

Recent Developments in Foreign Investment Review

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Foreign Investment Review in Canada



- Principal legislation: Investment Canada Act ("ICA")
- Authorizes Canadian government to review certain investments by non-Canadians in Canadian businesses
- Two aspects to ICA review:
 - "net benefit" review
 - "national security" review
- Key current issue: investment by state-owned enterprises ("SOEs")

Net Benefit Review

- Applies to acquisitions of control of a Canadian Business by a non-Canadian
 - "Non-Canadian": ultimate control is outside Canada
 - "Control": deemed if > 50% of voting interests acquired; rebuttable presumption if between 33.3%-50% of shares acquired
- Review process:
 - Generally conducted pre-closing
 - Cannot close until approval received
 - Typically takes 45-105 days
 - Undertakings required
- Very limited number of (non-cultural) rejections on net benefit grounds
 - MacDonald Dettwiler
 - BHP/Potash

Net Benefit Review (cont'd)

- Current financial thresholds based on "book value" of assets
 - \$344 million for direct acquisitions by or from "WTO investors"/\$5 million for non-WTO investors
 - \$5 million for "cultural business"
 - No review for "indirect" acquisitions of Canadian business by or from WTO investors/review for non-WTO investors if asset value over \$50 million
- Recent amendments, once in force, will shift threshold from "book value" to "enterprise value" (subject to certain exceptions)
 - Definition of "enterprise value" still in draft form
 - Threshold for WTO investors will rise to \$600 million (and eventually to \$1 billion)

National Security Review

- National security review process enacted in 2009
- Allows government to review and block foreign investments that "could be injurious to national security"
 - "National security" is undefined
- All investments in a Canadian business by a non-Canadian, not just acquisitions of control, potentially caught
- Process can take up to 130 days:
 - Recent amendments (once regulations are prescribed) will enable Minister to extend review

National Security Review (cont'd)

- At least 4 transactions blocked or abandoned due to national security concerns since 2009:
 - Uranium deposits in Africa (investor with ties to Iran)
 - Software (investor with ties to China)
 - Mobile phones (investor with ties to Russia)
 - Telecom services (investors with ties to Russia/Egypt/North Korea)

National Security Review (cont'd)

- Most recent rejection on October 7, 2013 – proposed investment by Accelero Capital in Allstream
- Allstream operates national fibre optic network that provides telecom services to, *inter alia*, federal and other governments
- Investors in Accelero Capital are citizens of, or have business ties with, Egypt/Russia/North Korea
- Government did not provide details on why rejected transaction; investors allege caught by surprise
- Runs contrary to government objective of increasing foreign investment in telecom sector

State Owned Enterprises ("SOEs")

- Specific guidelines issued in 2007
 - SOEs must demonstrate adherence to Canadian laws and practices, including standards of corporate governance and transparency and ability to operate on a commercial basis
 - Potential undertakings include appointment of Canadians as independent directors/listing of shares on Canadian stock exchange

SOEs (cont'd)

- In December 2012, federal government approved two major foreign SOE acquisitions
 - (CNOOC) / Nexen Inc.
 - Petronas / Progress Energy
- Transactions served as impetus for government to modify SOE Guidelines and to introduce amendments to ICA

SOEs (cont'd)

- "SOE" now defined much more broadly and includes:
 - Entities that are merely influenced, directly or indirectly, by a foreign government or an agency of such a government
 - An individual acting under the direction or influence of a foreign government or an agency of such a government
- SOEs will remain subject to asset value threshold
- No further SOE investments in oil sands other than in "exceptional circumstances"
 - Other industries could be subject to similar cap on investment if circumstances warrant

SOEs (cont'd)

- 2013 amendments: Minister now has power to determine that
 - An entity is controlled in fact by an SOE
 - An otherwise Canadian-controlled entity is controlled in fact by one or more SOEs
 - There has been an acquisition of control in fact by an SOE

SOEs (cont'd)

- Key considerations:
 - Extent to which a foreign state is likely to exercise control or influence over SOE acquiring Canadian business
 - Degree of control or influence SOE will exert on Canadian business acquired and on the relevant industry
 - Impact on corporate governance and reporting structure of the Canadian business
 - Whether the Canadian business to be acquired by the SOE will continue to operate on a commercial basis

Summing Up

- "Net benefit" subject to political imperatives at local, provincial and national levels – government and political implications at all levels need to be considered early and an appropriate strategy developed
- Stakeholders previously considered to have a marginal impact on approval now potentially more significant (i.e. unions, local politicians, special interest groups)
- Extra caution required for investments by SOEs
- National security review process has teeth
 - Trumps even other important government objectives
- Are all of these issues "chilling" foreign investment?/Does the government care?

ICA Risk Factors

- Nature of Offer: Hostile vs. Friendly
- Target Profile: "National Champion" vs. Junior Mining Property
- Buyer Profile: Strategic, Financial, SOE
- Buyer Reputation: Record with Prior Undertakings, Environmental, Labour Relations
- Post-Acquisition Plans
- Political Context: Local, Provincial, National

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