

Corporate Aspects of Trading and Investing Canada

1. INTRODUCTION

This brief memo relates to different ways to enter the Canadian market, and to the setting up of a corporation in Canada. It outlines the most commonly used profit-driven entities.

2. METHODS OF MARKET ENTRY IN CANADA

2.1 DISTRIBUTION AND AGENCY

One can use different strategies to export and distribute its goods in Canada. Distribution contract and agency contract are some of those.

Distributors buy goods from exporters to resell them at their own risks and for their own benefit. Still, distributors contribute directly and very closely to the distribution network, and are economically controlled by the exporters.

Agents are committed to finding clients for exporters. They negotiate contracts and are sometimes authorized to conclude and sign them on behalf of exporters.

2.2 BRANCH

Export and distribution of goods can also be done through branches.

2.3 PARTNERSHIPS

A partnership may be formed when two or more individuals or corporations carry on a business for profit. Unlike a corporation, a partnership is not a separate legal person. Partnerships are also distinguishable from joint ventures.

Canadian law recognises two forms of partnerships: general and limited.

In general partnerships, whether created by written agreement or not, each partner has unlimited liability for the debts and obligations of the partnership. General partnerships are governed by provincial law and registration requirements.

Limited partnerships are created under provincial statutes that require registration. One or more partners in a limited partnership must be designated as a general partner with unlimited liability for debts and obligations of the partnership. The liability of each of the remaining partners is limited to that person's investment.

2.4 SOLE PROPRIETORSHIPS

A sole proprietor is an individual who carries on business for his or her own account without the use of an intermediary organisation or the participation of other individuals, except employees. The sole proprietor is entitled to all the profits of the business and is personally responsible for all taxes, losses and liabilities.

2.5 JOINT VENTURES

A joint venture is an association of persons, natural or corporate, who agree by contract to combine their respective resources in an undertaking for joint profit without forming a partnership or a corporation. The agreement must establish a community of interest among the joint ventures, each of whom is both a principal and an agent in dealing with others, participating in the venture. Whether the joint venture is treated as a partnership depends on the agreement between the parties.

2.6 TRUSTS

In a trust, one person for the benefit of another holds the legal title to property. In addition to holding legal title to the property, the trustee is endowed with powers to manage it. Absent bad faith or negligence on the part of the trustee, the beneficiaries have little right to impose their will on the trustee. Because of the separation between the beneficial ownership and the management of trust property, trusts are rarely used for active business ventures in Canada. They are used primarily to hold investments, to defer taxes and to accomplish estate-planning objectives. Laws governing trusts in the province of Quebec differ from those of the rest of the country.

2.7 CORPORATIONS

Canadian companies may be incorporated under the *Canada Business Corporation Act* (CBCA) or any of the provincial or territorial corporations acts. Aside from providing limited liability to their shareholders, corporations offer many other business advantages. Under the statutes of most Canadian jurisdictions, a corporation is endowed with the status of a person and may therefore own property, carry on business, possess rights and incur liabilities.

3. FORMATION OF A LIMITED LIABILITY COMPANY

The Canadian political system integrates a parliamentary democracy on the Westminster model consisting of a federal regime, which shares the power between two levels of government, the federal level and the provincial one. According to the constitution, both levels have the legal authority to legislate on commercial matters. That is the reason why in the first place, the person who wants to establish a company needs to decide if it is going to be under the federal or a provincial act. It is important to note that the choice of a jurisdiction or another does not limit the possibility of doing business anywhere in Canada, but many factors must be taken under consideration to decide: is the company going to do business just in the province or with other provinces or countries, will the company be a subsidiary or a holding company of an other federal or provincial company, if the majority shareholder wants to restrict the power of the minority shareholders or not, etc.

Quebec and federal laws allow the incorporation of a “numbered company” which consist of a company having no specific name but merely an identification number (e.g.: 9001-8234 Quebec inc.).

Also, both laws do not impose a minimal or stated capital. As such, a company can be incorporated with a nominal capital (e.g.: 1\$).

3.1 CONSTITUTION UNDER THE CANADA BUSINESS CORPORATIONS ACT

The federal law provides for the protection of minority shareholders. This is the most important difference with the Quebec Companies Act.

To constitute a corporation under the *Canada Business Corporation Act*, the Director of corporations, in Ottawa, shall issue a certificate of corporation, upon receipt of the articles of incorporation.

The articles of incorporation shall follow the form that the Director fixes and shall set out, in respect of the proposed corporation:

- the name of the corporation;
- the province in Canada where the registered office is to be situated;
- the classes and any maximum number of shares that the corporation is authorized to issue;
- in the case of plurality of classes of shares, the rights, privileges, conditions and restrictions attached to each class;
- if a class of shares is issued in series, the authority given to the directors to determine, before issuance, the number and the designation of the shares of each series and the rights, privileges, conditions and restrictions attached to the shares of each series;
- if the issuance, transfer or ownership of shares of the corporation is to be restricted, a statement to that effect and a statement as to the nature of such restrictions;
- the number of directors or the minimum and maximum number of directors of the corporation;
- any restrictions on the business that the corporation may carry on.

Besides the articles of incorporation, a notice of registered office in the form that the Director fixes shall be sent to the Director together with any articles that designate or change the province where the registered office of the corporation is located.

At the same time, the incorporators shall send to the Director a notice of directors in the form that the Director fixes.

Important fact: at least twenty-five per cent of the directors of a corporation must be Canadian residents. If a corporation has less than four directors, at least one of them must be a Canadian resident.

Also, the approbation of the corporation’s name must be filed. The name of the company may be in English or in French.

Upon reception of the above-mentioned documents and upon the payment of the fees, the Director shall issue the certificate of incorporation. The cost of issuance by the Director of the certificate is 200\$CND if using Industry Canada's online incorporation feature, and 250\$ if using any means other than Industry Canada's online incorporation feature.

3.2 CONSTITUTION UNDER THE QUEBEC COMPANIES ACT, PART IA

Every province has its own incorporation act. In Quebec, to constitute a company, the articles of the company must be filed with the *Régistrare des entreprises* in two duplicates signed by each founder.

The articles of the company set out the following:

- the name of the company;
- the judicial district in which it establishes its head office in Quebec;
- the surname, given name and address of each founder;
- the amount to which its share capital is limited, as the case may be;
- the par value of its shares, as the case may be;
- in the case of plurality of classes of shares, the rights, privileges, conditions and restrictions attached to each class;
- if a class of shares is issued in series, the authority given to the directors to determine, before issuance, the number and the designation of the shares of each series and the rights, privileges, conditions and restrictions attached to the shares of each series;
- the restrictions, if any, imposed on its shares;
- the precise number or the minimum and maximum number of directors; and
- the limits, if any, imposed on its activities.

Like under the federal act, a list of the directors of the company indicating the surname, the given name and address of each, a notice of the address of the head office of the company and a research report on the corporate name desired must accompany the articles. The name of the company, if not a numbered company, has to be in French but may have an English version.

Unlike under the *Canada Business Corporation Act*, there's no restriction concerning a minimum of Canadian residents as directors.

Upon receiving the articles, the documents accompanying them and the fees prescribed, the Enterprise registrar must issue a certificate of incorporation. The fees to be paid upon the issuance of a certificate of incorporation are 300\$CND.

Under Quebec law, it is possible to create shelf companies. This allows corporate lawyers to have a company "on the shelf" which has neither shareholders nor members on its board but are otherwise fully functional. Therefore, if one needs a company immediately, the company is there, created (usually a numbered company) and ready to be used.

However, as the *Companies Act* is to be replaced by a new legislation, the *Business Corporations Act*, expected to become effective late 2010 or early 2011, at the latest, many changes are expected. This new Quebec law will be closer to the federal one, although with important differences. Minority shareholders, for example, will have new recourses that sometime go further than the federal legislation.

3.3 REGISTRATION

The Act respecting the legal publicity of sole proprietorships, partnerships and legal persons applies to every person or partnership subject to the requirement of registration. Are subject to the requirement of registration, among others, every legal person established for a private interest and which is constituted in Quebec, and every legal person not constituted in Quebec, which has its head office in the province of Quebec and carry on an activity in Quebec. Therefore, foreign corporations must present a declaration of registration to the Enterprise registrar if it carries on an activity in Quebec.

There are no fees for the registration of a company established under the *Companies Act*. However, federal corporations and foreign corporation must pay the fees for the deposit of a declaration of registration. The cost is 212\$ for a corporation, 43\$ for a partnership, 32\$ for a sole proprietorship and 32\$ for any other person or group.

The information relating to each registrant is proof of its contents in favour of third persons in good faith from the date on which it is entered in the statement of information.

3.4 CORPORATE FINANCE

Subject to the articles, the by-laws and any unanimous shareholder agreement, shares may be issued at such times and such persons and for such consideration as the directors may determine. Under the *Canada business corporation act*, shares do not and cannot, have a nominal value. They cannot be issued until the consideration for the share is fully paid in money or in property or past services. Under the *Companies act*, the shares may or may not have a nominal value, and do not have to be fully paid to be issued. If it is not fully paid, the amount of the balance is written on the shareholder's certificate. It can also be paid in money, property or past services.

4. MANAGEMENT OF A LIMITED LIABILITY COMPANY

A board of one or more directors shall manage the affairs of the company.

The board of directors may administer the affairs of the company in all things, and make or cause to be made for it, in its name, any kind of contract, which it may lawfully enter into. The board of directors may enact by-laws, not contrary to law, that regulate the business or affairs of the corporation. However, a unanimous shareholder agreement can transfer some of the board's powers to the shareholders who will then vote proportionally to the shares they hold.

Under the *Companies Act* in Quebec, when the board of directors consists of more than six directors, it may elect from among its members an executive committee composed of at least three directors. The executive committee may exercise the powers of the board of directors delegated by such by-law. The new *Business Corporations Act*, to replace the *Companies Act* in late 2010 or early 2011, will have new provisions regarding management of corporations.

Under the *Canada Business Corporation Act*, directors of a corporation may appoint from their number a managing director who is a resident Canadian or a committee of directors and delegate to such managing director or committee any of the powers of the directors.

Every year, an annual meeting of the shareholders of the company shall be held. At such meeting, directors shall adopt the balance sheet for the previous financial year, a general statement of income and expenditure, the report of auditor, and other information respecting the company's financial position.

5. DIRECTOR'S AND OFFICERS' LIABILITY OF A LIMITED LIABILITY COMPANY

Corporations are distinct from their shareholders. That is why their acts shall bind the Corporation.

However, in case of fraud, the court may hold the founders, directors, other officers or members of the corporation who have participated in the alleged act or derived personal profit therefore liable for any damage suffered by the corporation. In no case may a corporation set up judicial personality against a person in good faith if it is set up to dissemble fraud, abuse of right or contravention of a rule of public order.

Under the law, officers can sometimes be held liable for their act. Under the *Companies Act*, a company may not grant a loan to a shareholder if there is reasonable ground to believe that it could not discharge its liabilities when due. Directors who authorize the granting of financial assistance in contravention with the Act are severally liable for the sums involved and not yet recovered. Also, when a dividend is declared or paid and, consequently, the company becomes insolvent, the directors may be held liable for the sums not yet recovered. There are also other situations where a director could face a personal liability (misrepresentation, making of a false documents). The new *Business Corporations Act*, replacing the *Companies Act* and to become effective in Quebec late 2010 or early 2011, will provide for new liabilities, new means of exoneration and new rules regarding conflicts of interest.

6. TAXATION OF PROFITS

The effective rate in Quebec varies from 19% to 45.6% depending on the type of income and the residence of the shareholders.

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