

FOREIGN INVESTMENT SCREENING
UNDER CANADA'S *INVESTMENT CANADA ACT*

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Oliver Borghers, Emily Rix and Lorne Salzman
McCarthy Tétrault LLP

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Oliver Borgers, Emily Rix and Lorne Salzman¹

A. Introduction

1. After many years of relative obscurity, foreign investment screening has come back into the spotlight in Canada. Although Canada maintains an open, even eager, attitude towards foreign investment, a variety of new pressures have emerged that are leading to changes in the generally benign screening approach and attitudes that have prevailed since the 1980s.

2. On the one hand, there has been an increasing recognition that the current screening thresholds are too strict, and thus too many foreign investors are unnecessarily burdened with onerous screening requirements. After studying the matter, the Competition Policy Review Panel recommended in 2008 that these thresholds be liberalized and that particularly strict thresholds for several sensitive sectors be eliminated.² In response to these recommendations, the government implemented amendments to the *Investment Canada Act* ("ICA" or the "Act") early in 2009, and new regulations amending the *Investment Canada Regulations*³ are in the process of finalization.⁴

3. On the other hand, the government has demonstrated a tougher attitude towards foreign investors and foreign investments that raise public policy concerns. The most notable such concern in the post-September 11 era is, understandably, national security. With amendments to the ICA in 2009, the government gave itself new powers to screen investments that might be injurious to national security. The government has also applied the existing screening rules with

¹ Oliver Borgers, Emily Rix and Lorne Salzman are members of McCarthy Tétrault LLP's Competition Law Group. The comments in this paper, which we believe are accurate and reliable, are necessarily of a general nature. Clients are urged to seek specific legal advice on matters of concern and should not rely solely on the information provided herein.

² See www.ic.gc.ca/eic/site/cprp-gepmc.nsf/eng/home

³ SOR/85-611

⁴ See www.gazette.gc.ca/rp-pr/p1/2009/2009-07-11/html/reg2-eng.html. The *Regulations Amending the Investment Canada Regulations* were published for comment in the Canada Gazette Part I, Vol. 143, No. 28 on July 11, 2009. These regulations have not yet been registered.

new vigour, leading to the rare rejection of one high profile acquisition in 2008,⁵ and the first-ever legal action against an investor for failing to live up to its undertakings that were a condition of investment approval.⁶

4. Given these pressures, it is useful to look at the requirements and processes under the ICA as they currently exist, and to describe the changes that are being implemented. In the following pages, we describe the history of the ICA and the legal framework for foreign investment screening under the Act. We also describe some key practical issues that arise when dealing with foreign investment screening. We go on to review developments relating to State Owned Enterprises. We then describe the national security additions to the ICA, and offer our thoughts as to how they will be applied.

B. Background to the ICA

5. Beginning in the 1960s, Canadians increasingly expressed concern about the level of foreign investment in the country and its impact on the Canadian economy. These concerns were based on a perception of high and increasing levels of foreign investment in Canadian industry and natural resources, primarily from US companies. In response, the federal government sponsored a number of studies to investigate the level and implications of foreign investment in Canada.

6. Based on the recommendations in the ensuing reports, the federal Parliament passed the *Foreign Investment Review Act* (“FIRA”) in 1974. FIRA established the Foreign Investment Review Agency, a government department that reviewed direct foreign investment proposals before they could proceed, with final approval resting with the Governor in Council (that is, the

⁵ See paragraph 55 below and Industry Canada press release: “Minister of Industry Confirms Initial Decision on Proposed Sale of Macdonald, Dettwiler and Associates Ltd. to Alliant Techsystems Inc.,” May 8, 2008, at www.ic.gc.ca/eic/site/ic1.nsf/eng/04219.html

⁶ The Attorney General of Canada filed an application with the Federal Court in July 2009 for an order directing U.S. Steel to comply with undertakings it gave as a condition of approval of its 2007 acquisition of Stelco Inc. See Industry Canada press release “Industry Minister Clement Takes Further Steps to Hold U.S. Steel to Its Investment Canada Act Commitments,” July 17, 2009, at www.ic.gc.ca/eic/site/ic1.nsf/eng/04836.html
In response, U.S. Steel moved to challenge the validity of the enforcement proceedings on the basis that they contravened its rights under the Canadian Charter of Rights and Freedoms and the Canadian Bill of Rights. On June 14, 2010, the Federal Court of Canada dismissed U.S. Steel’s motion. U.S. Steel filed a notice of appeal of this decision and sought to stay the Attorney General’s application pending disposition of the appeal. On July 23, 2010, the Federal Court of Appeal dismissed U.S. Steel’s motion to stay the application.

federal cabinet). Both foreign takeovers of existing Canadian businesses and the creation of new foreign-owned businesses in Canada were subject to scrutiny. In order to be acceptable, a foreign investor had to demonstrate that the proposed transaction was likely to be of significant benefit to Canada. Review under FIRA was not intended to reduce foreign ownership, but instead to increase the benefits that Canadians would obtain from foreign investments.

7. FIRA was controversial from the beginning. Within Canada, FIRA was criticized because it failed to limit or even review the expansion of existing foreign-controlled businesses, and it did not address the establishment of “related businesses” by a foreign investor already established in Canada. Internationally, Canada was criticized, particularly by the US, by allegations that foreign takeovers were deliberately and unjustly being blocked in favour of Canadian purchasers and interests, and that excessive undertakings were being imposed as a condition of allowing foreign investment.

8. These criticisms, combined with the recession of the early 1980s, led the incoming Conservative government to move away from a policy of economic nationalism enshrined in FIRA. In 1985, the incoming government changed the focus of foreign investment review in order to specifically encourage foreign investment, leading Prime Minister Brian Mulroney to declare that “Canada is open for business again.”

9. FIRA was amended and renamed the “Investment Canada Act.” In contrast to FIRA, the ICA expressly stated that its purpose was to “encourage investment in Canada by Canadians and non-Canadians that contributes to economic growth and employment opportunities and to provide for the review of significant investments in Canada by non-Canadians in order to ensure such benefit to Canada.” Although the investment review process from FIRA was largely retained, the ICA raised the thresholds for review, shortened the time for review, and improved the efficiency of the review process in comparison to the procedure under FIRA.

10. Following the enactment of the ICA, the Canadian government exhibited a relaxed and facilitative approach to foreign investment (although the intensity of scrutiny under the ICA has been increasing over the past decade). In 2007, increasing public concern about the “hollowing out” of corporate Canada – for example, through the foreign takeovers of several prominent Canadian companies such as the Hudson’s Bay Company, La Senza, and Four Seasons Hotels –

as well as pressure from the political opposition, led the government to establish the Competition Policy Review Panel (the “Panel”) in 2007 with the mandate to review key elements of Canada’s competition and investment policies, gauge their efficacy, and make recommendations as to reforms.

11. In June 2008, the Panel issued its final report, *Compete to Win*.⁷ The report was generally critical of Canada’s competitiveness compared to its major trading partners, and placed some of the blame on obsolete or inappropriate rules that restricted foreign investment. In response, the government sponsored amendments to the ICA and these were passed by Parliament in March 2009. The amendments reduced and clarified some of the restrictions on foreign investment, but also imposed some new burdens, most notably through a new national security screening mechanism. In the following sections we will describe the ICA in its present form, which follows the 2009 amendments.

C. The Legal Framework of the ICA

12. The ICA is a complex statute. At its core, however, it contains two straight-forward procedures:

- (a) It requires non-Canadian investors that propose to make sizeable investments in Canadian businesses to submit their proposed investments for review and approval by the Canadian government; and
- (b) It requires non-Canadian investors that propose to make smaller investments in Canadian businesses, or to start up new Canadian businesses, to give notice of their proposed activities to the Canadian government.

A non-Canadian investor includes a Canadian incorporated entity that is ultimately controlled by one or more non-Canadians.

13. Once the foreign investor submits a completed review application or notice, as applicable, the government screens the investment for the following purposes:

- (a) In the case of an investment subject to the review/approval procedure, it is assessed to determine if it is “likely to be of net benefit to Canada.”

⁷ The report is available at www.ic.gc.ca/eic/site/cprp-gepmc.nsf/eng/home

- (b) In the case of an investment that is subject to the notification procedure, if it is in a “cultural business,” the notice may trigger a government decision to require a review/approval procedure. Thus, the investment will be assessed for its net benefit to Canada. Notifiable investments in non-cultural businesses – obviously the vast majority of businesses – are not assessed for their net benefit to Canada.
- (c) As of March 2009, all investments are assessed to determine if they could be injurious to national security.

14. In the following, we describe the procedures and screening activities in more detail. We will defer any discussion of national security screening, as that topic will be addressed below at Section F.

Which Investments are Caught by the ICA?

15. Subject to certain exemptions, the ICA applies to investments by non-Canadians to establish a new Canadian business or to acquire control of an existing Canadian business.⁸ Although this sounds like a simple and straight-forward statement, the reality is quite different. The ICA contains exclusions, presumptions, exceptions and a host of definitions that must be digested. Moreover, because the ICA has grown over the years as new concepts have been added and modified, the organization of the statute is frankly confusing. In the following paragraphs, we will describe the most important concepts in determining what is caught by the ICA.

16. The ICA sets out an extensive list of activities that are exempt from the operation of the statute. Some are predictable and others are not. The exemptions include, among others, an ordinary course acquisition of voting shares by a trader in securities, an acquisition in the course of realizing on security for a loan, and a corporate reorganization where the ultimate control does not change.⁹ The latter could, and probably should, be the subject of much elaboration, but unfortunately is only addressed in a few words. Exempt transactions, of course, do not incur any review or notice obligations.

17. A “non-Canadian” is unsurprisingly defined to be: “not a Canadian.” A “Canadian” means an entity that is “Canadian-controlled.”¹⁰ The ICA sets out a number of tests and

⁸ ICA, s. 11

⁹ ICA, s. 10

¹⁰ ICA, s. 3. A definition of “Canadian” individuals is also provided.

presumptions for determining Canadian-controlled status.¹¹ For example, an entity will be Canadian-controlled where Canadians own a majority of the voting interests in the entity.

18. A “Canadian business” is defined as a business carried on in Canada that has a place of business in Canada, individuals in Canada that are employed in connection with the business, and assets in Canada used to carry on the business.¹² A Canadian business does not lose that status simply because it is partly carried on in another country.¹³ That said, the business must satisfy the four Canada-focused criteria to be caught by the ICA. Further, a part of a business will be considered to be a Canadian business if it is capable of being carried on as a separate business.¹⁴

19. The term “business” is also defined in the ICA and means any undertaking capable of generating profit and being carried on in anticipation of profit.¹⁵ The business must therefore be actively earning revenues or be in a position to produce revenues from the sale of goods or services.¹⁶ Mere assets will not necessarily constitute a business for ICA purposes. The boundary can sometimes be tricky to assess; for example an undeveloped oil, gas and mineral property is generally not considered to be a business, but a drilled or developed property generally is considered to be a business.¹⁷ A Canadian-based head office (even if the commercial activities of the entity occur outside of Canada) is generally considered to be a “business” in Canada.

20. The phrase “new Canadian business” is also defined in the ICA.¹⁸ As one would intuitively expect, a new Canadian business is one that is unrelated to an existing business carried on in Canada by the non-Canadian.¹⁹ However, a more stringent requirement applies in the cultural business sphere.²⁰ In that case, a new Canadian business is defined to include a business activity that is related to an existing business, but where the new business activity is cultural in nature. Thus, a non-Canadian that operated a dental technician training college in

¹¹ ICA, s. 26 and 27

¹² ICA, s. 3

¹³ ICA, s. 31(1)

¹⁴ ICA, s. 31(2) and Interpretation Note No. 2

¹⁵ ICA, s. 3

¹⁶ Interpretation Note No. 4

¹⁷ *Ibid*

¹⁸ ICA, s. 3

¹⁹ The government has issued Related-Business Guidelines to assist in determining if a new business is related to an existing business. See www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00064.html#admin

²⁰ ICA, s. 15(a) and Regulations s. 8 and Schedule IV

Canada would likely be found to have established a new Canadian business by beginning to publish and sell books or videos on the dental technician topics that are taught at the college.

21. The phrase “to acquire control of a Canadian business” leads to what can be the most complicated analysis under the ICA. A non-Canadian can acquire control by acquiring voting shares or assets or by the acquisition of an entity that either carries on or controls an entity carrying on a Canadian business.²¹ For corporations, the acquisition of a majority of the voting shares is deemed to be the acquisition of control, and the acquisition of one-third or more of the voting shares is presumed to be the acquisition of control, although this can be rebutted by control-in fact evidence. For an entity that is not a corporation, the acquisition of a majority of the ownership interests is deemed to be the acquisition of control. Notwithstanding these deeming and presumption provisions, in the case of cultural industries, the Minister can look at control in fact evidence and make a determination that an acquisition of control has taken place.²²

Which Procedure Applies: Notification or Review?

22. After determining that the ICA applies to an investment, the next step is to figure out the procedure that will be followed to screen the transaction. As noted earlier, new investments and small acquisitions require the filing of a notification, whereas larger acquisitions (and acquisitions of cultural businesses) require a more onerous review procedure. In order to determine whether a review is required, one must examine the size of investment, whether the investor or the vendor is controlled in one or more countries that are members of the World Trade Organization (“WTO”), whether the acquisition is direct or indirect, and whether the target is a cultural industry. For an acquisition, the thresholds for review can be summarized as follows:²³

²¹ ICA, s. 28

²² ICA, s. 28(4). The Minister can make such a determination retroactively. See s. 28(6).

²³ ICA, s. 14 and s. 14.1

Type of Acquisition	WTO purchaser or vendor (Target is not a Cultural Business)	Non-WTO purchaser and vendor OR Target is a Cultural Business ²⁴
Direct	C\$299 million value of target's assets (soon to change; see below)	C\$5 million value of target's assets
Indirect (acquisition of control of a corporation outside Canada that controls an entity carrying on a Canadian business)	N/A (but is notifiable)	C\$50 million value of target's assets, EXCEPT C\$5 million value of target's assets if Canadian assets are >50% of all assets being acquired

23. This table does not tell the whole story, however. In the case of a new investment or acquisition where the target is a cultural business, the Minister can require a review if he sends a notice to the investing non-Canadian within 21 days of the ICA notification being filed.²⁵

24. The most important review threshold is the C\$299 million value of target's assets figure for acquisitions where either the purchaser or vendor is non-Canadian from a WTO country. This is the threshold that is relevant most frequently in circumstances where a review is necessary. On a date still to be fixed, this figure will increase significantly to C\$600 million, rising to C\$800 million and then C\$1 billion over the next six years. Thereafter it will increase pursuant to a formula that is geared to the growth of the Canadian economy. Moreover, for targets that are public companies, the basis of the calculation will move from value of assets to enterprise value. These changes are expected to be set out in regulations that are under development.²⁶

25. The calculation of the value of assets for the purpose of the ICA review thresholds is set out in the *Investment Canada Regulations* ("ICR").²⁷ The approach is to take the value shown on the audited financial statements for the latest financial year, although unaudited statements can

²⁴ See ICA, s. 14.1(5) which carves out an exception for the higher WTO investor threshold in the case where the target is a cultural business.

²⁵ ICA, s. 13(2)

²⁶ See www.gazette.gc.ca/rp-pr/p1/2009/2009-07-11/html/reg2-eng.html

²⁷ SOR/85-611

be used where audited statements are unavailable. The ICR also set out the information that must be submitted in a notification or a review application.²⁸

Notification Process

26. A notification contains a modest amount of information and can be filed before or up to 30 days following the implementation of the investment.²⁹ Following receipt of the notice, the Ministry assesses it for completeness and issues a receipt. If the Ministry decides that a review is warranted, the investor will be so advised. Eventually, basic details identifying the investor, the target and the nature of the target's business will be disclosed on the Ministry's website.³⁰

Review Process

27. A review application is a much more detailed document than a notification, and requires much care in its preparation. Of particular importance is the need to set forth the investor's plans for the business, including plans related to employment, participation of Canadians in the business, and capital investment.³¹

28. Most review applications are examined by the Investment Review Division ("IRD") of the Ministry of Industry (Industry Canada). Where cultural industries are involved, however, the review is conducted by the Cultural Sector Investment Review Office ("CSIR") of the Ministry of Canadian Heritage (Heritage Canada). Both departments will be involved where the target conducts cultural and other businesses.³²

29. The purpose of a review is to satisfy the relevant Minister that the investment "is likely to be of net benefit to Canada." The ICA requires that the review be completed within 45 days, although the Minister can unilaterally extend this by an additional 30 days.³³ As will be discussed below, these time periods can be further extended if national security issues surface. As well, the investor and the government can agree to extend the review period, and this does happen regularly.

²⁸ See Schedules I, II and III to the ICR.

²⁹ ICA, s. 12. That said, the proposed new regulations will increase the information that must be submitted.

³⁰ See www.ic.gc.ca/eic/site/ica-lic.nsf/eng/h_lk00014.html

³¹ ICR, Schedule II, s. 15

³² For more information on dual filing requirements, see www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00052.html

³³ ICA, s. 21-22

30. During the review period, the government officials consider the application and the net benefit submissions by the foreign investor. Other federal government departments and affected provincial governments will be consulted. Very commonly, the applicant will be asked to submit written undertakings in support of these submissions, for instance, as to employment levels and location of important offices and facilities. This can lead to intensive negotiations between the applicant and the government. When finalized, these undertakings are legally enforceable by the government.³⁴

31. Undertakings typically last for three years although they can be longer. During that period, the government can ask for status reports;³⁵ this is usually done at the 18 month mark. Where market conditions change such that the investor cannot reasonably be expected to abide by the undertakings, the government will sometimes negotiate amendments, although there is no legal requirement for the government to do so.

32. ICA reviews involving cultural businesses will take into account government policies that limit investment by non-Canadians in such businesses. These policies apply to the publication, distribution or sale of books, magazines and periodicals, and the production, distribution, sale or exhibition of film or video products or audio or video music recordings.³⁶ As a practical matter, a non-Canadian investor will find it difficult to obtain ICA clearance to acquire or establish a Canadian business in a number of these sectors. In other cultural businesses as well, and notwithstanding the lack of a particular sector policy, a non-Canadian investor will often find it a challenge to gain ICA clearance. The Ministry has issued guidelines with respect to the types of issues and undertakings that applicants should be prepared to address during the review process.³⁷

33. When an investment is finally approved, the investor is informed and basic details identifying the investor, the target and the nature of the target's business will be disclosed on the Ministry's website.³⁸

³⁴ ICA, s. 39(1)(e)

³⁵ ICA, s. 25

³⁶ See the Ministry of Canadian Heritage website at www.pch.gc.ca/pc-ch/org/sectr/ac-ca/eiic-csir/index-eng.cfm

³⁷ See www.pch.gc.ca/pc-ch/org/sectr/ac-ca/eiic-csir/net-eng.cfm

³⁸ See www.ic.gc.ca/eic/site/ica-lic.nsf/eng/h_1k00014.html

D. Working with the ICA

34. It is never too early to consider the ICA implications of a proposed investment. As soon as a non-Canadian investor, or a Canadian target, believes that a transaction is possible, all regulatory implications should be considered in order to assess potential issues, timing and structuring implications, as well as government and public relations strategies.

35. Where a notification is to be filed, the process is straight-forward and very unlikely to be controversial. Where, however, a review is anticipated, the parties should be prepared for a potentially onerous and time consuming process. In this section we offer our observations on the practical aspects of working with the ICA in such circumstances.

First Steps

36. Notify the officials: Early in the evolution of a reviewable transaction, and certainly if a public announcement has been made, it is commonplace to make a courtesy call to the agency that administers the ICA in order to advise them of the proposed transaction.³⁹

37. Begin collecting information: The information that is required and desirable to make a proper application for review is typically voluminous and complex. For example, the investor is required to submit a reasonably detailed business plan for the Canadian business. The collection and preparation of this information can be onerous and investors usually underestimate the effort and time required. Because it can sometimes take months to prepare the application, it is critical to begin the process of collecting the required information at a very early point.

38. Consider what additional advisers are appropriate: In most cases the investor will have legal and financial advisers engaged in respect of a proposed transaction. However, in some complex or sensitive cases, the talent and experience of public relations and government relations experts are invaluable. Careful consideration should be given, as soon as possible, to engaging experts whose “soft touch” can make the processing of a file much smoother for both investor and government alike.

³⁹ This is usually the IRD, but may also be the CSIR.

Preparing the Application for Review

39. The preparation of the application for review (hereafter referred to as the “Application for Review,” which includes the application form stipulated by government) typically focuses on four main components: (i) collection of data that is specifically required for the application form; (ii) collection of “supplementary” information; (iii) preparation of the plans for the Canadian business; and (iv) in most cases, preparation of a submission that outlines why the proposed investment is likely to be of net benefit to Canada.

40. Application Form: Set out in Appendix I to this paper is the list of information that is required to be submitted pursuant to the requirements of the application form, and a brief comment on the most notable information requirements.⁴⁰

41. Supplementary Information: Attached as Appendix II to this paper is an extract from the IRD website that sets out supplementary information that the officials strongly suggest be submitted with the Application for Review form.⁴¹ The investor is encouraged to provide as much of the requested supplementary information as is reasonably possible in order to avoid later delays in the process when the government officials inevitably ask for this information to complete their file.

42. Plans: Without a doubt, the most important element of any Application for Review is the articulation of the investor’s plans for the target following the acquisition. These plans are the key source of information on which the Minister assesses whether the proposed investment is likely to be of net benefit to Canada. Furthermore, the plans are the primary input for the development of the undertakings that the investor is usually required to provide in order to secure ICA approval. The Application for Review form requests the following:

20. Detailed description of the investor’s plans for the Canadian business with specific reference to

⁴⁰ For the purposes of this paper it is assumed that the draft regulations that will update and expand the Application for Review requirements have come into force as proposed. See Schedule II of the proposed *Regulations Amending the Investment Canada Regulations*, C. Gaz. 2009.I.2064. See www.gazette.gc.ca/rp-pr/p1/2009/2009-07-11/html/reg2-eng.html

⁴¹ See www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00076.html

(a) *the relevant factors set out in section 20 of the Act;*⁴² and

(b) *the current operations of the Canadian business.*

43. The Application for Review form prepared by the officials and available on its website⁴³ adds the following language in the form under the “plans” section:

The following list suggests a number of subjects you may wish to elaborate on, if they are relevant. Please note that it is simply a general guide and does not represent a list of obligatory subjects to be covered.

- *Employment (number and type of jobs created or lost)*
- *Additional investment (increased working capital provisions, expansion)*
- *Resource processing (value added, extent of processing)*
- *Utilization of parts, components and services (requirements of the Canadian business and opportunity for Canadian suppliers to compete in supplying them)*
- *Exports (percentage of exports compared to total sales, markets served, types of products or services exported)*
- *Canadian participation (number of Canadians as employees, managers, directors and owners)*
- *Productivity/efficiency (new or expanded plant, new equipment rationalization of activities, training)*
- *Technological development (nature of R&D, R&D expenditures and timing, R&D facility, R&D contract in Canada, use and terms and conditions to use licenses, patents, etc.)*
- *Product innovation/variety (different or complementary product lines, state-of-the-art products)*
- *International competitiveness (world product mandate, access to international distribution networks)*

The most frequent cause of delays in the review of applications is the lack of adequate information on the applicant's plans for the Canadian business. Applicants should

⁴² The factors set out in ICA, s. 20 are as follows:

(a) the effect of the investment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada and on exports from Canada;

(b) the degree and significance of participation by Canadians in the Canadian business or new Canadian business and in any industry or industries in Canada of which the Canadian business or new Canadian business forms or would form a part;

(c) the effect of the investment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;

(d) the effect of the investment on competition within any industry or industries in Canada;

(e) the compatibility of the investment with national industrial, economic and cultural policies, taking into consideration industrial, economic and cultural policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the investment; and

(f) the contribution of the investment to Canada's ability to compete in world markets.

⁴³ See <http://www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00063.html>

describe their plans in sufficient detail to enable the reviewing officer to obtain a clear understanding of their intentions. It is also helpful for applicants to provide three-year projections for the Canadian business for employment, sales, exports, capital expenditures and research and development expenditures, where relevant.

44. Preparation of proper and appropriate plans for purposes of the Application for Review can be quite challenging. In some cases the investor has already prepared a detailed business plan that addresses many of the points identified above and can be used as the basis for the plans that are attached to the application. However, it is often the case that detailed plans do not exist, much less plans that detail employment and expenditure projections over the following three or so years.

45. How long and detailed should the plans be? This is commonly the first question asked by a foreign investor but there is no easy answer. At the risk of being too general, it has been our experience that plans that focus on Canada and tackle about a dozen major elements of the business with reasonable detail and robust projections will likely be sufficient for the application to be certified complete and to allow the Minister to assess the investment. To the extent that the officials require more detailed plans, they will ask the investor for the appropriate elaborations.

46. Written Submission: It is also advisable to prepare a submission that accompanies the Application for Review. Often this consists of a written advocacy piece that highlights the elements of the transaction that are beneficial to Canada. In some cases it may also be appropriate to prepare a presentation for use by the investor's legal counsel together with a representative of the investor (and sometimes the Canadian business), when meeting with the officials to describe the transaction and its benefits.

The Review Process

47. As discussed above, once the Application for Review has been filed, the Minister has 45 days to consider the application. The Minister can, unilaterally, extend this period by another 30 days. Thereafter, the review period can only be extended by mutual consent of the Minister and the investor. During the review period there are usually four key stages that occur, and these are further discussed below:

- (i) intergovernmental consultation;

- (ii) provision of additional information to the government representatives;
- (iii) negotiating the content and scope of written undertakings to be given to the government, if any; and
- (iv) the formal Ministerial approval process.

48. Intergovernmental consultation: It is our understanding that once the Application for Review has been received by the officials and certified as complete, a request is made of each provincial or territorial jurisdiction that is impacted by the transaction for feedback on the proposed transaction. As part of this request, some or all of the Application for Review is provided to the provincial and territorial officials. Depending on the nature of the proposed investment, the officials will also interact with other federal government departments, as well as federal and provincial agencies.⁴⁴

49. Additional Information Requests: It is not unusual for the government to seek additional information in respect of the transaction. These requests for additional information can be made in writing or orally. Depending on the nature, size and complexity of the transaction, it may be advisable not only to respond to the information requests in writing, but also to meet with the officials in Ottawa.

50. Undertakings: A written undertaking is a promise made by the investor to the Minister for a stipulated period (typically three years, but it can be longer) to fulfill certain obligations. As discussed above, the Minister will only approve the acquisition of control of a Canadian business if he or she is satisfied that the transaction is likely to be of net benefit to Canada. Increasingly, over the past 10 years or so, the Minister has insisted on written undertakings to support a positive net benefit finding. The larger, or more sensitive, a transaction is, the more likely it is that undertakings will be required. Note, however, that many transactions are approved under the ICA without the investor having to submit written undertakings.

51. To the extent that the foreign investor expects undertakings will be required in support of a proposed transaction, this eventuality should be managed early on in the ICA process. The content and scope of the undertakings are typically based on the business plans. Although each transaction is different, undertakings often focus on Canadian employment levels, Canadian

⁴⁴ There may also be consultation with members of the security and intelligence community.

participation in management, Canadian capital expenditure levels, Canadian R&D commitments and the use of Canadian suppliers and businesses. Undertakings normally run for three years, although in special cases they can extend for five years or even longer.

52. The Canadian government typically accepts (and allows a caveat in the undertaking document) that where the investor is unable to fulfill an undertaking due to factors beyond its control, this will be taken into account in the monitoring of the undertakings.

53. Formal Ministerial Approval Process: Once the IRD or the CSIR is in a position to recommend an investment, a report, together with the undertaking agreement is sent to the Minister for consideration. The Minister, if he or she accepts the recommendation, will then approve the transaction. Where the Minister requires further information or is dissatisfied with any aspect of the proposed investment, the matter may be referred back to the IRD or the CSIR for further consideration.

54. Alternatively, the Minister may reject the approval and issue a notice that the transaction is not approved. In such a case, the investor has an additional 30 days to make further submissions or provide additional undertakings in the hope of securing approval.

55. Rejections of investments are rare. Indeed, in recent years, the Minister has disapproved only one transaction, although there have been rumors that other transactions were abandoned when it became clear that ICA approval would not be obtained. On May 8, 2008, the Minister of Industry decided that the over one billion dollar sale of Macdonald, Dettwiler and Associates Ltd. to US-based Alliant Techsystems Inc. was not likely to be of net benefit to Canada.⁴⁵ Although no formal reasons were given, many believe that the government was concerned about the loss of Canadian control over satellite technology (developed with government financial support) that could be used for surveillance of Canada's northern territory. It should be noted too that the national security review process introduced in March 2009, which provides the government with formal powers to prohibit or unwind foreign investments on the basis of national security concerns, has been invoked at least once already.

⁴⁵ See www.ic.gc.ca/eic/site/ic1.nsf/eng/04219.html

Confidentiality

56. Section 36 of the ICA provides that information obtained by the Minister is privileged and no one shall knowingly communicate or allow to be communicated any such information. These confidentiality protections are subject to certain exceptions, including information contained in any written undertaking given to the government (even though the undertaking may contain quite sensitive information).⁴⁶

57. Despite the government's right to disclose certain information, it has been government policy not to exercise the right of disclosure without investor consent. It is therefore common for the investor and the government to negotiate and agree on what information can be made public. The Minister has a desire to communicate to the public the outcome of a review and the basis for his or her conclusions, whereas the investor typically has an interest in keeping most of the information confidential. Usually the officials and the Minister are amenable to striking a compromise that balances the interests of both sides. It is not unusual for the scope and content of press releases and speaking notes to be discussed and reviewed in advance.

E. State Owned Enterprises

58. One area of focus for the government has been foreign investment by state-owned enterprises ("SOE"), which are enterprises that are controlled directly or indirectly by foreign governments. A 2006 government study, *Advantage Canada: Building a Strong Economy for Canadians*,⁴⁷ identified the concern that some foreign investments by SOEs with non-commercial objectives and unclear corporate governance and reporting may not benefit Canada, and it called for a principled approach in dealing with this concern. The government then issued SOE guidelines (the "Guidelines") in December 2007 to clarify how investments by SOEs would be addressed.⁴⁸

59. Although the same ICA principles apply to these transactions, the Guidelines make it clear that when assessing net benefit to Canada, the Minister will examine the corporate governance and reporting structure of the SOE. This examination will evaluate whether the non-

⁴⁶ ICA, s. 36(4)(b)

⁴⁷ Available online: Department of Finance, <http://www.fin.gc.ca/ec2006/pdf/plane.pdf>

⁴⁸ Industry Canada, Guidelines "Investment by state-owned enterprises - Net benefit assessment" (December 7, 2007), available online: <http://www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00064.html>

Canadian adheres to Canadian standards of corporate governance such as commitments to transparency and disclosure, independent members of the board of directors, independent audit committees and equitable treatment of shareholders, and to Canadian laws and practices. The examination also looks at how and the extent to which the non-Canadian is owned or controlled by a state.

60. The Guidelines indicate that the Minister will assess whether the Canadian business being acquired will continue to be able to operate on a commercial basis with respect to indicia such as where exports go, where processing takes place, the participation of Canadians in operations, and the capital expenditures to maintain the Canadian business. A SOE should therefore anticipate that it will be required to provide undertakings beyond those normally expected of a privately owned company. Indeed, the Guidelines go on to suggest undertakings that SOEs may offer to demonstrate net benefit, including the appointment of Canadians to boards of directors, employing Canadians in senior management positions, incorporation of a company in Canada, or a listing of shares on a Canadian stock exchange.

61. Recent examples of investments by SOEs that have received approval include PetroChina Co. Ltd.'s purchase of the majority interest in two oil sands assets controlled by Athabasca Oil Sands Corp. for \$1.9 billion,⁴⁹ Korea National Oil Corp.'s acquisition of Harvest Energy Trust,⁵⁰ and China Petroleum & Chemical Corp., or Sinopec's, acquisition of ConocoPhillips Co.'s minority stake in Syncrude Canada Ltd.⁵¹

F. The Recent Add-on for National Security Screening

62. In March 2009, Parliament amended the ICA to give the federal government the power to vet investments by non-Canadians on national security grounds.⁵² Canada joins countries including the United States, Australia and Germany in having explicit procedures to review, adjust, and if necessary, reject, foreign investments that are perceived to be injurious to national security.

⁴⁹ See http://www.aosc.com/upload/media_element/24/01/joint-venture-transaction-closes.pdf

⁵⁰ See http://cnrp.marketwire.com/cnrp_files/20091222-1222hte.pdf

⁵¹ See <http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/sinopec-free-to-buy-into-syncrude/article1618216/>

⁵² ICA, Part IV.1

63. The scope of the review is potentially very broad. There is no minimum investment threshold. A review can be undertaken for a takeover of or minority investment in an existing business or the start-up of a new business. To date, there is no list of sensitive sectors where a review is more likely; nor is there a formal procedure as in the US under CFIUS to “voluntarily pre-clear” potentially sensitive transactions, although pre-clearance is possible for acquisitions of control if proper notice thereof is made to the Minister of Industry prior to the implementation of the investment.

64. The criteria for evaluating a particular transaction are quite vague: the government need only be satisfied that it has “reasonable grounds to believe that an investment by a non-Canadian could be injurious to national security.” The terms “injurious” and “national security” are not defined.

65. Moreover, the remedies are very broad. The government can block a pending transaction or allow it to proceed subject to conditions. It can also order divestitures for completed transactions.

66. The entry point for national security screening will, in most cases, be the notification and review processes under the ICA. Under new regulations,⁵³ the Minister will have to initiate action (a) for a reviewable matter, up until 45 days after the review application is certified as complete, (b) for a notifiable matter, up until 45 days after certification of the notice, and (c) in all other cases, up until 45 days after the investment is implemented. A prudent investor would therefore typically not implement an investment until 50 days or so after the initial notice or application⁵⁴.

67. The Minister initiates a national security review by sending notice to the non-Canadian investor. The Minister can, and likely will, also send a request for information. Following this preliminary procedure, the Minister can either terminate screening or issue another notice, this time ordering a full national security review of the investment. The national security review

⁵³ *National Security Review of Investments Regulations*, SOR/2009-271 (“NSRIR”)

⁵⁴ Because in at least one case (see subsection 25.3(2)) the investor may only become aware of an order for review after it has been made (because the Minister’s obligation to give notice thereof only arises after the order has been made on a “without delay” basis), it is prudent in our view to wait at least five days after the expiration of the 45 day period before consummating the transaction.

process can take up to 130 days from the initial notice (or longer if the investor agrees to an extension)⁵⁵.

68. Again, the Minister can demand information from the non-Canadian or any other person involved. The investor will also be given the opportunity to make representations to the Minister. The Minister digests the information, consults the Minister of Public Safety and Emergency Preparedness and other agencies and then sends a report to the Governor in Council (*i.e.* the federal cabinet) with recommendations. The cabinet then makes a decision and issues an order that can block the investment, authorize the investment on conditions, or require divestiture (in the case of a completed investment).

69. As noted earlier, once the national security screening process begins, the deadlines for Ministerial decision-making in an ICA “net benefit” review are postponed.⁵⁶ Thus, the two procedures become, in effect, merged and will presumably lead to a synchronized outcome.

70. To provide some greater degree of predictability to potential investors and their targets, note that both the US and Australia (but not Canada) have provided guidance on the types of transactions that are more prone to national security attention; this guidance can likely be a useful starting point for Canadian assessments as well. What follows is a non-official amalgam of this guidance but omitting sectors that are not likely to be a concern in Canada (for example, where Canadian ownership and control rules apply, such as in the broadcasting, telecommunications and airline industries):

- Target companies involved in government contracting such as military, law enforcement, telecommunications technology, aerospace, radar, information technology and classified work generally.
- Target companies in the transportation, energy, nuclear, uranium mining or advanced technology sectors or that sell export controlled products.
- Purchasers that are state-owned companies and where investment decisions are not clearly independent of government.

71. Although Canada does not yet have a pre-clearance procedure, it is inevitable that some sort of process will develop. The early acquisitions will likely clear a path through the federal bureaucracy that others will then follow.

⁵⁵ ICA, Part IV.1 and NSRIR

⁵⁶ ICA, s. 21

72. As mentioned above, national security concerns were expressed in connection with the proposed acquisition of Forsys Metals by George Forrest International (GFI). Forsys Metals is a Canada-based mineral exploration company with uranium projects in Namibia. In August 2009, GFI received notification from Industry Canada pursuant to the national security provisions of the ICA and that it was prohibited from implementing the investment pending further notice.

G. To Conclude

73. Although Canada has benefitted mightily from foreign investment, it retains a perhaps surprising degree of skepticism that foreign investment is always beneficial. In the 1970s this skepticism led to close monitoring of foreign investment, and commitments by investors to undertake government-mandated measures such as supporting R&D and maintaining specified employment levels. In the 1980s, the pendulum swung in the other direction: although foreign investment was still monitored, the welcome mat was more clearly in evidence. Now, a more nuanced approach to foreign investment seems to be at work. Most foreign investment is welcome, and consequently most transactions will encounter no opposition from the ICA process (although undertakings will be extracted from the investor). However, more often than before, the government seems willing to push back against investments that are contrary to evolving public policy, such as concerns about national security or foreign-state-owned investors, and against investors that fail to live up to their commitments, even if this blemishes Canada's investment-friendly reputation. An interesting situation that may provide a gauge of the government's current approach to foreign investment is the developing battle for Potash Corporation of Saskatchewan (PotashCorp). While the PotashCorp's board has, at least initially, rejected BHP Billiton's August 2010 takeover bid, rumblings by potential investors such as China's state-owned Sinochem Corp. are likely attracting the attention of the Canadian government.⁵⁷

74. As attitudes to foreign investment have evolved, so has the ICA. An already complex statute has become lengthier and more complicated. The process of compliance has become more time-consuming and more expensive, even as the percentage of transactions that are subject to the onerous review process is decreased. An understanding of the legal framework and the

⁵⁷ See <http://business.financialpost.com/2010/09/09/chinese-play-for-potash-corp-will-force-canadas-hand-dundee/>

workings of the statute is an essential component of every acquisition or start-up involving foreign investors – which equates to a large proportion of investment transactions that Canadian lawyers will encounter. It is with this in mind that we have prepared this paper and its description of the key elements of ICA law and practice.

APPENDIX I – APPLICATION FOR REVIEW FORM

Set out below is a brief discussion of the requirements of the Application for Review form⁵⁸ (other than the plans).

1. *Name of the investor.* This usually consists of the legal entity making the acquisition.
2. *Names of the members of the investor's board of directors, the investor's five highest paid officers and any person or entity that owns 10% or more of the investor's equity or voting rights.* A key point to remember in addressing this question is the difference between the "investor" and any "parent" company. The directors and the five highest paid officers of the investor may be quite different from its parent company or an operating affiliate. Also, only direct holders of 10% or more in the investor should be identified (on the basis that the form, in questions 5 and 6 below, identify which indirect holders of an interest in the investor need to be identified).
3. *The mailing address, telephone number, fax number and e-mail address of the investor and any person or entity mentioned in item 2 and, in the case of an individual, their date of birth.* Self-explanatory.
4. *Whether the investor is a WTO investor or a NAFTA investor.* See section 14.1 of the ICA.
5. *Name and address of the ultimate controller of the investor, if any, and the manner in which control is exercised.* This is the requirement to provide the identity of an indirect parent that controls the investor if such control is not exercised directly.
6. *Whether a foreign state has a direct or indirect ownership interest in the investor and, if so, the name of the state.* Note that there does not appear to be a *de minimis* ownership level in respect of this question, which could make obtaining and providing such information cumbersome.
7. *Annual reports or, if not available, financial statements of the investor for the three fiscal years immediately preceding the implementation of the investment.* Self-explanatory.
8. *Description of the business activities carried on by the investor and by its ultimate controller, if any.* Self-explanatory.

Investment

9. *Name of the vendor and name of its ultimate controller, if any.* Self-explanatory.
10. *Copy of purchase and sale agreement or, if not available, an outline of the principal terms and conditions including the estimated total purchase price for the Canadian business and, if applicable, the estimated purchase price for all entities acquired.* Self-explanatory.

⁵⁸ These requirements are taken from the draft regulations that will update and expand the current Application for Review requirements and are expected to come into force imminently. The assumption is made that these requirements will come into force in their current form. See Schedule II of the *Regulations Amending the Investment Canada Regulations*, C. Gaz. 2009.I.2064 available at www.gazette.gc.ca/rp-pr/p1/2009/2009-07-11/html/reg2-eng.html

11. The sources of funding for the investment. The level of detail required here is unclear. As a general rule it probably is appropriate to identify major sources of funding and provide the identity of the financiers (as this question is likely geared to help the government identify national security concerns).

12. Date of implementation of investment. While this is self-explanatory, it may be appropriate to simply say “shortly after approval under the Investment Canada Act.”

Canadian Business

13. Name of the Canadian business. Self-explanatory.

14. Business or mailing address of the Canadian business. Self-explanatory.

15. Annual reports or, if not available, financial statements for the Canadian business for the three fiscal years immediately preceding the implementation of the investment. Self-explanatory.

16. Description of the business activities that are carried on by the Canadian business, including

(a) the locations in Canada where the business is being carried on; Self-explanatory.

(b) the business activities carried on at each location; Self-explanatory.

(c) the number of employees at each location; and Self-explanatory.

(d) the products and services that are or will be manufactured, sold or exported by the Canadian business and the code assigned to the products and services by the North American Industry Classification System (NAICS 2007) – Canada, 2007, published by authority of the Minister responsible for Statistics Canada. The NAICS 2007 codes can be found at www.statcan.gc.ca/subjects-sujets/standard-norme/naics-scian/2007/list-liste-eng.htm. What is not clear is whether the more general three digit code is sufficient for purposes of responding to this question, or whether the most precise code (up to six digits) is required for purposes of providing this information.

17. If the investor is not a WTO investor or a NAFTA investor, whether the Canadian business is, immediately before the implementation of the investment, controlled by a WTO investor or controlled by a NAFTA investor. Self-explanatory.

Assets

18. In the case of an investment referred to in section 14 of the Act or an investment referred to in section 14.1 of the Act and section 3.3 of these Regulations,

(a) if only the assets used in carrying on a Canadian business are acquired or if only control of an entity that carries on a Canadian business is acquired, the value of the aggregate of all assets acquired or of all assets of the entity that carries on the Canadian business, calculated in the manner described in section 3.1 of these Regulations; and

These information requirements can be confusing. Generally this section 18(a) will apply to transactions that are asset acquisitions, or where the entity only carries on business in Canada and is a private company.

(b) if control of an entity that carries on a Canadian business and control of one or more other entities is acquired, directly or indirectly, the value — calculated in the manner described in section 3.1 of these Regulations — of the aggregate of

(i) all assets of the entity carrying on the Canadian business and of all other entities in Canada the control of which is acquired, directly or indirectly; and

(ii) if control of a corporation incorporated elsewhere than in Canada is acquired, directly or indirectly, all assets of all entities both inside Canada and outside Canada the control of which is acquired in the same transaction.

Section 18(b) applies to the acquisition of private companies where the business is carried on in and outside of Canada. The question seeks to determine the value of the assets in Canada and the value of all assets acquired (including the Canadian assets).

19. In the case of an investment referred to in section 14.1 of the Act and section 3.2 of these Regulations, the market capitalization of the acquired entity calculated in the manner described in paragraph 3.2(2)(a) of these Regulations, its liabilities calculated in the manner described in paragraph 3.2(2)(b) of these Regulations and its cash and cash equivalents calculated in the manner described in 3.2(2)(c) of these Regulations.

Section 19 applies to the case of the acquisition of a public company.

APPENDIX II – SUPPLEMENTARY INFORMATION

Investment Canada Act*

Additional info

Suggested Supplementary Information

Application for Review under the *Investment Canada Act*

The Application for Review form on the Investment Review Division's website provides a list of suggested subjects that applicants are encouraged to elaborate on, where relevant, in order to assist staff in the assessment of the application. The list on the website refers to:

- Employment (number and type of jobs created or lost).
- Additional investment (increased working capital provisions, expansion).
- Resource processing (value added, extent of processing).
- Utilization of parts, components and services (requirements of the Canadian business and opportunity for Canadian suppliers to compete in supplying them).
- Exports (percentage of exports compared to total sales, markets served, types of products or services exported).
- Canadian participation (number of Canadians as employees, managers, directors and owners).
- Productivity/efficiency (new or expanded plant, new equipment rationalization of activities, training).
- Technological development (nature of R&D, R&D expenditures and timing, R&D facility, R&D contract in Canada, use and terms and conditions to use licences, patents, etc.).
- Product innovation/variety (different or complementary product lines, state-of-the-art products).
- International competitiveness (world product mandate, access to international distribution networks).
- Three year projections for: employment, sales, exports, capital expenditures and R&D expenditures.

In addition, the following would also be helpful, where relevant:

- Other Regulatory Bodies and Dates (indication of whether any other regulatory authorities are reviewing this transaction; dates on which filings were made and the expected expiry of any waiting period or expected date of issuance of a decision).

- Expected dates of any major events required to bring about the completion of the transaction, and the scheduled closing date of the transaction.
- Consideration (where the acquisition of a Canadian business is part of a larger transaction, allocation of total consideration to the Canadian business).
- Business Objective/Rationale (business rationale for the proposed transaction).
- Corporate chart(s) (corporate organization chart for both the investor (Canadian operations only) and the Canadian business being acquired as they are currently structured; corporate organization structure post-acquisition) The chart should describe the relationship between the parties and their affiliates.
- Management Organization chart and Functions (current management structure and functions of both the investor (Canadian operations only) and the Canadian business being acquired; post-acquisition management structure and functions of the Canadian operations).
- Benchmarks, examples (specific examples and benchmarks to support the net benefit argument, e.g. for efficiencies, productions, exports, R&D, capital expenditures, new technologies, etc.).
- The stock exchanges on which the investor's stock is listed and traded.
- Any web site addresses which may contain information relevant to the assessment of the proposed transaction.
- Any other information which the applicant considers relevant, e.g. with respect to the Canadian business, a brief about the industry it is in, the markets it serves, trends, etc...

*taken from IRD's website at www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00076.html