

Liberalizing the *Investment Canada Act*: Striking the Right Balance Between Investment and Economic Security

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I. INTRODUCTION

Canada thinks of itself as a country open to foreign direct investment (“FDI”).¹ The federal government has created several programmes and organizations, as well as entered into numerous international agreements, to increase the country’s attractiveness as an investment destination.² At the same time, territorial, provincial, and municipal governments compete aggressively to attract FDI. Sub-national governments offer investors a number of incentives to invest locally, including tax holidays,

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¹ See J Anthony VanDuzer, “The Legal Protection of Foreign Investment” in Wenhua Shan, ed, *The Legal Protection of Foreign Investment: A Comparative Study* (Oxford: Hart Publishing, 2012) 173 at 174 [VanDuzer, “Legal Protection”].

² Most recently, Canada launched “Invest in Canada”, a new federal organization dedicated solely to attracting global investment in Canada. See Canada, Global Affairs Canada, *Government of Canada launches Invest in Canada to attract global investment and create jobs*, News Release (Ottawa: GAC, 2018). In terms of international agreements, Canada is a member of the World Trade Organization and is subject to obligations related to investment, including the General Agreement on Trade in Services (“GATS”) and the Agreement on Trade-Related Investment Measures (“TRIMS”). Canada has also signed and implemented a number of bilateral and regional trade agreements that provide foreign investors with rights in Canada, including the NAFTA. In addition to trade agreements, Canada is a party to a large number of double taxation agreements to promote investment. See VanDuzer, “Legal Protection”, *supra* note 1 at 174-175.

ow-cost land and energy, as well as other inducements to reduce investors' cost of doing business.³

In spite of such initiatives, Canada is routinely criticized as being prejudicial to foreign investors, especially State-Owned Enterprises ("SOEs"). The federal *Investment Canada Act* ("ICA"),⁴ the cornerstone of Canada's regime for reviewing foreign investment, is often the focus of such censure.⁵ Canada ignores criticisms of the ICA at its peril. As a trade-exposed nation with a competitive advantage in capital-intensive natural resource industries, Canada is economically dependent on foreign investment and must be cognizant of how the ICA impacts foreign investors' perception of Canada.⁶

This paper argues that the ICA fails to strike the right balance between encouraging foreign investment and protecting Canada's economic security. It argues that the ICA's economic investment review, the so-called "net benefit test", should be replaced with a "national interest" standard to liberalize the Act.

II. OVERVIEW

The first part of this paper defines FDI, analyzes its benefits, and discusses why countries restrict foreign investment. In part two, the ICA's net benefit test will be reviewed. Part three will survey and comment on literature critiquing that test. Part four will discuss the shortcomings of the federal government's most recent efforts to reform the ICA. In part five, the conclusion will describe how the Act could be amended in a responsible manner to increase Canada's openness to foreign capital. Part 1: The Benefits and Drawbacks of Foreign Investment

³ *Ibid.*

⁴ *Investment Canada Act*, RSC, 1985, c 28 (1st supp) [ICA].

⁵ J Anthony VanDuzer, "Mixed Signals: What Recent Developments Tell Us About Canadian Foreign Investment Policy" (2010) 10 *Asper Rev Intl Business & Trade L* 247 at 248 [VanDuzer, "Mixed Signals"].

⁶ The stock of FDI in Canada in 2009 was \$549 billion, representing approximately 43% of Canadian Gross Domestic Product for that year. See VanDuzer, "Legal Protection", *supra* note 1 at 174.

III. THE BENEFITS AND DRAWBACKS OF FOREIGN INVESTMENT

A. FDI: What is it?

Foreign direct investment is an investment in an enterprise located in a “host country”; a country distinct from that in which the investor resides.⁷ FDI reflects the objective of establishing a long-term interest in the host country and a significant degree of control over the management of the investment enterprise.⁸

B. FDI Provides a Number of Economic Advantages

FDI is generally beneficial to host countries. At the macroeconomic level, foreign investment, whether through the acquisition of an existing company or the establishment of a “greenfield” business, typically results in higher living standards by promoting necessary elements of long-term economic growth.⁹

For instance, when a foreign investor acquires a domestic business, the investor may implement innovative technologies or adopt new management practices at that business. At the firm level, these investments may, and generally do, contribute to higher labour productivity.¹⁰ The acquisition by the foreign investor may also inject capital into the business. Increased capital may

⁷ See Michael Trebilcock, Robert Howse and Antonia Eliason, *The Regulation of International Trade*, 4th ed (New York: Routledge, 2013) at 566 See also Organisation for Economic Co-operation and Development, *OECD Benchmark Definition of Foreign Direct Investment*, Report (Paris, OECD, 2008) for a formal definition of FDI.

⁸ See Trebilcock, Howse & Eliason, *supra* note 7 at 566. FDI is distinguished from portfolio investment by the duration of the investment and the control it confers on the investor over the investment enterprise. A portfolio investment is an investment, typically in the form of securities of a business, held by a foreign investor solely for the purpose of earning a financial return. In this sense, portfolio investments differ from FDI because they are passive and potentially short-term.

⁹ See Robert M Solow, “A Contribution to the Theory of Economic Growth” (1956) 70 *Quarterly J Economics* 65 at 65-94; See Canada, Library of Parliament, *The Foreign Investment Review Process in Canada*, prepared by Mathieu Frigon, Publication No. 2011-42-E (Ottawa, LP, 2014) at 1.

¹⁰ See A Edward Safarian, “The Canadian Policy Response to Sovereign Direct Investment,” in Karl P Sauvart, Lisa E Sachs & Wouter PF Schmit Jongbloed, eds, *Sovereign Investment: Concerns and Policy Reactions* (New York: Oxford University Press, 2011) 431; Philippe Bergevin & Daniel Schwanen, “Reforming the Investment Canada Act: Walk More Softly, Carry a Bigger Stick” (2011) C.D. Howe Institute, *Commentary* no 337 at 2.

fuel the company's growth, encouraging economies of scale and enhanced competitiveness.¹¹ A number of studies support the proposition that FDI drives greater business productivity and efficiency. Statistics Canada has found that foreign-controlled firms in Canada tend to be larger, have higher labour productivity, innovate more frequently, and are more likely to have a research and development division than Canadian-controlled businesses.¹²

FDI also tends to have broader spill-over effects. Foreign investment often increases demand for local inputs, spurring the growth of domestic suppliers and new jobs.¹³ FDI may also enhance the competitiveness of domestic firms by allowing them to gain access to a larger variety of newer and higher-quality imported inputs through creating new linkages to global markets.¹⁴ Further, as domestic workers at foreign-controlled firms change jobs or start their own businesses, they may disseminate superior business practices and technologies throughout the national economy, improving domestic productivity.¹⁵ Customers also tend to benefit from foreign investment. Enhanced business efficiency and competitiveness typically drives down the costs of goods and services or enhances their quality, increasing consumers' purchasing power and utility. These are but a few of FDI's well-documented advantages.¹⁶

¹¹ See Bergevin & Schwanen, *supra* note 10 at 2.

¹² See Canada, Statistics Canada, *Global Links: Multinationals in Canada: An Overview of Research at Statistics Canada*, prepared by John R Baldwin & Guy Gellatly, Cat. 11-662-MIE - No. 014 (Ottawa: SC, 2007) at 7-9 [Statistics Canada, "Global Links"]. Bergevin and Schwanen also note that foreign-controlled firms, even when controlling for their generally larger size, often outperform Canadian-controlled businesses. See Bergevin & Schwanen, *supra* note 10 at 2.

¹³ See Hiau Looi Kee, "Local Intermediate Inputs and the Shared Supplier Spillovers of Foreign Direct Investment" *J of Development Economics*; Jozef Konings, "The Effects of Foreign Direct Investment on Domestic Firms" (2001) 9:3 *Economics of Transition*, 619-633.

¹⁴ See Goldberg, Pinelopi K, Amit Kumar Khandelwal, Nina Pavcnik, & Petia Topalova. "Imported Intermediate Inputs and Domestic Product Growth: Evidence from India" (2010) *Quarterly J of Economics*.

¹⁵ S Lall, "Monopolistic Advantages and Foreign Investment by UK Manufacturing Industries" (1980) 32:1 *Oxford Economic Papers* 101 at 102-22.

¹⁶ There is a considerable amount of literature on the benefits of FDI. Another common benefit of FDI is that foreign-controlled businesses typically provide more favourable compensation to employees. For instance, Statistics Canada has found that foreign-owned manufacturing firms pay their employees significantly more than Canadian-controlled businesses. See Statistics Canada, "Global Links", *supra* note 12. Another commonly cited advantage is that FDI fuels competition. For instance, foreign entrants into a market may

C. Countries Restrict FDI for Economic, Security, and Cultural Reasons

Despite its potential benefits, foreign investment has received “bad press” in Canada.¹⁷ Not only have the benefits of FDI been questioned, but many concerns with foreign investment have been raised.¹⁸ These concerns are often linked to sovereignty. It is argued that foreign ownership of a country’s businesses may lead to a number of economic harms, including: (1) the host country losing control over its economy, (2) the host country having difficulty subjecting foreign investors to the host country’s economic laws and regulations, and (3) foreign-controlled businesses becoming a conduit for foreign economic interference within the host country. Other concerns include harms to the host country’s (4) national security and (5) cultural distinctiveness.

1. FDI: Diminishing Control and Influence Over the Domestic Economy

One of the most cited concerns associated with FDI is that foreign ownership of domestic businesses will reduce Canada’s control and influence over the national economy. In its simplest form, detractors of foreign

promote competition between the investor and domestic incumbents. It is also argued that FDI creates incentives for domestic suppliers to adopt better practices in order to be “compatible” with the foreign-controlled company so as to win its business. This may drive domestic suppliers’ productivity and competitiveness. See Bergevin & Schwanen, *supra* note 10 at 2; Beata Smarzynska Javorcik, “Does Foreign Direct Investment Increase the Productivity of Domestic Firms? In Search of Spillover Through Backward Linkages” (2004) 94:3 *American Economic Review* 605 at 605-627.

¹⁷ See generally “For Sale: Corporate Canada”, *The Globe and Mail* (9 September 2006); Gordon Pitts, “Manulife CEO Issues a Call to Arms”, *The Globe and Mail* (19 January 2007).

¹⁸ A number of scholars have criticized the proposition that FDI contributes to productivity-enhancing technology transfers to host countries. These scholars point out that the correlation between FDI and technology transfers is weak or even negative. See e.g. K Maskus, “Encouraging International Technology Transfer” (2003) United Nations Conference on Trade and Development & International Centre for Trade and Sustainable Development, Issue Paper 7 at 26-27. Other scholars have argued that FDI “crowds out” domestic businesses, reducing market opportunities for domestic firms and therefore harming host countries. See e.g. Brian J Aitken & Ann E Harrison, “Do Domestic Firms Benefit from Direct Foreign Investment? Evidence from Venezuela” (1999) 89:3 *American Economic Review* 605 at 605-618; Simeon Djankov & Bernard Hoekman. “Foreign Investment and Productivity Growth in Czech Enterprises” (2000) 14:1 *World Bank Economic Review* 49 at 49-64.

investment fear that FDI will transform Canada into a “branch plant”, an economy dominated by foreign ownership and low-value activities.¹⁹ Critics argue that foreign investors acquiring Canadian companies will shift their management and value-added activities to the investors’ home jurisdictions, resulting in a decline or the “hollowing out” of corporate Canada.²⁰

These fears have been persistent. They initially arose in the 1960s and 1970s due to growing American ownership of Canadian businesses and have been recently fuelled by foreign acquisitions in Canada’s energy industry.²¹ The “hollowing out” of corporate Canada was consistently raised during the Competition Policy Review Panel’s consultations and in the Panel’s seminal report on Canadian competitiveness in 2008.²² Many academics, business leaders, unions, and other stakeholders told the Panel “that Canadian businesses [were] being swallowed by foreign competitors in an era of global consolidation.”²³ The Panel stated: “[it] has been argued that, relative to the size of its domestic capital market, Canada has been both the biggest net seller of companies in the world and the easiest country in which to acquire firms,” diminishing Canadians’ control and influence over the economy.²⁴

These concerns are elevated in Canada’s oil sands. Opponents of FDI fear that raw resources will be extracted and exported for processing and final consumption in the foreign investor’s home jurisdiction to the detriment of Canadian processors and consumers.²⁵ As a result, critics contend that Canada requires special rules preventing foreign investors from acquiring or “locking-up” oil sand businesses.²⁶

¹⁹ See Library of Parliament, *supra* note 9 at 1.

²⁰ *Ibid.*

²¹ See Oliver Borger, Emily Rix & Lorne Salzman, “Foreign Investment Screening Under Canada’s Investment Canada Act” (Paper delivered at the Canada Bar Association Annual Fall Conference on Competition Law, September 2010) at 4.

²² Canada established the Competition Policy Review Panel in 2008 to examine how Canada could become a more attractive destination for talent, investment, and innovation. The Panel, chaired by L.R. Wilson, put forward a number of recommendations on how the ICA could be reformed to increase foreign investment in Canada. See Canada, Industry Canada, “Compete to Win” *Final Report*, Competition Policy Review Panel (Ottawa: Industry Canada, 2008) at 15-16 [Competition Policy Review Panel, “Compete to Win”].

²³ *Ibid* at 16.

²⁴ *Ibid.*

²⁵ See Library of Parliament, *supra* note 9 at 7-9.

²⁶ *Ibid.* To a limited extent, Canada has responded to these concerns by restricting foreign

2. *FDI: Inadequate Regulatory Control*

Countries may also limit foreign investment to ensure investors' compliance with local laws. This concern is based on the notion that the foreign investor is "a kind of power unto itself", able to avoid the application of domestic laws to its operations within a host country "through the global diffusion of its activities."²⁷ While this concern may be less of an issue in Canada, where regulatory laws and enforcement mechanisms are strong, concerns persist.²⁸ Canada may have difficulty regulating foreign investor's domestic activities "where the bulk of the firm's assets and much of the information about [its] activities and decision-making is located abroad."²⁹

3. *FDI: Foreign Economic Interference*

Another major concern associated with FDI is that foreign-controlled Canadian businesses may be operated to drive the agenda of the investor's home jurisdiction, causing harmful economic distortions.³⁰ Critics of FDI argue that these concerns are elevated for SOE investors because of their inextricable ties with foreign governments. A key concern is that state-controlled firms may have an unwarranted competitive advantage as a result of government financial support.³¹ This may undermine healthy competition in an industry, forcing Canadian-controlled domestic firms to exit the marketplace.³² The unsuccessful proposal by state-owned China

SOEs' acquisitions in the oil sands. See generally Canada, Industry Canada, Statement Regarding Investment by Foreign State-Owned Enterprises, Guidelines, (Ottawa: Industry Canada, 2012) [Industry Canada, "SOE Statement"].

²⁷ See Trebilcock, Howse & Eliason, *supra* note 7 at 577.

²⁸ This may be a particular problem in developing countries where regulatory laws and their enforcement is weak. In such circumstances, FDI may have a number of negative spill-over effects within the host country, including impacts on the environment, human rights, labour rights, and indigenous rights. *Ibid* at 579-580.

²⁹ *Ibid* at 577.

³⁰ Safarian, *supra* note 10.

³¹ See Yuri Shima, "The Policy Landscape for International Investment by Government-Controlled Investors: A Fact-Finding Survey" (2015) Organisation for Economic Co-operation and Development Working Paper 2015/01 at 7.

³² Canada has responded to this concern. The ICA has sought to limit investments from SOEs who do not operate according to commercial principles. See generally Canada, Industry Canada, *Guidelines – Investment by state-owned enterprises – Net benefit assessment*, Guidelines revised 2012 (Ottawa: Industry Canada, 2012) [Industry Canada, "SOE Guidelines"].

Communications Construction Co. Ltd. (“CCCC”) to acquire control of Aecon Group Inc. (“Aecon”), a domestic construction and engineering business, is illustrative. Domestic competitors of Aecon, including; PCL Constructors Inc., Ledcor Group Ltd., and Graham Group Ltd., as well as the Canadian Construction Association, an industry group, protested the proposed transaction. They argued that if the transaction proceeded, Aecon “would easily be able to underprice domestic rivals on infrastructure projects in Canada” due to CCCC’s “easy access to Chinese government money”.³³

A related concern is that foreign investment will erode Canadian sovereignty as a result of the extraterritorial application of foreign laws to foreign-controlled Canadian businesses. The actions of Canada’s southern neighbor, the United States, provides an example. In the past, the United States has attempted to prevent subsidiaries of American firms operating outside of the United States, such as Walmart Canada Inc., from acquiring products from Cuba, a country embargoed by American import and export control laws.³⁴ Besides offending Canada’s sensitive national pride, the extraterritorial application of foreign laws in Canada may frustrate Canadian regulatory efforts.

4. FDI: National Security Concerns

Foreign investment may also raise national security concerns. Based on the “realist” notion that “no state should rely on others to furnish the weapons needed for its own defense,”³⁵ critics of FDI argue that investors’ ability to acquire Canadian businesses in the defense sector must be curtailed for

³³ Robert Fife & Steven Chase, “Construction group warns of price-cutting if Aecon sold to China”, *The Globe and Mail* (5 February 2018); See also Andrew Willis, Jeffrey Jones and Steven Chase, “Aecon rivals urge Ottawa to block Chinese takeover”, *The Globe and Mail* (16 January 2018), online: <theglobeandmail.com/report-on-business/aecon-rivals-urge-ottawa-to-block-foreign-takeover/article37631937/> [perma.cc/47S5-CWD3]. Aecon has rejected accusations that it would receive subsidies from Beijing if the transaction proceeded. According to an article in the *Globe and Mail*, Aecon stated that any subsidies that CCCC receives “are related to specific research and development projects in China” and that CCCC “does not receive government subsidies for its international activities.” See Robert Fife & Steven Chase, “Aecon raises red flag about opponent of its sale to Chinese state-owned firm”, *The Globe and Mail* (9 February 2018), online: <theglobeandmail.com/news/politics/aecon-raises-red-flag-about-opponent-of-its-sale-to-chinese-state-owned-firm/article37930765/> [perma.cc/CMG8-BXP8].

³⁴ See generally Howard Schneider, “Canada, U.S. Wager Diplomatic Capital in a Higher-Stakes Pajama Game”, *The Washington Post* (14 March 1997).

³⁵ *Ibid* at 575.

Canada to maintain control over domestic providers of arms. Restrictions on investment are warranted, they argue, because of foreign investors' potentially close relationship with their home jurisdiction's government. Where foreign investors are government-owned, have present or past government officials serving in management, or are the recipients of government subsidies or procurement contracts, there may be a legitimate basis³⁶ to fear that an investor's government will exercise influence over the investor so as to gain access to, or control over, the goods and services of the investor's Canadian business.³⁷

National security concerns have long been used to justify measures limiting foreign investment in Canada. In 2009, the ICA was amended to formalize Canada's review process for investments that may be injurious to Canada's national security.³⁸ The proposed acquisition of ITF Technologies Inc. ("ITF"), a Canadian information company, by O-Net Communications Ltd. ("O-Net") provides an example of an investment rejected on these grounds. In 2015, the Harper government disallowed the transaction fearing that O-Net, controlled by a subsidiary of state-owned China Electronics Corporation, would pass on ITF's proprietary technology to the Chinese military.³⁹

³⁶ One of the key issues with the national security argument for restricting investment is that it is often extended far beyond the case of very sensitive defense industries to sectors that only have an incidental affect upon national security. A prime example of how far the national security argument can be stretched to block a transaction is Canada's rejection of a greenfield investment by Beida Jade Bird Group, a Chinese company. Beida Jade Bird Group announced plans to build a factory in Québec to manufacture fire-alarm systems for the Chinese market. However, the Canadian government disallowed the investment fearing that the investment, located two kilometers from the headquarters of the Canadian Space Agency, would jeopardize Canada's national security. While the investment itself did not represent a risk to national security, the location of the investment next to a sensitive installation was sufficient to invoke the national security argument. See generally Jeff Gray, "Ottawa's 'national security' review a warning to foreign investors", *The Globe and Mail* (1 July 2015), online: <theglobeandmail.com/report-on-business/industry-news/the-law-page/ottawas-national-security-review-a-warning-to-foreign-investors/article25219593/> [perma.cc/C2J2-8VJ9].

³⁷ *Ibid*; VanDuzer, "Mixed Signals", *supra* note 5 at 251; Debra P Steger, "State Capitalism: Do We Need Controls?" (2008) 50 *Can-Asian Commentary* 1 at 2.

³⁸ See generally Canada, Innovation, Science and Economic Development Canada, *Guidelines on the National Security Review of Investments*, Guidelines (Ottawa: ISED, 2016).

³⁹ The transaction was subsequently approved under the Trudeau government. See Peter Franklyn & Jaime Auron, "Clearance for previously blocked investment suggests continued trend of flexibility in national security review", *Osler, Hoskin & Harcourt LLP* (4

5. FDI: Protecting Cultural Distinctiveness

Finally, countries may restrict FDI in order to protect their unique cultural heritage. Investment may be limited to prevent foreign investors, especially multinational businesses and the “global brand culture” which they create, from “suppress[ing]...the market [for] local creativity and difference”.⁴⁰ The cultural rationale for restricting foreign investment is particularly relevant in Canada given the country’s proximity to the United States, a global leader in cultural industries, such as music, film, and television.⁴¹ Restricting FDI may help protect a country’s cultural distinctiveness by propping up domestically-owned cultural businesses.⁴²

IV. THE INVESTMENT CANADA ACT: AN OVERVIEW

A. The Purpose of the ICA

Despite concerns with foreign investment, there is a notable level of consensus in Canada that FDI is beneficial on a net-basis. In response, Canada has sought to regulate FDI through the ICA in order to manage its effects. The ICA, which provides a framework for the notification and review of foreign investment, strikes a particular balance between encouraging foreign investment and protecting Canada’s economic security. This “balancing act” is reflected in the statutory purpose of the Act, which reads:

Recognizing that increased capital and technology benefits Canada...the purposes of this Act are to provide for the review of significant investments in Canada by non-

April 2017), online: <osler.com/en/resources/cross-border/2017/clearance-for-previously-blocked-investment-sugges> [perma.cc/9C8L-CDT2]; Wendy Walker, “Back to the drawing board: Canadian Government divestiture order in national security case set aside and new review to take place”, *Dentons Canada LLP* (16 November 2016), online: <dentons.com/en/insights/alerts/2016/november/17/canadian-government-divestiture-order-in-national-security-case-set-aside> [perma.cc/76VN-5GZ7].

⁴⁰ See Trebilcock, Howse & Eliason, *supra* note 7 at 579, citing Naomi Klein *NO LOGO: Taking Aim at the Brand Bullies* (New York: Picador, 1999).

⁴¹ The argument for restricting FDI in cultural sectors to preserve a country’s unique culture has faced significant criticism. For instance, Trebilcock, Howse and Eliason argue that “shutting the door to foreign investment will not create the resources to preserve and enhance national and local culture: shaping how foreign investors behave, through both voluntary and regulatory approaches is the better strategy.” See Trebilcock, Howse & Eliason, *supra* note 7 at 579.

⁴² The ICA provides special rules for the acquisition of control of Canadian cultural businesses. These rules have the effect of limiting foreign acquisitions in cultural industries.

Canadians in a manner that encourages investment, economic growth and employment opportunities in Canada.⁴³

B. A Shifting Balance

Canada's attempt to balance foreign investment with the country's economic security has shifted over time, generally in favour of greater openness to foreign capital. Indeed, the ICA was enacted to replace the far more restrictive *Foreign Investment Review Act* ("FIRA").⁴⁴ The FIRA, enacted in 1973, was aimed at restricting foreign investment in Canada after growing American ownership of Canadian businesses throughout the 1950s and 1960s.⁴⁵ Under the FIRA, any acquisition of a Canadian business by a foreign investor was reviewable and subject to the Governor in Council's approval.⁴⁶ Any investment failing to meet the statutory threshold for approval – a "significant benefit" to Canada – could be disallowed.⁴⁷

In 1985, the Mulroney government, facing criticism from investors and their governments, repealed and replaced the FIRA with the ICA.⁴⁸ The ICA, while closely modeled on its predecessor, narrowed the scope of foreign investment review and struck a new balance between FDI and economic security, "reposition[ing] Canada as a jurisdiction receptive to foreign investment."⁴⁹ The ICA reduced government oversight of foreign investment by, amongst other things, "raising review thresholds [for the application of the Act], changing the statutory review threshold from that of a 'significant benefit'

⁴³ See ICA, *supra* note 4, s 2.

⁴⁴ Library of Parliament, *supra* note 9 at 1.

⁴⁵ Robert Sroka, "Friends with Net Benefits: The Investment Canada Act and State-Owned Enterprises" (2017) 17 *Asper Rev Intl Business & Trade L* 181 at 183; Chrysten E Perry, Christopher W Nixon, Susan M Hutton, Frederick Erickson & Glenn Cameron, "As Foreign Investment Leaves, Canadian Ownership Grows", *Stikeman Elliott* (27 September 2017). Even today, American investment in Canada remains high. Approximately 53% of all FDI in Canada is American. See VanDuzer, "Legal Protection", *supra* note 1 at 174.

⁴⁶ Library of Parliament, *supra* note 9 at 1.

⁴⁷ VanDuzer, "Legal Protection", *supra* note 1 at 234.

⁴⁸ The United States was especially critical of the FIRA. The United States argued that acquisitions by American investors were being deliberately blocked in favour of Canadian acquirers. Americans also claimed that where transactions were approved, the Canadian government imposed excessive undertaking requirements on the investor as a condition of permitting the deal to close. See Borger, Rix & Salzman, *supra* note 21 at 4-6.

⁴⁹ VanDuzer, "Legal Protection", *supra* note 1 at 235.

to one of a ‘net benefit’... and establishing stricter time limits for reviews”.⁵⁰ Liberalization fueled a wave of foreign investment in Canada.⁵¹

More recently, Canada has taken a number of steps to recalibrate the ICA to enhance the country’s economic security. The introduction of special investment rules for SOE investors in 2007 serves as an example. This paper argues that these initiatives have come at the cost of encouraging investment in Canada. It also argues that the ICA should be rebalanced in favour of greater liberalization by replacing the net benefit test. Before making the case in favour of this, an overview and critique of the test will first be performed.

C. The Scheme of the Investment Canada Act

The ICA, administered primarily by the Minister of Innovation, Science, and Economic Development (“Minister”),⁵² authorizes Canada to assess proposed foreign investments to determine whether an investment is of a “net benefit to Canada” or “injurious to Canada’s national security”.⁵³ This paper considers the merits of the ICA’s economic or “net benefit” screen. Under this review, the ICA provides for the notification, and in limited circumstances, the economic assessment of foreign investments.⁵⁴

D. The ICA’s Notification Requirement

An investment by a “non-Canadian”⁵⁵ will fall within the ambit of the ICA’s notification requirement if the investor establishes a new Canadian business or directly or indirectly acquires control of an existing Canadian business.⁵⁶ The ICA contains detailed rules for determining when control of

⁵⁰ Competition Policy Review Panel, “Compete to Win”, *supra* note 22 at 28; See also VanDuzer, “Legal Protection”, *supra* note 1 at 234; Sroka, *supra* note 45 at 17.

⁵¹ Library of Parliament, *supra* note 9 at 1-2.

⁵² A proposed acquisition of control involving a Canadian “cultural business” is reviewed by the Minister of Canadian Heritage and is assessed against the specific cultural business policies of the Department of Canadian Heritage.

⁵³ See ICA, *supra* note 4, ss 4, 5 for the Minister’s duties and powers. *Ibid*, Part IV, Part IV.1.

⁵⁴ *Ibid*, Part III and IV.

⁵⁵ A “Non-Canadian” is an entity that is not a “Canadian.” A “Canadian” is a Canadian citizen, resident, government or Canadian controlled-entity. A “Canadian Business” is a business carried on in Canada that has its place of business in Canada, employees employed in Canada in connection with the business, and assets in Canada used in carrying on the business. *Ibid*, s 3.

⁵⁶ *Ibid*, s 11.

an existing business has been acquired by an investor.⁵⁷ However, in general, an acquisition of control (1) is presumed to occur if an investor acquires at least one-third of the voting shares of a corporation, and is deemed to occur (2) if an investor acquires all or substantially all of a Canadian business' assets or (3) acquires a simple majority of the voting shares of a corporation or voting interest of a partnership, trust, or joint venture.⁵⁸

On this basis, the ICA does not presumptively apply to an investment falling below the abovementioned thresholds. However, both the presumption against or for an acquisition of control may be rebutted by proving or disproving "control in fact."⁵⁹ Indeed, the Minister is authorized to analyze all investments, irrespective of the investor's proposed interest in the Canadian business, to determine, including retroactively, whether the investment confers control in fact on the investor.⁶⁰ The Minister's powers explicitly extend to determinations of whether a Canadian business is or is not controlled by a SOE.⁶¹

E. Notifications: Substantive Requirements

If an investment is subject to notification, the investor must file a notice with the Minister either before making the investment or within 30 days of the investment being implemented.⁶² Upon receiving notice, the Minister is required to provide the investor with a receipt indicating whether the transaction is reviewable.⁶³ If the Minister sends a notice of review to the investor within 21 days of sending the investor the receipt, then the investment can be subject to review.⁶⁴ However, if the information provided by the investor is correct and the Minister has provided the investor with a receipt indicating that the transaction is not reviewable, or if the Minister fails to

⁵⁷ *Ibid*, s 28.

⁵⁸ *Ibid*.

⁵⁹ *Ibid*, ss 28(4), 28(5), 28(6), 28(6.1), 28(6.2), 28(6.3), 28(7).

⁶⁰ *Ibid*.

⁶¹ *Ibid*, ss 28(6.1), 28(6.2), 28(6.3).

⁶² *Ibid*, s 12. The information that must be included in the notice is prescribed in Schedule I of the Investment Canada Regulations. See *Investment Canada Regulations*, SOR/85-611, Schedule I [ICA Regulations].

⁶³ See ICA, *supra* note 4, s 13(1).

⁶⁴ *Ibid*, s 13(1), 13(3).

subsequently send the investor a notice of review within 21 days, then the investor is free to implement the transaction.⁶⁵

F. The ICA's Net Benefit Test

In general, two factors determine whether an investment is reviewable.⁶⁶ The first factor, similar to the application of the Act's notification requirement, is whether the "non-Canadian" investor (1) establishes a new Canadian business, or (2) proposes to acquire, directly or indirectly, control of an existing Canadian business. The second factor, unique to the net benefit test, is whether the proposed investment exceeds certain specified monetary thresholds, measured either in "asset" or "enterprise" value.⁶⁷ Typically, only large acquisitions are subject to review. The dollar thresholds that determine whether an acquisition will be reviewable depend on five factors: (1) whether the acquisition is "direct" or "indirect",⁶⁸ (2) whether the investor is a "WTO Investor",⁶⁹ (3) whether the investor is a "Trade Agreement Investor",⁷⁰ (4)

⁶⁵ *Ibid.*

⁶⁶ The ICA exempts several types of transactions which would otherwise fall within the ambit of the Act, including: an acquisition of control of a branch business, an acquisition of control in connection with the issuance of security for a loan, and a corporate reorganization following which the ultimate control of the Canadian business remains unchanged. *Ibid.*, Part II.

⁶⁷ The method of calculating the "enterprise value" of the Canadian business that is the subject of the investment is prescribed in sections 3.3, 3.4 and 3.5 of the Investment Canada Regulations. The method of calculating the "asset value" of the Canadian business that is the subject of the investment is prescribed in section 3.1 of the Investment Canada Regulations. See *ICA Regulations*, *supra* note 62, ss 3.1, 3.3, 3.4, 3.5.

⁶⁸ ICA, *supra* note 4, s 28(1) provides detailed rules to determine whether the acquisition of control of a Canadian business is direct or indirect. As Nicholls summarizes: "[i]n [its] simplest terms, a direct acquisition refers to the acquisition of the shares or assets of a Canadian business, and an indirect acquisition essentially refers to the acquisition of a non-Canadian entity that directly or indirectly controls an entity carrying on a Canadian business." See Christopher C Nicholls, *Mergers, Acquisitions and Other Changes of Corporate Control*, 2nd ed (Toronto: Irwin Law, 2012) at 64 [Nicholls, "Mergers"].

⁶⁹ ICA, *supra* note 4, s 14.1(6) defines "WTO Investor." "WTO Investor" refers to a national or permanent resident of one of the 164 countries that are members of the World Trade Organization. See Nicholls, "Mergers", *supra* note 68 at 64.

⁷⁰ ICA, *supra* note 4, s 14.11(6) and the accompanying schedule defines "Trade Agreement Investors." A "Trade Agreement Investor" includes entities and individuals whose country of ultimate control is party to one of a number of trade agreements, including the Canada-European Union Comprehensive Economic and Trade Agreement and the North

whether the investor is a “SOE”,⁷¹ and (5) whether the subject business is a “Cultural Business”.⁷²

1. Private Sector WTO Investments

The review threshold for a private sector WTO Investor directly acquiring control of a Canadian business or a private sector non-WTO Investor directly acquiring control of a Canadian business, where the business is currently controlled by a WTO Investor, is \$1 billion in enterprise value.⁷³ Indirect acquisitions of control by either type of investor are not reviewable.

2. Private Sector Trade Agreement Investments

The review threshold for a private sector Trade Agreement Investor directly acquiring control of a Canadian business, or a private sector non-Trade Agreement Investor directly acquiring control of a Canadian business, where the business is currently controlled by a Trade Agreement Investor, is \$1.5 billion in enterprise value.⁷⁴ Similarly, indirect acquisitions of control by either type of investor are not reviewable.

3. SOE WTO Investments

The review threshold for SOE investors is considerably lower. It is also measured by “asset” value. The review threshold for a (1) SOE WTO Investor directly acquiring control of a Canadian business or (2) a SOE non-WTO Investor directly acquiring control of a Canadian business, where the business is currently controlled by a WTO Investor, is \$398 million in asset value.⁷⁵ Once again, indirect acquisitions of control are not reviewable.

American Free Trade Agreement. See Nicholls, “Mergers”, *supra* note 68 at 64.

⁷¹ ICA, *supra* note 4, s 3 defines “State-Owned Enterprise.”

⁷² *Ibid*, s 14.1(6) defines a “cultural business.” Nicholls summarizes a “cultural business” as a Canadian business that “produce[s] the books, magazines, and newspapers Canadians read, the music Canadians play or to which they listen, and the films or videos Canadians watch.” See Nicholls, “Mergers”, *supra* note 68 at 64.

⁷³ See ICA, *supra* note 4, ss 14.1(1), (2). Starting January 1, 2019, the threshold level will be adjusted annually based on growth in nominal GDP in accordance with the formula set out in subsection 14.1(2) of the ICA.

⁷⁴ *Ibid*, ss 14.11(1), (2), (3). Starting January 1, 2019, the threshold level will be adjusted annually based on growth in nominal GDP in accordance with the formula set out in subsection 14.11(3) of the ICA.

⁷⁵ *Ibid*, ss 14.1(1), (2). This threshold will be annually revised to reflect the change in Canada’s nominal Gross Domestic Product in accordance with the formula set out in subsection

4. *Non-WTO Investments and Investments in Cultural Businesses*

Finally, the review thresholds for a non-WTO Investor directly acquiring control of a Canadian business is \$5 million in asset value, and \$50 million in asset value for indirect acquisitions. These same thresholds apply to all investors who acquire control of a Canadian business that is a “Cultural Business.”⁷⁶

G. The Net Benefit Test: Substantive Requirements

The purpose of the ICA’s economic review is to determine whether an investment is beneficial to Canada on a net-basis. For a reviewable investment to be approved, the investor must persuade the Minister that the proposed investment is likely to be of a “net benefit to Canada”.⁷⁷ Generally, reviewable investments cannot be implemented until the investor has filed an application for review,⁷⁸ and the Minister, upon reviewing the investment, has satisfied himself that the investment is likely to be of a net benefit to Canada.⁷⁹ The Minister must complete a net benefit review within 45 days of the investor submitting an application, but that period may be unilaterally extended by the Minister for an additional 30 days.⁸⁰ The review period may also be extended past 75 days for an additional period if the Minister and the investor mutually agree.⁸¹ If the investment is not approved or a notice of extension is not received by the investor within the applicable time period, then the investment is deemed to be approved.⁸²

14.1(2) of the ICA.

⁷⁶ *Ibid*, ss 14(3), (4).

⁷⁷ *Ibid*, s 21(1), s 16(1).

⁷⁸ The information that must be included in the notice is prescribed in Schedule II of the Investment Canada Regulations. See ICA *Regulations*, *supra* note 62, Schedule II.

⁷⁹ An investor may implement an investment prior to the completion of the review in several limited circumstances, including 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 that is the subject of the review. See ICA, *supra* note 4, ss 16(1), 15(2). If an investor implements an investment that is disallowed by the Minister, the investor must divest control of the Canadian business. See ICA, *supra* note 62, s 24(1).

⁸⁰ ICA, *supra* note 4, ss 21, 22.

⁸¹ *Ibid*.

⁸² *Ibid*, ss 21(9), 22(4).

An investment will be disallowed if the Minister finds that the proposed investment is not likely to be of a net benefit to Canada. However, the ICA provides that where the Minister initially rejects the investor's proposal, the investor has a limited right to make additional representations and undertakings within 30 days to persuade the Minister of the investment's merits.⁸³ If this right is exercised, the Minister's subsequent decision is final and cannot be appealed.⁸⁴

Where the Minister disallows an investment, he must publicly disclose his reasons for the decision.⁸⁵ The Minister has yet to disallow an investment since this requirement came into force in 2009.⁸⁶ The ICA also authorizes, but does not require, that the Minister provide reasons for approving a transaction.⁸⁷ The Minister has never disclosed his reasons for accepting a transaction despite possessing the authority to do so.

The Minister has considerable discretion when deciding whether a proposed investment is of a net benefit. This is because the "net benefit" standard, an inherently vague concept, is not defined in the ICA or elsewhere. The broadly worded criteria which must guide the Minister's determination, provided for in section 20 of the Act as well as in several supporting guidelines, further enhance ministerial discretion.⁸⁸ In addition, neither section 20 nor the supporting guidelines provide any indication of how each evaluative criterion is to be considered, nor do they indicate each factor's relative importance.

The factors that the Minister must consider under section 20 of the ICA are:

1. [T]he effect of the investment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada and on 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

⁸³ *Ibid*, s 23(1), 23(2), 23(3).

⁸⁴ See VanDuzer, "Mixed Signals", *supra* note 5 at 258.

⁸⁵ See ICA, *supra* note 4, s 23.1.

⁸⁶ See *Budget Implementation Act*, 2009, SC 2009, c 2, s 452.

⁸⁷ See ICA, *supra* note 4, s 23.1.

⁸⁸ *Ibid*, s 38 provides the Minister with the authority to issue guidelines with respect to the application and administration of any provision of the Act.

- Canada of which the Canadian business or new Canadian business forms or would form a part;
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 or industries in Canada;
 5. the compatibility of the investment with national industrial, economic and cultural policies, taking into consideration industrial, economic and cultural policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the investment; and,
 6. the contribution of the investment to Canada's ability to compete in world markets.⁸⁹

In light of section 20, the net benefit test generally requires that the investor set out in its application projections on how the investment will impact Canadian: (1) employment, (2) capital expenditures, (3) management participation in the business, (4) research and development, (5) production, and (6) exports.⁹⁰ The Minister, in making his net benefit determination, may also consider investor-initiated undertakings. Undertakings are time-limited promises committing the investor to certain obligations relating to those factors enumerated under section 20.⁹¹ A typical undertaking is a commitment by the investor to maintain employment levels at the Canadian business for several years.⁹²

H. Application of the Net Benefit Test to SOEs

If the investor falls within the scope of the ICA's definition of a SOE, then as a part of the Minister's net benefit assessment, the investment will be scrutinized against specialized evaluative criteria.

The ICA defines SOEs in very broad terms. A SOE means: (1) a government entity of a foreign state, (2) an entity that is controlled or influenced, directly or indirectly, by a government entity of a foreign state, or

⁸⁹ *Ibid*, s 20.

⁹⁰ See Calvin S Goldman & Michael S Koch, "Competition Law: Recent Developments of Importance" *Goodmans LLP* (June 2016) at 148, online (pdf): <goodmans.ca/files/file/docs/Goodmans%20Competition%20Law%20June%202016.pdf> [perma.cc/36SB-WBB2].

⁹¹ Undertakings are typically binding on the foreign investor for a three-year period after the transaction has closed, or for five years for cultural businesses. An investor's undertakings are not publicly disclosed. See Borger, Rix & Salzman, *supra* note 21 at 16.

⁹² See Nicholls, "Mergers", *supra* note 68 at 66.

(3) an individual who is acting under the direction of a government entity or who is acting under the influence, directly or indirectly, of a government entity.⁹³

The specialized evaluative criteria are provided for in the *Guidelines – Investment by state-owned enterprises – Net benefit assessment* (“*SOE Guidelines*”).⁹⁴ The *SOE Guidelines* were issued under the Act in 2007 and were subsequently revised in 2012. They were issued in response to growing concerns that acquisitions by state-backed investors, especially in the energy sector, could harm the Canadian economy by undermining market dynamics.⁹⁵ The special criteria provided for in the *SOE Guidelines* include:

1. Whether the SOE adheres to Canadian standards of corporate governance;
2. Whether the SOE adheres to Canadian laws and practices, including adherence to free market principles;
3. Whether a Canadian business to be acquired by the SOE will likely operate on a commercial basis;
4. The effect of the investment on the level and nature of economic activity in Canada; and,
5. The nature and degree to which the SOE is owned and controlled by a state or its conduct and operations are influenced by a state.⁹⁶

In effect, the *SOE Guidelines* require that the SOE investor satisfy the Minister that the acquired Canadian business will operate in a manner that mirrors a market-oriented private-sector company, and that the SOE will not use the acquisition to effect the objectives of its political master.⁹⁷ The Minister, in making his net benefit determination, may also consider undertakings proposed by the investor to alleviate fears raised by the fact that the investor is government-owned.⁹⁸ The *SOE Guidelines* provide a list of undertakings that SOE investors have previously adopted, including “the

⁹³ See ICA, *supra* note 4, s 3.

⁹⁴ See Industry Canada, “*SOE Guidelines*”, *supra* note 32.

⁹⁵ In particular, the federal government feared that SOE-controlled Canadian businesses would be driven by the policies of foreign governments rather than purely commercial considerations. See Steger, *supra* note 37 at 2. VanDuzer suggests that the proposed acquisition of Noranda Inc., then Canada’s largest miner, by China Minmetals, a Chinese SOE, may have triggered the adoption of the *SOE Guidelines*. See VanDuzer, “Mixed Signals”, *supra* note 5 at 252.

⁹⁶ See Industry Canada, “*SOE Guidelines*”, *supra* note 32.

⁹⁷ See Goldman & Koch, *supra* note 90 at 148.

⁹⁸ See Industry Canada, “*SOE Guidelines*”, *supra* note 32.

appointment of Canadians as independent directors [on the Canadian company's board], the employment of Canadians in senior management positions [of the Canadian business], the incorporation of the [Canadian] business in Canada, and the listing of shares of the acquiring company or the Canadian business being acquired on a Canadian stock exchange."⁹⁹

I. SOE Acquisitions in Canada's Oil Sands

The Minister's review of a state-backed investment may also be evaluated in light of the *Statement Regarding Investment by Foreign State-Owned Enterprises* ("SOE Statement"), a policy issued under the Act in 2012. Pursuant to the *SOE Statement*, the Minister will only find an acquisition of control of a Canadian oil sands business by a SOE investor to be of a net benefit on an "exceptional basis."¹⁰⁰ An "exceptional basis" is not defined in the *SOE Statement* or elsewhere. The *SOE Statement*, like the *SOE Guidelines*, was published in response to increased levels of government-backed investment in Canada's energy industry, raising concerns that Canada's energy resources were being "locked-up" by foreign governments.¹⁰¹

J. Post-Approval Requirements

If an investor's transaction is approved by the Minister, then the investor will be obligated to comply with the terms of the approval, including any undertakings entered into. To ensure compliance, the Act requires that the investor provide the Minister with regular progress reports on the implementation of its undertakings.¹⁰² The Minister is authorized to order an

⁹⁹ *Ibid.*

¹⁰⁰ See Industry Canada, "SOE Statement", *supra* note 26. In providing justification for limiting government-backed investments in the oil sands, the *SOE Statement* states: "Canadian oil sands are of global importance and immense value to the future economic prosperity of all Canadians....[given that] Canada's oil sands are primarily owned by...private sector businesses....[i]f the oil sands are to continue to develop to the benefit of all Canadians, the role of private companies must be reinforced."

¹⁰¹ *Ibid.* The transactions triggering the release of the *SOE Statement* were China National Offshore Oil Corporation Ltd.'s acquisition of Nexen Inc., a Canadian energy firm with assets in the oil sands, and Malaysian-based Petroliaam Nasional Berhad's (also known as PETRONAS) acquisition of Progress Energy Canada Inc., a Canadian energy firm with assets in the Montney formation in British Columbia. Both transactions were approved by the Minister.

¹⁰² See Borger, Rix & Salzman, *supra* note 21 at 19-22.

uncooperative investor to carry out any unfulfilled commitment.¹⁰³ If the investor fails to comply with an order, the investor may be liable to a fine¹⁰⁴ or ordered to divest itself of the acquired business.¹⁰⁵

K. Addressing Uncertainty: Ministerial Opinions

Lastly, an unrelated, but critical element of the ICA is the Minister's authority to issue Ministerial Opinions. To address uncertainty arising under the ICA, a foreign investor may apply to the Minister for an opinion with respect to the interpretation or applicability of the *Act* to certain facts.¹⁰⁶ Opinions are binding on the Minister so long as the material facts upon which the Minister's opinion is based remain substantially unchanged.¹⁰⁷

V. A CRITIQUE OF THE "NET BENEFIT TEST"

A. Criticisms of the ICA are Masked

The ICA's net benefit test has faced significant criticism. Practitioners, pundits, and academics regularly opine that the ICA places a number of unnecessary hurdles in front of investors, diminishing Canada's ability to attract foreign capital. However, such critiques are often betrayed by the exceptionally high success rate of applications for review under the *Act*. Indeed, while approximately 1,740 reviewable investments have been approved by the Minister between 1985 and 2018, only a handful have ever

¹⁰³ The Federal Court of Appeal considered the validity of powers granted to the Minister under the ICA to enforce undertakings in *Canada (AG) v United States Steel Corp.* The case arose following United States Steel Corp.'s ("US Steel") acquisition of control of Stelco Inc., a Canadian steelmaker, in 2007. The Minister sought an order imposing a penalty of \$10,000 per day per breach until US Steel complied with undertakings it had provided concerning levels of steel production and employment in Canada. US Steel failed to comply with its undertakings due to financial stress caused by a significant economic recession. The court, rejecting US Steel's challenge, upheld the ICA's enforcement provisions. In 2011, the Minister dropped its court action against the company. The Minister and US Steel announced that new and enhanced undertakings had been agreed to. See *Canada (AG) v United States Steel Corp.*, 2011 FCA 176, 333 DLR (4th) 1. See also Nicholls, "Mergers", *supra* note 68 at 66-67.

¹⁰⁴ See ICA, *supra* note 4, ss 39-43.

¹⁰⁵ *Ibid.*

¹⁰⁶ *Ibid.*, s 37.

¹⁰⁷ *Ibid.*

been disallowed.¹⁰⁸ Rejected investments include the proposed acquisition of MacDonald, Dettwiler and Associates Ltd., an information and geospatial business, by US-based Alliant Techsystems Inc. in 2008, and the hostile takeover of Potash Corporation of Saskatchewan (“PotashCorp”), the world’s largest potash producer, by BHP Billiton Plc. (“BHP”), an Anglo-Australian company, in 2010.¹⁰⁹

Dwelling on the ICA’s exceptional approval rate is problematic. It creates the false impression that the Act is not a deterrent to foreign investment. However, as critics of the ICA argue, the ICA’s success rate conceals the fact that there may be a significant number of proposals that are never submitted due to issues with the Act.¹¹⁰ Commenting on this phenomenon, VanDuzer states: “[o]ver time, applicants and their legal advisors have learned what applications are likely to receive approval and thus only submit applications with conditions that are acceptable”.¹¹¹ This view has been endorsed by several legal practitioners.¹¹² Indeed, they contend that the number of proposals never submitted for review has likely increased significantly in recent years in light of several contentious reviews concerning state-backed investors, which has only “accentuated the uncertainty around deal-making, [particularly] in an era marked by ... accelerating global investment from SOEs”.¹¹³

Therefore, it is necessary to look beyond the success rate of applications for review – a flawed proxy for the efficacy of the Act. By doing so, it is apparent that the ICA suffers from a number of serious defects that must be remedied.

¹⁰⁸ This figure excludes proposed acquisitions of cultural businesses. See Peter Glossop, “Frequently asked questions concerning the *Investment Canada Act*,” (October 2017) at 7, online (pdf) Osler, Hoskin & Harcourt LLP: <osler.com/osler/media/Osler/reports/foreign-investment/Investment-Canada-Act-Frequently-asked-questions_2019.pdf> [perma.cc/J8EL-WZTZ].

¹⁰⁹ See Library of Parliament, *supra* note 9 at 4-5. Rejected investments under the ICA’s national security review are also rare. The proposed acquisition of the Allstream division of Manitoba Telecom Services Inc., a Canadian telecommunications business, by Accelero Capital Holdings in October 2013 is an example. BHP’s proposal was not technically disallowed by the Minister. Under section 23 of the ICA, BHP was authorized to make additional representations and undertakings in order to obtain ministerial approval of the deal after the Minister initially rejected the transaction. However, BHP withdrew its bid for PotashCorp. despite having this right. See Nicholls, “Mergers”, *supra* note 68 at 69-70.

¹¹⁰ See VanDuzer, “Mixed Signals”, *supra* note 5 at 266.

¹¹¹ *Ibid.*

¹¹² See Goldman & Koch, *supra* note 90 at 146.

¹¹³ *Ibid.*

B. The Net Benefit Test Rests on a Dubious Foundation

A key criticism of the net benefit test, championed by Safarian, is that it rests on a “dubious economic rationale.”¹¹⁴ Safarian argues that the underlying premise of the ICA, based on the protectionist FIRA, is the wholly inaccurate notion that foreign investment in Canada hinders the country’s economic development.¹¹⁵ This premise, personified in the enduring fear of Canada becoming a “branch plant”, is indeed largely false. If one looks hard, they will no doubt find prominent examples of foreign investments negatively impacting Canadians. For instance, United States Steel’s acquisition of Stelco Inc. in 2007 eventually led to well-publicized mill closures and employment losses.¹¹⁶ However, given the external forces facing the company, including a major economic recession, it is doubtful that Stelco Inc. would have continued its operations if the company remained Canadian-controlled. It is also doubtful, especially in a world where businesses increasingly operate globally and have diverse, international ownership, that there is something inherent to Canadian businesses that make them better “corporate citizens” than their foreign counterparts.¹¹⁷ Foreign investment, as already discussed, is generally beneficial to host countries.¹¹⁸ Further, foreign companies, especially in the Canadian context, typically provide greater benefits to the economy than domestic firms.¹¹⁹

There is also considerable evidence suggesting that concerns over the “hollowing out of corporate Canada” have been overblown. While dated, a report by the Conference Board of Canada found that despite increased foreign investment in Canada between 1999 and 2005, the number of head

¹¹⁴ AE Safarian, “Simplifying the Rule Book: A Proposal to Reform and Clarify Canada’s Policy on Inward Foreign Direct Investment” (2015) *CD Howe Institute*, Commentary no 425 at 12, online (pdf): cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_425.pdf [perma.cc/3YGU-S833].

¹¹⁵ *Ibid.*

¹¹⁶ Rio Tinto Group’s acquisition of Alcan Inc., a major miner and aluminum manufacturer, is another noteworthy case. The deal eventually led to a reduced Canadian head office and a decline in other economic activities in Canada.

¹¹⁷ There is some literature suggesting that domestically-controlled companies may better serve their home jurisdictions. However, this literature primarily concerns companies operating in developing and least developed countries.

¹¹⁸ See Statistics Canada, “Global Links”, *supra* note 12.

¹¹⁹ See Bergevin & Schwanen, *supra* note 10 at 3.

offices in Canada increased.¹²⁰ Further, contrary to the fear that foreign-controlled firms will shift their management to their home jurisdiction, Statistics Canada has found that such firms often “have a higher percentage of their employment in white-collar workers” than domestic firms.¹²¹ The Competition Policy Review Panel has also questioned the assertion that foreign investment has weakened Canadian control over the national economy. The Panel found that the proportion of the Canadian economy under foreign control has not changed noticeably over the last several decades despite Canada liberalizing its investment rules. Ironically, the Panel noted that the influence of Canadian-controlled companies has increased significantly on the world stage as Canadian firms are gradually increasing their share of global assets.¹²² To illustrate this trend, the Panel pointed to an encouraging statistic: “[t]he number of Canadian-owned and headquartered firms that ranked in the top five of their respective industries grew from 15 to 40 over the past two decades”.¹²³

In light of this research, one should question the motives behind individuals who claim that corporate Canada is being hollowed out. Nicholls questions the sincerity of some corporate leaders, stating: “one [must be] mindful of the possibility at least that some senior Canadian executives may find it convenient to use the Canadian flag as a form of camouflage for arguments favouring their own economic self-interest.”¹²⁴ One should also question whether limiting foreign ownership would promote the health of domestic companies and Canada’s national economy. The Competition Policy Review Panel suggested that limiting foreign investment may have the opposite effect. The Panel stated: “we do not believe that it is desirable – or possible – to stop the natural rhythm of creative destruction and renewal [associated with foreign acquisitions] ... [t]he benefits of competition are too great”.¹²⁵

¹²⁰ See Glen Hodgson, “Is Corporate Canada being Hollowed Out? It Depends Where You Are” (2007) *Conference Board of Canada*, Publication no 150-07, online (pdf): <conferenceboard.ca/temp/a616eca0-fa5e-4aa4-96cb-4d7e664a1961/150-07%20Corporate%20Canada%20Being%20Hollowed%20Out-Briefing.pdf> [perma.cc/Y8HZ-MKT9].

¹²¹ See Statistics Canada, “Global Links”, *supra* note 12 at 7.

¹²² See Competition Policy Review Panel, “Compete to Win”, *supra* note 22 at 16.

¹²³ *Ibid.*

¹²⁴ See Nicholls, “Mergers”, *supra* note 68 at 69.

¹²⁵ See Competition Policy Review Panel, “Compete to Win”, *supra* note 22 at 16.

If we accept the proposition that foreign investors are no worse than their domestic counterparts, then not only is the net benefit test unnecessary, but its discriminatory treatment of foreign investors makes the test highly protectionist. As a condition of gaining access to the Canadian market, the ICA subjects' foreign investors to an onerous review process and pressures such investors to make undertakings that Canada could never realistically demand from domestic businesses in similar circumstances.¹²⁶ This promotes Canadian firms' acquisitions of domestic businesses by imposing a substantial regulatory burden on foreigners.

C. The Net Benefit Test is Overly Discretionary

Another major criticism of the ICA is that the net benefit test is overly discretionary, resulting in unpredictable outcomes. As noted, the Minister has considerable discretion when deciding whether a proposed investment is likely to be of a net benefit. Since the investor bears the onus of demonstrating net benefit, the highly discretionary nature of the review makes it difficult for an investor to know the level of performance required in order to satisfy the Minister. As a result, the review process creates unnecessary risks as investors must dedicate significant time and money to satisfy vague and unclear review criteria, and ultimately the whims of whomever occupies the Minister's office.

To exacerbate this issue, the highly discretionary nature of the review process has potentially allowed assessments to be "captured" by domestic political considerations. This has led some commentators to argue that the Minister has on occasion disregarded the merits of an investor's proposal in the name of political expediency.¹²⁷

D. Political Meddling: Economic Protectionism

One of the most prominent examples of the net benefit review becoming possibly captured by political considerations was BHP's failed hostile takeover of PotashCorp, the largest producer of potash, and a significant source of local jobs and tax revenue for the Saskatchewan government.¹²⁸ The case is notable for the unprecedented degree of protectionism and politics which surrounded the Minister's application of the net benefit test. Brad Wall, then Saskatchewan's Premier, vocally opposed the takeover of PotashCorp, a

¹²⁶ See Safarian, *supra* note 114 at 13.

¹²⁷ See e.g. Goldman & Koch, *supra* note 90 at 148.

¹²⁸ *Ibid.*

“champion” of Saskatchewan’s economy. Premier Wall claimed potash situated within the province “belong[ed] to the people of Saskatchewan” and that foreign ownership of such a “strategic resource” would depress the province’s economy.¹²⁹ While prominent policy and business leaders supported the transaction and argued that provincial politics should stay out of the Minister’s net benefit determination,¹³⁰ Premier Wall may have had a significant influence on the Minister, Tony Clement, a fellow conservative.¹³¹ Minister Clement disallowed the proposed transaction, finding that the deal was not likely to be of a net benefit to Canada.¹³² Observers speculated that Minister Clement’s decision, popular amongst the public in Saskatchewan, was motivated primarily by upcoming federal and provincial elections.¹³³

E. Political Meddling: Canadian-Chinese Relations

With the formation of a new, Liberal-led government in 2015,¹³⁴ it seems that a different set of political considerations have begun to skew reviews under the ICA. Canadian-Chinese relations appears to be the factor having the most influence on the government’s decision-making.

A key element of the Trudeau government’s foreign-policy has been to establish closer economic relations with China.¹³⁵ Canada and China,

¹²⁹ See James Wood, “Premier Brad Wall warns against BHP turning Saskatchewan, Canada into ‘branch office’”, *The Saskatoon StarPhoenix* (26 October 2010), online: <thestarphoenix.com/news/premier+brad+wall+warns+against+turning+saskatchewan+canada+into+branch+office/3727706/story.html> [perma.cc/TK7E-JQV2].

¹³⁰ See John Manley, “Why Open, Fair Investment Rules are in Canada’s National Interest”, *Canadian Council of Chief Executives* (1 November 2010), online (pdf): <thebusinesscouncil.ca/publications/why-open-fair-investment-rules-are-in-canadas-national-interest/ [perma.cc/9LSN-5V5R].

¹³¹ Brad Wall led the Saskatchewan Party, a conservative, centre-right provincial political party. Tony Clement was, and still is, a member of the Conservative Party of Canada, a conservative, centre-right federal political party.

¹³² See Goldman & Koch, *supra* note 98 at 148

¹³³ *Ibid.* See also Brenda Bouw & Steven Chase, “Block Potash Corp. takeover, Saskatchewan to tell Ottawa”, *The Globe and Mail* (19 October 2010), online: <theglobeandmail.com/globe-investor/block-potash-corp-takeover-saskatchewan-to-tell-ottawa/article1215260/ [perma.cc/3E7G-Z6X8].

¹³⁴ The Liberal Party of Canada, lead by Justin Trudeau, won a landslide victory in Canada’s 2015 general election.

¹³⁵ See generally Canada, Prime Minister’s Office, Minister of International Trade Mandate Letter, Mandate Letter (Ottawa: PMO, 2015), online: <pm.gc.ca/en/mandate-letters/archived-minister-international-trade-mandate-letter-0> [perma.cc/N37L-MPDC];

currently in exploratory talks, are contemplating the launch of negotiations for a bilateral free-trade agreement (“FTA”). Beijing has made clear that it finds Canada’s review of Chinese investments under the ICA protectionist.¹³⁶ Indeed, Lu Shaye, China’s former ambassador to Canada, stated in 2017 that any FTA between the countries would limit investment reviews. Ambassador Lu Shaye, referencing difficulties that Chinese investors have had accessing the Canadian market, stated: “[t]he signing of the (free-trade agreement) is to provide a stable...institutional arrangement...so that [Chinese] investors won’t worry (that) their investments may encounter some difficulties or problems”.¹³⁷ In response to Chinese pressure, pundits and opposition parties have argued that the Trudeau government has kowtowed to Beijing, loosening restrictions on Chinese investment.¹³⁸

Indeed, in a revealing move, the Trudeau government revisited an order issued by the previous Harper government that sought to unwind O-Net’s acquisition of Canada-based ITF, a transaction deemed injurious to Canada’s national security.¹³⁹ As noted, the Harper government disallowed the transaction in 2015 under the ICA’s national security provisions, fearing that O-Net would exploit ITF’s proprietary technology to undermine Canada’s military edge.¹⁴⁰ In March 2017, the Minister, after conducting a second

Canada, Prime Minister’s Office, Minister of International Trade Mandate Letter, Mandate Letter (Ottawa: PMO, 2017), online: <pm.gc.ca/en/mandate-letters/archived-minister-international-trade-mandate-letter> [perma.cc/GJQ6-XSDY].

¹³⁶ Robert Fife & Steven Chase, “Canadians oppose sale of high tech firms to Chinese investors”, *The Globe and Mail* (2 July 2017), online: <theglobeandmail.com/news/politics/canadians-oppose-sale-of-high-tech-firms-to-chinese-investors-poll/article35531306/> [https://perma.cc/D7EW-QQLS] [Fife & Chase, “High Tech Firms”]; Andy Blatchford & Mike Blanchfield, “China sees free trade with Canada as way to avoid future Norsat-like uncertainty”, *CBC* (5 July 2017), online: <cbc.ca/news/politics/china-norsat-free-trade-canada-1.4190712> [perma.cc/K4LL-Q9U7].

¹³⁷ See Blatchford & Blanchfield, *supra* note 136.

¹³⁸ See generally Andrew Scheer, “Free trade with China doesn’t put Canadian interests first”, *The Globe and Mail* (6 July 2017), online: <theglobeandmail.com/opinion/free-trade-with-china-doesnt-put-canadian-interests-first/article35571538/> [perma.cc/3M2F-9SDU]; Steven Chase, “Liberals reverse course on Chinese takeover of Montreal high-tech firm”, *The Globe and Mail* (27 March 2017), online: <theglobeandmail.com/news/politics/liberals-reverse-course-on-chinese-deal/article34441975/> [perma.cc/H696-AGV3].

¹³⁹ See Franklyn & Auron, *supra* note 39; Walker, *supra* note 39.

¹⁴⁰ *Ibid*; Chase, *supra* note 138; Robert Fife & Steven Chase, “Beijing pressing for full access to Canada’s economy in trade talks”, *The Globe and Mail* (24 March 2017), online:

national security review, announced that cabinet approved the transaction, stating that the transaction was no longer injurious to Canada's national security.¹⁴¹ The transaction received quick criticism from the opposition. Tony Clement, the Minister who rejected the deal in 2015, stated: "[t]his is just political cover by a government that is bending over backwards to accommodate the People's Republic of China.... [t]he government is ignoring national-security concerns that were valid two years ago and are valid now".¹⁴² This view was widespread. Many commentators noted that the decision came days after Beijing warned Canada that restrictions on Chinese investments under the ICA "would reinforce existing Chinese skepticism about Canada's willingness to truly forge closer investment and trade ties with China."¹⁴³

More recently, the Trudeau government's June 2017 approval of Hytera Communications Co. Ltd.'s acquisition of Norsat International Inc. ("Norsat"), a Canadian satellite communications company, has drawn criticism.¹⁴⁴ Critics argue that the transaction undermines Canada's national security as Hytera Communications Co. Ltd's principal shareholder, Chen Qingzhou, has close ties with China's police and security agencies.¹⁴⁵ This is a

<theglobeandmail.com/news/politics/beijing-pressing-for-full-access-to-canadas-economy-in-trade-talks/article34412957/> [perma.cc/KM3J-7U48] [Fife & Chase, "Beijing Pressing"]].

¹⁴¹ See Franklyn & Auron, *supra* note 39.

¹⁴² Chase, *supra* note 140.

¹⁴³ *Ibid*; Chase, *supra* note 138; Fife & Chase, "Beijing Pressing", *supra* note 140.

¹⁴⁴ Another recent and highly contentious Chinese investment approved by the government was the acquisition of Canada's Retirement Concepts Inc., one of the largest providers of senior care in British Columbia, by Anbang Insurance Group, a Chinese insurer, in February 2017. To the surprise of many Canadians, the Chinese government took control of Anbang Insurance Group in February 2018 in order to "restructure" the company following an investigation into the insurer's former chairman for "illegal business practices." See Geoffrey Morgan, "The Chinese government now controls the biggest retirement home chain in B.C.", *The Financial Post* (23 February 2018), online: <business.financialpost.com/real-estate/property-post/the-chinese-government-now-controls-the-biggest-retirement-housing-chain-in-b-c> [perma.cc/KJL4-E9YQ]; Andrew Willis, Jeffrey Jones & Steven Chase, "Aecon rivals urge Ottawa to block Chinese takeover", *The Globe and Mail* (16 January 2018), online: <theglobeandmail.com/report-on-business/aecon-rivals-urge-ottawa-to-block-foreign-takeover/article37631937/> [perma.cc/5EKP-GJGC?type=image].

¹⁴⁵ See Robert Fife & Steve Chase, "Chinese firm expelled from trade association days before takeover of Canadian high-tech company", *The Globe and Mail* (21 July 2017), online: <beta.theglobeandmail.com/news/politics/chinese-firm-expelled-from-trade-association-

cause for concern as Norsat's clients include NAV CANADA (the owner and operator of Canada's civil air navigation system), defense contractors supplying and servicing the Canadian military, and the militaries of a number of Canada's allies.¹⁴⁶ While the Canadian government conducted a security analysis of the transaction, the Minister refused to conduct a formal national security review under the ICA. Not only was this decision criticized by Canadian opposition parties, but the United States and leading security experts also questioned the government's judgement.¹⁴⁷ For instance, Richard Fadden and Ward Elcock, former directors of the Canadian Security Intelligence Service, stated publicly that they would have recommended that the transaction be subject to a formal national security review.¹⁴⁸

Despite the Trudeau governments' record of approving contentious Chinese investments, not every reviewable transaction has gotten a free-pass. Notably, cabinet rejected the proposed acquisition of Aecon by state-owned CCCC in May 2018. The transaction, involving one of Canada's largest and best-known construction companies, was first announced in October 2017. After intense pressure from both opposition parties and industry stakeholders, the Minister issued a special order in February 2018 subjecting the deal to a formal national security review.¹⁴⁹ Opponents of the transaction were vocal in their hostility to the investment.¹⁵⁰ Amongst other things, they claimed that CCCC was a human rights abuser; that the transaction would undermine the national economy; and that Aecon's involvement in the construction and maintenance of nuclear power stations, military installations, and communications facilities could provide Beijing with undue access to Canada's critical infrastructure.¹⁵¹

days-before-takeover-of-canadian-high-tech-company/article35758019/>
[perma.cc/W68X-24SL] [Fife & Chase, "Expelled].

¹⁴⁶ *Ibid*; See Scheer, *supra* note 139; Fife & Chase, "High Tech Firms", *supra* note 136.

¹⁴⁷ Fife & Chase, "Expelled", *supra* note 145; See Scheer, *supra* note 139; Fife & Chase, "High Tech Firms", *supra* note 136.

¹⁴⁸ Fife & Chase, "Expelled", *supra* note 145. Other leading experts, such as David Mulroney, Canada's former ambassador to China, also questioned the deal.

¹⁴⁹ CBC, "Aecon takeover by Chinese firm delayed for national security review", CBC (12 February 2018), online: <<https://www.cbc.ca/news/business/aecon-ccci-national-security-review-1.4531277>> [perma.cc/QHH5-6RZW?type=image]

¹⁵⁰ *Ibid*; Willis, Jones & Chase, *supra* note 144.

¹⁵¹ Willis, Jones & Chase, *supra* note 144.

In spite of the doom and gloom scenario painted by the deal's detractors, many observers were surprised when Canada rejected the investment.¹⁵² Leading up to the government's decision, Beijing exerted a considerable amount of pressure on the Trudeau government to approve the transaction. For instance, in April 2018, then Ambassador Lu Shaye publicly stressed the importance of the deal in a rare interview with media. He stated that the Canadian media and public was "too sensitive about the Aecon cases" and asserted that Chinese state-backed investments, specifically the Aecon transaction, should be treated equally to those by other foreign firms.¹⁵³ Then Ambassador Lu Shaye also emphasized that if Canada rejected the transaction, Beijing would seek specific reasons from Canada as to why such a decision was made.¹⁵⁴ However, other commentators were less astounded by the decision. They noted that the decision's announcement came shortly after China personally embarrassed Prime Minister Trudeau by balking at the government's efforts to launch negotiations for a "progressive" FTA during a state visit in December 2017.¹⁵⁵

¹⁵² Prime Minister Trudeau failed to provide specific reasons for rejecting the deal but did cite a loss of sovereignty as one factor for cabinet's decision. See Robert Fife & Steven Chase, "Aecon deal threatened Canadian sovereignty, Trudeau says", *The Globe and Mail* (24 May 2018), online: <theglobeandmail.com/politics/article-aecon-cccc-deal-threatened-canadian-sovereignty-trudeau-says/> [perma.cc/G3WG-VJ3F?type=image] Cabinet's rejection of the Aecon deal no doubt departs from the government's practice of approving contentious Chinese transactions. However, it is likely too soon to determine if the government's decision represents a change in Canada's stance towards the Chinese. Indeed, several practitioners argue that the decision in no way signals a change. See Shuli Rodal, Michelle Lally, Peter Glossop, & Kaeleigh Kuzma, "Proposed Acquisition of Aecon by CCCI Blocked on National Security Grounds", *Osler, Hoskin & Harcourt LLP* (24 May 2018), online: <osler.com/en/resources/cross-border/2018/proposed-acquisition-of-aecon-by-ccci-blocked-on-national-securitygrounds#targetText=Proposed%20Acquisition%20of%20Aecon%20by%20CCCI%20Blocked%20on%20National%20Security%20Grounds&targetText=It%20was%20reported%20that%20Aecon's,indirectly%20acquiring%20control%20of%20Aecon.> [perma.cc/G57J-8QHU].

¹⁵³ Jesse Snyder, "China's ambassador says Canada is too 'sensitive' about the proposed Aecon takeover", *The Financial Post* (10 April 2018), online: <business.financialpost.com/news/chinas-ambassador-says-canada-is-too-sensitive-about-the-proposed-aecon-takeover> [perma.cc/5AUW-SPT2].

¹⁵⁴ *Ibid.*

¹⁵⁵ See The Canadian Press, "China wants no 'progressive' elements in any free trade deal with Canada: envoy", *CBC News* (10 April 2018), online: <cbc.ca/news/politics/china-trade-canada-progressive-1.4613602> [https://perma.cc/E3U4-TU5E?type=image]; Robert Fife

While the proposed ITF, Norsat, and Aecon investments concern the ICA's national security review, they are illustrative of how domestic politics may "capture" the net benefit test. Both the net benefit and national security tests provide a questionable amount of discretion to political decision-makers, allowing domestic politics to erode the objectivity of the investment review process. This undermines the purpose of the net benefit test by jeopardizing Canada's economic security while simultaneously deterring foreign investment by impairing the test's predictability.

Further, while the ITF and Norsat cases show a potential bias in favour of foreign investors, which may be a positive thing given Canada's need for foreign capital, the Aecon decision demonstrates that the ICA may not always be wielded by political decision-makers for the benefit of investors. Indeed, investors from China are likely to face increased difficulties accessing the Canadian market in the years to come given deteriorating Canadian-Chinese relations in the wake of the December 2018 arrest of Meng Wazhou, Chief Financial Officer of China-based Huawei Technologies Co. Ltd. ("Huawei"). Meng Wazhou's arrest, made at the request of American Justice Department officials,¹⁵⁶ has sparked a Chinese backlash against Canada. Beijing has responded to the detention of the senior Huawei executive by detaining Michael Korvig and Michael Spavor, two Canadians businessmen in China, on the basis that they were engaged in espionage; sentencing two other Canadians, Robert Schellenberg and Fan Wei, to death for drugs trafficking offenses; resorting to an ugly campaign of name-calling, including admonishing Canada for being a country of "white supremacy"; and ramping up economic sanctions against key Canadian exporters.¹⁵⁷ Canada has responded to China's aggression through its own measures. Amongst other things, Canada has rallied close allies against China in order to name and shame China's actions and raised the specter that Canada may ban Canadian

& Steven Chase, "Free-trade talks with China were stalled before Aecon rejection", *The Globe and Mail* (25 May 2018), online: <theglobeandmail.com/politics/article-free-trade-talks-with-china-were-off-the-rails-before-aecon-rejection/> [perma.cc/MS9Y-PGMQ].

¹⁵⁶ The Americans allege that Huawei sold communications equipment to Iran in contravention of an American-imposed embargo on the country. The Justice Department seeks Meng's extradition to the United States for prosecution.

¹⁵⁷ See CBC, "Huawei arrest: What's happening between Canada and China?", *CBC* (26 January 2019), online: <cbc.ca/news/world/huawei-meng-timeline-1.4989139> [perma.cc/SB2B-GS39?type=image].

communications businesses from adopting Huawei's next-generation 5G technologies from their networks.¹⁵⁸

The 2019 federal election may also bear heavily on the future treatment of Chinese investors under the ICA. If the Conservative Party of Canada was successful in forming the government following the 2019 general election that occurred on October 21, 2019, Chinese investors would undoubtedly face greater difficulty under the ICA. Andrew Scheer, Leader of the Conservatives, have vehemently opposed creating closer ties between Canada and China.¹⁵⁹ It is therefore likely that a Conservative-led government would have wield the ICA to significantly restrict Chinese investment.

F. The ICA: A Black Box

A lack of transparency in the application of the ICA, especially reporting by the Minister, exacerbates the problems caused by the net benefit test's overly discretionary nature. Canada has recognized this issue, amending the ICA in 2009 to bolster transparency. However, the government's reforms were half-measures, failing to rectify the issue. For instance, VanDuzer notes that since 2009, the Minister has been required to publish an annual report on the administration of the ICA.¹⁶⁰ While VanDuzer identifies this change as "a small step in the direction of improved transparency," he notes that the ICA does not prescribe any specific content that must be included in the report. Information included in several recent *Annual Reports* highlight the problem this has created. These reports, being high-level and summary in nature, provide very little detail on actual reviews or the effectiveness of the ICA in obtaining its statutory purpose.¹⁶¹

Other measures included in the 2009 amendments to enhance transparency have also been lacklustre. While the 2009 reforms require that

¹⁵⁸ *Ibid.*

¹⁵⁹ See Scheer, *supra* note 138.

¹⁶⁰ See ICA, *supra* note 4, s 38.1.

¹⁶¹ See generally Canada, Innovation, Science and Economic Development Canada, *Annual Report: Investment Canada Act, 2016-2017*, Annual Report (Ottawa: ISED, 2017), online (pdf): <[ic.gc.ca/eic/site/icalic.nsf/vwapj/2016-17AnnualReport.pdf/\\$file/2016-17AnnualReport.pdf](http://ic.gc.ca/eic/site/icalic.nsf/vwapj/2016-17AnnualReport.pdf/$file/2016-17AnnualReport.pdf)> [perma.cc/5HXU-WB3W]; Canada, Innovation, Science and Economic Development Canada, *Annual Report: Investment Canada Act, 2015-2016*, Annual Report (Ottawa: ISED, 2016), online (pdf): <[ic.gc.ca/eic/site/icalic.nsf/vwapj/ICA_Annual_Report_2015-16-ENv8.pdf/\\$FILE/ICA_Annual_Report_2015-16-ENv8.pdf](http://ic.gc.ca/eic/site/icalic.nsf/vwapj/ICA_Annual_Report_2015-16-ENv8.pdf/$FILE/ICA_Annual_Report_2015-16-ENv8.pdf)> [perma.cc/UDY6-LZW6].

the Minister provide reasons for a decision to reject an investment,¹⁶² the amendments authorize, but do not require, that the Minister publicly disclose reasons for why a transaction was approved.¹⁶³ This is a lost opportunity to enhance ministerial accountability and certainty under the Act. Because the Minister has not rejected a transaction to date, and the Minister has consistently failed to exercise his authority to provide reasons for an investment's approval, there is no publicly-available material to examine in order to independently validate the reasonableness of the Minister's assessment under the net benefit test. Further, without public material on how the Minister makes decisions under the net benefit test, prospective investors and their legal advisors cannot effectively develop an understanding on how the Minister will exercise his discretion.

Transparency in the application of the ICA is critical. Knowledge about domestic rules and how they will be implemented is an input considered in any investment decision, particularly for foreign investors having to navigate the different culture and legal systems of a host country.¹⁶⁴ The OECD notes that "meaningful information is...a powerful incentive to invest" because "transparency reduces risks and uncertainties,...helps unveil hidden investment barriers...[and], contributes to the leveling of the playing field among firms".¹⁶⁵ Reflecting on the package of amendments made to the ICA in 2009, VanDuzer concludes that "Canada seems unwilling to develop a robust, transparent investment review process that would constrain the existing broad discretion of the Minister and create a regime that would be more palatable to foreign investors".¹⁶⁶

¹⁶² See ICA, *supra* note 4, s 23.1.

¹⁶³ *Ibid.*

¹⁶⁴ See Organisation for Economic Co-operation and Development, *Public Sector Transparency and International Investment*, Report (Paris: OECD, 2003), online (pdf): <oecd.org/investment/investment-policy/18546790.pdf> [perma.cc/RL3D-7NWW] at 8.

¹⁶⁵ *Ibid.* In support of this proposition, the OECD points to a study conducted by Gelos and Wei which examined the relationship between transparency and the behavior of managers of emerging market funds. Gelos and Wei found that funds hold fewer assets in less transparent markets, suggesting that investment decisions are not being made on a fully informed basis. Therefore, improved transparency could improve the quality of investment decisions. See R Gaston Gelos & Shang-Jin Wei, "Transparency and International Investment Behavior" (2002) International Monetary Fund Working Paper WP/02/174.

¹⁶⁶ See VanDuzer, "Mixed Signals", *supra* note 5 at 258-259.

G. The ICA's Discriminatory Treatment of SOEs

In addition to these broader issues, the ICA's prejudicial treatment of state-backed investors is also concerning. The ICA discriminates against SOEs through the Act's broader application to government-backed investors (e.g. through a lower financial threshold for the application of the net benefit test) as well as by subjecting SOEs to more onerous review requirements (e.g. additional review and undertaking criteria under the *SOE Guidelines*). This special treatment creates additional barriers for state-led investments in Canada by raising the transaction costs of the review process, creating costlier conditions of approval, and significantly reducing the probability of an investment proceeding.¹⁶⁷ Safarian contends that these barriers are so severe that many of Canada's largest private businesses would fail to overcome them, creating "an unlevel playing field" for SOEs in Canada.¹⁶⁸ This is particularly true for SOEs investing in Canada's oil sands. Given the strong language used in the *SOE Statement*, many commenters argue that SOE acquisitions of control in the oil sands are *prima facie* prohibited.¹⁶⁹

H. SOEs: An Exaggerated Risk

As both the *SOE Guidelines* and *SOE Statement* highlight, Canada's concerns with SOEs are predicated on a fear that government-backed investors will operate according to the policy objectives of their political masters instead of commercial practices. If SOE investments proved to be an elevated risk on this basis, the ICA's differential treatment of state-backed investors may be warranted. However, there is a growing body of research suggesting that such fears are exaggerated.

For instance, Woo, Safarian, and Donnelly each independently argue that securing control of a Canadian business does not allow an investor, whether or not a SOE, to operate at will in Canada.¹⁷⁰ Woo contends that "critics of SOE-led investment tend...to almost always neglect to consider the ways in

¹⁶⁷ See Safarian, "Rule Book", *supra* note 114 at 1-10.

¹⁶⁸ *Ibid* at 9.

¹⁶⁹ *Ibid* at 15.

¹⁷⁰ *Ibid*; See James Donnelly, "Open for Business? Lessons Learned from the Land Down Under For Regulating Investments by State-Owned Enterprises in the Oil Sands" (2016) 16 *Asper Rev Intl Business & Trade L* 25 at 4; Yuen Pau Woo, "Chinese Lessons: State-Owned Enterprises and the Regulation of Foreign Investment in Canada", (2014) *China Economic J* 7:1 21-38 [Woo, "Chinese Lessons"].

which Canada can (and does) protect itself against undesirable behavior on the part of [SOEs] through domestic regulation.”¹⁷¹ Echoing this sentiment, Safarian states that SOEs’ activities are constrained considerably by federal, provincial, and municipal laws regulating “labour relations, competition, corporate operations, security, disclosure and a great many other activities”.¹⁷² In particular, Safarian criticizes Canada’s limitations on SOE investments in the oil sands. He notes that within the sector, “a myriad [of] laws and regulations” apply to oil and gas companies, including requirements for “licenses and other permissions on exploration, environmental review, exports, [and the] sourcing of supplies and other inputs.”¹⁷³ Donnelly, focusing specifically on competition law, asserts that “competition laws [are] designed to discipline intentional market-distorting activity, such as exporting goods below market prices, [and] will provide a check on SOEs’ activities”.¹⁷⁴

Beyond regulation, market forces may play a role in curbing unsavory SOE behavior. Cornish argues that the disclosure requirements for publicly-traded SOEs, coupled with market forces, means that public SOEs will “focus on the acquired firm’s economic interest, even where...government objectives exist.”¹⁷⁵ In a similar vein, Donnelly argues that SOEs’ behavior in Canada will be limited by competition with domestic firms. Donnelly states: “SOEs have an interest in maintaining a favourable reputation among industry players and consumers [in Canada] and will therefore behave accordingly.”¹⁷⁶ Looking specifically at Chinese SOEs, Donnelly points to SOEs’ improved efficiency and profitability as an indication that they are becoming increasingly driven by economic incentives.¹⁷⁷

SOEs are also facing government pressure to become more market-oriented.¹⁷⁸ In a recent report, Dobson highlights reforms to Chinese SOE

¹⁷¹ Woo, *ibid* at 34.

¹⁷² Safarian, “Rule Book”, *supra* note 114 at 14.

¹⁷³ *Ibid*.

¹⁷⁴ See Donnelly, *supra* note 170 at 4.

¹⁷⁵ See Margaret Cornish, “Behavior of Chinese SOEs: Implications for Investment and Cooperation in Canada” (2012) *Canadian Council of Chief Executives and Canadian International Council*, online (pdf): <thecic.org/wp-content/uploads/2017/04/Cornish_China_SOE_2012.pdf> [perma.cc/RWU9-WGSK].

¹⁷⁶ See Donnelly, *supra* note 170 at 4.

¹⁷⁷ *Ibid* at 4-5.

¹⁷⁸ However, in recent months the Communist Party of China has begun to reassert its influence over Chinese businesses, installing party officials in management teams,

policy, which has reduced the role of the state in government-backed investors' decision-making. She states that Beijing has become "more comfortable with allowing SOEs to pursue growth based on maximizing shareholder value, rather than national security."¹⁷⁹ As a result, Dobson argues that "modern governance practices are now gradually being introduced to the Chinese corporate world," resulting in improved transparency in accounting and auditing practices, and most importantly, greater corporate independence.¹⁸⁰

In sum, fears about state-led investments are likely overblown. Indeed, despite fears that state-backed firms operating in Canada are influenced or controlled by foreign governments, there is little, if no, evidence to date demonstrating that such firms are departing markedly from commercial practices.¹⁸¹ This may suggest that the ICA's response to SOEs is driven more by domestic politics and Canadians' negative perception of SOEs than by any real threat.¹⁸²

requesting that Chinese businesses share sensitive technology and information with the government, and giving the government more control over business decisions by requiring that managers seek the opinion of the Party. This has sparked some concern that China's progress on limiting government influence over Chinese businesses may be eroding. See e.g. Alexandra Stevenson, "China's Communists Rewrite the Rules for Foreign Businesses", *The New York Times* (13 April 2018), online: <[nytimes.com/2018/04/13/business/china-communist-party-foreign-businesses.html](https://www.nytimes.com/2018/04/13/business/china-communist-party-foreign-businesses.html) [perma.cc/72Z6-N45E]; Keith Zhai, "China's Xi to Tighten Communist Party Grip on Economic Life", *Bloomberg* (6 March 2018), online: <[bloomberg.com/news/articles/2018-03-06/china-s-xi-readies-sweeping-government-overhaul-to-empower-party](https://www.bloomberg.com/news/articles/2018-03-06/china-s-xi-readies-sweeping-government-overhaul-to-empower-party)> [perma.cc/585M-FNXU].

¹⁷⁹ *Ibid* at 4-6.

¹⁸⁰ See Wendy Dobson, "China's State-owned Enterprises and Canada's FDI Policy" (2014) 7:10 U Calgary School Public Policy Research Papers, online (pdf): <policyschool.ca/wp-content/uploads/2016/03/chinas-soes-dobson.pdf> [perma.cc/KV4K-SJSA].

¹⁸¹ See Cornish, *supra* note 175 at 44.

¹⁸² There is a growing body of literature suggesting that Canada's approach to regulating government-backed investors is driven primarily by domestic electoral politics. One source of opposition towards SOE-led investment in Canada may be Canadians' general aversion to government intervention in the economy. Henderson suggests that Canadians' concerns with SOE investments in the oil sands may be driven in part by past concerns with Canadian government energy policy. In particular, Henderson argues that Canadians' uneasiness about SOEs may be linked to Canadian's poor experience with the unpopular federal "National Energy Program", which encouraged Canadian ownership of energy assets, as well as the expansion of state-owned Petro-Canada into the oil sands. See Gail E Henderson, "The Regulation of Foreign Direct Investment by State-Owned Enterprises in Canada" (Paper delivered at the Workshop on Harmonization of Cross-Strait Financial

I. The ICA Ignores the Diversity and History of SOEs

Another issue with the ICA is that it treats SOEs equally when they are not. In fact, SOEs are incredibly distinct, having varied characteristics and histories. For instance, despite the popular view that SOEs are a Chinese or Asian phenomenon, they actually exist in numerous jurisdictions, including advanced market-oriented economies in the West. In 2009, OECD member countries alone reported the existence of more than 2000 SOEs.¹⁸³ Surprising to most Canadians, Canada's state-backed investors, especially its public pension plans, are some of the largest and most active international investors.¹⁸⁴ SOEs are also incredibly diverse. They differ in structure, intent, and governance. For instance, many SOE investors include sovereign wealth funds or public pension plans. While it is conceivable for these entities to become a vehicle for a state's interest, they may be distinct from SOEs whose primary objective is to achieve government policy objectives. Indeed, such entities are often legally obligated to operate at arm's length from political

Regulation, Hong Kong University, 13 April 2013), online: <papers.ssrn.com/sol3/papers.cfm?abstract_id=2281395>. Woo takes a different approach. Woo asserts that Canadians' concerns with SOE-led investment is likely a product of Canadian unease about China's growing global economic importance and a mistrust of the Chinese government, "whether it is on account of human rights abuses, a lack of democracy in China, suppression of the media or Beijing's position on a given international issue." See Woo, "Chinese Lessons", *supra* note 170 at 34. Public opinion polls conducted by the Asia Pacific Foundation of Canada indicate that Canadians are generally opposed to SOE investment, but especially investment from China. The think-tank found that 75% of Canadians oppose investments by SOEs (with 23% strongly against). When Canadians were asked about whether they supported a majority interest investment from different foreign SOEs, Canadians were least supportive of Chinese SOEs, with 76% opposed compared to only 14% in favour. Twice as many Canadians were supportive of investment by SOEs from Japan or France, and more than three times more supportive of investment by SOEs from the United Kingdom. See generally Asia Pacific Foundation of Canada, "National Opinion Poll: Canadian Views on Asia" (2013) Asia Pacific Foundation of Canada, online (pdf): <asiapacific.ca/sites/default/files/filefield/nop2018_0.pdf> [perma.cc/34ZZ-PANV]

¹⁸³ See Hans Christiansen, "The Size and Composition of the SOE Sector in OECD Countries" (2011) Organisation for Economic Co-operation and Development Working Paper 5, online (pdf): <oecd-ilibrary.org/docserver/5kg54cwps0s3-en.pdf?expires=1565970517&id=id&accname=guest&checksum=7D58E78B95BDA502C8A4D6B914FE87B5> [perma.cc/N2B9-T3CJ].

¹⁸⁴ See e.g. The Economist, "Canada's pension funds: Maple revolutionaries", *The Economist* (3 March 2012), online: <economist.com/finance-and-economics/2012/03/03/maple-revolutionaries> [perma.cc/JVV2-ZCPL].

decision-makers.¹⁸⁵ Lastly, SOEs also have very different reputations. While some SOEs, particularly those from China, have attracted criticism for unsavory business practices or poor governance, the vast majority have not.¹⁸⁶ Many European SOEs, for instance, have been praised for their adoption of best corporate practices.

It is also important to highlight that SOEs have a long and largely uncontroversial history of investing and operating in Canada. Despite recent criticisms of SOEs within Canada's oil industry, state-backed firms, such as Norway's Equinor Canada Ltd. (formerly Statoil Canada Ltd.), have played a critical role in expanding energy production, boosting the national economy, and filling government coffers.¹⁸⁷ Indeed, in July 2018 it was announced that Equinor Canada Ltd. and its Canadian partner, Husky Energy Inc., had reached a financial arrangement with the Province of Newfoundland and Labrador to develop the \$6.8 billion Bay du Nord project, an off-shore oil play

¹⁸⁵ See Edwin M Truman, "A Blueprint for Sovereign Wealth Fund Best Practices" (2008) Peterson Institute of International Economics, Policy Brief 08-3, I-21, online (pdf): <piie.com/sites/default/files/publications/pb/pb08-3.pdf> [perma.cc/YW5P-BTUN]. The Caisse de dépôt et placement du Québec is an example of a Canadian public pension plan that is driven, in part, by the public policy goals of its political master, the Province of Québec. The Caisse has a "dual mandate" which includes not only maximizing the assets of depositors but also promoting economic development in Québec. See Andrew Willis, "Quebec's Caisse gets comfortable with dual investment mandate", *The Global and Mail* (14 July 2017), online: <theglobeandmail.com/report-on-business/streetwise/quebecs-caisse-gets-comfortable-with-dual-investment-mandate/article35697902/> [perma.cc/PX3A-86T6?type=image] for a discussion of recent investments the Caisse has made to advance the objectives of its political master.

¹⁸⁶ See Truman, *supra* note 185.

¹⁸⁷ Matt Krzepakowski & Jack Mintz, "Canada's foreign Direct Investment Challenge: Reducing Barriers and Ensuring a Level Playing field in the Face of Sovereign Wealth Funds and State-Owned Enterprises" (2010) 3:4 U Calgary School Public Policy Research Papers at 1, 9. The Business Council of Canada, which represents many of Canada's largest private energy companies, supports the proposition that SOE-led investment is generally beneficial. Speaking to a committee of Parliamentarians examining the ICA, the leading industry group stated: "[t]he presence of SOEs in Canada is not new...[o]ur oil sands have been developed with the participation of a range of SOEs that have a positive track record of investment". See Ailish Campbell, "Notes for remarks to the Standing Committee on Industry, Science and Technology re: proposed changes to the Investment Canada Act dealing with state-owned enterprises", Business Council of Canada (23 May 2013), online (pdf): <thebusinesscouncil.ca/wp-content/uploads/2013/05/Statement-to-the-House-of-Commons-Standing-Committee-on-Industry-Bill-C-60-ICA-changes-23-May-2013-FINAL.pdf> [perma.cc/Q664-GV6L].

which could unlock 300 million barrels of recoverable crude.¹⁸⁸ As a part of the deal, Newfoundland and Labrador is expected to receive \$3.5 billion in much-needed royalties, taxes, and profits over a 14 year period.¹⁸⁹

Unfortunately, the ICA ignores the diversity and history of SOEs. Instead of finding a principled manner to distinguish SOEs according to the risk that they may pose to Canada's economic security, the ICA is indiscriminate in its application to such investors. This approach is overbroad. It creates significant and unjustifiable barriers to entry for the vast majority of SOE investors who pose no risk to Canada.¹⁹⁰

J. SOEs Should Still Be Regulated, However

While the ICA's treatment of SOEs is overbroad, critics are correct when they concede that SOE-led investment may still pose a legitimate threat to Canada. There is little doubt that government-backed firms may be more susceptible to state influence given their ties to foreign governments. SOE investments in the oil sands is also potentially problematic. If SOEs were given unfettered access to the oil sands, it is at least conceivable that the sector could become subject to undue state influence as a result of the high concentration of ownership of energy assets in the oil patch. As such, critics are also right when they suggest that SOE investments should be regulated.

Critics of the ICA have different views on how state-backed investments should be regulated. Dobson, for instance, argues that the ICA's special treatment of SOEs should be eliminated. She states that "[r]ather than block [state-backed] capital [under the net benefit test], Canadian regulators should monitor the behavior of all firms to ensure standards are met for safety, environment, labour, transparency and national security."¹⁹¹ Woo has a slightly different view. He asserts that the regulatory burden SOEs face is disproportionate to the risks posed by such investors. Woo argues that since

¹⁸⁸ Shawn McCarthy, "Newfoundland reaches deal with Equinor and Husky to pursue deep-water oil project", *The Globe and Mail* (26 July 2018), online: <theglobeandmail.com/business/article-newfoundland-reaches-deal-with-statoil-and-husky-to-pursue-deep-water/> [perma.cc/Q4F3-TXHP?type=image] .

¹⁸⁹ *Ibid.*

¹⁹⁰ This approach is especially troubling given that the ICA's special treatment of SOEs was motivated by concerns relating to Asian state-backed investors. This is apparent by looking at the transactions which spurred the adoption of the SOE Guidelines and SOE Statement. *Supra* note 95.

¹⁹¹ See Dobson, *supra* note 180.

the risk factor of “SOEs boil down to security issues, the proper mechanism for assessing those risks [should be] the national security provisions of the ICA.”¹⁹² VanDuzer also questions the status quo, suggesting that the *SOE Guidelines* may not have been necessary.¹⁹³ He states that the “[broad] criteria to be used by the Minister to determine if an investment is a net benefit to Canada provides ample basis to apply the kinds of considerations identified in the [*SOE Guidelines*] in reviewing SOE investments.”¹⁹⁴

Other countries’ approach to reviewing SOE investments may also suggest that specialized SOE rules are unnecessary. Very few countries have adopted Canada’s approach to such investors. A 2015 OECD study on the foreign investment review regimes of member states found that most states treated private investors the same as SOEs. It found that only four of the 46 countries party to the *OECD Declaration on International and Multinational Enterprises* had specific restrictions concerning SOEs.¹⁹⁵

K. SOEs: Legal Uncertainty

Besides the problematic treatment of SOEs by the ICA, legal uncertainty stemming from those sections of the Act concerning state-backed investors creates another barrier to foreign investment. A major source of this uncertainty is the Act’s definition of a SOE. One of the key issues with the broad definition is that the term “influenced, directly or indirectly” is undefined, granting the Minister considerable discretion in making determinations regarding the meaning of these words. This discretion creates the risk that investors who are nominally private, because they are not controlled in law or in fact by foreign governments, will be found to be a SOE because of a connection they may have with their home government through, for instance, minority government ownership, the receipt of subsidies, commercial contractual relations, or relationships with government officials.¹⁹⁶

¹⁹² See Yuen Pau Woo, “Chinese Foreign Direct Investment in Canada: Threat or Opportunity?” (2014) 7:1 *China Economic J* 21.

¹⁹³ See VanDuzer, “Mixed Signals”, *supra* note 5 at 249.

¹⁹⁴ *Ibid.*

¹⁹⁵ See Shima, *supra* note 31.

¹⁹⁶ See Shuli Rodal, Michelle Lally, Peter Glossop & Peter Franklyn, “Proposed Amendments to Investment Canada Act Capture Control-in-Fact Investment by State-Owned Enterprises”, *Osler, Hoskin & Harcourt LLP* (2 May 2013) at 3, online: <osler.com/en/resources/cross-border/2013/proposed-amendments-to-investment

The inclusion of “individuals” within the definition of a SOE introduces another layer of uncertainty. It creates the risk that the appointment of government board members to the foreign investor’s board of directors or senior executives’ personal relationships with foreign governments will place the foreign investor, who is technically private, within the scope of the ICA’s SOE definition.¹⁹⁷

The problematic nature of the SOE definition is made especially clear by its application to Chinese investors. Every single Chinese investor could potentially fall within its scope given that China is “a nominally socialist economy with a Leninist political system.”¹⁹⁸

A separate, but related concern is uncertainty created by the Minister’s power to determine, including retroactively, that an otherwise Canadian-controlled entity is controlled in fact by a SOE.¹⁹⁹ This power creates uncertainty about when the Minister will find a minority SOE investment, otherwise falling beneath the statutory acquisition of control thresholds, to be an acquisition of control by a SOE that is subject to the ICA.²⁰⁰

The ICA Creates Significant Economic Costs

The ICA acts as an undue barrier to foreign investment. The magnitude of the Act’s impact on investors, industry, and society is likely significant.

The ICA is a Major Barrier to Investors

From an investor’s perspective, the ICA reduces Canada’s attractiveness as an investment destination. The ICA not only increases the transaction costs of implementing an investment, but the high opportunity cost of the review

canada-act-captu> [perma.cc/FHC5-JRT2].

¹⁹⁷ *Ibid.*

¹⁹⁸ See Woo, “Chinese Lessons”, *supra* note 170 at 30.

¹⁹⁹ See ICA, *supra* note 4, ss 28(6.1), 28(6.2), 28(6.3).

²⁰⁰ The Minister’s ability to make control in fact determinations also applies to private sector investments. It may therefore be argued that this power does not discriminate against SOE investors. While true on its face, the application of control in fact determinations to SOEs is potentially more problematic because of the more onerous screening criteria for state-backed investors. Further, given Canada’s concerns with government-backed investors, it is possible, and perhaps likely, that these powers would be used more frequently in relation to SOEs.

process, relative to jurisdictions with clearer and more certain processes, may also dissuade investors from investing in Canada.²⁰¹

There is some evidence supporting this proposition. While a myriad of factors contribute to Canada's attractiveness as a destination for foreign investment, the ICA has regularly been singled out as impairing Canada's appeal.²⁰² For instance, the OECD identifies the ICA's "screening and approval restrictions" as a key factor in labeling Canada as one of the most restrictive jurisdictions for foreign investment.²⁰³ Since the OECD's rankings of countries' openness to FDI began, Canada has consistently ranked as one of the most restrictive countries relative to its OECD peers as well as major non-OECD economies.²⁰⁴ Indeed, in the OECD's 2017 rankings, Canada

²⁰¹ See Sroka, *supra* note 45 at 19. Goldman and Koch note that investors consider the nature of countries' investment review regimes when making investment decisions. They argue that the fact that an investor's proposed investment may be subject to a review that a competitor may not otherwise face, may negatively affect the investor's competitive position. See Goldman & Koch, *supra* note 90 at 150.

²⁰² See Bergevin & Schwanen, *supra* note 10 at 6. Factors contributing to FDI accumulation are multiple and complex. While the ICA and the ease with which foreign investors can access a given market may be a key factor contributing to Canada's attractiveness as a destination for FDI, other factors independent of the ICA are also important, including the general economic environment and the business climate of the jurisdiction.

²⁰³ The OECD's figures need to be treated with caution, however. A number of prominent observers, notably the Competition Policy Review Panel, have noted that the OECD's rankings contain flaws. Critics have therefore argued that Canada's restrictions on FDI are not materially distinct from those in other jurisdictions. In particular, observers point out that the rankings do not account for informal barriers to foreign investment that exist in other countries, nor do they take into account how restrictive, arbitrary, or transparent the various screening and approval processes are in different jurisdictions. Given these flaws, critics argue that the OECD's rankings are skewed against Canada because the country's approach to regulating FDI is "more explicit and visible than the approach adopted in many other countries that employ informal barriers." See Competition Policy Review Panel, "Compete to Win", *supra* note 22 at 29-30; Bergevin & Schwanen, *supra* note 10 at 6-7. Other observers note that when Canada's performance in the OECD's rankings are compared to similarly situated economies with large and developed natural resource industries, especially Australia, Russia, and New Zealand, Canada's performance is much more competitive. As one researcher has suggested, FDI restrictions in resource dependent economies may be more common because of the unique characteristics of natural resources, including the fact that they tend to be of limited supply. See Library of Parliament, *supra* note 9 at 8-9.

²⁰⁴ See generally Organisation for Economic Co-operation and Development, 2006 *FDI Regulatory Restrictiveness Index: Revision and Extension to More Economies*, Working Paper No 525 (Paris, OECD, 2006).

ranked in 54th place, well behind the United States (45th), the United Kingdom (23rd), Germany (14th), as well as other industrialized countries which compete with Canada for FDI.²⁰⁵

Other considerations lend support to this argument. Chief amongst them is the declining volume of foreign investment in Canada. While Canada's total stock of inbound FDI as a proportion of GDP is relatively high among industrialized countries,²⁰⁶ the proportion of FDI in Canada relative to the overall volume of world foreign investment has been in steady decline over the last 30 years.²⁰⁷ Indicative of this trend, Statistics Canada announced in 2018 that investment inflows into Canada dropped 26% in 2017 to a seven-year low.²⁰⁸

UNCTAD's survey of transnational corporations' FDI spending intentions may also suggest that the ICA is degrading Canada's attractiveness as a destination for investment. After ranking as the 16th most attractive jurisdiction for investments in 2011-2013, Canada fell off the list in 2014-2016, a period roughly coinciding with the issuance of guidelines limiting SOE investment.²⁰⁹ While Canada returned to the list for 2017-2019, Canada ranked in 18th place, well behind the United States and other industrial economies.²¹⁰

²⁰⁵ See Organisation for Economic Co-operation and Development, "FDI Regulatory Restrictiveness Index" (2019), online: <oecd.org/investment/fdiindex.htm>.

²⁰⁶ FDI as a proportion of Gross Domestic Product in Canada is "more than twice the level in the United States and over 12 times the level in Japan." See Competition Policy Review Panel, "Compete to Win", *supra* note 22 at 29-30.

²⁰⁷ See Bergevin & Schwanen, *supra* note 10 at 1.

²⁰⁸ See Canada, Statistics Canada, Foreign Direct Investment, 2017, *The Daily* (Ottawa: SC, 2018), online: <50.statcan.gc.ca/n1/daily-quotidien/180425/dq180425a-eng.htm> [perma.cc/4S8Z-9B3J]

²⁰⁹ United Nations Conference on Trade and Development, "World Investment Report 2011", *Report* (Geneva: UNCTAD, 2011), online (pdf): <unctad.org/en/PublicationsLibrary/wir2011_en.pdf> [perma.cc/TZ3Z-WL92]; United Nations Conference on Trade and Development, "World Investment Report 2014", *Report* (Geneva: UNCTAD, 2014), online (pdf): <unctad.org/en/PublicationsLibrary/wir2014_en.pdf> [perma.cc/Y2JT-TTJS]

²¹⁰ United Nations Conference on Trade and Development, "World Investment Report 2017", *Report* (Geneva: UNCTAD, 2017), online (pdf): <unctad.org/en/PublicationsLibrary/wir2017_en.pdf> [perma.cc/ZA3V-YHZU]. It is noteworthy that Canada's ranking for 2017-2019 was published prior to several events which may negatively affect spending intentions, including American tax reform, uncertainty caused by the renegotiating of the NAFTA, and the inability of Canada to

L. The ICA May Harm Canadian Business

In terms of the ICA's broader impacts, the Act may indirectly increase Canadian businesses' cost of capital as well as depreciate the value of Canadian companies by reducing the number and quality of competitive bids for Canadian firms.²¹¹ These considerations may, in turn, impact the national economy by acting as a disincentive for Canadian businesses to invest in their assets and to grow their businesses domestically.²¹² A reduction in the number of competitive bids for Canadian businesses may also impair the general disciplinary effect of the market for corporate control. By decreasing the pool of potential acquirers of domestic businesses, the ICA reduces the threat to managers of underperforming Canadian businesses that an acquirer will launch a takeover of the business. As a result, managers of Canadian businesses will have greater incentives to engage in self-enriching activities instead of maximizing shareholder value, decreasing the performance of domestic companies and potentially the competitiveness of the Canadian economy.²¹³

M. The ICA's "Chilling Effect" on SOE-Led Investment

The ICA may also be restricting state-led investment in Canada. Many scholars and practitioners argue that the ICA's special treatment of government-backed investors have "chilled" investments in Canada by "send[ing] a negative signal to SOE investors, many of whom already view Canada as a hostile environment."²¹⁴ This may be one explanation for

execute large-scale capital projects, such as the Trans Mountain Pipeline project. See generally Andy Blatchford, "Investment is flowing out of Canada and into U.S. after tax changes, RBC president says", *CBC* (2 April 2018), online (pdf): <cbc.ca/news/business/royal-bank-investment-ceo-1.4602161> [perma.cc/YZ32-RF2J?type=image]; Shawn McCarthy & Adrian Morrow, "NAFTA uncertainty hurts job creation, foreign investment, Canadian ambassador warns", *The Globe and Mail* (5 February 2018), online: <theglobeandmail.com/report-on-business/canadian-ambassador-says-nafta-deal-possible-by-end-of-march/article37858468/> [perma.cc/8NGW-N5FF?type=image] ; Dan Healing, "Kinder Morgan's Trans Mountain pipeline woes having 'chilling' effect on investment in Canada", *The Financial Post* (9 April 2018), online: <business.financialpost.com/commodities/energy/kinder-morgan-canada-shares-open-lower-after-it-suspends-b-c-oil-pipeline-work> [perma.cc/KX8L-V6MP].

²¹¹ See Sroka, *supra* note 45 at 1.

²¹² See Bergevin & Schwanen, *supra* note 10 at 3.

²¹³ See J Anthony VanDuzer, *The Law of Partnerships and Corporations*, 3rd ed (Toronto: Irwin Law, 2009) at 529-530.

²¹⁴ See VanDuzer, "Mixed Signals", *supra* note 5 at 253; Steger, *supra* note 37 at 11.

Canada's declining global share of FDI, as SOEs have become an increasingly important source of foreign capital.²¹⁵ Indeed, following the issuance of the revised *SOE Guidelines* and the *SOE Statement* in 2012, foreign investment in the oil sands declined by 92% over the following year. Further, since 2012, no significant foreign acquisition has occurred in Canada's oil sands, with the exception of Repsol S.A.'s acquisition of Talisman Energy Inc. in 2015.²¹⁶

While many factors may have contributed to this trend, including the collapse in the price of oil in 2015, increased production and operating costs, and delays in the approval and construction of pipeline infrastructure,²¹⁷ Donnelly argues that changes to Canada's investment regime played a major role.²¹⁸ Donnelly argues that Canada sent a strong message to SOE investors that Canada's energy industry is now closed off. This message was likely very clear to countries like China, where businesses in the energy industry, are typically carried on by SOEs.

The ICA's potentially chilling effect on SOE investments is highly problematic given the capital-intensive nature of Canada's natural resource industries. Canada needs foreign investment in order to realize its competitive advantage in the natural resource sector. However, Canada's move to limit SOE investments reduces domestic businesses' access to capital and creates the risk that major resource projects will be underfunded. There is some evidence backing this argument. Beaulieu and Saunders, for instance, found that the issuance of the *SOE Guidelines* and *SOE Statement* coincided with a significant decline in the financial health and value of companies operating in the oil sands, especially junior energy companies whose growth and energy projects are highly dependent on external investment.²¹⁹ Referring to energy industry spending figures for 2017, Schwanen notes that Canada appears to be "falling

²¹⁵ See Paul Boothe, "Compete to Win: The Wilson Panel Report Six Years Later" (2015) *Canadian Council of Chief Executives*, online (pdf): <ceocouncil.ca/wp-content/uploads/2015/02/Boothe-paper-March-2015-FINAL.pdf> [perma.cc/WC4Q-AFTE]; Steger, *supra* note 37 at 11.

²¹⁶ See Perry et al, *supra* note 45.

²¹⁷ *Ibid*; See also Healing, *supra* note 210.

²¹⁸ See Donnelly, *supra* note 170 at 2.

²¹⁹ See Eugene Beaulieu & Matthew Saunders, "The Impact of Foreign Investment Restrictions on the Stock Returns of Oil Sands Companies" (2014) 7:16 *Calgary School Public Policy Research Papers* at 2.

behind its competitors in [energy production, an] area of traditional Canadian comparative advantage.”²²⁰

N. The ICA’s Reputational Risks

Scholars have also argued that the ICA risks damaging Canada’s reputation as a destination for investment. Canada has worked hard to brand itself as an attractive jurisdiction for investment with strong sectoral clusters, stable laws, a sound banking system, and a highly educated workforce.²²¹ Uncertainty in the investment review process undermines these efforts.²²² As Safarian remarks: “reputation is difficult to build on a global level and once reduced, it is hard to restore where alternatives exist for foreign investors.”²²³

A closely related issue is reciprocity. If Canada establishes a reputation of being hostile to foreign capital, Canada puts itself at risk that other countries will close themselves off to Canadian investments.²²⁴ The experience of the Canada Pension Plan Investment Board provides some, albeit limited evidence to support this proposition. The Canadian SOE has faced resistance to its

²²⁰ See Daniel Schwanen, “Foreign Direct Investment in Canada – The Case for Further Openness and Transparency” (2018) CD Howe Institute, E-Brief at 4, online: <cdhowe.org/sites/default/files/attachments/research_papers/mixed/FDI%20-%20The%20Case%20for%20Further%20Openness%20and%20Transparency.pdf> [perma.cc/JU3C-EHXD].

²²¹ See generally Canada, Global Affairs Canada, *Invest in Canada: An Overview 2017, Report* (Ottawa: GAC, 2017), online (pdf): <international.gc.ca/investors-investisseurs/assets/pdfs/download/2-Flagship_report_overview.pdf> [perma.cc/4YUZ-4S2M]; Economist Intelligence Unit, “Business Environment Rankings, 2017”, (2017) Economist Intelligence Unit, online (pdf): <iberglobal.com/files/business_climate_eiu.pdf> [perma.cc/9AY7-6DYL]; Economist Intelligence Unit, “Democracy Index 2016”, (2016) Economist Intelligence Unit, online (pdf): <felipesahagun.es/wp-content/uploads/2017/01/Democracy-Index-2016.pdf> [perma.cc/Q72D-5YBK]; KPMG, “Competitive Alternatives 2016”, (2016) KPMG, online (pdf): <mmkconsulting.com/compalts/reports/compalt2016_report_vol1_en.pdf> [perma.cc/3RB2-V2UF]; World Bank Group, “Doing Business 2017: Equal Opportunity for All”, (2017) World Bank Group Flagship Report, online (pdf): <documents.worldbank.org/curated/en/172361477516970361/pdf/109551-REVISED-PUBLIC.pdf> [perma.cc/MCP4-8ZQ4]; World Economic Forum, “The Human Capital Report 2016”, (2016) World Economic Forum, online (pdf): <3.weforum.org/docs/HCR2016_Main_Report.pdf> [perma.cc/8F68-KFX5].

²²² See Safarian, “Rule Book”, *supra* note 114 at 1.

²²³ *Ibid* at 13.

²²⁴ *Ibid* at 1-2.

investments abroad and has had to go to great lengths to explain to foreign governments that it operates at arm's length from the Canadian government. These challenges have been particularly troubling in the jurisdictions of foreign investors whose investments have faced increased scrutiny in Canada.²²⁵

VI. RECENT REFORMS ARE INSUFFICIENT

In response to criticisms of the ICA, Canada has amended the Act on a number of occasions. Schwanen, for instance, notes that in the 10 years since the Competition Policy Review Panel issued its seminal report detailing how the Act could be reformed, Canada liberalized the ICA by creating new reporting requirements, publishing guidelines which provide greater clarity on the operation of the Act, and eliminating special financial thresholds for investments in certain types of industries.²²⁶ However, such reforms have been piece-meal. They have not addressed underlying concerns with the ICA, such as uncertainty under the Act or its prejudicial treatment of state-backed investors.

The most recent reform to the ICA, enacted in 2017, was to increase monetary thresholds for the application of the net benefit test.²²⁷ On its face, this amendment reflects a rebalancing of the ICA in favour of foreign investment as it could ostensibly reduce the scope of review under the Act. However, the effect of increasing the ICA's financial thresholds on the Act's application in some circumstances will be mitigated by amendments made to the ICA in 2009.²²⁸ In 2009, Canada abandoned "asset" for "enterprise" value as the measure for determining whether an investment met certain monetary thresholds.²²⁹ Since an investment's "enterprise value", a measure linked to the market value of a company, is typically much greater than the accounting value of that firm's assets, which are based on historical prices, the shift to

²²⁵ See Andrea Mandel-Campbell, "Foreign Investment Review Regimes: How Canada Stacks Up" (2008) *Conference Board of Canada*, online (pdf): <conferenceboard-ca.uml.idm.oclc.org/temp/1344051c-fb22-4a32-a3de-9e64753c32b1/08-151HowCanadaStacksUp.pdf>

²²⁶ See Schwanen, *supra* note 220.

²²⁷ See *Budget Implementation Act*, 2017, No. 1, SC 2017, c 20, s 192.

²²⁸ See VanDuzer, "Mixed Signals", *supra* note 5 at 254.

²²⁹ See *Budget Implementation Act*, 2009, SC 2009, c 2, Part 13.

enterprise value expanded the scope of review under the ICA.²³⁰ As VanDuzer puts it: “[this] mean[s] that some investments will be subject to review that would not have been reviewable prior to the [2009] amendments.”²³¹

This is not to say that Canada’s move to increase the Act’s financial thresholds or to alter the measure of value under those thresholds is not desirable. They are welcome changes. Increasing the ICA’s monetary thresholds is consistent with the view that FDI is generally beneficial. Further, as the Competition Policy Review Panel noted: “the concept of enterprise value better reflects the increasing importance to our modern economy of service and knowledge-based industries in which much of the value of an enterprise is not recorded on its balance sheet because it resides in people, know-how, intellectual property and other intangible assets.”²³²

However, in light of the 2009 amendments, Canada’s most recent reform to the ICA may provide little additional benefit to investors. Furthermore, even if the reform does have the effect of narrowing the scope of review under the net benefit test, the federal government has once again failed to address underlying issues with the ICA.

VII. CANADA SHOULD ADOPT A NARROWER, MORE PRINCIPLED INVESTMENT REVIEW REGIME

The ICA fails to strike an optimal balance between encouraging foreign investment and protecting Canada’s economic security, reducing Canada’s ability to attract foreign capital. To address this issue, a narrower and more principled investment review regime should be adopted. The Trudeau government should introduce legislation (1) replacing the ICA’s “net benefit” threshold with a “national interest” standard, (2) eliminating or minimizing

²³⁰ “Asset value” is based on the Canadian company’s assets as recorded on its balance sheet at the end of the last completed fiscal year before the company’s proposed acquisition. Dollar figures that appear on a balance sheet are accounting, not fair market values. As such, relying on asset value may significantly understate the market value of a company with significant holdings of capital assets if the assets were acquired in the distant past. Furthermore, reliance on asset value may undervalue companies as some valuable assets of a business are not recorded on the balance sheet at all, including intangibles such as “goodwill” generated by the business or the quality of the firm’s employees. See Christopher C Nicholls, *Corporate Finance and Canadian Law*, 2nd ed (Toronto: Carswell, 2013) at 339-440.

²³¹ See VanDuzer, “Mixed Signals”, *supra* note 5 at 255.

²³² See Competition Policy Review Panel, “Compete to Win”, *supra* note 22 at 31.

the Act's prejudicial treatment of SOEs, (3) raising monetary thresholds for the application of the new national interest test, and (4) enhancing the functionality of Ministerial Opinions. These changes would address Canada's lagging attractiveness as an investment destination, while preserving the country's ability to safeguard the national economy.

A. Replacing the “Net Benefit” Test Has an Opportunity Cost

Before discussing my proposal, it is important to note that amending the Act has an opportunity cost. One of the benefits of the current scheme which may be lost in the amendment process is practitioners' accumulated knowledge of the regime. Like any established system, the net benefit test has the advantage of being known. Practitioners are accustomed to the ICA's text and are familiar with how the Act has been applied in the past. Investors can therefore rely on practitioners' expertise to avoid complications which may arise under the Act.

Another benefit of the Act from the government's perspective is that the ICA's discretionary nature provides the Minister with considerable “political coverage” as well as a tool to better effect the government's domestic and foreign policy agenda. While both considerations are important, it is hard to see how they could outweigh the disadvantages of the status quo or the advantages of the narrower, more principled investment review regime.²³³

B. Rejecting the ICA and the Investment Review Process is Bad Policy

It is also important to recognize that there is an opportunity cost associated with reforming instead of rejecting the investment review process. Eliminating the economic review process would undoubtedly enhance the allocative efficiency of the investment market by increasing the market's ability to distribute foreign investment funds to those businesses most in need of capital. However, while Canadian target businesses may benefit from an unrestrained investment market, unmitigated risks associated with foreign investment, such as foreign economic interference, may neutralize or outweigh these efficiency gains in some occasions. Therefore, adopting a narrower, more principled review regime capable of sufficiently managing these risks is likely to be more beneficial than rejecting the regime altogether.

²³³ See Sroka, *supra* note 45 at 18; Interview of former Minister of Industry by Trevor Neiman (20 June 2018).

C. The “Net Benefit” Test should be Replaced with a “National Interest” Assessment

In order to reform the ICA, the scope of the Act should be narrowed by replacing the “net benefit” threshold with a more limited “national interest” standard.²³⁴ Specifically, the Act should be amended so that a foreign investment could only be blocked if the Minister found the investment “likely to be contrary to Canada’s national interest.”²³⁵ Further, upon the investor filing a notification of the transaction with the Minister, the Minister should

²³⁴ Like the net benefit standard, the “national interest” threshold should not be defined. This will ensure that the Minister has sufficient flexibility to apply the test to the unique circumstances of every investment. Nevertheless, “national interest” should be viewed in narrow terms. Schwanen has suggested a list of factors that the Minister should consider when considering Canada’s national interests, including the negative impact of the investment on “competition, fiscal or financial stability, or [the] ability of the government to regulate in matters ranging from safety to the environment.” See Schwanen, *supra* note 220.

²³⁵ The “national interest” test, utilized in countries like Australia, has been endorsed by a number of experts, including the Competition Policy Review Panel. See generally Competition Policy Review Panel, “Compete to Win”, *supra* note 22 at 32; Bergevin & Schwanen, *supra* note 10 at 17; Donnelly, *supra* note 170; Schwanen, *supra* note 220. Australia’s foreign investment review process is different from the proposed regime in several material ways. Under Australia’s investment review regime, a foreign investor making an acquisition of a domestic business which requires approval under the Foreign Acquisitions and Takeovers Act 1975 must apply to the Foreign Investment Review Board before the completion of the acquisition. The Board examines the foreign investment proposal and advises on the Treasurer of Australia, the ultimate decision-maker, on the implications of the proposed investment on Australia’s national interest. The Treasurer must consider several enumerated, but vague worded factors to determine whether the proposal is consistent with the country’s national interest under Australia’s Foreign Investment Policy, a document which guides the interpretation of the Act. These factors include the impact of the proposal on (1) national security, (2) competition, (3) domestic laws and policies, (4) the domestic economy and community, as well as (5) the character of the foreign investor. Neither the Act nor the Policy indicate how or the extent to which the Treasurer is to consider these factors. The Treasurer, not the investor, bears the onus of showing that the proposal is contrary to the national interests of the country. If the Treasurer finds that the proposal is contrary to Australia’s national interests, he or she may deny the investor’s application and prohibit the investment. The Treasurer does not need to publicly disclose the reasons for his or her decision. See e.g. John Tivey, “National Security Reviews 2017: A Global Perspective Australia”, *White & Case LLP* (9 November 2017), online: <whitecase.com/publications/insight/national-security-reviews-2017-global-perspective-australia> [perma.cc/R9SL-D7T8]; George Gilligan, Justin O’Brien, & Megan Bowman, “Foreign Investment Law and Policy in Australia: A Critical Analysis” (2014) Centre for International Finance and Regulation, Working Paper no 008/2014.

be required to notify the investor within 30 days disclosing whether the transaction is reviewable under the new test. If the Minister (1) sends a notice to the investor indicating that the transaction is not reviewable or (2) fails to notify the investor that the proposed investment is subject to review within the prescribed period, then the transaction should be deemed approved.

Under the new standard, criteria used to evaluate the investment, including factors currently enumerated in section 20, should be reframed as individual questions with explicit thresholds.²³⁶ This would replace the existing approach of listing neutral factors. For example, under section 20 of the current ICA, one criterion the Minister must consider is “the effect of the investment on competition within any industry or industries in Canada.”²³⁷ The ICA should be amended to reframe this criterion as: “is the effect of the investment likely to materially threaten competition within any industry or industries within Canada?”

Since the Minister is in the best position to determine if an investment is contrary to Canada’s national interest based on these criteria, the Minister, instead of the investor, should bear the burden of proof under the new test. The Minister should also be required to complete a national interest review within 45 days, with the investor having the option to extend that period for an additional 15 days.²³⁸ When the Minister does make a determination under the new test, the Minister should be obligated to provide explicit reasons for why a proposed investment failed or succeeded to meet the new threshold.

D. The National Interest Test Responsibly Narrows the Scope of Review

An advantage of the national interest standard is its effect on responsibly narrowing the scope of Canada’s economic screen under the ICA.²³⁹ By

²³⁶ An approach similar to this was proposed by Bergevin and Schwanen. See Bergevin & Schwanen, *supra* note 10 at 17.

²³⁷ See ICA, *supra* note 4, s 20.

²³⁸ The review period should be capped at 60 days. Under the current system, where there is no cap, the investor may often feel pressure from the Minister to agree to extend the review period past 75 days for an additional period. While capping the review period may negatively impact some investors at the margins, speeding up the review process will be more beneficial to investors on a whole.

²³⁹ The national security test under the ICA could be eliminated and subsumed by the new national interest standard. While a full analysis of this issue is well beyond the scope of this paper, a preliminary analysis suggests that collapsing the two tests is fraught with risks.

replacing the net-benefit test with the national interest test's higher threshold, Canada limits the Minister's discretion to reject an investment. The test will therefore encourage greater investment by limiting Canada's review of investment proposals and by signaling to the world that in all but exceptional circumstances, Canada will treat foreign investors' transactions no different than domestic acquisitions. Moreover, the test should achieve this objective all while maintaining Canada's economic security. The net benefit test is not necessary to protect Canada's national economy because the national interest standard, while admittedly limiting Canada's room to maneuver, should still provide the federal government with sufficient regulatory authority to reject investments that represent a threat to the national economy.

E. The National Interest Standard May Reduce Political Interference

The national interest test is also advantageous because it may reduce political interference in the review process. While the "national interest" standard is arguably as vague as the current threshold,²⁴⁰ meaning that the

While adopting a single national interest test could reduce uncertainty and transaction costs for investors under the Act by streamlining the investment review process, given the problems plaguing the national security screen, including the test being applied in an overly broad manner, importing the test into the national interest standard is likely to result in an expansion of the review process and increased uncertainty for investors. Australia's experience provides some insight into this issue. Australia's national interest test requires consideration of national security considerations. A number of scholars have argued that this enhances uncertainty for investors given the manner in which the Treasurer has expansively interpreted Australia's national security interests. See e.g. Andrew Lumsden & Corrs Chambers Westgarth, "The 'National Interest Test' and Australian Foreign Investment Laws", *Centre for Law and Markets and Regulation*, University of New South Wales, online: <clmr.unsw.edu.au/article/market-conduct-regulation/state-capital/the-%E2%80%9Cnational-interest-test%E2%80%9D-and-australian-foreign-investment-laws> [perma.cc/5Z5R-JF52]. In order to avoid this outcome, the two tests in Canada should likely be kept separate at this juncture.

²⁴⁰ Scholars in Australia have criticized their country's own national interest test for its ambiguous nature which has resulted in accusations that the test has been abused by political decision-makers to serve their own electoral interests. For instance, Lumsden and Westgarth argue that the definition of "national interest," which is not defined in the law governing Australia's review process, cannot be defined in any meaningful way. Indeed, they argue that the definition has changed over time depending on the mood of the Australian government and people. See Lumsden & Westgarth, *supra* note 239. However, it is important to note that unlike my proposal, Australia's governing legislation does not provide detailed guidelines against which the national interest standard can be assessed.

review process will still be subject to some political interference, concerns with the standard and the discretionary nature of the review process would be addressed by the reframed evaluative criteria under the Act, as well as by the requirement that the Minister provide explicit reasons for his decisions.

The reframed evaluative criteria limit discretion by establishing thresholds that the Minister must consider when evaluating an investment. This reduces subjectivity in the decision-making process by putting new restrictions on how the Minister considers factors under section 20. However, by stopping short of setting relative weights to each criterion, the new criteria preserve some ministerial flexibility, vital to allowing the Minister to evaluate transactions according to their unique circumstances.²⁴¹

More importantly, political interference is addressed by the requirement that the Minister provide detailed reasons for either accepting or rejecting a proposed investment. From such disclosures, a comprehensive body of justifications would develop allowing civil society to assess the reasonableness of the Minister's decisions. Any deviation from past determinations in the Minister's decision-making could then be checked against.²⁴²

Disclosures under the national interest test are much more practical than under the current model. Since the national interest standard is focused on government policy instead of the proprietary plans of the investor, the Minister is much better positioned to publicly disclose detailed reasons.²⁴³ The national interest test therefore overcomes a significant barrier to disclosure under the

Nor does legislation provide any indication of how the vague guidelines that do exist should be considered. Finally, Treasurer of Australia is not obligated to provide reasons for his or her decision to reject or approve an investment decision. Because my proposed national interest test adopts these safeguards, one can expect that the standard will become better defined over time and that it may be less susceptible to political manipulation. See Gilligan, O'Brien & Bowman, *supra* note 235.

²⁴¹ Sroka has argued that the ICA should be amended to replace the Minister's discretionary review of factors under section 20 with a quantitative scoring system with different weights set to the evaluative factors depending upon the nature of the investment. While this approach may provide for greater ministerial accountability, especially if review results are made public, it is not recommended that this approach be taken. It may unduly limit the Minister's ability to utilize his discretion to deal with investments that arise in unique circumstances. Further, the approach is likely a non-starter from a political perspective, given government's desire for flexibility and control. See Sroka, *supra* note 45 at 19-20.

²⁴² *Ibid* at 18.

²⁴³ See Bergevin & Schwanen, *supra* note 10 at 17.

net benefit test, namely, confidentiality concerns related to the investor's proprietary information.

F. The National Interest Test Could Reduce Transaction Costs

An added perk of the national interest test is its possible impact on investors' transaction costs. Over time, the new standard, and particularly its reverse onus, should reduce the amount of work and expense required to submit an investment proposal, reducing the Act's regulatory burden.²⁴⁴ Moreover, disclosure under the national interest test would also have the added benefit of providing third parties with greater clarity on how the test would be applied in the future. While not binding on the Minister, these reasons would establish expectations which would enhance certainty in the application of the ICA, minimizing risk and costs to investors. The requirement that the Minister's reasons be made public would also be much more consistent with Canada's international reputation for transparency and sound governance. This would boost Canada's reputation amongst investors and encourage greater investment.

G. Canada Should Eliminate its Discriminatory Treatment of SOEs

Besides adopting a new national interest test, Canada should eliminate the ICA's prejudicial treatment of government-backed investors.²⁴⁵ Where concerns with a SOE investment arise, they should be addressed through laws of general application or, where duly justified, the ICA's national security provisions. This more principled approach to regulating state-led investments rests on four propositions. First, Canada's indiscriminate treatment of SOEs is disproportionate to the risk that they pose. Therefore, by eliminating specialized SOE provisions, Canada will acknowledge that the majority of SOEs pose minimal or no risk to Canada's economic security and that state-led investments have played, and will continue to play, an important role in the Canadian economy. Second, eliminating the Act's prejudicial treatment of

²⁴⁴ See Donnelly, *supra* note 170 at 10. The new national interest standard may increase Canada's costs of reviewing transactions under the ICA. However, these costs may be offset by the fact that there would likely be fewer reviews under the ICA once the new standard was adopted.

²⁴⁵ For instance, the ICA's separate financial threshold for the application of the net benefit test to SOEs, the distinct evaluative criterion under the SOE Guidelines, and limitations on SOE investments in the oil sands under the SOE Statement should be eliminated.

SOEs levels the playing field between private sector and government-backed investors. This signals to the world that Canada is open to state-backed investments, a growing source of FDI. Third, removing SOE-specific provisions under the Act recognizes that SOEs do not operate at will in Canada and that laws of general application play an important role in checking SOE activities.²⁴⁶ And lastly, since the threat that SOEs pose to the national economy may be better characterized as issues of national security, it is more appropriate to screen SOE investments, where necessary, using the ICA's national security test.²⁴⁷

H. Alternatively, Canada Should Minimize its Discriminatory Treatment of SOEs

It may not be realistic to expect that Canada will depart radically from its position on SOEs under the ICA given Canadians' sensitivities.²⁴⁸ If Canada is resistant to eliminating the ICA's special treatment of state-led investments, the Act should be amended to minimize its discriminatory impact.

I. Eliminate the Separate SOE WTO Financial Threshold

To minimize the ICA's discriminatory treatment of government-backed investors, the Act should be amended to create a single financial threshold for WTO Investors, irrespective of whether the investor is a SOE. Eliminating the separate SOE WTO Investor threshold would repair Canada's damaged reputation amongst SOE investors as well as reduce uncertainty created by the Act's problematic definition of SOEs. For instance, with a single financial threshold for WTO Investors, investors with a proposed investment with a transaction value above \$398 million in asset value, but under \$1 billion in enterprise value, would no longer worry whether the Minister would find them to be a SOE under the ICA and thus be subject to the Act's economic screen.²⁴⁹

²⁴⁶ Amendments to domestic laws should be made where they are necessary to sufficiently regulate the activities of SOEs in Canada.

²⁴⁷ It is not suggested that the scope of the ICA's national security review be expanded in order to accommodate the review of SOEs.

²⁴⁸ Canadians are overwhelmingly opposed to state-led investment in Canada. See note 182.

²⁴⁹ See Donnelly, *supra* note 170 at 10.

J. Key Terms Relating to SOE Investments Should be Clarified

The ICA should also be amended to clearly define key terms relating to SOE investments. In particular, the ICA should be amended to define what constitutes “influenced, directly or indirectly” for the purpose of defining a SOE under the Act. The Minister’s current discretion to interpret these terms as he sees fit creates unnecessary risks for investors. Concretely defining “influenced, directly or indirectly” so as to minimize ministerial discretion and to allow investors to better determine when they will be found to be a SOE may encourage greater investment from entities who are deterred from investing in Canada because of the implications of being deemed a SOE.

The Minister should also exercise his authority to eliminate restrictions under the *SOE Statement* on SOE investments in the oil sands. If Canada is unwilling to adopt this measure, the Minister should at the very least provide public guidance on what constitutes “an exceptional basis” in the *SOE Statement* for the purpose of SOE oil sands investments.²⁵⁰ Any guidance should be framed in a similar fashion to the proposed evaluative criteria under section 20 of the Act.

K. Eliminate the Minister’s “Control in Fact” Power

The ICA should be amended to eliminate the Minister’s discretionary power to make control in fact determinations in relation to SOEs. The Minister’s ability to analyze all investments involving a government-backed investor, irrespective of the proposed interest in the Canadian business, to determine whether the transaction confers “control in fact” on the investor introduces too much uncertainty for minority SOE investors. This uncertainty is magnified by the Minister’s ability to make these determinations retroactively. Given the more onerous review requirements for SOEs under the ICA, determinations of control for SOEs should be based solely upon the established statutory thresholds so as to create a “statutory safe harbour” for minority SOE investors.

L. Raise Financial Thresholds

To further liberalize Canada’s investment regime, the ICA should also be amended to increase the financial thresholds for the application of the new national interest test. At the very least, financial thresholds should be increased

²⁵⁰ See Industry Canada, “*SOE Statement*”, *supra* note 32.

to offset the impact that the ICA's 2009 amendments had on expanding the scope of the Act.

M. Enhance the Functionality of Ministerial Opinions

Lastly, to address uncertainty under the Act in a more general fashion, the ICA should be amended to enhance the functionality of Ministerial Opinions. Ministerial Opinions currently minimize uncertainty for individual applicants, but not third parties. Where possible, Ministerial Opinions, like “Advanced Rulings” under the *Income Tax Act*,²⁵¹ should therefore be made publicly-available to others.²⁵² While Ministerial Opinions should not be binding on the Minister with respect to third parties, publicly-available opinions would nevertheless be invaluable. They would create expectations on how the Minister would interpret provisions and exercise discretion under the ICA. This would enhance certainty under the Act, especially with regard to the ICA's application to state-backed investors.²⁵³

VIII. CONCLUDING REMARKS

Canada's openness to foreign investment has shifted over time. Canada's investment review regime, enacted to impose limits on FDI in the name of economic nationalism, has gradually liberalized. Despite this trend, a more restrictive approach to foreign investment has returned in recent years. While Canada remains open to most foreign investors, it has created significant barriers for SOEs, limiting Canadian businesses' access to much-needed foreign capital. This approach – adopted in an era where SOEs play an increasingly important role in international business – has failed to appropriately balance investment with Canada's economic security.

²⁵¹ See Vern Krishna, *Income Tax Law*, 2nd ed (Toronto: Irwin Law, 2012) at 566-567.

²⁵² Like Advance Rulings, details about the identity of the applicant or confidential investor information should not be disclosed to the public. Because of the small number of transactions reviewed each year by the Minister, it will not always be possible to make opinions public without disclosing some of this information indirectly. Where this information could be gleaned by the nature of the transaction described in the opinion, the Minister should be authorized to keep this information private.

²⁵³ The Business Council of Canada has stated that many of its members have significant concerns with the ICA's definition of a SOE. The industry group requested that Ministerial Opinions be used to address such concerns. See Campbell, *supra* note 187.

To address this issue, a narrower and more principled investment review regime should be adopted. The ICA should be amended to adopt a new national interest test, the Act's prejudicial treatment of SOEs should be eliminated or minimized, monetary thresholds for the application of the new national interest test should be raised, and the functionality of Ministerial Opinions should be enhanced. These reforms would go a long way in improving Canada's attractiveness as an investment destination, while providing the federal government with a more principled approach of protecting the Canadian economy.