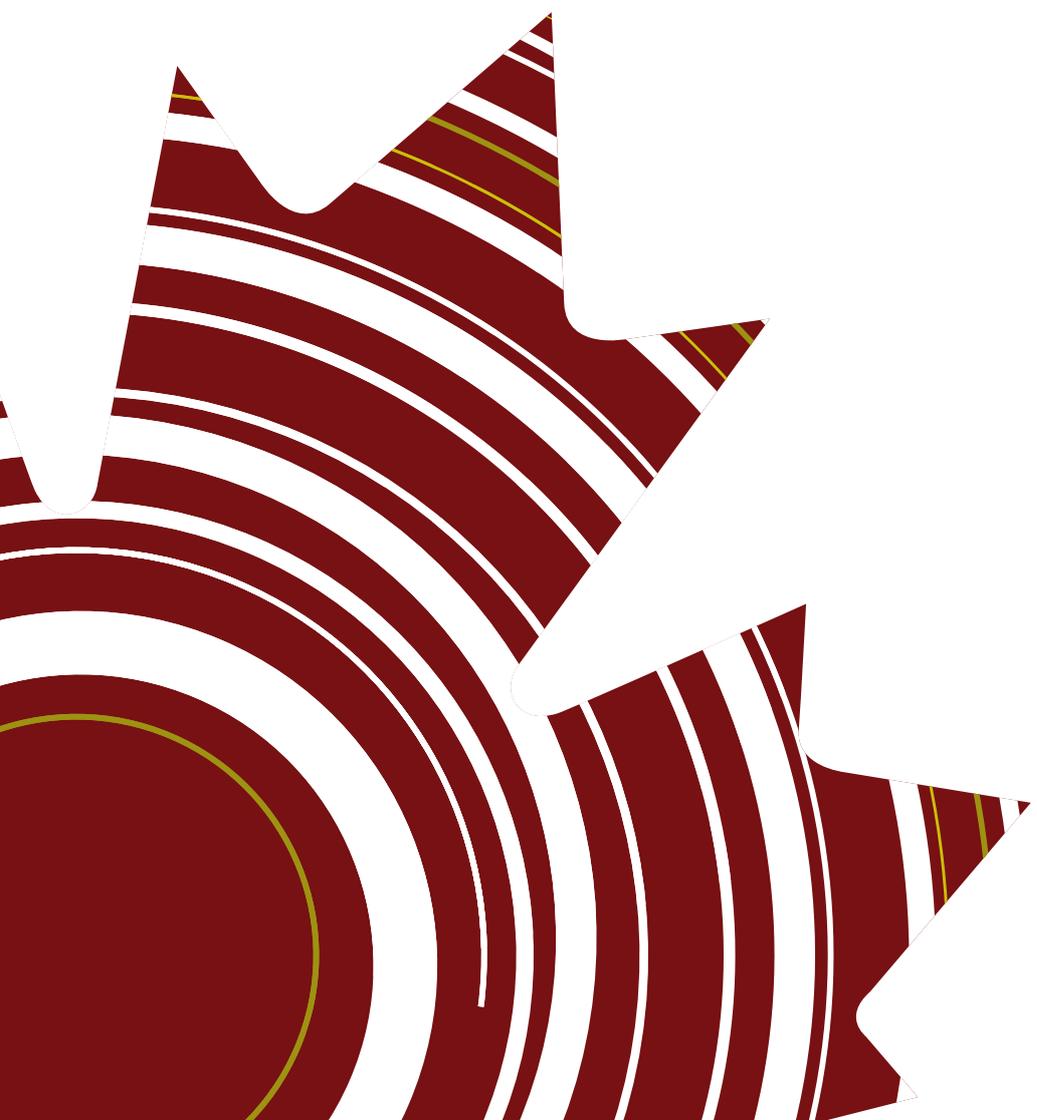




Office  
des transports  
du Canada

Canadian  
Transportation  
Agency

# Guide to Canadian Ownership and Control in Fact for Air Transportation



Canada 

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## Introduction

This Guide explains the Canadian ownership requirement for obtaining a licence to operate an air service from the Canadian Transportation Agency (Agency), and for maintaining such a licence.

It explains how the Agency interprets and applies the legal requirement for an air licence holder to be "Canadian" as defined in the [Canada Transportation Act](#) (Act).

This document is intended to support the Act, which is the definitive source for licence applicants and licence holders regarding the Canadian ownership requirement. Using this document and the examples it provides is not mandatory and nothing in this document supersedes the Act.

## Legislative Authority

The Agency is an independent, quasi-judicial tribunal and regulator that has, with respect to all matters necessary for the exercise of its jurisdiction, all the powers of a superior court.

The Agency oversees the very large and complex [Canadian transportation system](#), which is essential to the economic and social well-being of Canadians.

The Agency is responsible for ensuring all air carriers licensed to provide domestic air services meet the Canadian ownership requirements set out in the Act. These requirements state that air service licensees must be owned and controlled "in fact" by Canadians. The Agency uses business and other information to determine whether a licence holder or applicant is "in fact" Canadian. Those who wish to apply for a determination should also consult the [Application Process for Canadian Ownership Determinations](#).

The Agency conducts monitoring and enforcement activities to ensure ongoing compliance with licensing requirements.

## Definition of Canadian

As of June 27, 2018, "Canadian" is defined within [subsection 55\(1\) of the Act](#).

Refer to the Act for the complete definition, which includes:

- (a) a Canadian citizen or a permanent resident;
- (b) a government in Canada; and
- (c) a corporation;
- (d) limited partnership, partnership, proprietorship or other legal form of business enterprise where the following apply:
  - It must be incorporated or formed under the laws of Canada or a province (corporate entities only);
  - At least 51 percent of its voting interests must be owned and controlled by Canadians;
    - No single non-Canadian owns or controls, directly or indirectly, more than 25 percent of the voting interests in that corporation (either individually or in affiliation with another person). In addition, no more than 25 percent of the voting interest in a Canadian carrier is owned by foreign air carriers (either individually or in affiliation); and
  - It must be controlled in fact by Canadians.

Failure to meet these criteria will result in being considered non-Canadian.

*Note: Where the ownership of an entity resides with one or more corporations or other entities, the definition of Canadian will also be applied to those entities. If they are, in turn, owned by other entities, the Agency must determine who controls the company up to the top of the ownership chain, applying the definition of Canadian at each step.*

## **Consequences of Failing to Demonstrate Canadian Status**

If the Agency determines that a new licence applicant doesn't meet the Canadian ownership requirement, the licence application will be denied. If the Agency determines that an existing licensee no longer meets the requirement, the Agency must suspend or cancel the licence.

## Further Details

See [Annex A](#) for additional information about demonstrating that your corporation or other business enterprise is owned by Canadians.

See [Annex B](#) for the principles that guide the Agency's determination of "control in fact."

See [Annex C](#) for the factors the Agency considers when determining "control in fact."

See [Annex D](#) for examples of the Agency's previous Canadian ownership determinations.

## **Annex A: Canadian Ownership Requirements**

There are three requirements that must be met to be considered Canadian and therefore to obtain or maintain an air service licence:

1. [Incorporation or Formation Requirement](#);
2. [Voting Interest Requirement](#); and
3. [Control in Fact Requirement](#).

These three requirements are detailed below.

### **Requirement No. 1: Incorporation or Formation Requirement**

For a corporation, partnership, proprietorship or other form of business enterprise to be Canadian, it must be incorporated or formed under the laws of Canada or one of its provinces.

### **Requirement No. 2: Voting Interest Requirement**

For an enterprise to be considered Canadian, at least 51 percent of the voting interests need to be both owned and controlled by Canadians.

- "Voting interests" means voting securities and the votes assigned to those securities.
- "Owned by Canadians" means the securities are owned on a beneficial ownership basis by Canadians; it is not enough for them to be registered to Canadians.
- "Controlled by Canadians" means the votes attached to the securities should be exercisable by their Canadian beneficial owners.

No single non-Canadian may hold more than 25 percent of the voting interests, directly or indirectly, whether individually or in affiliation with another person. In addition, for any non-Canadian shareholders that have the authority to provide an air service in any jurisdiction (i.e. whether in Canada or abroad), the sum total of their voting interests cannot exceed 25 percent, either individually or in affiliation with another person.

## Affiliation

The term "affiliation" as it concerns two or more persons who may act together to exercise their voting interests, is defined in [subsection 55\(2\)](#) of the Act. Refer to the Act to see the complete list of circumstances in which corporations, partnerships, or sole proprietorships are considered "affiliated," which includes:

- one of them is a subsidiary of the other,
- both are subsidiaries of the same corporation, or
- both are controlled by the same person, corporation, or subsidiary of a corporation.

Also, if two corporations are affiliated with the same corporation at the same time, they are deemed to be affiliated with each other.

Note that the Act provides extensive detail on "affiliation," including the circumstances in which a corporation is controlled by a person other than Her Majesty in right of Canada or a province. Refer to the [Act](#) for the complete information.

## Publicly traded corporations

For an entity that lists its securities on a publicly-traded stock exchange, the percentage of voting interests owned by Canadians can be subject to constant fluctuations. To ensure that the entity continues to meet the ongoing requirements to be Canadian, the Agency may require the entity to put in place one of the following:

- a security constraint and control system, which is a system that restricts any purchase or transfer of the corporation's securities if it would result in a breach of the voting interest requirement; or
- a variable voting system. This is when non-Canadians are allowed to hold only variable voting shares. This results in the voting interest requirement being respected, because when the percentage of the variable voting shares exceeds the maximum allowable percentage of the total voting shares, the vote attached to each variable voting share automatically decreases to ensure that the maximum allowable threshold isn't exceeded.

## Requirement No. 3: Control In Fact Requirement

### Overview

To be Canadian, the company needs to be "controlled in fact" by Canadians.

Control in fact (also known as *de facto* control) differs from control in law (also known as *de jure* or legal control). Control in law is generally shown by owning enough shares to carry the right to a majority of votes. Control in fact goes beyond control in law as it includes the ability to exert control by any direct or indirect influence.

Although the term is not defined in the Act, the Agency considers control in fact to be:

- the power, whether exercised or not, to control the strategic decision-making activities of an enterprise and to manage and run its day-to-day operations.

Those who may have the power to influence a company's decisions can include minority owners, designated representatives, financial institutions, employees and others. They may use their influence either positively or negatively. For example, they may demonstrate a *positive* influence by requiring positive approval when a decision needs to be made. Conversely, *negative* influence could be the ability to veto a decision. Either way, the influence needs to be dominant or determining to be considered "control in fact."

Determining who has "control in fact" is a question of fact. The Agency evaluates this on a case-by-case basis, as each case is unique. The principles that the Agency follows when determining "control in fact" are listed at Annex B. The factors that the Agency considers are shown at Annex C. All managerial, financial and operational air carrier relationships (or proposed relationships) must be considered before making a determination.

Ownership structures with little or no involvement from non-Canadians do not normally require extensive analysis. Nevertheless, licence applicants and existing licence holders should take note of the "control in fact" issues concerning joint ventures and ownership by proxy.

## Joint Ventures

Applicants and licensees who enter into arrangements or joint ventures with non-Canadian air carriers should carefully consider whether this could result in joint or entire control by the non-Canadian. Such arrangements typically involve collaboration or strategic business decisions around matters like:

- prices,
- routes,
- schedules,
- capacity,
- ancillary services, and
- revenue and cost sharing.

The Canadian licensee must always be in a position to control its decision-making. They must be free of any dominant and determining influence from the non-Canadians participating in the joint venture. Otherwise, the non-Canadian could be found to be in a position of control, thereby resulting in the Canadian licensee no longer complying with the requirement to be Canadian.

*For additional information regarding joint ventures, please contact:*

National Air Services Policy Directorate  
Air Policy Group  
Transport Canada  
Place de Ville, Tower C  
Ottawa, Ontario  
K1A 0N5

Telephone: 613-993-7284 or 1-800-305-2059

Fax: 613-991-6445

Website: [www.tc.gc.ca](http://www.tc.gc.ca)

Email: [TC.natair-aernat.TC@tc.gc.ca](mailto:TC.natair-aernat.TC@tc.gc.ca)

### Ownership by Proxy

When a non-Canadian shareholder who makes a monetary investment transfers its corresponding voting interest to a Canadian who otherwise has only a nominal

investment in the applicant, the Agency will consider the substance over the form of the proposal. Business structures that violate the spirit of the control in fact requirement by using a Canadian proxy to hold the voting interests of a non-Canadian investor will likely not meet the requirement.

## **Annex B: General Principles for Determining "Control in Fact"**

### **All the facts are weighed together**

Normally, no single factor dictates whether control in fact is held by Canadians. The Agency considers and weighs all facts together to make a determination. There is no single objective test that can be relied upon to determine where control in fact lies. Judgment is required to evaluate the facts of each case.

### **Control does not need to be exercised**

Control does not need to be exercised for a person to have control in fact. When the individual has the ability to control, whether they use it or not, they are considered to have control in fact.

### **Control can reside with different individuals**

Control in law and control in fact can reside in the hands of different individuals or groups of individuals. Control in fact may exist even without ownership of any voting securities.

### **Joint Control**

Where an air carrier is controlled jointly by Canadians and non-Canadians, it is not considered to be Canadian.

## Annex C: Factors Considered in Determining "Control in Fact"

To determine who has "control in fact," the Agency assesses every applicable factor. This includes whether that factor, individually or in combination with others, provides any non-Canadians with:

- direct means to control the company (e.g., formal voting or other rights), and/or
- indirect means to control the company (e.g., ability to exert influence through their investment in the company or through any other means).

The Agency also considers the intent and ability of the non-Canadian(s) to exercise control over the company, particularly where control is obtained through indirect means.

Below is a list of factors considered by the Agency. This list is not exhaustive and is not ranked in any particular order of priority. There may be other factors depending on the situation.

Following the list there is more information about each factor. This includes information about risky situations that can emerge, and how licence applicants and licence holders can reduce the risk of receiving a negative "control in fact" determination.

### *Note: Importance of Risk Mitigation*

*Unless an applicant or licence holder takes steps to mitigate risks, situations identified as "high risk" will likely result in a negative determination. Situations identified as "medium risk" may result in a negative determination on Canadian ownership if they cause a non-Canadian's influence to be dominant and determining, whether on their own or in combination with other factors.*

*A situation identified as being risky when combined with other factors will not necessarily result in a negative Canadian ownership determination, but may be a contributing factor to a negative determination.*

## **LIST OF FACTORS:**

### **Corporate Governance Factors**

1. Board of Directors
2. Officers
3. Shareholder and Board of Directors' meetings

### **Shareholder Rights Factors**

1. Veto rights
2. Security rights, options, and warrants
3. Rights of first refusal/Pre-emptive rights
4. Power to wind up the company

### **Risks and Rewards Factors**

1. Risks and benefits
2. Concentration of voting interests

### **Business Affairs and Activities Factors**

1. Debt
2. Guarantees
3. Lease of assets
4. Financial strength and business activity
5. Management agreements
6. Operational or service agreements
7. Charterer/air carrier relationship

## **ADDITIONAL INFORMATION AND RISK-REDUCTION STRATEGIES:**

### **Corporate Governance Factors**

#### **1. Board of Directors**

The board of directors is elected by the shareholders to govern and manage the affairs of the corporation. The following conditions must be met for control in fact to reside with Canadians:

- Canadian shareholders must have the right to appoint no less than half of the board of directors.
- No less than half of the board members must be Canadian.

Generally, the same principle applies to board members sitting on individual board committees.

The Agency recognizes major investors will normally expect to have board representation reflective of their voting interest. Given that non-Canadians can hold up to 49 percent of voting interests (subject to the conditions prescribed in subsection 55(1) of the Act), the number of board members representing Canadians and non-Canadians could be equal.

#### *Risk Condition (Risk Level: High)*

Non-Canadian control in fact is indicated when:

- The board representation of the non-Canadian investors is disproportionately high compared to the voting interests held; or,
- The majority of board members are non-Canadians, regardless of who nominated them.

#### *Risk Mitigation*

If there are an equal number of Canadian and non-Canadian board members, there must be tie-breaker provisions in favour of the Canadian board members for control in fact to reside with Canadians.

## 2. Officers

Officers of a corporation serve at the pleasure of the board of directors. They are entrusted with the day-to-day responsibility of running the corporation. Officers normally do not have the ability to exercise control in fact. Officers do not need to be Canadian for the corporation to be considered Canadian by the Agency. However, control in fact implications could arise if officers have a relationship with non-Canadian shareholders that provides a means for the non-Canadians to exert influence over the operations of the air carrier.

### *Risk Condition (Risk Level: High)*

When the officers of the company have a fiduciary duty to, or are otherwise beholden to, the non-Canadian board members and/or the non-Canadian shareholders, this will be interpreted as indicating non-Canadian control in fact.

### *Risk Mitigation*

Officers must not be in a position to exercise control in fact. To avoid any ambiguity in this regard, they should be at arms' length from any non-Canadian shareholders of the business.

## 3. Shareholder and Board of Directors' Meetings

A quorum indicates the minimum number of members that must be present at a meeting for the meeting to be considered valid. The Agency generally expects a corporation's quorum provisions to require:

- no less than half of the shareholders or directors present at a shareholder or board of directors meeting be Canadian; and
- no less than half of the members at a board of directors meeting have been appointed by Canadian shareholders.

### *Risk Conditions (Risk Level: High)*

Non-Canadian control in fact is indicated when:

- Less than 50 percent of the shareholders or directors present at a meeting are Canadian;
- Less than 50 percent of the members at a board of directors meeting have been appointed by Canadian shareholders; and/or
- Non-Canadians can cast the deciding vote in a tie-breaker situation.

### *Risk Mitigation*

For shareholder meetings, when there is an equal number of Canadian and non-Canadian shareholders present, there must be a provision to ensure the Canadian shareholders always have the ability to cast the deciding vote.

For board of directors' meetings, when there is an equal number of Canadian and non-Canadian board members present, there must be a tie-breaker provision to ensure the director allowed to cast the deciding vote is a Canadian appointed by Canadian shareholders.

## Shareholder Rights Factors

### 1. Veto Rights

Veto rights allow a shareholder or director to reject or veto a resolution in spite of having majority assent. Veto rights come in many different forms. For example, the affirmative vote required of a specific shareholder or director for a resolution to pass is a type of veto right. The requirement for unanimous shareholder or director approval is another.

Generally, there are no Canadian ownership implications associated with non-Canadian shareholders and their designated directors having veto rights to protect minority shareholder investment.

### *Risk Conditions (Risk Level: High)*

A significant accumulation of restrictions could indicate that control in fact resides with non-Canadians. The risk increases when these restrictions are combined with other means of exercising influence.

Veto rights which are comprehensive and broad could indicate that control in fact resides with non-Canadians. This includes veto rights regarding:

- the selection, removal and remuneration of the company's officers and executives;
- the approval of the annual business plan; and
- changes to airline operations of the carrier.

### *Risk Mitigation*

As a general rule, veto rights that do not pose any control in fact implications are limited to matters outside the scope of the day-to-day operations of the air carrier. Veto rights that do not pose control in fact concerns must not have any impact on the operational, marketing and financial decisions made on an ongoing basis. For example, matters not normally considered to show control in fact include veto rights regarding:

- the payment of dividends;
- the sale or transfer of major assets;
- the incursion of large capital expenditures;
- entry into large and significant agreements, mergers, amalgamations and large business purchases;
- amendments to incorporation documents; and
- the issuance or redemption of capital stock.

The above kinds of veto rights could represent normal and acceptable provisions to protect the minority shareholders' investment.

The Agency will view control in fact as not residing with Canadians when the non-Canadian shareholders have the ability to veto matters that could be viewed as being related to day-to-day operations, or matters that do not pose a significant and demonstrable risk to the non-Canadian shareholder.

## **2. Security Rights, Options and Warrants**

The individual rights, privileges, restrictions and conditions attached to each class of security are relevant when evaluating control in fact. In addition to voting rights, there are other rights that could influence where control in fact lies. These include:

- redemption rights (right to force the corporation to buy back securities);
- conversion rights (right to exchange one security for another); and
- buy-out rights (right to acquire another person's interest in a security).

The same applies to rights associated with warrants and options that provide the right of conversion or the right to purchase securities of the corporation at specified prices. This particularly applies in cases where the holder has the right to convert from a non-voting to a voting interest.

*Risk Conditions (Risk Level: Risky When Combined With Other Factors)*

When a non-Canadian investor is the sole holder of the right or of a disproportionate amount of the rights, it indicates control in fact resides with non-Canadians, particularly when the rights can be exercised at prices below the market price.

*Risk Mitigation*

To ensure that control in fact resides with Canadians, the aforementioned rights must be exercisable at fair market value and be reciprocal to all of the shareholders.

### **3. Rights of First Refusal/Pre-emptive Rights**

Rights of first refusal and pre-emptive rights are contractual rights. These exist when a person has an opportunity to purchase securities or other assets from the owner on specified terms prior to their being offered for sale to a third party. All shareholders would normally have these rights in proportion to holdings for specific securities purchases.

If the potential purchase of securities or other assets could result in the air carrier no longer being Canadian, the proposed transaction will generally be considered to cause the loss of Canadian status. An additional provision would need to be inserted to ensure that no purchase of this type can proceed and be completed unless the air carrier remains Canadian.

*Risk Conditions (Risk Level: Risky When Combined With Other Factors)*

The Agency will view control in fact as not residing with Canadians when:

- rights of first refusal or pre-emptive rights are exercisable below fair market value and reflect terminology that unilaterally benefits the non-Canadian shareholder;
- rights concerning the purchase of specific securities are not reciprocal between the Canadian and the non-Canadian shareholder(s) and/or are disproportionate with the shareholdings in favour of the non-Canadian, or
- rights are not reciprocal to both Canadian and non-Canadian shareholders (i.e., are in favour of the non-Canadian shareholders only).

### *Risk Mitigation*

If rights of first refusal or pre-emptive rights reflect typical terms and are exercisable at fair market value, the Agency will generally view such rights as a means to protect shareholders from situations such as undesirable takeovers.

Rights concerning the purchase of specific securities should be held by all shareholders and be commensurate with the shareholdings.

## **4. Power to Wind Up the Company**

An individual shareholder or lender with the power to close down the company by calling loans payable on demand may be in a position to exercise control in fact over the affairs of an air carrier. This is because loans may contain standard covenants that:

- restrict how the funds may be used (e.g., the funds can only be used for a specific business purpose);
- restrict how the business may disburse funds (e.g., restrict the payment of dividends when the business is not profitable); and
- require that certain conditions be maintained (e.g., ensuring the business remains solvent and complying with any applicable legislation).

The breach of such covenants typically provides the lender with the right to call a loan payable and/or force the winding up of the business. This winding up may be carried out through sale, liquidation or otherwise. If loans contain standard

commercial loan covenants that are reflective of an arm's length lending relationship, where a lender is reasonably protecting itself from default, this is not indicative of control in fact over the company's affairs. For example, a bank does not normally control a company, even though it might have the ability to call a demand loan, due to a material breach of covenants leading to the winding up of the company.

### *Risk Conditions (Risk Level: High)*

If a non-Canadian's ability to influence the winding up of a company is so great that it poses an ongoing threat that effectively forces the Canadian board members to comply with the ongoing strategic business decisions of the non-Canadian board members, the Agency will consider this to be dominant and determining influence by the non-Canadian. This will result in the Agency finding that control in fact does not reside with Canadians.

For example, the breach of any covenant (within a very exhaustive list of items that encompass day-to-day strategic decision-making matters) that could trigger the wind-up process would be viewed as a condition that poses an ongoing threat.

### *Risk Mitigation*

To ensure that a loan does not create a control in fact concern, the loan agreement should:

- only contain standard commercial terms and covenants that protect the lender from the usual lending risks, and
- not interfere with typical day-to-day operations or strategic business decisions.

## **Risks and Rewards Factors**

### **1. Risks and Benefits**

The Agency generally expects that the parties that assume the majority of the risks and are entitled to the majority of benefits related to the air carrier's operation are also the parties with the ability to exercise control in fact. Risks are generally tied to the level of economic interest in the air carrier, including:

- investment in its voting, non-voting and debt securities;
- commitments for future investment; and
- any guarantees that may have been provided.

Benefits generally come from an entitlement to share in the expected profit of the company. They can also come from revenues that result from aircraft lease, managerial services, royalty and other similar agreements. However, as this is not always the case, the evaluation of other factors specific to each case is critical to a determination.

#### *Risk Conditions (Risk Level: Medium)*

Non-Canadian control in fact may be indicated if the disparity between the proportion of voting interests and the level of capital investment by the non-Canadian investor increases. The non-Canadian investor will be expected to ensure it has levers in place to minimize its risk while maximizing its return on investment. Consequently, applicants should expect applications of this nature to receive a high degree of scrutiny.

Non-Canadians whose commitments for future investment are necessary for the ongoing survival of the business raise control in fact concerns. This is because the business is dependent upon the non-Canadian investor, who is assuming the greatest risk. The higher the level of risk, the higher the expected reward. This can lead to situations where the non-Canadian gains dominant and determining influence.

A similar situation arises when the business is dependent upon the guarantee of the non-Canadian investor to finance the business. The reliance on non-Canadians for normal business financing activities strongly indicates non-Canadian control in fact.

#### *Risk Mitigation*

There may be situations where a non-Canadian invests a significantly higher proportion of capital than the Canadian shareholders, but accepts a disproportionately lower voting share in order to comply with the maximum permitted voting interest for non-Canadians under the Act. In these situations, applicants should ensure any agreements are structured

to limit the non-Canadian to a more passive role in the business and to have only those rights necessary to protect its investment in a minority voting situation.

To avoid raising control in fact concerns, the long-term viability of the business should not be entirely dependent on receiving future investment by the non-Canadian investor.

With respect to guarantees, applicants should ensure they are not dependent upon a non-Canadian investor to guarantee their debt. This is to avoid any concerns that the non-Canadian is assuming the majority of the investment risk.

## **2. Concentration of Voting Interests**

The concentration of voting interests owned and controlled by Canadians versus non-Canadians can show where control in fact lies. Situations can arise where the majority of the voting interests—while owned and controlled by Canadians—are dispersed among a large number of unrelated individuals each holding a small interest. In this situation, if a non-Canadian or a group of non-Canadians holds a concentration of the voting interests, it could indicate Canadian shareholders are not able to exercise control in fact.

As defined in the Act, the voting interest requirement contains restrictions to ensure that affiliated non-Canadians collectively do not hold more than 25 percent of the total voting interests. The Agency will verify that this restriction is being respected. It will also scrutinize the ownership structure to see whether a relatively small number of unaffiliated non-Canadians hold a disproportionate amount of the voting interests (versus a large number of unrelated Canadian shareholders with relatively small shareholdings).

### *Risk Conditions (Risk Level: Medium)*

Non-Canadian control in fact may be indicated when there are multiple Canadian shareholders and only one or two non-Canadian shareholders exist. In these situations, the non-Canadian shareholder(s) may try to create a strategic voting bloc. By aligning themselves with one or more of the Canadian shareholders, the non-Canadian shareholder(s) could instruct votes. While not necessarily indicating control in fact by the non-Canadian

shareholder(s), the Agency will consider whether the non-Canadian shareholder(s) could be in a position to influence the votes of a Canadian shareholder to vote.

### *Risk Mitigation*

Applicants should ensure that the ownership structure is designed in such a way to avoid situations where a small group of affiliated and/or unaffiliated shareholders could form a voting bloc.

## **Business Affairs and Activities Factors**

### **1. Debt**

Debt transactions executed in the normal course of business activity do not normally raise any control in fact concerns. However, there could be control in fact implications in cases where the monetary size of the debt is significant to the other sources of financing. Concerns may be raised if there is reason to believe the intent for the transaction extends beyond typical financing. In these cases, the specific terms of the agreements would be of particular significance. The Agency would scrutinize the following in particular:

- Provisions that provide for the debt to be converted into voting securities of the company; and
- Restrictions or veto rights that go beyond what would normally be expected from a passive lender.

The nature of the debt holders and their relationship to the air carrier would be equally important. A non-Canadian financial or lending institution would not normally have an interest in managing or influencing the direction of an air carrier. This would not raise concerns regarding control in fact. However, a non-Canadian air carrier or other non-Canadian investor might have different intentions. These could magnify indicators of control in fact.

### *Risk Conditions (Risk Level: Medium)*

Non-Canadian control in fact may be indicated when the applicant relies on substantial debt financing provided by a non-Canadian who is not at arm's length from the non-Canadian shareholder.

### *Risk Mitigation*

Commercial loans that are not guaranteed by non-Canadians and that are obtained from arm's length lenders such as financial institutions for the purpose of financing business operations do not raise control in fact concerns.

Loans obtained from non-Canadian lenders who have a relationship with the applicant, such as a shareholder of the business, should be based on commercial lending terms that reflect an arm's length relationship to avoid raising control in fact concerns.

Any restrictive covenants must be strictly limited to standard commercial lending clauses limited to the protection of a creditor. These covenants cannot interfere in any way with the normal day to day operations of the business.

## **2. Guarantees**

A debt or loan guarantee is a promise by a person or an entity to assume a debt obligation in the event of non-payment by the borrower. When a non-Canadian provides the guarantee, control in fact considerations will include:

- the monetary size,
- the terms,
- the borrower's level of dependence, and
- the guarantor's intent.

### *Risk Conditions (Risk Level: Medium)*

Non-Canadian control in fact is indicated when an applicant is dependent upon a guarantee from a non-Canadian (e.g., a non-Canadian shareholder) to obtain or secure debt financing.

### *Risk Mitigation*

To avoid raising control in fact concerns, lending agreements must not contain any means for a non-Canadian guarantor to exercise its influence over the direction of the air carrier.

### **3. Lease of Assets**

The operation of an air service is a capital-intensive business. It often involves the purchase or lease of aircraft, hanger space and other key assets.

An agreement with arm's length parties for the use of assets at market terms would not normally indicate control in fact. Control in fact is not normally indicated even in cases where a high concentration of assets is being provided by one or more parties.

Control in fact may be indicated when an air carrier is dependent on a specific party to provide assets that cannot be obtained practically or financially elsewhere. In these cases, the Agency would consider the following:

- The nature of the relationship;
- The terms of the agreement; and
- The intent or ability of the lessor party to influence the affairs of the air carrier.

### *Risk Conditions (Risk Level: Medium)*

Control in fact concerns are raised when an applicant is dependent upon a non-Canadian who is not at arm's length from the non-Canadian shareholder to provide the aircraft. Control in fact concerns are also arranged when the terms of the arrangement contain provisions that allow the non-Canadian to exercise dominant and determining influence. An example of such influence would include any provision that covers day-to-day business decisions such as aircraft routes and flight frequency.

### *Risk Mitigation*

To avoid raising control in fact concerns, asset lease agreements involving non-Canadians should reflect standard terms associated with an arm's

length business relationship. If the lease agreement contains any standard restrictive covenants, they must be limited to provisions that are intended to protect the assets and credit risk to the lessor. Covenants cannot infringe upon the normal day-to-day or strategic business operations of the applicant.

#### **4. Financial Strength and Business Activity**

The comparative financial strength, business activity and relevant expertise of individual shareholders can indicate which shareholders exercise influence and control in fact over an air carrier. This is especially true when dealing with shareholders who are non-Canadian air carriers. In these situations, the nature of the non-Canadian shareholders equity investment is important. This could be a passive investment from a private equity investment firm, or an investment from a business with extensive knowledge and experience in the aviation sector that intends to be active in the business operations. Also important is the ability or the need for the non-Canadian shareholders to offer financial, managerial and operational assistance to the air carrier.

The greater the financial ability and airline business acumen of the individual Canadian shareholders, the less likely a large, non-Canadian investor would be viewed as raising any control in fact concerns.

##### *Risk Conditions (Risk Level: Risky When Combined With Other Factors)*

Control in fact concerns are raised when non-Canadian shareholders have the ability to exercise dominant and determining influence through their greater experience and business knowledge in the aviation sector.

##### *Risk Mitigation*

If an applicant can show that the Canadian shareholders have the aviation sector experience and expertise necessary for the operation of the business, this reduces concerns that the non-Canadian investors may use their business experience as a means to exercise control in fact.

## **5. Management Agreements**

Management services can be an essential component of an air carrier's business strategy. However, some management agreements could result in an independent entity managing the affairs of the air carrier. Payment should be based on services rendered. Any incentive bonus should represent a small percentage of the overall fee and the overall corporate profit.

### *Risk Conditions (Risk Level: Medium)*

Control in fact concerns are raised when the person providing management services is a non-Canadian shareholder or is affiliated with a non-Canadian shareholder.

Non-Canadian control in fact is indicated when an agreement does not allow the board of directors of the applicant to have:

- the unilateral right to accept or reject any advice given by the manager; or
- the right to terminate the agreement.

### *Risk Mitigation*

When management services are provided by a non-Canadian, the following terms should be met to avoid any control in fact concerns:

- The manager should be an independent contractor in the airline management business rather than an employee of a carrier or an affiliate of any non-Canadian shareholders;
- The board of directors should have the authority for all major decisions; and
- The board of directors should have the right to terminate the management agreement (on reasonable notice and terms) if they are not satisfied with the manager's performance.

## **6. Operational or Service Agreements**

Operational or service agreements for the provision of services to the air carrier can sometimes include the provision of an aircraft with flight crew, maintenance

activities, ground-handling services, and reservations and other computer-based services.

Non-Canadian control in fact is indicated when:

- the service provider handles operations of the air carrier; or
- the service provider fee is based directly or indirectly on the profit or loss of the air service.

*Risk Conditions (Risk Level: Medium)*

Control in fact concerns are raised when a non-Canadian management services provider performs many or all of the major operational activities of the air service business on its behalf. This includes:

- managers who are not at arm's length from a non-Canadian shareholder; and
- any non-Canadian shareholders or their affiliates acting in the capacity of a management services provider.

*Risk Mitigation*

When an air carrier contracts a non-Canadian service provider to perform the day-to-day operational functions of the air carrier, or enters into an arrangement (such as a joint venture) with a non-Canadian air carrier, all major decisions (such as approval of the business plan, incursion of large debt and operational expansion) should remain with the air carrier's board of directors in order to avoid any control in fact implications. The air carrier must also be entitled to the profit and be responsible for any loss associated with the operation of the air service.

## **7. Charterer/Air Carrier Relationship**

A charterer leases the full aircraft capacity from the air carrier, which it then sells to the public, typically through a travel agent. Charterers fall under provincial jurisdiction. They are not subject to the Canadian ownership and control requirement of the Act. Charterers have the ability to enter into contracts with air carriers that dictate items such as the level of service, routes and schedules.

Normally, these charterer/air carrier relationships do not pose any federal control in fact implications.

*Risk Conditions (Risk Level: Medium)*

Control in fact concerns are raised when:

- a non-Canadian charterer assumes the role and responsibility of the air carrier, as shown by the assumption of the risks and entitlement to the benefits relating to the air carrier's operations;
- the air carrier intends to conduct business with only one charterer; or
- the air carrier does not have an arms' length relationship with the non-Canadian charterer.

*Risk Mitigation*

Charterer/air carrier relationships do not pose control in fact concerns on the air carrier if:

- the air carrier assumes the risks and benefits relating to the air carrier's operations; and/or
- the charterer, if non-Canadian, is in an arm's length relationship with the carrier.

## Annex D: Examples of Previous Canadian Ownership Determinations

Below are links to some of the Agency's previous public decisions that specifically address the requirement to be Canadian. There is particular emphasis in this list on decisions discussing the voting interest and control in fact requirements.

This list is not exhaustive, and is not presented in any particular order of priority. This list will be updated periodically.

- Decision No. [297-A-1993](#) (Canadian Airlines Decision)
- Decision No. [299-A-2000](#) (Air Canada Decision)
- Decision No. [511-A-2004](#) (ACE Decision)
- Decision No. [10-A-2010](#) (Sunwing Airlines Decision)
- [Public redacted version of October 6, 2010 Confidential Decision](#) (CHC Helicopters Canada Decision)
- Decision No. [32-A-2012](#) (Thunderhook Air Charter Services Decision)
- Decision No. [359-A-2012](#) (Cougar Helicopters Decision)
- Decision No. [423-A-2012](#) (Sunwing Airlines Inquiry)
- Decision No. [493-A-2012](#) (Alpine Helicopters Decision)