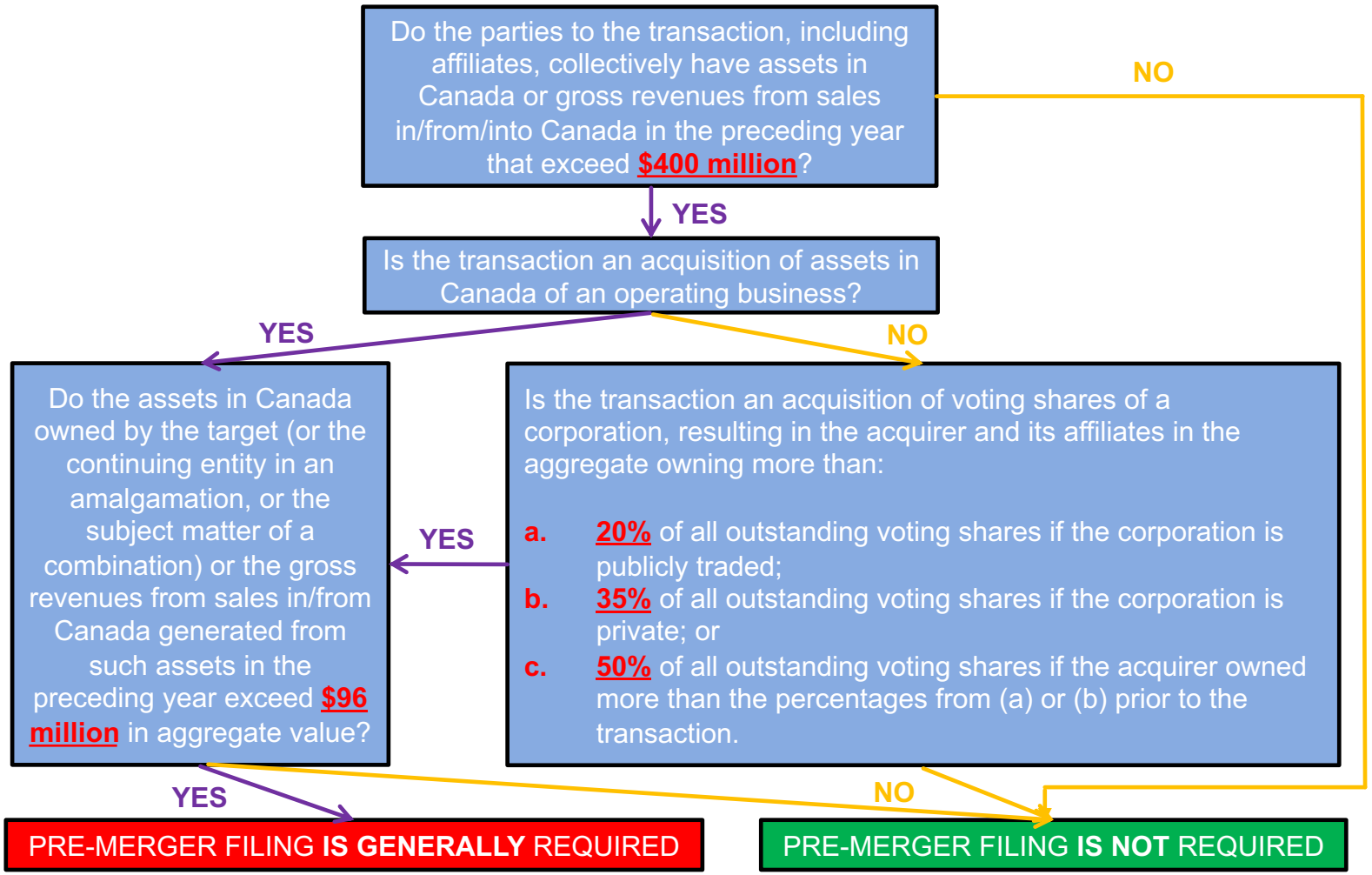
- **A number of tech-related antitrust cases have been filed in the US recently, brought by State AGs, the FTC and the DOJ**
- **The bases for these claims would support similar claims in Canada under the Act – particularly under these theories**
  - Merger control – including killer acquisitions
  - Abuse of dominance/monopolization
  - False and misleading representations

Count One – Unlawful Maintenance of Monopoly in the Personal Social Networking Services Market - Section 2 of the Sherman Act, 15 U.S.C. § 2

Canadian Merger Control – The Maple Version of HSR

- **The Act provides a two-stage merger review process similar to the US HSR process**
- **The waiting period for a notifiable merger (one which exceeds the thresholds) is 30 days, but can be extended by the issuance of a Supplementary Information Request ("SIR")**
  - A SIR is similar to a US second request, and if issued, the waiting period automatically extends to 30 days after both parties submit complete responses
- **Pre-merger notification is required where two thresholds are met. One threshold pertains to the size of transaction while the other considers the size of parties to the transaction.**
- **The Commissioner of Competition ("Commissioner"), who leads the Competition Bureau ("Bureau") has jurisdiction to challenge a merger (even if it is non-notifiable) within one year of closing on the basis that is it likely to substantially lessen or prevent competition ("SLPC").**
  - In 2019, the Bureau announced a heightened focus on finding and challenging non-notifiable deals

Is Pre-Closing Merger Notification Required?



Advance Ruling Certificates

- **The waiting period can be terminated early if an Advance Ruling Certificate ("ARC") is obtained.**
- **An ARC request is a written brief to the Commissioner that typically describes the transaction, and why it will not likely lead to a substantial lessening or prevention of competition.**
- **On deals with little to no overlap (i.e. where post-merger shares are <10%), filing of an ARC request can provide a much quicker and cost-effective clearance.**
  - 98.5% cleared within 14 calendar days
- **However, the filing of an ARC request does not engage the statutory waiting period, so there could be a timing risk if an ARC is not granted.**

Substantive Considerations in Merger Review – Just like the US

- **The Bureau will consider whether a deal is likely to lead to an SLPC by determining whether it will enhance the ability of the merged parties to exercise market power on either a unilateral or coordinated basis**
  - A unilateral exercise of market power would be where the post-merger parties could harm competition through their own unilateral conduct
  - A coordinated exercise of market power would be where the merger reduces the overall competitive vigor in a market
- **The Bureau considers both horizontal and vertical effects and can challenge a merger on the basis of either or both**
- **Non-price dimensions of competition can be considered harms in the competition analysis, including privacy protection and terms regarding use of consumers' data**
- **Analysis is similar to test under U.S. antitrust law**

Safe Harbor Thresholds

- **The Bureau has stated that it will generally not challenge mergers on the basis of concerns related to unilateral effects where the merged parties' post-merger share of any relevant market does not exceed 35%**
- **The Bureau has stated that it will generally not challenge mergers on the basis of concerns related to coordinated effects where:**
  - The merged parties' post-merger share of any relevant market does not exceed 10%; or
  - The post-merger market share accounted for by the four largest firms in any relevant market (the four-firm concentration ratio or CR4) is than 65 percent

Efficiencies in Canadian Merger Review

- **Unlike in the US and the EU, the Act:**
  - Provides a complete defence in a merger review for efficiencies that can be shown to outweigh any anti-competitive effects;
  - Does not require that efficiencies benefit consumers
- **Proof of even marginal efficiency gains is sufficient to require the Bureau to quantify anti-competitive effects so as to show that it outweighs the gains a balancing of efficiencies.**
- **Although rare, this can lead to divergent outcomes between the US and Canada**
  - In the Superior Plus/Canexus case, the Bureau and the US FTC considered a merger between producers of sodium chlorate and chlor-alkali products – and came to opposite decisions
  - Bureau cleared the transaction on the basis that the efficiency gains in Canada were greater than the anti-competitive effects of the transaction, such as higher prices
  - The efficiencies identified included the elimination of overhead costs, freight optimization and the elimination of duplicate corporate services

The Failing Firm Merger Defence

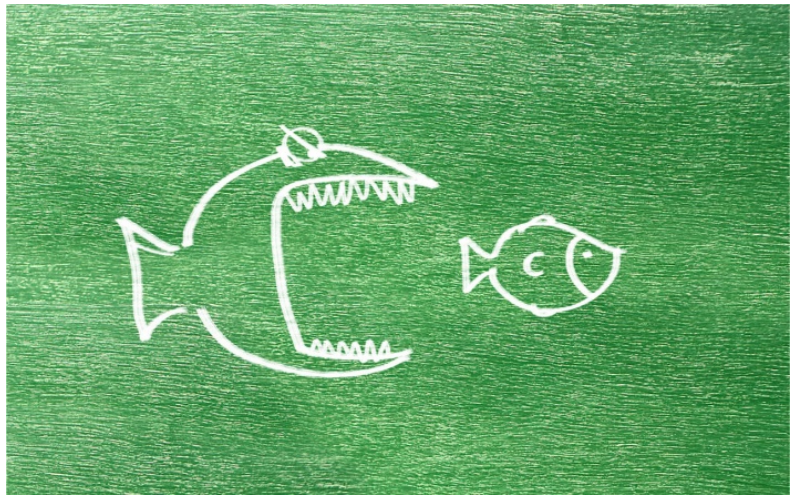
- **One factor relevant to the Bureau's assessment of a merger is whether the target has failed or is likely to fail**
  - The Bureau may allow an acquisition that would otherwise be likely to substantially lessen competition if it is satisfied that the target would otherwise fail and there is not a competitively preferable outcome
- **A firm is considered to be failing if:**
  - it is insolvent or is likely to become insolvent;
  - it has initiated or is likely to initiate voluntary bankruptcy proceedings; or
  - it has been, or is likely to be, petitioned into bankruptcy or receivership
- **The insolvency or likely insolvency must relate to the business where competition concerns arise**

Failing Firm

- **The Bureau will conduct a careful analysis of the firm's financial information**
  - E.g., financial statements, liquidity reports and forecasts, business plans, correspondence to and from creditors, as well as documents related to plans to initiate bankruptcy proceedings or seek creditor protection
- **When analyzing an acquisition of a firm that is determined to be failing, the Bureau will consider whether there are alternative scenarios with respect to failing firm that would lead to competitively preferable outcomes:**
  - Restructuring and retrenchment;
  - Competitively preferable purchaser; and
  - Liquidation

Killer Acquisitions

- **Competition authorities, including the Bureau, have publicly promised to be on the lookout for "killer acquisitions" – generally defined as where a large player buys a small player to prevent it from growing into a future competitive threat**
- **Recent US complaints outlined a series of alleged killer acquisitions by Facebook, including Instagram and Whatsapp**
- **The Bureau can go after alleged killer acquisitions – even of small non-notifiable deals**
  - Only difference from US is that Bureau has a one-year limitation period for merger challenges



Killer Acquisitions

- **The US DOJ recently brought a classic killer acquisition claim in the tech space that may herald future claims**
  - The parties abandoned the deal after the challenge was launched
- **DOJ claimed that acquiring Plaid, Visa would eliminate a nascent competitive threat that would, absent the deal, likely result in substantial savings and more innovative online debit services for merchants and consumers**
- **Competition from Plaid would mean that prices for online debit transactions would fall, benefiting merchants and consumers (through lower prices and/or rewards/incentives to switch to Plaid's pay-by-bank debit service)**
- **DOJ said the merger would "eliminate a disruptive and innovative competitor" and give Visa a "[f]ront row seat to what is happening in the [f]intech world (e.g. which apps are growing, at what velocity and where)", allowing Visa inside access to know which fintechs are more likely to develop competitive alternative payments methods – and how to beat or buy them.**

The Visa-Plaid Killer Acquisition Example

44. As Visa learned more about Plaid's efforts to launch its own pay-by-bank debit service that would directly compete with Visa, its executives grew increasingly alarmed. During an early November 2019 meeting involving executives from both firms, Plaid's co-founder explained how Plaid's nascent technology would allow merchants to shift transactions easily from traditional forms of online debit to Plaid's pay-by-bank debit service. This prompted a senior Visa executive to report internally that Plaid's co-founder had "described the service with the joy of someone who forgot we had 70% share." Ultimately, Visa recognized that the best course of action for its business was to eliminate Plaid as a competitive threat by purchasing Plaid itself. In internal documents, a Visa executive observed that "[t]he acquisition is in part defensive, not just for Visa but also on behalf of our largest issuing [bank] clients, whom we believe have a lot to lose if [pay-by-bank transactions] accelerate as the result of Plaid landing in the wrong hands. It is in our collective interest to manage the evolution of these payment forms in a way that protects the commercial results we mutually realize through card-based payments."

Abuse of Dominance – The Canadian Version of Monopolization

- **The Bureau has the power to bring cases just like the prominent cases that have recently been brought in the US against "Big Tech" giants Google and Facebook under the "abuse of dominance" provisions**
- **These provisions allow the Bureau to seek an order against a dominant firm or a dominant group of firms that engages in one or more practices of anti-competitive acts resulting in an SLPC**
  - As with mergers, non-price dimensions of competition can be considered competitive harms, including privacy protection and terms regarding use of consumers' data

False or Misleading Representations

- **The Bureau can challenge companies under the false and misleading representations provisions of the Act for promoting their products use false or misleading representations**
  - The representations caught can include ads, terms or service, or any other claims made by companies in any medium
- **The Bureau takes the position that claims regarding the protection of privacy – whether in public statements, privacy policies, etc – can be the basis for claims under these provisions if they drive consumers to use a site under false or misleading pretences**

In Sum…the Bureau can Challenge Big Tech

- The Bureau has the power to challenge Big Tech in many of the same ways as US and other global authorities have.
- It recently affirmed that the "core principles of competition law are generally up to the task of dealing with the digital economy"
- And the Bureau is loudly proclaiming its focus on the digital economy and Big Tech

Digital – The Bureau Talks a Big Game!

- **In July 2019, the Bureau appointed a Chief Digital Enforcement Officer (CDEO).**
  - **Says that the CDEO has helped to advance initiatives to modernize processes, be digital-by-design, and provide employees with new tools to enforce the law.**
- **Upon the appointment of the Commissioner to his term leading the Bureau in 2019, the Cabinet Minister appointing him wrote:**

> Some analysts have suggested that the emerging digital economy harkens back to previous eras where concerns about market dominance brought about break-up antitrust actions by regulators. Others have questioned whether the ease of data accumulation in the digital environment requires new tools or mechanisms to avoid abuse.
>
> I would be remiss in my role as Minister if I were not to consider how well suited our system is to the present and the future marketplace, with a view to ensure that our competition infrastructure is fit for this purpose and able to remain responsive to a modern and changing economy.

Digital – The Bureau Talks a Big Game!

- **February 2020 “cornerstone for the Bureau's future” released:**

- **In this document, the Bureau promises to make active – including proactive – enforcement its main focus.**

Reality?

- The Bureau has promised to make active – including proactive – enforcement its main focus – with a specific focus on Big Tech
- And yet, there is no indication of any action even remotely similar to that which has been launched in the US, EC and elsewhere, whether in merger reviews or other conduct claims
- The Bureau has talented, motivated and smart enforcers who want to be at the forefront of Big Tech enforcement
- And yet…

Why such Short Arms?

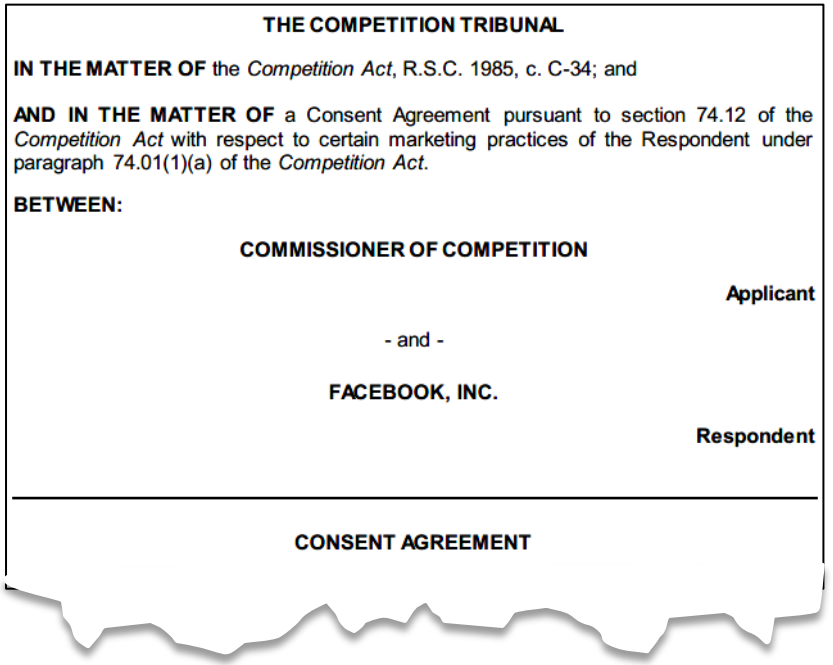
- **Likely the Bureau's biggest challenge is that it faces extreme budget challenges.**
- **Its overall budget is a drop in the bucket compared to other antitrust regulators**

Competition Regulator	Annual Budget (USD)
Canada	$37.8 million
European Commission	$122 million
US (DOJ + FTC)	$302 million
Australia	$182.2 million

- **Note that the US number does not include State AGs, which also invest large sums in antitrust enforcement**
- **Similarly, the EC number does not include member states, which also invest large sums in antitrust enforcement**

Seeking Bang for Its Buck

- **The budgetary challenges mean that the Bureau has to do the most it can with its budget**
- **If other regulators are doing the "dirty work" on "Big Tech", the Bureau has to justify why it should use precious limited resources on the same cases**
  - Effectively free-riding on fellow authorities
- **If it can be done reasonably cheaply, expect certain follow-on copycat claims, but they are not a priority**
  - Recent Cdn. $9 million (US $7.1 million) settlement with Facebook re its alleged false or misleading representations about disclosure of personal information is an example



THE COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34; and

AND IN THE MATTER OF a Consent Agreement pursuant to section 74.12 of the *Competition Act* with respect to certain marketing practices of the Respondent under paragraph 74.01(1)(a) of the *Competition Act*.

BETWEEN:

COMMISSIONER OF COMPETITION

Applicant

- and -

FACEBOOK, INC.

Respondent

CONSENT AGREEMENT

Other Impediments to Bureau Challenge

- Outside of the merger context, the Bureau is very limited in the penalties it can seek
- Abuse of dominance and most false and misleading representation claims carry a maximum fine of Cdn. $10 million (US $7.8 million) for a first offence and Cdn. $15 million (US $11.8 million) for subsequent offences

CBC **New tools, stiffer penalties needed to police big tech companies, says competition watchdog**

"The maximum penalties for anti-competitive behaviour [...] lack the teeth necessary to deter anti-competitive behaviour."

- Matthew Boswell
Commissioner of Competition

What Are We Likely to See from the Bureau?

- **This means that the most-likely Bureau actions against Big Tech will be in cases where there are specific and most-likely unique effects on Canadians – issues that other authorities won't go after**
- **The Bureau is also likely to save room to challenge "killer acquisitions" of Canadian tech companies by Big Tech – or other mergers involving homegrown companies**
  - Overlap here with the ICA processes

The ICA and Big Tech – The Long Arm Emerges

- **Contrary to the Bureau's relative inaction, the ICA – and in particular the National Security Review process – is getting a lot of use**
- **This can be difficult for foreign companies engaged in M&A in Canada**
- **The criteria on which National Security Reviews are conducted are not defined in the ICA or publicly revealed**
  - Even investors subject to national security reviews are generally only provided high-level descriptions of the concerns raised


THE GLOBE AND MAIL

If net benefit is mysterious, national security review is a black box

ICA 101

- **The ICA process begins with determining whether a deal is subject to Net Benefit Review – and if so, which type**
- **This is determined by calculating whether the deal exceeds the applicable monetary threshold**
- **The applicable threshold depends on a number of factors, including:**
  - Whether the country of origin of the "ultimate controller" of the investor is a member of the WTO and/or a participant in other trade agreements (such as USMCA/NAFTA 2.0) with Canada
  - Whether the investor is a "state-owned enterprise"
  - Whether the Canadian business is a "cultural" business
  - Whether the acquisition of control of the Canadian business is direct or indirect

Net Benefit Review – Thresholds

- **Key thresholds for direct acquisitions of non-cultural businesses**:

Investor Type	Threshold (Cdn.)	Basis for threshold
Private-sector investors from WTO member-states	$1.043 billion	Enterprise Value
Private-sector investors from the EU, US, Australia, Chile, Colombia, Honduras, Japan, Mexico, New Zealand, Panama, Peru, Singapore, South Korea and Vietnam	$1.565 billion	Enterprise Value
State-owned enterprise investors from WTO member-states	$415 million	Asset Value
Investors from non-WTO member-states	$5 million	Asset Value

Net Benefit Review – Thresholds

- **Other relevant thresholds:**

Investment Type	Threshold (Cdn.)	Basis for threshold
Indirect investments from WTO member-states in non-cultural businesses	Net Benefit Review not applicable	N/A
Indirect investments from non-WTO member-states	$50 million	Asset Value
Direct investments in cultural businesses	$5 million	Asset Value
Indirect investments in cultural businesses	$50 million	Asset Value

ICA 101

- **For any acquisition of a Canadian business that does not exceed the applicable threshold, an "ICA Notification" form has to be filed within 30 days after closing**
  - Same for any establishment of a new business in Canada by a non-Canadian
- **For any acquisition of a Canadian business that exceeds the applicable threshold, Net Benefit Review is required**
  - If a Net Benefit Review is required, there is a 45-day waiting period after filing an application for review with the Minister of Innovation, Science, and Economic Development ("Minister") (or, the Minister of Canadian Heritage, for cultural businesses) during which the transaction may not close
    - This can be extended unilaterally by the applicable Minister for an additional 30 days, or beyond with the consent of the parties
  - Where a business is involved in cultural and non-cultural activities, both Ministers must approve
- **The applicable Minister can approve a transaction, block it altogether, or approve with conditions**

Net Benefit Review Criteria

- **The investor must satisfy the Minister that the transaction will be of "net benefit" to Canada in order for it to be approved**
  - In making this determination, the Minister considers a number of evaluative factors – which provide a broad basis on which concerns can be expressed:
    - The effect of the transaction on economic activity in Canada;
    - The degree of participation by Canadians in the business post-closing;
    - The effect of the transaction on productivity, efficiency, technological development, product innovation, product variety, and competition in Canada, as well as Canada's global competitiveness; and
    - The compatibility of the transaction with national industrial, economic, and cultural policies.

Conditional Approval Following Net Benefit Reviews

- **Net benefit reviews often conclude with the Minister requiring the investor to agree to legally binding undertakings as a condition of approval**
  - These often include commitments re maintenance of employment, investment, Canadian content, etc.
  - Investors must provide annual post-closing reports to the Minister certifying ongoing compliance
  - Undertaking compliance is monitored for the duration of the commitment.
- **In addition to or instead of post-closing undertakings, the Minister can also require divestitures as a condition of approval**

National Security Review – The Big Gun

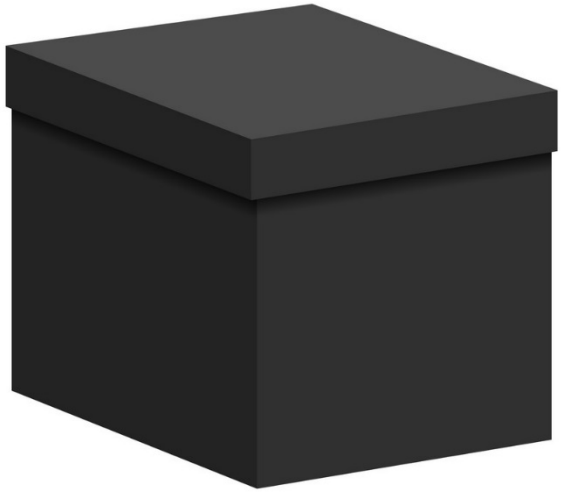
- **Given the high thresholds, most inbound private sector M&A – particularly from countries like the US with trade agreements with Canada – is not subject to Net Benefit Review**
- **But, National Security Review can be applied to virtually any investment of any value into Canada by a non-Canadian – including non-controlling investments – to determine whether they "would be injurious to national security"**
- **There are no thresholds applicable to the National Security Review process**
- **Regulations provide the time periods during which the Minister can initiate the National Security Review process**:
  - For an investment subject to Net Benefit Review, **45 days** from the date an complete application for review was filed
  - For an acquisition of control not subject to Net Benefit Review, **45 days** from the date on which ICA Notification is filed
  - For any other investment, **45 days** from closing

Consequences of National Security Review

- **The government can block the transaction (or require divestiture if already completed), approve it, or approve with conditions**
- **Binding undertakings to satisfy the government that an investment will not harm national security may be required as a condition of approval**
  - Including partial divestitures
- **While parties may offer undertakings to mitigate national security concerns, some concerns appear unable to be resolved**
  - For example, it was widely reported that Accelero offered a number of undertakings in order to secure approval of its purchase of MTS Allstream, including to terminate certain services provided to government and refrain from using equipment supplied by Huawei – but the transaction was still blocked
- **National security concerns can and have been raised outside of the formal review process to dissuade potential bidders or cause investors to abandon deals**
  - Lenovo/Blackberry (Chinese investor proposing acquisition of smartphone provider); George Forest International / Forsys Metals (uranium)

“Injurious to National Security”

- The “would be injurious to national security” criteria for blocking or imposing conditions on an investment under the National Security Review provisions is very broad, affording the government significant scope within which to prevent investments it believes would be problematic
- The concept of “national security” is not defined in the ICA, and the government has generally offered very little transparency into the true nature of its concerns with various investments

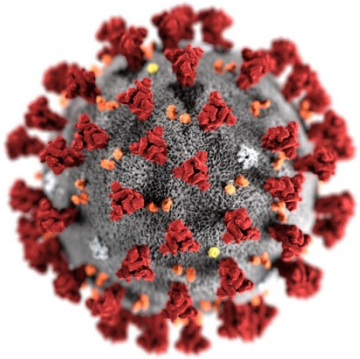


Substance of National Security Review

- **Prior to 2020, the only official guidance on the concerns covered by National Security Reviews provided that the following factors are considered with regard to the potential effects of the investment:**
  - Canada's defence capabilities and interests
  - Transfer of sensitive technology or know-how outside of Canada
  - Security of Canada's critical infrastructure
  - Supply of critical goods and services to Canadians, or the supply of goods and services to the government
  - Enabling foreign surveillance or espionage
  - Intelligence or law enforcement operations
  - Canada's international interests, including foreign relationships
  - Activities of illicit actors, such as terrorists or organized crime

COVID-19 and the ICA – “Enhanced Scrutiny”

- **In April 2020, citing the “unique” and “extraordinary circumstances” of the global COVID-19 pandemic and “sudden declines in valuations [that] could lead to opportunistic investment behaviour”, the government announced that would be subjecting “certain foreign investments into Canada to enhanced scrutiny”**
- **The specific targets of the “enhanced scrutiny” are investments in Canadian businesses:**
  - That are related to public health or involved in the supply of critical goods and services; or
  - By investors that are owned, subject to influence by or even closely tied to foreign states



Targets of National Security Review

- **It's clear that SOE – and really any Chinese investment – are subject to heightened scrutiny, pre-COVID and even more-so today**
  - SOE refers to more than actual state-controlled investors – even minority state-connected ownership has been cited as a concern
- **SOE investment in virtually any industry may raise concerns**
- **However, non-SOE investment has and will continue to be scrutinized in sensitive areas**
  - This is where American Big Tech should be prepared

Substance of National Security Review – Big Tech Concerns

- Concern about vulnerability of Canadian telecom/electronic infrastructure and sensitive data to potentially malicious foreign actors, have been the basis for a number of National Security Reviews pre-COVID
- Possible transfer of personal information to hostile foreign actors is a common concern
- American private sector investors are of less concern, but not immune from scrutiny
- Any investments related to public health or involved in the supply of critical goods and services have to be considered possible targets of National Security Review

Impact of National Security Review

- **Timelines potentially long: National security reviews can last for 200 days (or more with the consent of the parties)**
- **When the National Security Review processed is commenced, there is a good chance that adverse action will be taken**
- **In 2018/19, the process was commenced 9 times**
  - 2 were ultimately not reviewed (and therefore allowed)
  - 7 were reviewed
- **3 of the 7 investments that were reviewed were ultimately approved**
- **The other 4 did not survive:**
  - In two cases, divestiture was ordered
    - A Chinese investment in urban transit systems
    - A Swiss investment in engine, turbine and power transmission equipment manufacturing
  - In the other two cases, the investors withdrew the proposed investments

How to Prevent Unwelcome National Security Review Surprises

- **Most National Security Reviews are of deals that do not require pre-closing Net Benefit Review**
- **If buyers don't take steps to ensure that the time period during which the National Security Review process can be commenced has expired <u>before</u> closing, they can be subject to a post-closing National Security Review**
  - This can result in terrible outcomes, including costly divestitures
- **However, it's not difficult to include appropriate terms in the purchase agreement to ensure this cannot happen**

Thank You

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