SYMPOSIUM: CANADA AND THE UNITED STATES: A CHANGING RELATIONSHIP IN A CHANGING WORLD*

THE FOREIGN INVESTMENT REVIEW ACT OF CANADA

James M. Spence**

I. INTRODUCTION: THE BACKGROUND TO THE ACT

Over the past two decades, increasing concern has been voiced from many quarters in Canada over the degree of foreign domination of Canadian industry and resources. According to the "*Gray Report,*"[1] a report published in 1972 under the authority of the Government of Canada:

> The degree of foreign ownership and control of economic activity is already substantially higher in Canada than in any other industrialized country and is continuing to increase.
>
> Nearly sixty per cent of manufacturing in Canada is foreign controlled and in some manufacturing industries such as petroleum and rubber products foreign control exceeds ninety per cent. Sixty-five per cent of Canadian mining and smelting is controlled from abroad. Approximately eighty per cent of foreign control over Canadian manufacturing and natural resource industries rests in the United States.

---

* Proceedings of the Thirteenth Annual Regional Meeting of the American Society of International Law, held in Syracuse, N.Y., on April 3, 1976, at the Syracuse University College of Law. The views expressed by the participants do not reflect their official capacities or that of their organizations.

** Of the law firm of Tory, Tory, DesLauriers & Binnington in Toronto, Canada; formerly, Senior Legal Advisor to the Foreign Investment Review Agency of Canada. Unless otherwise indicated, the opinions expressed are those of the author and are not to be taken as a statement of Agency position or policy. Portions of the text of this paper are based on a paper delivered by the author under the auspices of the Law Society of Upper Canada in December, 1975.

1. GOVERNMENT OF CANADA, FOREIGN DIRECT INVESTMENT IN CANADA (1972) [hereinafter cited as GRAY REPORT]. The foreword to the *Report* notes that it "is not a statement of government policy nor should it be assumed that the government endorses all aspects of the analysis contained in it." *Id.* at v.

In terms of total national wealth, the proportion controlled by non-residents may be of the order of ten per cent. But about one-third of total business activity in Canada is undertaken by foreign-controlled enterprises.

The bulk of this heavy foreign direct investment in Canada has occurred since the end of the last war, and it has unquestionably played an important role in the growth of the Canadian economy over the past quarter century. It has provided ready access to capital, entrepreneurship, managerial skills, new technology and, in many cases, to markets abroad. Foreign investment has resulted in enterprises being undertaken in Canada which would not otherwise exist. It has contributed in an important way to the growth of production, employment, incomes and government revenues in Canada.

Foreign investment has also brought with it a number of major problems, which have become a matter of increasing concern to many Canadians over the past decade and more.

. . . .

The high and growing degree of foreign control of Canadian business activity can affect the balance between the manufacturing and resource sectors of the Canadian economy, and between the various sectors of manufacturing. The investment decisions of foreign-controlled corporations tend to reflect the laws and industrial priorities of foreign governments and economies which, in turn, influence Canadian industrial priorities. These objectives and priorities of foreign corporations and governments do not appear to have conflicted in a significant way with Canadian economic goals in the past, but the anticipated high level of demand for resources by foreign economies could lead to undue emphasis on resource development in the coming decades. This, in turn, could impose major limitations on the ability of Canadians in future to formulate an industrial development policy geared to Canada's own particular growth and employment objectives.

The high level of foreign direct investment also affects the structure of Canada's manufacturing industry. Many foreign corporations invest in Canada to extend the market for their manufactured goods. They tend to produce a wide range of products in short runs to supply the Canadian market only. Furthermore, Canada can become locked into accepting a pattern of innovation and technological development which has its origins abroad. These tendencies add to the relatively high costs in the Canadian economy stemming from a variety of domestic factors and result in the establishment of dependent manufacturing operations which, in many cases, are not in a position to compete internationally.

The substantial degree of foreign investment in Canada has also

> carried with it other significant economic and social costs—some of them intangible and difficult to measure, some of them not even readily apparent. Direct investment by foreign companies has led to establishment in Canada of "truncated" enterprises, in which many important activities are performed abroad by the parent or other affiliated firms. Foreign controlled firms do not seek to perform certain tasks in Canada, with the result that Canadian skills and capacities are not developed adequately to support foreign *or* Canadian controlled enterprises. This reliance on external sources for many of the inputs of industrial activity has meant a lesser development of Canadian capacities—and perhaps even a stultification of these capacities.[2]

In reviewing the responses of the Canadian government in the past to foreign direct investment, the *Gray Report* noted that, within a framework which has generally been very receptive to foreign investment, measures have been taken to limit direct investment in certain areas—or "key sectors"—of the economy, or to impose conditions on its entry.[3] For example, the Bank Act,[4] which governs the chartered banks in Canada, places a maximum of ten percent on the proportion of the shares that can be owned by any shareholder, resident or nonresident,[5] and restricts aggregate nonresident ownership to 25 percent.[6]

These approaches to the control or restriction of foreign direct investment typically apply to all enterprises in the regulated industry or industry sector. Accordingly, they are not tailored to the potential costs and benefits of specific transactions. Such rules have been applied only to certain industries and industry sectors such as banks, insurance companies, trust and loan companies, and broadcasting companies.[7]

In consequence, there were many areas of the economy—virtually all manufacturing activities, for example—where there were no controls over foreign investment. The increasing extent of foreign investment precipitated much public discussion about its relative costs and benefits, and there were spokesmen for various positions. Many persons argued that, apart from key sectors where a degree of Canadian ownership should be preserved, there

---

2. *Id.* at 5-6.
3. *Id.* at 13-26.
4. CAN. REV. STAT. c. B-1 (1970).
5. *Id.* §§ 53(1)(*a*)-(*b*).
6. *Id.* § 53(2)(*a*).
7. A number of provinces also have their own key sector legislation.

should be no controls on foreign investment. At the other end of the spectrum, others contended that foreign investment was by and large a detrimental thing and the time had come to "buy back Canada." There were a number of studies conducted under the authority of the federal government.[8] The most recent of these was the study which resulted in the *Gray Report.* The approach taken in that report was to compare costs and benefits:

> If foreign direct investment merely created problems, it would be a simple matter to deal with it; all foreign investments could simply be blocked. But in many cases foreign investment is a complex mix of costs and benefits, both of which are extremely difficult to quantify in economic terms—to say nothing of social, cultural and political terms—for the nation as a whole. Since foreign investment will likely continue to be an important factor in Canada for many years to come, Canadians must explore alternative means of reducing the cost of foreign investment and increasing to the greatest extent possible the benefits which it can bring to the nation over the long term.[9]

Among the benefits of foreign direct investment identified in the *Gray Report* are: an increase in economic growth, living standards, jobs, and tax revenues; significant contribution to the competitive climate of the industry involved; access to export markets; potential for training local personnel; and increased employment in regions where employment opportunities are scarce.[10] Along with these potential benefits, however, certain identifiable costs were noted. Foreign company investment decisions may not accord with Canadian objectives and priorities. The foreign investor may employ his "distinctive" capacity in Canada only as part of a "package" which includes other elements already available or potentially available in Canada—thus raising the cost. The foreign-controlled firm in Canada may fail to develop exports. Foreign direct investment can also lessen competition in certain circumstances. Foreign direct investment can act as a transmission belt for the entry of foreign laws into Canada, and for cultural influences which may or may not be desirable.[11]

---

8. *See, e.g.,* REPORT OF THE ROYAL COMMISSION ON CANADA'S ECONOMIC PROSPECTS (1957); REPORT OF THE TASK FORCE ON THE STRUCTURE OF CANADIAN INDUSTRY, FOREIGN OWNERSHIP AND THE STRUCTURE OF CANADIAN INDUSTRY (1968).

9. GRAY REPORT, *supra* note 1, at 7.

10. *Id.* at 41.

11. *Id.* at 41-43.

The *Gray Report* presented a number of reasons for administrative intervention in respect of foreign direct investment in order to attain greater benefits and to reduce the potential costs of such investment.[12] It argued specifically for a screening process: a case-by-case review of foreign direct investments as the means of intervention.[13]

In May of 1972, the Government of Canada introduced a bill providing for the review of foreign takeovers of Canadian businesses.[14] That bill was reintroduced in revised form as the Foreign Investment Review Act (Act) in January 1973,[15] providing for the review of both takeovers (Phase I) and new businesses (Phase II). The Act came into force with respect to Phase I on April 9, 1974.[16] Phase II came into force on October 15, 1975.[17]

The concerns which led to the enacting of the legislation are given clear expression in the law itself. Section 2(1) of the Act provides the following statement under the heading "Purpose of the Act."

> This Act is enacted by the Parliament of Canada in recognition by Parliament that the extent to which control of Canadian industry, trade and commerce has become acquired by persons other than Canadians and the effect thereof on the ability of Canadians to maintain effective control over their economic environment is a matter of national concern, and that it is therefore expedient to

---

12. *Id.* at 453-54. The *Report* stated:

(i) One aim of policy should be to ensure that a reasonable proportion of the benefits from the investor's distinctive capacities are obtained by Canadians. A review mechanism would allow Canada to marshal Canadian bargaining power in an effort to obtain the maximum benefits possible for Canada from foreign direct investment.

. . .

. . . .

(v) A review process is a mechanism with which international business is familiar, a fact which would probably make it easier for Canada to use this approach. It would focus on terms and conditions with which businessmen are well acquainted. As pointed out [elsewhere in the *Report*] most countries have some power of control over direct investment. A number of governments have some type of review process.

13. *Id.* at 451.

14. *See* Franck & Gudgeon, *Canada's Foreign Investment Control Experiment: The Law, the Context and the Practice,* 50 N.Y.U.L. REV. 76, 105-07 (1975).

15. Can. Stat. c. 46 (1973) [hereinafter cited as FIRA]. An "information kit" containing the Act and various other materials, including the Regulations and Guidelines issued under the Act, can be obtained from the Foreign Investment Review Agency, Ottawa, Canada.

16. [FIRA] Proclaimed in Force April 9, 1974, Except Certain Sections, SI/74-52, 108 Can. Gaz., pt. II, at 1533 (1974).

17. Certain Sections of the Act Proclaimed in Force October 15, 1975, SI/75-99, 109 Can. Gaz., pt. II, at 2477.

> establish a means . . . to ensure that . . . control of Canadian business enterprises may be acquired by persons other than Canadians, and new businesses may be established in Canada by persons, other than Canadians, who are not already carrying on business in Canada or whose new businesses in Canada would be unrelated to the businesses already being carried on by them in Canada, only if it has been assessed that the acquisition of control of those enterprises or the establishment of those new businesses, as the case may be, by those persons is or is likely to be of significant benefit to Canada, having regard to all of the factors to be taken into account under this Act for that purpose.[18]

This "assessment" purpose of the Act was underlined by the Honourable Alastair Gillespie, the Minister responsible for the Act at the time, when he announced the introduction of Phase II. In making the announcement, he emphasized that

> the purpose of the Foreign Investment Review Act is not to block foreign investment from any source or to discourage it, but rather to ensure that such investment is of significant benefit to Canada. Since its beginnings, Canada has had to rely heavily on foreign investment to help us develop this country. And we shall continue to need a great deal more investment in Canada by our friends abroad if we are to develop our full potential.[19]

II. THE SCHEME OF THE ACT

In general terms, the Act provides that no foreign person or foreign-controlled enterprise is permitted to take over an existing Canadian business, or to establish a new Canadian business unrelated to any of its existing Canadian businesses, without first receiving the approval of the government of Canada. In order to decide whether to approve an investment, the Cabinet is required under the Act to decide whether the investment "is or is likely to be of significant benefit to Canada."[20] To make that decision, the Cabinet is required to take into account the five factors enumerated in Section 2(2) of the Act. These are:

> (*a*) the effect of the acquisition or establishment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on re-

18. FIRA § 2(1).

19. 119 PARL. DEB., H.C. 7712 (Can. 1975), *reprinted in* Foreign Investment Review Agency News Release (July 18, 1975).

20. FIRA § 2(2).

source processing, on the utilization of parts, components and services produced in Canada, and on exports from Canada;
(*b*) the degree and significance of participation by Canadians in the business enterprise or new business and in any industry or industries in Canada of which the business enterprise or new business forms or would form a part;
(*c*) the effect of the acquisition or establishment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;
(*d*) the effect of the acquisition or establishment on competition within any industry or industries in Canada; and
(*e*) the compatibility of the acquisition or establishment with national industrial and economic policies, taking into consideration industrial and economic policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the acquisition or establishment.[21]

The Act provides that a minister of the government of Canada is to be designated for purposes of the administration of the Act.[22] The designated minister is the Minister of Industry, Trade and Commerce. The Act also provides for the establishment of the Foreign Investment Review Agency to advise and assist the Minister in connection with the administration of the Act.[23] It is perhaps worth repeating that the role of the Agency is only to "advise and assist" in the administration of the Act. As mentioned above, the decision whether to allow or disallow an investment is made by the Cabinet.

Various enforcement provisions are contained in the Act. One of these is a provision that the government may seek a court order to "render nugatory" an investment made in contravention of the Act.[24] This could involve an order prohibiting the exercise of voting rights on shares, or an order requiring the divestiture of shares or property.

III. THE REVIEW PROCESS

A. Notice

Section 8(1) of the Act provides that:

> Every non-eligible person, and every group of persons any member of which is a non-eligible person, that proposes to acquire control

21. *Id.*
22. *Id.* § 3(1).
23. *Id.*
24. *Id.* § 20. See notes 104, 106-09 *infra* and accompanying text.

> of a Canadian business enterprise shall give notice in writing to the Agency of such proposal in such form and manner and containing such information as is prescribed by the regulations.[25]

Section 8(2) contains a similar provision with respect to new businesses which are to be established in Canada.[26] Section 8(3) empowers the Minister, where he has reasonable and probable grounds to believe that a reviewable investment has been made or is proposed to be made, to make a demand for the giving of a notice.[27]

There are two sets of Regulations under the Act. The first set deals with the information required under a notice of an acquisition,[28] and the second set prescribes the information required in a notice of a new business.[29] The acquisition regulations require detailed information concerning the investor, the Canadian business to be acquired, and the investor's plans for that business. (The information requirements are abbreviated for certain small business acquisitions, as defined in the regulations.) The information as to the investor's plans is particularly important, since it forms the basis for the review process, that is, for the assessment of whether the investment is likely to bring "significant benefit to Canada." Indeed, the specific information requirements about these plans are closely keyed to the provisions of Section 2(2) of the Act. Similarly, the new business regulations require detailed information about the investor and the investor's plans, and provisions are made for abbreviated information in the case of certain small businesses. Under Section 8(4), the Agency is required to provide a receipt for the notice.[30]

B. Review and Assessment

The Assessment Branch of the Agency reviews the notice and consults with the provinces significantly affected by the investment and with those federal government departments whose views can be

---

25. *Id.* § 8(1). The term "non-eligible person" is the term used in the Act to refer to foreign persons and foreign-controlled enterprises, *id.* § 3(1). See notes 46-60 *infra* and accompanying text.

26. FIRA § 8(2).

27. *Id.* § 8(3).

28. Foreign Investment Review (Acquisitions) Regulations, SOR/75-204, 109 Can. Gaz., pt. II, at 682 (1975), *amending* SOR/74-154, 108 Can. Gaz., pt. II, at 1033 (1974).

29. Foreign Investment Review (New Business) Regulations, SOR/75-434, 109 Can. Gaz., pt. II, at 2142 (1975).

30. FIRA § 8(4).

expected to be relevant.[31] Through that procedure, the Agency develops a preliminary view of the application and then meets with the applicant to consider the matter further.[32] For example, it may be felt that the application has certain weaknesses which make it questionable whether it could receive government approval. In such a case, the assessment officers will explore with the applicant what possible improvements could be made in the plans. In other cases, it may be appropriate to look for a more detailed statement as to some part of the plans which has only been described in general terms. In order to confirm the plans of the applicant in clear terms, guarantees are usually given as to the manner in which the business will be carried on. For example, there may be an undertaking to purchase certain of the raw materials of the business from Canadian suppliers. When the Agency has formulated a recommendation, it is submitted to the Minister for his consideration and when he is satisfied with the recommendation, it goes forward to the Cabinet.[33]

If the Minister is not in a position, within 60 days after receipt of the notice, to make a favorable recommendation, the Agency must so notify the applicant pursuant to Section 11(1) of the Act.[34] The applicant then has the right to make further representations provided he advises the Agency he wishes to do so within a specified period. When all representations have been made, the recommendation goes forward.[35]

---

31. *Id.* § 9. Section 9 provides that:

> Following receipt by the Agency of a notice under subsection 8(1), (2) or (3), the notice shall be referred by the Agency to the Minister who shall thereupon review
>
> (*a*) the information contained in the notice,
>
> (*b*) any other information submitted to him by any party to the proposed or actual investment to which the notice relates,
>
> (*c*) any written undertakings to Her Majesty in right of Canada relating to the proposed or actual investment given by any party thereto conditional upon the allowance of the investment in accordance with this Act, and
>
> (*d*) any representation submitted to him by a province that is likely to be significantly affected by the proposed or actual investment to which the notice relates,
>
> for the purpose of assessing whether or not, in his opinion, having regard to the factors enumerated in subsection 2(2), the investment is or is likely to be of significant benefit to Canada.

32. *Id.* § 14. Section 14 prescribes definite rules of confidentiality in respect of information submitted by the applicant.

33. *See id.* § 10.

34. *Id.* § 11(1).

35. *See id.* §§ 11(2)-(5).

C. *Order in Council*

The Assessment process culminates in the order made by the "Governor in Council."[36] Section 12(1) provides as follows:

> On receipt by the Governor in Council of a recommendation or submission by the Minister with respect to an investment, the Governor in Council shall consider the recommendation and the summary submitted in connection therewith or the submission, as the case may be, and where, having regard to the factors enumerated in subsection 2(2), he concludes that the investment is or is likely to be of significant benefit to Canada, he shall, by order, allow the investment but where he does not reach that conclusion, he shall, by order, refuse to allow the investment.[37]

Section 13(1) is also important; it provides for a "deemed allowance."[38] This provision is considered to be a protection accorded to the applicant, rather than a mechanism available for use by the government to resolve cases.

D. *The First Year's Experience*

In October of 1975, the Minister presented the first annual report under the Act, for the fiscal year ending March 31, 1975.[39] During that period, only Phase I of the Act (the part relating to takeovers) was in effect.[40] The report summarized the results of the first year:

> Substantial benefits have been achieved for Canada as a result of the first year of federal government screening of foreign investment under the Foreign Investment Review Act. The benefits include some 7,000 new jobs and over $500 million in new investment. Additional benefits include increased exports, more purchases of Canadian goods and services, improved efficiency and technology, strengthened research and development, and greater variety of goods and services produced in Canada.
>
> . . . .
>
> The screening process is providing Canadians with greater opportunities to participate in the direction and management of Canadian industry. For example, roughly two-thirds of the assets transferred to foreign owners were already foreign controlled. In the great

36. For practical purposes, "Governor in Council" means the Cabinet.
37. FIRA § 12(1).
38. *Id.* § 13(1).
39. [1974-75] FOREIGN INVESTMENT REV. AGENCY ANN. REP. (1975).
40. See notes 16-17 *supra*.

majority of these cases the new owners undertook to provide a significant net increase in Canadian participation as shareholders, directors, and/or managers. Only one-third of the assets transferred to foreign owners were accounted for by Canadian controlled firms

. . . .

. . . Almost no large Canadian controlled companies were acquired by foreign investors. Of the total of 36 Canadian controlled companies allowed to be acquired, only 3 had assets of over $5 million.[41]

The report gave this description of the manner in which the criteria set forth in Section 2(2) of the Act have been applied:

Some of the criteria lend themselves to application, and have been applied, in a variety of ways. For example, "effect on employment" can pertain not only to number of jobs, but also to quality and terms of employment. Benefits have been obtained regarding quality of employment, job security, and pension or other employee benefits, as well as simply in terms of the overall number of employees.

The criterion which refers to "the degree and significance of participation by Canadians" is somewhat different from the other assessment criteria, which describe direct "economic" objectives, such as increases in employment, exports, resource processing, and productivity. Increased Canadian participation as shareholders, directors, and managers has many social, as well as economic, implications for the future of Canadians and of businesses in this country. The participation and influence of Canadians is often more important in key management positions or directorships than as shareholders. An especially important consideration, therefore, in assessing a proposed takeover is the degree of autonomy and authority that the proposed new owners would extend to their Canadian managers.[42]

The report noted that there were twelve disallowed cases, of which two involved foreign-controlled vendor companies. It went on to say:

In the 10 disallowed cases involving Canadian controlled vendor companies, the primary reason for disallowance was most frequently a reduction in Canadian ownership without any or sufficient offsetting benefit. The prospect of a major reduction in competition was the primary reason for disallowance in other cases.

---

41. [1974-75] FOREIGN INVESTMENT REV. AGENCY ANN. REP. 1 (1975).
42. *Id.* at 9.

> In one of the cases involving a foreign controlled vendor company, the applicant's plans for the vendor company did not seem much different from the course of development that the company could be expected to achieve under its existing ownership and management. Thus, the applicant could not be seen as offering anything that could possibly be regarded as being of significant benefit to Canada. In the other case, there was a distinct prospect of a major lessening of competition.[43]

The report also commented on the pattern of allowances in terms of the area of origin of the application:

> The Act does not contemplate discrimination among applicants on the basis of the country of apparent control. The administration of the Act has been consistent with this policy objective, as tends to be borne out by the figures. In resolved cases, approximately 70% were allowed for each of the major applicant areas of origin—the United States, Britain, and other [countries in] Europe.[44]

IV. PERSONS SUBJECT TO THE ACT

A. Non-Eligible Persons

As noted earlier,[45] the review requirements of the Act, as set out in Section 8, apply to any "non-eligible person and every group of persons any member of which is a non-eligible person . . . ."[46] "Non-eligible person" is defined in Section 3(1).[47] Stated in non-

---

43. *Id.* at 10-11.
44. *Id.* at 8.
45. See notes 25-27 *supra* and accompanying text.
46. FIRA § 8(1).
47. *Id.* § 3(1). Section 3(1) provides in part that:

"non-eligible person" means

(*a*) an individual who is neither a Canadian citizen nor a landed immigrant within the meaning of the *Immigration Act* and includes

(i) a Canadian citizen who is not ordinarily resident in Canada and who is a member of a class of persons prescribed by regulation for the purposes of this definition, and

(ii) a landed immigrant who has been ordinarily resident in Canada for more than one year after the time at which he first became eligible to apply for Canadian citizenship,

(*b*) the government of a country other than Canada or of a political subdivision of a country other than Canada, or an agency of such a government, or

(*c*) a corporation incorporated in Canada or elsewhere that is controlled in any manner that results in control in fact, whether directly through the ownership of shares or indirectly through a trust, a contract, the ownership of shares of any other corporation or otherwise, by a person described in paragraph (*a*) or (*b*) or by a group of persons any member of which is a person described in paragraph (*a*) or (*b*).

technical terms, "non-eligible persons" are: foreign individuals, foreign sovereigns, and corporations controlled by such persons. With respect to part (*a*)(i) of the definition, it should be noted that the regulations under the Act prescribe certain classes of citizens who are to be regarded as non-eligible.[48]

B. Determining Whether a Corporation is Non-Eligible

In practical terms, part (*c*) of the definition of "non-eligible person" is probably the most important part of the definition, since the question of "status" or "eligibility," for purposes of the Act, usually arises in connection with a corporation. Part (*c*) is framed expressly in terms of "control in fact" and not in terms of such more familiar concepts as "legal control" (sufficient voting shares to elect a majority of the board of directors). The concept of "control in fact" is not defined in the Act; it is apparently a broad concept, but it is not clear just how broad it is. Some people have observed that the specified examples of control in fact—"directly through the ownership of shares or indirectly through a trust, a contract, the ownership of shares of any other corporation"[49]—all involve legally enforceable rights. If the scope of the words "or otherwise" is to be limited in that fashion, then no one could be considered a "controller" unless he has a control base which consists of legally enforceable rights. This would mean that a person could not be considered the "controller" if, for example, he had founded the company and was the most experienced and respected member of the board but had no significant shareholdings and held no position other than his membership on the board. The broader reading of the concept is that "control in fact" means something like dominating influence, however exercised. On this broader reading, the person in the above example might well be thought to be the controller, depending on the actual degree of his influence in the affairs of the company. It is apparent that the concept of "control in fact" has some inherently vague aspects, and the more broadly that concept is read, the vaguer it is in danger of becoming. It is by no means clear that "dominating influences" can be disregarded in applying the "control in fact" test. Certainly, the view of the Agency to date has been that such factors must be taken into account in considering

48. Foreign Investment Review (Acquisition) Regulations, *supra* note 28, §§ 3(1)-(2); Foreign Investment Review (New Business) Regulations, *supra* note 29, §§ 3(1)-(2).

49. See note 47 *supra*.

whether a company has "eligible status" under the Act.[50]

The element of vagueness in the notion of "control in fact" does not permit the question to be ignored. Indeed, in certain circumstances, the Act places the burden on the corporation to establish its eligibility. Section 3(2) prescribes the following presumption as to non-eligible status:

> Where, in the case of a corporation incorporated in Canada or elsewhere,
> (*a*) shares of the corporation to which are attached
> (i) 25% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are publicly traded, or
> (ii) 40% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are not publicly traded,[51]
>
> are owned by one or more individuals described in paragraph (*a*) of the definition "non-eligible person" in subsection (1), by one or more governments or agencies described in paragraph (*b*) of that definition or by one or more corporations incorporated elsewhere than in Canada, or any combination of such persons, or
> (*b*) shares of the corporation to which are attached 5% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation are owned by any one individual described in paragraph (*a*) of the definition "non-eligible person" in subsection (1), by any one government or agency described in paragraph (*b*) of that definition or by any one corporation incorporated elsewhere than in Canada, the corporation is, unless the contrary is established, a non-eligible person.[52]

To whom must "the contrary" be "established"? Agency officers have frequently expressed the view that it is a court of competent jurisdiction which is intended. Accordingly, if a corporation is in a position to show that it is not foreign-controlled, it would be able to ignore the presumption.

The Act contains a mechanical provision intended to resolve problems of establishing the identity of the holders of small holdings. Section 3(5) provides, in effect, that any holding of less than one percent of the shares of a class held by an individual with a

50. There has as yet been no litigation in connection with the interpretation of the Act.
51. *See* FIRA § 3(6)(*a*). This provision defines "publicly traded" shares.
52. *Id.* § 3(2).

Canadian address may be treated as Canadian unless the corporation has knowledge to the contrary, provided the formalities prescribed by that section are complied with.[53]

Obviously, there can be situations in which no shareholder or group of shareholders can be identified as a controller. These include, for example, a company all the shares of which are widely held by the public, with no shareholder having a significant block. Also, there may be no other identifiable "controller." The Act deals with that situation in Section 3(7)(*b*), as follows:

> [W]here no one person or group of persons controls a corporation through the ownership of shares of the corporation or any other corporation, or where a corporation is a corporation without share capital, the corporation shall be presumed to be controlled by the group of persons comprising the board of directors or other governing body of the corporation, in the absence of any evidence that the corporation is in fact controlled by some other person or group of persons . . . .[54]

To understand the significance of this rule, it must be read in conjunction with Section 3(7)(*c*), which provides:

> [W]here a corporation is controlled by the board of directors or other governing body of the corporation the members of which body include one or more persons described in paragraph (*a*) or (*b*) of the definition "non-eligible person" in subsection (1),
>
> (i) if the number of members of that body who are persons so described does not exceed 20% of the total number of members of that body, the corporation shall be deemed not to be a corporation described in paragraph (*c*) of that definition,
>
> (ii) if the number of members of that body who are persons so described exceeds 20% of the total number of members of that body but is less than 50% of that number, the corporation shall, if it is established that no members of that body who are persons so described and who exceed 20% of the total number of members of that body act in concert[55] with one another in matters affecting the management of the corporation, be deemed not to be a corporation described in paragraph (*c*) of that definition, and
>
> (iii) if the number of members of that body who are persons

53. *Id.* § 3(5).

54. *Id.* § 3(7)(*b*).

55. It may be noted that the phrase "acting in concert" is not defined in the Act. *See also id.* § 3(7)(*a*).

> so described is 50% or more of the total number of members of that body, the corporation shall be deemed to be a corporation described in paragraph (*c*) of that definition.[56]

It is evident that these provisions define inclusively the term "corporate control." No corporation can be "uncontrolled" for purposes of the Act. If control cannot be located elsewhere, it is located in the board, and the composition of the board determines the eligibility of the corporation.

C. Groups with Non-Eligible Members

The Section 8 notice requirement[57] applies to "every group of persons any member of which is a non-eligible person."[58] This raises the question as to when an aggregation of persons may properly be considered to be a "group." The Act does not define the term "group." Section 3(7)(*a*) provides that the shareholders of a company cannot be regarded as a group unless they "act in concert with one another in any matter or transaction affecting the corporation or its management, ownership or financial affairs."[59] This seems to be the only guidance given by the Act as to the meaning of the concept, but it further involves the undefined term "acting in concert." It may be suggested that the mere fact that two persons reach the same conclusion on a particular question does not make them a "group"; what seems to be needed is some arrangement between them which obliges them to act in a particular manner. For example, if two persons agreed to carry on a business together under terms requiring their common consent to any proposed action, they would seem to be "acting in concert."[60]

D. Section 4(1) Opinions as to Eligibility

Section 4(1) of the Act provides that where any question arises under the Act as to whether a person is a non-eligible person or as to whether a particular business would be unrelated to any other business carried on by the person, the Minister, upon application, is to furnish to the applicant a statement in writing of his opinion.[61]

---

56. *Id.* § 3(7)(*c*).

57. See notes 25-30 *supra.*

58. FIRA §§ 8(1)-(2).

59. *Id.* § 3(7)(*a*).

60. The Act provides two special rules applicable to group situations in the corporate context. *See id.* §§ 3(6)(*b*), (*b*.1).

61. *Id.* § 4(1).

This statement is, if all material facts have been disclosed to the Minister, binding on the Minister for two years from the time when the statement was so submitted if, throughout that period, the ma terial facts so disclosed remain substantially unchanged.[62]

E. Canadianization

Since the coming into force of the Act, a number of companies have explored various methods by which they might achieve eligible status for purposes of the Act. One obvious method is to eliminate all of the interests of the foreign controller of the corporation. There has been at least one case in which this step was taken by a company which considered it important to achieve "eligibility." Another plan which has interested some companies might be called the "equity/voting split." These plans typically involve an effort to divorce the votes held by the controller from the equity and to vest those votes in the hands of Canadian voting trustees. The argument is then made that, by reason of the split, the company has become Canadian controlled. To date, the Agency has not been convinced that any of the plans of this sort which have been brought to its attention have been effective to make the company eligible.

V. REVIEWABLE INVESTMENTS: ACQUISITIONS

Where a non-eligible person (or a group with a member who is a non-eligible person) proposes to make an acquisition, that transaction will be reviewable under Section 8(1) of the Act if it is an "acquisition of control of a Canadian business enterprise."[63] Until October 15, 1975, there was an exemption for certain small businesses, defined as those with gross assets under $250,000 and gross revenues under $3,000,000.[64] As of October 15, 1975, the scope of that exemption was reduced. It now applies only where the business to be acquired is related to an existing business of the acquiring party in Canada.[65]

A. Canadian Business Enterprise

The following definitions in Section 3(1) are pertinent:

"Canadian business enterprise" means a business that is either a

62. *Id.*
63. *Id.* § 5(1).
64. *Id.* § 5(1)(*c*).
65. *Id.* § 31(3).

> Canadian business or a Canadian branch business;
> "business" includes any undertaking or enterprise carried on in anticipation of profit;
> "Canadian branch business" means a business carried on in Canada by a corporation incorporated elsewhere than in Canada that maintains one or more establishments in Canada to which employees of the corporation employed in connection with the business ordinarily report for work;
> "Canadian business" means a business carried on in Canada by
> (*a*) an individual who is either a Canadian citizen or a person ordinarily resident in Canada,
> (*b*) a corporation incorporated in Canada that maintains one or more establishments in Canada to which employees of the corporation employed in connection with the business ordinarily report for work, or
> (*c*) any number of individuals or corporations or combination of individuals and corporations, if any one or more of those comprising that number or combination are either individuals described in paragraph (*a*) or corporations described in paragraph (*b*) who, either alone or jointly or in concert with one or more other individuals or corporations so described, control or are in a position to control the conduct of the business.[66]

The provisions of Section 3(6)(*g*) are also important:

> [A] Part of a business that is capable of being carried on as a separate business is a Canadian business enterprise if the business of which it is a part is a Canadian business enterprise.[67]

Frequently, there is no difficulty in concluding that the subject matter of an acquisition is a "Canadian business enterprise," but occasionally this can be quite a problem. For example, is a company with divisions in a variety of places and one operating division in Canada, a Canadian business enterprise? Here the provisions of Section 3(6)(*g*) may be applicable. The question is: can the division be carried on as a separate business? In many situations it is not at all clear how that question is to be answered. It may involve consideration of the way in which the division has been operated by the vendor and the plans of the acquiring party for that division.

The question becomes more difficult where the business assets would not ordinarily be thought of as a "division." For example, under what circumstances could a ship be regarded as being

66. *Id.* § 3(1).
67. *Id.* § 3(6)(*g*).

"capable of being carried on as a separate business"? Obviously, the Section 3(6)(*g*) rule needs to be applied very carefully. Otherwise, a variety of situations could be brought within the Act which are probably beyond its intended scope.

There are other nonmanufacturing situations which pose questions of characterization. For example, are oil and gas rights which are not yet capable of production to be characterized as businesses, or as a part of a business capable of being carried on separately? Or are they more in the nature of inventory interests which can be transferred without effecting any change in control of the business? In January of 1976, the Minister published guidelines under Section 4(2) of the Act dealing with the acquisition of interests in oil and gas rights.[68] Those guidelines state generally that the acquisition of such interests cannot be considered to involve the transfer of control of a business, where the transaction is carried out by way of a "farm-out," or other similar arrangement, with respect to properties still under exploration.[69] On the other hand, where there is a sale of property which is capable of production and of being carried on as a separate business, the transaction would be reviewable.[70]

In the real estate industry, what is the proper characterization to accord to rental real property? Is it a business, or is it just an "investment," like a portfolio of debentures? Does it make a difference if the property is an apartment building, a commercial office building, a shopping center, and so on? Guidelines dealing with problems in the real estate area were issued in 1974,[71] but questions still arise. The proper treatment of real estate acquisitions is under active review within the Agency.

B. Acquisition of Control

The Act elaborates on the meaning of the acquisition of control with a series of technical provisions found in Sections 3(3), (6), and (8).

1. The General Limitation

In contrast to the relatively broad treatment given to the "control" notion for purposes of determining whether a corporation

68. Guidelines concerning Acquisitions of Interests in Oil and Gas Rights, 110 Can. Gaz., pt. I, at 947 (1976).

69. *Id.* paras. 3, 4.

70. *Id.* para. 5.

71. Guidelines concerning real estate business, 108 Can. Gaz., pt. I, at 1201 (1974).

is eligible,[72] for acquistion purposes the "notion" of "control" is restricted by Section 3(3)(*a*):

> For the purposes of this Act,
> (*a*) control of a Canadian business enterprise may only be acquired,
> (i) in the case of a Canadian business enterprise that is a Canadian business carried on by a corporation either alone or jointly or in concert with one or more other persons,
> (A) by the acquisition of shares of the corporation to which are attached voting rights ordinarily exercisable at meetings of shareholders of the corporation, or
> (B) by the acquisition of all or substantially all of the property used in carrying on the business in Canada, and
> (ii) in the case of any other Canadian business enterprise, by the acquisition of all or substantially all of the property used in carrying on the business in Canada . . . .[73]

The question arises from time to time whether the provisions of Section 3(3)(*a*) are "deeming" provisions or whether they prescribe a necessary condition. Do they deem a transaction of the sort described to be an acquisition of control, or do they simply provide that, unless the transaction falls within one of the described classes, it cannot be regarded as an acquisition of control? If the latter is the correct view, then a transaction could satisfy the condition but still not amount to an acquistion of control. For example, the acquiring party may already have indirect or ultimate control. Agency officers have tended to agree with the latter view, but there has been no official position taken on the question.

It should be noted that, because of the wording of Section 3(3)(*a*)(ii), control of a "Canadian branch business"[74] can only be acquired through the acquisition of the property used in that business. By implication, the indirect acquistion of control of that business, through the acquisition of the shares of the foreign corporation which carries it on, would not be reviewable.[75]

The phrase "substantially all of the property"[76] gives rise to

---

72. *See* FIRA §§ 3(1), (7).

73. *Id.* § 3(3)(*a*).

74. See notes 66-67 *supra* and accompanying text.

75. However, where the business is carried on by a foreign corporation through a Canadian-incorporated company, the sale of the shares of the foreign corporation may well give rise to reviewability. See notes 79-81 *infra* and accompanying text.

76. FIRA §§ 3(3)(*a*)(i)(B), (ii).

various questions. One is whether that phrase is to be construed as referring to quantitative considerations or to qualitative ones. For example, a business might dispose of some "critical" or "essential" asset even though it retained, in quantitative terms, most of its assets. There is certainly an argument to be made that such a transaction comes within the intent of the Act as to reviewability.

2. Deemed Acquisitions

There are two groups of provisions which deem certain transactions to be acquisitions. The first group, contained in Sections 3(3) (*c*), (*d*), and (*e*), deem certain transactions to be the acquisition of control of a business carried on by a corporation. These Sections provide that:

> (*c*) the acquisition by any person or group of persons of shares of a corporation to which are attached
>
> (i) 5% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are publicly traded, or
>
> (ii) 20% or more of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are not publicly traded,
>
> shall, unless the contrary is established, be deemed to constitute the acquisition of control of any business carried on by the corporation;
>
> (*d*) the acquisition by any person or group of persons of shares of a corporation to which are attached more than 50% of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, whether or not the shares of the corporation are publicly traded, shall, unless the person or group of persons acquiring the shares had, at the time of the acquisition, control in fact of the corporation, be deemed to constitute the acquisition of control of any business carried on by the corporation other than any such business carried on, for a purpose not related to the provisions of this Act, by it jointly or in concert with one or more other persons; and
>
> (*e*) an amalgamation of two or more corporations the effect of which is to continue the amalgamating corporations as one corporation (in this paragraph called the "amalgamated corporation") shall be deemed, except in the case of an amalgamation that is part of a corporate reorganization that is carried out for a purpose not related to the provisions of this Act and that results in the amalgamated corporation being controlled by the same person or group of persons that controlled each of the amalgamating corporations, to constitute the acquisition of control by the amalgamated corporation of the businesses carried on by the amalgamating corporations other than

> any business carried on, for a purpose not related to the provisions of this Act, by an amalgamating corporation jointly or in concert with one or more other persons who are not amalgamating corporations . . . .[77]

There are some noteworthy differences between the Sections. Section 3(3)(*c*) is a presumption which applies "unless the contrary is established." Sections 3(3)(*d*) and (*e*) are conclusive presumptions, but each contains an exception related to continuity of control. If the deeming clause of any of these Sections is applicable, then for the purposes of the Act there will have been an acquisition of control.

A second set of deeming provisions is set out in Sections 3(6)(*c*), (*d*), and (*d*.1). Essentially, they provide that an acquisition of rights to property is to be treated as the acquisition of the property to which the right applies. The text of the provisions is as follows:

> (*c*) a person who has a right under a contract, whether written or oral and whether express or implied, in equity or otherwise, either immediately or in the future and either absolutely or contingently,
>
> (i) to, or to acquire or dispose of, shares of a corporation, or to control the voting rights attaching to shares of a corporation, or
>
> (ii) to, or to acquire or dispose of, any property used in carrying on a business,
>
> . . . shall be deemed in any case described in subparagraph (i), to have the same position in relation to the control of the corporation as if he owned the shares, and, in any case described in subparagraph (ii), to have the same position in relation to the control of the business as if he owned the property;
>
> (*d*) the acquisition of any right described in paragraph (*c*) shall be deemed to constitute the acquisition of the shares or property to which the right relates except where it is established that the right was acquired for the purpose of safeguarding the interests of the person by whom it was acquired in respect of a loan made by him, or in respect of an amount paid or payable by him as consideration for the sale or assignment to him of any right or rights in respect of a loan made by another person, and not for any purpose related to the provisions of this Act;
>
> (*d*.1) the exercise of a right described in paragraph (*c*) shall be deemed not to constitute the acquisition, by the person who had the

77. *Id.* §§ 3(3)(*c*)-(*e*).

right, of the shares or property to which the right related, whether or not the acquisition of the right was deemed by paragraph (*d*) to constitute the acquisition of the shares or property . . . .[78]

A special rule is set forth in Section 3(6)(*h*) which provides that:

> [A] business carried on by a corporation that is controlled in any manner that results in control in fact, whether directly through the ownership of shares or indirectly through a trust, a contract, the ownership of shares of any other corporation or otherwise, by another corporation shall be deemed to be carried on by the controlling corporation as well as by the corporation by which the business is in fact carried on.[79]

An important application of this section appears to arise in the area of transactions in the shares of holding companies. Assume Corporation *A*, a U.S. company, proposes to acquire all the shares of Corporation *B*, another U.S. company, which has a Canadian subsidiary, Corporation *C*, which carries on business in Canada. The argument goes as follows: the business carried on by Corporation *C* is a "Canadian business" by reason of part (*b*) of the definition of that term.[80] Pursuant to Section 3(6)(*h*), Corporation *B* is deemed to carry on that business. Accordingly, the acquisition by Corporation *A* of all the shares of Corporation *B*—a company which carries on a Canadian business—satisfies the requirements of Section 3(3)(*a*)(i)(A) for a reviewable acquisition.[81] It can be questioned whether this argument is correct, but the Agency has to date taken the position that such transactions are reviewable.

3. Exclusions

Exclusions are transactions deemed not to be acquisitions of control. The first group of exclusions concerns corporations. The principal provision is set forth in Section 3(3)(*b*), as follows:

> [C]ontrol of a Canadian business enterprise that is a Canadian business carried on by a corporation either alone or jointly or in concert with one or more other persons is not acquired by reason only of

78. *Id.* §§ 3(6)(*c*)-(*d*.1).
79. *Id.* § 3(6)(*h*).
80. See note 66 *supra* and accompanying text.
81. See note 73, *supra* and accompanying text.

> (i) the acquisition by any person or group of persons of shares of the corporation to which are attached
>
> (A) less than 5% of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are publicly traded, or
>
> (B) less than 20% of the voting rights ordinarily exercisable at meetings of shareholders of the corporation, in the case of a corporation the shares of which are not publicly traded . . . .[82]

The second group of exclusions also concerns corporations. These are the exceptions in Sections 3(3)(*d*) and (*e*) mentioned above.[83] These two exceptions apply to particular instances of continuity of control. The Act, however, does not expressly provide, as a general rule, that continuity of control avoids reviewability. This has caused some considerable concern in connection with corporate reorganizations. For example, Company *A* controls Company *B* and decides to transfer the shares of Company *B* to a new company wholly owned by Company *A*. There is an argument that the new company has never had control of Company *B* and has now acquired control. Accordingly, it could be argued that the transaction is reviewable, even though it is clear that there is continuity of ultimate control in Company *A*.

To deal with these concerns, guidelines were issued under Section 4(2) of the Act, dealing with corporate reorganizations.[84] The guidelines state that transactions within a wholly-owned corporate group which do not result in any change in ultimate control and which involve a Canadian-incorporated business as the acquiring company are considered not to be reviewable.[85] Other corporate reorganizations may or may not be reviewable, depending on their facts.

Section 3(6)(*c*)[86] excepts from its provisions any right to acquire shares or assets "arising under a contract that is entered into after the coming into force of this Act and that provides that the right is not exercisable until the death of an individual designated therein

82. FIRA § 3(3)(*b*)(i).

83. See note 77 *supra* and accompanying text.

84. Guidelines Concerning Corporate Reorganizations, 109 Can. Gaz., pt. I, at 1570 (1975).

85. *Id.* § 3, at 1572.

86. See text accompanying note 78 *supra*.

or any such right that is contingent upon the Governor in Council allowing the investment that is the subject of the right."[87] Accordingly, the provisions of Section 3(6)(*d*) do not apply to deem the making of such a contract to be an acquisition. Of course, at the subsequent time when the rights are exercised, there may be an acquisition.

Section 3(6)(*d*) provides that the acquisition of a security interest is excepted from the general rule that the acquisition of a right is treated as the acquisition of the property to which the right related. When Section 3(6)(*d*.1) is taken into account as well, it is evident that the exercise of the security rights is also exempt from review.[88] This exemption would not extend to a buyer on a sale made pursuant to a power of sale in a mortgage, since the buyer is not exercising any security interest.

C. Agency Opinion Letters

A variety of questions can arise in determining the proper application of the Act to particular transactions. Is the subject matter of the transaction a Canadian business enterprise? Is there an acquisition of substantially all the business assets? Does the acquisition result in a change of control? Is there an applicable exception? While investors are free to proceed without consulting the Agency, they frequently consider it prudent to do so. The officers of the Compliance Branch of the Agency have the responsibility to assist enquiring investors to determine the implications of the FIRA on their transactions. In appropriate cases, the Agency provides a letter setting out its opinion on the reviewability of the specific transaction, based on the information provided by the investor.

VI. REVIEWABLE INVESTMENTS: NEW BUSINESSES

A. Effect of Phase II

Phase I of the Act, which regulated foreign acquisitions of already existing Canadian businesses, came into force on April 9, 1974.[89] As of October 15, 1975, the provisions of the Act relating to the establishment of new businesses became effective.[90] Section 8(2) of the Act provides as follows:

---

87. FIRA § 3(6)(*c*).

88. See text accompanying note 78 *supra*.

89. See notes 16-17, 19 *supra*.

90. Certain Sections of the Act Proclaimed in Force October 15, 1975, SI/75-99, 108 Can. Gaz., pt. II, at 2577 (1975).

> Every non-eligible person, and every group of persons any member of which is a non-eligible person, that proposes to establish a new business in Canada shall,
> (*a*) if immediately before the time when the new business is proposed to be established no other business is carried on in Canada by that person or group of persons, or
> (*b*) if each other business carried on in Canada by that person or group of persons immediately before the time referred to in paragraph (*a*) is a business to which the new business would, if it were established, be unrelated,
> give notice in writing to the Agency of such proposal in such form and manner and containing such information as is prescribed by the regulations.[91]

A business which was established prior to Phase II is not reviewable. Section 3(4) provides:

> For the purposes of this Act, a business is established in Canada only if there is an establishment in Canada to which one or more employees of the person or group of persons establishing the business report for work in connection with the business, and the time at which a business is established in Canada is the time at which the first of such employees reports for work in connection with the business at such an establishment.[92]

B. Exemptions from Review

1. Businesses which are not Established

The requirements of Section 8(2) apply only to businesses to be established in Canada. Accordingly, if a business is carried on in Canada without being established there, it would not be reviewable. For example, a sale or service operation conducted from across the border by a U.S. enterprise using U.S.-based personnel might very well not be established in Canada. It would therefore not be subject to review.

2. Expansions of Existing Businesses

The requirements of Section 8(2) apply only to the establishment of a new business in Canada. Section 3(1) of the Act defines a new business "as a business not previously carried on in Canada by the person or group of persons in relation to which the expression is

91. *See* FIRA §§ 31(1)-(2).
92. *Id.* § 3(4).

relevant."[93] Where a person has already been engaged in a business in Canada and proposes to carry on an additional activity, it is important to consider whether that activity is an expansion of the existing business or whether it constitutes a new business. If it is merely an expansion, it is not reviewable.

"Guidelines Concerning Related Business" have been issued pursuant to Section 4(2) of the Act.[94] Section 3 of the Guidelines deals with the meaning of the term "new business." Section 3(1) sets out the general principle:

> In determining whether an additional business activity of a non-eligible person constitutes a new business rather than the expansion of an established business, the goods or services produced by the activity is, for the purpose of these guidelines, the principal factor to be taken into account.[95]

The notes in the Guidelines concerning that Section indicate that there are a number of other considerations which are not, by themselves, significant. These include the use of new premises, continuity or change of personnel, and the use of a new organizational arrangement, for example, a new subsidiary company.[96]

3. New Businesses which are Related

Section 8(2) provides, in effect, that a new business is not reviewable if it is related to a business carried on in Canada by the same person immediately prior to the commencement of the new business. The notion of "relatedness" appears to acknowledge that every business enterprise must be regarded as an inherently dynamic and developing entity: that there are, for any business, a number of avenues of potential development which are a natural route for this growth. Thus, the Act does not freeze businesses at a particular moment in their growth. Rather, the Act permits the business to develop without review, provided that the line of development is a natural, "related," one for that business.

The concept of a "related business" is not defined in the Act. The principal purpose of the "Guidelines Concerning Related Business" is to set forth ways in which one business can properly be said to be related to another business. The Introduction states:

---

93. *Id.* § 3(1).
94. Guidelines Concerning Related Business, 109 Can. Gaz., pt. I, at 3358 (1975).
95. *Id.* § 3(1).
96. Notes Concerning Subsection 3(1), *id.*

> This section contains six Guidelines for determining if a new or acquired business of a non-eligible person is related to an established business of that person in Canada. If any one of the six Guidelines is satisfied, then the new or acquired business and the established business *are* related.
>
> The Guidelines employ a number of different concepts for determining relatedness between a new or acquired business, and an established business. These include *vertical integration* (Guideline 1 and 2); *direct substitutability* (Guideline 3); and *same technology and production processes* (Guideline 4). The fifth Guideline indicates that a new business is related to an established business if the new business results from *research and development* carried out in Canada by or on behalf of the established business.
>
> Guideline 6 provides for relatedness between two or more businesses to be established through their *industrial classification.* The classifications are based on the Standard Industrial Classification
>
> . . . .
>
> If none of the six Guidelines is satisfied, a new or acquired business of a non-eligible person may nevertheless be related to an established business of that person through some principle other than those provided for in Guidelines 1 to 6, or on the grounds that the quantitative requirements of those Guidelines are inappropriate to the particular economic or industrial situation.[97]

C. *Other Phase II Matters*

The "Guidelines Concerning Related Business" were not designed to deal with the full range of questions which may arise in connection with Phase II. One question which has arisen in discussions between Agency officers and investors is how the application of the related business concept applies to "joint ventures." The problem can arise in the following way. *A* and *B* have each separately carried on a particular type of business in Canada. They now determine that they will jointly conduct a business which, if it were carried on separately by each of them, would be related to their respective existing businesses. An argument based on the wording of Section 8(2) would be that, since *A* and *B* have not previously carried on business before as a group, the new business must be regarded as unrelated to the existing businesses. The contrary position is that the business can properly be said to be carried on by the participants in the group, and that therefore the new business is not

97. Introduction, *id.* § 4.

reviewable if it is related to an existing business of each of the participants. This position places more weight on the substance of the arrangements than on their form. In this respect, this position seems more consistent with the positions set out in the Corporate Reorganization Guidelines[98] and in the Note to Section 3 of the Related Business Guidelines[99] concerning the use of a new organizational arrangement.[100]

VII. ENFORCEMENT

Section 8(3) provides that, where the Minister has reasonable and probable grounds to believe that a reviewable investment has been made or is proposed to be made, he may make a demand for the giving of a notice. The demand stipulates the time within which the notice is to be given and indicates the nature of the proceedings that may be taken if the investor fails to comply with the demand.[101] The Minister has the authority to carry out an investigation where he has reasonable and probable grounds to believe that there is noncompliance with the Act.[102]

Under Section 19, the Minister may apply to a superior court for an injunction with respect to an investment in circumstances in which

> (*a*) the Governor in Council has not, by order, allowed the investment and is not deemed to have allowed it, or
> (*b*) although the Governor in Council has, by order, allowed the investment or is deemed to have allowed it, the terms and conditions on which the investment is about to be made or has been made, as the case may be, vary materially from those disclosed in any notice in writing given under subsection 8(1), (2) or (3) and in any other information or evidence given under this Act in relation thereto . . . .[103]

If the court is satisfied that these requirements are fulfilled, it may grant an injunction against the making of the investment or against any action in relation to the investment which would prejudice the ability of a court to make an effective order under Section 20.

---

98. See note 84 *supra*.

99. See note 96 *supra*.

100. *See also* FIRA § 3(1) ("non-eligible person") (note 47 *supra*); *id.* § 3(2) (text accompanying note 52 *supra*); *id.* § 3(6)(*h*) (text accompanying note 79 *supra*).

101. FIRA § 8(3.1).

102. *Id.* § 15.

103. *Id.* § 19(1).

Section 20 provides for an order to render an investment nugatory. The text of the Section is as follows:

> (1) Where a non-eligible person or group of persons any member of which is a non-eligible person has made an actual investment in circumstances in which
>
> (*a*) a demand has been served by the Minister under subsection 8(3) in relation to the investment and has not been complied with within the time stipulated in the demand,
>
> (*b*) the Governor in Council has, by order, refused to allow the investment, or
>
> (*c*) although the Governor in Council has, by order, allowed the investment or is deemed to have allowed it, the terms and conditions on which the investment has been made vary materially from those disclosed in any notice in writing given under subsection 8(1), (2) or (3) and in any other information or evidence given under this Act in relation thereto, a superior court, on application on behalf of the Minister, may make such order as, in its opinion, is required in the circumstances, to the end that the investment shall be rendered nugatory not later than the expiry of such period of time as the court considers necessary to allow in order to avoid or reduce, to the greatest possible extent consistent with the attainment of that end, any undue hardship to any person who was not involved in the investment knowing it to be subject to be rendered nugatory under this Act.[104]

It is important to note that a Section 20 order cannot be obtained merely because a non-eligible person has made an investment without going through the review process. The Section 20 order may be obtained only in the circumstances specified in subsections 20(1)(*a*), (*b*), and (*c*). Once the superior court has jurisdiction, it has the power to revoke or suspend voting rights attached to corporate shares or order the disposition of any stock or property acquired by such non-eligible person, on such terms and conditions as the court deems just and reasonable. If the person or persons subject to the court order are outside of Canada and refuse to comply, the court may vest such shares or property in a trustee to carry out the orders of the court.[105]

What does it mean to render an investment "nugatory"? The Act does not define the term. One meaning of nugatory is "having

104. *Id.* § 20(1).
105. *Id.* §§ 20(2)-(3).

no force." With this meaning in mind, it has been suggested that it would be within the power of a court under Section 20 to make an order requiring the rescission of a transaction. Obviously, there could be a great many transactions in which a rescission order would not be adequate to put the parties back in their original positions. For example, the vendor may have spent the proceeds of the sale. Section 20(2) makes it clear that orders prohibiting the exercise of rights and orders for divestiture are also within the scope of the power.[106]

Apart from the non-eligible investor himself, there are other persons whose interests may be affected by a Section 20 order. The vendor who sells to a non-eligible investor could be affected. The apparent possibility that a Section 20 order could be framed in terms of rescission has led many lawyers to advise their vendor clients to require evidence from the purchaser that he is not non-eligible. If the purchaser is non-eligible, it is common to make the transaction conditional upon approval under the Act[107] or on satisfactory confirmation that the transaction is not reviewable under the Act. The agreement may also contain a covenant that the non-eligible purchaser will take all necessary action expeditiously to obtain an approval. There may be a termination date, so that the parties cannot be held indefinitely to the transaction while the purchaser is seeking an approval.

Other affected persons are those who acquire their interest in the business subsequent to the foreign investor. For example, what is the position of the Canadian-controlled enterprise which purchases a business from a prior owner, also Canadian, who in turn had purchased from a company that may be known or believed to be foreign controlled? It is clear that a subsequent purchaser is not to be the subject of an order under Section 20 where he was not involved in the investment "knowing, or in circumstances where he ought reasonably to have known, that that investment was subject to be rendered nugatory."[108] When one considers the strict requirements for the applicability of Section 20,[109] it is difficult to imagine many cases in which a subsequent party purchased "knowing or . . . where he ought reasonably to have known" that Section 20 was

106. *Id.* §§ 20(2)(*a*)-(*c*).
107. See note 87 *supra* and accompanying text.
108. FIRA § 20(2).
109. See notes 104-05 *supra* and accompanying text.

applicable. Certainly, the knowledge or imputed knowledge required seems to go beyond mere knowledge or belief that a previous owner was a non-eligible person. There is another pertinent consideration. It is not easy to see how action taken against a subsequent owner could ever be effective to render nugatory the investment of a previous non-eligible owner who has departed from the scene. Indeed, the consequence of such action might instead be to render nugatory the investment of a Canadian, which would be, at the very least, a bizarre step in terms of the stated purpose of the Act.

The Agency has commenced a program of monitoring the performance of the undertakings given by applicants whose investments have been allowed. The procedure involves an Agency communication to the applicant, at appropriate intervals, requesting advice as to the steps taken to comply with the undertakings, followed by an appraisal of the response and any further steps indicated by that appraisal. In carrying out this monitoring function, the Agency will rely for guidance upon the remarks of the Honourable Alastair Gillespie, the Minister responsible for the Act at the time, as to the government's position on enforcement:

> You will recall that I suggested some undertakings at least would be based on the medium-term plans of the acquiring company. These plans would, to some extent, be based on conjecture about the future and therefore would simply reflect the company's anticipation concerning its future development. They would not be guaranteed in their entirety. Thus flexibility and good sense must be exercised by the Minister.
>
> In normal circumstances the inability to fulfill undertakings will lead to discussions with the Minister and perhaps to the negotiation of new undertakings. Like any contract, an undertaking can be modified with the consent of both parties. If, however, the failure to comply with an undertaking is clearly the result of changed market conditions—for example, the undertaking to export frisbees is followed by the collapse of the frisbee market—the person would not be held accountable. It should be remembered, however, that some understakings [*sic*] may be tailored to a range of market expectations.[110]

110. *Minutes of Proceedings and Evidence of the Standing Committee on Finance, Trade and Economic Affairs Respecting Bill C-132*, 29th Parl., 1st Sess., Issue No. 26, at 16 (June 5, 1973) (remarks of Minister Gillespie).

VIII. CONCLUDING COMMENTS

It will be evident from the above discussion that there are various areas of uncertainty about the scope of the jurisdiction of the Act. As further experience is gained, it is to be hoped that helpful clarifications can be provided either by way of further Guidelines or by legislative amendment, as appropriate. As well, the experience with Phase II, which has been underway for a little less than six months, will likely point up areas in which administrative practices can be refined and improved. At this stage, it would be rash to venture anything like a definitive appraisal of the Act and its consequences. The following rather tentative assessment was given a few months ago by an observer of the Agency who was closely involved with its initial development:

> The legislation is innovative and demands from both the Agency and the applicants flexibility and resilience if the screening process is to be administered fairly and effectively. There is every indication that both sides are exhibiting such flexibility and resilience. It may be unfortunate that it was felt necessary to enshrine the provisions relating to the applicability of the statute in such technical, convoluted terminology. No doubt all the phrases are not apt for application to all industries. Nevertheless, the real basis of the statute is working.[111]

111. Grover, *The Foreign Investment Review Act: Phase I*, 1 CAN. BUS. L.J. 97, 98 (1975).