

MARCH 1, 2022

Foreign Investment Review in Canada: Top Trends and Developments for 2022

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The past year generated substantial interest in the operation of the *Investment Canada Act* (ICA), especially the national security review process, against the backdrop of changes in government policy that purport to articulate a more expansive view of Canada's national security interests. We expect foreign investment review to remain an issue of public and political concern in 2022, with the prospect of amendments to the ICA regime on the horizon. These include proposed amendments to ICA regulations that would permit – and incentivize – foreign investors to report certain types of investments by non-Canadians that are not otherwise subject to mandatory notification.

As a companion piece to our [annual review](#) of top trends and developments in Canadian competition law, we discuss below what to expect for Canadian foreign investment review under the ICA in the coming year.

A. The Year in Review: Importance of National Security Reviews

On February 2, 2022, the Canadian Ministry of Innovation, Science and Economic Development, which is responsible for the ICA, released its 2020-21 Annual Report on the ICA, covering the period from April 1, 2020, through March 31, 2021.

Given that the Canadian government rarely provides details of specific ICA reviews, including declining to confirm whether a review even took place, the annual reports are indispensable for gaining insight into the workings of the ICA review processes.

The most recent Annual Report is no exception. Most important, it confirms the Canadian government's increased willingness to leverage its statutory tools under the ICA to assess the national security implications of foreign investments. Thus, in 2020-21, despite fewer foreign investments in Canada due to COVID-19-related factors, there were almost as many investments subject either to formal national security review or heightened screening as there were in the four prior reporting years *combined*. As in recent years, investments from China continued to attract a high level of national security scrutiny relative to investments from other countries.

At the same time, and in contrast to the growth in national security reviews under the ICA, data in the Annual Report reveal a sustained decrease in the number of foreign investments reviewed under the ICA's more traditional "net benefit to Canada" process, according to which certain very large investments are assessed for their likely impact on Canadian economic activity.

These developments are discussed in more detail below.

Decline in Net Benefit Reviews

The ICA's net benefit review process obliges a foreign investor to apply for government approval for any acquisition of control of a Canadian business that exceeds certain thresholds. If those thresholds are not exceeded, the investor's only obligation is to advise the government of the transaction by filing a "notification" at any time up to 30 days after closing. Similar notification obligations apply when a foreign investor establishes a new business in Canada.

In 2020-21, foreign investors submitted 826 filings under the ICA for acquisitions of control of Canadian businesses that were not Canadian "cultural" businesses; this number was 20% less than the 1,032 filings submitted in 2019-20. The Annual Report identifies COVID-19 as the primary reason for the decline in foreign investment in Canada. This is consistent with statistics maintained by the

Organisation for Economic Co-operation and Development (OECD), which indicate an approximately 50% reduction in foreign direct investment for Canada and the OECD countries in 2020 compared with 2019.

Of the 826 filings, 823 were notifications, down 19.6% from the 1,023 notifications filed in 2019-20, and only three were applications for net benefit review and approval. The three applications for review were down from nine in each of the previous three fiscal years, and much lower than the 22 applications in 2016-17. Indeed, 2020-21 saw the fewest applications for net benefit review since the first Annual Report was published in 2010-11. This continues a material downward trend in applications for review since the financial thresholds for such reviews were significantly increased starting in 2009 (see our previous [analysis](#) of this trend).

Despite the dramatic decrease in net benefit filings, the median review period for net benefit reviews in 2020-21 was 77 days, up slightly from 76 days in 2019-20 and 64 days in 2018-19.

The United States continues to be the primary source of reported investments subject to the ICA's net benefit review regime, accounting for 54.2% of all investments, up from 47% the year before. The European Union was in second place, collectively making 146 investments in 2020-21, down from 164 the previous year. The United Kingdom fell to third place from second place the previous year, with 61 investments in 2020-21 compared with 184 investments the year before; however, this was more in line with 2018-19, when it accounted for 74 investments. The number of Chinese investments remained stable, with 42 in 2020-21, compared with 41 in 2019-20 and 36 in 2018-19.

Increase in National Security Reviews

Under the ICA's national security review regime, the Canadian government can review all foreign investments – regardless of value – to determine if they could be “injurious” to Canadian national security. If the government identifies national security issues, it may prohibit the investment from proceeding, order the Canadian business to be divested (if closing has already occurred) or permit the investment to proceed with conditions that the investor must agree to (or abandon the transaction).

In contrast to the decline in net benefit reviews, national security reviews under the ICA increased to new highs in 2020-21, with 23 notices sent to non-Canadians informing them of a potential national security review. This number set a new record by a substantial margin and was almost the same number as had been issued in the four previous years combined. In addition, one other investment proceeded straight to a formal national security review.

Eleven of these 24 investments were subject to a formal national security review (12 did not proceed to formal review and one was withdrawn by the investor). This number represents a notable increase compared with the seven reviews initiated in the previous year, and constitutes more than one-third of the 32 national security reviews commenced over the past five years. The reviews also took a substantial period of time to complete, averaging 225 days across the 11 investments.

Of the 11 investments that were subject to formal review, four were allowed to proceed at the completion of the review with no remedies required, and sanctions were imposed in three cases. In the remaining four cases, investors abandoned their transactions after the formal reviews were initiated. In the three cases involving sanctions, one investor was prohibited from proceeding with the investment, and the other two were required to wind up or divest their investments.

Broader National Security Mandate

The increase in the number of transactions subject to a formal national security review process is likely at least partly attributable to the government's decision to expand the scope of potential national security concerns, largely as a result of the COVID-19 pandemic. This policy was articulated in the federal guidance released in April 2020 and in the updated Guidelines on the National Security Review of Investments (revised in March 2021). For example, pandemic-related concerns have caused the government to scrutinize more closely investments relating to public health and the supply of critical goods and services. The government's policy is now to subject all investments by foreign states or foreign state-owned enterprises (SOEs) to “enhanced scrutiny” for national security concerns, regardless of investment value. Other newly identified areas of scrutiny include transactions involving “critical minerals” and access to the private data of Canadians.

The government's broader focus is reflected in the investments that were subject to a formal national security review in 2020-21: one involved the metal ore mining industry (which was blocked) and three involved pharmaceutical manufacturing, scientific research or medical and diagnostic laboratories (one was permitted to proceed and two were withdrawn). Five of the investments related to software, computer systems or other telecommunications, a more "traditional" area of national security concern (three were permitted to proceed and two were required to wind up or divest); two other investments involved road construction and financial transaction processing (both were withdrawn).

China Still a Focal Point of National Security Review

The Annual Report also confirms that the jurisdiction of the investor remains a key factor in determining whether a transaction may be subject to national security review. Chinese investments accounted for seven of the 11 investments subjected to a formal national security review in 2020-21; one investment was blocked and one required divestiture. This is no surprise because Chinese investments have constituted a majority of the investments subjected to formal national security reviews in four of the past five years. The other countries of origin subject to formal reviews in 2020-21 were Taiwan, Russia, the United Kingdom and the United Arab Emirates (which involved the other transaction requiring a divestiture).

While the Annual Report does not identify the parties to transactions subjected to national security review, at least some of the China-related transactions may be gleaned from the public record. The single blocked transaction is likely the proposed acquisition by Shandong Gold Mining Co., Ltd., of TMAC Resources Inc., which the Canadian government prohibited in December 2020 (see a more detailed [analysis of the TMAC transaction](#)). Similarly, the Chinese investment that was required to be wound up or divested was likely China Mobile International (Canada) Inc., which did not file its notification under the ICA until October 2020, approximately four years after the statutory deadline, and was ordered to divest or wind up its Canadian operations in 2021 (see a more detailed [analysis of the China Mobile decision](#)).

B. The Year Ahead: Potential Amendments to the ICA Regime?

Continued Focus on National Security

We expect foreign investment review issues, especially as they relate to national security reviews, to continue to attract public and government attention in 2022. This focus is inevitable as the Canadian government continues to search for the proper balance between encouraging foreign investment in Canada and guarding against national security risks, especially insofar as China is concerned.

This issue has come to the fore in the ongoing debate over the Canadian government's decision not to initiate a formal national security review in connection with the acquisition of Neo Lithium Corp. by Zijin Mining Group Co., a Chinese SOE. The opposition parties in Canada's Parliament and some national security experts criticized the government's decision, and parliamentary hearings are currently investigating the matter further. According to the government, however, a proper and complete review was conducted, ultimately concluding that the transaction would not be injurious to Canadian national security and that a formal national security review was not required. The government appears to have reached this conclusion because, among other things, Neo Lithium's assets are located in South America and the type of lithium produced by Neo Lithium is of relatively lesser strategic importance than other types of lithium.

Standing Committee's Recommended Amendments

The Neo Lithium controversy amply demonstrates the ongoing debate over how vigorously the ICA's national security review process should be applied. Given the scrutiny and attention this case has received, it may also bolster existing calls to amend the ICA and enhance enforcement, particularly as it relates to national security matters.

In March 2021, for example, the House of Commons Standing Committee on Industry and Technology (INDU Committee) made several recommendations for amending the ICA, including the following:

1. The review thresholds for all investments by SOEs should be reduced to \$0, so that all such transactions are subject to the ICA's net benefit review and national security review regimes.

2. The ICA should be used to protect strategic sectors, including health, pharmaceuticals, agri-food, manufacturing, natural resources, and intangibles related to innovation, intellectual property, data and “expertise.”
3. Any Canadian business or entity holding a “sensitive asset” should be required to notify the federal government 30 days before implementing the transfer of that asset to a non-Canadian entity.
4. The government should be required to explain the factors for decisions made under the ICA, and to make public any undertakings or conditions imposed on foreign investors as the basis for the approval of transactions.

These proposals do not have the force of law, nor have they been incorporated into the revised ICA guidelines. They do, however, demonstrate a willingness among MPs to consider more aggressive reforms to the ICA in the future.

Task Force on Economic-Based Threats to National Security

In addition to the INDU Committee’s efforts, a federal government task force is currently leading an interdepartmental policy review examining whether additional measures are needed to ensure Canada’s continued ability to respond to economic-based threats to national security. Specific concerns include the loss of sensitive goods, technology and intellectual property; the malicious use of sensitive personal information of Canadians; and compromised critical infrastructure.

Among the issues the task force is exploring is whether the ICA should be amended, with a focus on three principal questions:

1. Should the ICA’s procedures be amended to expand the scope of transactions that are subject to mandatory pre-closing review?
2. Are mitigation measures (e.g., undertakings) that permit a transaction to proceed subject to conditions effective in dealing with potential national security concerns?
3. Should the penalties for non-compliance with the ICA be increased?

A public report that summarizes the input received by the task force is expected to be released by May 2022.

Mandate Letter to Responsible Minister

The impetus for reforming the ICA was given a further boost recently when Prime Minister Justin Trudeau’s latest ministerial mandate letter to Minister of Innovation, Science and Industry François-Philippe Champagne, who is responsible for administering the ICA, directed the Minister to “contribute to broader efforts to promote economic security and combat foreign interference by reviewing and modernizing the *Investment Canada Act* to strengthen the national security review process and better identify and mitigate economic security threats from foreign investment.” It is certainly possible that the Minister will take steps in 2022 to turn these high-level directions into concrete changes to the ICA.

Proposed Regulations to Permit Certain ICA Filings and Extend Time to Review Non-Notified Investments

In the interim, the government has proposed more modest amendments to ICA regulations that would allow investors to obtain pre-closing comfort for certain foreign investments, such as minority acquisitions, that do not require an application or a notification to be filed under the ICA’s net benefit regime.

The national security review process does not currently contemplate notifications where a net benefit filing does not have to be made – for example, in certain minority acquisitions. The government can initiate a formal national security review of such a transaction within 45 days of its implementation. Investors can informally contact the government to discuss such transactions pre-closing, but cannot obtain formal pre-closing comfort that they will not face a national security review until the expiry of the 45-day period following closing. Under the proposed amendments, investors could submit prescribed information before closing and if no issues are raised within 45 days of such filing, proceed with the assurance that the investment will not be challenged post-closing. Currently, if a non-notifiable investment

does not come to the attention of the government until after the 45-day period is expired, a formal national security review is not available for that investment.

However, the government's latest proposal addresses that scenario by providing that transactions where the investor does not file a notification, either pre- or post-closing, will be subject to a potential national security review for up to *five years* following closing. That is a dramatic increase from the current 45-day limit. In other words, if the amendments are adopted, foreign investors that may otherwise have elected not to advise the government of a transaction would now be faced with the choice of either providing notice "voluntarily" or accepting the risk of a possible national security review for five years. The government's objective seems to be to increase the reporting of transactions that might be of national security concern and that otherwise would have escaped its attention.

C. Implications

More National Security Reviews, But Perspective Needed

In 2020-21 a record number of investments received initial notices under the national security review process, and a record number of investments were then subjected to full formal reviews. That said, it is necessary to place this in perspective. Most important, only a tiny percentage of transactions that are within the scope of the ICA ever undergo formal national security review. In the last year, for example, only 11 out of the 826 transactions (1.3%) for which ICA filings were made went to a full formal national security review. Moreover, of these 11 transactions, four were permitted to proceed with no remedies required, meaning that even the commencement of a full national security review does not necessarily spell the inevitable demise of the transaction.

Canada's Balancing Act with Chinese Investments

Even in the case of Chinese investments, a national security review would not necessarily lead to their prohibition. Of the 42 Chinese investments for which ICA filings were made in 2020-21, only two (less than 5%) were ultimately prohibited or ordered to be unwound. This was the case even though, in its court filings in the China Mobile divestment proceedings, the federal government made the seemingly unequivocal statement that the government of China is "a foreign entity posing a strategic threat to Canada and carrying out activities detrimental to the national security and economic prosperity of Canada and other likeminded countries."

Careful Planning Required

In sum, the question of how vigorously the ICA national security review process will be applied remains unsettled and will be decided on a case-by-case basis. Therefore, potential foreign investors in Canada must continue to be diligent in assessing the potential implications of the ICA as part of their transaction planning. Future developments, including potential amendments to the ICA regime, will also need to be factored into the analysis.

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