

Where to Incorporate in Canada? An Increasingly Level Playing Field

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Introduction:

Competition encourages incremental innovation but, not surprisingly, can lead to substantial conformity.

As one competitor introduces a successful new innovation, it acquires a competitive advantage over other market participants. This advantage may be lasting or of short duration depending upon what barriers exist which make it relatively easy or difficult for others to replicate (or enhance) this new innovation. With low replication barriers, this competitive advantage is short-lived and this “new” innovation appears “old” once everyone eventually adopts it.

The net result is “conformity” as all competitors appear more similar than different over time. This conformity will continue to exist until the next successful incremental innovation appears and, assuming low barriers to replication continue to exist, conformity will again result. Obviously, if such barriers are relatively high, conformity is less likely to arise.

This innovation-conformity “loop” can be readily witnessed in many markets including the Canadian marketplace for “corporate laws”.

A careful review of changes in Canadian federal and provincial business corporations’ legislation over the past decade reveals that the “innovative” standards established by the modern CBCA and OBCA have been replicated to an increasing degree by other provinces.

This innovation-conformity loop can be seen not only within existing substantive “product features” (e.g., oppression remedies, director residency, financial assistance, etc.) but also in the “customer relations” function (i.e., facilitating on-line filings with lower filing fees) and in the area of new product development (i.e., ULCs offered by Nova Scotia, Alberta and now British Columbia).

¹ A very special thank you to various local provincial counsel for their assistance in helping us confirm certain local requirements summarized throughout this short publication.

² Canadian corporate laws are changing (and can be expected to continue to change) at an increasing pace given their importance to local economic development, etc. While the authors have attempted to ensure the accuracy of the contents of this publication with local counsel in each relevant province as at the date hereof, we take responsibility for any inaccuracies and encourage readers to seek the assistance of their own local counsel as necessary or desired.

Clearly, the competition among Canadian suppliers of “corporate laws” has heated up considerably over the past decade and, judging by the innovation-conformity loop seen in the marketplace for ULCs, the volume has been turned up markedly in the past five (5) years. Most recently, proposed law reform in Nova Scotia and Quebec shows a continued culture of conformity.³

This is not surprising as the economic prosperity of a given province is closely linked to its ability to attract capital. Assuming that the volume of new incorporations/continuances within a given jurisdiction has a direct link to the attraction of new capital in that jurisdiction, it is easy to see why business-friendly and “competitive” corporation laws are more important now than ever before.⁴

As acknowledged by Quebec's Minister of Finance in the December 2007 Working Paper on Quebec Companies Act Reform ("**Quebec 2007 Working Paper**"), corporations legislation can become a "tool of economic development" likely to maintain existing companies within a jurisdiction and also attract companies seeking a welcoming legislative structure. The Quebec Companies Act's last major updating was in 1981 and there is concern that, relative to other jurisdictions, Quebec's company law has "now become completely obsolete" and the reformation of this legislation has now become "indispensable". In fact, as evidence of such obsolescence, the Quebec 2007 Working Paper notes that approximately 1/3rd of all CBCA incorporations during each of 2004, 2005 and 2006 were companies with principal operations in Quebec.⁵

Practically, once provincial-specific political hurdles are overcome, the barriers to “innovation replication” within the marketplace for Canadian corporate laws become quite low. Hence, this innovation-conformity loop can be expected to continue for some time resulting in fewer material differences among jurisdictions and simplifying the process of helping clients select a suitable incorporation jurisdiction.

Interestingly, while the marketplace for Canadian corporate laws has become increasingly competitive so too has the marketplace for Canadian legal services. In the face of downward pricing pressures, law firms struggle to become more efficient in an effort to preserve profit margins squeezed by rising input costs and slower revenue growth.

One “efficiency tool” adopted across the entire legal community is the use of “checklists” to streamline discrete legal tasks such as incorporations. While the typical law firm

³ Amendments to the Nova Scotia Companies Act have been passed and are expected to be proclaimed on or about June 1, 2008. In December 2007, the Quebec Minister of Finance issued a working paper seeking industry consultations on broad reform to Quebec's Companies Act. The consultation period ended April 18, 2008.

⁴ This is also true of Canadian securities laws where conformity among provincial rules has arisen by necessity in order to assist Canada, as a whole, to compete with other jurisdictions fortunate enough to have a national regulator (e.g., the USA).

⁵ See Quebec 2007 Working Paper, Page 8.

incorporation checklist is a very useful means of quickly gathering key facts in a "fill-in-the-blanks" manner, it often fails to address fully the topic of "where to incorporate" and does not pose questions to explore this threshold issue.

Overview:

This short publication covers below a broad range of key (non-exhaustive) "jurisdiction shopping" variables and attempts to provide a comparative overview of current Canadian corporate laws across such variables. It is our hope that this short publication will assist counsel to better guide clients in making a more informed decision regarding "where to incorporate" within Canada.

A: How Much Does it Cost and How Fast Can I Get it Done?

- Filing Fees:
 - filing fees currently range from \$100 to \$330 across Canada
- Manual vs. Online Filing Procedures:
 - all jurisdictions currently permit on-line incorporations except Manitoba, Northwest Territories, Prince Edward Island and the Yukon Territories
- What are my “effective date” options?
 - most jurisdictions currently permit “future dating” of articles of incorporation⁶ although certificates of incorporation are typically not issued until the effective incorporation date
- How are Pre-Incorporation Contracts addressed?
 - all jurisdictions (including CBCA) have a regime to permit a corporation to subsequently adopt a pre-incorporation contract except Nova Scotia⁷ and Prince Edward Island

B: How Much Information Do I have to Share Publicly?

- Generally, no jurisdiction (including CBCA) requires the filing of any financial statements, other financial reporting or governance documentation regardless of size.⁸

C: Can I Get the Name I Want and Where Can I Use it?

- It is generally more difficult to obtain approval of a potentially confusing or similar corporate name under the CBCA than under the various provincial statutes (which generally only prohibit identical names).
- However, CBCA corporations that carry on business in various provinces cannot be denied the use of their corporate name if similar to an existing provincial name. In contrast, provincial name clearance does not provide any level of national name protection.

⁶ The only provinces which do not accommodate “future filing” of articles of incorporation are Newfoundland and Prince Edward Island.

⁷ In Nova Scotia, the adoption of pre-incorporation contracts is a matter which can be addressed within a company’s articles of association.

⁸ In Prince Edward Island and Nova Scotia (subject to change as a result of recent law reform), special resolutions must be filed with the Registrar along with a statutory fee in certain limited cases (e.g., resolutions to change a corporate name, to increase capital stock or to effect an amalgamation). Also, in Saskatchewan and Newfoundland, a statutory notice must be filed both when entering into or terminating a unanimous shareholder agreement.

D: Am I Stuck or Can I Move Around (Continuance)?

- Generally, all jurisdictions (including CBCA) have flexible regimes to permit existing corporations to enter or leave their jurisdiction via continuance except Quebec which has restrictions on direct continuances.
- The Quebec 2007 Working Paper acknowledges that Quebec's Companies Act is the only piece of Canadian corporate legislation which does not provide for ease of continuance. If Quebec corporate law reform aims to make this Act equally (or more) attractive than other jurisdictions, a continuance feature should be added (especially to facilitate the continuance of Quebec-based CBCA companies under the Quebec Companies Act once the reformation process has been completed).⁹
- ULC continuance in and out of Nova Scotia is more complicated than for limited liability companies but proposed law reform in Nova Scotia is attempting to simplify the ULC continuance process in Nova Scotia in light of existing ULC continuance rules in Alberta and British Columbia.

E: What Do I Need to Know About Corporate Directors?

- Are Canadian Resident Directors Necessary?
 - many jurisdictions have no director residency requirements – i.e., British Columbia, North West Territories, the Yukon Territories, Quebec, Nova Scotia, Newfoundland, Prince Edward Island and New Brunswick
 - since the CBCA took the lead in 2001, there is generally only a 25% director residency threshold in the following jurisdictions: CBCA, Alberta, Saskatchewan, Manitoba, Ontario and Newfoundland
 - in those jurisdictions that have reduced their director residency requirements to 25%, there are generally now either no residency requirements applicable to the composition of board committees or the committee residency requirements have also been reduced to 25%¹⁰
- Are Directors Subject to Statutory Duties and Liabilities?
 - most jurisdictions (including CBCA) prescribe statutory liabilities and standards of care for corporate directors (subject to available statutory due diligence defences)
 - in Nova Scotia, there is generally no statutory directors' liability so the regulation of director's behaviour is principally addressed by common law and may also be addressed in a company's articles of association

⁹ See Quebec 2007 Working Paper, Page 23.

¹⁰ In Manitoba, although the director residency threshold has been dropped to 25%, any board committee must still be constituted by a majority of Canadian resident directors. See *The Corporations Act* (Manitoba), Sections 100(and 110(2).

- Can Directors Delegate Authority to Shareholders or Board Committees?
 - most of the jurisdictions which do not impose directors' residency requirements do not provide for any "unanimous shareholder agreement" ("USA") regime
 - however, Quebec, New Brunswick and the Yukon Territories do provide for a "USA" regime notwithstanding that they do not impose any director residency requirements
 - of those jurisdictions which do impose a directors' residency requirement, all of them permit the use of USAs
 - as noted above, notice of the entering into of a USA in Saskatchewan and Newfoundland must be filed with the Registrar
 - most jurisdictions permit delegation to board committees only (or to shareholders by way of a USA) but otherwise not to any other persons as this would constitute an improper fettering of board authority
 - Quebec corporate laws are more restrictive and permit delegation only to an executive committee of at least 3 directors provided the board has at least 6 directors, 2/3rds shareholder approval has been obtained and the existing by-laws do not restrict such delegation¹¹

- How are Director Conflicts of Interest Addressed?
 - most jurisdictions have rules for the disclosure and declaration of conflicting (or potential conflicting) interests of corporate directors and for the voting and other procedures to be following at board meetings to approve such matters
 - in Nova Scotia, interested directors must disclose conflicts but are generally permitted to vote

- Are Directors Entitled to Statutory Indemnification?
 - most jurisdictions (including CBCA) provide generally for director indemnification regimes
 - statutory indemnity rules in British Columbia and Prince Edward Island are somewhat more restrictive and limited than Ontario and the CBCA
 - Nova Scotia's Companies Act does not currently provide for statutory indemnification of directors
 - Quebec's Companies Act imposes an obligation on companies to assume the defence of their directors (excluding cases of misconduct extending beyond the exercise of director duties)

¹¹ See Section 92 of the Quebec Companies Act.

F: Are there Restrictions on Providing Financial Assistance?

- Both the CBCA (in 2001) and the OBCA (in 2007) repealed all restrictions relating to related party financial assistance and assisted share purchases.
- In Nova Scotia, proposed legislation will liberalize financial assistance rules but retain a solvency test requirement.
- Quebec's Companies Act continues to prohibit loans/financial assistance by a corporation to its shareholders unless certain complex financial tests are met. The Quebec 2007 Working Paper briefly considers whether these restrictions should be repealed or reformed in future.¹²

G: Speaking About Corporate Governance?

- Where Can I Locate My Head Office?
 - with the exception of CBCA companies, the head office address of a company incorporated under the laws of a specific province must be located within such province
- Where Can I Hold Corporate Meetings?
 - with the exception of Prince Edward Island (which requires meetings to be held within the province), all jurisdictions generally permit corporate meetings (board and shareholder meetings) to be held outside of the jurisdiction of incorporation (although in some cases this flexibility must be provided for in corporate articles/by-laws or via requisite shareholder approval)
 - all jurisdictions generally permit corporate meetings (board and shareholder meetings) to be held via telephone or other electronic means (although in some cases this flexibility must be proved for in corporate articles/by-laws or via requisite shareholder approval)
- What Level of Shareholder Approval Is Need to Effect Fundamental Changes?
 - except for Nova Scotia and Manitoba, the CBCA and other provinces have a 2/3rds shareholder approval requirement for fundamental changes
 - Nova Scotia currently has a 75% special resolution threshold although this is subject to change as a result of recent law reform
 - in Manitoba, a shareholder resolution to amend the articles to convert a corporation with share capital to one without share capital (and vice versa) or to provide for the distribution of remaining property to a charitable organization upon dissolution must receive 95% shareholder approval¹³

¹² See Quebec 2007 Working Paper, Page 21-22.

¹³ See *The Corporations Act* (Manitoba), Section 167(3).

- Where Do I Have to Keep Corporate Records?
 - Alberta, British Columbia, Northwest Territories, Nova Scotia, Newfoundland, Prince Edward Island, Quebec and the Yukon Territories require records to be retained and made available for inspection at a company's registered or head office address or, in some cases, elsewhere within the applicable province
 - the CBCA, Ontario, Manitoba, New Brunswick and Saskatchewan permit record retention at a place other than a company's head/registered office address subject to certain restrictions
 - law reform in Nova Scotia is proposing that records may be retained outside that province provided they remain accessible locally

H: Tell Me About Share Capital:

- Authorized capital - fixed or unlimited?
 - all jurisdictions but Nova Scotia and Prince Edward Island generally permit unlimited authorized share capital
 - Nova Scotia and Prince Edward Island currently have fixed authorized capital regimes
- Do Shares Have to Be Fully Paid or Not Upon Issuance?
 - most jurisdictions provide that shares cannot be lawfully issued until fully paid for but Nova Scotia, Quebec and Prince Edward Island each permit shares to be issued that have not been fully paid for and, in the case of Prince Edward Island, shares are deemed to have been fully paid for upon issuance
- Non-Cash Consideration for Share Issuances?
 - in Nova Scotia, the board is not required to satisfy itself on "value" where shares are issued otherwise than for money
- Can I Change Stated Capital?
 - unlike other jurisdictions, Nova Scotia imposes a court approval process to reduce stated capital although proposed law reform will dispense with this court approval requirement
- Can A Company Hold its Own Shares?
 - many jurisdictions (including the CBCA and Ontario) do not permit a corporation to hold shares in itself
 - this is permitted in British Columbia if authorized by a corporation's articles although such shares cannot be voted and dividends cannot be paid on such shares¹⁴ and Alberta companies can also hold its own shares but only for 30 days

¹⁴ See *Business Corporations Act* (British Columbia), Section 82.

- Do I Need to Worry About Pre-Emptive Rights?
 - several provinces have corporate laws which contemplate that general pre-emptive rights can be conferred upon shareholders via unanimous shareholder agreement
 - in the case of CBCA corporations, such pre-emptive rights must be contained within the articles
 - in British Columbia, the former Companies Act required the directors of non-reporting companies to confer pre-emptive rights on existing shareholders of a given class; the new *Business Corporations Act* (British Columbia) requires the directors of companies incorporated prior to the coming into force of this new Act to adhere to these former statutory pre-emptive rights unless exempted by their articles¹⁵
 - similar to the former British Columbia law, Newfoundland's corporate legislation also contains mandatory statutory pre-emptive rights

I: What Rights Are Conferred Upon Minority Shareholders?

- Currently, most jurisdictions other than Quebec and Prince Edward Island provide for oppression remedies and other minority shareholder protections (e.g., shareholder proposals, dissent and appraisal rights, equitable winding up rights, ability to seek compliance order, etc).
- Although some recourse may be available under Quebec's Civil Code, shareholders have less legal protection under the current Quebec Companies Act relative to the other provinces as the Companies Act does not provide any statutory remedy for oppression or rights of dissent.¹⁶

J: How Easy is it to Amalgamate?

- All jurisdictions provide for both long-form and short-form (or equivalent¹⁷) amalgamation procedures among corporations subsisting under the same corporate statute.
- Some jurisdictions have procedures to permit “extra-territorial” amalgamations i.e., the amalgamation of corporations subsisting under different corporate statutes.¹⁸

¹⁵ See *Business Corporations Act* (British Columbia), Sections 62 and 442.1.

¹⁶ See Quebec 2007 Working Paper, Pages 6, 12 and 15.

¹⁷ Prince Edward Island permits 2 or more corporations to amalgamate via petition to the Registrar where they have the same objects (i.e., no concept of long or short form amalgamation) (see Section 77 of the *Companies Act* (Prince Edward Island)).

¹⁸ Alberta, British Columbia, Northwest Territories and Newfoundland provide for “extra-territorial” amalgamations generally in cases where one corporation is wholly-owned by another.

- Amalgamations in Nova Scotia require both 75% shareholder and court approval currently but proposed legislation will dispense with the court approval requirement and reduce the special resolution threshold from 75% to 2/3rds.

K: Can I Do Everything On-Line?

- Most jurisdictions permit some degree of electronic filings and this trend is continuing.
- At present, Manitoba, Northwest Territories, Prince Edward Island, Newfoundland and the Yukon Territories appear to be "manual only" jurisdictions.

L: How Easy is it to Dissolve/Wind-up?

- All jurisdictions provide generally for voluntary winding up procedures.

M: How Easy is it to Revive?

- All jurisdictions other than Nova Scotia provide generally for a corporate revival procedure.
- In Nova Scotia, currently corporate revivals may only be effected by court order obtained by the Registrar although Nova Scotia is proposing to add a statutory revival procedure shortly as part of its law reform.

Conclusion:

As the above comparative overview illustrates, there is a material degree of current (and proposed) "conformity" among Canadian corporate laws. However, for the time being, some significant differences do exist (e.g., director residency requirements, scope of minority shareholder protections, ability to continue/amalgamate, etc.) and depending upon a given client's hierarchy of objectives such differences may lead us to better answer the question "where should I incorporate".