

Submission to the Competition Policy Review Panel

by

Spectra Energy Corp.

Introduction and Summary of Recommendations

1. Spectra Energy welcomes the opportunity to make this submission in response to the Panel's invitation in its October 30, 2007 Consultation Paper.
2. Spectra Energy believes that steps can be taken to improve the foreign investment review process as it applies to energy pipeline businesses. These improvements will help Canadian firms to operate more efficiently and productively, and will help to improve Canada's attractiveness as a destination for foreign investment.
3. Spectra Energy urges the Panel to adopt the following specific recommendations:
 - (a) The *Investment Canada Act* should focus on reasonably identifiable foreign investment risks. These risks may be related to the investor (e.g. foreign state-owned entities) or the sensitive nature of the sector invested in (e.g. the cultural sector). Screening large transactions generally should be discontinued.
 - (b) If the current "net benefit test" is retained,
 - (i) Eliminate the need for a review where a non-Canadian acquires a Canadian business that is already non-Canadian owned,
 - (ii) Eliminate reviews in the transportation sector, given the recent amendments to specifically allow for merger reviews under the *Canada Transportation Act*,
 - (iii) If (ii) is not adopted, remove energy pipelines from the list of sensitive sectors,
 - (iv) Increase the dollar thresholds for review in sensitive sectors from the very low levels established many years ago,
 - (v) Allow the Minister to promulgate regulations to exempt classes of industries, or classes of transactions, from the review process, and
 - (vi) Redraft the *Investment Canada Act* to make it clearer and more logical. As presently drafted, the *Act* is convoluted, and difficult to understand and interpret.

Spectra Energy

4. Spectra Energy is one of North America's premier natural gas infrastructure companies. Our business consists of natural gas gathering and processing, transmission and storage, and distribution. For further information, see www.spectraenergy.com

5. In Canada, we own the Westcoast pipeline system which stretches 2,600 km from northeast and northwest British Columbia to the British Columbia/US border. We also own a majority of the 550 km Maritimes and Northeast gas pipeline, which connects Atlantic Canada with markets in New England.

6. In western Canada, our British Columbia pipeline and field services operations utilize more than 5,600 km of integrated raw gas gathering and sales gas transmission lines and five world-class processing plants to process and transport about 2 billion cubic feet of natural gas per day (Bcf/d). Also, our midstream operation owns interests in 13 processing plants and more than 1,600 km of gathering pipeline in the Western Canadian Sedimentary Basin in B.C. and Alberta. Our Empress system in western Canada includes 2.4 Bcf/d of natural gas liquids extraction and fractionation facilities and related liquids transportation and storage operations.

7. Through Union Gas, an integrated natural gas distribution, storage and transmission company, we serve about 1.3 million residential, commercial and industrial distribution customers in Ontario. We also have significant gas reservoir and salt cavern natural gas storage capabilities including ownership of an important gas storage facility in Dawn, Ontario.

8. We employ some 3200 personnel in Canada, with major offices in Vancouver, Calgary, Chatham and Halifax. Our Canadian revenues during fiscal year 2006 were \$3.6 billion. During this same period, we invested \$508 million in expanding and maintaining facilities in Canada. As is apparent, although Spectra Energy is not a Canadian for purposes of the *Investment Canada Act*, Spectra Energy is an important and long-term participant in the Canadian economy.

Our Interest in the Matters Being Examined by the Panel

9. Our interest in the Panel's work originates in our own experiences during the past decade. In that time, our Canadian businesses have undergone a number of corporate transformations. Major business units have been bought and sold, and we have undertaken various reorganizations. During the course of these activities, we have had occasion to deal with

the *Investment Canada Act* and the *Competition Act*. We have made various compliance filings under both statutes. And on numerous occasions we have had to analyze the various statutory provisions – some of which are very complex.

10. We are encouraged by the government's decision to appoint the Panel, and its mandate to make recommendations to enhance Canadian productivity and competitiveness. We are also encouraged that the Panel recognizes the important role of foreign investment to the Canadian economy and the need to make Canada an attractive investment destination.

11. The energy pipeline business strongly depends on access to foreign capital. Capital is needed both in the initial development stages of this critical infrastructure, and for ongoing projects. Some of the capital is furnished by way of debt, while some is furnished by way of equity. Each has a role. Given the large amounts of capital needed to build the energy pipeline infrastructure on which Canada depends, and the relatively small size of Canadian capital markets, Canada should want to smooth the way for foreign capital to reach its destination. And indeed, Canada, in our experience, has been largely receptive to foreign investment in the energy pipeline sector.

12. That said, more can be done to enhance Canada as an investment destination. As we will explain below, we believe that the investment review processes can benefit from improvement – particularly in regards to the *Investment Canada Act*.

13. When Spectra Energy makes a business acquisition or sale, the review processes under three separate statutes can be triggered:

- (a) *Investment Canada Act*. As a non-Canadian, most of our acquisitions will lead to a review by the Investment Review Branch of Industry Canada, as will most sales to a non-Canadian. As many of our activities involve the provision of a "transportation service", the value of assets threshold to cause a review is very low in most cases. The test is whether the investment is of net benefit to Canada.
- (b) *Competition Act*. Notice of a transaction must be given to the Competition Bureau where certain asset and sales thresholds are exceeded. Given the large size of the production units in the energy pipeline business, most mergers will invariably see these thresholds exceeded. The test is whether the merger prevents or lessens competition substantially, or is likely to do so.
- (c) *Canada Transportation Act*, Sections 53.1-53.6. The parties to a transaction involving a transportation undertaking that is notifiable under the *Competition Act*, must also make a related filing under the *Canada Transportation Act*. The Minister then decides if a second stage review is needed. If a second stage

review is ordered, the test is whether the transaction is in the public interest. This test seems to have two components: the potential lessening or prevention of competition (in which the Competition Bureau is a participant), and the public interest as it relates to national transportation.

14. In the following paragraphs, we will discuss the processes under each the *Investment Canada Act* and the *Canada Transportation Act*. We do not have any comments on the *Competition Act* review process. In our experience, the Competition Bureau handles the reviews expeditiously and without controversy – probably because the transactions that we have encountered do not raise any substantive competition issues.

Investment Canada Act Review

15. Foreign investment is vitally important to the well-being of Canada. The Panel explains the benefits of foreign investment as follows:¹

It has long been recognized that foreign direct investment (FDI) brings benefits to Canada through new sources of capital, ideas and know-how. As well, direct investment by Canadian firms in foreign markets enables them to be more productive and competitive and, ultimately, to create more and better jobs in Canada.

16. Given the acknowledged benefits of foreign investment, it follows that impediments to foreign investment should be kept as limited as possible. In this context, impediments can involve rejections of investment, or the imposition of conditions prior to permitting investment. But a requirement to endure an onerous, expensive or uncertain review process can also be an impediment to investment.

17. A review under the *Investment Canada Act* can be a demanding process. The review will assess the net benefit to Canada from the investment. This is a multi-faceted concept that takes into account the seven factors noted in Section 20 of the *Act*. In recent years, the review process has frequently led to foreign investors giving multi-year undertakings to maintain certain levels of employment or capital expenditures or other business activities as a condition for allowing the investment. Compliance with the review process can be time-consuming and expensive.

18. Further, trying to satisfy undertakings does come with a price tag. Many mergers and divestitures are undertaken with a view to achieving efficiencies. Sometimes, achieving those efficiencies can lead to staff realignments, redeployments or reductions. Sometimes achieving

¹ Consultation Paper, p. 2

those efficiencies can lead to changes in capital deployments and expenditures. Often, the exact shape of these efficiency-enhancing changes will not be known before the merger takes place. Where a foreign investor is required, as a condition to the approval of a merger with a Canadian company, to maintain employment levels and capital expenditures at particular levels, the merged entity can be forced into sub-optimal utilization of its business assets, and ongoing compliance costs. That in turn can lead to inefficiencies and, thus, reduced productivity.

19. Canada suffers from a lower level of national productivity as compared to the United States and many other developed trading partners. Indeed, that is one of the reasons behind the establishment of the Panel. One way in which the Panel could spur increased productivity is to recognize the costs to businesses inherent in the *Investment Canada Act* review process, and the need to provide undertakings, and to advocate a more retargeted test for reviewing foreign investment.

20. As the Panel considers such retargeting, it should bear in mind the April 2007 *Cabinet Directive on Streamlining Regulation*,² in which the federal government set the following objective for departments that are looking at industry regulation:

“limit the cumulative administrative burden and impose the least possible cost on Canadians and business that is necessary to achieve the intended policy objectives”

21. This objective makes good sense, and should be a guiding principle for the Panel as it considers the regulation of foreign investment.

22. The first point we would make is that foreign investment screening should address investments that pose reasonably identifiable risks to Canada. For example, we understand that the government wants to screen investments that raise national security concerns, or investment by foreign state-owned entities. We also understand the government has historically restricted investment in certain sensitive sectors of the economy, such as cultural industries. If these sorts of investments impose unacceptable potential risks, then they should be targeted and addressed as such. This might well be accomplished with sector specific legislation, examples of which currently exist in the telecommunications, broadcasting and airline sectors.

23. However, there are many other investment scenarios where screening achieves little of value, and may well be counter-productive to encouraging investment in Canada. In these situations, screening could be scrapped with little if any risk of adverse consequences. In

² See <http://www.regulation.gc.ca/directive/directive01-eng.asp>

particular, reviewing investments simply because the Canadian asset value exceeds \$295 million seems arbitrary and disconnected with any reasonably identifiable risk.

24. If, despite our recommendations for a more targeted approach to foreign investment screening, the current approach is retained, there are a number of changes that could be made to better focus the net benefit test while minimizing unnecessary regulation, including the following:

- (a) There should be no review where a non-Canadian acquires control of a Canadian business that is already controlled by a non-Canadian (other than acquisitions that raise national security concerns, or acquisitions by state-owned entities – assuming that the government pursues these as appropriate screening criteria). To the extent that the net benefit test has a purpose where a non-Canadian acquires control of a Canadian-controlled business, we are at a loss to see the value of a review where a change of control takes place for a business that is already non-Canadian controlled.
- (b) At present, transportation services (which include energy pipelines) are one of the sensitive sectors, with very low thresholds for review. However, under recent amendments to the *Canada Transportation Act*, the federal Cabinet can already screen mergers involving large transportation undertakings, whether domestic or transborder. Given these review powers, there is little reason to require a second review under the *Investment Canada Act*.
- (c) Energy pipelines are both regulated and immovable. Thus it is very difficult to see how a foreign investor can have any significant negative impact on Canada through an investment to acquire an energy pipeline. Accordingly, while there is justification for removing energy pipelines from the scope of review altogether, at the very least they should be removed from the list of sensitive sectors.
- (d) The review thresholds for the sensitive sectors should be raised from the very low levels that were established many years ago.
- (e) There Minister should have the ability to establish, by regulation, exemptions for classes of industries or classes of investments where the applicability of the *Act* is not warranted. This will allow the flexibility to deal with changing circumstances without the need for changes to the legislation.

25. Further, whether the net benefit test is retained, or whether a different test is selected, we urge the Panel to recommend the redrafting of the *Investment Canada Act*. The language in the current Act is very convoluted, reflecting changes that have been added to the legislation over the years. As a consequence, the statute is difficult to understand and interpret. We believe that a clearer, more logical and more modern approach can and should be developed.

Canada Transportation Act Review

26. Although the Panel has not specifically included the merger review process under the *Canada Transportation Act* (“CTA”) as part of its review, this review is very much related to the *Competition Act* merger review process.³ Accordingly, we felt it would be appropriate and relevant to submit comments on the CTA process.

27. As noted above, we see little value in subjecting investments involving energy pipelines to two reviews: one under the *Investment Canada Act* to assess net benefit; and another under the CTA to assess public interest. As between the two processes, our preference is for the CTA process, given its potentially reduced regulatory burden. However, if the *Investment Canada Act* test is to be retained for transportation services, then, as explained below, we recommend that that the CTA test be amended to exclude energy pipelines.

28. The two-stage CTA process described earlier was originally established following the Air Canada-Canadian Airlines merger in 1999. The CTA amendments mirrored the *ad hoc* procedure developed for that particularly contentious merger. Although originally restricted to airline transactions, the scope of the section was broadened in 2007 to include every large “transaction that involves a transportation undertaking”. We believe that this broadening was prompted by the possibility that one of the large Canadian railway companies might merge with a large US-based railway company.

29. We understand that the primary motivation behind sections 53.1-53.6 was to permit the federal cabinet to intervene where a transportation industry merger might lead to concerns about diminished service to small or remote communities and/or reductions in regional employment. The legislation allows the federal Cabinet to impose conditions for allowing the merger that address these (and any other) issues.

30. We are hard pressed to see how a merger in the energy pipeline business can trigger any significant concerns about service to communities and/or regional employment. Unlike airlines or railroads, energy pipelines cannot be moved from unprofitable routes and redeployed. In addition, energy pipelines are highly regulated, and any initiative to significantly alter service (or increase price) will invariably attract regulatory scrutiny and remedial action as necessary.

³ Under *Competition Act*, section 94(c), a merger that is approved under the CTA is exempt from challenge under the *Competition Act*. That’s said, as part of the CTA process, the Competition Bureau will examine the proposed merger and provide input to the CTA review.

Thus, a merger does not realistically threaten service levels. Moreover, because pipelines cannot be moved, the staff to operate and maintain the pipeline will be largely preserved in any merger. Indeed, it is difficult to think of any industry that is less prone to changes in service levels or employment following a merger than the energy pipeline industry.

31. Thus we believe that there are good reasons to remove transactions involving energy pipelines from the scope of the CTA review process, particularly in the event that these transactions must still be subject to the *Investment Canada Act* review process.

To Conclude

32. In 2006, the federal government published *Advantage Canada – Building a Stronger Economy for Canadians*.⁴ In it, the government recognized the impediments to foreign investment in the transportation sector, and their role in the international perception that Canada is not as hospitable a destination for foreign investment as it could otherwise be:

“Policy restrictions on foreign investment in Canada have contributed to our economy’s relative decline in foreign direct investment flows. According to the OECD, Canada has the highest level of explicit restrictions on foreign-equity ownership in the G7—primarily in the transportation and telecommunications sectors.”⁵

33. The energy pipeline business is a component of the transportation sector of the economy. Removing unnecessary restrictions on foreign investment will improve Canada’s image as a foreign investment destination, while at the same time helping Canadian energy pipeline businesses to operate more efficiently.

34. We have proposed a number of straight-forward changes to the foreign investment restrictions in the energy pipeline business. We believe that these changes will improve foreign investment screening in Canada, and we ask the Panel to give them careful consideration.

January 11, 2008

⁴ <http://www.fin.gc.ca/ec2006/pdf/plane.pdf>

⁵ *Ibid*, p. 87