QUIZ By Ryan Filson, partner, Maralynne Monteith, senior tax lawyer, and David Schulze, associate, WeirFoulds LLP

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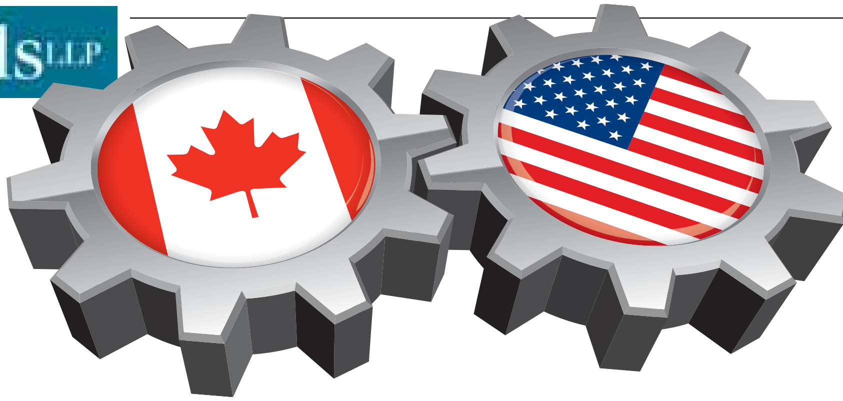

Cross-border acquisition

You get a call from Bud Richards, a Houston-based attorney who represents Tex Industries Inc., a Delaware corporation owned by an American individual who wants to acquire, for US$45 million, all of the shares of ABC Inc., an Ontario corporation that carries on a manufacturing business in Toronto. Bud wants you to help him structure, negotiate, paper, and close the deal.

1 Bud asks you for your views on the structure of the deal. He tells you that the CFO of Tex Industries has told him that for a previous acquisition they incorporated a Delaware subsidiary corporation to serve as the acquisition company and that he wants to do that for this deal as well. What do you recommend?

a) Tex Industries should buy the shares of ABC itself directly, but first it needs to register with the Ontario Securities Commission.
b) Tex Industries should incorporate a new Delaware subsidiary to use to buy the shares of ABC and that its name should be "Tex Industries (Canada) Inc."
c) Tex Industries should incorporate a subsidiary in a Canadian jurisdiction to use to buy the shares of ABC.

2 Bud recalls reviewing a client bulletin of your firm that mentioned the notice and review requirements under the Investment Canada Act that apply when a foreign corporation buys a Canadian business. Bud tells you that he assumes if he accepts your advice to establish a subsidiary in a Canadian jurisdiction to acquire the shares of ABC, then the Investment Canada Act does not come into play. What do you tell Bud?

a) He is right and the Investment Canada Act does not come into play.
b) Both the notice and review provisions of the Investment Canada Act apply to the transaction.
c) Notice provisions of the Investment Canada Act apply, but the review provisions do not.
d) The notice provisions of the Investment Canada Act apply, but further investigations will be required to determine whether the review provisions apply.

3 Bud calls you on a Sunday afternoon while you are walking the dog, and informs you that the vendor is asking whether the purchase price can be satisfied by the direct issue of US$45 million worth of shares of Tex Industries to the vendor without immediate tax consequences. He asks you whether this is possible. What do you tell him?

a) Possible.
b) Not possible.

4 Bud leaves you a voice message telling you that since the purchase price is calculated in U.S. dollars, Tex Industries wants to ensure that any judgment under the indemnities contained in the purchase agreement will be made in U.S. dollars, and that he has informed them that this would not be a problem. Is Bud correct?

a) Bud is correct.
b) Bud is not correct and Tex Industries cannot get the result it seeks.
c) Bud is not correct but Tex Industries can get the result it seeks.

5 It is the day before the closing, and you have spent the entire day on the phone and battling e-mail traffic. Late at night, as you are reviewing the documents for the governance transition of ABC, you realize that you have not yet received instructions on who are to be the directors of ABC going forward. You call Bud and he tells you that the owner of Tex Industries is a control freak and insists that he be the only director of ABC. Is there any problem with that?

a) No problem.
b) Problem.

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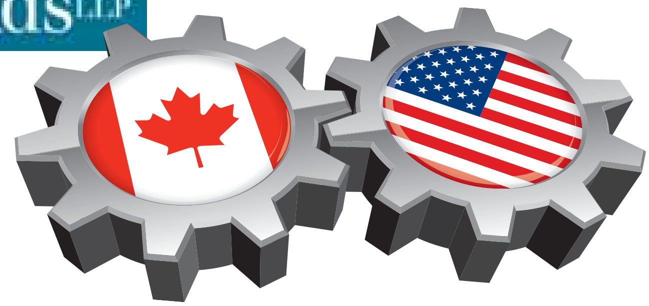
QUIZ ANSWERS



1 **(C)**
An acquisition company incorporated in a Canadian jurisdiction will typically be preferred when a non-resident corporation wishes to buy a Canadian business. By funding the amount of the purchase price first to the Canadian acquisition company, either as equity or part equity and part debt, then having it pay the price to the vendor, paid-up capital and/or a shareholders' loan is created in the acquisition company. Profits from the Canadian business may then be distributed to the foreign parent as a tax-free distribution of capital or loan repayment rather than a taxable dividend. Among other things, attention should be paid to applicable "thin capitalization" rules, the advantages and disadvantages of incorporating in various Canadian jurisdictions and the possibility of a post-closing amalgamation of the acquisition company and ABC.

2 **(D)**
The notice and review requirements of the Investment Canada Act must be considered whenever a non-Canadian investor directly or indirectly acquires control of a Canadian business. The fact that a Canadian acquisition company is used to acquire the shares of ABC is irrelevant since it is the nationality of the ultimate owners of Tex Industries that matters. Since Tex Industries is owned by an American individual, Tex Industries and its Canadian acquisition company would be considered to be non-Canadian. Accordingly, at the very least, the notification requirements of the Investment Canada Act would apply. Whether the pre-closing review requirements apply depends on whether the applicable financial thresholds established by the Investment Canada Act are exceeded. For acquisitions by investors which are "WTO investors" (which Tex Industries would be since it is owned by an American and the United States is a WTO member), the transaction, if completed in 2010, would be reviewable if the assets shown on the balance sheet of ABC at the end of its most recently completed fiscal year equal or exceed $299 million.

3 **(B)**
Section 85.1 of the Income Tax Act permits the disposition of shares (or other eligible property) on a tax-deferred basis where the consideration paid for those shares includes shares of the transferee corporation, but only where the transferee is a "taxable Canadian corporation" for the purposes of the Income Tax Act. As a Delaware corporation, Tex Industries would not qualify. The desired results may be achieved by using an exchangeable share structure and you should consider and canvass this option with Bud.

4 **(C)**
If the judgment is sought from an Ontario court, such judgment could not be given in U.S. dollars. Under s. 12 of the Currency Act (Canada), any monetary amount awarded in a legal proceeding in Canada must be in Canadian dollars. You should inform Bud of this requirement but you can also tell him that his client can get the result it seeks by including a "judgment currency" clause in the purchase agreement. Such a clause should provide that the amount of any judgment that would be awarded in Canadian dollars shall be converted to U.S. dollars with reference to an agreed-upon exchange rate and should contain a separate indemnity that requires the vendor to pay any shortfall resulting from a currency conversion at a date other than the date of payment.

5 **(B)**
Under s. 118(3) of the Business Corporations Act (Ontario), at least 25 per cent of the directors of an Ontario corporation must be resident Canadians, but where a corporation has less than four directors, at least one director must be a resident Canadian. Consequently, the American individual who owns Tex Industries cannot be the sole director of ABC going forward. You should have thought of this earlier and advised the client accordingly.

YOUR RANKING?

- **One or less correct:** *Might be time to brush up*
- **Two or Three correct:** *Not bad, but some further work needed*
- **Four correct:** *Very well done, but not perfect*
- **Five correct:** *Impressive*