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## ARTICLE

# National Security Guidelines Seek to Provide Clarity to Foreign Investors, but Uncertainty Remains

### Introduction

In its Fall Economic Statement 2016, the Government of Canada (the Government) announced that it would soon publish guidelines on the application of the national security provisions of the *Investment Canada Act* (ICA). On December 19, 2016, the Department of Innovation, Science, and Economic Development (ISED) moved forward with this proposal by publishing guidelines

- Procedural and evidentiary considerations relevant to national security reviews; and
- Factors that Cabinet will consider when assessing potential national security risks posed by an investment.

### Background

The ICA is Canada's foreign investment review statute of general application. It contains two separate review processes to which foreign investments in Canada may be subject:

1. A review process which considers generally whether an acquisition of control of a Canadian business by a foreign investor would be of *net benefit* to Canada (the Net Benefit Review); and
2. A review process which considers whether a foreign investment in Canada could injure Canada's national security (the National Security Review).

Whether a Net Benefit Review of an acquisition is required turns on whether the value of the assets of the target Canadian business exceeds the applicable financial threshold<sup>2</sup>. If the threshold is exceeded, investors must apply to the relevant Minister for a Net Benefit Review and observe a waiting period of up to 75 days prior to closing the investment. In order to secure approval under this process, investors must satisfy the Minister that the investment is likely to be of "net benefit" to Canada, having regard to evaluative factors set out in the legislation — to do this, investors typically give enforceable undertakings to the Minister that relate to these factors, including commitments on employment levels, economic activity, innovation, global competitiveness, and the participation of Canadians in management and on the board.

The ICA's separate National Security Review process, on the other hand, is conceptually similar to the process administered by the U.S. *Committee on Foreign Investment Review* (CFIUS)<sup>3</sup> — unlike the US CFIUS process, however, foreign investors cannot apply for a National Security Review under the ICA. Rather, these reviews are initiated at the sole discretion of the Minister of ISED (the Minister) and can extend for as long as 200 days.<sup>4</sup>

Since coming into force in March 20 09 , the federal Cabinet has ordered eight national security reviews. Outcomes of these reviews included orders directing the investor not to implement the investment (pre-closing) or to divest itself of the target (post-closing), as well as orders authorizing the investment subject to conditions aimed at reducing risk to Canada's national security.<sup>5</sup>

The ICA's National Security Review process had been criticized for the absence of a clear definition and guidance surrounding what qualifies as Canada's "national security", as well as the lack of transparency regarding this review process. By issuing these guidelines, the Government was hoping to provide "greater certainty to companies looking to invest in Canada while maintaining the integrity of the national security review process".<sup>6</sup>

### The Guidelines: Factors Relevant to National Security Risk

The Guidelines are notable for setting out a non-exhaustive list of factors that Cabinet may take into account when assessing the potential national security implications of an investment, including —

- Effects on Canada's defence capabilities and interests (including R&D or the supply of military weapons and technologies, space-related equipment, etc.);
- The transfer of sensitive technology or know-how outside Canada;
- Impacts on the supply of critical goods and services to Canadians ( including energy, utilities, food, transport, information and communication technology, health, water, and safety);
- Impacts on the supply of goods and services to the Government;
- Enablement of foreign surveillance or espionage, or the hindrance of intelligence operations and law enforcement;
- Impacts on Canada's international interests, including foreign relationships; and
- Involvement or the facilitation of activities of illicit actors (e.g. terrorists/terrorist organizations, organized crime).

These factors mirror (to a substantial degree) the list of illustrative factors relevant to CFIUS reviews published by the US Department of Treasury (the CFIUS Factors)<sup>7</sup>. Notably absent from the factors set out in the Canadian Guidelines, however, is the degree foreign state ownership, control, or influence over the investor. The Minister has previously published separate guidelines regarding the treatment of investments by these so-called state-owned enterprises (SOEs) in the context of *Net Benefit* Reviews<sup>8</sup>, however, foreign state ownership, control, and influence over investors have also raised concerns about Canada's national security, and are expected to continue to be relevant to National Security Reviews.

### The Guidelines: Protection of Relevant Information Under the *Canada Evidence Act*

The Guidelines are also notable for taking the position that certain information relevant to Cabinet's review may not be shared with the investor due to its sensitive nature, and more specifically, that protection of such information from disclosure to the investor may be claimed pursuant to the *Canada Evidence Act* (CEA).<sup>9</sup>

As a result, information that may be relevant to an ultimate decision by Cabinet can be withheld from the investor, thereby impairing the transparency of this process.

## Implications of the Guidelines

While the relevant factors listed in these Guidelines provide a certain degree of assistance and clarity to foreign investors who are considering investing in Canada, their potential application remains very broad. Furthermore, the withholding of relevant information from investors on national security grounds pursuant to protections in the CEA has potential to enhance — rather than lessen — investors' existing concerns relating to the lack of clarity and transparency surrounding the National Security Review process.

Further, Net Benefit Reviews are expected to become rarer in the years ahead due to expected increases to applicable financial thresholds for review<sup>10</sup>. With fewer and fewer investments being subject to Net Benefit Review, it remains to be seen whether the highly discretionary National Security Review process will be used strictly by the Government as a tool to mitigate national security concerns, or more broadly to address more general concerns of national interest that are have historically been reserved for Net Benefit Reviews (e.g. relating to employment levels, economic activities, innovation, Canada's global competitiveness, and participation by Canadians in management and on boards of directors).

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<sup>1</sup><http://www.ic.gc.ca/eic/site/ica-lic.nsf/eng/ik81190.html>.

<sup>2</sup> These thresholds vary depending on whether the investor is controlled by residents of a WTO member state, owned, controlled or influenced by a foreign state, or whether the target Canadian business is engaged in cultural business activities.

<sup>3</sup> Pursuant to the *Foreign Investment and National Security Act of 2007* (FINSA).

<sup>4</sup> The ICA sets out strict time periods within which the Minister can initiate a National Security Review.

<sup>5</sup> [\*Annual Report: Investment Canada Act \(2015-16\)\*](#) is available online.

<sup>6</sup> See [\*News release — Attracting global investments to develop world-class companies\*](#) (Dec. 19, 2016).

<sup>7</sup> See *Guidance Concerning the National Security Review Conducted by CFIUS*, 73 Fed. Reg. 74567 (Dec. 8, 2008).

<sup>8</sup> See [\*Guidelines — Investment by state-owned enterprises — Net benefit assessment\*](#).

<sup>9</sup> Section 38 of the CEA contains rules that prevent the disclosure of information or documents that contain "sensitive information" (defined as information relating to international relations or national defense or security in the possession of the Government, regardless of whether it originated inside or outside Canada).

<sup>10</sup> The Government recently announced that the review threshold applicable to direct acquisitions of Canadian businesses by investors controlled in WTO member states will increase from C\$600 Million to C\$1 Billion (in enterprise value) in 2017 (two years earlier than expected). Further, on implementation of the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union, this threshold will increase to C\$1.5 Billion for EU-controlled investors (as well as investors from other states that have FTAs with Canada that contain MFN commitments to those states).

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By: [Subrata Bhattacharjee](#),

Services: [Competition & Foreign Investment Review](#)

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## Related Contacts & Expertise

Subrata Bhattacharjee

Partner and National Chair, Competition and Foreign Investment Review Group

 Toronto

 [SBhattacharjee@blg.com](mailto:SBhattacharjee@blg.com)

 416.367.6371

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