



A BRIEF GUIDE TO DOING BUSINESS IN CANADA

I. INTRODUCING THE CANADIAN MARKET

Canada is a dynamic and multicultural nation of more than 33 million people, with one of the strongest economies in the world. A founding member of NAFTA (the North America Free Trade Agreement between Canada, the United States, and Mexico) and the G8 group of nations, Canada is a federation comprised of ten provinces and three territories,¹ governed by an elected Parliament and an appointed Senate, an executive branch (consisting of the Prime Minister and the Governor-General, the official representative of the British monarch), and an independent judiciary. Canada's capital is located in Ottawa (in the province of Ontario), and its three largest cities are Toronto (Ontario), Montréal (Québec) and Vancouver (British Columbia), respectively.

Reflecting its two founding cultures, English and French, Canada is an officially bilingual country. Benefitting from enormous territories (as the 2nd largest country in the world), abundant natural resources, highly-diversified and dynamic manufacturing, high-tech, and services sectors, and strong trading ties with the United States, Europe and the Pacific Rim, Canada is an ideal place for doing business.

Key economic highlights of Canada include:

- ❖ World's 9th-largest economy (2007 GDP of US\$1.33 trillion)
- ❖ World's 2nd-largest proven oil reserves, after Saudi Arabia
- ❖ Leading global supplier of natural gas, metals, timber and agricultural goods
- ❖ Global leader in the automotive, aerospace, pharmaceuticals and biotech industries
- ❖ Member of the NAFTA free-trade zone, along with the United States and Mexico

II. CANADA – A GATEWAY TO NORTH AMERICA

As a member of NATFA, Canada offers foreign investors access to a market of more than 440 million consumers and a combined GDP of more than US\$16 trillion. It also offers the most educated workforce in North America, with the highest percentage of secondary school and university enrollments. Canada spends more money on education, as a percentage of GDP, than any other country in the world. As the largest trading partner of the United States — U.S. trade with Canada exceeds all U.S.-EU trade combined — Canada offers foreign investors an attractive gateway to North America.

¹ From West to East, the ten provinces of Canada are British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Québec, New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland. The three territories, spanning most of northern Canada, are the Yukon, Northwest Territories, and Nunavut.

III. ESTABLISHING A LOCAL PRESENCE IN CANADA

Foreign companies wishing to enter the Canadian market by establishing a local presence will usually do so in one of four ways: (1) by establishing a Canadian branch operation; (2) by forming a Canadian subsidiary; (3) by acquiring an existing Canadian company; or (4) by entering into a joint venture with a Canadian company. Each of these alternatives is described briefly below.

(1) Establishing a Canadian Branch

Offshore companies may establish a branch operation in Canada provided that certain provincial filing requirements are fulfilled. The investor must decide in advance in which Canadian province, or provinces, the branch will be active and obtain an extra-provincial license from the government of each province. Obtaining the license is a relatively simple administrative procedure, although the requirements differ between provinces. In Ontario, for example, the investor must conduct a corporate name search in the register of companies, and submit the name search results along with its license application to demonstrate that its name complies with Ontario law (*e.g.*, that the use of the proposed name will not cause confusion with existing companies registered in Ontario). A local “agent for service” of claims must also be designated.

The primary advantage of establishing a branch operation is tax treatment — if the branch is not expected to earn profits in the initial years of operation, it may be possible to offset any losses against the investor’s income in its home jurisdiction. (However, double-taxation may be a concern, depending on the existence, and provisions of, any bilateral tax treaty between the home jurisdiction and Canada.) Conversely, operating a branch operation directly exposes the foreign investor to liability for conduct in Canada, as there is no intervening Canadian subsidiary to take legal responsibility for the investor’s actions.

(2) Forming a Canadian Subsidiary

Canada follows the English and American model of allowing investors to create a limited liability company, generally recognized by the abbreviations “Inc.” (“incorporated”) or “Ltd.” (“limited” liability) in the company’s name. The limited liability company plays a valuable role in that it creates an independent legal entity through which shareholders can carry on business, purchase and trade shares, and minimize their personal liability.

Generally speaking, a foreign investor forming a Canadian company may choose to do so in any of the ten Canadian provinces, or under the federal *Canada Business Corporations Act*. In each case, incorporation is a simple process of filing Articles of Incorporation with the appropriate governmental authority and paying a small fee. The key question for investors is typically choosing whether to establish a federal Canadian company or a provincial company. Where the investor anticipates carrying on business in multiple provinces, the federal alternative may be more attractive as a federal corporation may use its company name in every province, while a provincial corporation must register its company name in other provinces before carrying on business there.

Canadian companies generally act and are governed by a board of directors elected by the shareholders. Some provinces require a minimum number of directors to be resident Canadians. Federal companies, and provincial companies in Ontario, Alberta, Manitoba, Saskatchewan and Newfoundland, must have at least 25% Canadian directors. (There are no director residency requirements for provincial companies in British Columbia, Québec, New Brunswick, Nova Scotia

and Prince Edward Island.) In a few, specific sectors Canadian law requires a majority of a company's directors to be Canadians (*i.e.*, book publishing/distributing/retailing, film distribution, uranium mining). However, directors' meetings may be held outside Canada (although, for Ontario companies, the corporate by-laws must authorize such meetings). The use of signed resolutions or telephone meetings further reduces the logistical burden on directors. Furthermore, the federal and most provincial corporate laws allow the shareholders of a Canadian company to use a "Unanimous Shareholders Agreement" to restrict the directors' powers and to manage aspects of the company's business.

(3) Acquiring a Canadian Company

Rather than forming a new subsidiary, foreign investors interested in entering the Canadian market may choose to acquire an existing Canadian business (whether a competitor or not). M&A transactions in Canada follow the same general rules and procedure as in most Western regimes. However, Canada does employ a foreign investment review process which requires parties to transactions exceeding certain financial thresholds to file a simple notification with the federal government. The *Investment Canada Act* (described in Section III.5 below) may also require that certain large acquisitions, or transactions in a few culturally-sensitive sectors, be pre-approved by the federal Department of Industry or the Department of Canadian Heritage.

The acquisition of a business whose Canadian (not global) assets or turnover exceeded an annually-defined threshold — C\$70 million in 2009 — in the previous fiscal year must be pre-notified to the Competition Bureau, the domestic antitrust regulator.² Canada follows the model of most Western regimes and requires that the parties to the transaction observe a mandatory waiting period before the transaction may be closed. Other, industry-specific, regulatory approvals may be required, and in a small number of industries (telecommunications, broadcasting, newspapers, railways, airlines and financial services) there are limitations on the ownership percentage that a foreign investor can acquire. Canadian law does not require the parties to a merger or acquisition to consult or seek approvals from the company employees or union. Where "mass" employee terminations (*i.e.*, more than 50 employees to be terminated within four weeks of closing) are contemplated, the acquirer may be required to provide advance notice to the appropriate federal or provincial Ministry of Labour.

(4) Establishing a Joint Venture With a Canadian Company

Foreign companies not interested in forming a Canadian subsidiary or acquiring a Canadian company may instead choose to access the Canadian market through a joint venture with a local company. Doing so may be as simple as identifying a suitable (and interested) local partner and preparing the necessary joint venture agreements. Generally speaking, where the combined assets of the joint venture business generated Canadian turnover in excess of C\$70 million in the previous year, notification to and approval from the Competition Bureau will again be required.

(5) The *Investment Canada Act* (ICA)

The *ICA* creates a foreign investment review process to determine if certain kinds of transactions or investments will be of "*net benefit to Canada*". The *ICA* regime applies to both the

² However, where the parties to the transaction (together with their affiliates) did not hold combined Canadian assets, or achieve a combined Canadian turnover, in excess of C\$400 million in the previous year, the transaction will be exempted from the notification requirements.

acquisition of Canadian companies and the establishment of new Canadian businesses by foreign investors. Depending on the value of the business being created or acquired, and the industry sector concerned, the transaction may be notifiable (meaning that a simple, standard-form notification be provided to the Canadian government) or reviewable (meaning that an application and supporting documents be filed with the government, who must review and approve the transaction).

The ICA employs a complex series of financial thresholds, revised annually, to determine whether an acquisition is notifiable or reviewable. Generally, direct acquisitions by foreign investors from WTO nations will be notifiable if the value of the Canadian assets acquired exceeds an annually-determined threshold (C\$600 million in 2009). Much lower thresholds apply to acquisitions by non-WTO investors, and acquisitions of “cultural businesses” (*e.g.*, publishing, distribution or sale of books/magazines/periodicals/newspapers or music in print or machine readable form, as well as the production/distribution/sale/exhibition of film or video products or audio or video music recordings). Recent amendments to the law, similar to the U.S. CFIUS regime, provide for the review of any foreign investment, regardless of size, which may be “*injurious to national security*”. The law in this area is complicated and the advice of qualified counsel should be sought for acquisitions that may trigger these thresholds.

IV. ESTABLISHING AN INDIRECT PRESENCE IN CANADA

For a variety of reasons, some companies may consider entering the Canadian market without establishing a local presence. For these firms, it may be more advantageous to sell their products into Canada via an established local distributor, through a franchise, or by appointing a local agent.

(1) Sales Via Distributor

A distributor is an individual or company that purchases products from a supplier, taking title to (and risk for) the goods, and resells them under its own name. A good distributor offers a supplier access to an established local sales, marketing and distribution network for the supplier’s goods, without incurring the costs involved in establishing a direct local presence.

Unlike some other jurisdictions (for example, the treatment of automobile dealers in the United States, or exclusive distributors in Belgium), Canadian law does not provide specific rules for the formation and governance of distributorships. Distribution relationships are thus principally governed by the distribution agreement between the parties, making an effective distribution agreement essential for protecting a supplier’s interests. A good distribution agreement will cover key issues such as the distributor’s territory, any exclusivity arrangements, confidentiality obligations, the use and protection of the supplier’s brands, trademarks and other intellectual property, any joint/co-operative advertising and marketing, periodic reports on market trends and intelligence, *etc.* Control of resale prices, exclusivity clauses, and territorial designations may raise concerns under Canadian competition laws, and should be reviewed by experienced antitrust advisors in advance. Notably, even if the parties have included provisions governing termination in the distribution agreement, Canadian courts have consistently found that there is a duty on suppliers to act reasonably and in good faith in deciding whether or not to terminate a distributor.

(2) Franchising

Franchising law and regulation is a matter of provincial, not federal, authority in Canada. As of 2008, four Canadian provinces (Alberta, Ontario, New Brunswick and Prince Edward Island) have

enacted individual franchising statutes governing the relationship between franchisors and franchisees. These laws require the franchisor to provide a prospective franchisee with certain specific information (called a “disclosure statement”) at least 14 days before the franchisee enters into a franchise agreement or makes any payment to the franchisor. Where the franchisor fails to do so, the franchisee may typically sue for damages or have the franchising agreement between the parties rescinded. A franchisee may also sue for damages for any misrepresentations in the disclosure statement. The laws impose a range of other obligations on the parties, including a duty of “fair dealing” (defined in Ontario as a “*duty to act in good faith and in accordance with reasonable commercial standards*”).

(3) Agency Sales

As the name implies, an agent is not an independent operator, but acts on behalf of and in the name of the principal. The agent typically operates in a defined territory, promoting sales of the principal’s products or services in return for a commission.

Unlike the situation in EU states, for instance, there is no specific legislation in Canada governing agency relationships. It is therefore essential that the parties enter into a clear and specific written agreement setting out their respective rights and responsibilities. Importantly, regardless of any provisions in the agency agreement concerning termination, Canadian courts have consistently interpreted such agreements as imposing a duty of fair dealing on the principal, and a requirement to give the agent reasonable notice in advance of terminating the agency. In the absence of reasonable notice, a supplier will likely be liable for damages to the agent. Generally speaking, the longer the agency relationship between the parties, the more notice (or damages in lieu of notice) will be owed.

V. EXPORTING GOODS TO CANADA

The importation of goods into Canada is regulated by the federal government, with the federal *Customs Tariff* listing the applicable tariff for every category of goods. Under NAFTA, goods exported to, or imported from, the United States or Mexico generally move tariff-free (if they qualify as Canadian, American or Mexican goods under the “rules of origin” regulations). The federal Goods and Services Tax (or GST, similar to a VAT), at a rate of 5%, applies to most goods imported into Canada, including goods imported from the U.S.A. or Mexico.

VI. LABOUR RELATIONS

With the exception of a handful of “national” industries — including banks, airlines, interprovincial trucking, pipelines, telecommunications, and television broadcasting — labour and employment laws are generally determined at the provincial level. Thus, an employer will be bound by and should review the labour and employment laws of each province in which it is active. However, there are several common principles that apply throughout Canada:

- ❖ All provinces have employment standards legislation setting out minimum standards for wages, workplace safety, working hours, maternity leave, *etc.* Employers and employees cannot contract out of these obligations, unless it is to provide more favourable terms.
- ❖ A union may be certified as the exclusive bargaining agent for a group of employees. Once certified, the employer must bargain in good faith with the union to reach a collective agreement. A strike cannot be called during the life of a collective agreement.

- ❖ Terminated employees are entitled to reasonable notice, or payment in lieu of notice. As noted in Section III.3 above, “mass terminations” may require prior notice to government regulators.

VII. COMPETITION LAWS

Canada has adopted competition legislation which governs the conduct of companies in the marketplace. These competition rules are vigorously enforced by the Competition Bureau and backed up by behavioural orders, fines and — like the United States and the U.K. — the possibility of imprisonment for the most serious cartel and bid-rigging offences.

- ❖ **Multi-firm conduct.** Canadian law prohibits any agreement or arrangement among competitors (or potential competitors) which sets or controls prices, affects output levels, allocates customers or territories, or rigs or manipulates bids or tenders. A unique provision of the *Competition Act* also criminalizes any action by a Canadian company, taken on the orders of a person situated outside Canada, which gives effect to an illegal conspiracy or agreement (even where the Canadian company has no knowledge of the conspiracy). While cartels are the most obvious example of illegal horizontal agreements, other agreements between competitors, including the activities of trade or industry associations, may be at risk.
- ❖ **Single-firm conduct.** Like the EU, Canadian law prohibits “dominant” (*i.e.*, high market share) firms from abusing their market position by engaging in certain types of behaviour, including predatory (*i.e.*, below-cost) pricing, tied selling, exclusive dealing, charging excessive prices, controlling resale prices, or imposing other unfair terms of trade.

This brochure has been prepared for reference purposes only, and does not constitute legal advice or establish an attorney-client relationship between the reader and the authors. For more information or advice concerning the issues discussed herein, or indeed on any other aspect of doing business in Canada, please contact:

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