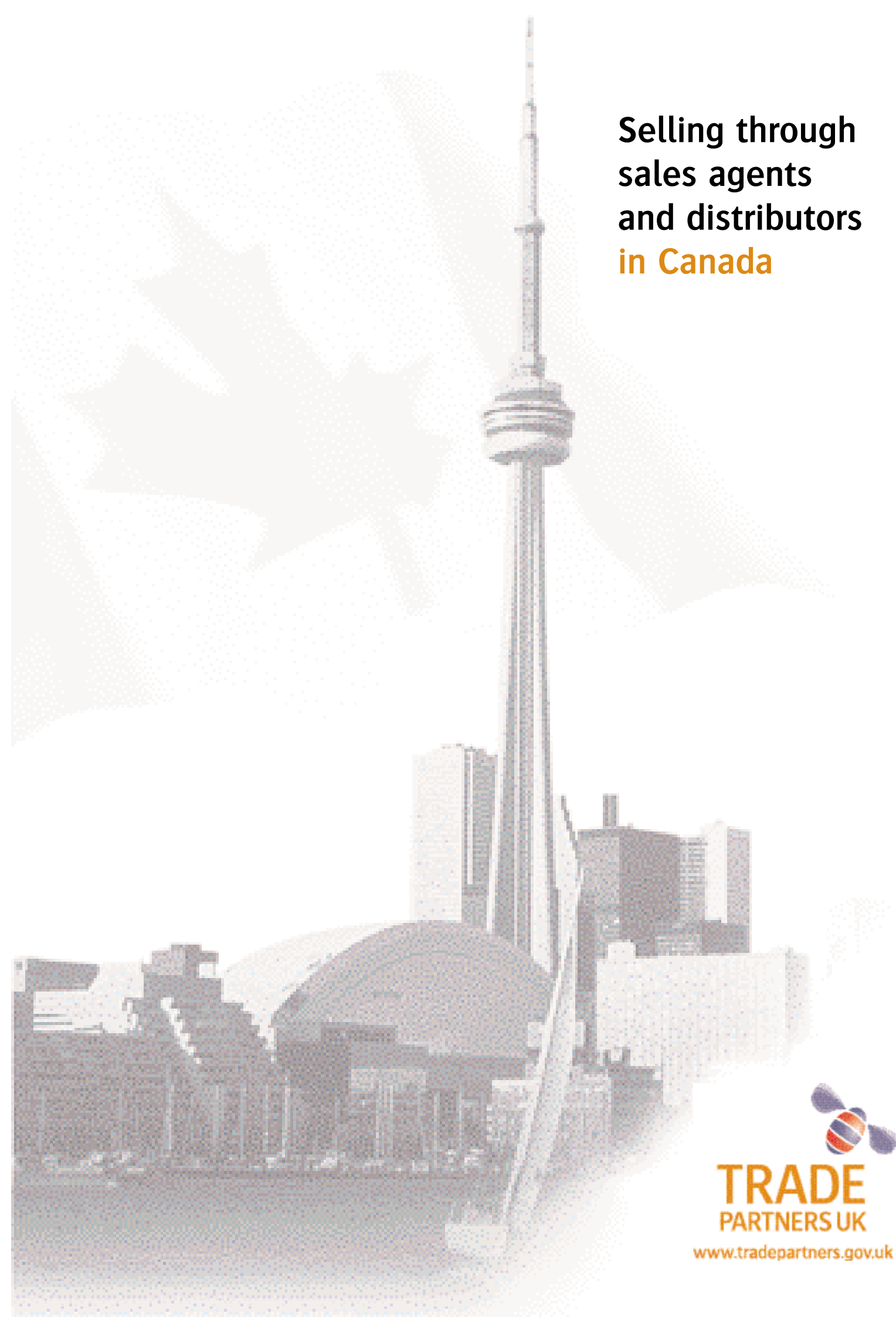




Selling through sales agents and distributors in **Canada**



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A guide for UK Companies

by Stikeman Elliott

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1. Overview

For a variety of reasons, a UK company may prefer to sell its products in Canada through independent businesses with an established presence in Canada rather than establishing a Canadian operation by incorporating a Canadian trading company.

This guide has been prepared to help British Trade International in advising UK companies on legal aspects of selling their products in Canadian markets through Canadian representation.

This is a general guide to the matters discussed in it:is not intended to replace the need, nor should it be used as a substitute,for independent professional advice in respect of any particular topic dealt with or referred to in it.

The DTI accepts no responsibility for its contents or for any errors or omissions in it.

2. Canada

Canada was ranked recently as one of the cheapest countries in which to do business. It is also in the world top fifteen for quality of life, with a stable political and economic environment rich in natural and human resources.

Canada is the world's second largest country geographically but has a relatively small population of just over 30 million. Notwithstanding this, it is a member of the Group of Eight (G-8) industrialised nations and has one of the Group's strongest economies.

The country is made up of ten provinces and three territories, with about 75 per cent of its population living in urban areas. The three largest cities are Toronto in the Province of Ontario, Montréal in the Province of Québec and Vancouver in the Province of British Columbia.

Canada is a constitutional monarchy and a federal state with a democratic parliament. Legislative authority there is constitutionally divided between the federal and provincial governments. Jurisdiction over areas like banking, transportation, competition and communications are matters of federal competency. Other areas, such as contracts, securities, property and employment, fall under the jurisdiction of the various provincial legislatures. Governments are democratically elected at federal, provincial and municipal levels and as the elections are independent it is

possible (and quite common) that the federal and provincial levels are governed by different political parties. The major parties in Canada are, however, decidedly close to the political centre and thus, this difference has not been particularly problematic.

With the exception of Québec, Canada is a common law jurisdiction, like England, the US and Australia. Québec is a civil law jurisdiction and has a European-style civil code which codifies the general principles of its law.

3. Representation: sales agents and distributors

(I) Distinction between sales agents and distributors

Any British manufacturer or supplier considering appointing a Canadian sales representative must grasp a fundamental distinction between the forms such representation may take, namely the distinction between a distributor and a sales agent:

- 'distributor' most commonly refers to a party (in this context a Canadian importer) that purchases goods from its principal (a British exporter) for resale in

its own name to its customers.

The distributor's income is derived from the mark-up price of goods resold to the distributor's customers.

- a 'sales agent' promotes sales for its principal without taking title to the goods or purchasing them for resale. The sales agent's compensation is typically earned on a commission basis where its efforts have led to a sale by the principal.

The principle differences between a distributor and a sales agent are set out in the following table:

Distributor	Sales agent
The distributor purchases and acquires title to products.	The sales agent neither purchases nor acquires title to products but finds purchasers to purchase the product from the manufacturer/supplier.
The distributor sets the price at which the purchased goods are to be resold by adding its own profit margin to the cost of purchasing the goods from the manufacturer/supplier.	The sales agent does not set the price at which customers purchase the goods. The sales agent's revenue is usually the commission earned on concluded sales.
The manufacturer/supplier may not, according to the applicable competition laws, set the price at which the goods purchased by the distributor are to be resold.	The manufacturer/supplier (and not the sales agent) sets the price at which customers purchase the products.
The distributor may, to increase its profit margins, request special deals from the manufacturer.	The manufacturer/supplier sets the price at which the goods are sold to the customers.
The distributor bears the risks of non-sale of and loss or damage to purchased goods.	The manufacturer/supplier bears the risk of non-sale of and loss or damage to inventoried goods.
The distributor cannot return unsold products.	The sales agent may return unsold products.
The distributor bears the risk of non-payment by customers and the supplier/manufacturer bears the risk of non-payment by the distributor.	The supplier/manufacturer bears the risk of non-payment by the customers.

There are a number of important variations in the previous arrangements. For example, a distributor may maintain an inventory of goods or may only purchase and take title to the goods if it has a purchaser for the goods.

Certain key features outlined opposite may be varied or extended in an appropriately worded agreement. For example, it is possible to prepare a contract so that a sales agent bears some of the credit risk in the event that a customer does not pay the manufacturer or supplier. Such an agent would be known as a *del credere* agent. Also, consideration should be given to such issues such as services/repair of goods and maintaining a supply of spare parts. It is not unusual for a distributor to undertake these functions and it would be less usual for a sales agent to do so.

(II) Choosing the representative

A distributor or sales agent could be appointed to serve part or the whole of Canada. In addition, a distributor or sales agent could be appointed as one of several such distributors or agents or on a sole or exclusive basis. Where more than one party will be appointed as the distributor and/or sales agent of a supplier in Canada, there are important competition rules which should be borne in mind, some of which are discussed later.

It is possible that a distributor or sales agent may wish to appoint 'sub-distributors' or 'sub-agents'. UK businesses should canvass this carefully with any prospective representative prior to making any commitments to permit a distributor or sales agent to do so.

The appointment of a sales agent or a distributor is not the only way of appointing an independent business to assist in the distribution of a manufacturer/supplier's products. Other methods include the establishment of a network of dealerships, the licensing of businesses and the conclusion of franchise agreements. These methods are not dealt with here, nor are issues relevant to UK companies wishing to sell directly to end-customers.

(III) Choosing the method of representation

Choosing one of the distribution methods below over another involves trade-offs and a balance must be found. The main choices are between faster or slower growth, greater or lesser capital requirements, more or less control over operations and broader or narrower penetration of markets.

Incorporating a Canadian trading company

It is possible to incorporate a Canadian subsidiary of a British supplier/manufacturer to distribute products in

Canada. In doing so, the manufacturer/supplier will retain full responsibility to capitalise and administer the distribution business. If the manufacturer/supplier is unfamiliar with Canadian markets, this avenue may not be free of difficulty and market growth may be slow. On the other hand, the supplier will retain full control of its brand, the customer service and the activities of employees engaged in the distribution process

Appointing a Canadian agent

The appointment of a Canadian agent or a network of Canadian agents removes some (but not all) of the responsibilities for the distribution process in Canada from the UK manufacturer/supplier. Depending on the strength of the prospective agent, penetration of the Canadian market may be both quick and broad. Also, it may be possible to get close to end-customers in a relatively cost-effective manner. The appointment of agents would mean that the UK manufacturer/supplier would lose some control over the distribution process but would still, however, be in a position to set the price at which the product is sold to end-customers.

Appointing a Canadian distributor

The appointment of a Canadian distributor removes the responsibility for distribution in Canadian markets from the manufacturer/supplier and allows the manufacturer/supplier to focus on its other activities,

such as production, procurement and distribution in other markets. Once again the extent and strength of the distributor's distribution network may allow fast and relatively easy penetration of Canadian markets. It may also be possible to gauge the needs of end-customers in those markets more effectively. Therefore the appointment of a Canadian distributor may be most appropriate where the product is to be distributed over a wide area or where the products complement the products that are distributed by existing distributors in Canada. The appointment of a distributor involves loss of control over the distribution process, extending to the price at which the product is sold to end-consumers. Furthermore, a distributor may continually pursue 'special deals' in its dealings with a supplier.

(IV) Appointment agreements

There are at least five basic principles that are essential to UK manufacturer/suppliers before concluding an agreement with a distributor or agent:

1. A manufacturer/supplier should thoroughly familiarise itself with the competence and reliability of the representative prior to making any appointment.
2. The manufacturer/supplier should obtain professional advice on the legal (including taxation) aspects of distributing its products in Canada.

3. A formal written agreement regulating the parties' relationship should be negotiated and signed as a pre-condition to launching the relationship. Professional advisers should be involved in this process.
4. Care should be taken in choosing the correct terminology to describe the nature of the relationship and the parties' mutual obligations.
5. The manufacturer/supplier should consider insisting that the duration of the agreement, at least initially, be limited in time. A decision to grant exclusive rights should be approached with caution.

The Annex contains a non-exhaustive list of some of the issues to be considered in drafting an agreement between a supplier and a representative that may be used in the above discussions and in reviewing any draft documentation.

4. Legal issues

As noted above, a business may be regulated at each of the three levels of government: federal, provincial and municipal. Any supplier doing business in Canada should establish which of such laws apply to the arrangements.

(I) The regulatory environment

It would be inappropriate to assume that the regulatory environment in Canada is the same as that in the USA. Some areas are more heavily regulated in Canada whereas others are less so.

There is a substantial body of consumer protection legislation dealing with the sale of goods to end-customers. This legislation is not dealt with here. By way of contrast, there is little legislation relating to the relationship between a manufacturer/supplier and a representative. There are, however, a few instances where such a relationship would be regulated.

The applicable competition legislation (discussed below) and, for example, the *Pyramid Distribution Act* of British Columbia are statutes of general application. The professions, financial institutions, securities dealers and real estate industries, to name but a few, are specifically regulated. The first enquiry should therefore consider the nature of the industry and the nature of the proposed distribution arrangement to ensure that there is no industry-specific legislation that would apply.

In the province of Alberta, the sale and grant of franchises is controlled by legislation, the *Franchises Act* (Alberta). Any proposed distribution arrangement involving either a distributor or a sales agent should be considered to ascertain whether it might inadvertently be governed by such franchise legislation. Similar legislation has been under consideration in Ontario for some time.

(II) Product distribution and Canadian competition law

The principal purpose of the *Competition Act* (Canada) is to maintain and encourage competition and to promote efficiency and adaptability of the Canadian economy. The *Competition Act* applies to suppliers selling goods into Canada, whether by selling to a distributor for re-sale or to a sales agent.

The *Competition Act* is a detailed piece of legislation spanning ten parts and over 100 sections. It is not possible to canvass the full implications of the legislation for product distribution in Canada here but a few comments may be made:

- The *Competition Act* contains detailed provisions governing a broad array of subject matter. These provisions are divided into criminal offences and civilly reviewable practices, each of which involves separate enforcement procedures. Criminal provisions relate to such practices as conspiracy, bid-rigging, predatory pricing, price

discrimination, promotional allowances, price maintenance and egregious cases of misleading advertising and deceptive telemarketing. Breach of these provisions may be prosecuted in the criminal courts and is punishable by fine and/or imprisonment. Practices that are reviewable under the *Competition Act* include refusal to deal, tied selling, exclusive dealing, market restriction, pyramid selling and multi-level marketing schemes, and abuse of dominant position. These practices are subject to a broad range of remedies, the primary being prohibition orders, and are adjudicated by a specialised Competition Tribunal. Finally, non-egregious cases of misleading advertising and deceptive telemarketing are subject to a separate enforcement regime, with available remedies including prohibition orders and administrative monetary penalties (i.e. fines).

- The *Competition Act* creates the possibility of private actions for conduct contrary to the *Competition Act's* criminal provisions or in violation of orders made thereunder. This right of private action, however, appears to be limited to so-called 'special damages' (i.e. damages actually suffered) and the costs of investigating the claim, which puts it in stark contrast to potential treble damage claims available under US antitrust laws.
- Another critical distinction of note to UK distributors with activities in Canada and the US involves price maintenance. In the US, the so-called Colgate Doctrine permits a supplier to declare unilaterally that it will not deal with any company that does not adhere to certain conditions, including with regard to pricing. In Canada, however, price maintenance is a per se offence. Any attempt by a supplier to compel customers to raise their prices (or to refrain from lowering them), including discontinuing supplies to a customer due to its low-pricing policy, could put it offside the *Competition Act's* criminal prohibition against price maintenance. This said, a supplier may be able to avoid the need for compliance with these provisions by arranging to distribute its products in Canada through a sales agent.
- The criminal prohibition on price discrimination prohibits a supplier from discriminating with regard to price in sales to competing purchasers of like quality and quantity. Given that sales must be of like quality and quantity, however, the *Competition Act* allows for volume discounts. It also allows for buyer groups, provided the buyer group meets certain criteria. Finally, the prohibition against price discrimination applies only in respect of goods; it does not apply to services. This said, price discrimination in the context of

services may contravene other provisions of the *Competition Act*, such as its abuse of dominant position provision.

- The *Competition Act* prohibits the granting of promotional allowances to customers unless they are granted on a proportional basis to each customer. While the underlying economic rationale of this provision is suspect, it cannot be ignored; it creates a criminal offence and prosecutions, while uncommon, are not unheard of.
- Many of the *Competition Act's* provisions are civilly reviewable. Of particular note in this regard are provisions concerning refusal to deal, tied selling, exclusive dealing and market restriction. As a general matter, however, these provisions should only raise difficulties where the supplier is a significant supplier of a product (i.e. the supplier has 'market power' in a defined 'product' and 'geographic market', in antitrust parlance).

(III) Agent binds principal

Where the representative is a sales agent, the agent may have actual authority to bind the principal in Canada. It is therefore important to define clearly the scope of the agent's authority in a written agreement. In addition, the agent may hold itself out to have greater authority than it does so it is important that the

manufacturer/supplier not allow such a false impression to be. Although a statement in a contract setting out the scope of the agent's authority will be of assistance in this regard, such a statement is not determinative.

(IV) Intellectual property issues

Patents

In order to enjoy patent protection in Canada, a Canadian patent must be registered. Pursuant to the Patent Co-operation Treaty of 1970, it is possible to file an international patent application in the UK, which designates Canada as a member country in which a patent is sought. Such a filing would, in effect, provide patent pending status in Canada. Thereafter, application may be made for a patent in Canada. Assuming the application satisfies the Canadian requirements for registration, the result will be the issuance of a patent in Canada.

Trademarks

A trademark must serve to distinguish the source of a particular product or service. While registration of a trademark under the *Trademarks Act* (Canada) is not mandatory, the extent of protection available to the owner of an unregistered trademark may be limited geographically to the area in which the trademark enjoys some notoriety. This may mean, for instance, that a UK supplier wishing to sell a product under a trademark in Canada could, at least initially, have difficulties protecting the trademarks.

A registered trademark, however, enjoys exclusive protection across Canada. In addition, the remedies available where there has been an improper use of a registered trademark are broader than those available to protect an unregistered trademark. For example, in addition to remedies for infringement, registered trademark owners may seek remedies for depreciation of goodwill in their trademarks. Finally, while a mere distributor of a product is unlikely to acquire rights in a trademark, a UK company may wish to pre-empt attempts by distributors to assert such rights by registering the trademark and ensuring that its distributor agreement specifies that the distributor arrangement does not confer rights in the trademark on the distributor, but rather that all such rights reside with the supplier/manufacturer.

Assuming that a trademark application does not encounter problems, such as opposition by another trademark owner or numerous initial objections by the Trade Marks Office Examiner, registration of a trademark (including associated legal fees and disbursements) costs approximately C\$2,000 and takes 1–2 years to obtain.

Copyright

Copyright is protected in Canada under the *Copyright Act* (Canada). Copyright protection arises from the time of creation of the work; therefore, registration is not a

pre-requisite to copyright protection in Canada. This said, registration carries with it certain evidentiary advantages in the event of a dispute. In addition to traditional copyright rights, it should be noted that the *Copyright Act* also includes protection of moral rights and neighbouring rights. Moral rights include the so-called paternity and integrity rights of the creator of a work. Neighbouring rights, on the other hand, include such rights as the rights of performers and in sound recordings. It is also worth noting that the *Copyright Act* includes a special regime for the importation of books, which, in effect, restricts the right to import books into Canada where an exclusive distributor has been appointed for Canada. Finally, the *Copyright Act* was recently amended to allow ‘private copying’ in exchange for a levy to be remitted on the sale in Canada of ‘blank audio recording media’ (i.e. blank audio cassettes, compact discs etc.) In this regard, proceedings are currently under way before the Canadian Copyright Board to establish the amount of the levy in the specific media to which the levy would apply.

Industrial designs and the design of semiconductor chips also enjoy protection in Canada under applicable legislation.

(V) Warranties and product liability

A manufacturer or supplier may incur liability because the goods it manufactures, sells, distributes or licences may cause injury to someone’s person or property. This is broadly referred to as ‘product liability’.

In Canadian law, product liability may arise from at least three sources, namely:

1. In contract (under both expressed or implied terms of a contract).
2. By operation of the law of negligence (tort). This makes it possible to be liable both to persons with whom one has contracted and to third parties.
3. In both contract and by operation of the law of negligence. Such liability is termed ‘concurrent liability’.

As product liability may arise from contract, the provisions of a contract are an important part of regulating the risk of product liability. This is especially so because of the existence of legislation, such as the various provincial sale of goods legislation (and the international sale of goods legislation adopting the Vienna Sales Convention), which has the effect of implying certain warranties where there is a contractual relationship of sale and purchase between two parties. The wording of a contract that aims to limit or exclude such liability should be carefully crafted in order to have the intended effect.

It is, furthermore, important to ensure that the terms of a negotiated agreement between a UK supplier and a Canadian representative are not superseded by later documentation, such as terms and conditions set out on the reverse of a purchase order emanating from the representative. Such later documentation may include inappropriate or erroneous warranties and give rise to an unexpected risk of liability. This risk may be managed by appropriately wording the agreement regulating the long-term supply and distribution arrangement between the supplier and the representative and by the supplier ensuring that any later terms emanating from the representatives are emphatically rejected.

The risk of concurrent liability means that a finding of negligence on the part of the supplier may override the effectiveness of any limited warranties or disclaimers dealt with in the contract.

It is, accordingly, important that liability arising from tort is expressly dealt with in the contract. Although contractual provisions are an important way of managing the risk of product liability, a contract between a supplier and a manufacturer limiting the grounds on which the supplier may be liable to the representative will not sterilise the risk of liability on the part of the supplier. It is possible that a UK manufacturer/supplier may be liable in tort law in Canadian

courts to third parties with whom the manufacturer or supplier did not contract. This is most likely to take the form of liability to end-users of the distributed products. There are, however, legal strategies that may be used in addition to operational quality control to deal with this risk. Firstly, the risk may be passed on to a Canadian representative by obtaining an indemnity from the representative. Obviously, such indemnification is only as good as the financial worth of the representative. In addition, an indemnity could be backed by making the Canadian representative take out and maintain adequate comprehensive general liability and product liability insurance. Finally, a UK manufacturer/supplier may wish to obtain insurance of its own risks.

As a broad generalisation, however, Canada is not nearly as litigious an environment as the US and there are only limited circumstances in which contingency fees are allowed. As a rule, damage awards in Canada are considerably more modest than those in the US. An individual's expenses for cost of care are considerably less in Canada than in the US because of Canada's socialised healthcare system. Another reason for lower damage awards, including awards for punitive damages, may be that juries are rare in civil trials in Canada.

To succeed in a claim for punitive damages in Canada, the plaintiff must show that the defendant acted with 'great misconduct worthy of the court's

condemnation for punitive damages'. The required standard is by no means clear. Although the conduct of the defendant in some situations will stand out as deserving of punishment, the required standard of conduct is often more nebulous. Ultimately, the decision is subjective. One provincial Court of Appeal has suggested that punitive damages would be awarded where the defendant's conduct 'offends the ordinary standards of morality or decent conduct in the community'.

Where punitive damages are awarded, there are no established rules to guide Canadian courts in quantifying them. However, courts have indicated that the amount of an award should be in relation to the gravity of the defendant's misconduct. In contrast to US courts, the trend in Canada has been to award modest punitive damage claims. The largest awards rarely exceed C\$1 million.

One of the most significant obstacles to product liability is the cost of litigation to potential plaintiffs. However, in Ontario and in other provinces, launching class proceedings under legislation such as the *Class Proceedings Act* (Ontario) may negotiate this obstacle. This may bring about a future increase in product liability litigation.

5. Canadian taxes

(I) Income tax

The sale or distribution of products in Canada by a non-resident of Canada may cause the non-resident to be considered to be carrying on business in Canada for the purposes of the *Income Tax Act* (Canada). However, to the extent that the non-resident person is a resident of the UK for the purposes of the Canada-United Kingdom Income Tax Convention, any income derived from such sale or distribution of products in Canada will not be subject to Canadian income tax unless the non-resident is considered to have a permanent establishment in Canada. A permanent establishment is a fixed place of business situated through which the business is carried on. For example, a UK resident employee of the non-resident that visits a trade fair in Canada, or that makes a sales trip to Canada, should not be considered a permanent establishment of the non-resident in Canada unless such person has, and habitually exercises in Canada, an authority to conclude contracts in the name of the non-resident.

An agent (other than an independent agent) will be considered to be a permanent establishment of a non-resident if such agent has and habitually exercises in Canada an authority to conclude contracts in the name of the non-resident. An independent agent will not be considered a permanent establishment of the non-resident if such an agent is acting in the ordinary course

of its business. Consequently, should a distribution arrangement be considered, tax advice should be sought in order to avoid the arrangement constituting a permanent establishment of the non-resident.

(II) Withholding taxes

Amounts paid by a resident of Canada to a non-resident with respect to most forms of passive income, including management or administration fees, interest and royalties, are generally subject to withholding tax on the gross amount of such payments. The rate of Canadian non-resident withholding tax under the *Income Tax Act* (Canada) is 25 per cent, subject to reduction pursuant to a tax treaty between Canada and the country of residence of the recipient. Under the *Canada-United Kingdom Income Tax Convention*:

- the withholding tax rate for interest and royalties is limited to 10 per cent
- any management or administration fees are not subject to such withholding tax, but rather to Canadian income tax only to the extent that the non-resident has a permanent establishment in Canada to which such fees are attributable.

There are certain important exceptions to these rules and in all circumstances tax advice should be obtained if a distribution arrangement involving the making of such payments is considered.

(III) Commodity, value-added and sales taxes

Customs duties, federal goods and services tax (GST) and provincial sales tax may be levied with respect to the import and export of goods into and out of Canada or the manufacturing and selling of goods in Canada. Additional excise taxes and duties may be payable on products such as alcohol and tobaccos. In certain circumstances, however, importers may benefit from a reduction, refund, drawback or possible elimination of customs duties.

The comprehensive 7 per cent GST applies at each stage of production. This is a value-added tax similar in concept to UK VAT and is payable by the purchaser on the amount paid for the goods or services. However, if the purchaser is involved in a commercial activity and has registered with the federal government to collect the tax, it is generally entitled to claim a credit for all GST paid on business services used in the course of its commercial activities. GST on imported goods and services is payable by the importer while exported goods and services generally are not subject to GST.

Any non-resident engaging in a commercial activity in Canada must register and charge and collect GST. The tax will also be imposed on most goods imported into Canada on the

value for duty on those goods, plus any applicable duties.

Special excise taxes and duties might also be levied. Excise taxes are levied on a limited number of goods imported into Canada, including certain clocks, jewellery, some automobiles, air conditioners for automobiles, gasoline products and tobacco products. Excise duties are imposed on spirits, Canadian brandy, beer or malt liquor and tobacco, cigars and cigarettes produced or manufactured in Canada. The *Customs Tariff Act* (Canada) provides for an additional customs duty to be levied on these goods when they are imported into Canada in an amount equal to the excise duties that would have been imposed had they been manufactured in Canada.

Retail sales taxes at rates varying from 6 per cent to 12 per cent are imposed by all provinces except Alberta, Québec and three of the Atlantic provinces (who have harmonised their retail sales taxes with the federal GST).

6. Language, packaging and labelling requirements

(I) Language legislation

Canada is officially a bilingual country (approximately 25 per cent of its population is French speaking). The majority of Canadian francophones reside in Québec. When doing business in Canada, a UK manufacturer/supplier must therefore take into account a series of federal and Québec laws and regulations which are designed to protect language rights and promote the survival of the French language and culture. These statutes include those relating to the packaging and labelling of products (discussed below).

The Québec *Charter of the French Language* is designed to make French the everyday language of work, instruction, communication, commerce and business in Québec and requires that all public signs, posters and commercial advertising in Québec be in French. Other languages are permitted, subject to certain restrictions.

The Charter also specifies that every inscription on a product (including the container and wrapping) or on a supplied leaflet, brochure or card be in French, although they may be accompanied by a translation in another additional language providing the French version is predominant. Instructions for use and warranty certificates must be in French and also may be given in another language. As a general rule, all catalogues, brochures and any similar

promotional materials used in Québec must be drawn in French but may be distributed in English or in another language as long as a French version is equally available. There are various and Labelling Requirements exceptions to the French labelling, inscription and signage requirements, such as for products intended for use exclusively for a market outside of Québec, for trademarks, greeting cards and for calendars and agendas not for the purposes of advertising.

The names of firms doing business in Québec are required to be in French, unless the statute under which they are incorporated says otherwise. Only the French firm name may be used in Québec, subject to the possibility of having a name registered as a trademark and using such a trademark on signs and in advertising. Certain non-French elements may, however, appear as part of the name and a version of the name in another language may also be shown on products that are offered for sale both in and outside Québec.

Both the Charter and Quebec consumer protection legislation require that communications with Québec customers be in French unless the customer requests otherwise.

Under the Charter, non-consumer Québec contracts containing printed standard clauses or which are pre-determined by one party may be in a language other than French if the parties expressly so request. It is therefore usual to include in

a contract a clause to the effect that the parties have expressly requested that it be drawn up in English. Québec consumer protection legislation requires that consumer contracts be drawn up in French only or, on request, in French and in another language.

Non-Quebec corporations which do business in Québec are required to comply with most of the provisions of the Charter such as those relating to labelling of products and communicating with consumers in French.

(II) Labelling and language

The regulations passed under the *Consumer Packaging and Labelling Act* (Canada) require that, as a general rule, the product identity and the net quantity identification be in both French and English. The dealer identification declaration may be in either French or English but, as a general rule, if the product is being sold in Québec both languages must appear. It is, therefore, usually easier to provide all the mandatory information in both languages. Under federal law, optional information, such as a trademark of the product, is not required information and therefore does not have to be marked in French (subject, however, to Québec legislation). The requirements apply to all consumer products marketed and sold in Canada, whether locally manufactured or imported, except for very limited

exceptions, such as for products both manufactured and sold locally. Goods marketed or sold in contravention of such requirements are subject to seizure and potential destruction by federal authorities.

Canadian labelling legislation sets out specific requirements as to where information such as product identity, net quantity and dealer's name and principle place of business must be placed on a package or label. There are also specific requirements regarding the size of type used. Accordingly, the acceptability of UK product labels that are already labelled for the international market must be evaluated on a case-by-case basis.

(III) Pre-packaged consumer products

Much of the legislation affecting the importation of goods into Canada relates to product standards or is designed to prevent unfair marketing practices and addresses potential health and safety concerns. The *Consumer Packaging and Labelling Act* applies, with some limited exceptions, to all pre-packaged consumer products sold in Canada. A label containing a declaration of net quantity must be applied to the product and must be clearly and prominently displayed easily legible, and in distinct contrast to any other information on the label.

The label must also show the identity and principal place of business of the person by or for whom the product was

manufactured, the identity of the product in terms of its generic name or in terms of its function and information about the nature, quality, age, size, material content, composition, geographic origin, performance, use and method of manufacture or production of the product. The regulations outline further requirements regarding bilingual labelling, the application of a label and the part of the label on which the information is to be shown. In addition, the Marking of Imported Goods Order made under the *Customs Tariff Act* (Canada) lists products that must be legibly marked, stamped, branded or labelled to indicate the country of origin. If the Order is not complied with, the goods will not be released until marked under Customs supervision at the expense of the importer.

(IV) Textiles

The Textile Labelling Act (Canada) and accompanying regulations state that any consumer textile article imported into Canada must have a label affixed to it containing prescribed information. However, regulations permit dealers to import incompletely or improperly labelled consumer textile articles provided the dealer labels the articles in Canada, notifies an Industry Canada inspector at the time of or prior to the importation with prescribed details about the articles and affords an inspector an opportunity to inspect the articles after labelling.

The label must show the textile content of the article and the name and postal address of the dealer by or for whom the article is made in both English and French. The regulations also prescribe the manner in which a trademark or descriptive term may be shown.

(V) Food and drugs

The Food and Drugs Act (Canada) protects consumers from fraud, injury and deceptive practices by imposing labelling and packaging standards in respect of foods, drugs, cosmetics and medical devices. The regulations made pursuant to the Act stipulate which foods and drugs must carry a label when offered for sale. 'Food' includes any article sold or represented for use as food or drink and 'drug' includes any substance sold or represented for use in the diagnosis, treatment or prevention of disease, the restoration or correction of organic functions or the disinfection of premises in which food is manufactured or kept. The definition of 'drug' is broad and many items not popularly considered to be drugs (such as toothpaste and antibacterial soaps) are regulated as drugs in Canada and may require that a Drug Identification Number be acquired before sale there.

The Canadian Food Inspection Agency publishes a Guide to Food Labelling and Advertising, which identifies those food claims (i.e. words such as 'pure', 'fresh' or

'natural') that may be subject to prohibitions respecting misleading and deceptive representations for foods. For example, the term 'organic' may only be applied to goods that have been certified by an independent organic certification body.

The Regulations with respect to food set out requirements regarding labelling, food additives, compulsory ingredients for some foods and freezing. More particularly, the name of the food, the identity of the manufacturer, the durable life of the product, special storage instructions, and all the ingredients of the product must be shown on the packaged food labels.

Narcotics and controlled and restricted drugs may only be imported by a pharmaceutical manufacturer or a distributor or other person licensed by the federal Minister of Health. Package information must include the name of the drug, the identity and location of the manufacturer, a quantitative list of the ingredients, the lot number of the drug, instructions for its use and the net amount of the drug in the container.

(VI) Hazardous products

The Hazardous Products Act (Canada) contains lists of consumer products which may not be advertised, sold or imported into Canada as well as consumer products which may only be advertised, sold or

imported in accordance with the Act and the regulations. The Act does not apply to materials regulated by the *Explosives Act* (Canada), the *Food and Drugs Act*, the *Pest Control Act* (Canada) or the *Atomic Energy Control Act* (Canada). The Controlled Products Regulations prescribe the information that must be contained on labels and material safety data sheets by suppliers of specified hazardous controlled products destined for use in the workplace. Included among the labelling requirements are applicable product and supplier identifiers, hazard symbols and appropriate information respecting risk and precautionary and first aid measures.

7. Relationships with representatives

(I) Establishing a relationship

Choosing the right distributor or sales agent involves establishing criteria for identifying potential representatives and delegating responsibility to the best people to consider those representatives. The responsible people should familiarise themselves with both the competence and reliability of representatives prior to making an appointment.

Both before and after commencing a relationship with a representative, it is important to communicate accurate information in relation to the products to be sold in Canada and not to make extravagant claims as to the anticipated sales or earnings for the representative. If discussions and projections are not realistic, the representatives may be disappointed when their expectations are not met and litigation may ensue.

(II) Control mechanisms

One of the keys to enjoying mutually beneficial relationships with representatives is the establishment of effective control mechanisms.

Procedures for the collection of payment are particularly important. If payment holidays are given to a representative then these should be documented formally in such a manner that ensures that the payment holiday is not understood as being a waiver on the part of the manufacturer/supplier of its right

to insist on punctual payment. Furthermore, a manufacturer/supplier should, in negotiating the contract with the distributor/sales agent, consider taking some form of security over the assets of the distributor/sales agent or, alternatively, from any person standing behind any corporate entity dealt with. The security taken should, at least, secure the payment of amounts owing under the distribution arrangement. A manufacturer/supplier should also consider taking security if a distributor/agent proves unreliable in making payments. However, it may be best not to wait until the problem of defaulting payment arises before seeking security, particularly in the situation where the distributor/agent is heading towards insolvency as security given under those circumstances may be subject to challenge in a subsequent insolvency situation.

In establishing the distribution arrangement, it is important to insist on performance-measuring criteria that are based on objective and correct data. Once these have been established, it is important to monitor both sales and the extent of compliance by the representative with the terms of the distribution arrangement and to act immediately in the event of any non-compliance.

In the event of non-compliance with either the performance criteria or the payment obligations, alternatives to terminating the relationship should be considered. In addition to the taking of security for payment, such alternatives may include negotiating the loss of any exclusivity enjoyed by the distributor/sales agent or the negotiation of a reduction in the size of the territory in which the representative has exclusivity.

(III) Ending a relationship

When a manufacturer/supplier wishes to terminate the relationship with a representative, an agreement for cause should be distinguished from termination without cause.

Termination for cause is typically by reason of default or breach on the part of the sales agent/distributor. The agreement with a representative should contain carefully considered clauses relating to default or breach and the circumstances in which default or breach may result in the termination of the agreement. Typically, certain defaults are capable of being cured and the agreement should provide for a notice of default to be given, describing the default and for the defaulting party to have an opportunity to cure the default. In other circumstances, usually insolvency related, the agreement

should be terminable without giving the defaulting party an opportunity to cure the default. In these circumstances, the agreement may terminate either automatically or at the option of the innocent party.

The 'paper trail' relating to the extent of performance of the representative and the agreement assumes particular importance when the termination of the agreement for cause is being considered. Legal advice must be sought before taking any action in connection with the termination of a distribution agreement as a precipitous or premature attempt to terminate an agreement for cause may expose the manufacturer/supplier to a claim for damages or other relief.

The termination of an agreement for cause should be distinguished from the termination of an agreement 'not for cause'. An agreement with a representative may be for a fixed duration. Such an agreement may permit the renewal thereof by one of the parties in certain circumstances or may provide for the automatic renewal of the agreement, in the absence of a notice of termination.

An agreement may not provide for any term and, accordingly, the duration of the agreement may not be clear from the documentation. The approach of the courts in these circumstances is to imply a term to the effect that any party may

terminate such an indefinite agreement on reasonable notice to the other party.

This means that:

- the right to terminate an agreement without cause, immediately, must be expressly provided in the agreement
- the issue of what is reasonable notice assumes considerable importance.

The courts approach the issue as to what constitutes reasonable notice as a factual inquiry. This means that the court considers all of the circumstances that pertain to the particular relationship between the manufacturer/supplier and the distributor/sales agent. In conducting this inquiry, the courts consider the following factors:

- the length and type of relationship between the parties
- the extent of the sales force employed by the parties whose distributorship was terminated
- the importance of the distribution rights to the party terminated
- the time needed by the terminated party to acquire a replacement line of products and to re-establish a viable business.

The nature of this inquiry means that it is of particular importance to obtain legal advice before terminating an agreement

not for cause, particularly where the agreement is silent on the duration or the circumstances in which it may be terminated not for cause.

Typically, a distribution agreement should provide for the rights and obligations of the parties upon its termination.

The matters to be considered include:

- the settlement of accounts payable by the distributor/agent
- the return or disposal of existing inventory
- the assumption of warranty obligations
- the discontinuance of the use of intellectual property relating to the products forming the subject of the distribution arrangement
- any future non-competition and non-solicitation obligations of the parties.

8. Available help

(I) British Trade International

The last 12 months have seen a significant change in the way Government support for British business abroad is delivered with the formation of British Trade International, a new unified organisation which brings together the work of the Foreign & Commonwealth Office and the Department of Trade and Industry under a single Chief Executive (Sir David Wright). British Trade International combines, in a single operation, all trade development and promotion work currently undertaken locally in the English regions by the Business Link network; trade support services provided nationally; and the commercial work overseas of over 200 embassies and other diplomatic posts.

(II) Export Canada

www.brittrade.com/exportcanada

The Government's Export Forum met in Autumn 1997 to review the markets on which trade promotion efforts were being concentrated and recommended twelve markets/areas for additional attention. This list was revised in early 1999 and Canada was added. The Forum recommended specifically that extra help should be offered to companies new to or inexperienced in exporting. Consequently Export Canada was officially launched on 9 December 1999.

Export Canada has been designed to support, as never before, UK companies targeting the Canadian market. The package will introduce UK SMEs who are new or inexperienced in exporting to the

Canadian market and ensure that they are prepared for and understand the various aspects of doing business in Canada, thereby putting them in a stronger position to succeed.

As well as running the Export Canada package, the Canada team at British Trade International co-ordinate an extensive programme of activity at home and abroad across a variety of industry sectors in partnership with the leading trade associations. The team also provide advice and access to a wide range of off-the-shelf information on sectors across Canada.

(III) TradeUK

British Trade International working with the Dialog Corporation, has established the TradeUK website (www.tradeuk.com) incorporating the TradeUK National Exporters Database and the TradeUK Export Sales Lead Service. These services act as an on-line shop window for UK goods and services around the world and a sales leads notification system to UK business free of charge.

(IV) Further information

For further information on the Export Canada package, missions and seminars in the UK and abroad and to obtain general market information, contact the Canada Team on:

Tel: 020 7215 8312

Fax: 020 7215 4604

Email: exportinfo.canada@xpdv.dti.gov.uk or visit the website at:

www.brittrade.com/canada.

9. Annex

Preamble

- 1 full description of the parties
- 2 date of entering into contract

Recitals

- 3 nature of principal's business and desire to appoint distributor or agent
- 4 nature of distributor or agent's business activities and desire, capability and legal capacity of distributor or agent to distribute principal's products or to find appropriate purchasers for principal's products

Appointment

- 5 appointment of distributor or agent
- 6 duration of appointment and circumstances in which appointment may be terminated
- 7 exclusivity or non-exclusivity
- 8 description of products to be distributed
- 9 the extent of the territory in which the distributed products may be sold
- 10 any right of principal to sell directly in the territory
- 11 coverage for affiliates and subsidiaries of principal

Prices and terms of sale by supplier

- 12 supplier's pricing and discounting policy
- 13 supplier's right to change pricing of product
- 14 whether prices include sales, excise or similar taxes
- 15 notification by distributor or agent when special price is required
- 16 currency of payment
- 17 consequences of exchange rate fluctuation

18 if sales agency, when commission earned and when payable

19 place of payment

20 delayed payment penalties, if any

21 indemnity by distributor or agent for local taxes

22 other terms and conditions of sale by supplier:

- delivery, passage of title and risk of loss of goods
- payment for freight and insurance
- delivery subject to any necessary Canadian governmental authorisation
- shipping arrangements and storage arrangements if shipments cannot be ready on schedule dates
- warranties
- limitation of liability
- supplier's right to terminate orders
- packing and labelling of product
- all orders subject to written acceptance by supplier
- liens

Principal's obligations

- 23 furnish products
- 24 furnish promotional literature
- 25 full warranty obligations
- 26 train distributor or agent, as may be necessary, on the use of the products
- 27 provide any required technical assistance in relation to the products
- 28 patent indemnification

Agent's or distributor's obligations

- 29 exercise best efforts to sell the products or find a willing and able purchaser for the products
- 30 properly install the products, if required
- 31 service the products both in and out of warranty
- 32 maintain complete records of customers and sold products
- 33 report to supplier on periodic basis on customers, new business, sales volumes, pricing, competitors' activities, and market

Conditions and forecasts

- 34 advise the supplier of pertinent specifications and regulations affecting the products, including packaging and labelling requirements
- 35 maintain adequate office, showroom or warehouse facilities
- 36 maintain an adequately trained sales force
- 37 maintain an adequate stock of inventory and replacement parts, if applicable
- 38 conduct adequate advertising
- 39 refrain from altering any name plates, patent markings, serial numbers or packaging
- 40 meet periodic sales quotas
- 41 refrain from engaging in competitive activities
- 42 advise supplier of patent or trademark infringement

Miscellaneous

- 43 restrict agent's capacity to bind the principal to stated matters
- 44 use by distributor or agent of supplier's trademarks
- 45 indemnity by distributor or agent for liabilities of supplier attributable to the actions of distributor or agent
- 46 any applicable rules governing sales by agent on behalf of the supplier/consignment sales (e.g. security interests of supplier, insurance of product and right of repossession of supply)
- 47 consequences of termination of relationship for existing stock in possession of distributor or agent, customer lists and compensation, if any
- 48 confidentiality of information furnished by supplier to distributor or agent
- 49 force majeure
- 50 forum for settlement of dispute, court or arbitration proceedings
- 51 governing law
- 52 non-assignability by distributor or agent, no agency or sub-agencies
- 53 right of supplier to add or delete products
- 54 registering or protection of patents, trademarks and copyrights in Canada.