The Newsletter of the International Investment & Development Committee

Volume 1, Issue 2

Fall 2008

ABA Section of International Law

Your Gateway to International Practice

International Investment & Development In Focus

Chairs' Comments

Daniel Marín Moreno and Mélida Hodgson

Dear Colleagues,

Welcome back! The International Investment & Development Committee has gotten off to a great start for the 2008-2009 ABA year, which is due to the ABA on December 1st. We sponsored several programs at the Fall Meeting in Brussels, September 23-26th (see inside), and had a well-attended committee dinner. We have also received a record number of requests for program sponsorship for the Spring Meeting, which will be held in Washington, D.C., April 14-18, 2009.

Our next big goal is the Year in Review. If you are interested in contributing to our Year in Review submission, please contact Jean Paul Chabaneix as soon as possible at jpchabaneix@estudiorodrigo.com.

Jean Paul returns as one of the committee vice-chair, along with Ignacio Randle and Theresa Garelli. Joining them are Mark McNeill of Shearman & Sterling and Ucheora Onwuamaegbu of the World Bank's ICSID.

Our featured article in this newsletter, regarding changes to Canada's foreign investment review law, concerns an issue of continuing interest to members of the IID Committee. In addition, one of our members offers advice on cross-cultural negotiations. We hope that you find these articles useful.

We look forward to your participation to make this the best year yet for the IID Committee!

Recent Developments in Canadian Foreign Investment Law

Mark C. Katz

Canadian Government Confirms Refusal of Foreign Acquisition under *Investment Canada Act*

Investments by non-Canadians in Canadian businesses are subject to the Investment Canada Act ("ICA"). Investments governed by the ICA must be notified to the federal government, and, in some cases (where "cultural businesses" are involved), advance approval must be obtained from either the Minister of Industry or the Minister of Canadian Heritage.

Considerable controversy has surrounded the ICA recently. In the wake of a surge of foreign acquisitions of Canadian businesses, some have argued that the ICA should be amended to make foreign investments more difficult or, at the very least, to enable the federal government to extract more concessions from foreign investors. On the other hand, a competing school of thought argues that the ICA should be amended to make it even easier for foreign acquirers to invest in Canada.

One of the points made by advocates of a more robust review of foreign investments is that, in its twenty-three years of existence, foreign acquisitions have almost never been refused approval under the ICA. Indeed, not until this year was the first non-cultural acquisition by a foreign investor denied. That occurred in May 2008, when Canada's Minister of Industry, the Honourable Jim Prentice, confirmed that he had declined to approve the proposed $1.325 billion acquisition by Alliant Techsystems, Inc. ("Alliant") of the space division of MacDonald, Dettwiler and Associates Ltd. ("MDA").

Alliant is a U.S.-based arms and rocket manufacturer. It announced its offer for MDA's space division in January 2008. MDA's space division developed, among other things, the famous

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Inside This Issue

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International Investment & Development In Focus

Cross-Cultural Negotiation for Foreign Investors

Luis E. Ore

Social and economic forces are challenging the way people do business around the world. Globalization makes our world smaller, and cross-cultural situations are at the core of this trend. Whether negotiating with foreign governments, potential strategic partners, or local communities abroad, understanding cultural and situational factors that influence how people negotiate and deal with conflicting situations is crucial to making or breaking any investment project.

Dealing with potential strategic partners can be challenging if negotiators do not have a shared understanding about how parties deal with decision-making processes, profit distribution, or conflict resolution, among other things; and do not make a good-faith effort to negotiate not only a deal but a business relationship. "Deal makers" can run up against "blocking coalitions" if they do not include other stakeholders in the negotiation process. A "deal implementer" mindset might leave everyone better off. The way investors approach negotiations and introduce investment projects to local communities can affect the viability of the project and model their future relationship. A negotiating approach based on cultural generalizations with an adversarial mindset instead of engaging individuals and stakeholders in joint problem-solving with a mutual-gains mindset can prevent the successful implementation of the investment.

For instance, distrust of the local communities in foreign investors might be a cultural tendency of risk avoidance or a situational factor affected by past experiences, or it might be based on community members' perception of incompatible intentions or conflicting interests. If the local communities distrust the foreign investors, the population might not want to deal with them or have the investment projects implemented in their communities. Local communities that belong to collectivistic societies tend to fit into the particularistic-dimension approach to the application of norms. According to this approach, the rule of law is applicable to particular individuals differently and may benefit people differently. Members of collectivistic societies tend to have a large power-distance dimension and tend to be more hierarchically minded. Therefore, members of this type of society tend to distrust their court and legal system, and when these local communities feel uncertainty, fear, or anger while facing foreign investment that might affect natural resources, its members tend to rely on political power to demand the protection of their lifestyle, the status quo, or their rights. People will tend to apply a power-based approach and to participate in rallies and protests to call their interests, needs, and concerns to the attention of political leaders and any other powerful group.

The challenge is to balance awareness of cultural and situational factors while building positive working relationships and negotiating mutually beneficial, lasting agreements that embrace foreign investment. Cross-cultural awareness among foreign investors is increasing dramatically. But simplistic, adversarial, and traditional negotiating approaches can prevent foreign investors, potential strategic partners, and other stakeholders from bridging differences, reaching shared understanding, creating value, and generating lasting, profitable agreements. Apart from the differences among societies that tend to be goal-oriented or relationship-oriented and among individuals having direct or indirect communication styles and linear-thinking or circular-thinking processing styles, negotiators need to factor in other cultural dimensions and situational factors that might affect their negotiation processes abroad. In a word, foreign investors can design processes and strategies that better face cross-cultural negotiations and successfully implement foreign investment projects.

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Luis E. Ore is founder of ORASI Consulting Group Inc. and chair elect of the International Development Committee of the Association of Conflict Resolution's International Section.

"The challenge is to balance awareness of cultural and situational factors while building positive working relationships and negotiating mutually beneficial, lasting agreements that embrace foreign investment."

Report on the IID Committee's Fall Meeting Programs

From Gdansk to Buenos Aires: The Role of Public-Private Partnerships Today

Speakers: Alejandro Ciero, Estudio Béccar Varela; Michel Deschamps, McCarthy Tétrault, and Terry Selzer, Stampe, Haume & Hasselriis Advokater; Daniel Marín Moreno (Moderator), Gómez-Acebo & Pombo

In this program, the speakers brought their diverse experiences in assisting their clients in obtaining, executing, and operating public-private partnerships (PPPs), especially regarding infrastructure projects, in several jurisdictions. The fact that the jurisdictions represented were in different stages of developing these partnership structures demonstrated how the approach and choice of structures needs to vary depending on whether the country has established and proven rules and structures (such as in the case of Canada and Spain) or whether these rules and structures are only starting to develop (as in the case of Argentina and Poland). The program additionally illustrated the different ways to handle the difficult balance between investment and its financing and return in a way that is acceptable to public administration and to the private investor. In some cases, the best approach may be to avoid the application of the specific PPP rules. The panel also discussed the dilemma between bidding processes with closed and detailed conditions on the one hand, which bring speed to the process but may cause difficulties after the bidding process is closed due to the lack of flexibility; and, on the other, more open processes with the opportunity to present or discuss alternatives, which make the bidding processes longer and more complex but may ease the execution of the project. In addition, we saw that intensive communication with public authorities is required in all cases. Finally, we enjoyed a large and participative audience that picked the brains of our speakers with their doubts and questions.

Foreign Investment Dispute Arbitration

Speakers: Bart Legum, Debevoise & Plimpton; Yas Banifatemi, Shearman & Sterling; Peter Turner, Freshfields; Jean Christophe Honlet, Salans; and Mélida Hodgson (Moderator), Foley Hoag

One of the hottest issues in foreign investment dispute arbitration today is the challenge of developing nations to the ICSID dispute resolution system. Indeed, Bolivia withdrew from ICSID earlier this year, and Ecuador limited the kinds of disputes that ICSID can adjudicate. The reason for this is a perception of bias in the World Bank against developing countries. Following up on a Spring Meeting program that examined the reasons behind this perception and the possible consequences of these countries' actions, this program examined some of the practical issues that arise in the context of non-ICSID foreign-investment dispute arbitration.

The program took the form of a lively roundtable before a standing-room-only audience. The issues addressed included the rule-of-law effect of foreign investment arbitration, the applicable law in investment arbitration, the perceived need for more developing country arbitrators for the legitimacy of the system, the issues faced by sovereigns in non-ICSID arbitration, and domestic review of arbitral awards. We had significant audience participation, which contributed to a quality exchange of views on these various important topics.

Report-Back
Report on the Committee's Fall Meeting Programs

"The approach and choice of PPP structures needs to vary depending on whether the country has established and proven rules."

Datebook

Datebook
Up-and-coming ABA-SIL and IID Committee events

ABA-SIL & IBA Present "The Next Big Wave of Cross-Border Litigation"
November 6-7, 2008, in Miami, FL, USA

ABA-SIL 60th Anniversary Program on the Universal Declaration of Human Rights
November 13-14, 2008, in New York, NY, USA

ABA-SIL Midyear Meeting
February 13-15, 2009, in Boston, MA, USA

ABA-SIL Spring Meeting
April 14-18, 2009, in Washington, DC, USA

ABA-SIL Annual Meeting
July 31-August 2, 2008, in Chicago, IL, USA

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"Canadarm," which is used by NASA; and the Radarsat 2 satellite, a remote-sensing satellite that scans Canada's Arctic region. Pursuant to a licensing arrangement, the data and images generated by the Radarsat 2 satellite are used by the Canadian government to monitor Canada's Arctic interests. The Canadian government also supported the development of Radarsat 2 with $445 million in funding. MDA decided to sell the space division because it said the business could not compete for the lucrative U.S. defence contracts necessary to survive unless owned by a U.S. company.

The potential acquisition of the Radarsat 2 technology by a U.S. firm was what proved to be the undoing of the proposed transaction. Concerns were raised that the sale of the satellite would compromise Canada's ability to exercise sovereignty over disputed territories in the Arctic region, where the U.S. government does not recognize the full extent of Canada's territorial claims. MDA and Alliant countered by claiming that the transaction would have no impact on the Canadian government's ability to access the satellite's data.

On April 8, 2008, Minister Prentice sent a letter to Alliant stating that the manufacturer had not passed the standard for approval under the ICA. In other words, Minister Prentice was not satisfied that Alliant would generate a "net benefit" for Canada. Although Minister Prentice did not disclose in the April 8 letter the reasons underlying his decision, the comments he made subsequently make clear that the fate of the Radarsat 2 satellite was a major consideration. Apart from concerns about the impact on Canadian sovereignty, the Minister also indicated that Canadian control of the Radarsat 2 technology is necessary if Canada is to have a vibrant aerospace sector.

The Minister's April 8 decision did not end matters definitively. The ICA gives parties thirty days following a refusal letter to persuade the Minister to reverse his decision. According to various press reports, both Alliant and MDA attempted to do just that. However, those attempts were unsuccessful, and the Minister confirmed his denial of the transaction on May 8, 2008.

The Alliant/MDA case represents a milestone in the history of the ICA, but its practical significance is much less clear. For example, even at the time of the announcement, the Minister did his best to dispel the impression that his decision heralded an era of economic protectionism for Canada. Even more importantly, if certain proposals to amend the ICA are eventually enacted (see below), the scope and impact of this legislation stand to be greatly reduced, which makes the likelihood of further denials even more remote.

Competition Policy Review Panel

On June 26, 2008, the Competition Policy Review Panel released its report, entitled "Compete to Win," on Canada's foreign investment and competition policies. The Panel was created in July 2007 by the federal government with the mandate of examining the impact of Canada's foreign investment and competition laws on the domestic and international competitiveness of the Canadian economy. The Panel's report and related materials are available at www.ic.gc.ca/epic/site/cprp-gepmc.nsf/en/home.

The Panel's report offers several far-reaching proposals to amend Canadian foreign investment review laws. These include:

- substantially increasing the ICA review threshold for acquisitions of Canadian businesses by non-Canadians to a $1 billion enterprise value (except in the case of cultural businesses) and reversing the onus in the review standard to require that the Minister find that the proposed acquisition would be contrary to Canada's national interest;
- removing the *de facto* prohibition on bank, insurance, and cross-pillar mergers of large financial institutions;
- increasing the limit on foreign ownership of air carriers to 49% of voting equity on a reciprocal basis through bilateral negotiation;
- initially allowing foreign companies to establish new telecommunications businesses in Canada or to acquire existing businesses with market shares of up to 10%, and subse-

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"The potential acquisition of the Radarsat 2 technology by a U.S. firm was what proved to be the undoing of the proposed transaction."

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quently further liberalizing foreign ownership restrictions in this sector; and

- liberalizing the non-resident ownership policy on uranium mining.

Recommendations to Amend the Investment Canada Act

The Panel's recommendations to amend the ICA would significantly limit the number of transactions to which the ICA could apply and would make it more difficult for the Minister to refuse approval of those transactions that would be caught.

Under the current regime, apart from certain specified sectors, the general review threshold for most direct acquisitions of Canadian businesses is $295 million, based on the book value of the assets of the relevant company. Acquiring parties whose transactions are subject to review under the ICA must persuade the responsible Minister that the acquisition will be of "net benefit to Canada." In almost all cases, this requires the foreign investor to provide the Minister with binding undertakings, setting out the specific steps it will take to improve the Canadian business.

The Panel's recommendations would change the current regime in two crucial ways. First, a substantially higher threshold for review ($1 billion) would apply, which means that far fewer transactions would require approval. Second, rather than investors having to justify that their transactions are of "net benefit" to Canada, the Minister would instead have the onus of demonstrating why the transaction should not proceed.

Recommendations to Amend Sectoral Foreign Ownership Restrictions

The Panel also recommended greater scope for foreign investment and ownership in several industry sectors which it examined. In some cases, the proposals are conditional on reciprocity or on the obtaining of other benefits from relevant foreign countries that currently restrict access to Canadian entities.

Financial Services

The Panel commented that since 1998, when the Minister of Finance declined to approve two separate proposed mergers of major Canadian banks, a *de facto* prohibition on mergers between large financial institutions in Canada has prevailed. The Panel noted the relative decline in the size of Canadian banks on a global scale since that time and commented that this has prevented Canadian-based financial institutions from competing more effectively in international markets. At the same time, the Panel noted that allowing greater international competition as well as more competition between bank and non-bank lending institutions in Canada would benefit both the financial services sector and the public interest in competitive and efficient markets. Accordingly, the Panel recommended that the Minister of Finance should remove the *de facto* prohibition on bank, insurance, and cross-pillar mergers of large financial institutions subject to regulatory safeguards enforced and administered by the Office of the Superintendent of Financial Institutions and the Competition Bureau.

Air Transport

Canada currently limits foreign ownership of Canadian air carriers to 25% of voting equity. In the Panel's view, increasing the level of foreign investment permitted in the air transportation sector would enhance sustainable competition in the Canadian industry without necessarily impairing service. The Panel recommended that the Minister of Transport increase the limit on foreign ownership of air carriers to 49% of voting equity on a reciprocal basis through bilateral negotiation and complete "Open Skies" negotiations with the European Union as quickly as possible to be more competitive with the U.S. industry. The Panel also recommended that the Minister issue a policy statement by December 2009 on whether foreign investors should be permitted to establish separate Canadian-incorporated domestic air carriers using Canadian facilities and labour.

Telecommunications and Broadcasting

The Panel noted the significant and continuing product innovation in the telecommunications and broadcasting sector, where current rules limit

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the holding of voting shares by non-Canadians to 20% at the operating-company level and 33.3% at the holding-company level. The Panel concluded that liberalizing foreign investment restrictions would bring demonstrable economic benefits by increasing competitive pressures on all participants in the market. Consistent with a recent federal government telecommunications policy review panel, the Panel recommended a two-phased approach to foreign participation in the industry. In the first phase, foreign companies would be permitted to establish a new telecommunications business in Canada or to acquire an existing telecommunications company with a market share of up to 10% of the telecommunications market in Canada. The second phase would follow a review of broadcasting and cultural policies, with the goal of liberalizing the sector in a manner that would be competitively neutral for telecommunications and broadcasting companies.

Uranium

The Panel recommended that the Minister of Natural Resources issue a policy directive to liberalize the non-resident ownership policy on uranium mining, subject to (i) new national security legislation coming into force and (ii) Canada's securing commensurate market access benefits allowing for Canadian participation in the development of uranium resources outside Canada or access to uranium processing technologies for the production of fuel for nuclear power plants.

Conservative Party Proposals

Canada recently held federal elections on October 14, 2008. The Conservative Party, which triumphed at the elections, announced during the campaign a platform that would implement many of the Panel's recommendations in respect of the ICA as well as take other steps with regard to foreign investment in Canada. Specifically, the new Conservative Government plans to:

- amend the ICA to increase the threshold for foreign investment reviews from the current level of $295 million in gross asset value to $1 billion in enterprise value, with the increase to be phased in over four years;
- ensure greater transparency in the ICA process by requiring the responsible Minister to give reasons if an investment is disallowed;
- establish a new national security review mechanism in the ICA to ensure that foreign investments cannot jeopardize Canada's national security;
- work with Canada's trading partners to ensure that foreign investment is a "two-way street" and that Canadian companies also receive increased access to investment opportunities abroad;
- increase the permissible level of foreign investment in domestic airlines from 25% to 49% through bilateral negotiations with Canada's major partners, such as Europe and the United States — a change that would also secure increased access to international flight routes and landing rights through Open Skies agreements; and
- revise the non-resident ownership policy for uranium mining and development, provided that Canada's able to negotiate reciprocal benefits with potential investor nations and that any foreign investments in this sector meet the national security test.

These proposals make evident that the Conservatives plan to curtail the application of the ICA to limited circumstances — for example, where "national security" interests may be implicated. In that regard, however, whether any amendments to the ICA are necessary is open to debate, since "national security" issues could easily be encompassed in a net-benefit review and appear, in fact, to have been the reason why the Alliant/MDA transaction was turned down.

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Mark C. Katz is a partner of Davies Ward Phillips & Vineberg LLP in Toronto, Canada

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About the Committee

The **International Investment & Development Committee** addresses issues facing the practitioner counseling clients making cross-border investments, including in emerging economies. These issues include 1) host country programs and reforms intended to promote investments from abroad, including privatization and public-private partnering initiatives and financial market reforms; 2) U.S., bilateral, multilateral, and export credit agency programs to aid these efforts; 3) problems raised by restrictive legal and regulatory requirements governing the making, maintenance, and divestment of investments; 4) unique issues relating to investments in particular sectors, such as those relating to infrastructure and project finance, insurance, and financial services; 5) developing legal and investment structures; and 6) the impact on international investment of developing international norms and standards, such as those relating to advancement and protection of individual legal rights, environmental protection, and the developing international criminal law. The Committee's home on the Internet can be found at http://www.abanet.org/dch/committee.cfm?com=IC752000.

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About the Newsletter

International Investment & Development In Focus is a newsletter published biannually by the International Investment & Development Committee of the American Bar Association Section of International Law. International Investment & Development In Focus provides updates on current development pertaining to international investment and development, Committee news, and other information of professional interest to members of the Committee.

Members of the Section of International Law may receive *Investment & Development In Focus* free of charge as a benefit of membership. To **subscribe** to the newsletter, simply subscribe to the Committee's listserv "INTINVESTDEV" at http://www.abanet.org/dch/committee.cfm?com=IC752000. In addition, the full text of current and past editions of *Investment & Development In Focus* are available on the Committee's website.

International Investment & Development In Focus accepts **submissions** for publication of IID Committee updates and up-and-comings for its Committee News section, comments and notes on significant developments relevant to the IID Committee's work for the Noteworthy section, notes and reviews of recent and relevant publications for the Bookends section, and announcements of relevant opportunities for the Bulletin Board section. Submissions should be sent electronically in Microsoft Word format to Josh D. Friedman at friedmjo@uchastings.edu. Author guidelines are available upon request from Josh D. Friedman at friedmjo@uchastings.edu.

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