May 24, 2018

ARTICLE

Canadian Government Blocks Chinese Foreign Investment Due to National Security Concerns

On May 23, 2018, it was announced that the Canadian government has used the national security provisions of the *Investment Canada Act* ("ICA") to block a proposed $1.5 billion takeover of Aecon Group Inc. by CCCC International Holding Ltd., a Chinese state-owned company and one of the world's largest engineering and construction firms. This major decision highlights the fact that the national security review process has become increasingly relevant for potential investors into Canada, particularly those which are state-controlled or which appear to have close ties to the government of a foreign state.

The national security review of the deal was launched earlier this year after the takeover was publicly opposed by, among others, Canadian construction competitors and by former directors of the Canadian Security Intelligence Service. Under the ICA, the Minister of Innovation, Science and Economic Development Canada ("ISED") can launch a national security review of any investment by a non-Canadian to acquire any part of an entity with a place of operations in Canada, employees in Canada or assets in Canada, if he "has reasonable grounds to believe" that the investment could be injurious to national security. If, following consultations with Canada's national security agencies, certain other government entities and potentially Canada's allies, an investment is found to pose a threat to national security, the government may block the investment entirely, as it has regarding CCCC's takeover of Aecon, or impose any conditions on its implementation that are deemed necessary to mitigate the risks to national security.

Although this decision has been made public, many are not. A key issue for state-owned or influenced investors seeking to invest in Canada, and the parties with whom they are attempting to transact, is the lack of transparency provided by the government as to the real criteria for determining which investments potentially threaten national security. There is also little clarity on the basis by which the government determines which investors it considers to be "influenced" by a foreign state, other than that it has made clear that actual or *de facto* control by a foreign state is not required for a concerning level of state-influence to arise.

Parties considering investing in Canada whose investments may be subject to a national security review also need to consider the extent to which the United States' interests may be considered in the ICA process. Although the Canadian government cannot block investments at the behest of other sovereign nations, ISED is clear that the concerns and views of allies are taken into account. Canada's failure to block — or even conduct a national security review of — the 2017 acquisition by a Chinese company of Canadian high-tech firm Norsat, which sold satellite-communications systems to the American military, was harshly criticized as a threat to American national security by American politicians, even though the deal was not subject to their national security review process. Following this, particularly given what some believe may be a desire to ensure that ongoing relations with the Trump administration on sensitive matters such as NAFTA are not impacted by concerns with the scrutiny Canada places on foreign state-influenced investment, it is reasonable for parties to consider whether American interests and potential concerns may be given significant weight in the national security review process. Although it is not known whether ISED consulted with the U.S. government in coming to its decision to block the Aecon acquisition, there is a strong possibility that such discussions did in fact occur.

The Canadian government's blocking of the deal due to national security interests appears to reflect a global trend toward protection of domestic entities in the face of Chinese foreign investment. The European Union recently proposed a new Foreign Direct Investment screening framework, which would allow for a more streamlined process for screening investments that could affect security or public order, giving the European Union the ability to block deals that are "likely" to affect critical infrastructure or technology.

It remains to be seen what CCCC and China will do in response to the Canadian government's decision. A spokesperson for the Chinese government, Lu Kang, stated shortly after the decision was announced that "if Chinese interests are undermined, we will take necessary actions to safeguard our rights and interests." They may seek a court's review of the decision, which was a remedy that was recently successfully taken by another Chinese investor in 2015 whose acquisition of a Canadian company was sought to be unwound on the basis of national security concerns under the ICA.

The decision threatens to exacerbate an ongoing sore point between China and Canada as they take tentative steps toward a potential trade agreement. Previous ICA blocks of Chinese investments have been flagged by China as protectionism masquerading as national security concerns, and the initial Chinese reaction to the block of CCCC's Aecon takeover was in the same vein. The Chinese government spokesperson stated that China is "opposed to political interference under the pretext of national security" and that they "hope the Canadian side can abandon prejudices and create a level playing field for Chinese enterprises."

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Services: Competition & Foreign Investment Review