FOREIGN INVESTMENT AND MERGER

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Doing Business in Canada

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DOING BUSINESS IN CANADA

This publication has been prepared to provide an overview to foreign investors and business people who have an interest in doing business in Canada. The material in this publication is intended to provide general information only and not legal advice. This information should not be acted upon without prior consultation with legal advisors.

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The following currency notation is used in this book.

CND Canadian Dollar

The global financial crisis of 2008 and 2009 revealed the strengths and weaknesses of the world's financial systems. It is universally recognized that Canada's well-regulated financial institutions proved to be a model of prudence to the world. While the Canadian and American economies are interrelated, Canada has forged its own path to become a leader in reducing barriers to global commerce. Canada offers a stable and potentially lucrative market for international businesses and investors.

Over 90% of Canadians live within 160 kilometers (100 miles) of the U.S.-Canada border. As a result, Canada and the United States share many economic imperatives and cultural influences. The economic and material aspirations and realizations of the Canadian and U.S. populations are strikingly similar.

From a historic perspective, however, Canada remains significantly different than the United States. Canada today is a highly multicultural society which generally respects and enshrines cultural heritage rather than encouraging the population to form a homogeneous melting pot. Colonized by the British and French, Canada remains a bilingual country; English and French are the two official languages. Approximately 59% of the population has English as their mother tongue while about 23% of the population is French-speaking (mostly in the province of Québec). The remaining 18% speak other languages.

Canada remains an attractive location for the establishment or expansion of business in North America. During the past decade, there has been a marked trend toward fiscal conservatism. Federal and provincial governments made serious efforts to reduce deficits and balance budgets. Budget surpluses have been achieved on the federal level and in many provinces. Inflation and interest rates have remained low.

Except in certain industry-specific situations where cultural values are at risk, Canada is receptive to foreign investment. Despite its relatively small population, Canada is one of the strongest trading nations in the world. Although historically Canada was an exporter of raw materials and an importer of manufactured goods, shipments from Canada are now balanced between raw materials and finished goods. In addition, Canada is recognized internationally as a world leader in such areas as fibre optics and telecommunications.

This book provides a general overview as of July 2013 of particular matters of interest to businesses considering entry into the Canadian market. Where appropriate, descriptions of both federal and provincial laws are provided. However, this book should not be considered an exhaustive review, and

particular businesses may be subject to industry-specific legislation and other legal requirements which are not dealt with in this book. Accordingly, before undertaking any business transaction involving entry into Canada, it is prudent to seek the advice of counsel.

1. WHAT LAWS INFLUENCE THE RELATIONSHIP BETWEEN LOCAL AGENTS AND DISTRIBUTORS AND FOREIGN COMPANIES?

Foreign companies doing business in Canada will be influenced by legislation, the common law and various international treaties. Canada's Constitution creates mutually exclusive jurisdictions for federal and provincial legislation. For example, Canada's intellectual property, competition, bankruptcy and criminal laws are solely within the purview of the federal government. Provincial legislative authority is granted for the regulation of trade and commerce, education and health within the province. However, the jurisdictional distinctions are often blurry, and the subject matter of federal and provincial legislation sometimes overlaps. In addition, Canada has entered into many international trade and tax treaties with other countries which will influence foreign companies doing business in Canada.

2. HOW DOES THE CANADIAN GOVERNMENT REGULATE COMMERCIAL JOINT VENTURES BETWEEN FOREIGN INVESTORS AND LOCAL FIRMS?

Legislation by the federal government and each of the provincial governments regulates ventures between foreign investors and local firms, including agents and distributors. From a contracting perspective, there is no material distinction between business parties who are foreign and those who are local.

The foreign investor will have to comply with the direct investment provisions noted below in question 3 and discussed in more detail in the Foreign Investment & Merger section of this Guide.

In addition, many obstacles to foreign investment have been removed as a result of the various free trade agreements that Canada has negotiated with other countries, such as the North American Free Trade Agreement discussed in detail in the International Trade section of this Guide.

3. WHAT ROLE DOES THE GOVERNMENT OF CANADA PLAY IN APPROVING AND REGULATING FOREIGN DIRECT INVESTMENT?

Non-Canadians who acquire control of an existing Canadian business or who wish to establish a new unrelated Canadian business are subject to the federal Investment Canada Act (ICA). In either case the non-Canadian investor must submit either a Notification or an Application for Review to the federal government. A Notification must be filed each and every time a non-Canadian commences a new business activity in Canada and each time a non-Canadian acquires control of an existing Canadian business where the establishment or acquisition of control is not a reviewable transaction. Only in certain circumstances does the ICA seek to review or restrict new investments by non-Canadians. In general terms, the transactions which are subject to review under the ICA are larger transactions, and transactions in certain politically and culturally significant sectors (as noted below in question 5). Securities transactions and venture capital deals, acquisitions of control in connection with realization on security, certain financing transactions and certain direct and indirect acquisitions of control by insurance companies are exempt from the ICA. For all other transactions a Notification needs to be filed.

More detailed information on the ICA and direct investment in Canada can be found in the Foreign Investment & Merger section of this Guide.

4. CAN FOREIGN INVESTORS CONDUCT BUSINESS IN CANADA WITHOUT A LOCAL PARTNER? IF SO, WHAT CORPORATE STRUCTURE IS MOST COMMONLY USED?

There is nothing preventing a foreign investor from conducting business in Canada without a local partner. All businesses, foreign or local, must register in the appropriate jurisdiction to conduct business; however, these are administrative filings.

Most foreign investors, however, would incorporate a new company in a Canadian jurisdiction in order to carry on their business. This Canadian subsidiary may be a standard limited liability corporation or it might be an unlimited liability corporation, depending on the tax characteristic of the parent's jurisdiction. More detailed information on the forms of business organization in Canada can be found in the Forms of Business Organization section of this Guide. In addition, the taxation of foreign investors and their Canadian subsidiaries is discussed in detail in the Taxes and Duties section of this Guide.

5. WHAT STEPS DOES THE CANADIAN GOVERNMENT TAKE TO CONTROL MERGERS AND ACQUISITIONS WITH FOREIGN INVESTORS OF ITS NATIONAL COMPANIES OR OVER ITS NATURAL RESOURCES AND KEY SECTORS (E.G., ENERGY AND TELECOMMUNICATIONS)?

As discussed in question 2, non-Canadians who acquire control of an existing Canadian business, or who want to establish a new unrelated Canadian business, are subject to the federal Investment Canada Act (ICA). The transactions subject to review include businesses within a prescribed type of business activity that is related to Canada's cultural heritage or national identity, and transactions where the Minister responsible has reasonable grounds to believe that an investment by a non-Canadian could be injurious to national security. Notice of the transaction is given to the Review Division of Industry Canada. When a transaction is reviewable under the ICA, the investor is required to file an extensive pre-closing filing called an Application for Review with supporting documents. When a review is conducted, the investor is prohibited from closing the transaction until the Minister's approval is obtained. Investment reviews under the ICA proceed in tandem with reviews under the Competition Act.

Merger or antitrust review and prenotification in Canada are governed by the Competition Act. Mergers that exceed a certain size threshold require the Commissioner of Competition to be notified prior to completion. Whether a notification filing is required is determined by the value of the assets in Canada and the annual gross revenues from sales in, from or into Canada of the parties to the transaction, and of the target corporation itself.

There are sectors in Canada, such as telecommunications and other broadcast-related sections, that have ownership restrictions imposed by the federal government. In addition, Canada has anti-dumping legislation which imposes duties to prevent unfair competition with domestic Canadian goods.

More detailed information on the direct investment and competition laws in Canada can be found in the Foreign Investment & Merger section of this Guide.

6. HOW DO LABOUR STATUTES REGULATE THE TREATMENT OF LOCAL EMPLOYEES AND EXPATRIATE WORKERS?

For employers in Canada, the employment relationship is governed by various federal and provincial acts that provide minimum standards for most employees. In most cases, individual or collective agreements will be governed by these minimum standards. Accordingly, Canada cannot be considered a jurisdiction in which there is employment at will. There are minimum standards which mandate that employees are entitled to receive either notice of the termination of their employment or pay in lieu of notice if their employment is terminated without cause. The legislative requirements are minimum standards only and do not restrict an employee's right to sue for breach of contract, wrongful dismissal or other damages arising from the termination of his or her employment. In the absence of a written contract to the contrary, termination of employment without cause generally requires significantly longer notice periods than those provided by the legislation. Appropriate reasonable notice periods have been established by common law through the litigation process on a case-by-case basis. The courts consider various factors, including the employee's age, length of service, position, remuneration, how the employee came to be employed, their chance of finding replacement employment and the manner of dismissal. The judge will consider all of these factors to determine the appropriate "reasonable notice" period.

Reasonable notice established by the common law in Canada often greatly exceeds the obligations of U.S. employers to their employees. The grounds for termination for cause in Canada are also very limited and reserved for the most serious misconduct (for example, where the termination results from acts of dishonesty of the employee, or where the employee has been warned in writing various times and provided with assistance, yet continues to perform below expectations).

More detailed information on employment law in Canada can be found in the Employment Law section of this Guide. In addition, more detailed information on business visitors (temporary residents), temporary workers, professional workers under the various international trade agreements and permanent residents can be found in the Immigration Restrictions section of this Guide.

7. HOW DO LOCAL BANKS AND GOVERNMENT REGULATORS DEAL WITH THE TREATMENT AND CONVERSION OF LOCAL CURRENCY, REPATRIATION OF FUNDS OVERSEAS, LETTERS OF CREDIT AND OTHER BASIC FINANCIAL TRANSACTIONS?

Banking, currency and negotiable instruments are regulated uniformly in Canada by the federal government. Specifically, all banks in Canada are regulated by the federal government. *The Bank Act*, S.C. 1991, c. 46 is the main federal statute which regulates Canadian banking. Canadian banks are divided into three distinct categories. Schedule I banks are domestic banks that are allowed to accept deposits which may be eligible for deposit insurance. Schedule II banks are foreign bank subsidiaries that are authorized to accept deposits which may be eligible for deposit insurance. Foreign bank subsidiaries are controlled by eligible foreign institutions. Schedule III banks are foreign bank branches of foreign institutions that are authorized to do banking business in Canada.

8. WHAT TYPES OF TAXES, DUTIES AND LEVIES SHOULD A FOREIGN INVESTMENT IN CANADA EXPECT TO ENCOUNTER?

When doing business in Canada, you can expect to encounter sales and transfer taxes, income and capital taxes, and custom and excise duties.

Canada has a 5% goods and services tax (GST) which applies to most goods and services on the purchase price. Those engaged in commercial activity in Canada having worldwide sale of goods and services subject to GST greater than CND30,000 per year must register to collect GST. Registration entitles businesses to input tax credits (ITCs) equal to the full amount of GST paid by them on all business purchases. Some nonresidents carrying on business in Canada are also required to register to collect GST. Most Canadian provinces charge a sales tax ranging between 5% and 10% on tangible property and certain services. Harmonized Sales Tax (HST) has been implemented in Nova Scotia, New Brunswick, Newfoundland, British Columbia and Ontario. HST applies to all goods and services that are subject to GST and ranges between 12% and 15%. Registrants for HST are entitled to claim ITCs. The province of Québec administers its own sales taxes together with the GST. The rate of the Québec sales tax is 9.975%. In addition, a land transfer tax, ranging from .02% to 2%, is payable on the acquisition of real property in each province.

Canada imposes a federal income tax on nonresidents who conduct business or sell real property in Canada. Canada also imposes a federal nonresident withholding tax on certain Canadian source payments. This requirement can be waived if the non-resident is carrying on business through a permanent establishment. Canada has entered into bilateral treaties with many countries which contain tax relief provisions. A foreign tax credit may be available in the nonresident's own jurisdiction. A corporation incorporated in Canada will be considered a resident of Canada for income tax purposes. This means the corporation will be subject to Canadian income tax on its worldwide income. Foreign businesses can also be carried on through branch operations. Provinces and territories typically impose income tax on corporations carrying on business within the province and some impose a capital tax on corporations.

All goods entering Canada go through a customs inspection at the point of entry. Documentation accompanying goods ascertains the transaction value of the goods (the price paid for the goods by the importer, subject to adjustments for royalties, shipping fees and transportation). The amount of customs duty is determined by the customs tariff that sets out a specific list describing the class of goods and setting out the corresponding rate of duty. Member countries of North American Free Trade Agreement (NAFTA) receive a preferential duty rate. Imported goods, such as alcohol and tobacco, are subject to a special duty under the customs tariff that is equal to the excise duty paid by Canadian producers.

There are special anti-dumping duties for imported goods sold in Canada at prices that are below the prices in the home market. Dumping occurs when the "normal value" of the imported goods exceeds the "export price." These anti-dumping duties are imposed to provide Canadian producers with relief from unfair import competition.

More detailed discussion of this topic can be found in the Taxes and Duties section of this Guide.

9. HOW COMPREHENSIVE ARE THE INTELLECTUAL PROPERTY LAWS OF CANADA, AND DO THE LOCAL COURTS AND TRIBUNALS ENFORCE THEM OBJECTIVELY, REGARDLESS OF THE NATIONALITY OF THE PARTIES?

Canada offers a fully developed and modern intellectual property law regime. Through federally based legislation that governs the acquisition and enforcement of intellectual property rights throughout Canada, parties are able to register and protect all aspects of intellectual property, including trade-marks, copyright, patents of invention and industrial designs. Canada is also a party to all of the major world intellectual property law treaties and conventions, including the Patent Cooperation Treaty, the Berne Convention and the various World Intellectual Property Organization treaties. Parties, including those based in foreign jurisdictions, have the ability to enforce their intellectual property rights in either the superior courts of the Canadian provinces, or, more often, in the Federal Court of Canada, which courts are required to enforce Canada's laws fairly and objectively, regardless of a party's national origin.

A more detailed discussion of this topic can be found in the Intellectual Property section of this Guide.

10. IF A COMMERCIAL DISPUTE ARISES, WILL LOCAL COURTS OR ARBITRATION OFFER A MORE BENEFICIAL FORUM FOR DISPUTE RESOLUTION TO FOREIGN INVESTORS?

Whether or not foreign investors will benefit more from bringing a dispute to private arbitration or to the courts will depend on the nature of the dispute. For example, a foreign investor may benefit from having a complex commercial matter arbitrated privately, as the parties can attempt to select an arbitrator who has experience and knowledge related to the subject matter at issue. Private arbitration can also be beneficial because it is generally a much faster process than court proceedings. In either case, Canadian law, and in particular Canada's Charter of Rights and Freedoms, guarantees equality under the law, which extends to foreign participants in court or arbitration proceedings, such that neither party to a dispute should benefit (or suffer) from the fact of their national origin.

INVESTMENT CANADA ACT

Non-Canadians who acquire control of an existing Canadian business or who wish to establish a new unrelated Canadian business are subject to the federal Investment Canada Act (ICA). In either case the non-Canadian must submit either a notification or an application for review. A notification must be filed each and every time a non-Canadian commences a new business activity in Canada and each time a non-Canadian acquires control of an existing Canadian business where the establishment or acquisition of control is not a reviewable transaction.

Only in certain circumstances does the ICA seek to review or restrict new investments by non-Canadians. In general terms, the transactions which are subject to review under the ICA are larger transactions, transactions involving businesses within a prescribed type of business activity that, in the opinion of the Governor in Council, is related to Canada's cultural heritage or national identity, and transactions where the Minister responsible has reasonable grounds to believe that an investment by a non-Canadian could be injurious to national security. Generally, for all other transactions only the notification need be filed.

The ICA applies where a non-Canadian establishes a new Canadian business, or acquires control of an existing Canadian business. The definitions in the ICA provide that natural persons will be "non-Canadians" unless they are Canadian citizens or permanent residents. Under the ICA, a permanent resident is defined as a person within the meaning of subsection 2(1) of the Immigration and Refugee Protection Act who has been ordinarily resident in Canada for not more than one year after the time at which s/he first became eligible to apply for Canadian citizenship. For corporations and other legal entities, the distinction between Canadian and non-Canadian is based on direct or indirect control, and the ICA sets out rules for determining what will constitute control in different circumstances. "Canadian business" is broadly defined to include any business that:

- Has a place of business in Canada,
- Has assets in Canada used in carrying on the business, and
- Employs one or more employees or independent contractors in Canada in connection with the business.

The ICA also contains detailed definitions and rules as to what will constitute an acquisition of control for various kinds of transactions such as asset transactions, share transactions and transactions involving the acquisition of voting interests in entities other than corporations.

There are a number of specific exemptions from the application of the ICA, which include certain securities transactions and venture capital deals, acquisitions of control in connection with realization on security, certain financing transactions, and certain direct and indirect acquisitions of control by insurance companies.

Although the potential scope of the ICA is broad, its impact in the vast majority of transactions is relatively minor. Specifically, most transactions will require only a notification under Part III of the ICA, and will not be subject to review under Part IV. Where an investment is subject to notification under Part III of the ICA, the investor must give notice of the transaction to the Investment Review Division of Industry Canada. The notification may be made before or within 30 days after closing and involves filing information concerning the investor and the investment. The information required for filing is straightforward and suggested forms for filing are available on Investment Canada's website. There are no filing fees.

Businesses that conduct activities involving Canada's cultural heritage or national identity such as:

i) the publication, distribution or sale of books, magazines, periodicals or newspapers in print or machine-readable form, other than the sole activity of printing or typesetting of books, magazines, periodicals or newspapers;
ii) the production, distribution, sale or exhibition of film or video recordings;
iii) the production, sale or exhibition of audio or video music recordings;
iv) the publication, distribution or sale of music in print or machine-readable form; or
v) radio communication in which the transmissions are intended for direct reception by the general public, any radio, television and cable television broadcasting undertakings and any satellite programming and broadcast network services

are considered cultural businesses and are subject to different filing requirements. For clarification, the investor should contact the Investment Review Division of Industry Canada. If the investment includes both a noncultural business and a cultural business, the investor should contact both the Investment Review Division and the Department of Canadian Heritage–Cultural Sector Investment Review to obtain more information regarding filing requirements.

Where a transaction is reviewable under the ICA, the investor is required to file an extensive pre-closing filing called an Application for Review, together with

various supporting documents. The purpose of the review is to determine whether the proposed transaction should be allowed because it will be of "net benefit" to Canada. The Minister of Industry (Minister) is entitled to a period of up to 75 days after filing to make that determination, and in transactions that give rise to substantive issues under the ICA, that review period may be, and often is, extended by agreement between the applicant and the Minister.

A transaction will automatically be subject to review under Part IV of the ICA if the applicable transaction size threshold is exceeded. With certain exceptions that are referred to below, the threshold applicable to direct acquisitions of control where the investor is a WTO member is an indexed amount which was equal to CND344 million in 2013. A lower threshold of CND5 million applies to direct acquisitions in each of the following circumstances:

- Where the investor is not a WTO member; or
- Where the business in question falls within the definition of a "cultural business" as previously described.

Notwithstanding the circumstances above, any investment which is usually subject only to notification, including the establishment of a new Canadian business, and which falls within a specific business activity that in the opinion of the Governor in Council is related to Canada's cultural heritage or national identity and listed in Schedule IV of the Regulations Respecting Investment in Canada, may be reviewed if an Order-in-Council directing a review is made and a notice is sent to the investor within 21 days following the receipt of a certified complete notification.

Where a review is required under Part IV, the ICA prohibits the investor from closing the transaction until the Minister's approval is obtained. An applicant/investor may request special permission to close earlier on the grounds that a delay would result in undue hardship to the investor or jeopardize the operations of the business.

Similarly, under Part IV.1 of the ICA, any investment which would normally be only to notification, including the establishment of a new Canadian business, may be ordered reviewable where the Minister, in consultation with the Minister of Public Safety and Emergency Preparedness, has reasonable grounds to believe that such investment by a non-Canadian could be injurious to national security.

Where a review is required under Part IV.1 and the investment has not yet been implemented, the ICA prohibits the investor from closing the transaction until otherwise allowed under the ICA.

Investment Reviews under the ICA often proceed in tandem with reviews under the Competition Act (Canada) (Competition Act). One of the factors in the net benefit determination under the ICA is the effect that the proposed transaction

will have on competition. For that reason, the reviewing agencies under the ICA will typically seek input from the Competition Bureau, and will not normally approve an application for review until the transaction has been approved under the Competition Act.

PREMERGER NOTIFICATION AND REVIEW

The rules respecting merger or antitrust review and prenotification in Canada are contained in Parts VIII and IX of the Competition Act. The responsible government agency is the Competition Bureau, and filings are made through its office in Hull, Québec. Please note that the thresholds and fee amounts established under the Competition Act are subject to change.

The Competition Act applies to any merger or proposed merger that is likely to result in a substantial lessening or prevention of competition. However, for mergers that exceed certain size thresholds, the Commissioner of Competition must be notified prior to completion. Failure to notify is a criminal offense.

The factors which determine whether a notification filing is required in respect of a proposed merger transaction are the value of the assets in Canada and the annual gross revenues from sales in, from or into Canada of the parties to the transaction, and of the target corporation itself. More specifically, for a merger transaction which takes the form of the acquisition of voting shares of the corporation carrying on the target business (or of its parent corporation), two monetary tests or thresholds are applicable, and they may be summarized as follows:

- The parties to the transaction (including their respective affiliates) together have assets in Canada with an aggregate value exceeding CND400 million or annual gross revenues from sales in, from or into Canada exceeding CND400 million; and
- The corporation, the shares of which are being acquired (and corporations controlled by it), has assets in Canada with an aggregate value exceeding CND80 million or annual gross revenues from sales in or from Canada exceeding CND80 million.

Both monetary tests or thresholds are subject to annual adjustment.

The first of the above tests is often referred to as the "party size threshold," and the second as the "transaction size threshold." For the purposes of the party size threshold, in a share purchase transaction, the parties are considered to be the purchaser of the shares and the corporation whose shares are being purchased.

For a merger transaction which involves an acquisition of assets, the same two tests apply, except that the transaction size threshold is applied to the value of

the assets being acquired and the annual gross revenues from sales in or from Canada generated from those assets.

A merger notification filing is required where **both** the party size threshold and the transaction size threshold are exceeded. Where a notification filing is required, the parties to the transaction are obligated to make the filing. The current filing fee for merger prenotification is CND50,000.

The initial waiting period during which parties may not implement a notifiable merger is 30 days after notification by parties (subject to early termination of the waiting period by the Bureau). If more information is needed, the Commissioner can issue a Supplementary Information Request any time during the initial waiting period. A Supplementary Information Request triggers a second 30-day waiting period, which commences when all information required to be provided in the Supplementary Information Request has been received.

The merger review process is initiated by an application to the Competition Tribunal for a remedial order on the grounds that the proposed transaction prevents or lessens, or is likely to prevent or lessen, competition substantially. The Commissioner of Competition may commence such an application before, or within one year after, substantial completion of the merger transaction.

If the parties to a proposed merger transaction desire certainty before closing, they may apply to the Competition Bureau for an Advance Ruling Certificate (an ARC). The fee for an ARC application is the same as the fee for a notification filing, and the supporting information that the Bureau will require in the first instance is substantially the same as well. If the Bureau issues an ARC in respect of a proposed merger transaction, it is estopped from applying for merger review in respect of that transaction as long as the transaction was fully and accurately described in the ARC application and is completed within one year after the issuance of the ARC. If the Bureau declines to issue an ARC, or if none is applied for and a notification filing is made under Part IX of the Competition Act, the Bureau may give some measure of comfort to the parties by issuing a nonbinding "no action letter" stating that in its view, grounds do not exist at the time of the letter to initiate merger review proceedings before the Competition Tribunal.

ANTI-DUMPING

In order to discourage the importation of goods at prices below the price at which such goods would be sold in the exporter's home market, Canada has anti-dumping legislation which imposes duties to prevent unfair competition with domestic Canadian goods. Similar duties may be payable when imported goods are subsidized in their country of manufacture. For a more detailed discussion, see the Customs and Excise Taxes section of this Guide.

Canada has become a world leader in reducing global trade barriers. Free trade with the United States and Mexico and freer trade with other countries have lowered many of the barriers to entering into the Canadian market. Canada, with its rich resources and vibrant marketplace, presents many opportunities for foreign businesses and investors. The foreign investor is encouraged to explore the competitive advantages of Canada. Sensitivity to the cultural, administrative and legislative differences in Canada will assist an enterprise's entrance into the Canadian market.

Through the general information provided in this book, we have attempted to illustrate the highly multicultural society that is Canada and to provide an overview of some of the main issues faced by foreign businesses and investors in Canada. It is important for foreign businesses and investors wishing to invest in Canada or enter into trade with Canadian businesses to understand the laws and culture of this country and to seek the advice of counsel at the appropriate time.

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