FOREIGN INVESTMENT IN THE EV BATTERY MARKET: REGULATORY FRAMEWORK IN NORTH AMERICA AND CANADA'S STRATEGIC EDGE

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The federal governments of Canada and the United States (U.S.) have both made efforts to put in place incentives and credits to attract and develop a domestic electric vehicle (“EV”) battery manufacturing and production industry. Why? A North American EV battery market would play a vital role in supporting strategic and policy objectives including energy transition initiatives, providing a local market for critical mineral production and enhancing North America’s net zero emissions policies. In addition to the strategic and policy objectives, it is notable that the EV battery market in North America is a burgeoning industry that was estimated to be worth approximately USD$1.82 billion in 2021 but grew to approximately USD$10.78 billion by 2023 alone. This market is projected to continue its rapid growth pace and reach a value of approximately USD$63.39 billion by 2032.[1]

The importance of the industry in supporting national policy initiatives is evident by the rapid and significant announcements in both Canada and the U.S. of government subsidies and incentives for the industry in the billions of dollars.[2] Both Canada and the U.S. are fiercely competing to attract investors and manufacturing companies to be the first to establish world-scale mines, transportation, and battery production. For foreign investors seeking to enter the market, it is critical to understand the legal and regulatory landscapes in both the U.S. and Canada.

This summary will explore the following: (1) Canada’s approach to foreign investment in the battery market, (2) the U.S. approach to the same, (3) compare and contrast the approaches and requirements being considered and enacted in the two nations, and (4) consider implications for Indo-Pacific companies.

Canada’s Approach to Foreign Investment in Critical Minerals

The Government of Canada, as part of its Paris Agreement commitments to achieve net-zero emissions target by 2050, is working to establish both a critical minerals industry and a local market for such critical minerals which support the entire value chain for critical minerals including the manufacture, sales and reclamation of EV batteries.[3] Under various ministries, the Government of Canada has put forward several investments and
incentives in support of these goals. For instance, in 2019, Canada created Incentives for Zero-Emission Vehicles, which provided consumers with an incentive of up to CAD$5,000 when purchasing an eligible vehicle. This program does not base eligibility on foreign investment qualifiers but rather determines eligibility based on the new vehicle’s status as either a battery-electric, plug-in hybrid electric or a fuel cell electric car. More recently, Canada published regulations amending the Passenger Automobile and Light Truck Greenhouse Gas Emissions Standards, thereby requiring 100% of new passenger cars and light trucks sold from 2035 to be zero-emission vehicles, thereby further incentivizing EV purchase.

The Government of Canada has expressed some concerns about foreign involvement within the critical mineral and EV battery industries. Such concerns have materialized through certain legislation and regulations such as under the Investment Canada Act (“ICA”). Between March 2021 and November 2022, Canada updated its guidelines and policies under the ICA to protect its critical minerals sectors from foreign state-owned enterprises (“SOEs”) and investors with close ties to foreign governments. The Government of Canada’s strategy intends to ensure that foreign investments provide an economic net benefit (the specified threshold for 2024 is CAD$1.326 billion in enterprise value for investments) and do not pose harm to national security. Particularly, significant transactions by foreign SOEs in Canada’s critical minerals sectors “will only be approved on an exceptional basis”, highlighting the Government of Canada’s cautious stance towards foreign involvement in strategic sectors. In 2022, specific investments were subject to increased scrutiny due to potential threats to national security and critical mineral supply chains. As a result, the following divestitures were mandated:

- Sinomine (Hong Kong) Rare Metals Resources Co., Limited was ordered to divest its investment in Power Metals Corp.
- Chengze Lithium International Limited was required to sell off its investment in Lithium Chile Inc.
- Zangge Mining Investment (Chengdu) Co., Ltd. had to divest its stake in Ultra Lithium Inc.

The policy framework for reviewing these potential investments under the ICA includes consideration of factors such as the potential for foreign state exercise of control over Canadian businesses, the impact on sector competition, adherence to Canadian corporate governance standards, and the operation of the Canadian business on a commercial basis. Additionally, all investments, regardless of their value, are subject to a national security review process, underscoring the importance of critical minerals to Canada’s economic prosperity and security. The inclusion of a “national security” review standard creates an element of uncertainty in the foreign investment process.

However, there are some general principles which can assist an investor when considering an investment in the Canadian battery and critical mineral markets. Investors can be certain that Canada has numerous
advantages in all stages of the supply chain in the battery market. For instance, as mentioned, investors in Canada will benefit from the major production of critical minerals, supported by global leaders in mining and mineral exploration. From there, Canada can provide industry expertise and the benefits stemming from the necessary trade agreements, plus a thriving manufacturing/ automotive industry to support the end-to-end manufacturing of batteries in the country. In the face of very significant investments made by the Government of Canada, including CAD$13 billion toward a Volkswagen AG battery plant in St. Thomas, Ontario, and CAD$15 billion in funding toward a Stellantis NV-LG Solution battery plant in Windsor, Ontario, there is a clear long-term commitment that investors can trust being exhibited by the Government of Canada.

The United States Approach to Foreign Investment in Critical Minerals

In 2022, the U.S. Government implemented the Inflation Reduction Act of 2022 ("IRA") which is a broad-encompassing piece of legislation that affects a wide range of industries. Within this, the IRA provides incentives for the domestic manufacturing industry to focus on clean energy and environmental considerations. Specifically, the IRA offers a USD$7,500 tax credit to purchasers of a “new clean vehicle” at the time of purchase. However, the IRA imposes restrictions on the eligibility for these clean vehicle tax credits based on the sourcing of critical minerals and the manufacturing of battery components. To fully qualify for these tax credits, a significant portion of the critical minerals must be extracted or processed in the U.S. or in a country with which the U.S. has a free trade agreement, such as Canada, or otherwise must be recycled in North America. For 2024, at least 50% of the critical minerals must meet these requirements to qualify for the incentive. However, after 2024, this percentage will increase by 10% annually, up to 80% after 2026. In addition to this requirement, the IRA specifies that the vehicle must also undergo final assembly in North America to qualify for the tax credits.

Within this, the IRA specifically disqualifies vehicles containing critical minerals or battery components from any “foreign entity of concern” (“FEOC”), with a broad interpretation of FEOC including entities owned by, controlled by, or subject to the jurisdiction or direction of the government of covered nations including China, Russia, Iran, and North Korea. To clarify this, the Department of the Treasury explained that a foreign entity includes the following: (1) a government or senior official of a foreign country; (2) a natural person who is not a lawful permanent resident or citizen of the U.S., or a protected individual; (3) any combination of persons organized under foreign laws or having its principal place of business in a foreign country; and (4) a U.S.-based entity controlled by, owned by, or subject to the direction of a foreign entity.[11]

In addition, a foreign entity is deemed to be a FEOC under any of the following scenarios: (1) if 25% or more of the board seats, voting rights, or equity interests are held (directly or indirectly) by the government of a covered nation; (2) if it is incorporated, domiciled or has its principal place of business in a covered nation; or (3) if in respect to critical minerals or battery materials, it has entered into contracts or engages in extraction or
These measures reflect the U.S. government’s efforts to reduce dependence on critical minerals from countries deemed as threats to national security while also promoting domestic and allied production and processing capabilities. The emphasis on tracing the source of critical minerals and manufacturing locations for battery components illustrates the strategic approach to safeguarding the American EV supply chain and supporting the transition to clean energy vehicles.\textsuperscript{13}

It is important to note that the IRA was implemented in 2022 and signed into law by President Joe Biden. As 2024 is a presidential election year in the U.S., investors and industries must be prepared that a change in government may mean changes to the regulations and incentives provided for in the IRA. This is especially the case as Donald Trump, the confirmed Republican presidential nominee, has already expressed his distaste for the IRA. While experts believe that investments in the battery market are a bipartisan issue, the U.S. election may still create uncertainty.\textsuperscript{14}

**Contrast Between Canada and the United States**

The strategies of these countries reflect different regulatory mechanisms and focal points in addressing the challenges of foreign investment and international cooperation in the critical minerals sector. A key distinction between Canada and the U.S. in regulating foreign investment in the battery and critical mineral market lies in their specific legislative actions and the scope of their restrictions.

Canada’s approach is characterized by a comprehensive review process under the ICA, with a focus on scrutinizing investments by SOEs and those with close government ties, emphasizing the protection of national security and economic benefits. The U.S., through the IRA, specifically targets the sourcing of critical minerals and the manufacturing of battery components to qualify for EV tax credits, aiming to reduce reliance on FEOCs and bolster domestic and allied nations’ supply chains. Both countries demonstrate a commitment to securing their critical mineral supply chains and enhancing their competitive positions in the global EV battery market.

Driven by the ambition to capture significant portions of the clean energy and EV battery sectors, both countries offer a range of incentives designed to attract investments to their markets and to encourage consumer adoption of clean energy technologies. The U.S. provides substantial incentives, alongside inherent benefits such as hosting leading automakers like Ford Motor Co., General Motors Co., and Stellantis North America. For entities active or conducting business beyond North America, Canada presents compelling advantages due to its ample natural resources, skilled workforce, and incentive programs that parallel those in the U.S. A significant benefit for Canadian projects, particularly concerning the Indo-Pacific region, is the logistical advantage of shipping resources from Canada, which can be up to 10 days faster than from the
Furthermore, investing in Canada allows companies to adeptly navigate and adhere to the IRA's stipulations on trade, trade agreements, and regulations concerning foreign entities.

**Indo-Pacific Connection**

Indo-Pacific companies are very well situated to participate in the North American critical mineral and EV battery markets, but specifically in the Canadian market. The Government of Canada has prioritized its economic partnership with its strategic partners in the Indo-Pacific region with its announced Canada Indo-Pacific Strategy and is well positioned with its skilled and trained workforce, the aforementioned incentive programs, as well as its geographical location, lending the nation a system that can efficiently make exports to and from Asia in terms of time and costs, to further support foreign investment. In addition, Canada is sending a large delegation of senior government officials and industry participants on official Trade Missions to the Indo-Pacific region throughout 2024, which McMillan is very honoured to be participating in. This further signifies Canada's interest and commitment to Indo-Pacific investors.

McMillan has the expertise to ensure that Indo-Pacific companies understand the complexities of doing business in Canada and have the knowledge and skill to successfully implement projects in Canada.

In addition to the above-linked resources, the following government resources may be helpful:

- Canadian Government: Canada's Indo-Pacific Strategy
- Canadian Government: Introducing Canada's Critical Minerals Strategy
- Albertan Government: Minerals strategy and action plan | Alberta.ca
- United States Department of State: 2023 Investment Climate Statements


[2] See: CBC.ca “Canada is pouring billions of dollars into the electric vehicle industry. Will it pay off? | CBC News”.


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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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