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# Pre-Merger Notification Interpretation Guideline Number 3

## Exemptions for Acquisitions in the Ordinary Course of Business (Paragraph 111(a) of the Act)

Canada

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**Enforcement guidelines**

June 20, 2011

Notice

**This publication replaces the following Competition Bureau publication:**

Enforcement Guidelines — Interpretation Guidelines #3: Paragraph 111(a). Exemptions for Acquisitions in the Ordinary Course of Business, May 2001

This Interpretation Guideline is issued by the Commissioner of Competition ("Commissioner"), who is responsible for the administration and enforcement of the *Competition Act* ("Act"). The purpose of this Guideline is to assist parties and their counsel in interpreting and applying the provisions of the Act relating to notifiable transactions. This Guideline sets out the general approach taken by the Competition Bureau ("Bureau") and supersedes all previous statements made by the Commissioner or other Bureau officials. This Guideline is not intended to be a binding statement of how discretion will be exercised in a particular situation and should not be taken as such, nor is it intended to substitute for the advice of legal counsel to the parties, or to restate the law. Guidance regarding a specific proposed transaction may be requested from the Merger Notification Unit[Footnote 1].

## Definition

Paragraph 111(a) of the Act provides that the following class of transaction is exempt from the application of Part IX of the Act:

**111.** (*a*) an acquisition of real property or goods in the ordinary course of business if the person or persons who propose to acquire the assets would not, as a result of the acquisition, hold all or substantially all of the assets of a business or of an operating segment of a business.

## Policy

In determining whether an acquisition of real property or goods is exempt under paragraph 111(a) of the Act, the first step is to determine whether the proposed acquiror will, as a result of the acquisition, hold all or substantially all of the assets of a business or of an operating segment of a business. If the assets being sold constitute all or substantially all of the assets of a business or of an operating segment of a business, the exemption in paragraph 111(a) is not available, regardless of whether the transaction is in the ordinary course of business. If the assets do not constitute all or substantially all of the assets of a business or of an operating segment of a business, then the transaction will be exempt if it is in the ordinary course of business.

In a proposed transaction that includes an acquisition of real property or goods that is exempt under paragraph 111(a) of the Act, the acquisition of any other assets in that transaction may be subject to notification under section 114 of the Act as if the assets were being acquired in a separate transaction.

## Step one: Will the acquiror, as a result of the acquisition, hold all or substantially all of the assets of a business or of an operating segment of a business?

The purpose of the latter part of paragraph 111(a) of the Act is to deny the exemption if the proposed transaction involves the sale of a group of assets that, when considered on its own, constitutes all or substantially all of the assets of a business or an operating segment of a business. Such acquisitions have the potential to concentrate productive capacity and thereby diminish competition.

The latter part of paragraph 111(a) of the Act applies to deny the exemption in two circumstances. The first is where, as a result of the acquisition, the purchaser will acquire all or substantially all of the assets of a business, which could include the assets of both operating and non-operating businesses. However, given that subsection 110(2) of the Act provides that Part IX of the Act applies only to an acquisition of assets of an operating business, the exemption in paragraph 111(a) could only apply to an acquisition of all or substantially all of the assets of an operating business. Consequently, for purposes of paragraph 111(a), the term "business" will be interpreted to mean "operating business", as that term is defined in section 108 of the Act.

The exemption in paragraph 111(a) of the Act does not apply where a purchaser proposes to acquire only a segment of an operating business and that segment is an operating segment. An operating business may have operating and non-operating segments. Each operating business will have at least one segment that is an operating segment. In addition, an operating business may have other operating segments and non-operating segments, such as dormant or mothballed facilities. Accordingly, where an operating business has both one operating segment and one non-operating segment, the latter part of paragraph 111(a) applies and the exemption is not available where the purchaser acquires the operating segment. Similarly, where an operating business has more than one operating segment, the latter part of paragraph 111(a) applies and the exemption is not available where the purchaser acquires at least one of the operating segments.

In considering whether a group of assets constitutes an operating business or an operating segment, the manner in which the vendor organizes or defines the group of assets is not determinative and, in many cases, will not be relevant. Each group of assets will be analyzed on its own to determine whether the group constitutes all or substantially all of an operating business or an operating segment. Each location of a company's business may be viewed as an operating business or an operating segment. Examples of an operating business or an operating segment may include, but are not limited to, a regional division, a company branch, a retail store or a factory.

The word "hold" in paragraph 111(a) of the Act is interpreted consistently with that word as it appears in subparagraph 2(4)(a)(i) of the Act. As a result, an asset may be held by a person "directly or indirectly, whether through one or more subsidiaries or otherwise, otherwise than by way of security only, by or for the benefit of that person." An asset is held directly if the person is the beneficial owner of the asset. In that circumstance, the asset is held by the person. An asset may be held indirectly by a person if a subsidiary of that person is the beneficial owner of the asset. An asset may also be held indirectly by a person that is the beneficial owner of the asset if legal or registered ownership is held by a third party, such as an agent or a trustee. In both circumstances, the asset is held for the benefit of the person.

Whether a particular group of assets constitutes "substantially all" of the assets of an operating business or an operating segment will depend on the circumstances of each case. Both quantitative and qualitative considerations will be examined. Generally, where a group of assets is such that the purchaser could reasonably be expected to carry on an operating business or an operating segment, the "substantially all" test will have been satisfied.

## Step two: Acquisitions of real property or goods in the ordinary course of business

For purposes of paragraph 111(a) of the Act, an acquisition of real property or goods is in the ordinary course of business if the acquisition is a routine business transaction, that is, the transaction is one which firms carry out in the conduct of business in general. Such a transaction does not include an acquisition of assets which would transfer, directly or indirectly, production capacity between firms in the same line or lines of business, unless the seller is replacing the production capacity provided by the assets being sold.

The following examples of acquisitions of assets that are exempt are not intended to be exhaustive. There may be other acquisitions of real property or goods that are in the ordinary course of business and therefore exempt under paragraph 111(a) of the Act.

One example of an acquisition of goods that is in the ordinary course of business is an acquisition of new goods. Acquisitions of new goods are routine sales by manufacturers, wholesalers or retailers. The term "new" implies that the goods have not been used to generate income. Acquisitions of new goods normally expand the supply of products or expand productive capacity and therefore do not tend to lessen competition.

Another example of an acquisition of goods that is in the ordinary course of business is an acquisition of current supplies. The word "current" means that the goods generally have a useful life of less than one year. However, if the purchaser's normal operating cycle is longer than one year, the goods may also have a useful life that is longer than one year. Current supplies include the following kinds of new and used goods:

- goods acquired and held solely for the purpose of resale or leasing to an entity that is not an affiliate of the purchaser (e.g., inventory);
- goods acquired for consumption in the daily conduct of the purchaser's business (e.g., office supplies or maintenance supplies); and
- goods acquired to be incorporated into the purchaser's final product (e.g., raw materials and components).

Purchases of current supplies are also routine. Again, acquisitions of current supplies should not in any way diminish the capacity of the selling firm to compete.

One example of an acquisition of real property that is in the ordinary course of business is an acquisition of new facilities. A new facility is a structure that has not produced income and was either constructed by the seller for sale or held at all times by the seller for resale. Like acquisitions of new goods, acquisitions of new facilities normally expand the supply of real estate products or expand productive capacity and therefore do not tend to lessen competition.

Another example of an acquisition of real property in the ordinary course of business is an acquisition of a used facility from a lessor that has held title to the facility for financing purposes by a lessee that has had sole and continuous possession of the facility since it was first built as a new facility.

## Examples

The examples below are hypothetical and are intended only to illustrate the Bureau's interpretation of this section as outlined above.

### Example 1

A intends to sell to B one of several grocery stores that A owns and operates. The assets to be sold include the store building and underlying real property, the store's inventory and the fixtures and chattels located at the store. Each of A's stores constitutes an operating business. The assets to be sold constitute all or substantially all of the assets of that operating business. Accordingly, B's acquisition of the grocery store from A does not meet the first test and is not exempt under paragraph 111(a). It is not necessary to consider the second test of whether the transaction constitutes an acquisition of real property or goods in the ordinary course of business.

### Example 2

A intends to sell to B one of several office buildings that A owns and manages. The office building is leased to a variety of commercial tenants. The assets to be sold include the building and underlying real property, A's interest as landlord under the leases with the commercial tenants, and the fixtures and chattels located at the office building. B intends to use the building as its head office. For that purpose, following the purchase of the office building, B plans to not renew the leases of the existing tenants upon the expiry of those leases. The office building to be sold constitutes an operating business. The assets to be sold constitute all or substantially all of the assets of that operating business. Accordingly, B's acquisition of the office building from A does not meet the first test and is not exempt under paragraph 111(a). It is not necessary to consider the second test of whether the transaction constitutes an acquisition of real property or goods in the ordinary course of business.

### Example 3

A and B are two telecom companies. A intends to sell to B 12 fibreoptic strands which represent half of the strands of a cable. The cable was originally acquired by A for its own use. The strands to be sold have never been used to generate income. The 12 fibreoptic strands do not constitute all or substantially all the assets of a business or of an operating segment of a business. Therefore, the transaction meets the first test. The assets to be sold were not purchased and held by A at all times for resale and therefore are not current supplies. While the assets are new given they have never been used, the transaction is not a routine sale given that the acquisition of these assets would transfer production capacity between firms in the same line of business. As a result, it does not meet the second test and is not an acquisition of goods in the ordinary course of business. The transaction is not exempt under paragraph 111(a).

### Example 4

A, a railroad company, intends to purchase a number of used locomotives engines from B, another railroad company. B does not intend to replace the capacity provided by the engines to be sold. The engines do not constitute all or substantially all the assets of a business or of an operating segment of a business. Therefore, the transaction meets the first test. The purchase of the engines is an acquisition of goods that transfers production capacity between firms in the same line of business. As a result, the transaction does not meet the second test as it is not an acquisition in the ordinary course of business and is not exempt under paragraph 111(a).

## Example 5

A, a car manufacturer, intends to acquire more than $35 million worth of steel from a steel producer to be used in the car manufacturing process. The transaction meets the first test as the steel being acquired does not constitute all or substantially all the assets of a business or of an operating segment of a business. The acquisition also meets the second test as it is a routine acquisition of raw material to be incorporated into the purchaser's final product and, accordingly, meets the definition of current supplies. The transaction is exempt under paragraph 111(a).

## Example 6

A is a brewery and B is a soft drink bottler. A intends to acquire two labelling machines and one bottle filler from B. The equipment being sold is not used by B. The assets being acquired are not all or substantially all of the assets of a business or of an operating segment of a business. Therefore it would meet the first test. The acquisition of these assets is not a transfer between firms with the same line of business. The acquisition is an acquisition in the ordinary course of business which meets the second test. The transaction is exempt under paragraph 111(a).

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# Footnote

Footnote 1

For further information, please refer to the *Procedures Guide for Notifiable Transactions and Advance Ruling Certificates* under the *Competition Act* at p.14.