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Foreign Investment Review Revisited

The Dubai Ports controversy earlier this year brought to light the question of foreign ownership review processes in the United States. The transaction would have resulted in a takeover by Dubai Ports World, a United Arab Emirates–based company, of a firm that manages significant operations at six East Coast ports in the United States. Whether the U.S. government should review foreign purchases of U.S. companies for possible national security problems was at the center of the controversy.

Similarly, there have been ongoing discussions about the adequacy of Canada's foreign investment review legislation, which does not empower the government of Canada to review investments in potentially sensitive areas such as defense, technology or natural resources or other foreign investments that could pose a national security threat.

With the exception of certain sensitive sectors, unless the Canadian business has assets that exceed $265 million, the foreign investment by a WTO investor is not subject to review. Transportation services (in addition to financial services, uranium mining and cultural/heritage companies) are considered part of a sensitive sector; therefore, the threshold for all foreign investors is significantly lower. Specifically, in the case of a direct acquisition of control, where the value of the assets of the Canadian business exceeds $5 million, the transaction is reviewable.

It is of interest to note that in June 2005, the then Minister of Industry introduced Bill C-59 to amend the *Investment Canada Act*, Canada's foreign investment review legislation. Bill C-59 was intended to broaden the scope of review by the Canadian government, allowing it to review any foreign investment in a Canadian business where such investment might compromise Canada's national security. Concerns about the Act's inability to block investments on the basis of national security arose when Minmetals (a corporation largely controlled by the government of China) sought to acquire Noranda, a major Canadian resource company. The takeover transaction was ultimately unsuccessful.

The additional review procedure contemplated in Bill C-59 could be invoked in any case in which the Minister believed on reasonable grounds that an investment "could be injurious to national security," regardless of the value of the assets acquired or whether control of the Canadian business was acquired.

Before Bill C-59 was passed, Parliament was prorogued and a federal election followed. The Conservative Party formed the new government. One of Bill C-59's supporters was David Emerson, who is now Minister of International Trade and Minister for the Pacific Gateway and the Vancouver-Whistler Olympics. The bill, should it be reintroduced, would likely have his support. U.S. and other foreign investors will want to monitor this legislative initiative closely.

Proposed Transportation Merger Review Process

Prior to 1996, industry-specific oversight of transportation sector mergers was established under the *National Transportation Act*, *1987*. Its provisions required that proposed transportation mergers (exceeding a nominal threshold of $10,000) be examined by the National Transportation Agency (the "NTA"). The NTA had the power to disallow a proposed transaction if it was found to be against the public interest. Industry-specific oversight in the transportation sector was terminated with the enactment of the *Canada Transportation Act* (the "CTA") in 1996. The government's view at that time was that any transportation merger that created anti-competitive effects would be subject to the *Competition Act* and that oversight by the Canadian Transportation Agency ("Agency") was no longer required.

In 2001, the final report of the *Canada Transportation Act* Review Panel (the "Review Panel") recommended that a new process for reviewing proposed mergers in all transportation modes under federal jurisdiction should be established to examine issues of broad national or trans-national interest. The Review Panel found that the *Competition Act* process has two apparent shortcomings. First, the scope of the review process is limited to competition issues—it does not consider broad national or public interest issues. Secondly, by the Competition Bureau (the "Bureau") assessment of a proposed merge, is not an open or public process. The Bureau's analysis is conducted in private, and all documentation is confidential.

The Review Panel decided that mergers in the transportation sector often involved matters of great public interest. As stated in the Review Panel's report (at page 105), "Transportation is key to the functioning of all sectors of the economy and the competitiveness of Canadian industry in the global marketplace."

Public Interest Determination

Proposed amendments contained in Bill C-11 (*An Act to amend the Canadian Transportation Act and the Railway Safety Act and to make consequential amendments to other Acts,*) introduce a new public interest review process for certain proposed transactions that involve a transportation undertaking. Bill C-11 received second reading on September 21, 2006. It is similar in content to Bill C-44 (introduced in March 2005), which did not proceed due to the intervening federal election.

The proposed legislation applies to federal undertakings—airlines, railways, bus operators, motor carriers, pipelines and related businesses. There is a question as to whether this review process would apply to a transaction where transportation is a small component of the target business or ancillary to the target's main business. On its face, the scope of transactions involving transportation undertakings that would fall under Bill C-11's proposed merger review procedures is excessively broad. This could result in uncertainty and delay in a number of transactions—which are likely not intended to be subject to such extraordinary review procedures.

The proposed public interest review process would be initiated by parties notifying the Minister of Transport (the "Minister") of a proposed merger that involves a transportation undertaking at the same time as notice under subsection 114(1) of the *Competition Act* is given to the Commissioner of Competition (the "Commissioner"). The party-size and transaction-size thresholds that apply to notifiable transactions under Part IX of the *Compe-*

tition Act are applicable here. In the case of a proposed transaction that involves an air transportation undertaking, the parties must also give notice to the Agency. A copy of the filing made with the Bureau is to be provided to the Minister, in addition to "any information with respect to the public interest as it relates to national transportation." There is a serious concern that the bill does not adequately provide for the protection of commercially sensitive confidential information of the parties to a proposed transaction that falls under this new public interest review process.

Within 42 days of the filing, the Minister must determine whether the proposed transaction raises "public interest" issues. If not, the parties may proceed to close the transaction (subject to receipt of other applicable regulatory approvals.)

If the Minister finds that the proposed transaction raises public interest issues, then the Minister may refer the proposed transaction to the Agency or other person as the Minister may designate to review the issues. Within 150 days (or such longer period that the Minister may allow), the Agency (or other person) must make a *public interest determination* and report to the Minister. In the case of a transaction that involves an air transportation undertaking, the Agency must also determine whether the transaction would result in the air carrier being "Canadian," as defined under the CTA (which limits foreign ownership in a Canadian air carrier to 25%).

Concurrently with the Agency's review, the Commissioner is given 150 days from notification of the proposed transaction to review and report to the Minister and the parties to the transaction on any concerns regarding "potential prevention or lessening of competition that may occur as a result of the transaction." The Commissioner's standard of review is notably different from that under the *Competition Act*, where a "substantial" prevention or lessening of competition is required to be found. Arguably, the use of "potential" affords the Commissioner a wider discretion in the review process under this proposed legislation. This raises a question as to why a different standard of review is being applied to transportation mergers as compared with mergers that occur in every other industry sector in Canada.

Following issuance of reports by the Agency and the Commissioner, respectively, the parties to the proposed transaction may undertake measures to address the concerns. Revisions to the transaction may be proposed by the parties to satisfy the concerns.

Finally, the Minister must decide whether to recommend approval of the proposed transaction to the governor in council (i.e., the federal cabinet), which ultimately must be satisfied that it is in the public interest to approve the transaction. There is broad discretion to specify terms and conditions that the cabinet considers appropriate as part of the approval. Parties that complete a proposed transaction without the cabinet's approval or that fail to comply with terms and conditions of an approval order risk prosecution and if convicted, a penalty of imprisonment (up to five years) or a fine not exceeding $10 million, or both.

Critics of the proposed legislation—which ultimately requires cabinet approval of a proposed merger in the transportation sector—suggest that it may result in transportation mergers being decided on the basis of political factors rather than potential competitive effects. They assert that the *Competition Act* is the appropriate means to address concerns about the effects on competition of mergers in the transportation industry. There is a concern that the public interest review provisions go beyond the scope of the general and established procedures and standards set out in the *Competition Act.* It remains to be seen whether this proposed industry-specific oversight of transportation sector mergers will become law in Canada.

Aviation Developments

Aircraft Lessors Beware

A recent decision of the Supreme Court of Canada has significant implications for aircraft owners and lessors that lease aircraft to air carriers that operate in Canada. *Canada 3000 Inc., Re; Inter-Canadian (1991) Inc. (Trustee of),* [2006] S.C.J. No. 24 is a case in which the Court, in essence, was called on to determine the allocation of the financial risk coincident with the collapse of an air carrier. The Court posed the question in this way: When an operator collapses, leaving unpaid bills for airport charges and air navigation services, the question becomes who takes the financial loss—the people who ultimately own the leased aircraft or the people who were obliged to (and did) provide the airport and navigation services?

Canada 3000 Inc. involved the interpretation of provisions of the *Airport Transfer (Miscellaneous Matters) Act*, S.C. 1992, c. 5 *(Airports Act)* and the *Civil Air Navigation Services Commercialization Act*, S.C. 1996, c. 20, ("CANSCA") that applied to the recovery of charges for services in the context of the failure of two Canadian airlines—Canada 3000 Airlines Ltd. and Royal Aviation Inc. ("Canada 3000") and Inter-Canadian (1991) Inc. Airline ("Inter-Canadian").

The Supreme Court considered four distinct questions in the case: (a) who was liable for charges imposed by CANSCA; (b) what is the relationship between the rights of seizure and detention of aircraft as "security" for unpaid fees provided for in the *Airports Act* and CANSCA and the rights of the leasing companies—referred to by the Supreme Court as the "legal titleholders"—that lease aircraft to airlines that incur charges under the *Airports Act* and CANSCA; (c) whether the detention and seizure rights included the right to sell seized aircraft; and (d) whether "ancillary" property, such as engines and onboard computer systems, were subject to the seizure and detention rights.

Before going bankrupt, Canada 3000 and Inter-Canadian operated their fleets of aircraft under leasing agreements with the respondent legal titleholders and were the registered owners of the aircraft under the *Aeronautics Act*. These air carriers incurred approximately $33.75 million in charges for civil air navigation and airport services provided by NAV Canada and the airport authorities pursuant to the *Airports Act* and CANSCA.

The case involved an exercise in statutory interpretation and the issues of interpretation are closely tied to context. Prior to CANSCA and the *Airports Act*, civil air navigation and airport services were provided by the federal government. Under the current legislative scheme, the privatized NAV Canada and airport authorities operate as self-funded corporations that provide

services on the basis of a cost-based tariff fixed by government regulation. The Supreme Court observed that they cannot withhold airport or navigation services even from an obviously failing airline.

At the time the measures in question were enacted, airline insolvencies and bankruptcies had become a fact of life throughout the airline industry. The legislative scheme shows that Parliament fully appreciated that in dealing with aircraft flown in and out of jurisdictions under complex leasing arrangements, the only effective collection scheme would be to render the aircraft themselves available for seizure, and thereafter to let those interested in them resolve their dispute about where the money should come from to pay the debts due to the service providers.

The Supreme Court determined that, although the legal titleholders are not directly liable for the charges due to the service providers, NAV Canada and the airport authorities were entitled to orders seizing and detaining the aircraft, and were entitled to have their claims satisfied out of the security posted in substitution for the aircraft. The Supreme Court's view was that the legal titleholders are sophisticated corporate players and are well versed in the industry in which they have chosen to invest. Since they can select which air carriers they are prepared to deal with and negotiate appropriate security arrangements as part of their lease transactions, they are in a better position to protect themselves against this type of loss than are the airport authorities and NAV Canada.

Parliament endeavored to create a comprehensive remedy that would be applicable across the country and would not vary from one province to another. This uniformity is especially vital since aircraft are highly mobile and move easily across jurisdictions.

On the question of whether the detention and seizure rights included the right to sell seized aircraft to satisfy the obligations owing, the Supreme Court said no. Neither the provisions of CANSCA nor the *Airports Act* empowered the authorities to sell the seized aircraft, nor was that authority implied in the creation of the right to seize and detain aircraft. The sole claim that can be asserted by NAV Canada and the airport authorities is "the claim to possession of the aircraft until their user charges are paid."

Two of the respondents leased to Canada 3000 the engines attached to two of the aircraft which, when seized, were airworthy. The Supreme Court decided that, for the present purposes, the engines are part of the aircraft in respect of which charges were incurred and that are the subject of the detention.

New Canada–U.S. Open Skies Agreement

September 1, 2006 marked the beginning of increased liberalization of the North American air transport industry. Implementation of a new *Open Skies Agreement* between Canada and the United States has resulted in an expansion of the 1995 *Agreement* and is intended to provide greater access and increased pricing flexibility.

Canada's air transport industry is currently in a period of growth, boosted by the recently announced Pacific Gateway Strategy and bilateral air transport agreements with China and India.

The new Canada-U.S. Open Skies Agreement establishes new freedoms for passenger airlines and all-cargo carriers, including fifth-freedom rights, all-cargo seventh-freedom rights and the ability to price competitively. It is hoped that these new developments will stimulate an increase in competition, place pressure on carriers to increase service quality and flight route coverage, and offer more direct routes and lower prices.

Maritime and Intermodal Transportation

One of the most exciting developments in Canada affecting the transportation industry relates to the Pacific Gateway Strategy. Canada is positioning itself as the gateway to North America for goods from China, India and other Asian countries.

With the surge in intermodal transportation, a recent decision of the Federal Court of Canada is of particular interest. Intermodal transportation and the ability of an inland rail carrier to invoke the benefit of an ocean carrier's "Himalaya clause" were the focal points of the decision.

In *Boutique Jacob Inc. v. Pantainer Ltd. et al.,* [2006] F.C.J. No. 292, the Federal Court of Canada held that section 137 of the *Canada Transportation Act* precludes a rail carrier from asserting the limitation of liability contained in an ocean carrier's Himalaya clause (even where it expressly extends the limitation of liability to its subcontractors). The court also held that section 137 of the Act is a bar to the limitation of liability found in a rail carrier's confidential contracts, where the aggrieved person is not a party to such agreement.

The Facts

Boutique Jacob Inc., through its freight forwarder, arranged for a shipment of women's clothing to be transported from Hong Kong, People's Republic of China, to Montreal, Canada. The freight forwarder engaged Pantainer Ltd. to perform the transportation. Pantainer issued Express Line bills of lading to Boutique Jacob. The value of the cargo was not declared. Pantainer, in turn, engaged and paid Orient Overseas Container Line ("OOCL") to transport the shipment from Hong Kong to Montreal. OOCL issued an electronic waybill, referring to its Web site for the applicable terms and conditions.

OOCL in turn engaged and paid Canadian Pacific Railway ("CP Rail") pursuant to the confidential rate contract between OOCL and CP Rail to transport the shipment by rail from Vancouver to Montreal. As a result of a train derailment, the cargo was destroyed. There was no dispute that the damages occurred during the rail carriage.

Boutique Jacob commenced an action against Pantainer, OOCL and CP Rail. The parties had dealt with each other on an ongoing basis.

Liability of Pantainer and OOCL

The court found that both Pantainer and OOCL were exempt from any liability for the loss suffered by Boutique Jacob and relied on an exemption clause found in Pantainer's bill of lading, which read:

> 6.5 The Carrier shall not be liable for any loss or damage arising from . . . h) any cause or event which Carrier could not avoid and the consequences of which the Carrier could not prevent by the exercise of due diligence.

Coincidentally, the same exemption clause was contained in OOCL's terms and conditions. Having noted that, the court nevertheless found that OOCL could rely on the exemption clause in Pantainer's bill of lading.

The court reaffirmed the Canadian law with respect to "Himalaya clauses" and stated:

> These so-called "Himalaya clauses" are well recognized terms in transport contracts, and they are enforceable by the courts notwithstanding a third party's complete ignorance of the existence of a clause granting it a benefit at the time of the performance of its own contract. They have long been recognized by the highest British Courts . . . and have similarly been endorsed by the Supreme Court of Canada. . . .

On that basis, the court dismissed the plaintiff's claim as against Pantainer and OOCL.

Liability of CP Rail

Turning to the claim against CP Rail, the court considered the obligations of CP Rail as a common carrier in the context of section 137 of the Act and the *Railway Traffic Liability Regulations*. The court found that CP Rail was clearly responsible for the loss or damage to the plaintiff's cargo.

CP Rail argued that it was entitled to benefit from the terms and conditions found in its confidential rate contract with OOCL, in CP Rail's published Tariff CPRS 7589, in OOCL's bill of lading or in Pantainer's bill of lading. The court held otherwise and stated:

> This argument would be compelling, as it is for the other two Defendants, if it was not for section 137 of the Canada Transportation Act. This section clearly provides that a railway company shall not limit or restrict its liability to a shipper except by means of "a written agreement." Now, there is no written agreement as between Jacob and CPR. . . .

Nor was CP Rail entitled to rely on its tariff (which would have limited its liability to $1,432.89) because it did not have a signed agreement with Boutique Jacob.

Of significance, the court held that CP Rail could not invoke the Himalaya clause in Pantainer's bill of lading nor in OOCL's terms. The court stated:

> But the application of these clauses [referring to the Himalaya clause] to a railway carrier would defeat the purpose of s. 137 of the Canada Transportation Act. It would make no sense to protect the shipper by prescribing that a railway company cannot limit its liability except by written agreement signed by that shipper, if the railway company could nevertheless achieve the same result through the means of a Himalaya clause found upstream in the contract of another carrier. I recognize that such reasoning results in a less advantageous position for railway companies as opposed to other carriers. But this is true not only for the purpose of liability but also in many other respects, since other modes of transportation are not as heavily regulated as are the railway companies.

CP Rail was held solely responsible for Boutique Jacob's damages and was not able to limit its liability. Damages were assessed on the basis of arrived sound market value. CP Rail has appealed the decision to the Federal Court of Appeal and the parties await a hearing date. A number of third parties have sought leave to intervene in the case and wish to appear and make submissions before the Federal Court of Appeal. ■

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