NORTH AMERICA

Recent legal changes affecting Canadian M&A

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IN THE LAST 18 months, a number of significant legislative changes have altered the Canadian M&A landscape for foreign investors. The changes generally improve Canada's attractiveness to foreign investment and this article addresses two areas of relevance to any entity assessing Canadian investments or acquisitions: tax law and competition law.

Tax law

When non-residents dispose of 'taxable Canadian property' (TCP) (as defined in the Income Tax Act (Canada)), they must comply with section 116 of such Act. This section requires that the purchaser withhold a minimum of 25 percent of the purchase price unless each seller obtains a clearance certificate (indicating that any taxes have been paid or acceptable security has been delivered) from the Canada Revenue Agency. Since many of Canada's international tax treaties provide that sales of certain types of TCP by foreign vendors are exempt from Canadian tax, section 116 often resulted in an unnecessary delay in full payment of the purchase price and created an administrative burden (particularly where numerous investors, such as limited partners, were involved). As noted by Canada's private equity and venture capital communities, these factors frequently discouraged investors from considering investment opportunities in Canada.

The bureaucratic and economic issues related to complying with section 116 have been significantly reduced by the amendment of the definition of TCP. Under the amended definition (which applies to transactions after 4 March 2010), shares of private Canadian corporations and interests in most partnerships and trusts will not qualify as TCP provided that not more than 50 percent of the fair market value of such shares/interests was derived from real property in Canada, Canadian resource properties or timber resource properties. Where shares/interests are not classified as TCP, the non-resident investor is not subject to section 116 or Canadian tax upon disposition. As a result, M&A lawyers can remove the various steps associated with section 116 compliance from closing agendas and non-resident vendors will avoid costs, delays and administrative obligations (such as applying for treaty relief).

The amendment to the definition of TCP represents a significant and positive development for foreign investment in Canada, particularly in sectors such as technology where the shares of the target are not likely to qualify as TCP.

Competition law

Recent amendments to Canada's Competition Act (effective in March 2009) included the adoption of a two-stage review procedure, similar to the 'second request' mechanism in the US. Under the amended Act, a statutory waiting period of 30 days commences when merger notification is received, and certified as complete, by the Competition Bureau. During this period, the Commissioner of Competition may issue a Supplementary Information Request (SIR). A SIR freezes the expiry of the statutory waiting period until the SIR has been complied with and, at that point, a second 30-day statutory waiting period commences. Upon the expiry of the applicable waiting period, the parties can legally close their transaction, unless the Commissioner has obtained an injunction from the Competition Tribunal.

These changes are significant for the following reasons. First, the previous review process permitted two types of notification forms (long form and short form), each with a different waiting period; the current process standardises the notification and waiting period for all transactions. This development, along with the SIR mechanism, aligns the Canadian system more closely with its US counterpart and will likely provide comfort to foreign investors; particularly where a transaction involves both US and Canadian merger reviews. Second, where the Commissioner required additional information concerning a proposed merger, and such information was not provided voluntarily by the parties pursuant to the previous process, she had to obtain a compulsory production order from the court. Now, while the Commissioner can still seek a production order, it is very unlikely that this will be necessary, as the SIR process provides her with considerable ability to compel the parties to provide information before a transaction can be completed.

The new powers granted to the Commissioner raise some potential concerns. First, SIRs may be used as a tool to extend the statutory waiting period to allow the Commissioner with more time to conduct her review of a merger. However, the Commissioner's public commitment to minimise the burden of the merger review process suggests that SIRs will not typically be used for such a purpose. Second, unlike a section 11 order, there is no judicial oversight regulating the Commissioner's ability to request information by using a SIR. In effect, the scope of a SIR request is limited only by the Commissioner's determination of relevance to its competitive assessment of the proposed merger. Finally, responding to SIRs will almost always involve extensive documentary productions, which are expensive and may take months to complete.

It is worth noting, however, that the Bureau's Merger Review Process Guidelines state that early consultation, and timely compliance with the Bureau's information requests, may reduce the necessity for, or scope of, a SIR. ■