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Cross-Border Private M&A in Canada:

10 Tips for Foreign Acquirers

Canadian private M&A slowed somewhat in 2015 and early 2016, owing to the depressed market for commodities, but deal flow is roaring back in the latter half of 2016. While Canadian M&A takes many cues from the United States and Europe, it is unique in many ways. A successful foreign acquirer advised by Canadian legal counsel will be armed with knowledge about these differences.

1 The Canadian Market Has Matured

Gone are the days of foreign private equity firms finding founder-operated businesses to acquire in Canada at a low multiple. The majority of sellers and buyers in reported private M&A transactions in Canada are strategic corporations or financial players rather than founders. Canadian M&A deals are increasingly done with the assistance of representation and warranty insurance. On the vendor side of multinational auction transactions, Canadian law firms have started providing vendor due diligence reports to bidders on a non-reliance basis.

2 What is Market?

Typical material deal terms in Canada are not just carbon copies of the U.S. or European practice. For example, as compared to the U.S., buyers of Canadian companies have been able to insist on higher caps to indemnification exposure in Canada. Survival periods tend to be longer in Canada. Anti-sandbagging provisions are often handled differently in Canadian transactions. Legal opinions have become much less common in private deals other than in the financial services and venture capital sectors.

3 Canadian Foreign Investment Review

Canada regulates all foreign investments under the *Investment Canada Act*. Transactions over a certain dollar-value threshold or in sensitive industries (e.g., cultural) are subject to review by the federal government, in which case a pre-closing waiting period will apply. All other foreign acquisitions of Canadian businesses are subject to post-closing notification. Reviewable investments made by state-owned enterprises (SOEs) are subject to other additional considerations.

4 Anti-Trust Regime and a Uniquely Canadian Defence

The anti-trust and competition regime established under the *Competition Act* (Canada) requires pre-notification merger filings when transaction and party-size thresholds are exceeded. Pre-closing waiting periods may apply. All acquisitions, whether pre-notifiable or not, are subject to possible competition review for one year following closing. The buyer can obtain an advance ruling certificate or no-action letter to foreclose the risk associated with a review. Canada now has a unique efficiencies defence to an otherwise anti-competitive merger.

5 Forget Everything You Know About Employment

Unlike the U.S., there is no "at-will" employment in Canada. Absent valid contractual provisions limiting the employee's severance entitlements, employees are entitled to "reasonable notice" of termination or payment in lieu of such notice. This means that, on an asset transaction, employment of non-unionized employees does not transfer automatically; employees must be offered employment by the acquiror. Severance entitlements for employees tend to be much higher in Canada than in other jurisdictions. The defined-benefit and defined-contribution pension plans that are used by many Canadian employers to supplement the federal Canada Pension Plan are subject to a web of federal and provincial legislation. Relevant to the acquisition of a Canadian business, these rules govern such things as recognition of an employee's past service and transfers of plan assets.

6 Regulated Commerce

Regulatory regimes in Canada are often more robust than in other jurisdictions. For example, federal and provincial restrictions on the collection, use and disclosure of personal information in Canada must be observed during and after transactions. Canadian privacy legislation requires knowledgeable consent to, and not merely notice of, intended purposes. Canada has enacted its own comprehensive corruption legislation that prohibits bribery of foreign public officials, among other things, by criminal sanction with no limitation period.

7 Canadian Intellectual Property Protection

Unlike other jurisdictions, Canada follows a "first-to-file" system for patents. Canadian trade-mark law elevates the importance of licences, requiring licences even for wholly owned subsidiaries. Canada has not adopted the International Patent Classification system, providing distinct cost advantages for applicants. Also, registrants can renew trade-marks without requirement of proof of use. The copyright "bundle" of rights is different than in the U.S., with no right to prepare "derivative works." A "work made for hire" is limited to the employment context and transfers of ownership must otherwise be in writing. Moral rights are protected more extensively and apply to all types of works. IP licences that are silent as to assignability or sublicenseability are generally not assignable or sublicenseable without the licensor's consent.

8 Death and Taxes

Normally, foreign buyers of Canadian shares will want to incorporate a Canadian acquisition company, which allows for the pushdown of any acquisition financing and the Canadian tax-efficient repatriation of funds up to the purchase price from Canada without Canadian withholding tax. Canada does not have entities similar to American LLCs to use as acquisition vehicles. Canadian unlimited liability companies afford the opportunity for flow-through tax treatment, but must be used with caution given the anti-hybrid rules in the Canada-U.S. tax treaty. Transactions in Canada involving the sale of "taxable Canadian property" (generally, Canadian real property interests) can require clearance from the Canada Revenue Agency or a partial holdback of the purchase price. Canadian thin capitalization rules require that debt owing to related non-resident parties not exceed 1.5 times equity. In asset deals, it is also important to consider sales taxes and whether exemptions are available.

9 To Sue or Not to Sue

While litigation costs in Canada tend to be lower than in the U.S. due to streamlined rules of civil procedure, frivolous litigation is not common in Canada. This may in part be a result of Canada's loser pay system. The successful party in Canadian litigation is generally awarded at least part of their costs and damage awards tend to be lower than in the U.S. Also, punitive damages are extremely rare. Jury trials are extremely rare in Canadian civil matters, except for certain limited types of litigation, for example, libel or personal injury. In Ontario, commercial disputes are heard at a special division of the courts by judges with specialized commercial knowledge. Judges are appointed, not elected. While Canada allows contingency fees, the practice is not widespread and, generally speaking, the contingency payments are not as large as in the U.S. Most provinces require pre-trial mediation, which tends to encourage pre-trial settlement.

10 Quebec is Distinct

The province of Quebec, unlike all other Canadian jurisdictions, is governed by a civil law system derived from the *Napoleonic Code*. Its laws can differ dramatically from the rest of Canada and need to be taken into account when acquiring or selling a business with assets or employees there. In addition, Quebec has legislation that protects the use of the French language.

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