



February 21, 2018

Via email: david.tkachuk@sen.parl.gc.ca

The Honourable David Tkachuk
Chair
Senate Committee on
Transportation and Communications

Dear Senator Tkachuk:

Re: Bill C-49, *Transportation Modernization Act* and Foreign Ownership

I am writing on behalf of the Canadian Bar Association's Air and Space Law Section (CBA Section) to comment on the proposed increase to foreign ownership limits of air carriers in Bill C-49, *Transportation Modernization Act*.

The Canadian Bar Association is a national association of approximately 36,000 lawyers, Québec notaries, students and law teachers, with a mandate to promote improvements in the law and the administration of justice. The CBA Section comprises lawyers from across Canada who represent aircraft operators and financiers, aerospace companies, airports and aerodromes and equipment manufacturers.

Summary

We understand that the government's objective in increasing foreign ownership limits is to attract foreign investment, to encourage growth in the Canadian aviation sector and increase competition (aiming for more choice and reduced fares for consumers). A specific target of these measures could be Ultra Low Cost Carriers, which have been slow to enter the Canadian market. The CBA Section believes that the proposed amendments, namely the introduction of sub limits to foreign ownership, may not achieve the intended objective.

Canadian owned and controlled

Section 55(1) of the *Canada Transportation Act* defines "Canadian" as follows:

[...] a Canadian citizen or a permanent resident within the meaning of subsection 2(1) of the *Immigration and Refugee Protection Act*, a government in Canada or an agent of such a government or a corporation or other entity that is incorporated or formed under the laws of Canada or a province, that is **controlled in fact** by Canadians **and** of which at least 75%, or such lesser percentage as the Governor in Council may by regulation specify, of the voting interests are **owned and controlled** by Canadians. [emphasis added]

To qualify as “Canadian” and operate a domestic or international air service, foreign ownership and *control* in the corporation is limited to 25% of the voting interest.

With respect to control, an air carrier must establish to the satisfaction of the Canadian Transportation Agency that, in addition to control in law, *control in fact* of the air carrier does not lie in non-Canadian hands. This is often referred to as the *de facto* control test.

The Agency considers a long and varied list of factors to determine if an air carrier is “Canadian”, including amongst others ownership and voting structures, composition of management, affirmative and pre-emptive rights held by shareholders, operational structures, and assets.

The Bill amends the definition of “Canadian” by raising the foreign ownership and control limit to 49%, but introduces two sub limits:

- (i) no single non-Canadian may hold more than 25% of the voting interests, either individually, or in *affiliation* with another person in a Canadian air operator; and
- (ii) foreign air operators may not in the aggregate, hold more than 25% of the voting interests in a Canadian air operator.

The Bill does not remove the *de facto* control requirement.

Sub limits may reduce incentive to invest

In December 2015, the [Canada Transportation Act Review Report](#) (Report), a comprehensive statutory review of the *Act*, recommended increasing foreign ownership limits to 49%. It did not recommend any sub limits, i.e. the proposed 25% limit on individual foreign investors, or the 25% aggregate cap on foreign air carrier investors.

In our view, if the intent of the proposed amendments is to attract foreign capital to provide an economic stimulus to Canada’s aviation sector and increase consumer choice, the amendments as drafted may not meet that objective.

In our [submission](#) on the Report, we commented that increasing the foreign ownership limit to 49% may not, in itself, attract more foreign capital, given the *de facto* control requirement.

For the following reasons, the introduction of the sub limits may erode any stimulus that the liberalization of foreign investment limits may have generated.

1. Corporate law protections not available to foreign investors: Under Canadian, provincial and territorial corporate law statutes, blocking fundamental changes to a corporation requires the approval of at least 33 1/3 of shareholders. Limiting a single foreign investor to 25% ownership does not give enhanced shareholder protection to that investor. The only way non-Canadian financial investors could benefit from the enhanced shareholder protection would be to invest as a consortium or an unincorporated joint venture. We discuss the challenges with this below.
2. Foreign operational investors may not be interested: Some Canadian air carriers may seek foreign investment not only for financial reasons, but also to gain network connectivity, operational support and competitive access to support services. Limiting foreign air carrier investment to 25% may not help a Canadian air carrier looking for more than a pure cash injection. A sophisticated foreign air carrier investor may prefer a bigger ownership stake or more influence in the air carrier.

Sub limits do not enhance Canadian control requirements

As explained above, the definition of “Canadian” (in both the current *Canada Transportation Act* and the proposed amendments) imposes a limit on foreign ownership and also on control. The air carrier must establish that foreign ownership does not exceed 25% (or 49%), and also that a non-Canadian does not *control* more than 25% (or 49%) ownership interests in the air carrier.

Since the *de facto* control test remains in place and the Agency makes this determination after a detailed analysis to protect against undue foreign influence, the proposed sub limits on foreign ownership are of debatable value and may in fact be counterproductive to the amendments’ objective. It is difficult to see how the sub limits enhance Canadian control requirements.

Conclusion and Recommendations

The government’s objective in increasing foreign ownership limits – to attract foreign investment to encourage growth in the Canadian aviation sector and increase competition – may not be achieved by the proposed amendments in Bill C-49. To help the government achieve its goal, the CBA Section recommends:

- The proposed definition of “Canadian” should be reviewed. Consideration could be given to removing the proposed sub limits. Alternatively, the definition could remain unchanged, and the Governor in Council could prescribe levels of foreign ownership by regulation (permitted under the current Act).
- The proposed sub limit that caps foreign ownership by any individual to 25% should be clarified, including the extent to which *unaffiliated* entities can agree to cooperate, where that cooperation would not result in the exercise of control by foreign interests on the operation of the air carrier. For example, while a joint venture does not appear to fall within the definition of “affiliated” in the *Act*, would an arrangement where the voting shares are exercised in tandem undermine the proposed changes? The proposed language is vague and could lead to abuse or inhibit investment given the uncertainty.
- The Senate Committee should hear from experienced business professionals with a proven track record of investing in air transportation undertakings. These experts can offer their views on how the proposed changes to foreign ownership levels may impact the Canadian air transportation sector.

We trust that our comments are helpful. We would be pleased to discuss in greater detail or answer any questions that you may have.

Yours truly,

(original letter signed by Marc-André O’Rourke for Naomi Nind)

Naomi Nind,
Chair, CBA Air and Space Law Section