Doing Business & Investing In...

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CHRISTOPHER MUNN
HOGG, SHAIN & SCHECK

Christopher Munn
Tax Partner
Hogg, Shain & Scheck

Web: www.hss-ca.com

"Low interest rates, the availability of credit and a sound expanding economy." Christopher Munn shares Canada's invest-appeal.

Christopher Munn is a tax partner with Hogg, Shain & Scheck Professional Corporation in Toronto, Canada. He is a graduate of Wilfrid Laurier University, receiving his CA designation in 1990. Hogg, Shain & Scheck provides accounting, auditing, taxation and management consulting services to entrepreneurs and subsidiaries of foreign entities.

Q What makes Canada an attractive investment/business destination?

Canada is the second largest country in the world with a population exceeding 33 million; half of which resides within 150 kilometres of the U.S. border.

Canada's exports approximately 72% of goods to the United States, 7% to Europe, 4% to China and 2% to Japan.

Businesses currently benefit from low interest rates, the availability of credit and a sound expanding economy. Canadian banks have strong balance sheets due to regulation, strong capitalization and conservative practices. Unemployment rates are slowly improving and inflation remains low.

Foreign investors should consider an investment in Canada for the following reasons:

- Attractive business environment.
- Strong growth record – Canada has led all G7 countries in economic growth from 2003-2012.
- Incredible market access – foreign investors will have access to both NAFTA and the EU once the Comprehensive Economic and Trade Agreement comes into force.
- Highly educated workforce.
- Competitive R&D environment.
- Low tax rates – overall marginal tax rate is the lowest in the G7.
- Financial stability.

Q What policies currently exist in Canada that benefit business and investment?

Investment Canada Act ("ICA"): Foreign investors have always played a significant role in providing the necessary capital to develop Canada's economic potential. Non-Canadian investors must essentially follow the same rules that apply to Canadian corporations. Since Canada has no exchange control laws, investors can easily repatriate profits from Canada.

Foreign investment is subject to limited government regulation which has usually taken the form of:

- Withholding taxes on outbound dividends, certain types of interest or royalties;
- Special incentives applicable only to Canadian controlled corporations;
- Limits on the degree of foreign ownership especially in sensitive areas of the economy.

The ICA's purpose is to encourage investments by both Canadians and non-Canadians which will contribute to economic growth and employment opportunities in Canada. It also provides for a review mechanism of significant investments by non-Canadians to ensure there is a benefit to Canada.

When establishing a new business (except in cultural areas) or acquiring a small business (<$5 million in assets), the foreign investor is only required to notify the government of their investment. No review is required. If a review is necessary, the approval process is usually fast and straightforward due to government imposed deadlines, and the limited range of reviewable transactions. There is a tendency for the government to approve a majority of the reviewable transactions.

Competition Act: This is a Federal statute which outlines the basic principles for the conduct of business that are designed to promote competition and efficiency in the Canadian economy. The Competition Act contains both criminal offences for anti-competitive behaviour and non-criminal provisions regulating the review of certain trade practices and the review of certain merger transactions.

PIPEDA: A foreign investor must be aware of Canada's personal information protection legislation. PIPEDA (Personal Information Protection And Economic Document Act) forces every business to obtain an individual's consent when it collects, uses or discloses the individual's personal information. Each business is responsible for safeguarding all collected personal information.

Employment Standards: Every province has enacted legislation that regulates various aspects of the employer-employee relationship including minimum wage, holiday pay, overtime pay, leaves of absence, termination and severance.

The Canada Labour Code governs the employment standards of a unionized workforce.

Q How does Canada's tax system fit into the business/investment equation?

Income Tax: Canadian residents are taxed on their worldwide income. Non-residents of Canada are usually subject to tax on their Canadian source income, including income from a business or employment carried on in Canada, and income from the disposition of "taxable Canadian property". Individuals are taxed at graduated rates. These rates depend on the type of income, province of residence and other factors. The highest marginal tax rate in 2013 was approximately 50% while the lowest top marginal rate was approximately 39%.

The rate of taxes incurred by corporations depends on the nature and size of the business activity carried on, location and other factors. In 2013, the highest rate of tax applicable to ordinary business profits of a non-Canadian-controlled private corporation was 31%, while the lowest rate was 26%.

Withholding tax of 25% applies to certain types of Canadian source income of non-residents. The withholding rate may be reduced or eliminated by the respective tax treaty/convention. The necessary withholding taxes are the responsibility of the payer.

Carrying On Business Through a Canadian Subsidiary: A corporation incorporated in Canada will be subject to tax on its worldwide income. Transactions with any person not at arm's length (parent corporation) generally takes place at fair market value. Canada's transfer pricing rules will require contemporaneous documentation.

Non-resident owned corporations are subject to special rules which place limits on the deductibility of interest expenses. These thin capitalization rules provide that the interest deduction will be proportionately limited where the debt to equity ratio exceeds 2 to 1.

Carrying On Business In Canada Through A Branch Operation: A non-resident corporation carrying on business in Canada will be subject to the corporate tax rates as noted above as well as branch tax.

Sales & Other Taxes: Canada applies a 5% value-added tax called the goods and service tax (GST) which applies to taxable supplies made in Canada. GST is also charged on taxable goods imported into Canada. Every business involved in a commercial activity is entitled to claim an input tax credit to recover the GST paid.

Currently there are five provinces (New Brunswick, Newfoundland and Labrador, Nova Scotia, Prince Edward Island and Ontario) that have harmonized their provincial tax system with the GST. This harmonized sales tax (HST) applies to the same transactions as the GST and the rates vary between 13% and 15%.

Provincial Sales Taxes: British Columbia, Saskatchewan and Manitoba levy provincial sales tax (PST) to the end-user of most tangible personal property and certain services.

Payroll Taxes: Manitoba, Ontario and Newfoundland and Labrador assess an employer payroll tax that is based on the gross remuneration paid in the Province. Quebec charges a similar tax in the form of contributions to the provincial health services fund.

Other Taxes: Customs duties and excise tax; Provincial capital taxes; Land transfer tax; Annual taxes on the ownership of real estate.

Q What are the various forms of business organizations available to carry on business in Canada?

Some common arrangements are partnerships (general and limited), corporations, branch operation, trusts, co-ownerships, joint ventures, unlimited liability companies (ULC) and proprietorships.

The business structure to be implemented will depend on the circumstances of the investor, the nature of the business activity, the method of financing, income tax ramifications and any potential liabilities.

The most common business organization is a corporation with share capital. A corporation is a separate legal entity from its owners and differs in this respect from partnerships, trusts, co-ownerships and joint ventures. The corporation can be incorporated Federally or under Provincial law.

A partnership is not a separate legal entity and each partner will share in the profits and losses. The Canadian Income Tax Act provides certain rules that allow the "flow through" of losses to the partners which then can be deducted from their other income. Each partner is exposed to the liabilities of the partnership. This exposure can be reduced by forming a limited partnership which essentially limits the partners' risk to its investment in the partnership.

Since a corporation is the most popular vehicle to carry on business in Canada, the foreign investor must be cognizant of the following aspects of Canadian corporate legislation:

- If Federally incorporated, 25% of the corporation's directors must be Canadian. This requirement differs if incorporated under provincial legislation. Some provinces and territories have no residency requirements
- Each director must be an individual
- Directors are responsible for a number of liabilities and obligations
- Directors do not have to be shareholders
- Minority shareholders have significant rights
- Corporation is not obligated to file financial statements with governments
- Shareholders' identity is not a matter of public record
- Books and records of the corporation must be kept in Canada.

A United States entity wishing to carry on business in Canada may consider using an unlimited liability company ("ULC"). This vehicle allows for favourable treatment as "flow-through" entities for U.S. tax law. Recent changes to the Canada-US Tax Treaty should be considered before using an ULC.

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Professional Corporation
Chartered Accountants