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Investment Canada and the Resource Sector

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The New Policy – Objectives

The Government of Canada has moved to implement a major election promise by introducing new foreign investment regulation legislation. The Investment Canada Bill (Bill C-15, first reading, December 7, 1984) initiates major changes in Canadian foreign investment policy and, in particular, responds to strong dissatisfaction expressed by both Canadian and foreign investors over Canada's investment climate. Much of this dissatisfaction had focused on the Foreign Investment Review Agency (FIRA), and the severe dampening effect that its review process, coupled with the Canadianization elements of the National Energy Program, had had on new energy industry investment.

A major objective of the new Conservative government policy is to present a friendlier Canadian environment for foreign investors. Industry Minister Sinclair Stevens has emphasized the importance of investor perceptions. According to Minister of International Trade, James Kelleher, the intention is to show that Canada is "under new management". Instead of facing potential foreign investors with an adversarial regulatory system – and one often perceived to be slow, inflexible, secretive, and unreasonably demanding – the new policy welcomes foreign investment. This is subject only to an "oversight" form of control, with significant potential restrictions confined to sensitive activities related to Canada's cultural heritage or national identity.

The Investment Canada Bill

The Investment Canada Bill changes and clarifies the role and powers of FIRA. In particular:
- The Agency is renamed "Investment Canada".
- New foreign investment, with the exeption of that determined by the Cabinet to be related to Canada's cultural heritage or national identity, will not be reviewed by Investment Canada.
- However, notice must still be given to Investment Canada by non-Canadians who propose any investment to establish or to acquire control of a Canadian business, and the Agency will advise whether the proposed investment is not reviewable.
- Foreign takeovers of existing Canadian companies will be reviewed only if the target company has assets of $5 million or more, or if the proposed takeover is in a culturally-sensitive area. Proposals reviewed will be approved if the investment is likely to produce a "net benefit" (as opposed to the existing "significant benefit") for Canada.
- Indirect takeovers – sales of Canadian subsidiaries of foreign corporations to other foreign corporations – will be screened if the assets of the Canadian subsidiary exceed $50 million, if culturally-sensitive areas are involved, or if the subsidiary's assets exeed $5 million and this represents more than half the value of the total international transaction.
- Detailed rules and presumptions for determination of Canadian ownership status are set out in the Act.
- Investment Canada will make recommendations for final decisions by the Minister of Industry (as opposed to the Cabinet under the old system).
- Review must be completed within 75 days of submission of a complete application (unless the applicant otherwise agrees), or the investment will be deemed to be approved.
- Investment Canada is also given duties, in its role as advisor to the Minister, to promote foreign investment in Canada.

Conflicting Policies

A major policy shift is proposed for the Agency. While FIRA could be characterized as a foreign investment watchdog agency, Investment Canada's role in "facilitating foreign investment" is emphasized. However, it is important to note that Investment Canada does retain functions in screening foreign investment proposals relating to major direct or indirect foreign takeovers of Canadian business enterprises. New foreign investment related to Canada's cultural heritage or national identity is also potentially reviewable.

Investment Canada will be required to pursue objectives that, to some degree at least, are in conflict. On the one hand it is under a duty to advise and assist the Minister in promoting foreign investment in Canada. On the other,

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it must advise the Minister whether any particular proposal is reviewable, and if so, assist the Minister in determining whether it is likely to produce a net benefit for Canada. In these circumstances, even the most impressive balancing performance by the Agency and the Minister is unlikely to avoid totally charges of conflict of interest.

For example, the imposition of time-limits on agency decisions is designed to eliminate the expensive delays associated with regulatory lag. However, because the responsibility for ensuring that review is completed within the prescribed time frame falls on Investment Canada, there will be an unfortunate but inevitable incentive for agency officials to be aggressive and demanding and to pressure proponents to agree to time-limit extensions. This may well raise objections that it is the old FIRA process under another name.

On the other hand, if the Agency is seen to be too active and aggressive in the promotion of new foreign investment, the clamour will emanate from the temporarily-lost legion of Canadian economic nationalists. It should be remembered that opinion surveys continue to show (depending on how the questions are posed) significant popular support for such nationalistic goals as increased Canadian ownership in the oil and gas industry. It might be observed also that former members of the now-defunct Committee for an Independent Canada met recently to discuss its possible re-birth.

Legal Issues – Uncertainty

There are also legal issues apparent in the Investment Canada Bill that bear on these more general policy questions. First, there is the definition of the investment areas for which foreign proposals would continue to be subject to review. The terms "cultural heritage" and "national identity" are far from precise, and are not defined. However, the federal Cabinet is authorized to prescribe specific types of business activity that, in its opinion, are related to Canada's cultural heritage or national identity. This is likely to be done by regulations under s.35. Background materials released with the Bill refer to "culturally sensitive areas such as book publishing and film production and distribution". This provides a strong clue to the types of businesses likely to be designated.

It must be remembered, however, that the operative mechanism is a discretionary power vested in Cabinet. As a matter of interpretation, it is arguable that "national identity" could, for example, be applied to the natural resource sectors, such as the traditional coastal fishing industries that continue to strongly influence regional lifestyles, and generally contribute to Canada's national identity as a maritime nation. Even with respect to the energy resource area, proponents of the National Energy Program have argued that those policies and legislative measures were necessary to maintain Canada's identity, given the national economic importance of the energy sector.

Moreover, different terms have been used in statutes related to the Canadian publishing and broadcasting industries. For example, the *Broadcasting Act,* R.S.C. 1970, c.B-11, s.3, refers to provision for expression of "Canadian identity" and to safeguarding, enriching and strengthening the "cultural, political, social and economic fabric of Canada". The *Cultural Property Export and Import Act,* S.C. 1974-75-76, c.50, refers to "national heritage in Canada", while the encouragement of production of Canadian feature films is the only general objective stated in the *Canadian Film Development Corporation Act,* R.S.C. 1970, c.C-8. The fact that these statutes, concerned with promotion of Canadian culture, use different language suggests that the term "national identity" was intended to include areas of activity beyond the traditional cultural field.

Notwithstanding any stated policy, and even notwithstanding regulations that designate traditional cultural activities only, the wider discretion to designate additional types of business activities, including natural resource sector activities, remains. However, even if this extension occurs, proposals that would be reviewable may still be excluded from review if Cabinet, on the recommendation of the Minister, considers it to be in the public interest (s.15(b)). This further discretion merely introduces another aspect of uncertainty for prospective foreign investors.

"Net Benefit to Canada"

Another uncertaintly arises from the new "net benefit to Canada" criterion for approval of reviewable investment proposals. This clearly establishes a standard different from the previous "significant benefit" for Canada. There will be a lower standard to be met by foreign investment proposals. The literal meaning suggests a "net of detriments" approach.

Section 20 prescribes factors to be taken into account in determining net benefit to Canada. But how should the relevant factors be weighted? Is it now possible, given the new standard, that serious deficiency in relation to one or more of the factors could be counterbalanced by strength on other matters to produce "net benefit"? Some further definition can be provided by ministerial guidelines and interpretation notes, as contemplated by s.38. Essentially, however, the Agency and the Ministry begin with a slate clear of any interpretive "jurisprudence" or other policies that could give greater certainty to foreign investors.

This uncertainty is compounded by the fact that, while both the basic decision standard and the scope of Agency review have been substantially changed, the factors to be taken into account are little changed from those in the *Foreign Investment Review Act,* S.C. 1973-74, c.46. The Investment Canada Bill repeats word-for-word the old factors, with the addition of references to cultural policies and cultural policy objectives, and a new factor concerning Canada's ability to compete in world markets.

A final set of uncertainties has been carried over from the former Act. Like the *Foreign Investment Review Act,* the Investment Canada Bill contains no requirement that reasons for decisions on investment proposals be given. The practice under FIRA was to give no reasons for disallowance of a proposal. Part of the original basis for this reluctance to give reasons for decisions was the confidentiality provisions contained in the *Foreign Investment Review Act.* It has been pointed out that these

requirements were apparently intended to protect foreign investors and not the Government of Canada (E.J. Arnett, R. Rueter and E.P. Mendes, "FIRA and The Rule of Law", 62 Can. Bar Rev. 121 (1984) at 127). In fact, many foreign investors, as well as their legal advisors, have expressed concern that FIRA officials have been unduly secretive and unhelpful in the application and review process. These provisions have been retained essentially intact in the new Act, including a prohibition on disclosure of undertakings given by foreign investors where, in the opinion of the Minister, the person who gave the undertaking would be prejudicially affected (s.36(5)).

New provisions for advisory opinions have been included in the Investment Canada Bill (s.37). The Minister shall, in the case of questions as to Canadian ownership status (and "may" in relation to the applicability of any other provision of the Act), provide advisory opinions that are binding so long as the information submitted is accurate and the material facts remain unchanged. However, these rights to advisory opinions are unlikely to remove completely the suspicion produced by continuation of the confidentiality provisions, and by the apparent survival of the practice of giving no reasons for final determinations.

All of this is not to suggest that the Investment Canada Bill represents bad policy. Nor is it suggested that Investment Canada is merely FIRA under another name. The point is that an abrupt change in policy direction in an area as significant as foreign investment is unlikely to go smoothly. In a desire to retain what it considers the best of the existing "watchdog" approach to foreign investment policy, while at the same time moving aggressively to promote beneficial foreign investment, the government has left itself open to charges that Investment Canada will be hampered by apparent conflicts of interest. It also seems clear that the introduction of new statutory standards and decision factors, as well as a new regulatory process, will produce legal as well as policy uncertainties, at least in the short term. An important test of the new policy, the new Agency, and the implementing statute, will be the success of the Ministry and Investment Canada in removing or reducing these uncertainties.

Churchill Falls: A Comment

The decision last spring by the Supreme Court of Canada in the *Churchill Falls* case *[Churchill Falls (Labrador) Corporation Ltd.* v. *Attorney-General of Newfoundland* (1984), 8 D.L.R. (4th) 1 rvg. (1982), 134 D.L.R. (3d) 288 (Nfld. C.A.), *sub nom. Reference re Upper Churchill Water Rights Reversion Act, 1980]* touches on a number of significant issues in constitutional law – especially as it affects the limits of a province's power to manage its natural resources.

Although the background to the case involves a lengthy and complicated series of events, the essential facts can be stated briefly. In the late 1950s, active consideration was given to the possibility of developing the immense hydro-electric potential of the Churchill River (then called the Hamilton River). To this end the Government of Newfoundland entered into a lease with Churchill Falls (Labrador) Corporation Limited (hereinafter CFLCo). CFLCo, then a subsidiary of Brinco Limited, is now jointly owned by two provincial Crown corporations, Newfoundland and Labrador Hydro and Hydro-Quebec, approximately two thirds and one third, respectively. This lease was approved by the *Churchill Falls (Labrador) Corporation Limited (Lease) Act, 1961,* S.N. 1961, No. 51, as am. (hereafter *Lease Act*).

The development of the Churchill Falls site was dependent on surmounting two major obstacles – the financing of its considerable capital costs, and the development of technology to allow the efficient transmission of power over long distances to potential markets. In both these respects the participation of Hydro-Quebec was crucial. Hydro-Quebec engineers devised a means of effective energy transmission using high-voltage lines, and certain financial commitments by Hydro-Quebec provided for security in the event of insufficient funds to complete the project or CFLCo's inability to meet debt service payments. Most critical to the financial success of the project, however, was Hydro-Quebec's 1969 agreement with CFLCo to purchase the power produced by the development for a period of 40 years (with an option for Hydro-Quebec to renew for another 25 years). It is this agreement – the Power Contract – which has been at the centre of the interprovincial dispute surrounding Churchill Falls.

The Churchill Falls development was largely constructed between 1967 and 1974, with transmission of power to Quebec beginning in 1971. From an early date, the Power Contract was a source of conflict between the governments of Quebec and Newfoundland. The heart of the problem lay in Newfoundland's attempts to recall power for its own use, pursuant to a term in CFLCo's statutory lease which authorized export, "[p]rovided that upon the request of [Newfoundland] consumers of electricity in the Province shall be given priority where it is feasible and economic to do so". In 1976 two requests were made – first to Hydro-Quebec, and then to the Province of Quebec – for diversion of power (first 600 MW, and later 800 MW) for the use of Newfoundland. These unsuccessful requests were followed by the adoption by Newfoundland of an Order in Council requiring CFLCo to supply Newfoundland with 800 MW of power beginning in October 1983. CFLCo refused to comply in view of its commitments to Hydro-Quebec under the Power Contract, thus initiating a lengthy process of litigation in the courts of both Quebec and Newfoundland.

In an apparent attempt to resolve the issue quickly and definitively, the Government of Newfoundland in 1980 passed the *Upper Churchill Water Rights Reversion Act,* S.N. 1980, c.40 (hereafter the *Reversion Act*), and, prior to its coming into force, referred the legislation to the Newfoundland Court of Appeal for an advisory opinion as to its validity. In its judgment of March 5, 1982, the Court held unanimously that the *Reversion Act* was *intra vires.* This decision was appealed to the Supreme Court of Canada.

The *Reversion Act* purported to repeal the *Lease Act* and provided for the reversion of all water rights in the project to the province. While both secured creditors and shareholders of CFLCo were to be compensated directly under the Act, CFLCo itself was not. Moreover, any actions for compensation not based on the rights given in the *Reversion Act* were barred.

Four major grounds of constitutional challenge to the *Reversion Act* were put forward. Two of these (objections to the legislation as regulating interprovincial trade and commerce, and as relating to an interprovincial work or undertaking) were not addressed by the Supreme Court, and a third – a challenge based on the "sterilisation" of a federally incorporated company – was dismissed. In its judgment on the latter point, the Court effectively rejected the reasoning of the British Columbia Supreme Court in the heavily-criticized case of *British Columbia Power Corp.* v. *A.-G. B.C.* (1963), 47 D.L.R. (2d) 633. It is now clear that federal incorporation by itself will not insulate corporations from otherwise-valid provincial expropriation of their natural resource holdings.

The key to the decision, however, rests in the Court's finding on the fourth contention – that the legislation was directed at affecting extra-provincial property and civil rights. At issue was the conflict between two leading cases: *Royal Bank of Canada* v. *The King* (1913), 9 D.L.R. 337, [1913] A.C. 283 (and a line of cases which followed it) on the one hand, and *Ladore* v. *Bennett,* [1939] 3 D.L.R. 1, [1939] A.C. 468 on the other. In the former case, the Privy Council suggested strongly that provincial statutes affecting extra -provincial rights may be *ultra vires,* regardless of whether the effect is merely incidental. In the latter case, Lord Atkin suggested that as long as in pith and substance the impugned legislation relates to matters within provincial competence, the mere fact that rights outside the province are affected as a necessary incident to the exercise of valid authority will not result in the legislation being struck down. McIntyre J., writing for the Court in *Churchill Falls,* and following the Newfoundland Court of Appeal, as well as the views of many writers on the matter, opted for the *Ladore* v. *Bennett* test – that is, in order to be *ultra vires,* the *Reversion Act* must in pith and substance be directed at extra-provincial rights.

It was in pursuing its inquiry into the matter of the true characterization of the legislation that the Supreme Court parted ways with the Court of Appeal. Central to the former's finding of "colourability" of the legislation was the admission into evidence of a pamphlet, "The Energy Priority of Newfoundland and Labrador". This Newfoundland government publication had been issued in November 1980, immediately prior to the passage of the *Reversion Act,* apparently in an effort to explain Newfoundland's position to the financial community. While the Newfoundland Court of Appeal was prepared to accept such extrinsic evidence to show the *context* in which the Act had been passed, the Supreme Court went further and admitted it as an aid "to ascertain ... its true object and purpose as well" (at 19, D.L.R.). This latter approach had been raised as a possibility by Dickson J. in *Reference re Residential Tenancies Act* (1981), 123 D.L.R. (3d) 554, [1981] 1 S.C.R. 714, and was pursued with vigour by the Court in *Churchill Falls.*

Indeed, *Churchill Falls* is remarkable as an indication of the weight which the Court is now prepared to give extrinsic evidence. It seems clear, from a reading of the Court's relatively brief discussion of the point, that the pamphlet in question was by far the dominating factor in the finding of colourability. Nor did the Court feel concerned to justify at any length the acceptance of the particular evidence as "not inherently unreliable or offending against public policy" (at 19, D.L.R.). The Court has clearly come a long way from its cautious and hesitant handling of such material in the *Reference re Anti-Inflation Act* (1976), 68 D.L.R. (3d) 452, [1976] 2 S.C.R. 373.

In the end the Court found that, as evidenced by the pamphlet and the history of dealings between Quebec and Newfoundland, the *Reversion Act* was in pith and substance directed at affecting rights under the Power Contract. Because it was concluded (again with remarkably little discussion of the matter) that the rights under the contract were situate in Quebec, the legislation was held *ultra vires* the Province of Newfoundland.

In the result, the Supreme Court has clarified to some extent its position on a number of significant constitutional questions, while leaving others still open to speculation. The over-ruling of the *British Columbia Power Corp.* case and the rejection of the *Royal Bank* test will be welcomed by many writers – and, for that matter, by provincial governments. The Court's continued movement towards a greater enthusiasm for extrinsic evidence may receive a more mixed reception, but represents a direction that is unlikely to soon change, especially as the Court becomes increasingly engaged in Charter cases.

More disappointing, although not surprising, was the Court's failure to address two of the grounds argued before it. Most tantalizing, however, is the question (not asked in this case) of how the Court would have reacted had Newfoundland continued to pursue its rights as lessor, and acted *qua* proprietor rather than *qua* legislator in attempting to retrieve power for its own use. Substantial case authority suggests that such a course of action might have enjoyed greater success before the Court.

J. Owen Saunders

Newfoundland Economic Council Seminar

On November 20, 1984, the Executive Director, Constance Hunt, was one of three featured speakers at a seminar sponsored by the Economic Council of Newfoundland and Labrador in St. John's. The seminar was entitled "Management of Oil and Gas Resources", and her paper dealt with legal and constitutional issues related to the utilization of Alberta's Energy Resources Conservation Board as a model for the Newfoundland offshore. Norm Strom, a member of the ERCB in Calgary, delivered a paper entitled "The Role of the Alberta Energy Resources Conservation Board in the Management of Oil and Gas Resources in Alberta: Possible Lessons for the Newfoundland Case". Arne Nielsen, Chairman of the Canadian Petroleum Association, presented a paper entitled "The Experience of the Oil and Gas Industry re the Alberta Energy Resources Conservation Board and Possible Lessons to be Applied to the Newfoundland Case".

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