Blaney McMurtry
BARRISTERS & SOLICITORS LLP

EXPECT THE BEST

Canada and China Sign Major Agreement to Stimulate Direct Foreign Investment

by Patrick Gervais and Nailah Gordon-Decicieo
Originally published in *Blaneys on Business* (December 2012)

Patrick Gervais practices with Blaney McMurtry's corporate commercial group. A member of the Ontario and New York bars, he provides counsel and service in a wide range of commercial matters. He is fluent in French and speaks Spanish and Chinese.

Patrick may be reached directly at 416.597.4891 or pgervais@blaney.com.

Canada and China have signed a *Foreign Investment Promotion and Protection Agreement* (FIPA) intended to increase direct investment in both countries. Canada was scheduled to ratify the agreement some time in November. It was to take effect one month after ratification by both countries.

For Canadian investors, the effect of the ratified FIPA may be greater direct investment in China. Alternatively, Chinese investors will have the potential to drive expansion of operations located in Canada.

Designed to stimulate and protect Canadian and Chinese investments and investors, the agreement defines rules and obligations to regulate foreign investments to and from each country, including mandatory arbitration for dispute settlement.

The main obligations created by the agreement include: (i) non-discriminatory government treatment for investments made by Canadian investors in China and Chinese investors in Canada, (ii) provisions to protect investors in case of expropriation, and (iii) a defined dispute settlement mechanism.

Key Distinctions

Canada currently has 24 FIPAs in force. Most are similar in form and substance. The agreement with China differs by adopting standards more common in Chinese bilateral investment treaties. The main distinctions between the Canada-China agreement and the others are:

1. Agreement Lifespan of 31 Years

Unlike other FIPAs with an indefinite term and a termination provision with one year's notice by either party, the Canada-China FIPA would have an initial lifespan of 15 years, with the standard one year notice for termination thereafter. If ratified, investments made prior to termination would be subject to the Canada-China FIPA for an additional 15 year period after the effective termination date. An investment made prior to its initial termination could be subject to the agreement for 31 years after its entry into force. For example, if the FIPA were ratified in 2012 and the investment was made during the last year of its operation (i.e. 2028), the FIPA would apply to that investment until 2043.

2. No 'National Treatment' at the Establishment and Acquisition Stage

A second key distinction in the Canada-China agreement is that it does not provide prospective new investments into China with 'national treatment' (where foreign firms are treated as though they were Chinese firms).

In other Canadian FIPAs, such as the one with Jordan, investors receive 'national treatment' at the establishment and acquisition stages. Although the Canada-China FIPA affords 'most-favoured-nation

treatment' at the usual establishment and acquisition stages, it excludes 'national treatment' from these stages. In effect, the protection is limited to stages arising after a deal closes, including the expansion, management, conduct, operation and sale or other disposition of investments in its territory. This is more in line with practices found in other Chinese bilateral investment treaties than with those of Canada. The *Investment Canada Act* and its Chinese equivalent still apply, allowing both governments to veto investments at the establishment and acquisition stages when they are viewed as not providing a net benefit to their country.

3. Default Dispute Resolution Out of Public View

As in other FIPAs, Canada's agreement with China provides for arbitration to settle disputes pertaining to breaches of the agreement. In contrast to the standard FIPAs, however, the arbitration hearings of the parties are, by default, private, unless the host government determines that it would be in the public interest to make the dispute resolution public. For example, an arbitration hearing for a Canadian investor in China claiming damages under the FIPA would be private unless China decided it was in the public interest to make it public. This is a departure from the general Canadian practice in other bilateral investment treaties.

Nailah Gordon-Decicieo is completing the business law rotation of her articles with Blaney McMurtry LLP. She graduated with a Juris Doctor from the Faculty of Law, University of Windsor and with Honours from the DeGroote School of Business, McMaster University. Nailah has an interest in commercial and international law issues and has lived and worked in the United Kingdom and Jamaica.

Exceptions

As in other FIPAs, specified industries are explicitly exempt from the application of the Canada-China accord. In particular, measures pertaining to cultural industries (broadly defined to include publishing, film or video recordings, music recordings and radio communications) are excluded. Other exceptions include certain environmental measures, security matters, and the protection of essential security interests. Free trade areas, aviation, fisheries or maritime matters are excluded solely from the 'most-favoured-nation treatment' protection.

Expropriation

The expropriation provisions of the Canada-China FIPA are standard and prohibit the expropriation of investments or returns of investors, other than for a public purpose and against compensation at fair-market value. The mechanism for determining fair market value is specified in the FIPA.

Looking Forward

The government of Canada believes that the Canada-China FIPA will promote greater direct investment between the two countries. Canadian and Chinese firms contemplating foreign direct investment in the other country should be aware that conflicts could be resolved by private arbitration should the host country decide public arbitration is not in the public interest.

In addition, the government of Canada can anticipate that it may experience several claims by Chinese firms given the increasing number of Chinese inbound investments in Canada. This may result in greater exposure by the Canadian government to potential damages if Chinese investors are wronged by the Canadian government's actions. ■