

# Mergers And Acquisitions In Canada

**Section 4:** Foreign Investment Notification and  
Approval Under the *Investment Canada Act*



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# Foreign Investment Notification and Approval Under the *Investment Canada Act*

## Introduction

The *Investment Canada Act*<sup>54</sup> (the “Act”) regulates certain investments in Canadian businesses by non-Canadians.<sup>55</sup> The purpose of the Act is “to provide for the review of significant investments in Canada by non-Canadians in order to ensure net benefit to Canada and to provide a mechanism for reviewing and blocking investments that may be injurious to national security.”

The Act is administered and enforced by Industry Canada and, in particular, the Director of Investments (the “Director”) at the Investment Canada Review Division, with ultimate approval for reviewable transactions granted by the Minister of Industry (the “Minister”). For certain investments that relate to Canadian cultural businesses, the Department of Canadian Heritage (“Heritage Canada”) is responsible for administering the Act.

Although first enacted in 1985, and despite a large number of reviews of foreign investments to date, only two foreign investments outside of the cultural sector have been refused.

While compliance with the legislation can range from a minor inconvenience to the more involved negotiation of specific undertakings relating to future employment, capital expenditures or other commitments, it has not proved to be a significant impediment to foreign investors wishing to invest in Canada.

## Notification and Review

Under the Act, investments by non-Canadians to establish a new Canadian business, or to acquire control of an existing Canadian business, are subject to either notification only or to review and approval, unless a specific exemption applies.<sup>56</sup> Notification is an administrative formality and is required in respect of the establishment of a new Canadian business by non-Canadians or the acquisition of control by non-Canadians of an existing Canadian business that falls below the applicable threshold for review. A notification must be filed at any time prior to, or within 30 days of, the implementation of the investment.

Where an investment is reviewable, the investor is obliged to complete an application providing prescribed information about the investor and its plans for the existing Canadian business. In the case of most reviewable investments, including all direct acquisitions of control of a Canadian business, the investment cannot be implemented unless it has been reviewed and the Minister is satisfied that the investment is likely to be of net benefit to Canada. There are no filing fees in respect of either a notification or an application for review.

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54 (R.S., 1985, c. 28 (1st Supp.))

55 For the purposes of the Act, a non-Canadian includes any entity that is not controlled or beneficially owned by Canadians.

56 Exemptions are set out in section 10 of the Act.

## Thresholds for Review

In respect of the acquisition of control of an existing Canadian business by non-Canadians, there are several thresholds for review under the Act. The applicable threshold depends on:

1. whether the non-Canadian investor is from a country that is a member of the World Trade Organization (a “WTO investor”<sup>57</sup>) or the Canadian business being acquired is already controlled by a WTO investor;
2. whether the acquisition of control is direct or indirect; and
3. whether the Canadian business that is being acquired is a “cultural” business, as defined in the Act.

At the time of publication, direct acquisitions of control of a Canadian business<sup>58</sup> (that is not a “cultural” business) will be subject to review where the book value of the assets of the Canadian business equals or exceeds CDN\$312 million. However, recent amendments to the Act, not yet proclaimed, will see this changed. Under the amended threshold, direct acquisitions of control of a Canadian business (that is not a “cultural” business) will be subject to review where the “enterprise value” of the Canadian business exceeds CDN\$600 million<sup>59</sup> for WTO investors, and where the “book value” of the assets of the Canadian business equals or exceeds CDN\$5 million for non-WTO investors.<sup>60</sup> “Enterprise value” has not been defined yet.

Indirect acquisitions of control (that is, the acquisition of a corporation incorporated outside of Canada which in turn controls, directly or indirectly, a Canadian entity) are generally not reviewable. Indirect acquisitions can be subject to review, if the acquisitions are by non-WTO investors from sellers who are non-WTO investors or Canadians and the assets of the Canadian business being acquired have a book value of CDN\$50 million or more, or if the book value of the assets is below the CDN\$50 million threshold, the book value of the assets is at least CDN\$5 million and comprises greater than one-half of the value of the entities whose control is being acquired pursuant to the transaction.

## Cultural Businesses

Notwithstanding the foregoing, if the Canadian business being acquired is a cultural business, then the threshold for review of direct acquisitions of control is CDN\$5 million and for indirect acquisitions of control is CDN\$50 million, respectively, regardless of whether the investor qualifies as a WTO investor. These cultural business thresholds are based on the book value of the assets, as already described, and will not be based on “enterprise value” even when the amendments to the Act are implemented.”

Note that acquisitions of control of cultural businesses that fall below these thresholds, as well as establishments of cultural businesses, may still be subject to review if they include activities described in (a) to (d) below, upon the order of the Governor in Council (i.e., the federal cabinet).

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57 In determining whether an investor is a WTO investor, if the ultimate parent is a widely held public company that is not controlled in fact through the ownership of its voting interests, the acquiring entity would be considered to be a WTO investor if two-thirds of the members of the board of directors of the public company are any combination of Canadians and nationals of other WTO member states.

58 A direct acquisition includes an asset acquisition or the acquisition of the shares of a Canadian-based company or the ownership interests in a Canadian partnership trust or joint venture.

59 This will be the WTO investor threshold for the two years following implementation of the amendment, increasing to CDN\$800 million for the two years after that, and then to CDN\$1 billion for the next year and part-year to December 31, with annual indexing for inflation thereafter pursuant to a formula in section 14.1 of the Act.

60 Under the Act, the book value of the assets is the aggregate of all assets being acquired, as shown in the audited financial statements (or unaudited statements if audited statements are not available), for the Canadian business for its fiscal year immediately preceding the implementation of the investment.

The Act and related regulations set out the following definition for the “cultural business” activities that trigger review at the lower thresholds:

“cultural business” means a Canadian business that carries on any of the following activities, namely, (a) the publication, distribution or sale of books, magazines, periodicals or newspapers in print or machine readable form, other than the sole activity of printing or typesetting; (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) radio communication in which the transmissions are intended for direct reception by the general public, any radio, television and cable television broadcasting undertakings, and any satellite programming and broadcast network services.

As outlined above, if the Canadian business being acquired is engaged in any of these business activities, then the lower thresholds for review apply to both direct and indirect acquisitions of control. Heritage Canada, and not Industry Canada, is responsible for review and approval of the investment where the Canadian business is considered to be a “cultural business.”

### **Applications for Review and the Review Process**

Where the applicable threshold for review has been exceeded, the investor must file an application for review providing prescribed information about the investor and the Canadian business. In case of direct acquisitions, the application must be filed prior to the completion of the transaction and must include a description of the purchaser’s plans for the Canadian business. The plans should set out the net benefit of the investment to Canada including, if applicable, capital expenditure projections and the effect of the investment on employment, the location of head office, technological development, competition and participation of Canadians in the senior management of the Canadian business.

The Act provides that, following receipt of a completed application for review, the Minister has an initial 45-day period to make a determination as to whether the investment is likely to be of net benefit to Canada. This period may be extended by the Minister unilaterally for a further 30 days. Any additional extensions must be with the consent of the investor. In cases where the Minister has advised the investor, within the initial 45-day period or any extension period, that he or she is not satisfied that the investment is likely to be of net benefit to Canada, the investor may make representations and submit undertakings in respect of the Canadian business within 30 days of the notice, or any further period agreed upon between the investor and the Minister. After the expiry of the 30 days, or any agreed upon extension, the Minister must notify the investor that he or she is, or is not, satisfied that the investment will be of net benefit to Canada. If the investment was implemented but is not ultimately approved by the Minister, the investor must divest control of the Canadian business.

A reviewable investment may not be implemented prior to the investor receiving a decision from the Minister that the investment is of net benefit to Canada, unless one of three exceptions applies:

1. where the Minister is satisfied that a delay in implementing the investment would result in undue hardship to the investor or would jeopardize the operations of the Canadian business, and the Minister has sent a notice to the investor permitting implementation of the investment prior to completion of the review process;
2. where the investment is an indirect acquisition (as defined above); and
3. where the investment is not normally reviewable, but the Government exercises its authority by Order-in-Council to review the investment because it involves a cultural business activity.

### **Net Benefit to Canada Test**

Where an investment is reviewable, the investor may not implement the investment or complete the transaction until the Minister has determined that the investment is or is likely to be of “net benefit to Canada,” in the language of the Act. In determining this, the Minister will consider the following statutory factors:

1. the effect on the level of economic activity in Canada, employment, resource processing, the utilization of parts and services produced in Canada, and exports from Canada;
2. the degree and significance of participation by Canadians in the Canadian business or new Canadian business, and in any industry or industries in Canada;
3. the effect of the investment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;
4. the effect of the investment on competition within any industry in Canada;
5. the compatibility of the investment with national industrial, economic and cultural policies; and
6. the contribution of the investment to Canada’s ability to compete in world markets.

### **Net Benefit - State-owned enterprises**

In December 2007, guidelines were released by Industry Canada outlining the criteria for review of investments by state-owned enterprises (“SOEs”). The guidelines, which apply to enterprises that are owned or controlled directly or indirectly by a foreign government, state that the Minister will review the corporate governance and commercial orientation of SOEs in determining whether reviewable acquisitions of control by SOEs are of net benefit to Canada. Governance will be evaluated to determine adherence to Canadian corporate governance standards, such as commitments to transparency and disclosure, independent members of the board of directors, independent audit committees and equitable treatment of shareholders. The Minister will also assess whether the business to be acquired by the SOE will continue to have the ability to operate on a commercial basis regarding matters such as export markets, capital expenditures, and research and development.

### **National Security Review**

In March 2009, the Act was amended to incorporate a new mechanism for the review of investments by non-Canadians which may be injurious to national security. This review may be applied to any investment in a Canadian business by a non-Canadian, including investments not otherwise subject to the legislation such as minority investments.

Pursuant to the national security screening process, the Governor in Council may take any measures in respect of the investment that the Governor in Council considers advisable to protect national security, including: (a) directing the purchaser not to implement the investment; (b) authorizing the investment on

condition that the non-Canadian (i) give any written undertakings to Her Majesty in right of Canada relating to the investment that the Governor in Council considers necessary in the circumstances, or (ii) implement the investment on the terms and conditions contained in the order; or (c) requiring the purchaser to divest itself of control of the Canadian business or of its investment in the entity. In order to trigger a national security review, within 45 days of the date on which the notification or application for review has been filed and certified as complete or within 45 days of the date of closing of a transaction for which neither an application for review nor a notification is required, either (a) the Governor in Council must order a review of the transaction or (b) the Minister must issue a notice to the purchaser indicating that a review may be necessary on grounds of national security, in which case the Governor in Council has 25 days from the date of notice to order a review.

### **Undertakings and Progress Reports**

In many cases, Industry Canada (or Heritage Canada in the case of cultural businesses) will require undertakings from the investor for a period of at least three years (often five years in the case of very large, high profile investments) following implementation of the investment that will demonstrate the “net benefit” of the investment to Canada. Undertakings are generally negotiated by the investor and Industry Canada and will relate to the statutory factors outlined above. The most common areas requiring undertaking commitments from investors include Canadian participation in management, location of the headquarters for the Canadian business, employment levels, ongoing capital expenditures, and increased technological development or productivity resulting from the investor’s acquisition of control.

Once the investment has been determined to be of net benefit to Canada, the investor may proceed with its implementation. If undertakings are provided in connection with the plans for the Canadian business, the investor will be required to provide a progress report on the status of its plans and undertakings within 18 months of implementation. For cultural businesses, progress reports are usually requested by Heritage Canada on an annual basis.

### **Opinions**

Where there is uncertainty or special circumstances exist, an investor may seek an opinion from the Minister or the Director with respect to any matter of interpretation of the Act. Once an opinion is issued by Industry Canada (or Heritage Canada in the case of cultural businesses), it is binding upon the Minister and the Director for so long as the material facts upon which the opinion was based remain substantially unchanged. The opinions sought generally concern the status of an individual or entity as a Canadian (and accordingly, whether the Act applies), and the application of the Act’s provisions, including whether there are grounds for an early implementation of the investment. All information and submissions provided pursuant to the Act, or received by Industry Canada and its officials in relation to an investor or a Canadian business, are treated as privileged and confidential and may not be disclosed subject to limited exceptions, including for the purpose of administering the Act or with the consent of the parties to whom the information pertains.

### **Recent Developments**

In May 2008, the Minister, for the first time, rejected a transaction that did not raise cultural or heritage concerns. The transaction involved the proposed CDN\$1.3 billion acquisition of the information systems and

geospatial service operations of MacDonald, Dettwiler and Associates Ltd. (“MDA”) by US-based Alliant Techsystems Inc.

Since no decision was published (note that the Act was amended in 2007 to require the minister to provide reasons for a rejection), it is not certain on what basis the Minister concluded that the transaction was not likely to be of net benefit to Canada. It is likely that national security considerations were an important factor, given MDA’s role as a pioneer of what are perceived to be leading-edge Canadian space technologies, including operation of Radarsat-2, a sophisticated surveillance satellite linked to Canada’s ability to monitor possible violations of Canada’s claims of Arctic sovereignty. Moreover, considerable public concern was expressed that the proposed sale would transfer to non-Canadians significant technologies developed at the expense of the public.

In November, 2010, a proposed \$39 billion hostile take-over of Potash Corporation of Saskatchewan by the Anglo-Australian firm BHP Billiton was also rejected, following an intensive public relations campaign led by the Premier of Saskatchewan which placed significant political pressure on the minority Conservative federal government. Reasons for the decision were not provided, since BHP Billiton technically withdrew its application for review.

Undertakings are subject to “force majeure” type of exceptions but otherwise enforceable. In July 2009, the Minister brought legal proceedings against US Steel to compel it to comply with undertakings (given when it acquired Stelco in 2007) relating to employment and production at Stelco’s Canadian facility. The Minister is also seeking a penalty of \$10,000/day for each day of non-compliance.

## **Conclusion**

Foreign investment in Canada can require approval under the Act. The review process can give rise to difficult issues and may necessitate the negotiation of undertakings that affect how business is conducted for a period of time following acquisition. Fraser Milner Casgrain LLP has extensive expertise in assisting clients to navigate the requirements of the Act.



# About FMC

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