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Foreign buyers of Canadian businesses are less likely to require approval from the Minister of Innovation, Science and Economic Development under the “net benefit to Canada” test as a result of increases in the review thresholds this year. At the same time, acquisitions of even small Canadian businesses—including minority investments—can still be subject to national security review. The Canadian Government’s recent (August 31, 2017) annual report on the *Investment Canada Act* (the Report) highlights the relative infrequency of such reviews; however, the consequences of such a review can be draconian (e.g., divestiture of a completed transaction). Helpfully for prospective foreign investors, the Report also provides some insight into the reasons national security reviews may be ordered.

## “Net benefit” review streamlined

The review of foreign investments into Canada under the “net benefit to Canada” test has been significantly streamlined this year for private sector investors (i.e., those that are not controlled or influenced by foreign governments) from certain countries. As of September 21, 2017, the new review threshold under the Canada-European Union Comprehensive Economic and Trade Agreement (CETA) came into effect, significantly increasing the threshold for EU investors to CA\$1.5 billion in enterprise value of the Canadian target. This means that fewer transactions will be subject to the “net benefit to Canada” test that typically requires investors to provide commitments to the Government relating to, among other factors, levels of employment, participation of Canadians in senior management, maintaining head office functions in Canada and capital expenditures.

The increase in the review threshold is good news for foreign investors and not just those from the European Union. Private sector investors from countries with which Canada has a free trade agreement also benefit from the higher review threshold. These “free trade countries” are: Chile, Colombia, Honduras, Mexico, Panama, Peru, South Korea and the United States.

In addition to the higher threshold applicable to investors from the EU and the “free trade countries”, the Government has accelerated the increase in the “net benefit to Canada” threshold applicable to investors from other World Trade Organization countries from CA\$800 million to CA\$1 billion - two years ahead of schedule.

## Greater disclosure on national security review

The Report analyzes the numbers of foreign investments into Canada, the sources of those investments and the sectors in which they are made. It also provides modest, yet helpful insights into the Government’s current approach to the national security review process.

### Frequency of national security reviews

The Report provides more detail than past reports on national security reviews of foreign investments, including the frequency of such reviews and their results.

In 2016-17, of the 22 applications, 715 notifications and other investments that that were subject to review for potential national security concerns, only four notices were issued to extend the period of time the Government has to consider whether a national security review should be ordered. In two of the four cases, no order for a national security review was made.

Five full-fledged national security reviews were conducted in 2016-17. Four of those were the result of Cabinet Orders while one review was pursuant to a November 2016 Federal Court Order, which set aside a 2015 Cabinet Order (under the previous Government) for divestiture, and remitted the matter back to the Minister for a “fresh” review (the O-Net case). A final Cabinet Order was issued in all five cases in which reviews were conducted. In three cases, the non-Canadian was ordered to divest itself of control of the Canadian business. In two cases, the investment was authorized with the imposition of conditions that mitigated the identified national security risks to a degree that allowed the investment to proceed.

These results highlight two points for foreign investors. First, if there is any doubt whether a national security could be a concern in a transaction, investors should make the appropriate filing (a notification or application for review) more than 45 days prior to closing to receive comfort that a review will not be ordered nor a divestiture remedy sought. Second, mitigation of the national security risk now appears to be a remedy that has become more accepted by the Government in certain circumstances.

Finally, the Report also underlines the lengthy potential duration of the review process – more than 200 days if each stage of the national security process is fully engaged.

## Reasons for national security reviews

The Report also highlights the national security factors that, since 2012, have given rise to either (i) an extended period of consideration regarding whether a national security review should be conducted; or (ii) a Cabinet Order for national security review. These include the potential:

- injury to Canada’s defence capabilities;
- transfer of sensitive dual-use technology or know-how outside of Canada;
- impact on the supply of critical goods and services to Canadians;
- enabling of foreign surveillance or espionage;
- injury to Canada’s international interests; and
- of the investment to involve or facilitate organized crime.

The most common factors were: the potential for transfer of sensitive dual-use technology or know-how outside of Canada; the potential to negatively impact the supply of critical services to Canadians or the Government; and the potential to enable foreign surveillance or espionage.

## Looking forward

The Government’s efforts to reduce the number of “net benefit to Canada” reviews should be welcome news to investors looking to buy Canadian businesses. However, this streamlining leaves behind investors who are state-owned enterprises (SOEs), which continue to be subject to a lower review threshold (CA\$379 million in the book

value of the Canadian target's assets). In addition, there has been no formal renunciation by this Government of the previous Government's policy banning SOE acquisitions of control of Canadian oil sands businesses.

The Government's provision of more guidance regarding national security review with the release of its guidelines late last year and its enhanced communication relating to national security review in the Report are helpful to foreign investors and their advisors. At the same time, as a result of a few investments that have captured media attention in 2017 (including the O-Net case), there is a perception in some quarters that national security reviews may be more subjective, politically motivated, and therefore, unpredictable than previously thought. Whether this view has merit is difficult to ascertain given that, despite the Government's efforts to increase transparency, the national security review process in Canada remains largely opaque.

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