THE CANADIAN BAR ASSOCIATION
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June 16, 2020

Via email: INDU@parl.gc.ca

Ms. Sherry Romanado, M.P.
Chair, Industry, Science and Technology Committee
House of Commons
Ottawa, ON K1A 0A6

Dear Ms. Romanado:

**Re: Investment Canada Act Study – COVID-19 implications**

The Competition Law Section of the Canadian Bar Association (CBA Section) is pleased to offer its comments to the Industry, Science and Technology Committee to inform its study of the Investment Canada Act (ICA).

The CBA Section promotes a greater awareness and understanding of legal and policy issues relating to competition law and foreign investment. Its members, especially those in the Section's Foreign Investment Review Committee, have significant experience navigating the ICA, including net benefit to Canada reviews and national security reviews. As such, we believe we are well positioned to offer the Industry Committee valuable observations and insights.

**Key Conclusions**

1. The government's ability to adjust the ICA's net benefit review thresholds in response to the COVID-19 crisis may be significantly limited by Canada's international trade obligations.

2. The government has no practical need to adjust the ICA's national security review regime in response to the COVID-19 crisis, given the tremendous powers already available to the government under that regime and the April 18, 2020 policy statement[1] setting out its intention for closer scrutiny of certain investments under the ICA.

**Background**

With very limited exceptions, any foreign investor must file under the ICA whenever it acquires control of an existing Canadian business or establishes a new Canadian business. The breadth of this requirement is such that hundreds of filings are made to the Investment Review Division of Innovation, Science and Economic Development (IRD) every year. In 2018/2019 (the most recent fiscal year for which data is available), foreign investors made 962 filings under the ICA.

[1] See Policy Statement on Foreign Investment Review and COVID-19

A filing under the ICA requires the foreign investor to give details about itself, including its officers and directors, shareholders, ultimate controller and ultimate country of origin, whether it has direct or indirect state-ownership, how and from whom it finances its investment, value of its investment, all of the locations of the Canadian business in question, identity of the existing owner and number of employees of the Canadian business and a copy of the transaction agreement. This information must be certified by a director or officer of the investor.

**Key Statistics**

In relation to the 962 investments filed with IRD in the last year:[2]

- Approximately 1% (nine investments) were subject to a net benefit review on the basis that they exceeded certain financial thresholds. Such an investment may not be completed unless and until the Minister determines that it is "likely to be of net benefit to Canada". The number of investments subject to net benefit review has fallen dramatically in the past five years, primarily due to the five-fold increase in the most commonly applicable financial threshold and enshrinement of this threshold in international trade agreements. This is explained in further detail below.
- Approximately 1% (nine investments) were subject to a national security notice issued by the government. These notices are issued where the government has potential concerns on the national security implications of an investment. Once a notice is issued, an investment may not be completed unless and until the government allows it to be completed. The government may prohibit the investment outright, permit it subject to conditions, or allow it to proceed. If the investment is already completed before a national security notice is issued, the government may order a divestiture.
- Approximately 98% (over 940 investments) were subject neither to net benefit review (because they fell under the net benefit financial thresholds) nor a national security notice (because the government elected not to issue such a notice). For all these investments, the government had 45 days from the date of the filing to decide whether to issue a national security notice but declined. The IRD's Director of Investments' Annual Report[3] states that these investments "were reviewed under the multi-step national security process set out in the ICA.". This is understood to mean that the government performs an initial screen on all investments during the 45-day period after the filing is received to determine whether to issue a national security notice.

**Net Benefit Review**

Prior to 2009, the ICA did not include a national security review – the only review under the ICA was a net benefit to Canada review for transactions that exceeded the applicable financial thresholds. During this period, the number of net benefit reviews peaked at 57 annually, at a time when roughly 500 filings were made. In other words, at the peak, roughly 10% of investments filed under the ICA were subject to net benefit review. Contrasted with nine net benefit reviews (out of 962 filings) in the most recent fiscal year, the approximate proportion of investments filed under the ICA subject to net benefit review has fallen from 10% to 1% over a ten-year period.

This decline has been primarily caused by tremendous increases in the net benefit review financial thresholds. More particularly, in the five-year period between early 2015 and early 2020, the most commonly applicable net benefit review threshold increased from $369 million in book asset value to $1.613 billion in enterprise value.

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2 We excluded statistics on cultural businesses as these businesses are unique. Also, the number of these investments is negligible and would have no impact on the present analysis.

3 See Annual Report for 2018-2019

By way of background the 2008 Competition Policy Review Panel report, *Compete to Win*,[4] contained 65 recommendations, one of which was to increase the ICA net benefit review threshold to $1 billion in enterprise value. No change was made until seven years later in April 2015, when the most commonly applicable threshold was increased to $600 million in enterprise value with further increases in quick succession since then.

The tables below compares the net benefit review thresholds in 2015 and 2020 (ignoring the exceedingly rare case of an investment by an investor who is not a member of the WTO). We also list the national security threshold for a complete picture.

| **Transaction Feature** | **2015 Net Benefit Threshold** |
|---|---|
| WTO Investor (includes trade agreement investors, a category which did not yet exist) | $369 million book asset value |
| Cultural Business | $5 million or $50 million book asset value (depending on facts) |

| **Transaction Feature** | **2020 Net Benefit Threshold** |
|---|---|
| Trade Agreement Investor (examples include USA, Mexico, all EU members, Australia, Japan, Korea, Chile) | $1.613 billion enterprise value |
| WTO Investor (examples include China, Russia, India, Brazil) | $1.075 billion enterprise value |
| State-Owned Investor (from virtually any country) | $428 million book asset value |
| Cultural Business | $5 million or $50 million book asset value (depending on facts) |

| **Transaction Feature** | **National Security Threshold (2009 to present)** |
|---|---|
| Any non-Canadian investor | $0 |

The net benefit threshold increases above occurred after the national security review regime was introduced in 2009. As the government implemented even higher net benefit thresholds, it did so knowing that it retained national security jurisdiction over any investment in sensitive and critical sectors that would no longer be subject to net benefit review, such that if an investment was particularly sensitive or strategic it could elect to review it under the national security provisions. As such, the government had a degree of "protection" when implementing the higher net benefit thresholds, via the national security review regime.

The *National Security Guidelines* under the ICA state that when assessing proposed or implemented investments under the national security provision, the Minister or Governor in Council may consider (but is not limited to) the following factors:

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

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4 See Compete to Win (June 2008)

- Involvement in the research, manufacture or sale of goods/technology identified in Section 35 of the *Defence Production Act*;
- Potential impact of the investment on the security of Canada's critical infrastructure. Critical infrastructure refers to processes, systems, facilities, technologies, networks, assets and services essential to the health, safety, security or economic well-being of Canadians and the effective functioning of government;
- 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;
- Potential of the investment to enable foreign surveillance or espionage;
- Potential of the investment to hinder current or future intelligence or law enforcement operations;
- Potential impact of the investment on Canada's international interests, including foreign relationships; and,
- Potential of the investment to involve or facilitate the activities of illicit actors, such as terrorists, terrorist organizations or organized crime.

**Net Benefit Review – Trade Agreements**

It appears that at least some of the increases in the net benefit review thresholds cannot be reduced because they are enshrined in Canada's free trade agreements. We suggest that the Committee confirm this with trade agreement experts in the federal government. This may save the Committee significant time and resources.

Put differently, and while we understand that the Committee intends to study "whether the current *Investment Canada Act* valuation thresholds are adequate to trigger a net benefit review given the potential extreme devaluation of companies within strategic Canadian industries," the government's decision to include specific ICA thresholds in trade agreements appears to limit its ability to meaningfully reduce the net benefit thresholds.

Canada may have limited ability to respond to a devaluation of companies in sensitive and critical sectors under the net benefit provisions by lowering the net benefit thresholds (but could respond under the national security provisions). For example:

Canada-United States-Mexico Agreement (CUSMA)

- Paragraph 3 of Reservation I-C-1 in Annex 1-Schedule of Canada sets a $1.5 billion threshold for trade agreement investors (this includes the United States and Mexico), adjusted in accordance with the applicable methodology. (This methodology leads to the current $1.613 billion threshold).
- Paragraph 1 sets a $1.0 billion threshold for WTO investors, adjusted in accordance with the applicable methodology. (This methodology leads to the current $1.075 billion threshold).
- Paragraph 5 sets a $398 million threshold for state-owned investors from any country, adjusted in accordance with the applicable methodology. (This methodology leads to the current $428 million threshold).

Comprehensive Economic and Trade Agreement with the EU (CETA)

- Paragraph 1 of Reservation I-C-1 in Annex 1 of the Schedule of Canada-Federal, sets a $1.5 billion threshold for EU investors, adjusted in accordance with the applicable methodology. (This methodology leads to the current $1.613 billion threshold).

- Paragraph 3 similarly sets a $369 million threshold for state-owned investors from any country, adjusted in accordance with the applicable methodology. (This methodology leads to the current $428 million threshold).

Comprehensive and Progressive Agreement for Trans-Pacific Partnership (TPP)

- Paragraph 1 in Annex 1- Schedule of Canada in the ICA section sets a $1.5 billion threshold for investors of an original signatory for which the TPP has entered into force, adjusted in accordance with the applicable methodology. (This methodology leads to the current $1.613 billion threshold).
- Paragraph 3 similarly sets a $369 million threshold for state-owned investors from any country, adjusted in accordance with the applicable methodology. (This methodology leads to the current $428 million threshold).

WTO, under the General Agreement on Trade in Services of 1994 (WTO-GATS)

- Page 4 of Canada's Schedule of Specific Commitments sets a $153 million threshold for 1994 to be adjusted annually for inflation. It also states that the threshold is to be established and published in the Canada Gazette. This inflation-based methodology would have led to a $428 million threshold for WTO investors in 2020, although the government increased this threshold to $1 billion and then to $1.075 billion for WTO investors, which figure is published in the Canada Gazette. It also appears to have enshrined this threshold in CUSMA. The $428 million threshold applies to state-owned investors.

The Canadian government's ability to apply lower net benefit review thresholds may be limited given its international trade obligations. We recommend that the Committee confirm if this is the case with trade agreement experts.

**National Security Review**

The government has extraordinary powers under the national security reviews provisions of the ICA. In contrast to the net benefit review provisions, which allowed the review of only nine (out of 962 investments) in the last fiscal year, it was in the government's discretion to issue a national security notice for any of the 962 investments.

Our understanding is that the government did conduct an initial national security screen of all these investments, issued a national security notice where it had concerns, and then prohibited those investments where its concerns could not be assuaged. In addition, the government's extensive powers under the national security review provisions extend beyond acquisitions of control even to minority investments.

In response to the current crisis, the government issued a policy statement on April 18, 2020 stating that it will pay particular attention to foreign direct investments of any value in Canadian businesses related to public health or to the supply of critical goods and services. The government stated that it will also subject all foreign investments by state-owned investors (or investors with close ties to foreign governments) to enhanced scrutiny under the ICA, which may include requiring additional information from investors and extending review timelines.

Given the government's extensive powers under the national security review provisions and the April 18 policy statement, we do not believe that any changes to enhance the government's national security review powers are necessary or desirable.

For example, we understand that the Committee will study "whether Canada should place a temporary moratorium on acquisitions from state owned enterprises of authoritarian countries". Under the national security review provisions, the government can already review and block any acquisition by any enterprise (state-owned or not) from any country (authoritarian or not).

A policy as contemplated above would only limit the government's ability to make case-by-case assessments of each investment and potentially exacerbate international tensions. In addition, the government's policy statement of April 18 already clarifies that investments by state-owned enterprises will be subject to closer scrutiny, which may result in certain transactions being prohibited if the government so determines.

**Key Conclusions**

Our primary conclusions are:

1. The government's ability to adjust the ICA's net benefit review thresholds in response to the COVID-19 crisis may be significantly limited by Canada's international trade obligations.

2. There is likely no need to adjust the ICA's national security review regime in response to the COVID-19 crisis, given the tremendous powers already available to the government under that regime and the April 18 policy statement.

That said, given the IRD's increased workload arising from the closer scrutiny of investments, the government should consider whether the IRD and its sister agencies are adequately funded to ensure net benefit and national security reviews are conducted rapidly and efficiently.

**Other Observations**

We also considered the scenario where the Committee concludes either that: (i) it would not be inconsistent with Canada's international trade obligations to impose lower net benefit review thresholds either on a country-specific basis or on a sector-specific basis; or (ii) it desires, as a matter of policy, and without amending the ICA or its regulations, to impose a "moratorium" policy on investments from certain countries or in certain sectors (as was done in December 2012 when the government issued a policy stating that acquisitions of control of oil sands businesses by state-owned enterprises would not be found to be of net benefit to Canada, assuming they exceeded the relevant thresholds).

There is no consensus among members of the CBA Section on this scenario. At a minimum, great care would be required to clearly define sectors or countries where different thresholds or some sort of temporary "moratorium" would apply, to avoid ambiguities or create uncertainty on the application of the ICA. Otherwise, a chilling effect on entirely benign investments could occur, precisely at a time when Canada is facing severe economic challenges.

In addition, as the COVID-19 crisis eases, the change could become irrelevant or even counter-productive. Above all, there is a strong argument that the national security review provisions of the ICA already address the problem that the Committee has identified, in the sense that the government already has jurisdiction to review and prohibit any investment in Canada in sensitive or critical sectors by any foreign investor. As such, a policy specific to particular sectors or particular countries would not give the government any power that it does not already have.

The *National Security Guidelines* under the ICA identify broad sectors of Canadian industry that are more likely to attract close scrutiny from a national security perspective. It may be the Committee's view that existing national security provisions should be applied to prohibit more transactions. We

do not have a consensus on this question, and we believe it is ultimately a question for national security experts.

Some of our members expressed the view that it may be appropriate to require state-owned enterprises to submit their ICA filings on a pre-closing basis. The government currently encourages state-owned enterprises to file on a pre-closing basis but there is no legal requirement to do so (other than in the very rare case where the net benefit thresholds are exceeded).

Nevertheless, many state-owned enterprises currently file on a pre-closing basis to avoid the scenario where the government issues a national security notice post-closing and then potentially requires that the Canadian business be divested. A requirement to file on a pre-closing basis would ensure that if the government had unresolved national security concerns about a state-owned enterprise investment, it could prevent the investment from occurring rather than requiring that it be unwound after it had closed. No consensus was reached on this point, but it may be a matter for the Committee to consider further.

We appreciate the opportunity to make this submission and would be pleased to assist the Committee as we can.

Yours very truly,

*(original letter signed by Marc-Andre O'Rourke for Huy Anh Do)*

Huy Anh Do
Chair, Competition Law Section