

Mergers and Acquisitions

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U.S. Steel: Federal Court Upholds the Constitutionality of Section 40 of the *Investment Canada Act*

Before Industry Minister Tony Clement sent a demand letter to United States Steel Corporation (“US Steel”) in May of 2009, it was unclear how sharp the teeth of the *Investment Canada Act* (the “Act”) could be. That demand letter (described in our client communication entitled Minister Clement’s Letter to US Steel) illustrated the government’s resolve. Last week, a decision of the Federal Court upheld the constitutionality of the federal government’s remedial powers under the Act, indicating that the teeth may have some bite.

Background

In 2007, US Steel gave certain undertakings to the Canadian government as part of its takeover of Stelco Inc. (“Stelco”). Pursuant to the Act, where a non-Canadian proposes to acquire a Canadian business that meets or exceeds certain size thresholds, the transaction is subject to review by the Industry Minister (and/or, for certain cultural acquisitions, the Minister of Canadian Heritage). The acquiror must satisfy the relevant Minister(s) “that the investment is likely to be of net benefit to Canada.” Often acquirors will be asked to provide, and will provide, undertakings to bolster the transaction’s benefits. US Steel’s undertakings addressed concerns including the protection of Canadian jobs and Stelco’s operations in Hamilton.

Statutory Framework

Section 39 of the Act provides the Minister with the power to send a demand where the Minister believes that the non-Canadian acquiror has failed to comply with an undertaking. Section 40 of the Act provides the Minister with the power, where an acquiror has failed to comply with a demand made under Section 39, to apply to a superior court for any order that, in the court’s opinion, the circumstances require, including, for example, compliance with the undertaking, the imposition of monetary fines or even forced divestiture.

US Steel challenged the constitutionality of Section 40 on the basis that it violates both the presumption of innocence and fair hearing provision of the *Canadian Charter of Rights and Freedoms* and the fair hearing provision of the *Bill of Rights*.

Overview of Reasons

With respect to the *Charter*, US Steel’s arguments were based on the premise that an order under s.40 is either by its nature a criminal proceeding or involves the imposition of true penal consequences. In short, the Federal Court held that a s.40 proceeding is not by its nature criminal; in the court’s view, the acquiror is not being called to account to the public, as in a criminal prosecution, but rather is “being called to account to the government for a failure to honour commitments made to the government,” akin to a civil enforcement mechanism. Similarly, the court held that an order under s.40, particularly a monetary penalty, is not a “true penal consequence” but is rather a means “to promote and ensure the attainment of the legislative objectives.” Significantly, the court held that the amount of an administrative monetary penalty is not determinative. Rather, it appears that such penalties, even if potentially very large, do not trigger the constitution as long as the legislative regime as a whole meets the *Charter’s* requirements.

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With respect to the *Bill of Rights*, US Steel claimed that the procedure provided for under Section 40 of the Act does not allow for a fair hearing in accordance with the principles of fundamental justice. The court dismissed these claims on the grounds that, in the context of the Act, an acquiror would be afforded sufficient procedural protections to satisfy the principles of fundamental justice.

Conclusion

The Federal Court's decision remains subject to appeal. However, the decision should provide the government with some confidence that its remedies under the Act are enforceable. The decision should also remind those interested in Canadian acquisitions or mergers that the government is not only willing, but also likely able, to enforce any undertakings.

Please contact any member of the Goodmans M&A team to discuss this matter.