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Frequently asked questions concerning the *Investment Canada Act*

For more information, please contact Shuli Rodal, Michelle Lally or Kaeleigh Kuzma in Osler's Competition and Foreign Investment Group.

Author: Peter Glossop

The following are some frequently asked questions (FAQs) concerning the application, administration and enforcement of the *Investment Canada Act*. These FAQs and responses are of a general nature, and cannot be regarded as legal advice.

1. When does the *Investment Canada Act* apply?
2. What are the thresholds for review?
   (a) Financial Threshold
   (b) Acquisition of Control Threshold
3. What are the implications of the enterprise value threshold for investment reviews?
4. Are there any exemptions from filing under the *Investment Canada Act*?
5. If a transaction does not meet thresholds for review, is the investor required to obtain any kind of clearance, or take any action?
6. Do specific considerations apply to investments involving a cultural business?
7. What is considered a "cultural business"?
8. Are there any other sensitive sectors besides culture?
9. Can investors implement a proposed investment pending approval?
10. When will the investor receive approval of a reviewable investment?
11. What does "net benefit" mean?
12. How many investments have not been approved?
13. What happens once the Minister approves an investment?
14. Does the Minister publicly disclose an investor's undertakings?
15. What considerations apply to an acquisition of control by a state-owned enterprise (SOE)?

16. Which investments are subject to a national security review?
17. What does "national security" mean?
18. How do investors receive national security clearance?
19. If a national security review has been ordered and referred to the Governor in Council, what measures may the Governor in Council take?
20. What has been the experience so far with national security reviews?
21. How does the *Investment Canada Act* review process relate to the *Competition Act* review process?

When does the *Investment Canada Act* apply?

The *Investment Canada Act* (ICA) applies when a "non-Canadian" (e.g., an "entity" that is not Canadian-controlled):

- establishes a new business in Canada, or
- proposes to acquire control -- directly or indirectly -- of an existing Canadian business.

"Canadian business" is defined in the ICA as a business carried on in Canada that has:

- a place of business in Canada,
- an individual or individuals in Canada who are employed or self-employed in connection with the business, and
- assets in Canada used in carrying on the business.

Note that the ICA applies even if the Canadian business being acquired is not Canadian-controlled.

Direct investments, where the enterprise value or the book value of the Canadian business exceeds prescribed monetary thresholds, or those raising national security concerns, are subject to government approval. Except for certain cultural transactions and those raising national security concerns, all other acquisitions of control and establishments of new Canadian businesses are subject to a notification process only.

What are the thresholds for review?

Financial Threshold

A direct acquisition by a non-Canadian that is controlled by nationals of a specified free trade party (the European Union, the United States, the United Kingdom, Mexico, Australia, Brunei, Chile, Colombia, Honduras, Japan, Malaysia, New Zealand, Panama, Peru, Singapore, South Korea, the United Kingdom or Vietnam) to acquire control of a Canadian business, or a sale of a Canadian business when it is controlled by nationals of these nations, is only reviewable on a pre-closing basis by the Minister of Innovation, Science, and Economic Development if the enterprise value of the Canadian business exceeds $1.711 billion (in 2022; this amount is indexed annually).

For investments or divestitures by investors controlled by nationals of a World Trade Organization (WTO) member state, the *direct acquisition* of a Canadian business, or a sale of a Canadian business controlled by a WTO investor, is only reviewable on a pre-closing basis by the Minister of Innovation, Science, and Economic Development if the *enterprise value* of the Canadian business exceeds $1.141 billion (in 2022; this amount is indexed annually).

The case of a direct acquisition must be distinguished from that of an indirect acquisition. In an indirect acquisition, the investor acquires shares of a non-Canadian corporation, which in turn owns shares in a Canadian corporation. An indirect investment is not reviewable either on a pre-closing or a post-closing basis, except if the Canadian business is a "cultural business". In this circumstance, the acquisition is subject to review where the book value of assets is $50 million or more. An indirect investment may also be reviewable where it raises a national security issue.

Enterprise value is calculated differently, depending on whether the Canadian business is a publicly traded or privately held entity, or consists of assets.

Direct acquisition of a publicly traded entity – the publicly traded entity must have an enterprise value greater than the appropriate threshold, based on its market capitalization, plus its total liabilities excluding its operating liabilities and minus its cash and cash equivalents.

- Market capitalization is calculated by using the average daily closing price of the target's quoted equity securities on the entity's principal market (i.e., where the greatest volume of trading occurred during the trading period) over the most recent 20 days of trading ending before the first day of the month that immediately precedes the month in which the application for review or notification is filed.
- If there are unlisted equity securities, the fair market value of such securities, as determined by the board of directors of the investor or other person authorized to make that determination, is included.
- Total liabilities, excluding operating liabilities, cash and cash equivalents are determined based on the most recent quarterly financial statements.

Direct acquisition of a privately held entity –the privately held entity must have an enterprise value greater than the appropriate threshold, based on the total acquisition value, plus its total liabilities excluding its operating liabilities and minus its cash and cash equivalents.

- Where the investor is acquiring 100% of the voting interests, total acquisition value is the total consideration payable. Where the investor is acquiring less than 100% of the voting interests, total acquisition value is the aggregate of the consideration payable by the investor, the consideration payable by any other investors, and the fair market value determined by the investor of any portion of the voting interests that is not being acquired.
- In circumstances where the parties are non-arm's length, or consideration is nominal or zero, total consideration payable is fair market value.
- Total liabilities, excluding operating liabilities, cash and cash equivalents are determined based on the most recent quarterly financial statements.

Acquisition of assets – the assets must have an enterprise value greater than the appropriate threshold, based on the total consideration payable, plus the liabilities that are assumed by the investor (other than operating liabilities), and minus the cash and cash equivalents that are transferred to the investor.

- In circumstances where the parties are non-arm's length, or consideration is nominal or zero, total consideration payable is fair market value.

Direct acquisition by a state-owned enterprise (SOE) investor – the applicable threshold is book value of assets of the Canadian business is $454 million or more (in 2022; this amount is indexed annually).

Acquisition of Control Threshold

An investment by a non-Canadian must involve an acquisition of control in order for the ICA to apply. An acquisition of control is presumed to occur if a non-Canadian acquires one- third or more of the voting shares of a corporation, and is deemed to occur if a non-Canadian acquires a majority of the voting shares of a corporation or a majority of the voting interests of a partnership, trust or joint venture.

An acquisition of less than one-third of the voting shares of a corporation, or less than a majority of the voting interests of a partnership, trust or joint venture, is deemed not to be an acquisition of control (except in cases involving a cultural business or an SOE investor, where a control in fact test applies).

An investment by a non-Canadian must involve an acquisition of control in order for the ICA to apply.

An acquisition by a non-Canadian of all or substantially all of the assets used in carrying on a Canadian business is an acquisition of control.

What are the implications of the enterprise value threshold for investment reviews?

The enterprise value threshold has several implications:

- For public bids, there is an element of strategy in deciding when to make an ICA filing. Thetime period for calculating the share price for market capitalization is determined when an ICA filing is made. It is possible that the first bidder may file a notification based on an enterprise value which is below the threshold (i.e., no ICA review would be required for that bidder). If the announcement of this first bid has the effect of increasing the target's share price, this has the potential to result in an uneven playing field amongst foreign bidders. While the first bidder would not be subject to ICA review, if there is a significant time gap in between bids such that enterprise value must be re-calculated to take into account the impact on share price as a result of the first offer, subsequent bidders may be subject to ICA review if the enterprise value has increased above the threshold.
- SOE and private sector investors are subject to different thresholds. As a result, it is possible that a private sector investor may trigger a review as a result of the target's enterprise value exceeding the appropriate threshold, while that same investment by an SOE would not trigger a review if the book value of the target's assets is below the $454 million asset value threshold. The converse may also occur, i.e. a private sector investor may not be subject to review if the enterprise value of the target is below the enterprise value threshold, while an SOE may be subject to review because the book value of the target exceeds $454 million.
- Consideration payable and fair market value determinations in acquisitions of privately-held entities and assets have ICA filing implications.

Are there any exemptions from filing under the *Investment Canada Act*?

The ICA exempts several types of transactions, for example:

- an acquisition of control of a branch business;
- an acquisition of control in connection with the realization of security granted for a loan or other financial assistance and not for any purpose related to the ICA;
- a corporate reorganization following which the ultimate control of the Canadian business remains unchanged; and
- certain acquisitions of control or establishments of new Canadian businesses where the investor is a foreign bank or is associated with a foreign bank.

If a transaction does not meet thresholds for review, is the investor required to obtain any kind of clearance, or take any action?

If a direct or indirect investment by a non-Canadian does not meet the review thresholds set out above, the investor must file a notification with the Investment Review Division (IRD). A notification must be filed at any time prior to the implementation of the investment or within 30 days after its implementation. Non-Canadians who establish a new Canadian business also must file a notification.

Do specific considerations apply to investments involving a cultural business?

Review thresholds for acquisitions of control of a Canadian cultural business are $5 million in book value of assets of the business for direct investments and $50 million in book value of assets of the business for indirect investments. For an indirect acquisition of a cultural business, where the value of the worldwide assets of the Canadian business exceeds 50% of the value of all assets acquired, the review threshold is $5 million in book value of assets.

Unlike non-cultural businesses, indirect investments in the cultural sector are reviewable on a post-closing basis. If the assets of the cultural business fall below the thresholds for review, the Governor in Council (i.e., the federal Cabinet) may still order a review on a discretionary basis. Cultural investments are reviewed by the Department of Canadian Heritage.

What is considered a "cultural business"?

"Cultural business" is defined in the ICA. A cultural business is a business that carries on any of the following:

a. the publication, distribution or sale of books, magazines, periodicals or newspapers in print or in machine readable form (but excludes businesses involved only in the printing or typesetting of these items);

b. the production, distribution, sale or exhibition of film or video recordings;

c. the production, distribution, sale or exhibition of audio or video music recordings;

d. the publication, distribution or sale of music in print or machine readable form; or

e. any business activities involving radio communication intended for direct reception by the general public, any radio, television and cable television broadcasting undertakings and any satellite programming and broadcast network services.

Notably, there are special policies which prevent or restrict investments in the film distribution, and book publishing and distribution sectors. However, the government has been adopting a more flexible and pragmatic approach to enforcement of these policies. For example, in 2010, Amazon.com was permitted to establish a Canadian fulfilment centre and Apple Canada was granted approval to establish iBookstore Canada, in return for certain commitments to strengthen the Canadian book sector. In 2012, Target received approval to sell cultural products, including books, when it launched its stores in Canada. In 2014, the Department of Canadian Heritage approved Torstar Corporation's sale of the Harlequin book business to HarperCollins Publishers, a subsidiary of News Corp. (a transaction which on its face was prohibited by the book policy). In 2017, Netflix entered an agreement with the government which allowed it to avoid the traditional taxation framework applied to broadcasters in exchange for a $500 million investment for content creation in Canada. In 2019, Hasbro's acquisition of Toronto- based film, music and television content producer and distributor Entertainment One (eOne) was approved.

Are there any other sensitive sectors besides culture?

Until 2009, the lower review thresholds which still apply to acquisitions of control of cultural businesses also applied to acquisitions of control of Canadian businesses involved in financial services, transportation services, and uranium production. These industries are no longer subject to these lower thresholds. In addition to specific sectoral review legislation, however, acquisitions in these sectors may be subject to national security review in the same way as all other sectors of the economy.

With respect to national security, based on the limited experience to date, certain sectors may be more likely to attract scrutiny, including aerospace, defence, network and data security, telecommunications and sensitive technology.

Investors may also encounter provincial government concerns during an ICA review, such as during the attempted 2010 acquisition of Potash Corp. by BHP Billiton (Saskatchewan) and the 2012 offer by Lowe's to acquire Rona (Quebec).

Can investors implement a proposed investment pending approval?

Generally, the direct acquisition of a Canadian business cannot be implemented until the Minister of Innovation, Science, and Economic Development (or Minister of Canadian Heritage for cultural transactions) "is satisfied that the investment is likely to be of net benefit to Canada". In a global transaction, where the Canadian business is being acquired directly, and there is no obstacle to closing outside of Canada, it may be necessary on closing to "carve out" the Canadian portion of the acquired business until the transaction is approved by the Minister.

Indirect transactions involving WTO investors or sellers are not reviewable. Indirect cultural transactions may be implemented without obtaining pre-closing approval.

When will the investor receive approval of a reviewable investment?

Investors must file an application for review with the IRD prior to implementation of the investment, and allow sufficient time for review by the IRD and the Minister's office before closing. The Minister has up to 45 calendar days (which he/she may extend by an additional period of 30 calendar days) to determine whether the investment should be approved. The review period may be extended past 75 days for an additional period which is determined by agreement between the IRD and the investor. It is prudent to allow at least 75 days for approval. The median review time from April 1, 2018 to March 31, 2019 was 64 days. During this period, one lengthy review contributed to an average review time of 72 days.

What does "net benefit" mean?

Net benefit is not defined in the ICA. However, the Minister will consider the following factors set out in the ICA to determine whether an investment is likely to be of "net benefit":

- effect of the investment on the level of economic activity in Canada, on employment, on resource processing, on the utilization of parts, components and services produced in Canada and on exports from Canada;
- degree and significance of participation by Canadians in the Canadian business;
- effect of the investment on productivity, industrial efficiency, technological development, product innovation, and product variety in Canada;
- effect of the investment on competition within any industry in Canada;
- compatibility of the investment with national industrial, economic and cultural policies (taking into consideration provincial policy objectives); and
- contribution of the investment to Canada's ability to compete in world markets.

In practice, this means that the investor will have to set out in its application for review projections for Canadian employment, capital expenditures in Canada, Canadian management participation and responsibilities for the Canadian business, R&D activity in Canada, production in Canada and exports, and other relevant information. Foreign investments in cultural businesses must take into account the goal of the Department of Canadian Heritage to promote Canadian content across various forms of media. In addition, the investor typically – though not always – must submit binding undertakings to the Minister confirming its commitment to perform the key elements of these plans. Undertakings apply over a three-year period after closing (five years for a cultural investment).

How many investments have not been approved?

Between June 30, 1985 and March 31, 2019, the Minister reviewed and approved approximately 1,758 investments.

Thus, in over 30 years, only a handful of major proposals outside the cultural area were disallowed (e.g., Macdonald Dettwiler and Associates Ltd.'s proposed acquisition by Alliant Techsystems Inc. in May 2008, BHP Billiton plc's proposed hostile takeover of Potash Corporation of Saskatchewan in November 2010, Accelero Capital Holdings' proposed acquisition of the Allstream division of Manitoba Telecom Services Inc. in October 2013, and China Communications Construction Company Limited's proposed takeover of construction firm Aecon Group Inc. in 2018).

What happens once the Minister approves an investment?

After receiving approval and implementing the investment, the investor must comply with its undertakings. The investor is also required to submit a "progress report" to the IRD approximately 12 – 18 months after closing and every 12–18 months thereafter for the duration of the undertakings, so that the IRD may assess whether the investor is complying with its undertakings.

The Minister is empowered to demand that an investor comply with its undertakings. If an investor fails to comply with a demand issued by the Minister, the Minister may apply to a superior court for an order directing the investor to comply with the undertakings, requiring it todivest itself of the acquired business and imposing a penalty not exceeding $10,000 for each day of contravention.

In 2009, the Minister brought court proceedings against U.S. Steel in relation to alleged shortcomings in performing its undertakings. In 2011, the Minister reached an out-of-court settlement with U.S. Steel, in return for U.S. Steel's commitment to significantly enhanced undertakings. Typically, however, an investor will reach an agreed solution with the Minister concerning a failure to fulfill undertakings.

After receiving approval and implementing the investment, the investor must comply with its undertakings.

Does the Minister publicly disclose an investor's undertakings?

Normally, the Minister does not publicly disclose an investor's undertakings. However, in connection with enforcement proceedings in the U.S. Steel case, certain undertakings were disclosed.

In addition, the IRD may disclose the fact that an application has been filed under the ICA, and at what point the investment is in the review process. Prior to making such a disclosure, the IRD will inform the investor. The IRD will not disclose the information if the investor satisfies the IRD that the disclosure would prejudice the investor.

An investor may voluntarily disclose the general tenor of its proposed undertakings for strategic reasons.

What considerations apply to an acquisition of control by a state-owned enterprise (SOE)?

Investments by SOEs, including sovereign wealth funds, are analysed under the usual "net benefit" factors in the ICA, as well as special guidelines which refer to:

- the nature and extent of control by the foreign government,
- the SOE's corporate governance, operating and reporting practices,

- the SOE's adherence to free market principles,
- the effect of the investment on the level and nature of economic activity in Canada, and
- whether the Canadian business will retain the ability to operate on a commercial basis.

In an SOE transaction, the Minister will consider requesting undertakings such as appointing independent Canadian directors, employing Canadians in senior management, incorporating the business in Canada and listing shares of the SOE or the Canadian business on a Canadian stock exchange.

In December 2012, following the Minister's approval of Malaysian-controlled PETRONAS' $6-billion acquisition of Progress Energy Resources Corp. and CNOOC's $15.1-billion acquisition of Nexen Inc., the government announced it was taking a more restrictive approach to reviewing investments in Canada by SOEs. Although the government stated that it continues to welcome and encourage foreign investment in Canada, it indicated a clear preference for private foreign investment over investment by SOEs, minority SOE investments over acquisitions of control by SOEs, and a lower tolerance for SOEs acquiring control of, or material influence over, leading firms in any sectors of Canada's economy. Further, the government stated that acquisitions of control in the Canadian oil sands by SOEs will only be permitted in "exceptional" circumstances.

In 2013, the ICA was amended to introduce an expanded definition of SOE to include individuals acting under the direction of a foreign government and individuals and entities directly or indirectly influenced by a foreign government. The Minister may determine whether an entity is controlled in fact by a SOE or whether there has been an acquisition of control by a SOE, or that an otherwise Canadian-controlled entity is controlled in fact by a SOE.

Acquisitions by SOEs which do not confer control are not reviewed under the SOE guidelines, but may be subject to review under the national security jurisdiction.

In April 2020, the Government of Canada announced a new policy in response to the global COVID-19 global pandemic regarding investments into Canada by SOEs which may be motivated by non-commercial imperatives that could harm Canada's economic or national security interests. The new policy indicates that, from a practical perspective, investments involving SOEs may be subject to requests for additional information or extensions of timelines. For more information, see Osler Update: Canada still open for business despite new COVID-19 policy (April 23, 2020).

Which investments are subject to a national security review?

An investment is subject to national security review if the Minister considers that the investment could be injurious to national security and if the Governor in Council (i.e., the federal Cabinet, on the Minister's recommendation) makes an order for review. Notably, even establishments of new businesses and investments which do not involve an acquisition of control of a Canadian business may be subject to national security review.

What does "national security" mean?

"National security" is not defined in the ICA. In 2016, the government released a set of guidelines for the national security review process. The guidelines state that, in assessing the national security implications of a proposed investment, the nature of the asset or business activities and the parties, including the potential for third party influence, involved will generally be considered.

The guidelines also provide nine factors that are used to determine whether a national security review will be conducted. These include:

- the potential effects of the investment on Canada's defence capabilities and interests;
- the potential effects of the investment on the transfer of sensitive technology or know-how outside of Canada;

- involvement in the research, manufacture or sale of goods/technology identified in Section 35 of the *Defence Production Act*, which refers to controlled goods such as firearms and military equipment;
- the potential impact of the investment on the security of Canada's critical infrastructure;
- the potential impact of the investment on the supply of critical goods and services to Canadians, or the supply of goods and services to the Government of Canada;
- the potential of the investment to enable foreign surveillance or espionage;
- the potential of the investment to hinder current or future intelligence or law enforcement operations;
- the potential impact of the investment on Canada's international interests, including foreign relationships; and,
- the potential of the investment to involve or facilitate the activities of illicit actors, such as terrorists, terrorist organizations or organized crime.

In April 2020, the Government of Canada announced a new policy in response to the global COVID-19 global pandemic regarding enhanced national security review for investments related to public health and critical goods and services. For further information, see Osler Update (April 23, 2020).

How do investors receive national security clearance?

For an investment involving an establishment of a new Canadian business or an acquisition of control of an existing Canadian business, an investor may obtain comfort on national security issues by submitting the legally required notification or application for review. However, there is no prescribed clearance process for transactions which do not require notification or review, even though such transactions may be subject to review under the ICA on the basis of national security. The national security guidelines encourage investors to contact the IRD at the earliest stage of aproposed investment.

The Minister has 45 days after the certified date of a notification or an application for review to notify the investor that an order for national security review may be issued. An investment that is not subject to notification or review may be voluntarily disclosed to the Minister; the Minister may notify the investor up to 45 days after the transaction has closed that an order for national security review may be issued.

Including all of the interim review periods and the final period in which the Governor in Council may take action with respect to the investment, a full national security review may last up to 200 days (or longer, if the investor and the Minister agree to an extension). The average duration of review for cases subject to full national security review in 2018-19 was 161 days.

If a national security review has been ordered and referred to the Governor in Council, what measures may the Governor in Council take?

The Governor in Council may, by order, take any measures it considers advisable to protect national security. Measures include:

- directing the investor not to implement the investment,
- authorizing the investment on the condition that the investor provide undertakings or implement the investment on specified conditions, or
- requiring divestiture of the investment (if previously completed).

What has been the experience so far with national security reviews?

In the seven-year period from April 1, 2012 to March 31, 2019 there were 22 Cabinet level national security reviews. These reviews led to four transactions being blocked, seven transactions being subject to divestiture orders, four being permitted with conditions, four being subject to no further action and four transactions being withdrawn by the investor after Cabinet-level review was ordered. Seven of the 22 review cases occurred in the most recent 2018-19 timeframe. To put these seven cases in context, however, they represented less than 1% of all notified and reviewed investments (i.e. 962) during this period.

How does the *Investment Canada Act* review process relate to the *Competition Act* review process?

The ICA review is undertaken separately from the review of a proposed transaction on competition law grounds under the *Competition Act* (CA). The CA review is undertaken by the Competition Bureau. The Minister may delay the approval of a proposed transaction while the Competition Bureau is reviewing it under the CA. One of the net benefit factors listed in the ICA is the effect of the investment on competition within any industry in Canada. The Minister may also decide to approve a transaction that is still under review by the Bureau.

For more information, please contact:

Shuli Rodal
Partner, Competition/Antitrust & Foreign Investment
srodal@osler.com
416.862.4858

Michelle Lally
Partner, Competition/Antitrust & Foreign Investment
mlally@osler.com
tel: 416.862.5925

Kaeleigh Kuzma
Partner, Competition/Antitrust & Foreign Investment
kkuzma@osler.com
tel: 403.592.7264