



PERSPECTIVE

Draft *Investment Canada Act* Regulations Provide More Details of New National Security Review Process and General Review Threshold

July 15, 2009

On March 12, 2009, the Government of Canada passed legislation amending the *Investment Canada Act* (ICA). These amendments made a number of significant changes to the ICA, including the following:

- Introducing a national security review process.
- Changing the general net benefit review threshold for most acquisitions of Canadian businesses by non-Canadians from C\$312 million in book value of assets to C\$600 million in enterprise value, once new regulations come into force, rising progressively to C\$1 billion over a four-year period.

On July 11, 2009, the Government of Canada published proposed regulations that specify the time periods for national security reviews and define the concept of "enterprise value". Key aspects of the proposed regulations are summarized below. (See "[Amendments to the Investment Canada Act: What Do They Mean For You?](#)" for more detail on the March 2009 amendments.)

While the proposed regulations provide greater detail for the new processes, despite market concerns they still do not provide a mechanism for national security pre-closing clearance for most transactions and could result in some surprising and arbitrary enterprise value calculations for general net benefit review thresholds.

National Security Review Process Timelines

The national security review process permits the Canadian government to review investments that could be injurious to national security and provides that the federal Cabinet may impose any measures that it considers advisable to protect national security.

Under this process, Cabinet may, on the recommendation of the federal Minister of Industry, order a national security review. If Cabinet orders a review, the Minister is required to send a notice to the investor that the investment will be reviewed, and the proposed transaction cannot be completed while the review is pending. If the transaction has already been completed, a review can still be ordered (and remedies, including

divestiture of the Canadian business, can still be required) following implementation of the transaction.

The time period within which the Minister must give the investor the first notification of a review, or possible review, runs from the time the Minister becomes aware of the investment up to 45 days after the relevant starting point. For reviewable investments, the 45-day period starts on the date of filing of the application for review. For investments that are not subject to review, the proposed regulations are unclear, but in any event the period during which the Minister can order a review, or possible review, will extend to at least 45 days after closing.

Where the Minister gives notice of a possible review, Cabinet, on the recommendation of the Minister, has a further 25 days to determine whether to order a review of the transaction.

If Cabinet orders a review, the Minister will consult with other government officials and departments. Following these consultations, if the Minister is satisfied that, or is unable to determine whether, the investment would be injurious to national security, the Minister must submit a report, with recommendations, to Cabinet. Alternatively, if the Minister is satisfied that the investment will not be injurious to national security, notice to that effect must be sent to the investor. Under the draft regulations, the deadline for the Minister to submit a report and recommendations to Cabinet, or give notice stating that no action will be taken, is 45 days from the date on which Cabinet ordered a review of the investment.

If the Minister submits a report and recommendations, Cabinet may then order any measure it considers advisable to protect national security, including prohibiting the investment, attaching conditions, or requiring the foreign investor to divest itself of its investment. The proposed regulations require that such an order be made within 15 days from the date on which the Minister reported on the investment to Cabinet. The Minister is then required to notify the investor of Cabinet order without delay.

Enterprise Value

In the case of an acquisition of control of a Canadian business which is publicly-traded, the "enterprise value of the assets" of the Canadian business would be the market capitalization of the entity plus its liabilities minus its cash and cash equivalents.

Market capitalization is obtained, generally, by multiplying the average daily closing price of each class of equity security by the average number of that security outstanding, in each case over the last 20 days of trading in the relevant entity's last fiscal quarter, and summing these figures for each class of equity security. In the case of unlisted equity securities, where the average daily closing price is unknown, the draft regulations propose using the average daily closing price of the entity's primary class of security equities as a proxy. It is not clear why the regulations equate the value of a class of unlisted equity securities to the value of the primary class of listed securities.

An "equity security" means a security of an entity that carries a right to vote in all or certain circumstances, to participate in the earnings of the entity or to receive the remaining property of the entity on its dissolution or liquidation, but does not include a right, warrant or option to acquire such a security.

The entity's liabilities, cash and cash equivalents are determined using the financial statements of the entity for the fiscal year immediately preceding the implementation of the investment. It is not clear why the regulations refer to the end of the last fiscal quarter when valuing equity securities but refer to the last fiscal year when valuing liabilities and cash.

In the case of acquisitions of control of a Canadian business which is not publicly-traded or where there is an acquisition of all or substantially all of the assets, the enterprise value of the assets of the Canadian business would be calculated according to the method set out in the existing ICA regulations (i.e., book value of the assets of the Canadian business as at the end of the last fiscal year, as reflected in the most recent annual financial statements).

The proposed regulations are available online at <http://canadagazette.gc.ca/rp-pr/p1/2009/2009-07-11/pdf/g1-14328.pdf> (starting at page 48) and are open for public comment until August 10, 2009.

If you have any questions regarding the foregoing, please contact [George Addy](#), [John Bodrug](#), [Mark Katz](#), [Chris Margison](#), [Jim Dinning](#), [Hillel Rosen](#) or any other member of the Competition and Foreign Investment Review Group at Davies Ward Phillips & Vineberg LLP at 416.863.0900 (Toronto) or 514.841.6400 (Montréal).

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