The ten most frequently asked questions when companies are looking to expand their enterprises into the Canadian market.
Doing Business in Canada

Members of Minden Gross LLP have combined their expertise for the following ten questions that are most often asked when companies are looking to expand their enterprises into the Canadian market. Lawyers from the Business Law, Tax, Bankruptcy and Insolvency, Labour and Employment, Real Estate and Litigation groups have shared their knowledge here so that you will be successful.

Minden Gross LLP is a business law firm based in Toronto, ON, Canada. As the exclusive Toronto member of Meritas Law Firms Worldwide, one of the world’s largest and most respected providers of legal services, we have the unique ability to help companies grow their business in Canada while also having access to over 6,900 lawyers in over 220 global markets around the world.

For more information about Doing Business in Canada, please contact:

Brian J. Temins, MBA
Partner
(416) 369-4169
btemins@mindengross.com
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How does Canada protect personal information and how do its privacy laws impact the way organizations conduct business in Canada?

To minimize the risk of violating Canadian privacy legislation, businesses need to establish a privacy policy and practices that conform to Canada’s privacy laws and fair information practice principles. These policies and practices need to be communicated effectively to all relevant employees and they should be transparent to all customers. Canada has both Federal and Provincial privacy acts.

The federal *Personal Information Protection and Electronic Documents Act* (PIPEDA) sets out specific procedures regarding the collection, use and disclosure of personal information. PIPEDA applies to every private organization that collects, uses or discloses personal information in the course of commercial activities. A commercial activity includes any transaction, act or conduct that is of a commercial character, including the selling, bartering or leasing of donor, membership or other fundraising lists. Personal information means information that can be used to identify an individual. PIPEDA sets out 10 Fair Information Practice Principles that businesses must follow in establishing policies for the collection, use and disclosure of personal information:

1. Accountability
2. Identifying Purposes
3. Consent
4. Limiting Collection
5. Limiting Use, Disclosure and Retention
6. Accuracy
7. Safeguards
8. Openness
9. Individual Access
10. Challenging Compliance

Generally, if a business collects, uses, or discloses personal information, it must first inform the individual and obtain his/her consent.

Federal and provincial privacy laws must also be considered in any business transaction that involves the disclosure of personal information. Examples are the purchase of a business, which requires the prior disclosure of information under the legislation, or the collection of customer information related to individual sale transactions with Canadian consumers.

Provinces that enact substantially similar privacy protection legislation are exempt from the application of PIPEDA. Alberta and British Columbia have done this. In Ontario, PIPEDA regulates disclosure of
personal information within the commercial sector, while the exchange of personal health information is regulated by the province’s *Personal Health Information Protection Act* (PHIPA).

Failure to comply with Canada’s privacy laws can result in complaints to the Federal or Provincial Privacy Commissioners, investigation by these Privacy Commissioners, orders or fines.

**What are the laws and regulations that apply to a foreign investor acquiring a Canadian business?**

**A. Investment Canada Act**

The federal *Investment Canada Act* (ICA) applies to transactions in which non-Canadians acquire control of an existing Canadian business or establish a new Canadian business. In either case, the non-Canadian must submit a Notification or an Application for Review to the federal government, which then decides whether to approve or reject the proposed transaction.

For the purposes of the ICA, individual “Canadians” include citizens or permanent residents who have been living in Canada for more than one year after becoming 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. “Canadian business” is broadly defined to include any business that has assets, a place of business and one or more employees or independent contractors in Canada.

The ICA also contains detailed definitions and rules as to what constitutes 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 several specific exemptions from the application of the ICA. These include certain securities transactions and venture capital deals, acquisitions of control in connection with the realization on security, certain financial transactions and certain insurance company direct and indirect acquisitions of control.
Most transactions are not subject to formal review under the ICA. Parties are only required to submit a notification form either before the transaction is completed or within 30 days thereafter.

An acquisition of a Canadian business by a non-Canadian may be subject to review if the value of the assets being acquired exceeds the applicable transaction size threshold. The threshold for investors from WTO member countries is fixed annually by regulation. With certain exceptions, the 2011 threshold has been fixed at $312 million. Non-WTO member investors face a lower threshold.

Also, a review may be required for a transaction that would otherwise not be reviewable if it involves Canada’s cultural heritage or national identity or if it might affect national security.

Where a transaction is reviewable, the investor is required to file an extensive pre-closing filing called an Application for Review together with various supporting documents. The investor is prohibited from closing the transaction until approval has been obtained. An investor may request special permission to close earlier on the grounds that a delay would result in value hardship or jeopardize the business. The purpose of the review is to determine whether the proposed transaction is of “net benefit” to Canada.

Investment reviews under the ICA often proceed in tandem with reviews under the Competition Act. One of the factors in the net-benefit determination is the effect that the proposed transaction will have on competition. For this reason, the ICA reviewing agency 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.

B. Merger Pre-Notification and Review

Canadian rules respecting merger or anti-trust review and pre-notification are contained in the federal Competition Act. The Act establishes two threshold tests for determining whether a prospective merger requires formal approval. The first, sometimes referred to as the party size test, is based on the value of the assets in Canada and the annual Canadian gross revenues of the parties to the transaction (including their respective affiliates).

The second test, sometimes referred to as the transaction size test, is based on the value of the assets in Canada and the annual Canadian gross revenues relating to the business that is the subject of the transaction. Where both the party size test and the transaction size test are exceeded, the Competition Act requires both parties to make a notification filing in advance of the transaction.
The Commissioner of Competition, responsible for enforcing the *Competition Act*, may request the Competition Tribunal to review a proposed transaction on the basis that it will, or is likely to, prevent or lessen competition substantially. Strictly speaking, such an application is possible even in relation to a transaction to which the merger pre-notification requirements do not apply. If an application challenging a transaction is ultimately successful, a wide range of remedial orders is available, including an order dissolving the merger if it has been completed or prohibiting its completion if it has not.

Where a proposed merger requires pre-notification, it is common for the parties to apply to the Competition Bureau, the responsible government agency established under the Act, for an Advance Ruling Certificate (ARC). If an ARC is issued in respect of a proposed merger, the Competition Bureau will not subsequently challenge the transaction as long as the information provided in the ARC application is complete and accurate and the transaction is completed within a year after the ARC is issued. As an alternative to an ARC, the Competition Bureau may issue a “no action” letter advising the parties that it does not intend to commence an application for merger review.

### C. Anti-Dumping

Canada has anti-dumping legislation that imposes duties to prevent unfair competition with domestic goods. This legislation aims specifically at preventing the importation of goods at prices below their selling price in the exporter’s domestic market. Duties may also be imposed when imported goods are subsidized in their country of manufacture.

### What does a foreign investor need to know about federal and provincial labour and employment laws in Canada?

Canadian workplaces are regulated by both statutory and common law. Most workplaces are regulated by provincial statutes that vary from province to province. A new business venturing into Canada would be wise to determine the specifics that will affect employees in the province where it will be operating. Some of the issues investors need to be aware of are:

#### A. Successor employer

Most provinces have statutory provisions that deem employment to be continued after the disposition of assets. This results in the purchaser’s responsibility for the previous tenure of the employees of the purchased business. As described below, this can result in substantial obligations including, but not limited to, amounts due on termination without cause as well as accrued and unpaid vacation pay. If implemented properly, employment contracts can help limit a purchaser’s obligations,

Unionized workplaces present their own unique set of factors. On the sale of a business in most provinces, the collective agreement is deemed to bind the purchaser unless the provincial labour board orders otherwise.
B. Termination without cause

Canadian notice or pay provisions can be substantial and do not follow an “at will” model. The common law specifically provides that all employees are entitled to reasonable notice or pay in lieu of notice upon termination. Reasonable notice is based on an employee’s age, length of service, level of responsibility, ability to find replacement employment, manner of dismissal and circumstances of hire. Each case is determined on its own facts. For example, a long-service, senior employee could be entitled to as much as 24 months’ pay or notice.

Employers may contract out of these obligations but such arrangements cannot provide for anything less than the required statutory payments that exist alongside the common law obligations. While these statutory payments vary from province to province, an employer should be prepared generally to pay one week per year of service to a maximum of eight weeks for termination pay and in certain provinces, severance pay as well. Again, employment agreements can assist employers by limiting obligations on a termination without cause.

C. Statutory leaves of absence

Each province grants employees leaves without pay for various reasons (i.e., parental, pregnancy, emergency) with a statutory right to be re-instated to the position they held prior to the leave.

D. Human rights obligations

Each province has statutes that prohibit discrimination and harassment based on prohibited grounds such as race, colour, religion, sex, sexual orientation, age, disability and family status. To protect employers against human rights applications, written anti-harassment/anti-discrimination policies are highly recommended.

E. Deductions and remittances

In most provinces, employers are required to deduct provincial and federal taxes, employment insurance, Canada pension plan payments, workplace safety premiums and employer health taxes. There is personal director liability for failing to make these payments.
What do foreign investors need to know about Canada’s government and legal system?

A. Canada’s Government

Canada is both a constitutional monarchy that operates under a parliamentary system of government and a federal state comprising three territories and 10 largely self-governing provinces. Parliament is located in Ottawa, the capital of Canada, and comprises the House of Commons and the Senate. The 308 members of the House of Commons are elected and the 105 Senators are appointed by the prime minister.

The Constitution of Canada, which consists of several major pieces of legislation dating back to Confederation in 1867, distributes power among three separate branches: the executive, the legislative and the judiciary. It further divides political authority between the federal government and the legislative assemblies in the 10 provinces. Areas such as defence, foreign affairs and international trade, the monetary system, patents, bankruptcy/insolvency, criminal law and certain “national” sectors such as financial services and telecommunications fall under federal jurisdiction. The provinces have legislative authority over critical areas as education, health care, municipal affairs, securities regulation and natural resources.

B. Legal system and courts

Canada’s legal system is based on British common law, with the exception of the province of Quebec, which follows the French-based civil law system in matters of private law. Commercial litigation usually takes place in the federal courts or in a province’s superior court. Canada generally has a “loser pays” civil litigation system, meaning that the losing side in a legal action usually pays some portion of the successful party’s legal costs.

For example, in Ontario, the country’s most populous province and where most of its economic activity takes place, the Superior Court of Justice comprises various branches including the Commercial List Court in Toronto and the Small Claims Court. The Commercial List Court, which hears most business-related matters, has a team of judges with experience in managing complex commercial litigation. For claims less than $25,000, the Small Claims Court is a less expensive and faster way of settling disputes.

The Ontario Court of Appeal is the province’s highest court. Appeals from this court, as well as from all other provincial appellate courts, may be heard by the Supreme Court of Canada, whose decisions are final and binding on all lower courts.
The federal government has also established the Federal Court, the Federal Court of Appeal and the Tax Court. The Federal Court specializes in areas such as intellectual property and maritime law and federal-provincial disputes, while the Tax Court specializes in tax cases. All courts generally look to Canadian jurisprudence, particularly that from their own province, but may also consider English and U.S. law as well as decisions from other common law Commonwealth jurisdictions such as Australia and New Zealand.

Ontario has a mandatory mediation program in Toronto and Ottawa for most civil, non-family case-managed actions.

Arbitration is an increasingly popular form of settling commercial disputes and Canadian courts will generally recognize and enforce arbitration decisions made in other jurisdictions.

What are the main forms of business organization in Canada? How does one choose which one is most suitable from a tax and liability perspective?

Some of the main forms of business organization in Canada are:

A. Corporations

A corporation is a distinct legal entity that has perpetual existence and is afforded all the rights of a natural person. The shareholders’ liability exposure is limited to the amount of their equity investment.

A corporation offers investors access to a wide variety of capital and financing opportunities. Corporations may be incorporated and organized under either the federal Canada Business Corporations Act (CBCA) or the equivalent legislation in any of the provinces. The respective advantages of various corporate statutes will determine the choice made. While the CBCA and some of the equivalent provincial legislation require that some percentage of the board of directors be resident Canadians, certain provinces do not have residency requirements.

B. Unlimited liability corporations

Nova Scotia, Alberta and British Columbia provide for the...
incorporation of unlimited liability corporations, which may have significant tax advantages for U.S. corporations.

C. Foreign branch corporations

In most areas of commercial activity, foreign corporations are generally entitled to carry on business in Canada as a branch, provided that extra-provincial licenses are obtained in the relevant jurisdictions. Failure to create a separate corporate entity will expose the foreign corporation to all liabilities incurred in the Canadian operations. Furthermore, if independent financing for the Canadian operation is required, it will be easier to obtain if a Canadian or Provincial Corporation exists.

D. Partnerships

A partnership is a relationship that exists between two or more people (individuals or other entities) who carry on business in common with a view to earning profit. Each partner is liable for all of the debts and the liabilities of the partnership. Unless otherwise specified in a partnership agreement, all partners must contribute equally to the capital of the partnership, are entitled to share equally in any profits and obligated to share equally in all losses. Partnerships are governed by provincial statutes. However, partnership agreements can override the statutes, and it is almost always advisable to establish one.

E. Limited partnerships

A limited partnership restricts the exposure of passive individual partners to any liabilities incurred by the business. In a limited partnership, there are one or more general partners (who are exposed to unlimited liability) and one or more limited partners. Liability varies by province. Under Ontario legislation, for example, limited partners become liable as a general partner in the event they take part in the control of the business.

F. Limited liability partnerships

In a limited liability partnership, individual partners are personally liable only for their own actions and for those of the people they directly supervise or control. However, limited liability partnerships are available only in certain professions.
What does a foreign investor need to know about Canadian environmental laws?

Both the federal and provincial governments have enacted environmental protection legislation that may impose liabilities on corporations and their directors. Some laws create liability concurrent with the corporation while some create primary liability for acts or omissions of the directors.

The major piece of federal legislation is the Canadian Environmental Protection Act. Several provincial environmental statutes further extend the scope of directors’ liability to include the duty to prevent a corporation from committing an offence. For example, the Ontario Environmental Protection Act and the Ontario Water Resources Act require directors to exercise all reasonable care to prevent the corporation from committing offences such as unlawful discharges, failing to report discharges, unlawfully handling or depositing waste, obstructing regulatory authorities and failing to comply with approval requirements. This potential liability exists irrespective of whether the corporation is charged with or convicted of an offence. If charged, the director or officer has the onus of proving that he or she satisfied the duty.

Almost all of these statutes provide for substantial penalties, including fines of up to several million dollars or imprisonment or both. In most cases, however, due diligence defences are available and it is highly unlikely an investor will be found liable for an environmental offence, except in a most egregious case.

What are the salient features of Canadian bankruptcy and insolvency legislation?

In Canada, an insolvent company (or person) refers to an entity that is unable to meet, or has ceased paying, its obligations as they become due, or whose aggregate property is not, at fair valuation, sufficient to enable payment of all its obligations.

In general, there are three options available to insolvent entities in Canada: restructuring, bankruptcy or receivership.

A. Restructuring
   i) Using the CCAA

A federal Companies Creditors’ Arrangement Act (CCAA) restructuring process is available to insolvent companies with debt in excess of $5 million. In a CCAA restructuring, a company is granted a court-ordered protection period called a stay, during which no party can take any action against the company. Customers cannot terminate contracts or commitments to purchase services because of the filing and suppliers must continue to supply goods and services (provided they are paid going forward from the date
of the stay). However, conventional lenders and suppliers cannot be forced to grant further credit to the company.

A court-appointed monitor (an accounting firm selected by the company) is appointed to monitor the business and financial affairs of the insolvent person, but the company remains in control of its own assets, management personnel and directors.

The initial stay lasts 30 days. A company will often apply for an extension and will likely make subsequent applications to continue to extend the stay as long as it can be credibly argued that the process continues to have some purpose. Completing a CCAA restructuring usually takes between 4 - 18 months.

The stay provides the company with breathing room from its creditors in order to produce a plan, called a plan of arrangement, under which funds or other assets will be made available to the creditors in lieu of paying the company’s debts in full. To succeed, a plan of arrangement must offer creditors more than they would receive under a bankruptcy.

In order for a plan to be accepted by a company’s creditors, it must be approved by those holding two-thirds of the proven debt as well as a majority of the creditors with proven claims. Once the plan of arrangement is accepted by the creditors and approved by the court, the company emerges from creditor protection and is freed from any remaining pre-filing debts.

The main advantage of the CCAA process is its flexibility and debtor-friendly character, such that the company is given a fair chance to restructure its obligations. The main disadvantages are longer restructuring periods and higher professional costs due to the court-driven nature of the process.

**ii) The BIA proposal process**

Restructuring under the federal *Bankruptcy and Insolvency Act* (BIA) is available to all insolvent companies regardless of the size of their debt. Unlike the CCAA process, a company may file a Notice of Intention to Make a Proposal (NOI) and obtain an automatic stay without appearing in court. The federal government appoints a proposal trustee (akin to the CCAA monitor) but, again, the company remains in control of its assets and business operations.

A NOI filing provides the company time to file a proposal, the form of which is materially similar to the CCAA. The voting requirements are the same as with the CCAA. Following acceptance of the proposal by the creditors and approval by the court, the company emerges from bankruptcy protection. Its pre-filing debts are discharged, provided the terms of the proposal are performed.

The main advantages of the BIA proposal process are shorter restructuring periods and fewer court attendances, resulting in reduced professional costs. The main disadvantage is its rigidity. A company is required to file a proposal within 30 days of filing its NOI. Extensions can be sought, but only up to five times for a maximum of six months, following which, if no proposal is filed, the process is deemed to have failed. For companies with complex operations and/or debt structures, six months is often
insufficient. Most importantly, and differing from the CCAA, if a BIA proposal is rejected, the company is automatically deemed bankrupt. For these reasons, companies with sufficient debt tend to use the CCAA process.

**B. Bankruptcy**

At any time, provided it is insolvent, a company can make a general assignment for the benefit of its creditors and become bankrupt. In this circumstance, the company loses control of the operation of its business and its assets automatically vest in the hands of the bankruptcy trustee, subject to the rights of the secured creditors.

The main advantage of a bankruptcy is that it allows management to walk away from the company completely. This loss of control is also its main disadvantage. Bankruptcy usually means the death of a company. While possible, a bankrupt company rarely attempts to restructure under the BIA. Accordingly, filing for bankruptcy carries a stronger stigma than filing for bankruptcy protection.

**C. Receivership**

Receivership is usually a remedy used by a creditor against a debtor company on behalf of one or more creditors. However, in certain limited circumstances, a company may appoint its own receiver with a view to arranging for the sale of its assets for the benefit of its creditors.

A receiver is a third-party accounting firm appointed by either the court, or privately by a secured creditor, for the purpose of managing the business and/or overseeing its sale. The broad underlying purpose of any receivership is to ensure assets are not dissipated during its operation and to maximize value for the benefit of creditors.

It is possible to have a receivership simultaneously with a CCAA or BIA restructuring and following a bankruptcy.

**How does Canada protect intellectual property?**

In Canada, intellectual property rights can be protected in several ways. The three most common are through trademarks, copyrights and patents.
A. Trademarks

The federal Trade-marks Act defines a trademark as a mark used to distinguish wares or services manufactured, sold, leased, hired or performed by the owner of a trademark from similar wares or services of others.

A person can obtain registration in Canada of a foreign registered trademark under certain conditions, and such registration provides the owner with exclusive use of the trademark for 15 years. Registration may be renewed indefinitely for further 15-year periods.

As in most other countries, a trademark cannot be registered if it is clearly descriptive or deceptively misdescriptive of the details of its origin, or if it can be confused with an existing registered trademark.

Under certain conditions, it may be appropriate for a foreign corporation to register a trademark even when it is not actively carrying on business in Canada; e.g., if a foreign corporation grants rights to use or sell a product bearing its trademark.

Because Canada does not use the international class system for defining wares and services, the description of wares and services used in marks from other jurisdictions may have to be redrafted to be registered in Canada.

The Trade-marks Act has not yet been amended to reflect issues surrounding Internet domain names.

B. Copyright

Under the federal Copyright Act, the creator of every original literary, dramatic, musical and artistic work (including computer software databases) has the exclusive right to produce or reproduce in any material form, perform, or deliver in public or publish the work, or any substantial part of the work, or authorize the doing of any of the above.

Copyright exists once a work is created. Canadian copyright generally lasts for up to 50 years following the lifetime of an author, but some exceptions apply with regard to the following:

- Anonymous and pseudonymous works
- Posthumous works
- Cases of joint authorship
- Photographs
- Cinematographic works
- Where copyright belongs to Her Majesty
• Sound recordings
• Communication signals

Canada is a member of the Berne and the Universal Copyright conventions. Under these, copyright protection is extended to nationals of member countries or to works first published in those countries. Copyright infringement can lead to legal action with statutory penalties.

With the evolution of technology and digital information, the Copyright Act has continuously been amended to respond to the online age and to align Canada with its international obligations.

In 2010, a comprehensive new bill was tabled to modernize the Copyright Act, in particular in connection with digital rights. However, as of March 2011, this revision had yet to be enacted. The status of that or other legislation should be consulted in connection with launching any substantive new digital initiatives in Canada.

C. Patents

Under the federal Patent Act, an inventor or assignee of the inventor who is first to file (not first to invent) an application in respect of an invention will be entitled (subject to certain qualifications) to a patent. A patent gives the patentee the exclusive right to make, construct, use and sell the invention for a period of 20 years (non-renewable) from the date of filing the application.

To be patentable, the invention must be new, useful and not have been obvious to a person skilled in the art or science to which the invention relates. Patent infringement action may lead to legal action, and an infringer is liable for damages to the patentee and to all persons claiming under the patentee.

What are the rules regarding foreign investment in the Canadian real estate market?

Real property in Canada is a matter of provincial jurisdiction and with the exception of Quebec, real property law is based on common law principles. In Quebec, real property law is governed by the Civil Code of Quebec. Given the vast differences between the common law and civil law systems, real property law in Quebec is not addressed herein.

A. Acquisition of real property

Land acquisition in Canada typically begins with the parties negotiating and entering into an Agreement of Purchase and Sale (APS). The APS is the foundation of every real estate transaction, setting out the legal rights and obligations of the respective parties. In order to be enforceable, the APS must be written and signed by both parties.
Once all of the APS terms and conditions have been fulfilled, ownership of the property can be conveyed. This is typically accomplished by registering a transfer of title. Canada has two registration systems: the registry system and the land titles system. Under the registry system, the chain of title must be examined and verified for the 40-year period preceding the date of the proposed transaction. Under the land titles system, certification of a title eliminates the need for a title search. While British Columbia, Alberta, and Saskatchewan operate exclusively under the land titles system, Nova Scotia, Prince Edward Island and Newfoundland continue to operate solely under the registry system; Ontario, Manitoba and New Brunswick maintain both systems in varying degrees.

B. Foreign ownership

Canada’s federal Citizenship Act, allows non-residents to acquire, hold and convey real property in the same manner and under the same conditions as Canadian citizens or residents, including corporations and other entities.

C. Investment vehicles

Canada offers a number of investment vehicles, including trusts, special real estate investment trusts (REIT) and joint ventures, through which foreign investors can acquire, hold and convey real property.

i) Bare trusts

Corporations, REITs and individual property owners often structure their real property ownership so that a separate entity (typically a single-purpose corporation) holds registered title to the property as a bare trustee on behalf of the true beneficial owner. Bare trusts offer a number of advantages to foreign investors. For instance, where the beneficial owner is not a legal entity capable of holding registered title to land (such as a REIT, for example), bare trusts provide a useful alternative arrangement. Further, bare trusts provide a number of tax incentives and confidentiality, allowing beneficial owners to transfer ownership of property without undergoing title registration.

ii) Real estate investment trusts

A REIT is a type of trust unique to the real estate market. It functions by consolidating the capital of several investors in order to invest in the real estate market through either (i) the direct acquisition of income-producing real estate assets or (ii) the acquisition, development, management and/or sale of various real estate assets. Investors are typically issued units, or shares, in the REIT and their pro rata share of the REIT’s income or losses.
iii) Joint ventures

A joint venture is a relationship between two or more entities that have jointly invested their assets or carry on business together with a view to profit. Joint ventures can be organized in a variety of ways, including joint-venture corporations, partnerships and co-ownerships/co-tenancies. The joint venture arrangement selected will depend on available tax incentives and business concerns.

D. Tax considerations

i) Land transfer tax

Every Canadian province imposes some form of land transfer tax or registration fee when land is conveyed. Although the tax rate varies across the provinces, it is typically based on the sale value.

Ontario is the most aggressive province in taxing real estate conveyances. Imposed at graduated rates, the land transfer tax for most commercial transactions is approximately 1.5 per cent of the total consideration. For most commercial property sales in Toronto, there is an additional municipal land transfer tax of approximately 1.5 per cent.

ii) Sales tax

In Canada, a Federal Goods and Service Tax (GST) is payable on the acquisition of real property. Most provinces levy a Provincial Sales Tax (PST) as well, and a number of provinces have combined the two taxes as a Harmonized Sales Tax (HST).

iii) Withholding taxes

Moneys paid by Canadians to non-residents as interest, dividends, rents and most other forms of income from property are subject to Canada’s withholding tax. The withholding rate is 25 per cent, but may be reduced in certain instances under an applicable tax treaty.

E. Financing and security

Most real estate financing in Canada is arranged with institutional lenders such as banks. Financing terms will vary among institutions depending on the nature of the transaction and the risks involved.

When providing such financing, lending institutions typically take both primary and collateral security in the real property and related assets. While the most common form of primary security is a mortgage or charge, collateral security typically includes general security agreements, personal guarantees or an assignment of leases and rent where the property receives rental income.
What are the key taxation considerations for a foreign investor?

A. Basis of ordinary income taxation

Under the federal Income Tax Act (ITA), the primary basis for applying taxation is residence. A resident of Canada is taxed based on his/her worldwide income. In contrast, a non-resident is taxed only on taxable income earned in Canada in cases where the non-resident was employed in Canada, disposed of “taxable Canadian property” or carried on business in Canada. (Taxable Canadian property includes real estate in Canada.) Non-residents may also be subject to provincial income tax in cases where the non-resident carries on business through a permanent establishment.

B. Tax treaties

Canada has entered into over 80 tax treaties with other jurisdictions. A tax treaty may reduce or eliminate a non-resident’s ordinary income taxation or withholding tax. Generally, these tax treaties provide that business income earned by a non-resident is not taxable in Canada except to the extent that such income is attributable to a permanent establishment (i.e., a fixed place of business) in Canada. Withholding tax rates imposed under the ITA as well as the branch tax rate (discussed further below) are usually reduced in the tax treaties.

C. Residence

Under the ITA, a corporation is deemed to be resident in Canada if it was incorporated in Canada after April 26, 1965. Pursuant to common law principles, a corporation is also considered to be resident in Canada for income tax purposes if its central management and control is located in Canada. This is generally based on where the directors of the corporation meet and exercise control. Residency “tie-breaker rules” in any applicable tax treaty must also be considered.

D. Subsidiary versus branch

A foreign corporation may carry on business in Canada either through a subsidiary as a separate legal entity or as a branch or division of the foreign corporation.

If the foreign corporation incorporates a Canadian subsidiary, the subsidiary is deemed to be a resident of Canada. If the subsidiary repatriates profits to its foreign parent, non-resident withholding taxes may apply, depending on the nature of the payment.
If the foreign corporation does not incorporate a Canadian subsidiary and carries on business in Canada through a permanent establishment, Canadian tax will be applicable on income from its business operations. In addition, a special branch tax will be imposed on the after-tax profits of the Canadian branch operations that are not reinvested in Canada. The branch tax rate is 25 per cent, but may be reduced by an applicable tax treaty. The branch tax serves as a rough equivalent to the withholding taxes that would have been payable on dividends paid by a Canadian subsidiary to its foreign parent.

When choosing between a subsidiary and a branch, non-income tax concerns such as regulatory compliance or the desirability of segregating Canadian assets and liabilities from their foreign equivalents should be considered. As well, one should take into account tax considerations including:

(i) the desirability of using any Canadian start-up losses against the foreign parent’s income (possible only with a branch);

(ii) the requirement that a Canadian income tax return must be filed and a certain amount of disclosure about the foreign parent will be necessary where a branch is utilized;

(iii) the ability to subsequently incorporate the branch on a tax-free basis; and

(iv) the likelihood that if a branch is used, one will typically pay the higher of the two tax rates of the two jurisdictions.