Is There a Chill in the Air? Recent Decisions under the *Investment Canada Act* (Canada)

Including the *Attorney General of Canada v. United States Steel Corporation and U.S. Steel Canada Inc.*

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Introduction

It has been an interesting time for Prime Minister Harper and foreign takeovers in Canada. You might be excused for wondering how it is that a Conservative government is the only federal government in the 25 years of the existing legislation involving reviews of foreign acquisitions to both block foreign acquisitions (2) and bring enforcement action in Court for breach of undertakings in respect of a foreign acquisition (1)[1]. Previous Liberal and Conservative governments allowed significant foreign acquisitions to proceed – even of what were argued at the time as 'Crown jewels' of the Canadian economy. Has something changed? Is this a trend, and is it likely to result in any further changes or guidance on the key elements required for approval by the Investment Review Division of Industry Canada ("**Investment Canada**") of future acquisitions?

Since 1985 when the ICA was introduced to replace the old "Foreign Investment Review Act", the federal government has reviewed more than 1,600 acquisitions and, other than a proposed acquisition of a division of Macdonald Dettwiler in 2008 and the proposed acquisition of Potash Corp. by BHP, all were approved.

This paper will cover, in particular, the case of *The Attorney General of Canada v. United States Steel Corporation and U.S. Steel Canada Inc.*[2] (the "**US Steel Case**") as well as the most recent decision to reject the proposed acquisition by BHP Billiton, an Australian corporation, of Potash Corp., a "Canadian business" under the ICA. While prognostications on what these recent actions by the Federal Government might mean for future acquisitions is extremely difficult, there are certain strategies that might be employed by potential acquirers gleaned from the learning in these decisions. The federal government has also advised that it will provide greater clarity on the 'net benefit to Canada' test. At the time of writing, such guidelines have not been released.

Background to the ICA

Unlike other regulatory approval regimes, such as competition review under the *Competition Act* (Canada), review under the *Investment Canada Act* R.S., 1985, c. 28 as amended by *An Act to Amend the Investment Canada Act*[3] (the "**ICA Amendment**") (as amended, the "**ICA**"), is inherently political. The determination in any particular case is made by the Minister of Industry.

The stated purpose of the ICA is:

[1] For a table of total investments reviewed/notified from 1985 through to September 30, 2010, see Appendix A to this paper.

[2] Federal Court of Canada Trial Division (2010 FC 642)

[3] Bill C-59 introduced certain amendments to the ICA, and included a change to the review thresholds, the latter of which has yet to be proclaimed in force.

> "Recognizing that increased capital and technology benefits Canada, *and recognizing the importance of protecting national security*[4], the purposes of this Act are to provide for the review of significant investments in Canada by non-Canadians in a manner that encourages investment, economic growth and employment opportunities in Canada and to provide for the review of investments in Canada by non-Canadians that could be injurious to national security."[5]

Under the ICA, Industry Canada will review a foreign investment if the value of the acquired assets used in the Canadian business is equal to or greater than C$5 million for a direct acquisition. A direct acquisition is the acquisition of substantially all of the assets or a majority (in certain cases 1/3rd or more) of the shares or voting interests of the entity carrying on business in Canada. An indirect acquisition is only reviewable if either (i) the value of the assets in Canada represents less than or equal to 50% of the value of all of the assets acquired in the transaction and the value of the Canadian assets is C$50 million or more *or* (ii) the value of the assets in Canada represents more than 50% of the assets acquired in the transaction and the value of the Canadian assets is C$5 million or more.

Notwithstanding the above thresholds, however, under an agreement establishing the World Trade Organization ("WTO"), a special status is conferred upon nationals of WTO member states and the entities controlled by them. There are two primary advantages. First, other than an acquisition in one specific "sensitive" industry described below, indirect acquisitions by a WTO investor are not reviewable. Secondly, the investment threshold limit that triggers review is higher for WTO investors. At present, the threshold for review is C$299 million. As a result of the ICA Amendment, the thresholds for review of investments proposed by WTO investors will increase to an "enterprise value" of C$600 million. That threshold will remain in effect for two years after which it will increase to C$800 million for one year and increase again the following year to C$1 billion. Thereafter, the threshold will increase annually based on GDP. These new thresholds however, have not yet been proclaimed in force. Any transaction below the applicable threshold is not reviewable unless the Canadian business is a "cultural" business. If an investment falls within this prescribed business activity then the investment is subject to review and approved by the Minister of Canadian Heritage.

If a proposed investment is subject to review, and is not in respect of a "cultural business", the Minister of Industry, will, on recommendation of Investment Canada, either approve or reject the proposed investment. Investments in respect of a "cultural business" related to national identity are the responsibility of the Minister of Canadian Heritage. A cultural business is a business carrying on the following activities (a) publication, distribution or sale of books, magazines, periodical or newspapers in print or machine readable form, other than the sole activity of printing or typesetting of books, magazines, periodicals or newspapers; (b) the production, distribution, sale or exhibition of film or video recordings; (c) the production, distribution, sale or exhibition of audio or video music recordings; (d) the production, distribution or sale of music in print or machine readable form; or (e) radio communication in which the transmissions are

[4] Text added in 2009 amendments.

[5] Section 2 of the *Investment Canada Act*

intended for direct reception by the general public, any radio, television and cable television broadcasting undertakings and any satellite programming and broadcast network services.[6] Many of these activities have foreign ownership restrictions in any event, such as broadcasting, which are required to be complied with as well.

The Minister of Industry has the power to order divestiture of control of a Canadian business that is the subject of an investment. Where a proposed investment is rejected, the ICA allows for negotiations to take place between Investment Canada and the investor to amend the terms of the application. Additional commitments, plans or undertakings with respect to the expenditure of certain amounts on capital or technology, the maintenance or increase of employment levels, Canadian participation in senior management and the retention of head office functions in Canada may be necessary to attain approval. Investment Canada, in the course of its review, will seek input from provincial governments or other government departments that they believe may be affected by, or have an opinion on, the investment.

If a review is required, then Investment Canada must, within 45 days after receipt of a complete review application, advise the investor whether or not the investment is, in the view of the Minister, of "net benefit" to Canada. The Minister is entitled to a 30-day extension, on notice to the investor, for completion of the review. After such time, the Minister may request an extension, which must be mutually agreed to by the investor. The Minister has taken the position, although not supported by legislation, that if a proposed transaction is still in review by the Competition Bureau, then the Minister will not approve the investment as a net benefit to Canada until the Bureau has completed its analysis and does not propose to refer the merger to the Tribunal.

Review Process and Undertakings

Foreign acquirers may offer, or be asked to provide, certain 'undertakings' under the ICA. These are written commitments to the Crown to fulfill certain matters in connection with the investment in the Canadian business and to have those monitored by the Federal Government for a period of time. Typically, the investment is reviewed on the date which is 18 months after implementation. If, at that stage, there appears to be substantial compliance with the undertakings and plans submitted by the investor at the time of the review, at least consistent with original expectations and subsequent economic circumstances, and if there are no further major economic commitments to be fulfilled, then there will be no further monitoring. If there is a deficiency in compliance, the Minister and the investor will together determine an appropriate time for future follow-up, typically a further eighteen month period of monitoring.

[6] Section 14.1(6) of the ICA

National Security

Pursuant to amendments to the ICA by virtue of the ICA Amendment[7], a new national security test provides for the Minister of Industry to make a recommendation to cabinet to block a merger on national security grounds. If the Minister of Industry, after consultation with the Minister of Public Safety and Emergency Preparedness, and following representations which may be made by an investor, is satisfied that the investment could be "injurious to national security", the Governor in Council (the Governor General acting on the advice of the Federal Cabinet) may take measures considered advisable to protect national security including prohibiting completion of the investment or, if an investment has been completed, the divestiture of the investment.

In September, 2009, the Minister of Industry introduced the national security review of investments regulations[8]. More interesting than the technical implementation provisions of the Act that are introduced by the new regulations (such things as the relevant agencies to whom information may be disclosed in such a review, which is a lengthy list) is the regulatory impact analysis statement that accompanied the regulations. National security threats are generally brought to the attention of the Minister through Canada's security and intelligence agencies (and yes, information submitted to Investment Canada can be disclosed to CSIS and to the RCMP). The new section of the ICA applies regardless of whether an investment is subject to review under the Act. In other words, a proposed acquisition of a Canadian business that, for example, falls below the current C$299 million threshold for review, might still be found to be potentially injurious to national security. If an investor receives a notice prior to closing, then they are then prohibited from completing the investment until the Minister gives notice that the investment is acceptable, generally 45 days after the Minister becomes aware of the investment, and extendable if there is expressed concern. If the investment has closed, which may certainly have been the case in an investment requiring only notification rather than review, the Governor in Council to whom the Minister has referred the concern, many order divestment.

What is "Net Benefit to Canada"

The ICA sets out certain criteria by which the Minister will assess whether an acquisition by a foreign entity meets the 'net benefit to Canada' test. These are:

- the effect of the investment on the level and nature of economic activity in Canada including employment, resource processing, utilization of parts, components and services produced in Canada and exports from Canada

- the degree and significance of participation by Canadians both in the Canadian business but also in any industry or industries of which the Canadian business forms, or would form a part

[7] The introduction of the "national security" amendment was after the Government's decision in MDA referred to in this paper.

[8] Canada Gazette Part II, Vol. 143, No. 20 (September 17, 2009)

- the effect of the investment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada
- the effect of the investment on competition in Canada
- the compatibility with national industrial, economic and cultural policies
- the contribution of the investment to Canada's ability to compete in world markets.

The test is broad and discretionary. The Minister has tremendous latitude to assess submissions in a review process, and if necessary, require undertakings of an investor to more specifically address net benefit criteria.

What does Investment Canada look for? Some commentators have suggested that investors merely go through a bit of a 'check the box' exercise in filing an application for review. If various key 'net benefit' categories listed above can be positively answered, then the investor generally expects that it will meet the Minister's requirements. For example, keeping the headquarters of the Canadian business in Canada, maintaining or, even better, enhancing employment opportunities in Canada, indicating that the strength of the international presence of the acquirer will bring market opportunities (i.e. export) to the Canadian business, outlining the financing capabilities of the acquirer which will lead to increased capital expenditures in the Canadian business – these are all positive indicators to achieving the positive approval of the Minister, without undertakings and consequent monitoring requirements.

Beware negative disclosure. Most acquirers will do what they need to do to meet profitability objectives. That is certainly understood. However, a fistful of positive net benefit criteria can be thrown off by plans to 'act on synergies by rationalizing a Canadian division' (or words to that effect). While the guidelines refer to assessments being made on the basis of measuring the aggregate net effect after offsetting negative effects against positive effects, it is incumbent on the investor to point out the weighting towards a net favourable effect. If possible, steps should also be taken to ensure minimal impact, including steps proposed to be taken to minimize the effect of any negative consequences. If there are disclosed closures, or expected reductions in employment arising from the proposed investment, then Investment Canada will more likely look to offset such negative results of the transaction with undertakings imposed upon the investor concerning the positive net benefit to Canada portions of the investor's application. If a transaction's economics warrant 'bad news' types of post-integration steps, the investor should consider the implications, both from a timing perspective and from the perspective of offering and fulfilling undertakings early in its transaction assessment.

State Owned Enterprises

The only specific guidance that Investment Canada has issued to date with respect to 'net benefit to Canada' (other than a guideline with a recitation of the net benefit criteria) concerns 'state owned enterprises' ("SOE's")[9]. Specifically, the Government set out that, in respect of SOE's

[9] Guidelines — Investment by state-owned enterprises — Net benefit assessment issued in October, 2007

proposing to acquire Canadian businesses, the Minister will review such investments, as with all other investments, in accordance with the net benefit to Canada test. In particular, though, SOE's should be aware that the Minister will pay particular attention to the corporate governance and reporting structure of the SOE, whether the SOE "adheres to Canadian standards of corporate governance (including, for example, commitments to transparency and disclosure, independent members of the board of directors, independent audit committees and equitable treatment of shareholders), and to Canadian laws and practices"[10]. The examination will also cover how and the extent to which the non-Canadian is owned or controlled by a state.

Although SOE acquisitions of Canadian businesses represented, at the time of the introduction of the guideline, only about two percent of all acquisitions subject to review, the government was particularly concerned about SOE foreign acquisitions in the resource/commodity sector in Canada. To that end, the government set out certain matters that it intended to assess in the context of a net benefit to Canada test, including whether the Canadian entity would, following the completion of the acquisition by the SOE, still be able to operate on a commercial basis with respect to (i) where to export; and (ii) where to process; as well as with respect to (iii) the participation of Canadians in the operations both in Canada an abroad; (iv) the support the entity would have in innovation, research and development; and finally, (v) that an appropriate level of capital expenditure would be made to maintain the Canadian business in a globally competitive position. The Government, therefore, was concerned about Canadian businesses being acquired by SOE's simply to secure a steady supply of a commodity, without further effort to advance the business on its own merits.

Plans and Undertakings

An investor required to submit an application for review of a proposed acquisition must, as part of the application, include "a detailed description of the investor's plans for the Canadian business with specific reference to the relevant factors set out [in the Act]."[11] The guidelines helpfully suggest that investors include as much detail in the submitted plans as possible. Doing so will reduce the likelihood that undertakings will be necessary to implement the plans. An undertaking may be required by the Minister and offered by an investor to achieve a positive review. If an investor provides an undertaking, but fails to comply with any one or more undertakings, the Minister may send a demand for compliance within a specified time. If there is still no compliance following demand, the Minister may apply to Court for an order to, among other things, direct the investor to divest control of the investment, direct compliance with the undertaking or impose a penalty no exceeding C$10,000 for each day the investor is in contravention of its undertakings.

What usually happens when an investor fails to meet its undertakings?

There is a fair degree of cynicism with respect to whether undertakings mean anything or whether investors will live up to them. US Steel committed to some 31 undertakings in respect of its acquisition of Stelco. In the case of BHP's proposed acquisition of Potash Corp., referred

[10] *Ibid* note 9

[11] Schedule II – Investment Canada Regulations

to later in this paper, BHP indicated that it made numerous promises to the Government, including as would be applicable to the Government of Saskatchewan. Arguably, BHP set the bar very high in terms of prospective undertaking requirements.

Aside from US Steel's acquisition, there have been various acquisitions where significant undertakings, including with respect to employment, had been given to the Government, and yet, arguably, not complied with. At least to the casual observer, there are similarities between the US Steel acquisition and Companhia Vale do Rio Doce's acquisition of Inco and Xstrata's acquisition of Falconbridge where net benefit commitments such as continued (or increased) employment or sustained (or increased) production were most likely given by way of undertaking to the Government, and in both cases, where actions on the part of the acquirers caused such commitments to fall short. Following each of the Vale and Xstrata acquisitions, each of the acquirers laid off employees and curtailed production in large part as a response to declining metals prices. Neither was challenged by the Government.

The US Steel Case

That brings us to the US Steel Case. What perhaps surprised many is that a court action was brought at all. Given the background of a significant global recession, that Stelco, the Canadian business acquired by US Steel had only emerged from creditor protection some three years prior, at the very least it brought question to whether this was *the* case that the Government wanted to flex its muscle with. Nevertheless, the case is underway, and while we have yet to know the outcome, there is some interesting learning from the proceedings.

Background to the US Steel Case

United States Steel Corporation ("**US Steel**"), proposed to acquire through 1344973 Alberta ULC (now U.S. Steel Canada Inc.) control of Stelco Inc. US Steel is an American corporation, and was therefore subject to the provisions of the ICA. As such, US Steel filed the prescribed application for review under the ICA and then met with officials of Investment Canada to discuss the proposed investment. Following those meetings, US Steel submitted thirty-one written undertakings to the Minister of Industry in support of its acquisition. The term of the undertakings was three years. According to US Steel's factum (August 26, 2009) in the US Steel Case, the wording of the relevant undertakings at issue were:

> "4. The Investor will increase the annual level of production at the Canadian business by at least 10% over the Term (excluding periods of interruption in production due to capital investment projects) relative to the average of the last three completed calendar years; and
>
> 10. Over the Term, the Investor will maintain an average aggregate employment level at the Canadian business of not less than 3,105 employees on a full-time equivalent basis if the bar mill continues to be operated, or 2,790 employees on a full-time equivalent basis if the bar mill is sold or closed."[12]

[12] US Steel Factum (August 26, 2009) – paragraph 7.

The $1.5 billion transaction closed in October, 2007.

At the time of its acquisition, US Steel, as a 'non-Canadian' acquirer was required to submit to review under the ICA. According to US Steel's Factum, on October 10, 2007, US Steel submitted 31 written undertakings to the Minister of Industry arising from its application for review under the ICA. US Steel asserts in its Court documents that it made those undertakings on the basis of its projections for steel in 2007. As a result of the sudden turn in the world economy, and in particular the effect of the recession in the US, those projections turned out to be significantly optimistic. In March, 2009, US Steel closed its Hilton (Hamilton) and Lake Erie mills, laying off some 1,500 employees.[13] That announcement followed previous layoffs of 700 employees at the Hamilton mill as a result of a shutdown of the mill's blast furnace in November, 2008. Looking through the lens of 2008, US Steel argued, the expectations of demand for steel were vastly different. The dire straits that the automobile industry, consumer appliance industry and the oil and gas industry found themselves in starting in 2008, all affected US Steel.

According to US Steel's Factum, on May 5, 2009, the Ministry of Industry sent a demand letter to US Steel, requiring a response with respect to the non-fulfillment of two of US Steel's undertakings. Specifically, the demand issued to US Steel was for compliance with the following undertakings:

(i) increasing steel production at the Canadian Business, such that (1) in the period from November 1, 2007 to October 31, 2009, steel production at the Canadian Business is greater than or equal to a total of 8,690,000 tons (2 x 4,345,000); and (2) in the period from November 1, 2009 to October 31, 2010, steel production at the Canadian Business is greater than or equal to 4,345,000 net tons; and

(ii) taking all such steps as are necessary to ensure that over the Term of the Undertakings [US Steel] maintain an average level of employment at the Canadian Business of 3,105 employees on a full time equivalent basis.

US Steel responded, in writing, outlining the change in economic circumstances for steel generally and US Steel in particular. Apparently, US Steel outlined many of the 'net benefit' things it had done after the acquisition, including debt retirement, environmental and safety initiatives, capital investments, and expansion of production capabilities and markets.

Whether Stelco, in the absence of US Steel's acquisition would have survived in the current economic environment was also raised, but as with projections on potential sales, the demise of a corporation is also difficult to assess. But in this case, Stelco had been in creditor protection under the *Companies Creditors Arrangement Act* in 2006 and emerged from that by shedding several divisions. A year later, US Steel proposed an acquisition. It may be safe to say that Stelco itself would have had similar issues in the economic environment faced by US Steel. US Steel's argument on the nature of undertakings, is that by its own guidelines, the Government is obliged to review those undertakings in light of any factors that are beyond the control of the

[13] Powell, Naomi, Hamilton Spectator, March 4, 2009

acquirer. The dramatic and sudden downtown in the US automobile manufacturing industry in 2008 was certainly both unpredicted and far more dramatic than either US Steel or the Government could have surmised.

US Steel claims that it attempted to meet with the Minister directly, but that it was instead 'summarily' informed that the Minister had directed the Attorney General of Canada to initiate proceedings under section 40[14] of the ICA. The case commenced with an application by the AG to the Federal Court for an Order enforcing the two breached undertakings, and an administrative fine of $10,000 per day, per breach ($20,000 per day). After skirmishes around the question of whether two parties were entitled to intervener status in the case, US Steel then filed a notice of motion for a determination that sections 39 and 40 of the ICA, upon which the Minister relies to enforce the undertakings, are constitutionally invalid.

Although I am spoiling the punch line here, US Steel lost this round. US Steel filed an appeal in the case, and then sought a stay of proceedings in respect of the initial application by the AG to the enforcement remedies requested by the Minister. It lost that round too. For reasons of brevity, I will not outline the considerable case law invoking the *Bill of Rights* and the Canadian *Charter of Rights and Freedoms*, both of which were extensively canvassed in US Steel's constitutional challenge. The following, though, is a brief summary of the arguments put forward in connection with the constitutional challenge.

Interveners

As mentioned above, two parties sought intervener status in the US Steel Case. The first was Lakeside Steel Inc. ("**Lakeside**"), a competitor of Stelco. Lakeside sought to intervene for the purpose of seeking an order that US Steel divest itself of Stelco because Lakeside was interested in acquiring it. The second party was the United Steelworkers Union (the "**Union**") which sought to intervene, in part, on the basis that an order should be made in the proceedings to award damages to the Union as a result of US Steel's actions.

US Steel argued that neither Lakeside nor the Union should be granted intervener status because neither met the principal test of being affected by the outcome of the case. Further, undertakings with the Minister are confidential, and were negotiated without input from third parties. Nothing in the ICA allows for private remedies.

Lakeside, on the other hand, argued that the cessation of steel production at Stelco's Lake Erie mill "adversely affected Lakeside Steel's ability to obtain certain grades of raw steel for specialized orders, or to obtain steel on credit terms as favourable as those previously enjoyed." Lakeside did not say it was contractually entitled to such terms and there was no allegation of breach. However, Lakeside suggested that US Steel should be ordered to divest its interest, and was seeking intervener status with respect to the assertion of such remedy. While divestiture is a

[14] Section 40 of the ICA provides that if a non-Canadian…..fails to comply with a demand [under section 39 of the ICA] an application may be made on behalf of the Minister to a superior court for an order. Examples of orders are set out under the heading "Plans and Undertakings" earlier in this paper.

remedy under the ICA in respect of a breach of undertaking, in the US Steel Case, the Attorney General was not seeking such an order.

The Union's request for intervener status was on the basis that, as the exclusive bargaining agent at the Hamilton and Lake Erie facilities, which were now idled, the Union had suffered because of a drop in union dues. The Union did not assert that the collective agreement had been breached, nor that any employment/labour laws had not been abided by. Nevertheless, the Union asserted that this loss of dues caused the Union loss, for which US Steel ought to be responsible in damages for.

Both interveners were granted leave to intervene in the US Steel Case, and that order is now being appealed by US Steel. Factums in that appeal were filed in mid-October of this year. US Steel's argument includes the assertion that neither party has met the test for intervener status because each failed to demonstrate a legal (not factual) interest in the outcome of the proceedings, and that neither party has a justiciable issue between themselves and US Steel. As a result, the decision to grant intervener status to Lakeside and to the Union was clearly wrong. Particularly galling to US Steel, I would imagine, is that the interveners were each seeking remedies unique and beneficial to them, which were not sought by the Attorney General. As US Steel puts it, "[t]he Intervention Order risks converting a bilateral legal proceeding into an open-ended public policy debate."[15] The Union, on the other hand, argues that the Federal Court ought not to interfere with an Order unless there is a clear case of misuse of judicial discretion.

The outcome of this particular skirmish has yet to be determined.

Constitutional Challenge

On October 2, 2009, US Steel brought an application under Rule 107 of the Federal Court Rules challenging the validity of sections 39 and 40 of the ICA. As a high level summary of the issue, US Steel asserted that the ICA straddles quasi-criminal, civil and administrative boundaries and violates fundamental principles of constitutional law, due process and natural justice. As it is easier to establish the challenge, I outline only to the arguments set out by US Steel, rather than the arguments, which in fact were successful, of the Attorney General. The decision in this matter accepts the Attorney General's position.

Specifically, US Steel argued that the ICA allows the Government to interfere with private investments and property without procedural safeguards and substantive constraints. Because the ICA provides for high penalties, such as the divestiture (which US Steel referred to as forfeiture) and 'multi-million dollar' fines –the process of exercising such rights and exacting such penalties must be in accordance with 'principles of fundamental justice and due process of law'. Under the ICA the Minister can commence the process through administrative demand without a hearing, and then seek to enforce such demand through an order.

> "(i) The legislation allows the government to interfere with the enjoyment of property in the absence of a hearing which accords with the principles of fundamental

[15] Motion under Rule 51 of *The Federal Courts Rules* - Memorandum of Fact and Law of US Steel, paragraph 11.

justice, thereby violating section 2(e) of the *Bill of Rights*. The application of section 2(e) of the *Bill of Rights* does not depend on the characterization of the legislation as quasi-criminal; and

(ii) When properly construed as a penal provision that creates a quasi-criminal offence, the legislation violates the presumption of innocence, contrary to section 11(d) of the Canadian *Charter of Rights and Freedoms.*"[16]

As a quasi-criminal offence, US Steel argued, it should be entitled to the full suite of constitutional protections including full rights of disclosure; right to know the case to meet; the right against self-incrimination; the presumption of innocence; the burden of proof beyond a reasonable doubt, and certainty with respect to *actus reus* and *mens rea*.

US Steel's position on the *Bill of Rights* was simply that a person cannot be deprived of property or economic rights without a fair hearing in accordance with the principles of fundamental justice. Section 2 of the *Bill of Rights* states:

"Every law of Canada shall, unless it is expressly declared by an Act of the Parliament of Canada that it shall operate notwithstanding the Canadian Bill of Rights be so construed and applied as not to abrogate, abridge or infringe or to authorize the abrogation, abridgement or infringement of any of the rights or freedoms herein recognized and declared, and in particular, no law of Canada shall be construed or applied so as to: … (e) deprive a person of the right to a fair hearing in accordance with the principles of fundamental justice for the determination of his rights and obligations."[17]

Principles of fundamental justice have been held to include the right to disclosure, the right to know the case to meet and the right to be given fair notice of proscribed conduct. Specifically, US Steel argued that (a) the imposition of a remedy as significant as forced divestiture is a serious and direct impact on the enjoyment of property; (b) the imposition of a fine of $10k per day per breach is a serious fine, and affords little protection to the investor because there is no procedural protection before its imposition; (c) the Minister can start a summary civil proceeding and the investor is required to answer the Minister without knowing the Minister's reasons or information considered by the Minister in initiating the process; and (d) the ICA does not set out the required burden of proof.

US Steel's *Charter* arguments are based on a presumption of innocence under section 11(d) of the *Charter*. That right is comprised of procedural rights including the right to know the case to meet; the right to have the Minister, in this case, prove his case; and the right to a burden of proof that protects against convictions circumstances where there is reasonable doubt as to guilt. Further, a section 11(d) right applies to both a criminal and a 'quasi-criminal' offence. The latter, in US Steel's view, was applicable here because on failure to meet the Minister's

[16] US Steel Factum, paragraph 10

[17] US Steel Factum – paragraph 49.

demands, the investor is subject to true penal consequences – namely significant fines, and potential divestiture. If an investor further fails to comply with the order, then the investor is faced with contempt of court proceedings which bring with them the spectre of imprisonment

Federal Court Decision

The Federal Court released its decision on June 14th of this year with respect to the constitutional challenge raised by US Steel. The Court rejected the US Steel arguments, and concluded that section 40 of the ICA does not violate either section 11(d) of the *Charter* or section 2(e) of the *Bill of Rights* on the basis of the following:

1. Section 40 of the ICA is not, by nature, a penal proceeding and section 11 of the *Charter* is not engaged by the magnitude of the monetary penalty claimed. While US Steel characterized the penalty as a "King Kong fine", the magnitude of the fine does not have support in jurisprudence. A governmental body may have unlimited power to fine, but to determine whether it is in fact a penal consequence, the Court must determine whether the fine is imposed for the purpose of redressing the harm done to society or whether it is imposed for a particular private purpose. Even if the continuing accumulation of the monetary penalty results in a large financial result, any monetary penalty must be assessed in the context of the transaction at issue. The financial threshold for requiring review of investments was, at the time of the US Steel application, C$281 million. A monetary penalty of $10 thousand per day per breach may not be significant. The Court further determined that the purpose of the monetary penalty is to promote and ensure the attainment of legislative objectives.

2. As to the *Bill of Rights*, the Court determined that there is a distinction that can be drawn between decisions that implicate the life, liberty and security of the person involved and those having only an economic impact, as is the case here. As referred to in the context of the *Charter* argument, the magnitude of the penalty including the forced divestiture possibility, have to be viewed in the context of the legislative scheme: "As well, the parties seeking ministerial approval are sophisticated, well represented, economic actors who are given an opportunity of voluntary compliance before the application at issue is undertaken." As a result, the cases US Steel presented as supportive of its assertion that it was not being given adequate opportunity to defend itself were all procedural cases in the criminal context, and not of use in this circumstance. The Court determined that there are adequate procedural protections to permit US Steel to know the case it has to meet.

US Steel has appealed the decision on the constitutionality of sections 39 and 40 of the ICA and, of course, the underlying request for an order from the Minister to the remedies requested for alleged breach by US Steel has also yet to be heard. US Steel also applied for a stay of the underlying proceedings pending the Federal Court of Appeal's disposition in the appeal of the 'validity' order (referred to above). The Federal Court of Appeal, however, determined that the tests for a stay, set out in *RJR-MacDonald v. Canada (Attorney General)*[18], namely that (i) a

[18] [1994] 1 S.C.R. 311

serious issue exists; (ii) it would suffer irreparable harm if the stay were not granted; and (iii) that the balance of convenience favours a stay, were not met.

Conclusions to Date in US Steel

The US Steel Case has yet to unfold, including with respect to the underlying action of the Attorney General to obtain an order for compliance with the undertakings given by US Steel and to the monetary penalty imposed. Whether we have a decision in that case will depend upon the outcome of the constitutional appeal.

Assuming the decision of the lower court is affirmed on appeal, the interesting part of the merits of the underlying case can be seen in US Steel's position with respect to the intentions of the Government set out in the ICA guidelines concerning plans, undertakings and monitoring post-acquisition.

In its factum in the constitutional challenge, US Steel certainly emphasized that the ICA guidelines explicitly state that plans and undertakings are based, to some extent, on projected circumstances and the monitoring of an investor's performance will recognize this factor. Where inability to fulfill a commitment is clearly the result of factors beyond the control of the investor, the investor will not be held accountable. The guidelines then beg the question. If external factors are recognized in determining whether an investor has met its obligations or not, in this case, (and ignoring what other motivations may be behind the decisions that US Steel made with respect to the Canadian mills), it is hard to argue that external factors were not dramatically different 18 months after the closing of the acquisition. If Investment Canada recognizes the external factors in the first instance in accepting plans and undertakings, then, as US Steel asserts, how can it possibly be non-compliant? Although US Steel was successful in obtaining confidentiality orders in respect of various affidavits, we can determine from the confidentiality order that US Steel has presented by way of affidavit cost information, customer information and purchasing volumes and forecasts, amongst other information both industry and company-specific relevant to the effect of the economy on its business in the relevant period.

Referring to US Steel's undertakings (set out above on page 11 of this paper), it would certainly suggest that for future reference, undertakings based on projections of growth, whether in employment or production (or both) or similar projections of growth in expenditures or expansion of facilities, for example, be tempered with parameters on economic forecasting. Rather than relying on the guidelines, it may be prudent, to the extent that Industry Canada would accept such qualifications in similar circumstances, to expressly qualify the projections.

BHP Billiton vs – Brad Wall?

I would be remiss in not making mention in this paper of the very recent saga of the failed takeover bid for Potash Corp. of Saskatchewan by BHP Billiton. As referenced at the beginning of this paper, BHP submitted an application for review of its proposed investment (acquisition), in advance of a tender to the bid by the shareholders of Potash, The Minister of Industry, Tony Clement, issued an initial decision rejecting the approval of the BHP investment on the basis that it does not meet the net benefit to Canada test. While BHP had a period of time (to December 4, 2010) to make further submissions including any additional undertakings in an effort to convince

the Minister that a net benefit to Canada would arise from the transaction, BHP opted not to submit further undertakings and has, as a consequence, opted to withdraw.

This second rejection of a foreign acquisition (the first being a rejection of Alliant Techsystems Inc.'s proposed acquisition of the Information Systems Business of MacDonald Dettwiler and Associates Ltd.)[19] will bring some scrutiny to the ICA 'net benefit to Canada' test. On November 14, 2010, Prime Minister Harper announced, while at the Asia- Pacific Economic Cooperation summit in Yokohama, Japan, that "the Government will be in a position not only to give reasons for the decision but to give broader guidance to the investment community on the kind of foreign investment it is and is not seeking within Canada."

The BHP saga was an interesting one to watch. While it appeared that the preliminary reaction to the proposed investment by the Federal Government was positive, or at least, neutral, the consistent appeals from the Premier of Saskatchewan to the enormity of 'losing a Canadian icon' in a 'strategic resource' was influential. Certainly, even if you set aside the political expediency of a minority Government faced with the potential threat of loss of 13 seats (and possibly more) it would be a fair argument to suggest that a significant monetary hit to the Province of Saskatchewan's treasury, which was alleged to be a very real outcome of a BHP takeover, is not a 'net benefit' to Canada. However, whether or not that would have occurred or could have been contained, controlled or deferred is not known. It has certainly been speculated that BHP offered a long, and expensive list of undertakings:

- "Remain in Canpotex, the export arm of Potash Corp., Mosaic and Agrium, for five years.
- $450-million (U.S.) exploration and development investment over the next five years, over and above spending already planned on BHP's Jansen potash project in Saskatchewan. Jansen is set to be the world's biggest potash mine.
- $370-million additional spending on infrastructure in Saskatchewan and New Brunswick.
- Commitment to forego certain tax benefits. Saskatchewan estimated the province stood to lose between $3-billion (Canadian) and $6-billion over 10 years in taxes and potash royalties if the takeover had proceeded.
- Move more than 200 jobs from outside Canada to Saskatchewan and Vancouver.
- Maintain current job levels at Potash Corp.'s Canadian mines for five years and increase overall employment in Canadian potash businesses by 15 per cent in that time.
- $250-million (U.S.) performance bond to ensure the company fulfilled its undertakings.
- $8-million a year in spending on community programs, mainly in Saskatchewan and New Brunswick.

[19] The rejection of the ATK bid for MDA's division was based on a 'national security' concern.

- Investment in the University of Saskatchewan."[20]

Interestingly, as the debate unfolded, Canadian business leaders made a number of statements that both supported an open foreign acquisition market, and a certain 'patriotic' reaction that applauded the outcome in this case. Every time there is a proposed take-over of a Canadian business that either represents one of Canada's world-class companies (Potash Corp. is the largest potash producer in the world) there is a public discussion about the 'hollowing out' of corporate Canada. The BHP/Potash debate provoked a similar debate. In this case, the discourse was also infused with a healthy dose of skepticism because of what the US Steel Case and arguably previous known undertakings have disclosed concerning commitments of buyers generally in seeking approval under the ICA.

Clarity of the regulations and guidelines governing both (a) a determination of 'net benefit to Canada'; and (b) the enforcement of such rules, will be extremely helpful to foreign acquirers. The call for clarity comes from domestic investors as well. The Canada Pension Plan Investment Board has now called on Ottawa to address the ICA rules, largely because it has significant holdings in domestic natural resource companies, including mining and oil sands. It would be helpful to its own valuation analysis to know whether companies in which CPPIB has invested can be open to a universe of buyers. In the absence of such clarity, there would appear to be a concern that either natural resources in Canada will be treated differently from other industries under the ICA or that, at least, there are may be certain economic sectors (or companies within key sectors) that are 'untouchable'.

However, I would expect that the Government will and in its interests should use caution in the rush to 'clarity'. If rules become too 'technical', it may invite a 'technical' response removing from the Government the flexibility it needs to assess, in context, any given acquisition. A number of commentators have speculated on what kind of decision the Minister would face in a hostile bid for Research in Motion by a foreign entity. Would that not depend upon its state of being at the time? By comparison, the Government, even on the appeal of the Premier of Ontario to reject it, approved the acquisition by Ericsson AB of a significant portfolio of key mobility patents held by Nortel Networks for just over $1 billion. Might that decision, appropriately, have been different if Nortel were healthy and pensions were covered? RIM is a strong company, world class in its industry with innovative products and technology and, as such, it carries the Canadian flag globally. The same was once said of Nortel.

Acquirers could use guidance in the form of interpretation bulletins, or at the least, technical backgrounders[21] to assist in determining how to approach an Investment Canada review. We will now have to wait for the Minister's reasons for rejecting the BHP bid to determine whether they provide any useful guidance. Comprehensive reasons would go a long way to providing parameters for applications for review and potentially, proposed undertakings. As mentioned earlier in this paper, there is a view shared by many investors that the process of both the

[20] Kiladz, Tim. "BHP Billiton's $1 billion Promises", Globe and Mail, November 15, 2010.

[21] For example, the Competition Bureau issues 'technical backgrounders' in respect of merger analysis and other areas of the *Competition Act* reviewed by the Bureau.

application for review, including representations made to Investment Canada, and of undertakings, is a bit of a ‘check the box’ exercise. If the various enumerated items in the ‘net benefit to Canada’ section of the ICA are addressed in some fashion, then the Minister will likely simply say ‘yes’. Having some sensitivity to the key issues of ‘net benefit’ in any given circumstance, as well as creativity in presenting (and living by) undertakings that are contextual and appropriate must, in the end, be better for Canada which is presumably, the purpose of the ICA.

Certainly, what the BHP / Potash acquisition reinforces, as do the proceedings in the US Steel Case is that challenging, or potentially challenging investments should be part of a rigorous preparation prior to filing an application for review.

Appendix A
Number of Investments
June 30, 1985 to September 30, 2010[22]

	Cumulative Total	**Percentage of Total Acquisitions**
Acquisitions	13,841	77.29%
Direct	11,824	22.71%
Indirect	2,017	
Reviewed and Approved	1,637	11.83%
Notifications Only	12,204	88.17%
New businesses	4,068	n/a
From:		
United States	10,944	61.11%
Japan	572	3.19%
EU	3,982	22.23%
Other	2,411	13.46%
To:		
Ontario	9,973	55.69%
Quebec	2,616	14.61%
BC	2,039	11.39%
Other	3,281	18.32%
In:		
Resources	1,295	7.23%
Manufacturing	5,079	28.36%
Wholesale and Retail Trades	4,287	23.94%
Business & Other Service Industries	4,814	26.88%
Other Services	2,434	13.59%

As an additional note, between 1999 and 2008, Heritage Canada reviewed 101 foreign acquisitions of cultural business, approving 98 and rejecting three.[23]

[22] Investment Canada, updated October 7, 2010

[23] CBC News - The 'net benefit' of foreign takeovers, November 15, 2010

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