

Canada's rejection of Petronas throws spotlight on takeover laws

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* Opaque Investment Canada Act sets foreign takeover rules

* Government promised two years ago to clarify conditions

* State-owned enterprises may be a special case

By Euan Rocha

TORONTO, Oct 22 (Reuters) - Canada rejected Malaysian state oil company Petronas' bid for Progress Energy Resources Corp under the terms of the Investment Canada Act - an opaque piece of legislation created, in part, to draw more foreign investment into Canada.

The act gives the industry minister the power to review any major takeover of a Canadian company by a foreign investor to determine if the deal is of "net benefit" to Canada.

But despite several promises to explain the issues it looks at when it decides whether to approve a takeover, Canada has not clarified what "net benefit" means, leaving frustrated companies and investors demanding more details.

The act came under the spotlight in 2010 when Canada blocked BHP Billiton's \$39 billion hostile bid for the world's largest fertilizer maker, Potash Corp, arguing that it was not of net benefit to Canada.

Industry Minister Christian Paradis used the same argument late on Friday, saying he was not satisfied that Petronas' \$5.2 billion friendly bid for Progress would be of net benefit to Canada. He would not give any details but said the companies had 30 days to come up with new proposals.

Progress Energy Chief Executive Michael Culbert on Monday told Reuters he had received no indication from the government that it had concerns about the deal and blamed a "communications breakdown" for the 11th-hour veto. Culbert said he believes the deal can get back on track, with new talks starting this week.

At the time the transaction was announced in June, Petronas committed to keeping Progress Energy's upstream operations in Calgary. It also said it would invest substantial sums to build liquefied natural gas infrastructure in Prince Rupert, British Columbia for a planned LNG export facility.

The Investment Canada Act, a 1985 replacement for legislation that allowed Canada to review all foreign takeovers, lists several factors that the government can take into account, including jobs, innovation, competition (internationally and within a sector), and the compatibility of a deal with "national industrial, economic and cultural policies."

But there is no explanation and little detail about these, or about a national security clause and rules for dealing with state-owned enterprises like Petronas and China's CNOOC Ltd , whose C\$15.1 billion bid for Nexen Inc is also under scrutiny.

"Obviously one question this (ruling) raises is the signal it sends to other foreign state-owned investors - and CNOOC in particular," said Subrata Bhattacharjee, a partner with Heenan Blaikie in Toronto. "It puts practical pressure on CNOOC in whatever negotiations are under way."

"A rising tide raises all boats - so it is fair to say that both investors would have to deal with the government's latest thinking about foreign investment review of these types of deals," said Bhattacharjee, co-chair of the firm's national trade and competition group.

The current review threshold is C\$330 million -- a fraction of the size of many takeovers on the market.

Foreign investment and competition lawyers say some degree of obscurity within the act is necessary to give the government the leeway to rule on sensitive takeovers, but nonetheless they say the current legislation could use some additional clarity.

"It would be far from total transparency. It would be more like, here are the six net benefit factors we consider and we will tell you how we approach these things," Tony Baldanza, a partner with Fasken Martineau who heads the firm's antitrust and competition law group, said of the ways the law might change.

"However, you are not going to be able to tick boxes and predict an outcome in all cases."

Canadian Prime Minister Stephen Harper on Monday promised to provide foreign investment guidelines "fairly shortly" that may provide clarity on how the government reviews bids, especially ones from state-owned entities.

Despite fears that Canada is adopting a more protectionist stance with the Progress-Petronas decision, some believe that the government can minimize the fallout if it does spell out the factors it takes into account when considering takeovers by state-owned entities.

"It may be that the announcement is intended to signal that Canada will apply a common set of, perhaps tougher, criteria when assessing whether or not bids by any state-owned entities are 'likely to be of net benefit' to Canada," said Jay Hoffman, who is partner and co-chair of the business law group of Miller Thomson LLP in Toronto.

"If this is the intent and the guidelines for SOEs are ultimately clarified, the level of foreign investment by SOEs going forward may not be as negatively impacted by this decision as a flat out rejection," he said. (Reporting by Euan Rocha; Editing by Janet Guttman and Steve Orlofsky)

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