

Canada: tough new policy on foreign SOE investment in critical minerals sectors

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On Oct. 29, 2022, the Canadian Federal Government (GoC) announced that, effective immediately, it will be exercising its authority under the *Investment Canada Act* (ICA) to increase scrutiny of investments into the Canadian critical minerals sector by foreign state-owned or state-influenced (SOE) investors, in accordance with a new *Policy Regarding Foreign Investments from State-Owned Enterprises in Critical Minerals under the Investment Canada Act* (the Policy). On Nov. 2, 2022, GoC [announced that](#) it had ordered three Chinese companies to divest minority investments they had made in Canadian mining companies.

What you need to know

- The ICA potentially allows the GoC to screen foreign investments in Canadian businesses under an economic “net benefit” test and/or a national security test.
- Investments by foreign SOEs have generally been subject to more intense scrutiny by the GoC in recent years, and some have been blocked on national security grounds. The scope of the national security test has steadily expanded since its inclusion in the ICA.
- The GoC has identified 31 “critical minerals” such as lithium and other rare earths, but also metals such as copper and zinc as being critical for Canada.
- The Policy essentially provides that SOEs (particularly those that are not those from “non-likeminded foreign governments”) will, in most circumstances face difficulty in gaining approval for investments that involve critical minerals under either the “net benefit” or national security tests.
- The Policy will be applied not only to investors that are state owned or influenced, but also to those “who could be compelled to comply with extrajudicial direction from foreign governments”.
- Within days of the release of the Policy, GoC ordered three Chinese companies to divest themselves of minority investments they had made in Canadian mining companies. Each of these Canadian companies owns lithium mines, in addition to other mineral properties.

What this means for non-Canadian investors that are state-owned or state-influenced

On March 11, 2021, the government introduced a [Critical Minerals List](#), identifying 31 minerals “considered critical for the sustainable economic success of Canada” and its allies. The Policy seeks to strengthen the protection of Canada’s interests in the critical minerals space by stating that any investment, at any stage of the value chain, related to these critical minerals by investors tied to foreign-state governments (irrespective of the value of the investment or whether it confers control) will be very closely scrutinized. This appears to indicate a higher level of scrutiny than the “enhanced scrutiny” [announced for certain sectors](#) in April 2020 and highlights the need for foreign investors, with any potential foreign state ties to consider how to satisfy the Canadian government, that their investment will not present a risk to Canada’s growth, prosperity or security.

The types of investors subject to the Policy are much broader than just ultimately state-owned entities. The ICA considers SOEs to include entities ultimately controlled by individuals or entities that are subject to the influence or direction of foreign state governments, and the Policy expressly identifies the entities as targeted as those:

- that are owned by foreign governments;
- that are closely tied to or subject to influence by foreign governments; or
- that could be “compelled to comply with extrajudicial direction” from foreign governments.

Particularly heightened scrutiny is applied to investments from SOEs from “non-likeminded governments”. This is consistent with [recent statements from the Deputy Prime Minister](#) articulating a Canadian international trade policy that favours interaction with nations with “shared values”. The decision to require three Chinese companies to divest their minority investments in Canadian businesses that own critical mineral properties, resulting from national security reviews that most likely had been completed prior to release of the Policy, is consistent with the approach articulated therein; indeed in many cases, such the content of the Policy simply reflects the current enforcement approach. Of note, at least one of the Canadian businesses from which a Chinese company was ordered to divest does not own any mines in Canada. Furthermore, at least two of the Chinese companies ordered to divest are publicly listed.

As national security reviews are not conducted in a transparent fashion, it is difficult to provide firm views, but at a minimum, the results in these three cases suggest that in the critical minerals context, state “influence” in some form may present as much deal risk under the Policy as outright state ownership. In addition, even businesses with critical minerals operations wholly outside Canada may not be immune to scrutiny, especially if they involve lithium or rare earth minerals. This is not to suggest that all transactions in the sector are off limits, but that prudent deal planning will include healthy diligence about ownership and other interests held by state owned or state influenced entities, as well as any particularly sensitive activities of the target.

The government’s power to restrict foreign investment

Investments to acquire control of Canadian businesses that exceed certain monetary thresholds are required to undergo a net benefit review (NBR) process, which considers whether the investment likely to be of net benefit to Canada – an essentially economic test. Under the ICA’s separate national security review (NSR) process, the government has the power to review virtually any investment of any value into Canada by a non-Canadian to determine whether they “would be injurious to national security”. No

monetary thresholds apply to the NSR process, and minority/non-controlling investments can be reviewed.

The Policy provides that where NBR applies, GoC will only approve an SOE investment in critical minerals “on an exceptional basis”. It will also consider the extent of foreign state control or influence that will be had on the Canadian business, whether it will continue to operate on a commercial basis in accordance with free market principles, and whether it will continue to adhere to Canadian corporate governance and other laws and standards. GoC will also consider the degree of competition and concentration of foreign ownership in the relevant sector.

In the context of an NSR of such an investment, the Policy provides that GoC will consider the size, scope and location of the Canadian business, its strategic value to Canada, the extent of foreign state control or influence that will be had on the Canadian business, the effect that the investment may have on the ability of Canadian supply chains to exploit the critical minerals at issue, and “the current geopolitical circumstances and potential impact on allied relations.” The recent order that three Chinese companies divest their minority interests in Canadian mining companies was pursuant to an NSR, as non-controlling investments are not subject to NBR.

Under either review process, the government can block an investment entirely, require the investor to agree to binding commitments regarding its ownership of the business to assuage concerns, and/or require divestitures.

Conclusion

The Policy represents the GOC’s strongest statement to date expressing scepticism about SOE investment in Canada. It suggests that securing approval for investments in the critical minerals sector by any investors closely tied to foreign states will be very difficult in most circumstances. Such investors still wishing to proceed should plan for a rigorous review process, be prepared to strongly defend their commercial orientation and ability to further Canada’s economic interests, and be aware of the [timing considerations involved in reviews under the ICA](#).

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