

# Canada

MARCELA B. STRAS, NEVEN F. STIPANOVIC, JOHN W. BOSCARIOL,  
ORLANDO E. SILVA, JUSTIN VINEBERG AND MARK KATZ\*

## I. Introduction

The Conservative Party won Canada's federal elections in January 2006 for the first time in twelve years.<sup>1</sup> Stephen Harper was sworn in as the twenty-second Prime Minister of Canada on February 6, 2006, succeeding Liberal Party leader Paul Martin. Shortly after taking office, on April 27, 2006, Prime Minister Harper announced agreement on the basic terms of a Softwood Lumber Agreement (SLA or the Agreement) with the United States, which was signed on September 12, 2006 and entered into force on October 12, 2006. This article will review the developments behind the Agreement. In addition, the article will review new developments in foreign investment law, proposed amendments to The Proceeds of Crime (Money Laundering) and Terrorist Financing Act, amendments to the Ontario Securities Act, and recent Supreme Court decisions.

## II. Canada – U.S. Softwood Lumber Agreement

Canada and the United States signed the SLA on September 12, 2006.<sup>2</sup> Following substantial amendments, the Agreement entered into force on October 12, 2006.<sup>3</sup> It remains unclear, however, whether the SLA is the final chapter in a dispute that has lasted over twenty-five years.<sup>4</sup>

---

\* Marcela B. Stras, Partner, Baker & Hostetler LLP and Vice Chair of the Canada Committee; Neven F. Stipanovic, Associate, Baker & Hostetler LLP; John W. Boscariol, Partner, and Orlando E. Silva, Associate, McCarthy Tétrault LLP, Toronto, Canada (2006 Developments in Canadian Bilateral Investment Treaties and Disputes); Justin Vineberg, Partner (Supreme Court Trademark Decisions) and Mark Katz, Partner (Investment Canada Act), Davies, Ward, Phillips & Vineberg LLP, Montreal & Toronto, Canada, respectively.

1. The new government has a minority position in the House of Commons with 125 seats to the Liberals' 102.

2. See Softwood Lumber Agreement, U.S.-Can., Sept. 12, 2006, 35 I.L.M. 1195 [hereinafter Agreement].

3. See Agreement Between The Government of Canada And The Government of The United States of America Amending The Softwood Lumber Agreement Between The Government of Canada And The Government of The United States of America Done At Ottawa On 12 September 2006, U.S.-Can., Oct. 12, 2006 [hereinafter Amended Agreement].

4. The current dispute dates back to 1982, when the U.S. lumber industry initially petitioned the U.S. Government for imposition of countervailing duties against imports of Canadian softwood lumber.

Canada and the United States previously signed an agreement in 1996 governing the importation of softwood lumber from Canada.<sup>5</sup> That agreement expired on March 31, 2001. The following business day, the U.S. lumber industry filed a petition with the U.S. Department of Commerce (Commerce) and the U.S. International Trade Commission (ITC), alleging it was materially injured by dumped and subsidized imports of Canadian softwood lumber.<sup>6</sup> On May 22, 2002, Commerce imposed antidumping (AD) and countervailing duties (CVD) on imports of softwood lumber from Canada.<sup>7</sup> From the Canadian perspective the duties were protectionist and unlawful measures, improperly requiring its exporters to deposit millions of dollars each day with the U.S. Bureau of Customs and Border Protection (U.S. Customs). Canadian industry requested reviews of the U.S. agency determinations by North American Free Trade Agreement (NAFTA) binational panels and U.S. federal courts, while the Canadian Government challenged the actions under the World Trade Organization's (WTO) dispute settlement system. By the end of 2006, most of the pending cases either were concluded or near resolution.

#### A. LEGAL DEVELOPMENTS IN 2006

Decisions in two cases in March and April of 2006 precipitated the announcement of the Agreement. In March 2006, a NAFTA binational panel's unanimous ruling appeared to settle in Canada's favor the issue of whether the Canadian softwood lumber industry was being unfairly subsidized by Canadian provincial governments. In its original investigation in 2001-02, Commerce found that the Canadian lumber industry was unfairly subsidized and imposed a CVD order on imports of Canadian softwood lumber.<sup>8</sup> Subsequently, however, a NAFTA panel formed to review the Commerce determination found that Commerce had not properly calculated the subsidy rate in its original investigation and remanded the case for reconsideration. This sequence was repeated five times. Each time, on remand, Commerce recalculated the subsidy rate but still found that the Canadian lumber industry was unfairly subsidized. After the fifth remand, however, Commerce finally determined that the Canadian subsidy rate on softwood lumber was sufficiently low so as to be *de minimis*, a rate which Commerce must disregard in making a CVD determination.<sup>9</sup> In March 2006, the NAFTA panel upheld Commerce's determination.<sup>10</sup>

On April 7, 2006, the U.S. Court of International Trade (CIT) ruled that U.S. Customs violated the NAFTA Implementation Act in applying the Continued Dumping and Subsidy Offset Act of 2000, commonly referred to as the Byrd Amendment, to AD and CVD

5. See *Canadian Exports of Softwood Lumber*, 61 Fed. Reg. 28,626 (June 5, 1996).

6. See Notice of Initiation of Antidumping Duty Investigation: Certain Softwood Lumber Products from Canada, 66 Fed. Reg. 21,328, 21,331 (Apr. 30, 2001).

7. See *Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 36,068-70 (May 22, 2002) (providing notice of amended final determination of sales at less than fair value, of antidumping duty order, and of amended final affirmative countervailing duty determination and notice of countervailing duty order).

8. *Id.* at 36,069.

9. See 19 U.S.C.S. §§ 1671b(b)(4)(A), 1671d(a)(3). If Commerce in its investigation determines that a countervailable subsidy is not being provided, it must terminate the investigation. See 19 U.S.C.S. § 1671d(g)(2).

10. See *Certain Softwood Lumber Products From Canada, Final Affirmative Countervailing Duty Determination, USA-CDA-2002-1904-03* (Mar. 17, 2006) (Fifth Remand Determination).

duties on goods from Canada and Mexico.<sup>11</sup> The Byrd Amendment directs U.S. Customs to distribute collected AD and CVD duties to affected domestic producers that supported the petition for the investigation. By finding that the NAFTA Implementation Act forbade application of the Byrd Amendment to Canadian goods, the CIT effectively ruled that the U.S. lumber industry would not be entitled to any of the more than \$5 billion in duties collected on imports of softwood lumber from Canada since May 2002. The basic terms of the SLA were announced shortly after this decision on April 27, 2006.

However, the litigation continued. On July 21, 2006, the CIT issued a decision in *Tembec v. United States*,<sup>12</sup> which found unlawful the U.S. Government's amendment of the AD and CVD orders to base them on an ITC affirmative Section 129 determination.<sup>13</sup> That latter determination was made by the ITC under Section 129 of the Uruguay Rounds Agreements Act,<sup>14</sup> purportedly to bring the United States into compliance with a prior adverse WTO panel decision.<sup>15</sup> The U.S. Government used that attempted amendment to keep the AD and CVD orders in place notwithstanding the negative ITC determination on remand in 2004 that resulted from the appeal of the original case to a NAFTA panel.<sup>16</sup> On October 13, 2006, one day after the SLA went into effect, the CIT issued its remedy decision and final judgment in *Tembec v. United States* ordering the U.S. Government to refund all cash deposits collected since the imposition of the AD and CVD orders in 2002.<sup>17</sup> The CIT expressly rejected the U.S. Government's argument that

11. See *Canadian Lumber Trade Alliance v. United States*, 425 F. Supp. 2d 1321 (Ct. Int'l Trade 2006). To bring U.S. law into conformity with its WTO obligations, the U.S. Congress enacted legislation to terminate the distribution under the Byrd Amendment of AD and CVD duties on merchandise that enters the United States after September 30, 2007. See 19 U.S.C. § 1675c, *repealed by* Deficit and Reduction Act of 2005, Pub. L. No. 109-171, § 7601.

12. See *Tembec, Inc. v. United States*, 441 F. Supp. 2d 1302 (Ct. Int'l Trade 2006). In the original investigation, the ITC found no present injury to the U.S. industry. See *Softwood Lumber from Canada (Final)*, USITC Pub. 3740, Inv. Nos. 701-TA-414, 731-TA-928 (Nov. 24, 2004).

13. See *Softwood Lumber from Canada*, *supra* note 12.

14. See *Uruguay Round Agreements Act*, Pub. L. No. 103-465, § 129, 108 Stat. 4809, 4836-39 (1994), codified at 19 U.S.C. § 3538 (2000).

15. See Panel Report, *United States—Investigation of the International Trade Commission in Softwood Lumber from Canada*, WT/DS277/R (Mar. 22, 2004). The WTO panel found that the United States complied with its decision; however the WTO Appellate Body reversed. See Appellate Body Report, *United States—Investigation of the International Trade Commission in Softwood Lumber from Canada*, WT/DS277/AB/RW (May 9, 2006).

16. See *Softwood Lumber from Canada*, USITC Pub. 3815, Inv. Nos. 701-TA-414, 731-TA-928 (Sept. 10, 2004) (Negative Remand Determination). The NAFTA panel affirmed the Negative Remand Determination and the Extraordinary Challenge Committee (ECC) dismissed the U.S. challenge to the NAFTA panel's decision. See *Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 69,584-85 (Nov. 30, 2004); In the Matter of Certain Softwood Lumber Prods. from Canada, ECC-2004-1904-01-USA, Opinion and Order of the ECC (Aug. 10, 2005).

17. See *Tembec, Inc. v. United States*, No. 05-00028, slip op. 06-152 (Ct. Int'l Trade Oct. 13, 2006). The U.S. Government moved for reconsideration and to vacate the final judgment claiming the case was moot, due to the SLA, when the final judgment was entered on October 13, 2006. See *Motion for Reconsideration and to Vacate*, filed by the U.S. Government on Nov. 13, 2006. The Canadian industry, the Government of Canada and the four largest provinces opposed that motion arguing that the final judgment resolved a live case and controversy that still existed on October 13, 2006. See, e.g., *Opposition to Motion for Reconsideration and to Vacate*, filed by the Government of Canada et al., on November 25, 2006. The court denied the U.S. motion for reconsideration and to vacate on February 28, 2007. See *Tembec Inc. v. United States*, No. 05-00028, slip op. 07-28 (Ct. Int'l Trade Feb. 28, 2007). The Court vacated its judgment as no longer necessary, but expressly left its decision in place. *Id.*

NAFTA panel decisions have prospective effect only. Consequently, all of the illegally collected cash deposits had to be returned and not just those made after the effective date of the final NAFTA panel decision in November 2004.

## B. THE AGREEMENT

The United States agreed to revoke the AD and CVD orders and refund all cash deposits collected since May 2002; Canada agreed to distribute \$1 billion to U.S. interests, including \$500 million to the petitioning U.S. industry.<sup>18</sup> The net return to the Canadian industry is approximately \$4.4 billion out of the \$5.4 billion in duties deposited with U.S. Customs since 2002. The Agreement guarantees that, with certain exceptions, no new trade cases will be filed for at least three years, which is one year after the earliest time when the Agreement can be terminated.<sup>19</sup>

Canada also agreed to implement an export tax of up to 22.5 percent in place of the current U.S. import duty of 10.7 percent; the export tax would kick in when the price of lumber falls below \$355 per thousand board feet.<sup>20</sup> The SLA also permits the Canadian regions to elect a volume constraint that would lower the export tax.<sup>21</sup>

The terms of the SLA, signed on September 12, 2006, required the support of companies accounting for 95 percent of all cash deposits on import entries of Canadian softwood lumber and the termination of all ongoing litigation.<sup>22</sup> The implementation initially was delayed from October 1, 2006, to November 1, 2006, as the Canadian Government did not appear to have sufficient support from its industry.<sup>23</sup> Behind the scenes, however, the two governments secretly amended the SLA to eliminate those pre-conditions and implemented the Agreement on October 12, 2006.<sup>24</sup>

18. See Agreement, *supra* note 2, at arts. III (revocation), IV (refund) (\$500 million was earmarked for the U.S. Coalition for Fair Lumber Imports (the petitioners), \$450 million to fund “meritorious initiatives,” and \$50 million for a new binational industry council). The U.S. Trade Representative announced that “meritorious initiatives” money will go to Habitat for Humanity, the American Forest Foundation, and a newly created U.S. Endowment for Forestry and Communities. See Peter Morton, *Softwood Pact to Benefit Select Charities: US\$450-million Fund*, FINANCIAL POST, Oct. 14, 2006.

19. See Agreement, *supra* note 2, at art. XX.

20. *Id.* at art. VII. At a price of \$355 or above, the export tax does not apply. As the price drops, the tax escalates up to the maximum of 15%, which is applied at a price of \$315 or lower. *Id.* The cash price of lumber on October 12, 2006, ranged between \$250 and \$252 per thousand board feet. See Allan Dowd, *Canada Says Trade Deal Not to Blame for Lumber Woe*, REUTERS NEWS, Oct. 12, 2006. Consequently, at the time of implementation of the SLA, Canadian exporters were required to pay the maximum 15% tax. However, the Agreement provides for an additional surcharge of 50% of the export tax to be applied on a retroactive basis should the volume of exports from the relevant region exceed specific levels based on monthly U.S. consumption for the prior year. See Agreement, *supra* note 2, at art. VIII.

21. See Agreement, *supra* note 2, at art. VII. For example, when the price of lumber is below \$315 the export tax is 5%—as opposed to 15% with no volume restraint—but the maximum volume that can be exported to the United States from that region is that region’s pro rata share of 30% of expected U.S. consumption for the month. The regions for purposes of the Agreement are the British Columbia Coast, the British Columbia Interior, Alberta, Saskatchewan, Manitoba, Ontario, and Quebec.

22. See Agreement, *supra* note 2, at art. II & Annex 2A.

23. See, e.g., *Softwood Lumber Pact Snagged on a Catch-22: The Deadline is Three Days Away; The Parties Are Hung up on Faith, Money and Litigation. Odds on Success Are Between Remote and Zero*, THE VANCOUVER SUN, Sept. 28, 2006.

24. See Amended Agreement, *supra* note 3, at arts. I, III, Annex 2A.

Upon its announcement in April 2006, the Agreement was opposed by the Liberal Party and many members of the Canadian lumber industry.<sup>25</sup> The conservative government needed the support of the Bloc Quebecois (Bloc) to obtain temporary approval of the SLA in the Canadian Parliament. The Bloc, with fifty-one votes in the House of Commons, accepted the deal in September 2006,<sup>26</sup> assuring the passage of the Ways and Means Motion that procedurally allowed the SLA's export tax to be implemented temporarily pending a vote in the Parliament.<sup>27</sup> The SLA was formally approved by both chambers of the Parliament and received Royal Assent on December 14, 2006.

### III. Investment Canada Act

#### A. XSTRATA/FALCONBRIDGE

Most non-Canadian companies considering acquisitions in Canada are aware that their transactions may be subject to the notification and substantive review provisions of the Competition Act. However, it often comes as a rude surprise to foreign acquirers that they may also have to contend with the Investment Canada Act (ICA), Canada's foreign investment review legislation.<sup>28</sup>

Where the statutory thresholds are met, the ICA requires non-Canadians acquiring Canadian businesses to obtain pre-closing approval from Canada's Minister of Industry or, if the transaction involves the acquisition of a "cultural" business, from the Minister of Canadian Heritage.<sup>29</sup>

Reviewable investments are assessed by the responsible Minister to determine if they are of "net benefit" to Canada.<sup>30</sup> Although transactions are rarely denied approval, the time required to complete the ICA process may become an issue where pre-closing ap-

25. See, e.g., Steve Mertl, *Softwood Deals Set to Go Oct. 12*, THE GLOBE AND MAIL, Oct. 6, 2006.

26. See INSIDE U.S. TRADE, Sept. 15, 2006, Aug. 18, 2006.

27. THE GLOBE AND MAIL, Sept. 11, 2006. The Ways and Means Motion (Bill C-24) implements the Canadian export tax as directed by the SLA.

28. Investment Canada Act, R.S.C., ch. 28 (1985) (1st Supp.), available at <http://laws.justice.gc.ca/en/I-21.8/>.

29. *Id.* §§ 14-14.1. The ICA's thresholds for review are largely based on the value of the assets of the Canadian business being acquired and will vary depending on whether: (i) the acquiror or the vendor qualifies as a "WTO Investor" under the ICA (i.e., is controlled by citizens of WTO member countries); (ii) the acquisition of control of the Canadian business is direct or indirect (the latter involving the acquisition of a foreign corporation with a Canadian subsidiary); and (iii) the Canadian business is engaged in certain prescribed industries (cultural businesses, transportation services, financial services or uranium mining). Thus, the direct acquisition of a Canadian business by or from a WTO investor will be subject to review if the assets of the Canadian business exceed \$265 million (Cdn.) in value (this is the threshold for 2006; it is adjusted annually). On the other hand, indirect acquisitions involving WTO investors are not reviewable. The thresholds are much lower if non-WTO investors or the prescribed industries referred to above are involved: \$5 million for direct investments and \$50 million for indirect investments (these thresholds do not change annually). In some circumstances, investments in cultural businesses can be reviewable even if they fall below these thresholds.

30. *Id.* § 16. The ICA sets out a series of criteria which the Minister may consider in making the "net benefit" determination, including: the effect of the investment on the level and nature of economic activity and employment in Canada; the degree and significance of participation by Canadians in the Canadian business; the compatibility of the investment with national industrial, economic and cultural policies; the contribution of the investment to Canada's ability to compete in world markets; and the effect of the investment on competition. See *id.* § 20.

proval is required (there is an initial review period of forty-five days, but this may be extended in more complex cases). Moreover, it has become common practice for the responsible Minister to extract “undertakings” from foreign investors as a condition of approval. These undertakings can be extensive and costly. Typically, they involve, among other things, commitments to retain a certain level of employment in relation to the Canadian business, to continue to locate corporate offices in Canada, to guarantee participation of Canadians as directors or in management, and to make capital and other investment expenditures in Canada. Foreign investors also may be required to add Canadians to their own board of directors and to maintain or to establish a listing on Canadian stock exchanges.

The year 2006 witnessed one of the most extensive ICA reviews undertaken to date, involving the proposed acquisition by Xstrata plc (Xstrata) of Falconbridge Limited (Falconbridge). Xstrata is a global natural resources group based in Switzerland;<sup>31</sup> Falconbridge was a Canadian-based mining company with worldwide operations in nickel, copper, zinc, and aluminum production.<sup>32</sup>

Apart from the sheer size of the transaction (the largest successful all-cash offer in Canadian history),<sup>33</sup> and the involvement of a sensitive Canadian resource sector, the situation was complicated by the fact that Xstrata’s bid for Falconbridge was both unsolicited and competed against an alternative friendly offer by Canadian-based Inco Limited (Inco).<sup>34</sup> This created an unusual level of political and public interest in the transaction, given that it pitted a potential foreign takeover against a made-in-Canada solution.

Because Inco is a Canadian company, its offer for Falconbridge did not have to secure ICA approval. However, Inco had become embroiled in a protracted and difficult review process of its own involving competition authorities in the European Union (EU) and, to a somewhat lesser extent, in the United States.<sup>35</sup> This led to calls in Canada for a “level regulatory playing field” (i.e., that the Minister of Industry should at the very least withhold ICA approval for Xstrata’s bid until Inco received its foreign antitrust approvals so as not to give Xstrata an “unfair” advantage over Inco). Indeed, in an unprecedented step, the Standing Committee on Industry, Science, and Technology of Canada’s House of Commons convened a special meeting at which a unanimous motion to this effect was adopted.<sup>36</sup>

Xstrata ultimately obtained its ICA approval in July 2006, following an extension of the initial forty-five day review period (and also after Inco had received its EU and U.S. antitrust clearances). According to a press release issued by Xstrata at the time, the undertakings it provided to satisfy the net benefit test included the following commitments:

31. See Xstrata plc, *Group Information*, <http://www.xstrata.com/corporate.php>.

32. See Falconbridge Limited, *Corporate Profile*, <http://archive.xstrata.com/falconbridge/>.

33. *Canada: Foreign Investment Drives M&A*, INT’L FIN. L. REV., Dec. 2006, at 1 (“Swiss-based Xstrata finalized its \$21.2 billion takeover of Falconbridge, the largest all-cash offer in Canadian history, after rival Canadian bidder Inco was itself bought by Brazil’s CVRD for \$17 billion.”).

34. Christopher J. Chipello, *Inco Drops Bid for Falconbridge and Clear the Way for Xstrata*, WALL ST. J., July 29, 2006, at A2.

35. Bernard Simon, *Inco Bid Faces EU and US Scrutiny*, FIN. TIMES, Feb. 15, 2006, at 26.

36. CANADA, HOUSE OF COMMONS, STANDING COMMITTEE ON INDUSTRY, SCIENCE AND TECHNOLOGY, EVIDENCE, (Issue No. 6, June 1, 2006), 39th Parl., 1st Session, 2006. OTTAWA: PUBLIC WORKS AND GOVERNMENT SERVICES, 2006, available at <http://cmte.parl.gc.ca/Content/HOC/Committee/391/INDU/Evidence/EV2245507/INDUEV06-E.PDF>.

- establishment of a new standalone global nickel business, headquartered in Toronto, Ontario, with both the CEO and a majority of senior management consisting of Canadians;
- establishment of a new technology research and development unit based in Sudbury, Ontario;
- establishment of new regional head offices for Xstrata's copper and zinc business units, to be located in Toronto, Ontario, with the COO and a majority of senior officers consisting of Canadians;
- establishment in Canada of Xstrata's global headquarters for copper recycling;
- prohibition against layoffs of operating staff for three years at any of Falconbridge's operating facilities in Canada;
- increased capital, R&D, and exploration expenditures in Canada;
- identification of a potential Canadian candidate for the position of non-executive director of Xstrata; and
- funding for community and social initiatives in Canada, with a particular focus on supporting aboriginal communities.<sup>37</sup>

Three days after Xstrata received ICA approval, Inco announced that it had allowed its bid for Falconbridge to expire.<sup>38</sup> Xstrata subsequently acquired control of Falconbridge in mid-August, 2006.<sup>39</sup>

#### B. THE "HOLLOWING OUT" OF CORPORATE CANADA—MYTH OR REALITY?

One of the arguments raised by opponents of Xstrata's takeover of Falconbridge was that the acquisition would contribute to the hollowing out of the Canadian corporate sector. This is a long-standing objection to foreign acquisitions of Canadian businesses. Proponents of this view argue that foreign takeovers lead to the elimination of Canadian head offices, resulting in a direct loss of head office employment—particularly senior management functions—as well as a reduction in demand for ancillary financial, legal and other services.

A study released by Statistics Canada in July 2006, however, found that these concerns may not be valid.<sup>40</sup> Looking at the data for the years 1999 to 2005, the study reported that foreign takeovers have not had a negative impact on employment in Canadian head offices. Instead, more head offices were actually created than were closed as a result of foreign takeovers, and there was a net increase in levels of head office employment.<sup>41</sup> By

37. See Press Release, Xstrata Plc., Xstrata Receives Investment Canada Act Approval (July 25, 2006), available at <http://www.xstrata.com/news/200607251.en.pdf>.

38. See Press Release, Inco Ltd., Inco's Offer for Falconbridge Expires; Focus Shifts to Two-way Combination with Phelps Dodge (July 28, 2006), available at [http://www.inco.com/newscentre/newsreleases/default.aspx?posting\\_id=3746](http://www.inco.com/newscentre/newsreleases/default.aspx?posting_id=3746).

39. See Press Release, Xstrata Plc, Xstrata Acquires Additional 67.8% of Falconbridge and Extends Offer to 25 August 2006 (Aug.15, 2006), available at [http://www.xstrata.com/press\\_release.php?id=AC&nb=200608151.en.html](http://www.xstrata.com/press_release.php?id=AC&nb=200608151.en.html).

40. See Desmond Beckstead & W. Mark Brown, *Head Office Employment in Canada, 1999 to 2005*, STATISTICS CANADA, July 13, 2006, available at <http://www.statscan.ca/english/research/11-624-MIE/11-624-MIE2006014.pdf>.

41. *Id.* at 10.

contrast, firms that went from foreign to Canadian control experienced a decline in head office employment.<sup>42</sup>

Indeed, more generally, the report concluded that much of the dynamism in Canada's head office sector is generated by foreign-controlled firms.<sup>43</sup> Thus, between 1999 and 2005, foreign firms accounted for all of the growth in the number of head offices in Canada and the majority of the gains in head office employment.

These findings have important implications for the debate surrounding foreign investment in Canada. The fact that foreign control does not necessarily lead to a reduction in head office employment, or senior management input, appears to undercut at least one argument against restricting foreign investment in Canadian businesses.

### C. POSSIBLE AMENDMENTS?

Not surprisingly, the minority Conservative government currently in power in Canada appears to encourage, rather than discourage, foreign investment. This has led the government to announce that it will undertake a review of the ICA to ensure that it is in line with best practices in other jurisdictions and maximizes the benefits of foreign investment while retaining Canada's ability to protect its national interests.

The government's commitment to review the ICA is set out in a document entitled *Advantage Canada*, which was released by Canada's Department of Finance on November 23, 2006.<sup>44</sup> *Advantage Canada* describes the government's long-term plan for making Canada a "true world economic leader." Based on the tenor of the comments in *Advantage Canada*, it appears that the government's intention is to generally reduce the scope or application of the ICA except in certain circumstances. For example, the plan suggests that one instance in which government intervention may be justified is when a large, state-owned enterprise with noncommercial objectives and unclear corporate governance and reporting procedures attempts to acquire a Canadian business.

This latter point is likely a reference to the concerns that were raised when state-owned China Minmetals Corporation sought to acquire Noranda, Inc. in 2005.<sup>45</sup> The Minmetals transaction did not proceed, but the former Liberal government introduced proposed amendments to the ICA to ensure that the Minister would be able to review (and block) transactions on national security grounds.<sup>46</sup> The Liberals were defeated before these amendments could be passed, but it appears that the minority conservative government now intends to consider similar provisions as part of its ICA review. If adopted, this would put Canada in line with other major trading partners, such as the United States, that also permit the screening of foreign investments for reasons of national security.

42. *Id.* at 11.

43. *Id.* at 15.

44. Press Release, Department of Finance, Canada, Canada's New Government Releases Advantage Canada: An Economic Plan to Eliminate Canada's Net Debt and Further Reduce Taxes, (Nov. 23, 2006), available at <http://www.fin.gc.ca/news06/06-069e.html>.

45. See generally Aaron A. Dhir, *Of Takeovers, Foreign Investment and Human Rights: Unpacking the Noranda-Minmetals Conundrum*, 22 BANKING & FIN. L. REV. 77 (Oct. 2006).

46. Bill C-59, An Act to Amend the Investment Canada Act, 1st Session, 38th Parliament, 2005 (First Reading: June 20, 2005), available at [http://www2.parl.gc.ca/content/hoc/Bills/381/Government/C-59/C-59\\_1/C-59\\_1.PDF](http://www2.parl.gc.ca/content/hoc/Bills/381/Government/C-59/C-59_1/C-59_1.PDF).



#### D. FOREIGN OWNERSHIP RESTRICTIONS IN CANADIAN TELECOM

On March 22, 2006, the government-appointed Telecommunications Policy Review Panel (the Panel) issued its final report on Canada's telecommunications industry.<sup>47</sup> The Panel was formed to assess and provide recommendations with respect to the institutional and regulatory framework governing the Canadian telecom industry.

One of the areas the Panel examined was the issue of foreign investment limits. The Panel concluded that the current limits, including a 20 percent cap on direct foreign ownership of common telecom carriers, are among the most restrictive and inflexible in the OECD.<sup>48</sup> Given the benefits of expanded investment in Canadian telecoms, especially in emerging markets, the Panel recommended replacing Canada's current foreign ownership restrictions with a more flexible public interest test.<sup>49</sup> The new test would assess potential foreign investments based on a variety of factors, including improved competition, better service and innovation, head office location and functions, R&D, employment, public safety, and national security.<sup>50</sup> The Panel also urged that any relaxation of foreign investment rules be applied consistently and in a competitively neutral way to both the telecom and broadcasting industries.<sup>51</sup>

### IV. Canadian Bilateral Investment Treaties and Disputes

A number of developments during 2006 made this a particularly active and significant year for Canadian bilateral investment treaties (BITs) and disputes. Over the last decade, BITs have quickly emerged as a viable option for businesses seeking protection of their investments in foreign jurisdictions. Traditionally, when investment disputes arose, foreign investors were limited to seeking remedies through either the host country's domestic court system or diplomatic claims. The BITs are an attractive alternative because they provide a mechanism to pursue damages claims directly against host states through international arbitration. This is reflected in the phenomenal growth in the negotiation of these agreements worldwide. In 1989, there were less than 400 BITs in force and by the end of 2005, that number increased to approximately 2,500.<sup>52</sup>

#### A. NEW CANADA-PERU BIT

On November 14, 2006, Canada and Peru signed a BIT, otherwise referred to in Canada as a Foreign Investment Protection and Promotion Agreement (FIPA).<sup>53</sup> This is Canada's first BIT to be negotiated in eight years and the first to be based on Canada's new Model FIPA. This will bring the number of BITs Canada has with developing and

47. The Panel's report is available at [http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/report\\_e.pdf/\\$FILE/report\\_e.pdf](http://www.telecomreview.ca/epic/internet/intprp-gecrt.nsf/vwapj/report_e.pdf/$FILE/report_e.pdf).

48. *Id.* at 11-13—11-14.

49. *Id.* at 11-25—11-26.

50. *Id.* at 11-25.

51. *Id.* at 11-26.

52. U.N. Conference on Trade and Development, *Developments in International Investment Agreements in 2005*, IIA Monitor No. 2 (2006), UNCTAD/WEB/ITE/IIA/2006/7.

53. Agreement for the Promotion and Protection of Investments, Nov. 14, 2006, Can.-Peru, available at <http://www.maeci-dfait.gc.ca/tna-nac/documents/Canada-Peru10nov06-en.pdf>.

newly industrialized countries to twenty-three.<sup>54</sup> Canada is currently in the process of active BIT negotiations with Jordan, India, and China. Negotiations with Jordan have just commenced and those with India are near completion. Although negotiations with China have presented challenges, it is expected that they will be concluded in 2007. Exploratory discussions are also in the works with Indonesia, Vietnam and Kuwait and the launching of formal negotiations is expected to follow in the next few months.<sup>55</sup>

The Canada-Peru BIT closely mirrors the 2004 Model FIPA, with a few exceptions, and is comprised of fifty-two articles and fifty pages of reservations and exceptions.<sup>56</sup> It has three core substantive obligations:

- *Nondiscriminatory treatment*: Foreign investors and their investments must be accorded treatment no less favorable than that accorded to domestic investors (national treatment) and investors from any other country (most-favored-nation treatment or MFN treatment);<sup>57</sup>
- *Fair and equitable treatment*: Foreign investments must be accorded fair and equitable treatment in accordance with international law, including full protection and security;<sup>58</sup> and
- *Compensation for expropriation*: Expropriation, or measures equivalent to expropriation, must be for a public purpose, nondiscriminatory, in accordance with due process of law, and accompanied by payment of prompt, adequate, and effective compensation.<sup>59</sup>

Certain obligations contained in the Canada-Peru BIT, however, differ from those contained in other Canadian BITs. These changes arise in at least five key substantive areas of investment protection:

- The scope of protected investments has been narrowed in contrast to the broad and open-ended asset-based definition found in previous BITs; the definition now consists of a closed list of qualified investments and specifically excludes certain assets;<sup>60</sup>
- Reference to the “returns of investors” is absent from the operative provisions of the Canada-Peru BIT, including the provisions concerning fair and equitable treatment, expropriation, national treatment, and MFN treatment; as a result, challenging host government measures which significantly impact returns but not the underlying investment itself could be more difficult;

---

54. Canada has concluded BITs with the following countries (entry into force date): Russia (1989); Poland (1990); Czech Republic (1992); Slovak Republic (1992); Argentina (1993); Hungary (1992); Ukraine (1995); Latvia (1995); the Philippines (1996); Trinidad & Tobago (1996); Barbados (1997); Ecuador (1997); Egypt (1997); Romania (1997); Venezuela (1998); Panama (1998); Thailand (1998); Armenia (1999); Uruguay (1999); Lebanon (1999); Costa Rica (1999); and Croatia (2001).

55. Current information on Canada's regional and bilateral initiatives is available on the website of Foreign Affairs & International Trade Canada, <http://www.international.gc.ca/tma-nac/reg-en.asp>.

56. Canada's existing BITs typically contain less than twenty articles and few reservations and exceptions.

57. Agreement for the Promotion and Protection of Investments, Nov. 14, 2006, Can.-Peru, arts. 3, 4 & Annex B.4.

58. *Id.* at art. 5.

59. *Id.* at art. 13 & Annex B.13(1).

60. *Id.* at art. 1.

- Broad MFN exceptions available to host governments significantly limit the ability of investors to benefit from the host government's MFN obligations, including the potential to benefit from more favorable treaties negotiated by the host with third countries;<sup>61</sup>
- Fair and equitable treatment is limited to treatment accorded to covered investments in accordance with the "customary international law minimum standard of treatment of aliens";<sup>62</sup> although this is an evolving area of the law, host governments have argued that the "customary international law" standard represents a higher threshold for demonstrating breach than the "international law" standard of treatment generally provided for in Canada's existing BITs; and
- Clarifications of what may constitute expropriation, including indirect expropriation, may lead to a tolerance of a wider range of regulatory interference that has the effect of significantly diminishing, but not completely destroying, an investment's value.<sup>63</sup>

The Canada-Peru BIT also modifies and supplements a number of other provisions contained in Canada's existing BITs. These include those dealing with investor-state dispute settlement, prudential measures and financial services, national security, public access to hearings and documents, and participation by non-disputing parties.

As Canada's first BIT in eight years, and as the first to be based on the 2004 Model FIPA, the negotiation of the Canada-Peru BIT represents a watershed moment in the development of Canada's BITs. Arguably, the protections to investors under this treaty have been significantly diluted when compared to Canada's existing BITs. This is likely a reaction by the Canadian government to its role as a respondent in several NAFTA Chapter 11 cases.

## B. FUTURE BIT NEGOTIATIONS

In addition to Jordan, India, China, Indonesia, Vietnam, and Kuwait, Canada has identified the following countries for future BITs: Dominican Republic, Hong Kong, Algeria, Pakistan, Uzbekistan, Mongolia, Paraguay, Morocco, and the United Arab Emirates. The Canadian government is considering streamlining the obligations contained in the Model FIPA and is currently consulting with the Canadian business community.

## C. ENCANACORP. V. REPUBLIC OF ECUADOR

The UNCITRAL Tribunal award in *EnCana Corp. v. Republic of Ecuador*, LCIA Case No. UN3481, February 3, 2006, (Canada-Ecuador BIT) is the first award to be issued in an investor-state dispute brought under a Canadian BIT.<sup>64</sup>

The dispute arose out of a denial by the Ecuadorian tax authorities (*Servicios de Rentas Internas* or SRI) of value-added tax (VAT) refunds to EnCana's subsidiaries incorporated in Barbados and operating in Ecuador under a series of participation contracts entered

61. *Id.* at art. 4 & Annex B.4.

62. *Id.* at art. 5.

63. *Id.* at art. 13 & Annex B.13(1).

64. The award is available at [http://www.investmentclaims.com/decisions/Encana\\_Ecuador\\_Award.pdf](http://www.investmentclaims.com/decisions/Encana_Ecuador_Award.pdf).

into with Petroecuador, the Ecuadorian State oil company, for the exploration and production of oil.<sup>65</sup> Under the contracts, EnCana received a percentage of the oil extracted, called the “participation factor,” depending on the level of output. For a short time, the SRI granted refunds of the VAT paid in connection with the production of oil for export. The SRI then changed its policy and began denying VAT refunds for foreign oil companies for several reasons that included issues of legislative interpretation and a claim that the VAT had already been reimbursed through the participation factor. EnCana’s principal claims before the Tribunal were that Ecuador’s actions breached the expropriation, fair and equitable treatment, and national treatment provisions of the BIT.<sup>66</sup> Upon bringing its BIT claim, proceedings brought by EnCana’s subsidiaries in the Ecuadorian courts were withdrawn.<sup>67</sup>

The Tribunal determined that the claim concerned a tax measure, and, therefore, it only had jurisdiction to consider the expropriation claim.<sup>68</sup> Under the BIT, only the expropriation provision could be applied to a tax measure.<sup>69</sup> In a split decision, the majority of the Tribunal, Professor James Crawford (President), and Christopher Thomas rejected both the direct and indirect expropriation claims. The majority proceeded on the assumption that EnCana’s subsidiaries had a right to VAT refunds under Ecuadorian law but held that this right was not expropriated by Ecuador. In terms of indirect expropriation, the Tribunal held that foreign investors have neither the right nor legitimate expectation that the tax regime will not change and that only in extreme cases will the incidence of a tax measure constitute indirect expropriation.<sup>70</sup>

According to the Tribunal, issues of indirect expropriation arise “only if a tax law is extraordinary, punitive in amount or arbitrary in incidence.”<sup>71</sup> The Tribunal concluded that notwithstanding a certain degree of financial impairment, EnCana’s subsidiaries were able to continue to operate and EnCana was not denied “in whole or in significant part” the benefits of its investment.<sup>72</sup> In terms of direct expropriation, the Tribunal held that in order for an expropriation claim to be made out, the actions of an executive agency, such as a tax authority, must amount to “an actual and effective repudiation of legal rights.”<sup>73</sup> The majority was of the view that an expropriation does not occur until the executive agency has made a “definitive determination contrary to law.”<sup>74</sup>

The dissenting arbitrator found that Ecuador had expropriated EnCana’s returns on investment and that EnCana was entitled to compensation.<sup>75</sup> He criticized the majority for effectively reading in a requirement for the exhaustion of local remedies under the

---

65. *Id.* ¶ 23.

66. *Id.* ¶ 107.

67. *Id.* ¶ 102.

68. *Id.* ¶¶ 147, 149.

69. The Ecuadorian and Canadian tax authorities did not exercise the option available to them under the BIT to jointly veto the expropriation claim.

70. *Id.* ¶ 173.

71. *Id.* ¶ 177.

72. *Id.*

73. *Id.* ¶ 195.

74. *Id.* ¶ 194.

75. The Partial Dissenting Opinion is available at [http://www.investmentclaims.com/decisions/Encana\\_Ecuador\\_Partial\\_Dissent.pdf](http://www.investmentclaims.com/decisions/Encana_Ecuador_Partial_Dissent.pdf).

expropriation provision of the BIT.<sup>76</sup> He further noted that the BIT provides for the opposite in that it “precludes the possibility for the foreign investor to pursue or continue claims regarding measures challenged under the Treaty before the national courts or authorities of the host state.”<sup>77</sup>

Although the governing UNCITRAL Rules provide that in principle the costs of arbitration shall be borne by the unsuccessful party, the Tribunal ordered otherwise, holding that it would be just and equitable for Ecuador to bear the costs of arbitration.<sup>78</sup> Ecuador was ordered to reimburse EnCana for over \$300,000 for the costs of arbitration.<sup>79</sup>

## V. The Proceeds Of Crime (Money Laundering) And Terrorist Financing Act

On October 5, 2006, the Harper government introduced a bill to amend The Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA).<sup>80</sup> The PCMLTFA was passed by the Canadian Parliament in the immediate aftermath of September 11, 2001, with the aim to strengthen the reporting of suspicious transactions by financial intermediaries to the newly created Financial Transactions and Reports Analysis Center of Canada (FINTRAC).<sup>81</sup> The proposed bill now seeks to extend the reach of FINTRAC by enhancing client identification and record-keeping measures for financial institutions and intermediaries, identified as banks, trust and loan companies, life insurance companies, securities dealers and casinos.<sup>82</sup> It would require the covered institutions and intermediaries to: monitor transactions by foreign nationals and members of their immediate families who hold prominent public positions;<sup>83</sup> report attempted suspicious transactions;<sup>84</sup> create a federal registration system for money service businesses and foreign exchange dealers;<sup>85</sup> extend the amount of information FINTRAC can disclose;<sup>86</sup> and expand information sharing between federal departments and agencies.<sup>87</sup>

Significantly, the proposed legislation would remove the requirement in the current law that legal counsel file suspicious transaction reports or other prescribed transaction reports.<sup>88</sup> That requirement has been subject to numerous legal challenges, and the Canadian courts have issued injunctions excluding legal counsel from the application of the act

76. *Id.* ¶ 28.

77. *Id.* ¶ 29.

78. *Id.* at Award, ¶ 202.

79. *Id.* ¶ 203.

80. See Press Release, Department of Finance, Government of Canada, Canada's New Government Toughens Anti-Money Laundering and Anti-Terrorist Financing Regime (Oct. 5, 2006), available at <http://www.news.gc.ca/cfmx/view/en/index.jsp?articleid=244019>. The text of the bill, as introduced in Parliament, is available at <http://www2.parl.gc.ca/HousePublications/Publication.aspx?Docid=2384496&file=4>.

81. See The Proceeds of Crime (Money Laundering) and Terrorist Financing Act, 2001 S.C., ch. 41 (Can.).

82. Bill C-25, An Act to Amend the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and the Income Tax Act and to Make a Consequential Amendment to Another Act (Oct. 5, 2006).

83. *Id.* ¶ 8 (amending PCMLTFA § 9).

84. *Id.* ¶ 5 (amending PCMLTFA § 7).

85. *Id.* ¶ 10 (amending PCMLTFA §11).

86. *Id.* ¶¶ 26, 27 (amending PCMLTFA §§ 55, 56).

87. *Id.*

88. *Id.* ¶ 9 (amending PCMLTFA § 10).

and regulations in several provinces.<sup>89</sup> The courts, however, did not get an opportunity to address the merits of the claims; following the injunctions, the Canadian Government excluded lawyers from the regulations that required them to report suspicious monetary transactions.<sup>90</sup> The proposed amendment to PCMLTFA would now remove this requirement from the statute.

## VI. New Legislation Amending The Ontario Securities Act

On December 31, 2005, amendments to the Ontario Securities Act went into effect, establishing, for the first time in Canada, statutory liability for secondary market disclosure by public companies and its executives.<sup>91</sup> The new law may make it easier for shareholders to sue public companies and their executives for misleading or untrue statements in public documents, and its effect is not limited to companies operating in Ontario. Alberta and Manitoba already have followed Ontario's lead, introducing the same legislation verbatim in 2006. British Columbia is planning to introduce its own version, which in important respects is different from Ontario's law, creating fears of litigation arbitrage across Canada.<sup>92</sup>

The new law extends the statutory liability for misrepresentation found in corporate documents.<sup>93</sup> Previously, misrepresentation would give rise to statutory liability only if found in certain documents, such as an annual report. The new law extends the reach of statutory liability to misrepresentation found in essentially any corporate document—even a press release.<sup>94</sup> The law does, however, distinguish between core and non-core documents in terms of the burden of proof required to succeed on such a claim.<sup>95</sup> If alleged misrepresentation is demonstrated in a core document, for example a prospectus, the defending company would bear the burden of showing it conducted a reasonable investigation to ensure information was accurate.<sup>96</sup> Misrepresentation in a non-core document such as a press release would require a showing that the defendant had knowledge of the misrepresentation.<sup>97</sup> Moreover, the new law does provide some protection against frivolous claims—plaintiffs are required to obtain leave from the court in order to file a claim and there is a cap on the damages.<sup>98</sup>

89. Fed'n of Law Societies of Canada v. Canada, 2002 C.R.D. 81.60.00-03 (court in Nova Scotia granted injunction to legal counsel); Fed'n of Law Societies of Canada v. Canada, 2002 A.C.W.S. LEXIS 2693 (2002) (court in Saskatchewan grants interim relief to legal counsel); Fed'n of Law Societies of Canada v. Canada, 2002 T.L.W.D. LEXIS 20 (Ont. S.C.J. 2002) (Ontario court grants injunction to legal counsel).

90. See Sam Porteous, *Lawyers Must Not Be Exempt from Ottawa's New Anti-Money-Laundering Legislation*, *Says Security Analyst Sam Porteous*, THE GLOBE AND MAIL, Apr. 1, 2003, at A17.

91. These amendments were originally part of an omnibus bill—Keeping the Promise for a Strong Economy Act (Budget Measures), 2002—commonly known as Bill 198. Bill 198 was introduced in Ontario in 2002 and, with certain exceptions, entered into force in April 2003. Keeping the Promise for a Strong Economy Act (Budget Measures), 2002, S.O. 2002, ch. 22 - Bill 198.

92. See Sandra Rubin, *Forum Shopping Fears: Alarm Bells Are Ringing in the Executive Suites of Listed Corporations over B.C.'s Plan to Adopt Its Own Shareholder Class-Action Regime*, FINANCIAL POST, Sept. 20, 2006.

93. See Ontario Securities Act, Pt. XXIII.1.

94. *Id.* § 138.3.

95. *Id.* § 138.4.

96. *Id.* §§ 138.4(6)-(7).

97. *Id.* § 138.4(1).

98. *Id.* §§ 138.7-8.

## VII. Supreme Court Of Canada\*\*

### A. TRADEMARK DECISIONS

On June 2, 2006, the Supreme Court of Canada issued two landmark decisions, one involving an iconic figure of pop culture, Barbie dolls,<sup>99</sup> and the other, the venerable champagne house, Veuve Clicquot Ponsardin.<sup>100</sup> In both cases, the owners of the internationally established trademarks lost. The unanimous decisions upheld the right of “Barbie’s,” a small chain of Montreal-based restaurants, and “Clicquot,” the name used by a group of women’s wear shops in Quebec and Eastern Ontario, to use their names as registered Canadian trademarks.

In the Barbie case, it was contended by Mattel, Inc., the owner of the trademark “Barbie” in association with dolls and accessories, that there was a likelihood that consumers would think that the restaurants had something to do with the dolls, and hence the restaurants should not be permitted to register the name “Barbie” as a Canadian trademark in association with restaurants. In the Veuve Clicquot case, the champagne maker alleged that not only was the registration of the Clicquot trademark by the women’s clothing chain in association with the sale of mid-market women’s clothing confusing with the trademarks held by Veuve Clicquot, but that its use depreciated the goodwill inherent in the Veuve Clicquot brand and trademark.

Both decisions were based principally on findings of fact. In Veuve Clicquot the Supreme Court accepted the trial judge’s findings that ordinary consumers would be unlikely to make any mental link between the trademarks and the respective wares and services of the parties. Veuve Clicquot’s depreciation argument was also dismissed by the court because it did not show that the women’s boutique “made use of marks sufficiently similar to Veuve Clicquot to evoke in a relevant universe of consumers a mental association of the two marks that is likely to depreciate the value of the goodwill attaching to [Veuve Clicquot’s] mark.”<sup>101</sup>

Similarly, in the Barbie case, the restaurant owner had to demonstrate that use of both trademarks in the same geographic area would not create the likelihood of confusion (i.e., mistaken inferences in the marketplace). The court concluded that “although a trademark’s fame is capable of carrying the mark across product lines where lesser marks would be circumscribed to their traditional wares or services,” each situation must be judged in its full factual context.<sup>102</sup> Accordingly, the court ruled that since the “Barbie” trademark had not transcended outside dolls and doll accessories, there was no likelihood of confusion in the marketplace.

---

\*\* The information in this section was previously published on June 7, 2006, under the title, “What Would the Harried Consumer Think—Supreme Court Landmark Trade-mark Decisions,” at the Davies, Ward, Phillips & Vineberg LLP website, [www.dwpv.com](http://www.dwpv.com).

99. *Mattel, Inc. v. 3894207 Canada Inc.*, [2006] 2006 A.C.W.S.J. LEXIS 2678.

100. *Veuve Clicquot Ponsardin Maison Fondée en 1772 v. Boutiques Clicquot Ltée.*, [2006] 2006 A.C.W.S.J. LEXIS 2677.

101. *Veuve Clicquot*, [2006] 2006 A.C.W.S.J. LEXIS 2677.

102. *Mattel*, [2006] 2006 A.C.W.S.J. LEXIS 2678.

