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Editor-in-Chief: Karl P. Sauvant (Karl.Sauvant@law.columbia.edu)
Managing Editor: Jennifer Reimer (jreimer01@gmail.com)

A new economic nationalism? Lessons from the PotashCorp decision in Canada

by
Sandy Walker*

In its *World Investment Report 2011*, UNCTAD reported that liberalizing investment policy measures taken globally in 2010 outnumbered restrictive measures.[1] Without the benefit of statistics, investors might have drawn the opposite conclusion, witnessing what appears to be a rising tide of national resistance to foreign takeovers: the Australian Foreign Investment Review Board's rejection of a takeover of the Australian Securities Exchange by the Singapore Exchange, Italian concern over a French company's takeover of dairy giant Parmalat and the US Government's requirement that Chinese company Huawei divest certain assets it had acquired from 3Leaf.

In Canada, the rejection by the Canadian Government of the takeover of Potash Corporation of Saskatchewan (PotashCorp) by Australian mining giant BHP Billiton (BHP) has raised similar anxieties. However, closer scrutiny of the PotashCorp decision reveals that it does not portend a sea-change in the foreign investment review process in Canada. Rather, it underlines that politics can occasionally hijack the review of foreign investments, in contrast to other areas of law (such as merger control under competition law) that tend to have a more predictable, less open-ended framework of analysis.

The PotashCorp decision represented only the second time in Canada's history of foreign investment review legislation (Investment Canada Act or ICA) that a foreign investment outside the cultural sector has been rejected. PotashCorp is the largest producer of potash (a key ingredient in fertilizer), reported to have about 20% of global potash capacity. The Canadian Government found that BHP's bid did not meet the "net benefit to Canada" test for approval

* Sandy Walker (sandy.walker@fmc-law.com) is a partner in the Competition/Antitrust & Foreign Investment Review Group of Fraser Milner Casgrain LLP. The author wishes to thank Subrata Bhattacharjee, Andrea Bjorklund and Gus Van Harten for their helpful peer reviews. **The views expressed by the author in this *Perspective* do not necessarily reflect the opinions of Columbia University or its partners and supporters. *Columbia FDI Perspectives* (ISSN 2158-3579) is a peer-reviewed series.**

[1] See http://www.unctad.org/templates/webflyer.asp?docid=15189&intItemID=2068&lang=1&mode=downloads.

under the ICA. Among other factors, the Canadian Government was not satisfied that BHP was prepared to make sufficient commitments in respect of capital expenditures or PotashCorp's membership in the potash export consortium, Canpotex.[2] At the time, the federal Minister of Agriculture also referred to potash as a "strategic resource."[3]

Despite these explanations, the PotashCorp decision is properly viewed as an exceptional and largely political response to a number of factors:

- The Premier of Saskatchewan's success in galvanizing opposition to the deal across Canada, based on expressed concerns over a significant reduction in tax revenues and foreign ownership of a "strategic" resource.
- The ruling Conservative Party's minority government status, which made it vulnerable to a potential loss of seats in the 2011 election -- particularly in the province of Saskatchewan where there was strong support for the Premier's opposition.
- The hostile nature of BHP's bid.

The absence of official reasons for the PotashCorp decision fostered anxiety about the Government's openness to foreign investment. This was particularly the case in light of the significant and, in some respects, unprecedented undertakings BHP had offered Canada. The latter included foregoing tax benefits, remaining a member of the Canpotex potash export consortium for five years and establishing its global headquarters in Saskatoon. BHP also offered a US$ 250 million performance bond to the Government to backstop its undertakings, likely to allay public concerns about compliance.

There are (at least) three lessons to be drawn from this decision. First, potential stakeholders in the Investment Canada process, particularly the provinces, have learned that political agitation can yield concrete results. However, whether this lesson will translate readily to other transactions is open to question: provincial leaders typically have more diverse and conflicting constituencies than Saskatchewan where the potash industry is very significant, and the federal government is no longer politically fragile, having won majority government status in May of 2011.

Second, the Canadian Government is sensitive to criticism that its decision regarding PotashCorp could discourage foreign investment in Canada and, accordingly, has portrayed this case as exceptional and not indicative of a potentially worrisome trend of deploying national interest tests in a way that impedes the flow of international investment.[4] Indeed, no deals have been rejected in the year since the decision, although it is telling that the Government has still not brought into force a 2009 amendment to the ICA that would increase the review threshold and thereby reduce the number of foreign investments subject to review.

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[2]See Cassandra Kyle, "BHP Billiton withdraws potash bid, citing 'net-benefit' bar," *Postmedia News,* Nov. 15, 2010, available at: www.canada.com/news/Billiton+withdraws+potash+citing+benefit/3827505/story.html.

[3] Eric Reguly, Andy Hoffman and Brenda Bouw, "BHP's hopes fade as Ottawa calls potash 'strategic,'" *The Globe and Mail*, November 5, 2010, p. B1.

[4] See Peter Lichtenbaum and David Fagan, "Lessons in mediating for dairy warriors," *Financial Times*, April 20, 2011.

Third, some foreign investors may increasingly turn to self-help measures to address uncertainty over the Government's approach to foreign investment. For example, by making minority investments of less than a third of a corporation's shares, foreign investors can avoid scrutiny under the ICA, unless the investment is potentially injurious to Canada's national security. In addition, in the resources sector, foreign businesses may negotiate "off-take agreements" entitling them to a share of production as a means of securing access to natural resources.

Investors can take comfort that the *PotashCorp* decision does not signal a new protectionism in Canada. Nevertheless, in Canada as elsewhere, foreign investors must be alert to the possibility that political sensitivities may jeopardize a small number of deals involving perceived national champions.

For further information, including information regarding submission to the *Perspectives*, please contact: Vale Columbia Center on Sustainable International Investment, Jennifer Reimer, FDIPerspectives@gmail.com or jreimer@lyhplaw.com.

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