

Welcome to Canada: what foreign businesses should know before settling up north

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This article provides you with a brief overview of the main considerations that come with expanding your business into Canada. For an overview of employment considerations when expanding your business globally, [please see our article](#).

Business formation: which vehicle should you choose?

When expanding your business into Canada, the first decision that you must make is how you will structure your business. Will your business be carried on directly, as a branch of the foreign entity, or should it be created as a separate Canadian business organization? A separate entity may take the form of a subsidiary corporation (with either limited liability or, in some provinces, unlimited liability), a proprietorship, or a partnership (which may be general or limited) or some form of joint venture.

Advantages of a branch office

Lower startup costs: The branch office of a foreign corporation need only apply for an extra-provincial license to carry on business in each province in which it operates. Extra-provincial licenses are relatively straightforward and inexpensive to obtain.

No Canadian resident director requirements: Depending on the jurisdiction of incorporation, a Canadian subsidiary may need a prescribed number (eg, 25 percent) of resident Canadian directors (as detailed below). However, no such requirements apply to branch offices.

Advantages of a subsidiary corporation

Containment of liability: As a general rule, a Canadian subsidiary will have limited liability, and claims made against it would not extend to its foreign parent. A branch office does not have limited liability protection, and as a result the foreign corporation may be liable in Canada. Furthermore, with a Canadian subsidiary, only the directors of that subsidiary may be subject to potential liability, as opposed to the directors of the parent corporation in the case of a branch office.

Application of Canadian laws: A foreign parent corporation using a branch office could become subject to several Canadian laws to which it would not be subject if it used a subsidiary, including Canadian tax legislation requiring foreign corporations to open their books and records to Canadian tax audit. Only directors of the Canadian subsidiary may be subject to potential liability, as opposed to the directors of the parent corporation in the case of a branch office.

Filing separate tax returns: A Canadian subsidiary will file its own separate tax returns in Canada. There is no need for the foreign parent corporation to file tax returns in Canada.

Dealing with local authorities, lenders, and contract counterparties: It may be easier for a subsidiary corporation to obtain regulatory approvals, loans and other financing, and to enter into contracts with other Canadian companies.

Market impact: Operating as a Canadian subsidiary often has a greater impact on clients and suppliers than a branch office because it fosters a perception of permanency.

Employees and creditors: Potential employees may feel that being employed by a Canadian entity offers more stability and job security than being employed by a branch. Similarly, potential creditors may be less willing to deal with a branch because of an impression that loan satisfaction and debt recovery could be more difficult.

On a balance, the use of a subsidiary is generally preferred.

The following assumes you have opted for the incorporation of a Canadian subsidiary to your business.

Where should you incorporate?

In Canada, companies may be incorporated under the federal *Canada Business Corporations Act* (CBCA) or under one of the analogous provincial or territorial business corporations acts.

The CBCA and several provincial acts require that at least 25 percent of the directors of a corporation be resident Canadian [1]. These acts further provide that if a corporation has fewer than four directors, at least one must be a resident Canadian. British Columbia, Nova Scotia, Prince Edward Island, New Brunswick, Quebec, Alberta, and Ontario's acts do not have a directors' residency requirement.

If your company can easily appoint enough resident Canadians to serve as directors, then you may consider incorporating under any of the acts considered. If identifying resident Canadian directors could be a problem, consider incorporating under Provincial Acts that do not have residency requirements, taking into account the other factors discussed below.

If you are an American business, there may be US tax advantages to choosing to form the Canadian subsidiary as an unlimited liability company (a ULC) in a province without residency requirements. Unlike regular Canadian companies, ULCs are treated as flow-through entities for US tax purposes. In some situations this can be advantageous for the overall tax planning of the business.

How to set up the new company?

The process of forming a company in Canada is similar to setting up a corporation in the US. In order to incorporate federally or in any Canadian province or territory, a company must submit its articles of incorporation and run a name search report. Your new subsidiary's articles of incorporation will comprise the following:

- name (unless it is a numbered company)
- registered office address (this cannot be a post office box)
- first director(s) and/or incorporator(s) and

- share capital and any share provisions.

After incorporating, the subsidiary will have to address various organizational matters. Its directors will have to pass organizing resolutions which will include approving the bylaws, banking authority, appointing directors and officers and issuing shares.

If your company plans to finance its new Canadian subsidiary, the method capitalization will have to be assessed. As the Canadian corporate tax rate of approximately 27 percent is currently lower than the US corporate tax rate, for example, it is now typical to finance Canadian subsidiaries exclusively with equity.

In addition, the subsidiary will need to complete various registrations in order to fully operate in Canada, including the opening of accounts with the Canada Revenue Agency.

What else should you keep in mind?

Employment

- If Canadian employees will be hired, you may want to apprise yourself of the basic features of Canadian employment law, including employment standards, occupational health and safety, human rights and privacy legislation.
- Employment agreements with the Canadian entity for all employees in Canada are strongly recommended as there is no "at will" employment in Canada and severance costs can be significant if not properly limited by contract. It is advisable that your employees in Canada not be employed by your non-Canadian business.

Intellectual property

- It is recommended that you consult with legal counsel on intellectual property matters as the preferred location of intellectual ownership from a legal perspective will depend on a number of factors, including the type of intellectual property, and whether the intellectual property in question is a derivative of any prior intellectual property. By way of example, trademarks used by both a foreign parent and Canadian subsidiary corporation would normally be owned by the parent or by a holding company. Regardless, whoever owns the trademarks needs to properly license them to everyone who uses the trademarks. In contrast, copyright created by a subsidiary corporation should usually be owned by such subsidiary, unless the works in question are improvements or derivatives of works owned by the parent company.
- You should consider protecting your businesses' trade names and marks and other intellectual property under Canadian law. For example, even though legal rights to a trademark arise from usage alone, unregistered trademarks do not benefit from the same protections as registered trademarks in Canada. Registration is often advisable.

Other

- The company should consider whether any industry specific regulations or licenses will be required in order to carry on its business in Canada.
- As a foreign business, the company will have to notify Industry Canada under the [Investment Canada Act](#) of the establishment of an investment in the subsidiary.

- Canada has strict anti-spam and privacy legislation. The company will need to have a program in place to comply with the legislation. The penalties for breaching the legislation can be massive.

Useful links

- The Government of Canada has produced a webpage which sets out the distinctions between different business vehicles.
- To stay current on the most recent developments in Canada's legal landscape, visit our [Canada in Focus](#) blog.

^[1] "Resident Canadian" generally means an individual who is a Canadian citizen ordinarily resident in Canada or a permanent resident within the meaning of the Immigration Act (Canada) and ordinarily resident in Canada.

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