Implications of U. S. MNCs for Canada and its Economic Policies in the Twentieth Century

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Abstract
This study examines the U.S. Multinational Corporations implications and Canadian economic policies during 20th century. It discusses how the U.S MNCs put a heavy drain on the Canadian economy and what the Canadian government took different steps to counter them. The Canadian economy is heavily dominated by multinational corporations, which are nearly concentrated in all the sectors of its economy. This ‘undue’ foreign control caused a lot of balance of payments problem and developed a truncated industry in Canada. To overcome these problems the government appointed different commissions which submitted their recommendations to increase the national employment levels, diversity of employment, technological advancement, competitive strength, export volumes and reduce imports. In the light of these recommendations, the government adopted different policies to achieve its national economic goals. It gave taxation concessions to the local periodicals and publications to make them competitive with the U.S MNCs. Trudeau government announced National Energy Program (NWP) which put ownership restriction on the foreign MNCs and put them at disadvantageous position compared to Canadian MNCs. The Canadian government also introduced FIRA (Foreign Investment Review Agency) which was a screening body for the foreign investment and which caused a lot of resentment among foreign investors.

Keywords: Canada; U.S.; Multinational Corporations; Foreign Direct Investment; International Political Economy

I. Introduction
This study examines the U.S. Multinational Corporations implications and Canadian economic policies during 20th century. The Canadian economy is heavily dominated by multinational corporations, which are nearly concentrated in all the sectors of its economy. In 1970s, these MNCs control 65 percent of combined manufacturing, mining, petroleum and natural gas, 98 percent of rubber industry, 82 percent of chemicals, 46 percent of pulp and paper, 61 percent of agricultural machinery, 74 percent of the electrical apparatus industry, 59 percent of transportation equipment, and 96 percent of the automobile and parts industry (Dhawan, 1981: 422). This undue foreign control caused a lot of balance of payments problem and developed a truncated industry in Canada. To overcome these problems the government appointed
different commissions which submitted their recommendations to increase the national employment levels, diversity of employment, technological advancement, competitive strength, export volumes and reduce imports. In the light of these recommendations, the government adopted different policies to achieve its national economic goals.

II. The Nature of Foreign Investment in Canada

Canada has two types of foreign investment: direct investment and portfolio investment. In the foreign direct investment, the investor gets control over the decision-making matters of the invested-in unit proportionate to his equity. Moreover, in this investment the capital may be contributed in different forms like research development, technological knowledge and managerial skill (Dunning, 1972: 11-12). In the portfolio investment, the equity may be in the form of governmental loans, loans by international agencies, borrowing via bonds and short term loans. The major difference between the direct investment and the portfolio investment is that in the latter the investor has no control over the management of the invested-in unit. Secondly, the profit in the direct investment depends on the performance of the unit but in the portfolio investment the obligations are fixed (Reuber, 1973: 53).

The Canadian foreign investment has both kinds of investment with different proportion. In the 19th century, the British had ninety percent portfolio investment and ten percent direct investment. But when the American foreign investment came in Canada, the situation reversed with most of the investment was direct investment. This foreign direct investment increased the Canadian frustration when they were not allowed to participate in the U.S. business. The American affiliates are almost wholly owned by the parent companies and the local investors have no opportunity to buy stocks in some of the most successful companies in their own country. A German who wants to invest in the leading company in the German oil industry has to buy Standard Oil of New Jersey. A Canadian who wants to invest in the leading company in the Canadian computer industry has to buy International Business Machines (IBM). An Australian who wants to buy shares in the leading company in Australian automobile industry has to buy General Motors. But these companies are U.S., not German, Canadian or Australian companies. Foreign investors in such enterprises can have only miniscule voice in determining the policies of these companies in their own countries (Model, 1967: 644).

a. Exclusion of Foreign MNCs from Key Sectors

Fearing heavy foreign ownership, the Canadian government has excluded the foreign MNCs from certain sectors of the economy. Foreign ownership and control is effectively excluded or sharply restricted in Canada the airline industry, railroad, commercial banking, radio, television and other industries.

b. The Banking Act of 1967

In 1967, the Canadian government amended the Bank Act to restrict foreign holdings in Canadian Chartered banks. Since all other banks were Canadian-owned, this legislation affected only to the Mercantile Bank, which had been purchased from Dutch owners in 1963 by Citibank. Despite warnings from Canadian officials that government would implement Banking Act retroactively, Citibank purchased Mercantile Bank. Citibank wanted an exemption from this provision by gaining the U.S. government support. The struggle between Canada and the U.S. over the issue led to an exchange of diplomatic protest notes between the governments. Citibank and the U.S. government threatened to retaliate against the Canadian banking operations in the U.S. if it did not
change her policy. The Canadian government ultimately passed legislation that gave Mercantile bank a momentary five-year exemption from ownership provisions. Mercantile bank issued new shares to bring the Canadian stock-ownership in the bank up to 75 percent. The Canadian government succeeded in the face of powerful corporate and diplomatic pressures, in maintaining Canadian control over the banking sector.

It was not always the federal government, which blocked undesirable foreign takeovers. The provincial governments also took measures to prevent foreign investment in certain sectors of the economy. For example, in 1971, the owner of McClelland and Steward suffered from a lack of working capital, and sought a buyer for the company. Only American publishers expressed interests but to prevent the American takeover of the company, the Ontario government provided finance.

c. The Canadian Policies to Improve Technology and Balance of Payments

Different Canadian investigation reports not only pointed out heavy foreign MNCs ownership but also highlighted the technological and balance of payments implications of these MNCs for Canada. The reports found that branch-plant firms have developed a truncated industry in Canada. All major research and development activities are carried out in the U.S. and Canadian firms are functioning just like on assembling and sale points for the parent companies, which made Canada totally dependent upon the U.S.

The reports also discussed that the foreign MNCs are also a major source of capital outflow from Canada. It is generally believed that the MNCs bring capital, reduce imports and increase exports of the host states. But the reports found that the situation is different in Canada where U.S. multinational corporations are shifting more capital out than bringing in. they have increased imports rather than exports. This has worsened the balance of payments situation in the country. To overcome this technological backwardness and balance of payments problem, the Gray report suggested a monitoring agency for foreign MNCs in Canada and Trudeau government in 1974 implemented this suggestion.

d. Foreign Investment Review Act (FIRA)

Different countries have established different monitoring instruments to evaluate the performance of multinational corporation's subsidiaries. The British government established such agency to scrutinize all investment projects after World War II. The agency will determine whether the project will make a significant contribution to the United Kingdom's industrial efficiency by providing foreign know-how and techniques (Dunn, 1973: 123). The Canadian government also wanted to introduce such legislation for the transfer of latest technology and the establishment of R&D facilities to Canada. To achieve, these objectives, Trudeau government passed Foreign Investment Review Act on April 9, 1974, which authorized to establish an agency FIRA, to screen new foreign investment in Canada.

e. The Key Elements of the Act

The Foreign Investment Review Act does not apply to financial capital flows or portfolio investment but only to the following two forms of investment:

The acquisition of control of a Canadian business enterprise by foreign individuals, corporations, governments, or groups containing foreign members, through the acquisition of shares or of the property used in carrying on the business; and The establishment of a new business in Canada either by foreign persons who do not already have an existing business in
Canada or by foreign persons who have an existing business in Canada, if the new business or expansion is unrelated to the existing business.

The government to determine whether that investment is of significant benefit to Canada must review all foreign investments subject to Act. The Act specifies five factors to be taken into account in assessing the significant benefit. These factors are given in section 2(2) as follows:

(i) The effect of the acquisition or establishment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada, and on exports from Canada;

(ii) The degree and significance of participation by Canadians in the business enterprise or new business and in any industry or industries in Canada of which the business or new business forms or would form a part;

(iii) The effect of the acquisition or establishment on production, industrial efficiency, technological development, product innovation and product variety in Canada;

(iv) The effect of the acquisition or establishment on competition within any industry, or industries in Canada, and;

(v) The compatibility of the acquisition or establishment with national industrial and economic policies, taking into consideration industrial and economic policy objectives as enunciated by a province, likely to be significantly affected by the acquisition or establishment (Rugman, 1977: 322).

f. The Structure of FIRA
The Act provides an establishment of the Foreign Investment Review Agency to advise and assist the minister responsible for the administration of the Act. The responsible minister has always been the minister of industry, trade and commerce. The minister is given a significant role in the administration of the Act. Among other tasks, he is required to give individual opinions as to whether the investor is an eligible person (that is, non-Canadian) and as to whether a proposed new business is related to the investor's existing business in Canada (Section 4(1)). The minister has also legal responsibility to review and assess each application and to make a recommendation to the governor-in-council (the cabinet) on whether to allow or disallow the transaction. The final decision as to whether to allow or disallow a transaction lies solely with the governor-in-council. Thus the agency advises, the minister recommends, and the governor-in-council decides all such cases which are subject to review.

g. The Review Process
The review procedure could be divided into four categories: (i) the ruling process, in which it is determined whether a transaction is reviewable, (ii) the assessment process, in which an application is assessed for significant benefit, (iii) the decision-making process, in which the minister recommends and the governor-in-council makes the decision to allow the investment; and (iv) the enforcement process, in which disallowed investment proposals are watched to make certain that the investment does not take place.
h. The Ruling Process

Many companies or individuals approach the agency each year to find out whether their planned investment would be subject to review under FIRA. Sometimes their inquiries are answered in informal discussion with agency staff. Some other time, formal requests are made to know the agency opinion but these guidelines have no statutory authority to bind the agency. Even if the agency has expressed an opinion that a transaction is not reviewable, the minister still has the option to require the investor to file an application if he concludes that the proposed investment is reviewable. However, the issuance of ministerial opinion has legal binding on the minister for a period of two years provided that all facts have been disclosed and the facts remain substantially unchanged for that period of time.

i. The Assessment Process

When it is clear that an investment is reviewable, it is then referred to the assessment branch which tries to get maximum possible significant benefit from investors and notifies the provincial and federal governments about the new investment, to know their concern about it. For this purpose, two procedures have been adopted, one for small investment called simple procedure and the other for large investment called standard Procedure.

The simple procedure has been adopted for small investment, which comprises of less than $2 million of assets and less than one hundred employees. In such kinds of investment, brief information are given to the agency, it notifies all the concerning provincial and federal departments about the new investment. After getting response from these departments, agency views whether to recommend the application for approval to the minister or ask the applicant to go for standard procedure. This whole procedure almost takes one week.

The minister is asked to follow the standard procedure if the investment comprises of more than $2 million in assets or more than one hundred employees. In this procedure, the entire application is sent to the provincial government and different federal government departments like consumer and corporate affairs to know its effects on Canada. Meanwhile the agency also looks at the pros and cons of this investment and drafts a memorandum for the minister’s signature. The memorandum includes the agency's opinion on whether or not the proposal meets the test of significant benefit to Canada (Dhawan, 1981: 456-57).

j. The Decision Making Process

When the application has been assessed by the agency, it is sent to the minister who reviews the application in the light of information's gathered from the agency and decides whether to allow or disallow the application. He has also the choice of rejecting or accepting the advice of the minister. Once the minister has decided upon his recommendation, the application proceeds to the cabinet, which gives the final decision. In small business, the minister recommendation is approved without any comments. In large businesses, the minister memorandum is thoroughly evaluated by the cabinet committee on Economic Development and then is sent to the cabinet for ratification (Dhawan, 1981: 460).
k. The Enforcement Process

The agency's enforcement process embodies two responsibilities: to make sure that the disallowed investment does not take place; and secondly make certain that the approved investment would take place according to the permission of the cabinet.

l. National Energy Program (NEP)

The foreign ownership was also dominating the energy sector of Canada by controlling more than 70 percent of its energy resources. Foreigners controlled more than 50 percent shares of nineteen out of the top twenty-five oil and gas producing companies. They accounted for 75 percent of Canadian oil and gas sales, and were taking many times more capital out of the country than they were investing in their new developments. This heavy concentration of foreign ownership frightened different governments, which appointed various investigation commissions. In the light of these commission's suggestions, Trudeau government announced National Energy Program in 1980. On October 28, 1980, the minister of finance, Alien Mac Eacheu introduced the National Energy Program in the House of Commons along with the budget document. The NEP was aimed to increase the Canadian ownership level in oil and gas up to 50 percent by 1990.

The National Energy Program stipulated that a 25 percent carried interest should be reserved for the Crown in every oil exploration on Canadian land. The Canadian government enacted another law, which authorized federal government to acquire 25 percent share of existing leases. But the most discontenting clause was that the government agreed to pay the drilling cost of only productive wells and not of the dry holes during the exploration. NEP denied the expenditures of the dry wells, which are considered part of the development cost, to the foreign investors. This foreign oil corporations acquisition policy by Canadian government without due compensation sent a tremor among the U.S. MNCs (Clarkson, 1985: 68).

National Energy Program also phased out the depletion allowances, which favored large corporations by allowing them to deduct the exploration cost from their revenues. This policy was replaced by Petroleum Incentives Program (PIP) which tried to encourage Canadian companies to join the energy sector by making direct payments for exploration. By this policy, a small corporation without sufficient resources could get as much benefits as a giant corporation. Moreover, the Canadian government discouraged oil gas exploration on the provincial land and encouraged on federal land where it could take the entire rent. Although the PIP had been criticized for its discriminatory but it did not exclude the foreign corporations from getting 25 percent compensation of their exploration cost. However, a company could get compensation up to 80 percent if it has 74 percent Canadian share. The most important provision of National Energy Program was that it declared that any exploration firm must have at least 50 percent private or public Canadian ownership in any oil exploration project in Canada (Behrman, 1971: 38).

This Canadianization aspect of the NEP caused a substantial irritation to the American government and MNCs. They blamed that Canada is blatantly violating the internationally accepted principle of national treatment. The Canadian spokesmen refuted the charges that their motivations were anti-American, nationalist or socialist, as the U.S. business press had expressed. The result of this NEP was that Petro-Canada bought Petrofina from its Belgium owners. Likewise, other Canadian firms such as Doome Petroleum,
Canadian Pacific, and Seagram bought out some Canadian branches of American multinational corporations to make a profit out of the NEP policies.

m. Protection of Cultural Industries

The overwhelming dominance of American periodicals and broadcasting also threatened Canadian cultural & publishing industry. This apprehension had been expressed several times by the different Canadian governments. In 1951, Vincent Massey reported: “American cultural impact was so great that there was a danger that it would stifle rather than stimulate our creative effort, therefore, it would be as necessary to spend money for culture as for military defense; the two can not be separated” (Clarkson, 1985: 76).

The Royal Commission on broadcasting also warned about the threat to Canadian identity from the cultural onslaught of the U.S. The Royal Committee suggested that Canadian government should spend substantial resources on broadcasting and publications to promote its cultural developments. The development of these projects should be carried out under the aegis of the government because the private broadcasters always rely on the American programs do not meet the Canadian cultural objectives.

In 1961, another Royal Commission probes the conditions of Canadian periodicals and publications. It concluded that the United States had the World's most penetrating and effective apparatus for the transmission of ideas and warned that Canada is more vulnerable to it than any other country of the world. It pointed out that every three out of four magazines read by Canadian came from the United States. It, therefore, recommended steps that might improve the development of Canadian periodicals and enable them to compete more effectively with the U.S. publications that are a major threat to them.

In 1965, the Canadian government proposed to waive the income tax deduction for the cost of advertising in a newspaper or periodical more than 25 percent owned by non-Canadians. This discrimination against American periodicals led a row between the two countries and the President Kennedy discussed the issue with the Canadian Prime Minister Pearson. This presidential intervention and diplomatic pressure dissuaded the Canadian government from the implementation of this measure.

In 1960s, Time and Reader’s Digest took nearly sixty percent of Canadian magazine advertising revenue. This made it difficult for Canadian magazine to survive. Therefore, another Royal Commission in 1970 recommended that all tax exemptions granted to Time and Reader’s Digest should be withdrawn. The Canadian governments ultimately introduced Bill C-58 in 1976 to make Canadian ads in Time and Reader’s Digest non-deductible from income tax. At the same time, the bill also declared that the costs of advertising on American television stations would also be non-deductible from the income tax. This measure gave some relief to the Canadian magazines by giving them protection from foreign competition. However, to counter this move, the U.S. government waived the tax exemption granted to the U.S. citizens visiting to Canada (Walton, 1972: 215).

n. Canadian Policies for Joint Ownership

The ownership patterns of multinational corporations generally determine governmental policies. The wholly owned affiliates have different effects and the jointly owned affiliates have different consequences on the host states. If the affiliate is wholly owned, it can adopt any policy, which is beneficial to the parent company without caring for
the host state interests. However, if the subsidiary has joint-ownership, it has to justify all of its policies to its shareholders. Therefore, the wholly owned subsidiary has more authority in its decision-making matters. Secondly, joint ventures can also reduce deficit in the balance of payments because the dividends are distributed among the local and foreign shareholders proportionate to their shares. This local participation reduces the capital flight from the country. Thirdly, the joint ventures also reduce the imports because if the affiliate were wholly owned by the parent company then most of the transaction would take place between the parent and affiliate, which would increase imports. On the other hand, if there were a joint venture, it would have most transaction with the local market and in this will reduce the imports from the parent company. The Canadian governments, therefore, adopted joint ownership policy to reduce foreign dominance. For example, the tax on dividends was lowered for subsidiaries with 25% Canadian ownership than for operations with a lesser amount of local ownership (Stopfford, 1972: 183).

o. Canadian Development Corporation (CDC)

The Canadian government not only put foreign MNCs at disadvantageous position but also established Canadian Development Corporation to make Canadian Corporation more competitive with foreign MNCs in the key sectors of the economy. Trudeau government in 1970s was of the opinion that foreign direct investment has often been achieved by acquisition of an existing domestically owned business. Many of these foreign acquisitions of Canadian-owned companies occurred because there were no large Canadian firms, which could acquire existing domestic firms. To overcome this adverse situation, the Canadian government established the Canadian Development Corporation (CDC) in 1971, 48 percent of which was owned by the federal government. The main objective of CDC was not let the Canadian corporations to go in the hands of the foreigners. Secondly, it also aimed to enable the Canadian citizens to purchase shares in the foreign corporations in Canada. One major achievement of CDC was that it purchased 30 percent interest in Texasfuld Inc (Behrman, 1971: 44-45).

The Canadian economy has huge foreign investment but the proportion of foreign direct investment outstripped foreign portfolio investment because American MNCs, which have a lion’s share in foreign investment because Canadians have not been given participation opportunities.

The Canadian government, therefore, opted for different policies to ensure the Canadian involvement in the different business activities. Some sectors of the economy were earmarked specifically for the locals. Moreover, the Canadian government initiated NEP to control the foreign ownership. The government also established a screening body FIRA which evaluate the benefits of new foreign investment.

FIRA attempted to increase the net benefits for Canada by bargaining with the investors and preventing them when they were not beneficial for the country. It has been observed that the significant benefit criterion was quite vague and broad and was difficult for an investor to fulfill these requirements. FIRA provided an opportunity to negotiate for greater benefits for Canadians from any proposed foreign investment.

In practice, as intended by the government, FIRA has not operated merely as a screening agency. It has taken a part in the bargaining process with the objective of increasing the benefits to Canada, while reducing the costs. It has apparently withheld approval until firm promised more jobs, investment and exports for the country.
During 1970s, the FIRA was alleged to have significantly reduced the foreign inflow of capital. The FIRA's rejection rate of 20 percent was a formidable barrier to foreign investment and it was high, compared to the other developed countries where rejection rate was not more than one percent. The length and cost of the application process also discouraged some firms even from applying. Therefore, the most straightforward objection made by the American government was that the very existence of FIRA undoubtedly discourages many would-be investors. FIRA was an obstacle to the free flow of international investment capital. Moreover, the American businessmen complained that the process of FIRA is tedious and its time span to evaluate the application should be decreased.

The growing American government pressure forced the Canadian government to revise its policies. In 1984, Prime Minister Brian Mulroney announced to change his foreign investment policy. FIRA was replaced in June 1985 by a new agency with much friendlier name Investment Canada. The aim was to facilitate the foreign investment rather than hinder it from crossing the border. Since then, virtually all foreign investment and all foreign takeovers have been allowed to proceed without any scrutiny. Under the new bill, any corporation with simple majority of Canadian equity would be considered 100 percent Canadian-owned. FIRA considered firm Canadian if two third voting shares belong to the Canadians. The new legislation affected the status of some 20 corporations, which now attained the national treatment privilege from the Canadian government (Holtfrerich, 1989: 153).

III. Conclusion

This study examines how the U.S. MNCs put a heavy drain on the Canadian economy and what the Canadian government took different steps to counter them. The Canadian government gave taxation concessions to the local periodicals and publications to make them competitive with the U.S MNCs. Trudeau government announced National Energy Program (NWP) which put ownership restriction on the foreign MNCs and put them at disadvantageous position compared to Canadian MNCs. The Canadian government also introduced FIRA (Foreign Investment Review Agency) which was a screening body for the foreign investment and which caused a lot of resentment among foreign investors.

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