# GUIDE FOR THE CONSTRUCTION INDUSTRY WHEN DOING BUSINESS IN THE UNITED STATES

Published by
*Canadian Construction Association*

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For legal or tax advice, please consult a qualified professional.

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# TABLE OF CONTENTS


**1. UNITED STATES MARKET ..... 4**

1.1 Purpose of the Guide ..... 4
1.2 Before Heading South . . ..... 4
1.3 Canada and the United States: The Largest Trading Partnership in the World ..... 4
1.4 Understanding the North American Free Trade Agreement (NAFTA) ..... 5
1.5 Understanding the U.S. Market ..... 6
1.6 Barriers to the U.S. Market ..... 6

**2. PLANNING FOR THE UNITED STATES ..... 7**

2.1 Getting Ready To Do Business in the U.S. ..... 7
2.2 Assessing Your Company's Readiness ..... 7
2.3 Create an Export Plan for Doing Business in the U.S. ..... 7

**3. ENTERING UNITED STATES ..... 8**

3.1 Entering Your Chosen Market ..... 8
3.2 Establishing a U.S. Entity ..... 8
3.3 Certification of Authority ..... 9
3.4 Professional Licenses ..... 10
3.5 Pre-Qualification ..... 11
3.6 Market Entry for Services Versus Goods ..... 11
3.7 The Essentials of Export Contracts ..... 11

**4. TAXATION, FINANCING, INSURANCE AND BONDING ..... 13**

4.1 Tax Registrations ..... 13
4.2 Obtaining Contract Insurance and Bonding ..... 13
4.3 The Basics of Export Financing ..... 14
4.4 Obtaining Financial Assistance ..... 14
4.5 Dealing with Non-payment ..... 14
4.6 Reducing Financial Risk through Accounts Receivable Insurance ..... 15
4.7 Reducing the Risk of Exchange Rate Fluctuations ..... 15
4.8 Tools to Minimize Foreign Exchange Risk ..... 15

**5. IMMIGRATION ISSUES ..... 16**

5.1 Introduction ..... 16
5.2 Non-Immigrant Business Classifications ..... 16
5.3 Entry Problems ..... 19
5.4 Company Personnel Crossing the U.S. Border ..... 20

**6. EMPLOYEE ISSUES ..... 21**

6.1 Mandatory Minimum Wage Rates ..... 21
6.2 Workers' Compensation Insurance ..... 21
6.3 U.S Workers' Compensation: Considerations for Canadian Contractors ..... 22
6.4 Purchasing a U.S Workers' Compensation Policy ..... 23

**7. CUSTOMS ISSUES ..... 25**

7.1 Introduction ..... 25
7.2 The New Border Security Environment ..... 25
7.3 Customs Brokers and What They Do ..... 25
7.4 Clearing U.S. Customs ..... 26

7.5 Get Prepared Early ... 26
7.6 Getting Your Paperwork in Order (Routine Shipments) ... 26
7.7 The ACE System ... 27
7.8 Moving Construction Materials Across the Border ... 27
7.9 Moving Construction Equipment Into the United States ... 27
7.10 Bringing Construction Equipment Into Canada ... 28
7.11 Bringing Canadian-Sourced Equipment Back Into Canada ... 29
7.12 Bringing U.S.-Sourced Equipment Into Canada ... 29
7.13 Temporary Importation Bond ... 29
7.14 Required Documentation for Formal Entry ... 29
7.15 Informal Entry of Goods ... 30
7.16 Penalties and Seizures ... 30
7.17 Customs and Border Issues: An Ongoing Priority ... 30

**8. LIEN LAW TRUSTS: MORE VALUE THAN A MECHANIC'S LIEN ... 32**

8.1 The Purpose of a Trust ... 32
8.2 Drawbacks of a Mechanic's Lien ... 32
8.3 Statutory Lien Law Trusts ... 33
8.4 Trust Fund Statutes ... 33
8.5 Solutions ... 34
8.6 More Powerful Than a Lien ... 35
8.7 Trust Fund Tools ... 35

**9. APPENDIX A: GLOSSARY OF TRADE TERMS ... 37**

9.1 General Terms ... 37
9.2 International Commerce (INCO) Terms ... 37
9.3 Transportation and Delivery Terms ... 38
9.4 Financial and Insurance Terms ... 39
9.5 Partnership, Alliance and Market Entry Terms ... 40
9.6 Legal Terms ... 41

**10. APPENDIX C: RESOURCE DIRECTORY ... 42**

# 1. UNITED STATES MARKET

## 1.1 Purpose of the Guide

The primary purpose of this Guide is to foster a better understanding of doing business in the United States as a viable market opportunity for Canadian-based construction firms.

This Guide primarily targets small to medium-sized construction firms who do not have the resources to employ in-house expertise in this complex area. The objective is not to make all construction firms exporters but to expand their knowledge and understanding about exporting to the United States and to define the many resources that are currently available. Even firms that are already exporting will find useful information, tips and resources.

This Guide has been prepared by members of the Canadian Construction Association (CCA), International Business Committee, drawing on the expertise of professional, legal, tax and brokerage firms as well as from the vast resources of government agencies such as Export Development Canada. In addition, CCA firms currently exporting products and services to the United States have shared exporting experiences in the form of Case Studies.

## 1.2 Before Heading South . . .

With a market of approximately 301.3 million people, the United States is the world's largest economy. Its size gives it the power to influence global acceptance of everything from consumer goods to industrial standards, and makes it a magnet for exporters all over the planet. Simultaneously, the U.S. is a major supplier of goods and services both to its own domestic markets and to markets around the world.

Because of its size and vast range of needs, the U.S. can be a very good place for an exporter to do business. But the same characteristics that make it attractive can also make it a difficult market, because exporters to the U.S. must compete not only with each other but with U.S. domestic suppliers. Moreover, the wide variety of market segments can make it hard for an exporter to focus on the areas where the company can best apply its strengths.

Canadian exporters must also face the challenge of treating the U.S. as a market separate from Canada. While the similarities of language, standard of living and attitudes give Canadians a unique advantage over exporters from other countries, they can also cause us to overlook the many ways in which the two nations are different. Canadian construction firms that understand these differences will greatly improve their chances of success south of the border.

## 1.3 Canada and the United States: The Largest Trading Partnership in the World

The United States is Canada's largest trading partner and is the largest market for Canadian goods and services.

$577 billion annual trade

- $359 billion exports to the USA
- $218 billion imports from the USA

$500 billion in annual investments

- $224 billion to the USA
- $274 billion from the USA

The Canada-U.S. Free Trade Agreement (1989) and the North American Free Trade Agreement (1994) have both been crucial to increasing market opportunities for Canadian exporters in the U.S.

### 1.4 Understanding the North American Free Trade Agreement (NAFTA)

NAFTA, is an agreement among Canada, the United States and Mexico to remove impediments to trade and investment among the three countries.

The North American Free Trade Agreement provides comprehensive disciplines for trade in goods and services, investment, intellectual property and dispute settlement. One of its major achievements has been to eliminate the tariffs on most goods originating in the member nations. Another has been to liberalize regulations affecting matters such as investment and cross-border trade of services. These have provided many excellent business opportunities for Canadian exporters and continue to do so.

While the intent of NAFTA is straightforward, the agreement itself and its side agreements are complex. For a clear understanding of how NAFTA regulations may affect your specific export activities, you will need to consult specialists in cross-border trade, such as lawyers, brokers and shippers.

NAFTA is most likely to have an immediate effect on your export initiative in two areas:

- **Cross-border movement of personnel:** Under NAFTA, certain types of professionals and business people can work temporarily in the U.S. There are many restrictions, however, since NAFTA is primarily an agreement for free trade in goods, not for free trade in labour.
- **NAFTA Rules of Origin:** NAFTA rules of origin determine whether an exported product receives preferential tariff treatment when moving between Canada, the U.S. and Mexico. The rules are based on the Harmonized System of tariff classification and vary from product to product, depending on the product's composition. Basically, however, your goods will qualify for NAFTA originating status if:
    1. the good is wholly obtained or produced in one or more of the NAFTA countries (including those goods that are entirely grown, fished or mined in a member country – it does not include goods purchased in a NAFTA country that were imported from a non-NAFTA country);
    2. the good is made up entirely of components and materials that qualify in their own right as goods that originate in one or more of the NAFTA countries;
    3. the good meets the requirements of a specific rule of origin for that product, as listed in NAFTA Annex 401;
    4. the good qualifies under NAFTA Article 401(d), which applies to only a few cases; or
    5. the good is automatic data processing equipment or parts qualifying under the provisions of NAFTA Annex 308.1.

The most common of these five requirements is the third, which applies to a good that includes any non-originating materials in its production. Non-originating materials are:

- materials or components you import from a non-NAFTA country; or
- materials produced in one or more of the NAFTA countries but which fail to satisfy the rules of origin in their own right.

NAFTA provides a rule of origin for every type of good that incorporates non-originating materials. In many cases, two different rules may apply to a good, and the good may qualify under the rule appropriate to the good's production. Once you actually begin exporting, you will need to fill out Certificate of Origin forms for those products for which NAFTA originating status is claimed.

## 1.5 Understanding the U.S. Market

There is actually no single "U.S. market". What you will actually find in the U.S. are markets – lots of them, segmented by race, religion, age, geography, nationality, citizenship status, income bracket, occupation, political persuasion, industry, profession, trade and so on.

This is hardly surprising: given the sheer size of the United States and the relative affluence of its 301.3 million people, the needs and desires of its population are not likely to be the same across the country. This variety presents Canadian exporters with a myriad of opportunities.

To put the size of these markets into better perspective, we can think of each state as a nation, with a Gross State Product (GSP) equivalent to a country's Gross Domestic Product (GDP). In this framework, California's GSP is equivalent to the GDP of France, and Texas' GSP is equivalent to the GDP of Canada.

What this implies, for you as a Canadian exporter, is a strong need for careful market research and a well thought-out export strategy. To be successful, you will have to be very focused.

## 1.6 Barriers to the U.S. Market

Exporters should be aware of the impediments to trade presented by non-tariff barriers, security issues and "buy American" policies.

Generally, barriers to trade are described as tariff or non-tariff barriers. A tariff is a tax applied to merchandise imports and, less frequently, on exports. The tax may be levied either on an ad valorem basis (a fixed percentage of the value of an imported product) or on a specific basis (a fixed levy per unit of imported product). Following a final tariff reduction between Canada and Mexico, which took effect on January 1, 2003, virtually all trade in the NAFTA region has flowed tariff-free.

Non-tariff barriers (NTBs) are government measures or policies, other than tariffs, that restrict or distort international trade. As tariffs are lowered or eliminated, for example by a free trade agreement, it becomes more important to address non-tariff measures that can be used to frustrate trade. Examples of NTBs include import quotas, discriminatory government procurement practices and discriminatory measures to protect intellectual property. A further class of non-tariff barrier is that of technical barriers to trade (TBTs), such as government requirements for unnecessary duplicate testing and certification of an imported product.

It is important to find out as early as possible if there are any barriers that will affect your exports. If a barrier does exist, you should determine how it may affect your access to your U.S. market, your pricing of your product or service, and your costs of doing business in the United States.

A second major barrier to the smooth flow of U.S.-Canada trade is that of security. The 2001 terrorist attacks in the United States caused greatly increased concern about U.S. domestic security, and this has significantly affected how exports from Canada and around the world enter the U.S. Security measures continue to evolve and may complicate your export business, for example by slowing traffic across the border or by requiring more preparation and documentation.

"Buy American" policies can also present barriers to Canadian exporters. As an example, one of the largest markets in the U.S. is the public-sector procurement market. This includes the federal-level General Services Administration (GSA) and Department of Defence (DoD), as well as state procurement agencies. These organizations are mandated to "buy American" whenever possible.

# 2. PLANNING FOR THE UNITED STATES

## 2.1 Getting Ready To Do Business in the U.S.

To prepare a United States export initiative, you first have to decide whether your company is actually ready to step onto the U.S. stage. Being “export-ready," involves having the financial, human and production capacity to meet the demands of the export market you want to enter. The first step in your readiness assessment must be to conduct market research; that is, to find out if there is a U.S. market segment that wants and/or needs what you are offering.

## 2.2 Assessing Your Company's Readiness

After identifying a market segment, for example a demographic or a region where your product might do well, your next step is to decide whether your company is in fact ready to be an exporter. You might consider this in the light of the following questions:

- The U.S. is a ferociously competitive market. What advantages does your product or service have that will set it above its competition?
- Can you obtain the working capital needed for any necessary expansion, such as staff or production space?
- Do you have enough cash flow to sustain you until payment for your goods or services is received?
- Will your product or service need different packaging and promotional materials? For example, will brochures need to be in English and in Spanish?
- Can you obtain the financing needed to promote your product or service in the U.S.?
- What further research are you doing to identify the market you are going to enter? Is it time, for example, for an on-the-ground survey of the territory?

## 2.3 Create an Export Plan for Doing Business in the U.S.

Your research is underway and you have assessed your export readiness. Now it is time for your export plan, because a good plan will vastly improve your company's chances of success in the United States. Your plan will also be crucial if you need financing, because financial institutions will not lend to a business that has not developed one. Your export plan will be similar in many ways to your business plan, except that it will concentrate on the conditions of the U.S. market.

An Export Plan should include the following:

- description of how you will organize your export activity;
- analysis of your product and its suitability to the U.S. market;
- overview of your market research;
- description of the methods by which you will enter the U.S., such as promotion and distribution;
- analysis of U.S. regulatory, logistical and risk factors and how you will deal with them; and
- implementation plan and a financial plan.

Second, a solid financial plan for your export initiative is a must. In addition to including a capital budget and a cash budget, it must allow for fluctuations in the value of the Canadian dollar that may affect your profitability in the U.S. market or at home. A good financial plan is also essential if you need to approach lenders for working capital, letters of guarantee or other kinds of financial assistance.

## 3. ENTERING UNITED STATES

### 3.1 Entering Your Chosen Market

Many Canadian companies providing construction materials and services have found exciting and lucrative business opportunities in the United States. Starting a U.S. operation is not a casual undertaking, however; it requires careful planning and preparation. Very few contractors will be able to meet the deadlines for a construction project if they have not taken certain steps prior to soliciting work or submitting a bid. Exporting to the United States means that you will have to become familiar with a new set of business laws. While there is no substitute in these areas for good legal counsel, you will make better decisions if you have a basic knowledge of things like NAFTA rules, U.S. tax laws and Canadian customs and export regulations.

Your research so far may suggest several ways of actually entering your new market. Depending on your product or service and your resources, you might establish a United States business presence.

### 3.2 Establishing a U.S. Entity

One of the first decisions a Canadian contractor must make is whether to conduct U.S. operations through a branch of its Canadian organization or whether to establish a separate U.S. entity. Either approach is permissible. In general, however, it is recommended that a Canadian company form a U.S. entity for its U.S. operations.

As a practical matter, a Canadian company will wish to separate its U.S. operations from its Canadian operations. Tax laws require separate accounting of U.S. income and expenses. Ordinarily, the company will wish to establish separate bank accounts in the United States.

As discussed below, professional licensing laws may require separation of management functions as well. Establishing a U.S. corporation may also permit a Canadian contractor to limit the risks of its U.S. operations to the assets of the U.S. entity. Many Canadian companies appreciate this potential benefit as they venture into the unfamiliar U.S. market. By forming a U.S. entity, Canadian companies also avoid some of the detriments which might be associated with being from a "foreign company," whether pure chauvinism or legitimate concerns about collectability of payments due and enforceability of contracts.

***Case Study: JJM Construction - A Canadian Family Business Lays Down U.S. Roots***

*Back in the 1940s, British Columbia's JJM Construction was founded on the Miller family's vision to provide innovative products and services for its customers, while building a successful organization that would thrive into the future. All business decisions were built on a long-term approach, lasting solutions and long-term relationships.*

*More than 60 years and two generations later, the family-owned business is a testament to that vision, generating approximately $50 million in annual revenues and boasting a long list of satisfied clients in Canada and the United States. Predominantly serving the public sector, this diversified company is involved in a broad range of multi-disciplinary projects such as highway, bridge, airport, dam and marine construction, and environmental and navigational dredging.*

***Building a Foundation in the U.S.***

*By the late 1960s the Miller family business owned gravel pits in the U.S., first in Point Roberts and later in Blaine, Washington. "Back then, it was very straightforward to haul sand and gravel across the border," says Dee Miller, Vice-president, Finance and Administration for JJM Construction Ltd.*

*It was the U.S.-registered gravel pit operation, Miller Aggregate Inc., that provided the basis for JJM Construction's American operations. Eventually the pits were sold and Miller Aggregate Inc. had its name changed to Miller Contracting Inc to handle the U.S. operations. "U.S. corporate decisions were based on professional advice we received from accountants, lawyers, agents and brokers on both sides of the border," says Miller. "We found it was much easier to invest in professionals than go through a long learning curve on our own and possibly make costly mistakes along the way."*

*... (cont.)*

***JJM Construction (cont'd)***

*"The United States is an excellent market for us," Miller adds. "It's close by our Canadian head office, with a similar culture. Limited competition in the Pacific Northwest marine construction industry supports stronger margins, especially when the U.S. dollar is significantly stronger than the Canadian." Today, the company carries out marine construction projects on both sides of the border ranging from $5 to $15 million.*

*And while there's a lot of work involved in setting up an American subsidiary, Miller says it's not that much different than setting up a new construction business in Canada. "The taxes are different, the forms have different names, and it's a bit of a puzzle the first time through the process. But once you're set up, it's fairly straightforward.*

***Keeping Up With the Jones Act***

*There are still challenges, however, and the biggest one that JJM Construction has faced is the U.S. Merchant Marine Act of 1920, also known as the Jones Act.*

*"Basically, the Jones Act says that only American-owned and made ships can conduct most shipping activities in U.S. waters," explains Miller. "This means that as a Canadian company, we're very limited in what we can do. The Jones Act considers dredging equipment to be part of shipping, so we can't put barges to work in the U.S. or perform dredging projects."*

*The trick, says Miller, is to find work in areas that the Jones Act allows. For example, while they can't dredge and their ships aren't allowed to carry cargo between U.S. ports, they can move rock from Canada to a U.S. port and place it. Placing rock is used in building underwater berms and remedial work.*

*At the same time, JJM Construction is looking to expand into other types of projects in the U.S., such as airport and port construction. "Now that we have an established United States company, it's a stepping stone to other projects," Miller says.*

Once a Canadian company makes a decision to form a U.S. entity, it must then decide what type of entity to create. Liability concerns dictate the use of one of the types which limit the liability of the owners of the entity to the assets of the entity itself, that is, a corporation, limited liability company, limited partnership, or limited liability partnership. The determination of the appropriate type of entity should be made in consultation with a U.S. lawyer and an accountant. Most often, the decision will be to form a corporation.

Unlike Canada, the federal government in the United States does not charter corporations. As a result, a Canadian contractor must select a state in which to incorporate its U.S. entity. Each of the states has its own laws governing the structure and functioning of corporations chartered in that state. Commonly, the state of incorporation is chosen taking into account factors like: the flexibility of the corporation law in the state; the amount of taxes and fees which must be paid merely to maintain the corporate existence; the location of the company's U.S. operations (at least in the initial years); the ease of incorporating; and, to a lesser extent, the convenience of company management. Delaware is a common choice for incorporation because Delaware's corporate law is widely known and understood throughout the United States, its fees are nominal, and the incorporation process is relatively quick and easy there.

It is recommended that Canadian construction companies hire a U.S. lawyer to form their U.S. business entity. Once the Canadian company has gathered the information and made the decisions about corporate structure needed to form the U.S. entity, the process ordinarily takes no more than 7-10 days. State fees, service fees, and legal fees to form a corporation in the U.S. may total about USD $1,500.

### 3.3 Certification of Authority

Any business entity, whether owned by U.S. citizens or by others, must obtain a Certificate of Authority (or "qualify") to do business in every state in which it does business other than the state of its formation (incorporation). This requirement applies both to business entities formed in the U.S. and to those formed outside the U.S. The precise scope of business activities that constitutes "doing business" in a state for these purposes varies from state to state. Generally, construction operations in any state will constitute "doing business" in that state so as to require any out-of-state entity to "qualify" unless the contractor is involved only in a single project within a particular state and that project is of very short duration. The "qualification" process in every state is actually a registration process. The business must file certain information with the appropriate state office, pay the application fee, and pay the required annual fee.

The purposes of "qualification" are to provide formal notice to the state government, potential creditors and others dealing with the business entity of its presence in the state, its proper name and address of its principal offices, and the name and in-state address of an agent upon whom notices and lawsuits can be served. There are several commercial companies with offices in every state that serve as registered agents for an annual fee. Qualifying to do business in a new state generally takes no longer than 7-10 days.

Doing business in a state without first qualifying can subject a contractor to penalties in that state. In some states, such penalties can be quite substantial if the contractor does business for a significant amount of time. More importantly, a contractor that fails to qualify to do business in a state may have difficulty enforcing its contracts in that state because the contractor will be barred from initiating legal proceedings in the courts of that state until it qualifies to do business there.

### 3.4 Professional Licenses

Licensing requirements for construction professionals vary substantially from state to state. Licensing of architects, engineers, plumbers and electricians is universal, although the requirements are not uniform. Some states do not license general contractors; other states may have several categories of general contractors, depending on the size and nature of the construction projects. There are states that license excavation contractors, fire-sprinkler contractors, irrigation contractors, industrial contractors, heavy-construction and roadway contractors and others. Every contractor must carefully explore the licensing requirements in a new state before seeking work in that state.

A few states require the construction professional to be licensed only when he/she actually performs construction work. However, most jurisdictions require the professional to obtain needed licenses before soliciting work, advertising its availability to do work, signing a contract or submitting a bid. The penalties for engaging in these activities without a proper license also vary from state to state, but can include fines, jail, forfeiture of money earned for work performed without a needed license, and inability to bring suit to recover monies earned but not paid.

There are two types of construction professional licenses, those which are issued after registration, and those which are issued after testing. Registration-type licenses are generally issued promptly after submitting the required information and fee. Licenses requiring testing may only be issued a few times per year. It is common in many states for tests to be offered only 2-4 times per year. The tests generally require applicants to show both proficiency in the construction discipline in question and knowledge of local laws and regulations. In some instances, persons who have obtained a professional license in one state may be eligible for licensure in other states with similar requirements, without taking a test. The extent of these reciprocal licensure provisions varies from state to state, and is often limited to architecture and professional engineering.

When a license is issued after a test, the license is usually issued to the individual who took the test, rather than to the company. There is often a company license as well, but it is issued only to companies with a licensed individual responsible for construction operations in that state. It is recommended that at least two individuals from each company obtain licenses so that business operations need not cease if the licensed individual is fired, leaves the company, is promoted or relocated, or becomes disabled or dies. In many states with licensure testing, a company can obtain a company license by hiring a person who already has an individual license. However, this is often not a desirable approach. Under the licensing laws, the individual with the license must be given operational authority over the work in that state. Many companies hesitate to give that much authority over a new venture to a new employee.

The amount of time that it takes to obtain a license varies considerably from state to state. In states where a test is required before the license is issued, many months may pass between the time the application process is initiated and the time the license is granted. Consequently, it may be necessary to apply for a license in a state well before an opportunity arises to bid on a project there.

### 3.5 Pre-Qualification

Project owners often require prospective bidders to pre-qualify before submitting a bid. Generally, they seek proof of the experience, competence and financial resources and stability of prospective bidders. Private owners, the federal government and many local governments require pre-qualification on a project-by-project basis. The pre-qualification requirements are generally set out in the bid documents, and the deadlines for pre-qualification are closely related to the bid date.

Many state agencies, including many highway departments, have an annual pre-qualification program. In such cases, the pre-qualification process is not related to any particular project. As a result, the timetable for meetings of the officials responsible for pre-qualification may not coincide with the bid date for a particular project. A contractor planning to work on projects for such an agency should apply for pre-qualification well in advance of any work it wishes to perform.

### 3.6 Market Entry for Services Versus Goods

Unlike goods, service exports tend to be intangible. Nevertheless, the major methods of delivering services fall into categories that are quite similar to those for delivering goods. For example, exporters of goods and exporters of services can both benefit from direct selling; in fact, if you are a service company with a unique skill or knowledge, you might consider contracting your service directly to American clients.

Alternatively, you might market your service indirectly through an intermediary who negotiates a service contract for you with the client. Or you might establish a partnership with a firm whose service dovetails with yours, to the advantage of both companies.

The method you choose will depend on the nature of your service, the resources available to you and the particular U.S. market you are entering. No matter which approach you select, however, you must focus on establishing an awareness of your firm in the target market and on demonstrating the credibility, competence and professionalism of the service it offers. And, as always, you will have to ensure that your management and staff are sensitive to the culture, values and business practices of your American clients.

Your research so far may suggest several ways of actually entering your new market. Depending on your product or service and your resources, you might establish a United States business presence. Or you might use a manufacturer's representative or set up a partnership or strategic alliance with a like-minded American business.

For both producers of goods and providers of services, an alliance of some kind can be a very advantageous way to penetrate the U.S. market, because it can help resolve problems related to professional accreditation, movement of personnel across the border and U.S. tax and legal status. Moreover, combining the technical and financial strengths of the two businesses can make you both more competitive – and in the highly aggressive U.S. business environment, that can be a very good strategy indeed.

### 3.7 The Essentials of Export Contracts

Export contracts, because they are drawn up between companies from countries often having different business laws, regulations and attitudes, are more likely to cause disputes than straightforward domestic contracts. This can be true even when the countries have as much in common as Canada and the United States. You should therefore make your export contracts as clear, precise and comprehensive as is reasonably possible.

The basic provision of a contract for the sale of goods is that you, the seller, will transfer ownership of the goods to your buyer in return for payment. The rest of your export contract specifies the terms and conditions for doing this, and at the minimum should describe:

- who is party to the contract;

- the contract's validity conditions;
- the goods you will provide;
- the purchase price of the goods and the terms for payment, inspection and delivery of the goods;
- where transfer of title to the goods takes place;
- any warranty and/or maintenance terms and conditions;
- who is responsible for obtaining import or export licenses;
- who is responsible for paying taxes;
- any contract performance security requirements, such as bank letters of guarantee;
- what to do if your buyer defaults or cancels;
- the provisions for independent mediation or arbitration to resolve disputes, and whether this would take place in the United States or Canada; and
- the contract completion date.

All parties must sign the contract. For instance, if you are working through a representative, be sure that the actual buyer signs the contract. The representative's signature is not necessarily enough, because without the buyer's signature, there is no written evidence that the buyer owes you money. Last but certainly not least, have the contract examined by a lawyer familiar with the U.S. export market.

# 4. TAXATION, FINANCING, INSURANCE AND BONDING

## 4.1 Tax Registrations

Besides forming a U.S. entity and qualifying it to do business in each state of operation, a business must register with the taxing authorities in the various places in which it operates. All U.S. business entities must obtain a Taxpayer Identification Number (also known as an Employer Identification Number or "EIN") from the federal Internal Revenue Service ("IRS"). Canadian business entities that operate directly in the U.S. (instead of forming a U.S. business entity to carry on their business in the U.S.) may also be required to obtain an EIN. The EIN is used to identify the company for purposes of collecting income tax, federal excise taxes and social security and Medicare payments. It is obtained without a fee by filing a form with the IRS. The application form is generally prepared by the entity's lawyer or accountant at the time the entity is formed, and it ordinarily takes the IRS a short time to issue an EIN. U.S. banks require the EIN to open a bank account for the corporation.

The U.S. tax system, like most tax systems, is complicated, so you will need legal and accounting professionals to help you avoid unexpected tax liabilities that you did not factor into your pricing, sales contracts or profits. Failure to pay or collect the correct taxes may incur penalties above the actual tax amount owed.

The United States applies taxes to both businesses and individuals. It has two different levels of tax jurisdiction: the first is at the federal level under the U.S. Internal Revenue Service (IRS), and the second is at the state level. Taxes can be based on income, or on the sale or use of a good or service (for example, state sales taxes).

Companies are also required to register with the taxing authorities in each state of operation, as well as the state of formation. Some states require separate registration for state income tax purposes, employment taxes, sales and use taxes. Once again, the forms for registration are commonly prepared and submitted at the time a corporation is formed or is qualified to do business in a new state. A company should register for sales tax purposes before collecting payment for any goods or taxable services. Counties or cities in some states may also assess income and sales and use taxes.

Adding another layer of complexity is the Canada-United States Tax Treaty, which is intended to avoid double taxation and which will affect the way that both Canadian and U.S. tax systems evaluate your export trade. Unfortunately, the treaty does not apply to state income taxes and this may have consequences for your tax situation.

U.S. clients often ask the Canadian exporter to file a "Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding," or form W-8BEN. This form generally applies when products or services are made, processed or otherwise undertaken in the U.S. by the Canadian firm, and for which the Canadian firm will receive payment from the American client. As a general rule, though, if you are a firm that simply exports goods to the U.S., you will not be required to file this form.

## 4.2 Obtaining Contract Insurance and Bonding

As a condition for closing the deal, your U.S. buyer may require you to provide financial security that will protect the buyer against any failure, on your part, to meet your obligations under the contract. Such security can take several forms, such as an on-demand bank letter of guarantee, a standby letter of credit or a surety performance bond.

Your regular surety bonding broker can be of great assistance here, including identifying a U.S. provider or looking at security instruments specifically designed for Canadian exporters by agencies like Export Development Canada (EDC).

If you provide one of these instruments, make sure that your contract clearly stipulates your performance obligations, as well as the conditions under which your buyer can make a valid call for non-performance so as to have the security paid out to him.

### 4.3 The Basics of Export Financing

It may not be possible for you to finance the extra costs of an export initiative entirely from your company's resources. For example, you might need additional financing to cover production and operating costs until the goods are finished, shipped and paid for. In such cases, you will need to know what financing might be available and where you can obtain it on the best terms.

There are several types of basic financial assistance for export ventures: pre-shipment financing, post-shipment financing, medium-term financing and project financing.

**Pre-shipment export financing:** You may require additional financing to produce the goods or services your buyer wants. To persuade a lender to help you, you will need a firm export sale and a contract that is acceptable to the lender in terms of repayment risk, payment terms, production timeframes, and recourse conditions.

**Post-shipment export financing:** This covers your financial needs during the time between shipping the goods and receiving payment for them.

**Medium-term export financing:** This is often used with capital goods exports. You can usually obtain such assistance for terms of 180 days to two years, and possibly for terms lasting up to five years.

**Project financing:** This usually applies to large undertakings such as major capital projects. This is the most common export field for small to medium Canadian construction businesses, since such projects tend to be long-term, complex and demanding. If you are considering becoming involved in one, be sure to obtain help from project-finance experts from the very beginning.

### 4.4 Obtaining Financial Assistance

There are three chief sources for the financial help you may need: banks, government assistance programs and venture capital. As with domestic business operations, bank lines of credit or loans are commonly used to help fund export operations.

### 4.5 Dealing with Non-payment

If you have delivered your goods or services to a U.S. customer that has not paid you, what recourse do you have?

You can hire a lawyer or a collection agency, but it can still be very difficult for a Canadian exporter to recover payment from recalcitrant U.S. customers, especially if the customers have sought bankruptcy protection. Legal action can be exceedingly costly, so arbitration or mediation to settle out of court is much preferable, if you can arrange it. This, of course, presupposes that you wrote an arbitration/mediation clause into the contract with your buyer. If you did not, your best course is to obtain legal advice and consider whether it is even worthwhile to pursue payment.

Hiring a licensed collection agency can also help to encourage payment. Although cheaper than hiring a lawyer, this is still expensive because collection agents usually take a percentage of the receivable as payment.

To ensure that accounts receivable are collectible and to mitigate the risk of non-payment, it is recommended that you purchase accounts receivable insurance. This recommended solution is described below.

### 4.6 Reducing Financial Risk through Accounts Receivable Insurance

After cash in advance, accounts receivable insurance is the best way to avoid the most serious consequences of buyer non-payment. In Canada, these types of insurance are the specialty of Export Development Canada and include:

**Accounts Receivable Insurance:** EDC will cover up to 90 percent of your losses if your U.S. buyer does not pay as the result of a wide variety of commercial and political events, including buyer bankruptcy and default.

**Contract Frustration Insurance:** EDC protects you against specific political or commercial risks and will cover up to 90 percent of your losses on individual export contracts for services, capital goods or projects.

**Wrongful Call Insurance (also called Bid Insurance or Performance Security Insurance):** Useful for exporters who have to post a bond, EDC will cover up to 95 percent of your loss if your buyer, without reason, makes a demand against your standby letter of credit or letter of guarantee (a "wrongful call").

### 4.7 Reducing the Risk of Exchange Rate Fluctuations

Fluctuations in the value of the Canadian dollar relative to the United States dollar can affect export profits either positively or negatively. This is called foreign exchange risk or FX risk, and you have to factor it into your operational plans and product pricing. If you do not, your budgeting may go off track, you may not have enough cash to meet payment obligations, and you may even risk bankruptcy. There are two major types of exposure:

**Transaction exposure:** Suppose you conclude a contract with a buyer and he commits to pay you in U.S. funds 60 days after delivery. Now suppose the Canadian dollar drops in value against the U.S. dollar by the end of that 60 days. Because of this, your buyer's payment will be worth more to you once it is converted into Canadian currency. Conversely, if the Canadian dollar rises during that 60 days, the payment will be worth less to you after conversion to Canadian currency. The risk of this happening is called transaction exposure.

**Economic exposure:** If transaction exposure is the small picture, this is the big one. If the Canadian dollar rises a great deal, as it did beginning in 2003, Canadian goods and services will cost more in the United States. This may cause U.S. buyers to buy less, drive harder bargains or look for better deals elsewhere.

### 4.8 Tools to Minimize Foreign Exchange Risk

You can minimize foreign exchange risk by using tools such as:

**Forward contracts:** In these contracts, you agree to sell a fixed amount of U.S. currency to a commercial bank, at a fixed price, at some future date. This removes your uncertainty about what your export deal will actually be worth and protects you if the Canadian dollar rises against the American. On the other hand, if the Canadian dollar goes down (which means the payment will be worth more than formerly), you do not get the benefit.

**Exposure netting:** In this strategy, you match U.S. currency inflows with U.S. currency outflows, to eliminate or "net out" the exposure. If your types of transactions allow it, and if you pick the right financial instruments, you can come out very close to even.

**Currency options:** These contracts give you the right (but not the obligation) to buy or sell foreign currency at a specified price, within a defined time period. Unlike forward contracts, options let you benefit from favourable fluctuations in exchange rates.

# 5. IMMIGRATION ISSUES

## 5.1 Introduction

U.S. law provides varied opportunities for foreign nationals to come to the United States to engage in business activities. The North American Free Trade Agreement (“NAFTA”) expanded these opportunities for Canadians, and certain procedural accommodations provided in U.S. immigration laws make the application process for many classifications less burdensome for Canadians. Canadians may seek work-authorized entry in either temporary (nonimmigrant) or permanent classifications (i.e., the “green card”). Ordinarily, entry in the nonimmigrant classification is sought first, and an immigrant status may follow. For Canadians, applications for entry in certain nonimmigrant classifications may be made in person at the border and an immediate adjudication may be rendered by an officer of the U.S. Customs and Border Protection (“USCBP”), one of the immigration components of the Department of Homeland Security (“DHS”).

Immigration is a planning tool to be analyzed in relation to other legal issues, as shown in the following examples. Decisions regarding the corporate structure of a Canadian construction company’s U.S. operations should be analyzed in parallel with immigration issues in order not to eliminate the use of certain immigration options. Also, before a Canadian company signs a lease for premises in the United States, it should first verify that it shall be able to move key Canadian personnel to the U.S.

## 5.2 Non-Immigrant Business Classifications

### 5.2.1 Business Visitors (B-1)

This category is intended for temporary business-related travel to the U.S., where all compensation for the visitor is paid from a Canadian source. This category has traditionally been limited to activities such as attending business meetings or soliciting orders from U.S. customers. Under NAFTA, however, an expansive range of specific activities is permitted. These activities include:

**Marketing:** market research and trade shows

**Sales:** representatives and agents taking orders and negotiating contracts without delivering products or providing services

**Research and Design:** technical, scientific and statistical research

**After-sales service:** Under NAFTA, after-sales service is described as follows:

> *“Installers, repair and maintenance personnel and supervisors, possessing specialized knowledge essential to a seller’s contractual obligation, who are performing services or training workers to perform services pursuant to a warranty or other service contract incidental to the sale of commercial or industrial equipment or machinery (including computer software) purchased from a company located in Canada, during the life of the warranty or service agreement.”*

United States immigration regulations add two requirements. The first requirement is that the machinery or software must have been manufactured outside the United States. The second requirement, which may be of particular interest, is that after-sales service which includes construction work will not be permitted, save for a narrow exception for supervisory and training activities.

### 5.2.2 Professionals (TN-1)

Under NAFTA, various professionals are permitted to enter the U.S. on a temporary basis to engage in their profession, and they may be paid from U.S. sources. NAFTA lists the qualifying professions and any other eligibility requirements, such as professional licenses, degrees or years of experience. The TN permission is

valid for up to one year, but unlimited extensions of stay may be granted so long as the applicant does not indicate an intention to permanently reside in the U.S. The TN application, accompanied by supporting documentation, may be made at the border or at USCBP pre-flight inspection at certain major Canadian airports (e.g., Trudeau, Pearson, Winnipeg, Calgary and Vancouver).

Professions of particular interest to CCA members include engineers, geologists and scientific technicians/technologists ("ST/T"). The profession of ST/T does not require a baccalaureate degree. However, the applicant must satisfy three criteria:

- Possess theoretical knowledge of one of several scientific disciplines, e.g., chemistry, engineering, geology, geophysics;
- Be able to solve practical problems in that discipline or to apply the discipline's principles to basic or applied research; and
- Work in direct support of a professional in one of the disciplines.

In November 2002, the former U.S. Immigration and Naturalization Service (since merged into DHS) provided guidance to immigration officers evaluating the qualifications of ST/T applicants. The Memorandum contains conservative interpretations of the requirements:

- Individuals whom the ST/T supports must qualify as a professional in their own right.
- The ST/T's work must be inter-related with that of the supervisory professional, i.e., managed and reviewed by professional supervisor, and provide input to supervisory professional's work.
- The ST/T's theoretical knowledge should have been acquired through successful completion of at least two years of training in a relevant educational program.

The two-years of post-secondary education need not be in a single, continuous program. In our experience, individuals may qualify as an ST/T by presenting evidence of completion of multiple, post-secondary educational programs totaling at least two years, e.g., military training. Certain work/study programs offered by trade schools have also passed muster.

#### 5.2.3 Intracompany Transferees (L-1)

An executive, manager or employee having "specialized knowledge" who has worked abroad for at least one of the previous three years for a Canadian employer may enter the U.S. under this category to work for a U.S. affiliate, subsidiary or branch office of the Canadian employer. This immigration classification is desirable because it may later serve as the basis for a permanent residence in the case of executives or managers (L-1A). To apply, the employer's completed petition accompanied by supporting documentation must be presented at the U.S. border or at pre-flight inspection described above. The required one-year period abroad cannot have had significant interruptions.

Canadian firms that have not been doing business in the United States for at least one year will be considered a "new office" under U.S. immigration regulation. As a new office, the Canadian company will have to show that it: (1) has secured sufficient physical premises to house the U.S. business (i.e., one-year lease); and (2) has the financial ability to pay the employees transferred to the United States and to commence doing business.

The L-1 classification is particularly attractive for its flexibility. For example, the Canadian employees transferred to the United States may be paid by the Canadian employer or its U.S. affiliate. Spouses of L-1 transferees may obtain work authorization through a relatively simple application process. With extensions, beneficiaries of this classification may be allowed to work in the United States for seven years (executives and managers) or five years (specialized-knowledge personnel).

### 5.2.4 "Specialized-knowledge" Applications (L-1B)

This category requires the petitioning organization to demonstrate that the applicant has an advanced level of knowledge of, and expertise in, the company's processes and procedures, and that this is not simply general knowledge held commonly throughout the industry. Since no particular academic degrees are required for the specialized knowledge sub-classification, applications for L-1B intra-company transferees are carefully scrutinized by USCBP officials to ensure rejection of common laborers who do not possess truly specialized knowledge. In addition, L-1B candidates who will be stationed primarily at a worksite other than that of the U.S. affiliate of their Canadian employer can expect more probing questions.

### 5.2.5 Temporary Workers in Short Supply (H-2B)

Companies typically use the H-2B category to employ skilled or unskilled foreign nationals for positions for which the employer has a temporary need, and for which qualified U.S. workers are unavailable. The temporary need must be: a one-time occurrence; or a seasonal, peak-load or intermittent need. Under current regulations, in order to show that it cannot find capable U.S. workers, the company must apply for temporary labor certification ("TLC").

The TLC process may not be initiated more than 120 days before the date of proposed employment. *First*, the employer files a TLC request with the local office of the *state* workforce agency ("SWA"); this includes recruitment for the position and determination of the prevailing wage. The company must show recruitment campaign results *and* that U.S. employees are unavailable for the position(s) advertised (e.g., why U.S. job applicants were rejected). *Then*, the U.S. Department of Labor ("DOL") reviews the petitioner's submission regarding completion of the first stage with the SWA. Once DOL issues its temporary labor certification, the employer may file its H-2B petition with U.S. Citizenship and Immigration Services ("USCIS"). If the employees identified in the petition will be working at multiple locations, USCIS may require an itinerary for these individuals. Note that the H-2B classification is among those eligible for premium processing, under which the petitioner receives a response from USCIS within 15 *calendar* days. The additional fee for premium processing for *each position* (not each employee) is $1,000.

***Case Study: The Miller Group - Paving the Way for People on the Move***

*Several years ago, when Toronto-based The Miller Group was working on a project in Maine, a U.S. Immigration official spotted a Canadian employee operating equipment. Unfortunately, while the employee had a valid U.S. work permit to train other workers, operating equipment wasn't part of the deal. Even though it was an honest mistake, the official immediately sent not just the employee, but also the entire crew, back to Canada.*

*"Thankfully, nothing went on their records and within a week we had them all back in Maine under the proper permissions," says Steven Damp, Vice President, The Miller Group. "But this example shows how strictly you need to follow the rules. Ten or 15 years ago, some companies would put guys on a truck and drive across the border. You can't do that anymore."*

*Damp's advice for companies wanting to do construction projects in the U.S. today is to the point: "Don't take shortcuts. It's best to get a U.S. labour lawyer, preferably one who specializes in the state where you plan to cross the border – as well as the state where you plan to work."*

*Founded some 90 years ago under the original name of A.E. Jupp Construction, The Miller Group is a diversified Canadian company with a proud history in road construction, paving, road rehabilitation, and engineering construction for public and private-sector clients throughout North America. The Miller Group was involved in many major projects of the great road-building boom of the 20th century, including the Alaska Highway. With more than 3,400 employees today, The Miller Group says it bases its success on time-proven construction methods and innovative technology, backed by strong technical and financial resources.*

*Damp says the Miller Group first began doing work in the U.S. when it picked up some contract work in Georgia. "At that time, we learned the two biggest challenges of doing business in the States. One is dealing with legislative and document requirements, such as taxes, insurance, licensing and bonding. The other is labour mobility."*

*... (cont.)*

In January 2005, USCIS and DOL proposed changes which would streamline the H-2B program. Under the proposed one-step process, most employers would no longer be required to file for a labor certification from DOL before filing an H-2B petition with USCIS. Instead, most employers would file an H-2B petition

directly with USCIS after conducting their recruitment for U.S. workers. These proposed regulations have not been adopted.

*Case Study: The Miller Group (cont.)*

***Honesty is the Best Policy***

*Until recently, Canadians traveled with relative freedom into the U.S., and this sometimes included the "smile and wave" approach to crossing the border to work. The traveler was either waved through without any questions from border guards regarding the purpose of their visit, or a company letter and return ticket was produced, indicating the traveler would be working in the States for a specified purpose and length of time.*

*Damp doesn't recommend the smile and wave method. "The Miller Group's corporate culture says you never lead anyone to believe you're going to the States on vacation when you're going there to work. It's a foolish risk that puts your customers and workers in peril, and can delay the project and damage your reputation."*

*And while taking explanatory company letters to the border isn't dishonest, it's still risky, according to Damp. "Three-quarters of the time, the person (at the border) will let you in, but you can still be refused or told to come back the next day, causing delays to the project." Once again, Damp's advice is to hire a labour lawyer. "Since we did this five years ago, virtually all our workers have been accepted."*

*The Miller Group also found that opening a subsidiary in Atlanta has helped. "Setting up a U.S. business is very complex and requires substantial costs upfront," says Damp. "It doesn't mean you can work in all states. But once it's done, you can have your American business enter into contracts to make things easier, and use your business lawyer to find out what you need to do to comply in each state or case."*

The annual cap (limit) for the H-2B program is 66,000. In May 2005, legislation entitled "*Save Our Small and Seasonal Business Act of 2005*" (the "*SOS Act*") provided relief to employers adversely affected by the annual cap being reached early in the *calendar* year; the U.S. Federal Fiscal Year ("USFY") begins October 1 of the *previous* calendar year. For example, the cap for USFY 2005 was reached in January 2005. The *SOS Act* divides annual allotment of H-2B's into two portions: 33,000 distributed in the first half of USFY, and the remaining issued in the second half for employers whose seasonal needs occur between April 1 and September 30.

The *SOS Act* exempts from the cap certain foreign nationals, called "returning workers"; in order to qualify, the worker must have counted against the H-2B numerical cap during any one of the three U.S. Fiscal Years immediately preceding the USFY of the requested employment start date. While the annual H-2B visa cap remains at 66,000, this provision of the *SOS Act* effectively increased the number of workers available to U.S. employers by exempting those returning workers from the cap.

## 5.3 Entry Problems

### 5.3.1 Immigration Issues for Construction Services

Cross-border movement of workers has become a difficult issue for Canadian construction companies engaged in projects in the U.S. The entry of construction workers and tradespeople is not covered by NAFTA; instead, the entry of these types of workers is subject to labour certification by the U.S. Department of Labour.

As a result, scheduling can be a major issue for a construction company; getting workers cleared for U.S. entry can take weeks, which can cause serious problems with project deadlines. Managing the application process yourself will be complicated and time-consuming, and your best strategy may be to hire a legal expert to deal with it.

### 5.3.2 Immigration Issues for After-Sales Services

Repair, warranty, maintenance and related services are described under NAFTA as work done by:

> "*...installers, repair and maintenance personnel and supervisors, with specialized knowledge essential to a seller's contractual obligation, performing services or training workers to perform*

*services, pursuant to a warranty or other service contract which is incidental to the sale of commercial or industrial equipment or machinery. This includes computer software, purchased from an enterprise located outside the U.S."*

U.S. immigration officials can be quite sensitive about after-sales service. Hands-on building and construction work do not fall under the after-sales service provision of the NAFTA business visitor category, so you will need to prove that the work you will be doing inside the U.S. does, in fact, fall under the NAFTA regulations. To do so, you will need a copy of the original sales contract, which must clearly state the service work to be done. Showing a company letter that describes the reasons for the business trip is also a good idea.

## 5.4 Company Personnel Crossing the U.S. Border

Canadian construction firms that do business in the United States, even those that eventually end up setting up a U.S. subsidiary or sales office, will occasionally need to send personnel there. To solicit new bids or orders, to complete contracts and to conduct after-sales service, you need people on the ground. So being aware of the issues involved in moving people across the border becomes an absolute must.

### 5.4.1 Passports

As this is being written, American officials are currently implementing rules that will require all Canadians traveling there to carry a valid passport. These rules are already in effect for those traveling by south of the border by air. However U.S. Customs and Border Protection has pushed back the requirement for those entering by land or sea.

The target implementation date is available on the U.S. Department of Homeland Security website. (See Appendix C: Resource Directory)

As a result, U.S. border officials strongly advise Canadians planning to travel there to procure passports as soon as possible.

### 5.4.2 Business Visitors to the United States

Construction personnel that travel to the United States could be subject to a variety of laws and regulations, depending on the length of their stay, whether they will be remunerated for their services by a U.S. company, the type of work that they do and the individual states that they plan to visit.

Canadian visitors that travel to the U.S. temporarily for business purposes, such as attending business meetings, conducting market research, providing after sales service or soliciting new business and who are paid by their Canadian employer generally fall under the (B-1 Visa) provisions. Canadian visitors to the United States whose activities are governed by the B1 provisions, generally do not require a visa.

That said, in general, temporary business visitors to the United States are not permitted to engage in after sales services construction work. The only exception would be for supervisory and training activities.

### 5.4.3 NEXUS Program: Simplified Border Clearance

The NEXUS program is an initiative designed to speed up border clearance for low-risk, pre-approved travelers into the United States and Canada. The Canada Border Services Agency and the United States Customs and Border Protection (CBP) are cooperating on the program, which is designed to both boost security and speed up travel.

The program's 130,000 or so members get a membership identification card that they can use at all land, sea or air ports of entry. To become a program member, travelers need to submit an application, satisfy all eligibility criteria and then pass a risk assessment.

# 6. EMPLOYEE ISSUES

## 6.1 Mandatory Minimum Wage Rates

The federal government and every state have imposed minimum-wage laws which govern virtually all workers. These laws generally will not adversely affect Canadian construction companies, however, since the wages paid to Canadian employees are usually in excess of these rates.

Another minimum-wage scale applies, however, on many public projects. The federal government, through the so-called *Davis-Bacon Act*, mandates that every person working on a project with federal funding (whether the project is a federal project, state project or local project) must be paid the so-called "prevailing" wage rate for workers in each classification. The "prevailing wage rates" are set periodically by the Secretary of Labor, and are intended, in part, to reduce the bidding advantage otherwise held by non-union employers who may not otherwise provide the pay rates or benefits required under union contracts. Many states have adopted similar programs for some or all of their state projects.

These minimum wage rates must be included in the contract documents for federally funded projects, and generally are set out in the bid documents for state projects as well. These rates may have the practical effect, however, of reducing any competitive advantage that might otherwise be obtained through generally lower wages paid to Canadian employees.

## 6.2 Workers' Compensation Insurance

Canadian workers receive health benefits by virtue of their citizenship (and provincial residence) which are not generally available to U.S. citizens. Because those benefits extend to care for injuries sustained at work, many Canadian companies mistakenly conclude that they need not obtain workers compensation insurance for Canadian citizens working on U.S. projects. This is not the case, however, neither under the applicable laws nor under standard construction contracts.

It is uniformly the law throughout the various states that every employer must either provide commercial workers compensation insurance to protect its employees or, in limited circumstances and with the state's approval, self-insure against that risk. Officers and directors of companies which do not provide this kind of insurance can be found personally liable for workers compensation benefits and may be subject to criminal liability as well.

In addition, special rules apply in the construction context which may expand the scope of the "employees" of a company beyond the Canadian citizens it pays. Employees of uninsured subcontractors are regarded as the employees of the general contractor or subcontractor that hired the uninsured subcontractor. Under this provision, then, the Canada-based company that used subcontractors to perform a part of its work might find itself responsible for workers compensation benefits to the employees of that subcontractor. Those employees may well not be Canadian citizens, with the Canadian health benefits.

Finally, all of the major forms of construction contracts in the United States require the general contractor and all subcontractors to maintain workers compensation insurance. This is a universal requirement because of the special provision in the workers compensation laws discussed in the preceding sentences. Property owners become responsible for workers compensation benefits to construction workers employed by uninsured contractors and subcontractors. As a result, the owners impose contract provisions requiring the contractors to obtain insurance to protect the owners from that kind of liability.

*Case Study 4: Orbi Metal Construction, Inc. - Insuring a Bright Future*

*Even at a young age, brothers Carlos and Néstor Stella had a dream of launching a company that specialized in the planning, manufacture and erection of architectural and ornamental metal structures. In 1990, with the help of two friends, they realized that dream with the launch of Orbi Metal Construction, Inc. Understanding the pride of company ownership, they eventually even set up a work cooperative, giving their employees the opportunity to become partial owners of the company too. In 2006, they achieved ISO certification.*

*When you do what you love, you tend to do it well. With the Stella brothers at the helm, Orbi Metal Construction quickly established a reputation for quality work and an ability to handle complex structural steel projects.*

*But as the company grew and expanded, they began to eye a larger, even more promising market south of the border. "Our work was very specialized, and so the market here in Canada was relatively narrow," explains Carlos Stella. "When we entered the U.S. market in 1998, it not only offered more opportunities, but the strong American dollar at the time also meant we were very competitively-priced, including our labour, and we could earn stronger revenues as well."*

*The company's skill and cost-effectiveness earned increasing success in its new market. Orbi Metal Construction strengthened its American presence in 1999 by opening a U.S. division called Orbi Iron Works, and over the next several years, it worked on such prestigious construction projects as the Harvard University Life Sciences Building, the Smith College Fine Arts Center in Massachusetts, and the American Airlines Arena in Miami, Florida.*

*But when the Canadian dollar began to grow stronger after the Millennium, the company began to lose their competitive price advantage. "We were also working at times in states with very strong unions, and this further increased our prices," says Stella. "In 2005/2006, we decided to work with our own installation crew."*

*To achieve this, Orbi had to go through the usual process of getting permissions for its employees to work in the U.S. "Our employees had to pass exams and get licenses, and we hired an immigration lawyer and had visas prepared."*

*Insuring a Good Outcome*

*A particular challenge, however, was getting insurance. "It is not easy to get liability insurance or workers' compensation insurance down there, because of the whole American environment of personal injury and liability lawsuits," Stella explains. But Stella was able to convince the insurers to cover the company. "We did this by showing them that we had a rigorous Canadian safety program, that we worked very prudently and that we had lots of contracts and were therefore financially solid."*

*They also needed help with receivables insurance. "As the suppliers of architectural metals, we're generally sub-contracted by the general contractor of a project, who is in turn contracted by the project owner," Stella says. "However, if the owner defaults on paying the general contractor, the general contractor is under no obligation to pay the sub-contractors." The Stella approached Export Development Canada, who worked with the company to devise receivables insurance coverage for both the general contractor and the project owner.*

*"We're now working in Washington, DC and have picked up $10 million in contracts," Stella says. "We're a good team, and we try to improve every day. Ultimately, it is the quality of your work that helps you perform, whether it be in the U.S. or Canada."*

## 6.3 U.S Workers' Compensation: Considerations for Canadian Contractors

Canadian contractors are increasingly doing business in the United States. Unfortunately, Workers' Compensation coverage issued by the various provincial Workers' Compensation Boards (hereinafter referred to as WCB) although broad enough in scope under some circumstances to cover injuries to Canadian workers in the U.S may not be acceptable to either the state jurisdiction in which the U.S work is being performed or the party with whom the work is being contracted.

The jurisdictional and contractual requirements may mean that U.S Workers' Compensation (hereinafter referred to as USWC) insurance will be necessary for even the smallest contracting operation. The circumstances that require WC insurance are many and varied e.g., Canadian employees who make extended U.S visits or who maintain temporary residency in the U.S. (site supervisors or engineers) overseeing installations.

Deciding on proper coverage is complex insofar as each state has its own USWC laws. Consequently, contractors with U.S operations should consider the following when deciding how to insure their employees.

Construction contracts in the U.S typically have insurance provisions where the responsibilities of the contracting parties are specified for various areas of insurance.

There are basically two insurance arrangements which arise in the Workers' Compensation area. The first is an 'Owner Controlled Insurance Program (OCIP)' under which the contract issuer e.g., project owner, arranges insurance for all contracted parties to be insured under one policy with one insurer. If this situation applies then the Canadian employees falling under the scope of the contract are picked under the OCIP. You may be able to approach your provincial Workers' Compensation Board to exclude the payroll for the subject employees while working in the United States.

The second situation arises by default, that is, if the contract does not fall under an OCIP then YOU will be responsible for ensuring that your employees are properly covered for USWC; however, the means with which this can be accomplished depend on the circumstances.

Before getting into the USWC options you have, a discussion (see below) of two concepts is appropriate.

Extraterritoriality and Reciprocity- Extraterritorial provisions extend workers' compensation coverage from a 'home' jurisdiction (e.g., state or province) while he/she performs temporary work in another jurisdiction. A 'home' jurisdiction is where the permanent employment contract between employer and employee originated. Benefits for work related injuries are provided as if the worker were in the home jurisdiction.

The complement to extraterritoriality is the concept of reciprocity where two jurisdictions agree to honor the extraterritorial provisions of the other. This finds application when employees from each of the reciprocating jurisdictions have occasion to work within one another's territory.

While extraterritoriality and reciprocity exist between the provinces and between many states and it is true that provincial WCB coverage is extra-territorial for Canadians traveling to the U.S for temporary work, reciprocity does not generally exist cross-border between provinces of Canada and any of the states in the U.S. This places the Canadian based contractor in a dilemma.

Despite each Canadian contractor having extraterritorial coverage under WCB for its employees working in the U.S, the absence of reciprocity means that the U.S state in which the Canadian is working will not recognize WCB as valid USWC coverage.

It follows that the U.S entity with whom the contract is being entered is unlikely to accept WCB as 'proof of coverage'. The circumstance being described assumes that the work in the U.S. is done under contract and as such the expectations for proof of USWC coverage becomes more rigorous. This arises since injuries to a Canadian employee would not be subject to the doctrine of 'exclusive remedy' because a USWC policy was not purchased which would otherwise bring the employee under the workers' compensation statutes of the state. Without 'exclusive remedy' the Canadian contractor and U.S contract issuer would be vulnerable to a tort action from the employee to recover for its injuries. Every state's workers compensation law contains an 'exclusive remedy' provision that stipulates that the benefits prescribed in the workers' compensation statutes are the sole remedy for injuries sustained on the job. Without the provisions of exclusive remedy injured employees can sue their employer under common law. Significantly, most states allow suits against the employer if the employer has failed to purchase workers compensation insurance.

In practice, the extension of Canadian WCB to your employees applies if their presence in the U.S is short in duration and if their work in U.S is not required to be evidenced by 'proof of USWC' by the U.S entity for which the work is being performed.

### 6.4 Purchasing a U.S Workers' Compensation Policy

Purchasing a policy for USWC will require you to assemble information and to consider options based upon the circumstances of your insurance requirements.

### 6.4.1 Exceptions - Monopolistic States

There are five states in which the procedure for purchasing USWC coverage is similar to the WCB provincial models, that is, where workers' compensation insurance is purchased from a government agency. These states: North Dakota (ND), Ohio (OH), Washington (WA), West Virginia (WV) and Wyoming (WY) are known as 'Monopolistic State Funds' where USWC is purchased by the employer directly from the state. If your contract involves work in these states you can approach the state funds directly.

# 7. CUSTOMS ISSUES

## 7.1 Introduction

Canadian construction companies that do business in the United States almost by definition need to deal with customs and border issues on a regular basis. Depending on the nature of the project that they are involved in, Canadian companies shipping goods, soliciting business or completing contracts south of the border may need to send equipment, products or personnel there. Each of these cross-border movements can lead to challenges at the border if they are not handled correctly. The following are common customs and border issues facing local firms who want to build their U.S. business.

## 7.2 The New Border Security Environment

The implementation of the North American Free Trade Accord during the late 1980s and early 1990s led to a vast increase in border traffic and smoother flows at the border, as tariffs on a vast variety of goods crossing there were first reduced and then eliminated. Strong and growing economies on both sides of the border also resulted in a somewhat more relaxed attitude among border officials to people crossing the Canada-U.S. frontier.

However 9-11 changed all that. Since then, the United States has invested heavily in border security, hired new agents, implemented information technology systems, boosted regulations and began enforcing others that had previously not been enforced to the same degree. In fact one of the biggest challenges that Canadian construction companies face when dealing with border issues is navigating the new border security environment.

The U.S. Customs and Border Protection Department is currently developing and implementing a new commercial trade processing system, called the Automated Commercial Environment (ACE), which is expected to go a long way toward facilitating legitimate trade, while lengthening border security. Other initiatives, such as the NEXUS program, which now includes over 130,000 members, simplifies border clearance for regular low-risk travelers.

Many of the new American (and Canadian) border protection initiatives are being phased in gradually over the course of several years. Not surprisingly, border personnel may sometimes seem overwhelmed by the transition. The result has been long border line-ups and more paperwork for Canadian companies. That said, businesses that take the time to familiarize themselves with U.S. customs and border issues, will go a long way toward alleviating those difficulties.

## 7.3 Customs Brokers and What They Do

Your U.S. customs broker will act on your behalf to clear your goods through customs and deliver them to their final destination. In the United States, customs brokers are licensed, bonded and regulated by U.S. Customs and Border Protection.

Using a U.S. customs broker is usually mandatory. The benefits of doing so, for the exporter, include:

- Brokers stay up-to-date with all customs regulations and procedures, and will be aware of changes well before you are.
- They prepare all the export documentation that Canada and U.S. Customs require.
- Before your goods can clear customs, U.S. regulations require a bond for their value plus any duties. Your broker will arrange this bond for you.
- A broker will clear your goods through customs quickly, sparing you storage costs.

To find a U.S. customs broker, check the Web site of the National Customs Brokers & Forwarders Association of America (NCBFAA). Alternatively, you can find a broker at a particular port of entry by visiting the Ports of Entry page on the U.S. Customs and Border Protection site. Select the port of entry and scroll down the page to the link for its brokers list.

As already noted, your broker will handle most of the documentation and procedures required to clear your shipments into the United States.

### 7.4 Clearing U.S. Customs

You should ensure with your carrier that the importer of record will be notified of your shipment as soon as it arrives at U.S. Customs. The importer of record is responsible for filing all entry documents with the authorities at the port of entry. When exporting from Canada to the U.S., the importer of record can be the exporter (you), your consignee/buyer, or the U.S. customs broker.

If you want to defer payment of duties and processing fees until you have completed the sale of your goods, you can have them sent to a bonded warehouse. Duties and fees are not levied until the goods leave the warehouse.

After the goods have arrived at the port of entry, they will be examined by U.S. Customs officials to determine:

- the value of the goods for customs and duty purposes;
- the validity of the marking and labeling;
- the validity of the invoice;
- whether the shipment contains any prohibited goods; and
- whether the requirements of other U.S. federal agencies, such as the Department of Agriculture, have been met.

Once the customs officials have decided that the shipment and its documentation are in order, the goods are allowed to proceed into the U.S. The broker then determines the duties or fees payable and files this information, along with any payment due, with U.S. Customs. After official appraisal of the goods, the entry is "liquidated," meaning that the final computation of duties and/or drawback is complete.

### 7.5 Get Prepared Early

Probably the most oft repeated advice by Canadian carriers, customs brokers and construction companies that deal regularly with shipments into the United States is to prepare early. In practice, that means engaging the services of a reputable customs broker, who can run through the processes with you and let you know the potential pitfalls regarding the products that you plan to ship.

Canadian construction companies ship a broad variety of consumable goods into the United States, many of which are specialized in nature. That means getting the facts straight, regarding the tariff classification of the products to be shipped is crucial, as is preparing a dossier to back oneself up just in case that determination is challenged.

### 7.6 Getting Your Paperwork in Order (Routine Shipments)

Once a Canadian construction company is registered within the ACE system and then begins to ship product regularly to the Untied States, things get substantially easier for everyone involved: the exporting company, the carrier, customs brokers and border personnel. These shipments then to certain extent tend to gradually become routine.

That said, many participants in the process have stressed the fundamental importance of getting all of the paperwork done correctly. Among the more common documentation required by both U.S. and Canadian customs officials for shipments crossing the border are a bill of lading, packing slip, certificates of origin and pro-forma or actual invoice. An inordinate amount of border headaches are caused by ignoring this basic step.

### 7.7 The ACE System

During late 2006, the U.S. Customs and Border Protection (USCBP) announced that henceforth all transportation carriers that plan to bring cargo into the United States need to submit electronic manifests prior to arriving at specific land border crossings. This initiative is part of the Automated Commercial Environment, an electronic trade processing system that is currently being developed by the USCBP to ease trade and beef up border security.

The upshot is that Canadian construction companies that are planning to use their own trucks to ship products to the United States need to make sure that they are registered into the ACE System. Once the application is complete, the USCPB can then store the crew, equipment and shipper information in an account, which in principal makes future border crossings easier, by reducing processing times.

That said, some stakeholders have noted that at the time of this writing, the application backlog to join the ACE system remains long. Thus companies that intend to sign on need to do so well in advance. Another point to remember is the Automated Commercial Environment deployment is a work in process. U.S. border officials are labouring diligently to implement the system at all of the country's 99 land crossing points, after which the system will then eventually be extended to all rail, air and sea cargo ports. Until that process is complete, exporters should to expect the occasional glitch in the system.

### 7.8 Moving Construction Materials Across the Border

Despite the existence of a North American Free Trade Area, the movement of construction materials and equipment from Canada into the United States remains constrained by a variety of U.S. legislation and regulatory statutes. The sheer volume and scale of this legislation make it imperative that any Canadian firm seeking to do business in the United States get appropriate legal and technical support earlier on in the process, so that potential hurdles can be overcome.

Among the many legal texts that may apply, depending on the products or equipment being shipped by Canadian construction companies into the United States, are Title 19 of the Code of Federal Regulations, (which deals with customs issues), the U.S. *Bio-Terrorism Act*, the U.S. *Trade Act* of 2002 and the *Jones Act* regarding the transit of foreign vessels on U.S. navigable waters.

### 7.9 Moving Construction Equipment Into the United States

Canadian companies that complete construction engagements south of the border will often want to move equipment there, either permanently or temporarily. As with many border challenges, the type of construction equipment that Canadian companies may want to send south can fall in a wide range of categories, all which are subject to different laws and regulations. In addition to NAFTA criteria, equipment sent to the United States may be subject to Department of Transportation, environmental protection and other guidelines.

> ***Case Study: Aluma Systems Canada, Inc- Concrete Solutions to Equipment Crossing***
>
> *When crossing the border between Canada and the U.S., the need to prove a person's place of origin is commonly understood. But less commonly known is a company's need to prove where its equipment originated. With duties, tariffs, taxes and restrictions for use riding on the answer, equipment essentially requires its own set of documentation, almost like a human passport. "And make sure," cautions Ian Steer, Aluma Systems Canada Inc., "that your 'Made in Canada' labels themselves don't in turn have 'Made in China' printed on them."*

*Case Study: Aluma Systems Canada, Inc- (cont.)*

*Aluma Systems, purchased in 2005 by American-based Brand Services, is a world leader in scaffolding and concrete construction forming and shoring. Celebrating its 35th anniversary in 2007, Aluma Systems has helped build high-rises, hotels, parking garages, airports and bridges, including the Confederation Bridge linking Prince Edward Island to mainland Canada. The company has been doing business in the United States since the 1970s, and has more than 3,500 employees and $860 million in annual revenues.*

*"Our equipment is rented by other companies to use on their construction projects, so it's always moving," says Steer. "If your equipment is manufactured in Canada or the United States, you can get it across the border fairly quickly. But not if you haven't done your homework first."*

***Keep Meticulous Records***

*For Aluma Systems, that homework begins by keeping meticulous records of where a piece of equipment was built, where it's going and where it's been, and even where and when it's received repairs or upgrades. The reason for all the documentation, as Steer explains, is that even some new parts made in a foreign country can cast doubt on a piece of equipment's place of origin. This can cause delays and possibly result in higher duties and taxes on the piece.*

*"It can look like a big challenge, but it's worth your while to document and label every piece," says Steer. "You also need to make sure you have all the key documents, like the ownership, proof of export, and the NAFTA certificate of origin, to name a few."*

*Steer adds that Aluma Systems has two full-time employees just to complete all the paperwork. "We've also created checklists of everything we need to do to move a piece of equipment, including all the special requirements you need for shipping certain types of equipment, such as computers for example," he says.*

*The company also makes use of professional help such as specialized lawyers and customs brokers. "Processes are important too, and it's important to pay attention to those details as well. We hire customs brokers who can walk our equipment through the customs process. They're experts on what to do, so they can generally get it through faster."*

*While it might seem daunting, Steers advises that once the homework is done, the U.S. is a big and lucrative market for Canadian companies. "We were Canadian-owned, but our success story was built by doing business in the United States. It's only difficult when you try to rush things through."*

Companies that transfer equipment, whether it be tractors, paving machines, asphalt rollers or any other device that helps complete a contract to their U.S. subsidiaries are subject to the rules of traditional consumption entries. In certain cases, depending on where that equipment was acquired, particularly if it was from a non-NAFTA nation, the equipment may be subject to duty.

As result, shippers will need a valid NAFTA certificate to prove the equipment's origin. The upshot is that keeping a clear record of each piece of equipment's origin, use and any additions or improvements that may have been made to it is an absolute must. Customs officials have also been known to make distinctions between equipment that a company owns and equipment that is leased. In the case of leased equipment, customs officials have on occasion asked for proof that the lessee has the right to transfer the equipment out of the country.

### 7.10 Bringing Construction Equipment Into Canada

The main customs and border issues that Canadian construction companies that do business in the United States deal with regarding equipment, tend to be when they move machinery, trucks, tools and the like from their Canadian operations into the United States in order to complete contracts or assignments.

But getting the equipment into the United States is only part of the story. Getting it back into Canada also can have its challenges, as does arranging temporary or permanent equipment transfers from U.S. based subsidiaries back to their Canadian parents.

The fact of the matter is that although the Canada Border Services Agency tends to be a bit more relaxed than its U.S. counterpart, Canadian construction companies that move goods across the 49th parallel regularly will still need to keep up with regulatory changes and other developments.

### 7.11 Bringing Canadian-Sourced Equipment Back Into Canada

Very often Canadian contractors send their own (Canadian-sourced) equipment to the U.S. However when their work there is done, they will often want to bring that equipment back into Canada. Fortunately goods, including equipment, that originated in Canada, which are sent to the United States, can be brought back here tariff and duty free, as long as they have not been “advanced in value or improved in condition by any process of manufacture or other means.”

That said, as with all border issues, keeping one’s paperwork in order remains a priority. Documentation related to the equipment’s history, use and ownership, coupled with the initial proof of export documentation provided to U.S. border officials (such as the bill of lading, pro-forma invoice and so on) as well as a Canada Customs Invoice, need to be in order when the equipment is brought back.

### 7.12 Bringing U.S.-Sourced Equipment Into Canada

Many Canadian construction companies set up U.S.-based subsidiaries in order to facilitate their operations there. On occasion, they will want to transfer equipment from those U.S. operations into Canada either temporarily or permanently. As with most NAFTA goods, construction equipment is exempt from duty. However if the equipment originates in whole or in part in third party nations, duty may be applicable. As a result, maintaining proof of the equipment’s origin is a must.

That said, equipment brought into Canada will be subject to the Federal Goods and Services Tax (GST) as well as to provincial sales taxes on the value of those goods at the time they are imported. If the equipment is brought into Canada temporarily, then a refund can be claimed when they are re-exported to the U.S.

In the case of leased goods, companies must pay GST on the full value of the equipment brought into Canada. However, once again, if the equipment is imported temporarily, then the GST can be reclaimed when the goods are re-exported back into the U.S.

### 7.13 Temporary Importation Bond

In general, under NAFTA, if the equipment to be transferred is made in Canada or the United States, getting it across the border is fairly straightforward and payment of duties will not be required. However in certain cases, particularly if there is duty to be paid when moving equipment, companies may elect to apply for a Temporary Importation Bond.

Temporary Importation Bonds (or TIBs) as they are known in the customs trade, are governed by the provisions in Title 19 of the U.S. Code of Federal Regulations, part 113. Canadian construction companies are eligible to apply for a TIB, if the equipment is to be sent to the United States and will remain there for less than a year before being re-exported.

That said, TIBs are not cheap to arrange and they require more paperwork than a typical consumption export. It may sometimes thus be easier in the long run in some cases to just send equipment to the U.S. under traditional provisions and to just pay the duty.

### 7.14 Required Documentation for Formal Entry

Your shipment, if destined for formal entry, will require the following documents and information:

**Commercial invoice:** Also known as a business invoice, this must exactly represent the content and value of your shipment. If you just happen to toss in a few promotional items at the last moment and they are not on the invoice, the customs inspector may hold your shipment at the border until you clarify what is going on. Also, never declare goods, such as promotional items or samples, as being of "No commercial value." U.S. customs officials may decide to impose a value of their own or may even refuse entry of the goods.

**NAFTA Certificate of Origin:** A document that certifies the country where the product was made (i.e., its origin). A common export document, a certificate of origin is needed when exporting to the United States. It must be used for Canadian-made goods to qualify for preferential tariff treatment under the North American Free Trade Agreement.

**Importer ID Number:** Also known as the Customs Assigned Number, this is used by U.S. Customs to establish bond coverage, release and entry of merchandise, liquidation, the issuing of bills and refunds, and drawback processing. Your customs broker can help you obtain the number or you can get it yourself by submitting Form 5106 to U.S. Customs.

**Bill of Lading or Airway Bill:** Your freight forwarder, carrier or broker is responsible for filling it out. A bill of lading is not needed for mail shipments.

**Entry Manifest:** The carrier is responsible for filling this out. Again, this is not needed for mail shipments.

**Entry/immediate Delivery:** This is used for time-sensitive shipments, such as fresh produce, and replaces the entry manifest. The carrier is responsible for submitting this to U.S. Customs before the shipment arrives at the port of entry.

**Harmonized System Tariff Classification (HS Code)**

Depending on the nature of the goods, the shipment may also need to be accompanied by permits or licenses (if they are controlled goods) and a packing list.

### 7.15 Informal Entry of Goods

Your goods are considered an informal entry if their value is less than US$2,000, and provided they are not controlled goods. As we also mentioned earlier, informal entry does not require a broker if the shipment is accompanied by the exporter, or if the consignee comes to the port of entry to collect it.

Documentation for informal entry is less stringent than it is for formal entry. The shipment must have its commercial invoice with it. You should also include a NAFTA Certificate of Origin; while this is not legally required by U.S. Customs, providing one will smooth your shipment's path across the border.

### 7.16 Penalties and Seizures

U.S. Customs levies severe penalties for fraud or negligence, so you have to be very sure that the information you give about your exports is accurate and complete. If you discover errors after your goods have entered the U.S., notify your customs broker immediately; you may be able to avoid penalties through prior disclosure of the mistake (in other words, before U.S. Customs detects it).

You will not normally be penalized for clerical errors or omissions, but negligence or gross negligence, as defined by U.S. Customs, can draw penalties of up to four times the duty or 40 percent of the value of the goods. The penalty for outright fraud, such as false valuation, can be the entire value of the shipment or seizure of the shipment. Again, your best defence against such problems is to be very thorough and precise in preparing your documentation.

### 7.17 Customs and Border Issues: An Ongoing Priority

Border issues between Canada and the United States are not going to go away anytime soon. However because of the size and potential of the U.S. market, Canadian companies are going to need to show greater sensitivity to those issues than they did during the good old days in the post-NAFTA and pre-9-11 period.

Recent media attention regarding the more than 10 million Mexicans who are now in the U.S. illegally, threatens to make the subject a major issue in the 2008 U.S. presidential campaign and its aftermath. Any further enforcement on the U.S. southern border no doubt risks turning attention to the 49th parallel too.

Furthermore, America’s War on Terror is unlikely to wrap up anytime soon. U.S. armed forces are deployed in well over a hundred countries. In many of those countries these forces are engaged in conflicts, ranging from anti-drug operations in Columbia to anti-guerrilla operations in Iraq, Afghanistan, Pakistan and the Philippines. And as 9-11 demonstrated, retaliation by any one of America’s many adversaries on its homeland could come at any time.

As a result, Americans in general, not just customs and border officials, are far more sensitive to security issues than many Canadians can understand. That means Canadian companies that want to move people, products or equipment across borders, need to adjust their business strategies and operations to make sure that they comply with evolving cross border issues.

## 8. LIEN LAW TRUSTS: MORE VALUE THAN A MECHANIC'S LIEN

Lien Law Trusts can be more powerful than a mechanic's lien and can help ensure you get paid when you take on a construction project in the United States. We will examine how these trusts are used to protect subcontractors and vendors using the New York Trust Fund Statute in Article 3-A of the New York State Lien Law as an example.

When a Canadian construction firm does not get paid on time, one of the first things that comes to mind is a construction mechanic's lien which can be a valuable tool to enforce the right to get paid. However, a mechanic's lien can come with a minefield of problems and expenses. An alternative is a Lien Law Trust. Lien Law Trusts are not available in all States; only twelve have such statutes. Where available, these tools should be considered when a subcontractor or vendor is unpaid.

Twelve American states impose this special financial obligation upon contractors, subcontractors and sometimes owners. This protects subcontractors, vendors and lower-tier subcontractors, and provides a greater assurance of payment. It arises from the application of a trust upon construction funds in the hands of contractors.

### 8.1 The Purpose of a Trust

In common law, a trust is created when one party seeks to protect assets. A parent might set up a trust for their child. The parent is the grantor and the child is the beneficiary. The parent might designate an attorney, bank or some other representative as the trustee to manage the trust.

A trustee is charged with legal responsibility for taking care of the beneficiary, which is a duty of trust and fidelity. Their motive must always be in the best interests of the beneficiary, not themselves. If they take money, they are responsible and in some cases, can be charged under the Criminal Code with larceny.

This concept of a trust between a trustee and beneficiary applies to the construction industry in States with trust fund statutes.

### 8.2 Drawbacks of a Mechanic's Lien

A mechanic's lien alone does not necessarily put money in the hands of a subcontractor or a vendor. The lien must be foreclosed, which can be burdensome and expensive. A mechanic's lien is foreclosed against real property or public funds in those States which permit a public improvement mechanic's lien.

In concept, the foreclosure ends when the property is sold. Parties with an interest in the property must be named in the lawsuit. The lenders and other lienors must be named, the list varies from State to State. The lienor must worry about lien priorities. A secured financial lender, for example, might have priority over a subcontractor or vendor in a lien foreclosure, so the lender is entitled to the lion's share.

In some States, the value of a lien can also be limited by the status of payments in the contracting chain. For example, if a construction owner has paid a general contractor in full at the time that a lien is filed, the lien may have no value. The value of the lien may be limited by the fund of money, known as the lien fund, that exists between the owner and the general contractor at the time of filing. Likewise, the value of the lien can be limited by the fund of money owed from a general contractor to a subcontractor, a problem for a vendor or sub-subcontractor.

For example, a vendor which supplies structural steel to a subcontractor must be concerned that there is adequate money owed from the owner to the general contractor, and from the general contractor to the subcontractor at the time the lien is filed. If these funds are not adequate to satisfy the lien, then the foreclosure may result in partial or no recovery.

This is why foreclosure proceedings can be time-consuming, expensive and frustrating. Consider a $50,000 mechanic's lien on a $20 million high rise in New York City. What is the value of that $50,000 mechanic's

lien when that lienor is only one lien of $5 million worth of mechanic's liens being foreclosed? What is the cost of foreclosure? This is why you may want to consider statutory lien law trusts in addition to a mechanic's lien.

### 8.3 Statutory Lien Law Trusts

In States where there is trust fund law, a general or prime contractor that receives payment from a construction owner must use the payment first to pay beneficiaries. The general contractor becomes trustee of those funds.

The statutes define who are the beneficiaries of that trust. For example, in New York State the beneficiaries of the Lien Law Trust Fund include:

- Subcontractors
- Material vendors/suppliers
- Laborers
- Draftsmen
- Architects

A typical lien law trust statute provides that upon receipt the trustee/general contractor must utilize the funds first for the payment of beneficiaries. For example:

A general contractor submits a progress payment application to an owner for $100,000. The owner pays $95,000, the amount due minus 5%. The $95,000 payment becomes a trust fund. The general contractor becomes a trustee for that $95,000.

The general contractor has the obligations of a trustee with all funds which are due to the beneficiaries:

At the time that the general contractor received $95,000, a vendor is owed $40,000. There is a trust obligation imposed upon the general contractor for the benefit of that vendor in the amount of $40,000.

The general contractor is now in the possession of trust fund assets. As a trustee, the general contractor must apply the trust fund assets for the trust purposes before the general contractor applies the money to its own overhead or profit. Trust purposes include payment of subcontractors and vendors. If trust funds are applied by the trustee to some purpose other than the payment of trust fund obligations, then the general contractor may have diverted trust funds. A diversion of trust funds can carry serious legal implications. Consider the following:

1. The general contractor's progress payment application was his fifth application for payment on the project. There are other projects in progress where the general contractor is late in paying vendors. The general contractor needs to support new projects and pay old debts. The general contractor applies $75,000 of the $95,000 payment to those other projects.

OR

2. The general contractor needs a new pick-up truck. $40,000 buys a nice pick-up truck.

These are examples of diversions of trust fund assets. Whether the diversion is for the purpose of paying someone on another project, for buying a pick-up truck or for some other purpose, the diversion is illegal.

### 8.4 Trust Fund Statutes

Twelve of the 50 States are Trust Fund States. Each State has its own laws, procedures and statute of limitations for the commencement of an action.

Arizona, Colorado, Delaware, Florida, Illinois, New Jersey, New York, Maryland, Michigan, Oklahoma, Texas and Wisconsin are Trust Fund States.

Trust fund statutes can include such powerful tools as the following:

- Personal liability
- Punitive damages
- Attorneys' fees
- Damages at law
- Recovery from third parties
- Return of assets to the fund

Whenever a subcontractor or vendor is unpaid, they should consider utilizing the trust fund statutes. Statutes vary between States and can change through legislative amendment every year. Current legal advice should be obtained from an attorney experienced in trust fund litigation.

### 8.5 Solutions

When funds are diverted, you need to take action against the trustee to recover the money and possibly damages. Consider the following letter which was presented to an EDC-insured vendor on a project in New York State from a general contractor in Seattle, Washington.

> *Dear Vendor:*
>
> *I am writing you to bring you up to date with problems General Contractor, Inc. has been experiencing with the bank that finances our operations through an accounts receivable line of credit.*
>
> *The bank is requiring general Contractor, Inc. to adhere to a strict budget for completion of ongoing projects for which they are willing to advance funds. All other account proceeds are required to be applied against the line of credit, collateralized by the accounts receivables, in order to decrease the loan amount to a point at which the ratios return to conformance.*
>
> *Effectively, they are requiring the loan to be paid prior to any other debt reduction other than debt incurred for current projects. Amounts due on previous completed projects are anticipated to be paid through cash flow and profits generated on current and future projects.*
>
> *We have been negotiating with the bank for approximately three months in order to minimize the impact of this, but the bank has maintained a hard line and has refused to allow use of funds for anything but debt reduction and ongoing project costs.*
>
> *We believe that we have an agreement with the bank that will satisfy the bank for payment on the existing line and allow us to proceed with new projects under a separate line of credit which will allow use of proceeds to satisfy a payment plan for other outstanding debt.*

This general contractor acknowledged it received funds for the project, and that its lending institution directed that the funds received be paid to the lender to satisfy overdue line of credit obligations. The general contractor diverted trust assets by diverting project funds from its vendors and subcontractors to its lender.

The general contractor is now exposed to a civil action suit. The financial damages will be measured by the amount of money diverted which was money belonging to the innocent vendor. An important aspect of trust

fund legislation is that the trust funds are not the property of the general contractor. The funds are actually the property of the beneficiaries.

In some States, if the innocent vendor can establish where the funds were sent, the vendor may petition the Court for relief returning the funds back into the trust for disbursement to beneficiaries. A beneficiary may bring an action against a party, such as a bank, which knowingly receives diverted funds. That third party may be liable to the vendor for receiving diverted funds.

### 8.6 More Powerful Than a Lien

Some States permit a beneficiary to take steps that reach beyond the corporate shield of a trust fund trustee. They permit an action to be commenced directly against the corporate principals, including officers and owners, who knowingly and intentionally participate in a diversion. The corporate form does not protect these individuals from personal liability. Strong public policy reasons encourage the liability of corporate principals and officers who knowingly and willfully participate in the diversion. They have taken money that belongs to another and spent it in violation of the trust.

A diversion of trust assets can be a criminal larceny. A diversion of trust assets can be criminal because the diverting trustee has taken funds which are not its property and applied them for some purpose other than those defined by statute. Depending upon the value of the diverted funds, the larceny may be a felony or a misdemeanor. Some United States District Attorneys and State Attorneys General will prosecute these larcenies. When faced with a trust fund diversion, the unpaid subcontractor or vendor should consider reporting the possible diversion to prosecuting authorities having jurisdiction over the project. Those authorities will typically be a County District Attorney or a State Attorney General.

A diversion can be considered a fraud or defalcation under the United States Bankruptcy Code. That fact brings an increased level of liability to a trust fund trustee. When an individual or entity files bankruptcy, civil actions or lawsuits against the company or person are automatically stayed. The same rule applies to a true trust fund action, except there is an important difference. A trust fund plaintiff may obtain permission from the Bankruptcy Court to continue with its action against the trustee in Bankruptcy Court. This is because the trustee's actions may be a fraud or larceny which is not protected under bankruptcy laws. For example:

> *ABC General Construction received the $95,000 payment. $75,000 of the trust funds were applied to other projects in order to become current with vendors on those other projects. The general contractor diverted $75,000 in trust assets. A beneficiary or a vendor brings an action against ABC in a State Court. ABC files bankruptcy. The beneficiary also commenced an action against the principals of ABC who knowingly and intentionally diverted the trust assets. Those corporate principals have also filed bankruptcy. The beneficiary/vendor may be able to obtain relief from the automatic stay in bankruptcy and maintain an adversary action against both the corporate debtor and the individual debtor.*

Some trust fund States provide yet another powerful tool. An action can be commenced against a trustee for punitive damages, which provides a greater incentive for a trustee to properly manage and disburse trust funds.

### 8.7 Trust Fund Tools

Trust fund statutes may permit an unpaid beneficiary to demand a complete accounting from its trustee. The accounting must be verified under oath, and provide a detailed analysis of all trust fund assets received by the general contractor. The accounting will include a detailed check-by-check analysis of all payments made with trust fund assets. They require that each check be identified, together with the check number, date, payee and payee's address.

Discovery in trust fund litigation should include a complete report from the general contractor's cost accounting system. These are programs where general contractors enter all costs assessed against a project. Cost accounting programs will show labor dollars paid, materials purchased and application of project funds to overhead. Overhead may include a contractor's general conditions such as the project site trailer, site storage facilities, vehicles dedicated to the site and project manager. Remember that a trustee must first apply trust funds for payment of the beneficiaries. A trustee which takes trust assets to pay its overhead or profit may be diverting trust assets. The information contained in a complete job cost accounting report can be beneficial to the subcontractor or vendor. In some instances we have found these reports indicating payment of attorneys' fees with trust fund assets.

# 9. APPENDIX A: GLOSSARY OF TRADE TERMS

International trade carries its own particular terminology. The following are trade terms that new exporters will encounter in published sources and trade discussions.

## 9.1 General Terms

**Anti-dumping Duty:** A special duty imposed to offset the price effect of dumping that has been determined to be materially harmful to domestic producers. (See also Dumping.)

**Counter-Trade:** A general expression meaning the sale or barter of goods on a reciprocal basis. There may also be multilateral transactions involved.

**Countervailing Duties:** Additional duties imposed by an importing country to offset government subsidies in an exporting country, when the subsidized imports cause material injury to domestic industry in the importing country.

**Dumping:** The sale of an imported commodity at a price lower than that at which it is sold within the exporting country. Dumping is considered an actionable trade practice when it disrupts markets and injures producers of competitive products in the importing country. Article VI of the General Agreement on Tariffs and Trade permits the imposition of special anti-dumping duties against dumped goods equal to the difference between their export price and their normal value.

**Export Quotas:** Specific restrictions or ceilings imposed by an exporting country on the value or volume of certain exports designed, for example, to protect domestic producers and consumers from temporary shortages of the goods affected or to bolster their prices in world markets.

**Export Subsidies:** Government payments or other financially quantifiable benefits provided to domestic producers or exporters contingent on the export of their goods and services.

**GDP/GNP (Gross Domestic/National Product):** The total of goods and services produced by a country.

**Subsidy:** An economic benefit granted by a government to producers of goods, often to strengthen their competitive position. The subsidy may be direct (e.g. cash grant) or indirect (e.g. low-interest export credits guaranteed by a government agency).

**Surcharge or Surtax:** A tariff or tax on imports in addition to the existing tariff, often used as a safeguard measure.

**Tariff:** A duty (or tax) levied on goods transported from one customs area to another. Tariffs raise the prices of imported goods, thus making them less competitive within the market of the importing country. Under the North American Free Trade Agreement, most tariffs on Canadian goods and services to the United States and Mexico have been eliminated.

## 9.2 International Commerce (INCO) Terms

Shipping terms set the parameters for international shipments, specify points of origin and destination, outline conditions under which title is transferred from seller to buyer, and determine which party is responsible for shipping costs. They also indicate which party assumes the cost if merchandise is lost or damaged during transit.

**Cost and Freight (C&F):** The exporter pays the costs and freight necessary to get the goods to the named destination. The risk of loss or damage is assumed by the buyer once the goods are loaded at the port of embarkation.

**Cost, Insurance and Freight (CIF):** The exporter pays the cost of goods, cargo and insurance plus all transportation charges to the named port of destination.

**Delivered at Frontier:** The exporter/seller's obligations are met when the goods arrive at the frontier, but before they reach the "customs border" of the importing country named in the sales contract. The expression is commonly used when goods are carried by road or rail.

**Delivered Duty Paid:** This expression puts maximum responsibility on the seller/exporter in terms of delivering the goods, assuming the risk of damage/loss and paying duty. It is at the other extreme from delivered ex works (see below), under which the seller assumes the least responsibility.

**Delivered Ex Quay:** The exporter/seller makes the goods available to the buyer on the quay or wharf at the destination named in the sales contract. There are two types of ex quay contracts in use: ex quay duty paid, whereby the seller incurs the liability to clear the goods for import, and ex quay duties on buyer's account, whereby the buyer assumes the responsibility.

**Delivered Ex Ship:** The exporter/seller must make the goods available to the buyer on board the ship at the location stipulated in the contract. All responsibility/cost for bringing the goods up to this point falls on the seller.

**Delivered Ex Works:** This minimal obligation requires the seller only to make the goods available to the buyer at the seller's premises or factory. The seller is not responsible for loading the goods on the vehicle provided by the buyer, unless otherwise agreed. The buyer bears all responsibility for transporting the goods from the seller's place of business to their destination.

**Ex Works (EXW):** The price quoted applies only at the point of origin and the seller agrees to place the goods at the disposal of the buyer at the specified place on the date or within the period fixed. All other charges are for the account of the buyer.

**Free Alongside Ship (FAS):** The seller quotes a price for the goods that includes charges for delivery of the goods alongside a vessel at the port. The seller handles the cost of unloading and wharfage, loading, ocean transportation, and insurance are left to the buyer.

**Free Carrier.(named port):** Recognizing the requirements of modern transport, including multi-modal transport, this principle is similar to Free on Board (see below), except that the exporter's obligations are met when the goods are delivered into the custody of the carrier at the named port. The risk of loss/damage is transferred to the buyer at this time, and not at the ship's rail. The carrier can be any person contracted to transport the goods by road, sea, air, rail or a combination thereof.

**Free on Board (FOB):** The goods are placed on board the vessel by the seller at the port of shipment specified in the sales contract. The risk of loss or damage is transferred to the buyer when the goods pass the ship's rail.

**Free on Rail and Free on Truck (FOR/FOT):** Again, the same principles apply as in the case of ordinary FOB, except that the goods are transported by rail or road.

### 9.3 Transportation and Delivery Terms

The following are common terms used in packing, labelling, transporting and delivering goods to international markets.

**Area Control List:** A list of countries to which any export (except humanitarian items) requires an export permit.

**Bill of Lading:** A contract prepared by the carrier or the freight forwarder with the owner of the goods. The foreign buyer needs this document to take possession of the goods.

**Certificate of Origin:** A document that certifies the country where the product was made (i.e. its origin). A common export document, a certificate of origin is needed when exporting to many foreign markets. It must be used for Canadian-made goods to qualify for preferential tariff treatment under the North American Free Trade Agreement.

**Commercial Invoice:** A document prepared by the exporter or freight forwarder, and required by the foreign buyer, to prove ownership and arrange for payment to the exporter. It should provide basic information about the transaction, including description of goods, address of shipper and seller as well as delivery and payment terms. In some cases, the commercial invoice is used to assess customs duties.

**Consular Invoice:** A statement issued by a foreign consul in the exporting nation describing the goods purchased. Some foreign governments require Canadian exporters to first obtain consular invoices from their consulate in Canada. A fee is usually charged.

**Customs Declaration:** A document that traditionally accompanies exported goods bearing such information as the nature of the goods, their value, the consignee and their ultimate destination. Required for statistical purposes, it accompanies all controlled goods being **exported under the appropriate permit.**

**Customs Invoice:** A document used to clear goods through customs in the importing country by providing documentary evidence of the value of goods. In some cases, the commercial invoice (see page 53) may be used for this purpose.

**Dock Receipt:** A receipt issued by an ocean carrier to acknowledge receipt of a shipment at the carrier's dock or warehouse facilities. (See also Warehouse Receipt.)

**Ex Factory:** Used in price quotations, an expression referring to the price of goods at the exporter's loading dock.

**Export Control List:** A list of goods and technologies that require export permits to be exported from Canada, pursuant to the Export and Import Permits Act.

**Export Permit:** A legal document that is necessary for the export of goods controlled by the Government of Canada, specifically goods included on the Export Control List (see above) or goods destined for countries on the Area Control List.

**Freight Forwarder:** A service company that handles all aspects of export shipping for a fee.

**Insurance Certificate:** A document prepared by the exporter or freight forwarder to provide evidence that insurance against loss or damage has been obtained for the goods.

**Landed Cost:** The cost of the exported product at the port or point of entry into the foreign market, but before the addition of foreign tariffs, taxes, local packaging/assembly costs and local distributors' margins. Product modifications prior to shipment are included in the landed cost.

**Packing List:** A document prepared by the exporter showing the quantity and type of merchandise being shipped to the foreign customer.

**Pro Forma Invoice:** An invoice prepared by the exporter prior to shipping the goods, informing the buyer of the goods to be sent, their value and other key specifications.

**Quotation:** An offer by the exporter to sell the goods at a stated price and under certain conditions.

**Warehouse Receipt:** A receipt identifying the commodities deposited in a recognized warehouse. A non-negotiable warehouse receipt specifies to whom the deposited goods will be delivered or released. A negotiable receipt states that the commodities will be released to the bearer of the receipt.

### 9.4 Financial and Insurance Terms

The following are the most commonly used terms in international trade financing.

**All Risk:** This is the most comprehensive type of transportation insurance, providing protection against all physical loss or damage from external causes.

**Bid Bond:** When an exporter is bidding on a foreign contract, a bid bond guarantees that the exporter will take the contract if the bid succeeds. An exporter who refuses the contract must pay a penalty equal to the amount of the bond.

**Cash in Advance (Advance Payment):** A foreign customer pays a Canadian exporter prior to actually receiving the exporter's product(s). It is the least-risk form of payment from the exporter's perspective.

**Confirming House:** A company, based in a foreign country, that acts as a foreign buyer's agent and places confirmed orders with Canadian exporters. They guarantee payment to the exporters.

**Consignment:** Delivery of merchandise to the buyer or distributor, whereby the latter agrees to sell it and only then pay the Canadian exporter. The seller retains ownership of the goods until they are sold, but also carries all of the financial burden and risk.

**Document of Title:** A document that provides evidence of entitlement to ownership of goods, e.g. carrier's bill of lading.

**Documentary Collection:** The exporter ships the goods to the foreign buyer without a confirmed letter of credit or any other form of payment guarantee.

**Documentary Credit (sight and term):** A documentary credit calling for a sight draft means the exporter is entitled to receive payment on sight, i.e. upon presenting the draft to the bank. A term documentary credit may allow for payments to be made over terms of 30, 60, or 90 days, or at some specified future date.

**Draft (Bill of Exchange):** A written, unconditional order for payment from one party (the drawer) to another (the drawee). It directs the drawee to pay an indicated amount to the drawer. A sight draft calls for immediate payment. A term draft requires payment over a specified period.

**Export Financing House:** A company that purchases a Canadian exporter's foreign receivables on a non-recourse basis upon presentation of proper documentation. It then organizes export arrangements and provides front-end financing to the foreign buyer.

**Factoring House:** A company that buys export receivables at a discount.

**Letter of Credit:** An instrument issued by a bank on behalf of an importer that guarantees an exporter payment for goods or services, provided the terms of the credit are met.

**Letter of Credit (Confirmed):** A Canadian bank confirms the validity of a letter of credit issued by a foreign bank on behalf of the foreign importer, guaranteeing payment to the Canadian exporter provided that all terms in the document have been met. An unconfirmed letter of credit does not guarantee payment so, if the foreign bank defaults, the Canadian exporter will not be paid. Canadian exporters should accept only confirmed letters of credit as a form of payment.

**Letter of Credit (Irrevocable):** A financial institution agrees to pay an exporter once all terms and conditions of the transaction are met. No terms or conditions can be modified without consent of all parties.

**Open Account:** An arrangement in which goods are shipped to the foreign buyer before the Canadian exporter receives payment.

### 9.5 Partnership, Alliance and Market Entry Terms

The following expressions define the various types of partnership or alliance arrangements as well as methods of market entry common in international trade.

**Agent:** A foreign representative who tries to sell your product in the target market. The agent does not take possession of - and assumes no responsibility for - the goods. Agents are paid on a commission basis.

**Co-marketing:** Carried out on the basis of a fee or percentage of sales, co-marketing is an effective way to take advantage of existing distribution networks and a partner's knowledge of local markets.

**Co-production:** This arrangement involves the joint production of goods, enabling firms to optimize their own skills and resources as well as take advantage of economies of scale.

**Cross-licensing:** In this form of partnership, each firm licenses products or services to the other. It is a relatively straightforward way for companies to share products or expertise.

**Cross-manufacturing:** This is a form of cross-licensing in which companies agree to manufacture each other's products. It can also be combined with co-marketing or co-promotion agreements.

**Distributor (Importer):** A foreign company that agrees to purchase a Canadian exporter's product(s), and then takes responsibility for storing, marketing and selling them.

**Franchise:** This is a more specific form of licensing. The franchise is given the right to use a set of manufacturing or service delivery processes, along with established business systems or trademarks, and to control their use by contractual agreement.

**Joint Venture:** An independent business formed cooperatively by two or more parent firms. This type of partnership is often used to avoid restrictions on foreign ownership and for longer-term arrangements that require joint product development, manufacturing and marketing.

**Licensing:** Although not usually considered to be a form of partnership, licensing can lead to partnerships. In licensing arrangements, a firm sells the rights to use its products or services but retains some control.

**Trading House:** A company specializing in the exporting and importing of goods produced or provided by other companies.

### 9.6 Legal Terms

The following are some of the more common legal terms encountered in international transactions.

**Arbitration:** The process of resolving a dispute or a grievance outside of the court system by presenting it to an impartial third party or panel for a decision that may or may not be binding.

**Contract:** A written or oral agreement which the law will enforce.

**Copyright:** Protection granted to the authors and creators of literary, artistic, dramatic and musical works, and sound recordings.

**Intellectual Property:** A collective term used to refer to new ideas, inventions, designs, writings, films, and so on, protected by copyright, patents and trademarks.

**Patent:** A right that entitles the patent holder, within the country which granted or recognizes the patent, to prevent all others for a set period of time, from using, making or selling the subject matter of the patent.

**Trademark:** A word, logo, shape or design, or type of lettering which reflects the goodwill or customer recognition that companies have in a particular product.

## 10. APPENDIX C: RESOURCE DIRECTORY

Several government agencies exist specifically to help Canadian exporters do business abroad. Among them are:

**Business Development Bank of Canada (BDC):** Provides flexible financing for the development of international markets, R&D, product modifications and new production equipment or technology. http://www.bdc.ca/en/home.htm

**Canadian Commercial Corporation (CCC):** Provides international contracting services to Canadian exporters, as well as special market access to those targeting U.S. public procurement markets. http://geo.international.gc.ca/can-am/main/menu-en.asp

**Canadian Trade Commissioner Service (TCS):** The TCS provides services to Canadian business in Canada and abroad. Services include market research studies and country-specific reports. TCS also provides market prospects, local company and visit information, conducts key-contact searches and arranges face-to-face briefings for Canadian companies that are prepared to do business abroad. The Virtual Trade Commissioner, also available from the TCS, is a personalized, password-protected, Web-based resource that will give you market information and business leads that match your international business interests. Register when you visit the TCS Web site. http://www.infoexport.gc.ca/ie-en/MarketReportsAndServices.jsp

**Export Development Canada (EDC):** Provides finance services for Canadian exporters and investors, particularly small- and medium-size enterprises. It offers a wide range of financing tools to exporters of all sizes, in all sectors. Thousands of exporters use EDC to make sure they get paid or to provide access to the money they need to export more successfully. http://www.edc.ca/english/index.htm

**Foreign Affairs Canada:** Provides information related to foreign affairs, foreign policy, travel assistance, passport services and more. http://www.international.gc.ca/index.aspx

**Industry Canada (Strategies Website):** Provides general and specific information of use to exporters, including market reports and the Trade Data Online research tool. http://www.ic.gc.ca/epic/site/tdo-dcd.nsf/en/Home

**Industry Canada (Sources of Financing Website):** May also help you identify other private or public sources of financing. http://strategis.ic.gc.ca/epic/site/sof-sdf.nsf/en/Home

**International Trade Canada:** Provides information, statistics and analysis related to the Canadian economy and international trade. http://www.international.gc.ca/index.aspx

**Statistics Canada:** Canada's central statistical agency. Produces statistics and statistical reports on Canada's population, resources, economy, society and culture. http://www.statcan.ca/start.html

**U.S. Customs and Border Protection:** For more information general information about and security issues customs issues. http://www.cbp.gov/xp/cgov/import/

**U.S. Department of Homeland Security:** http://www.dhs.gov/index.shtm

**U.S. Department of State's Business Visa Center:** Information on US visa requirements for construction industry personnel at (202) 663-3198 or by email to businessvisa@state.gov ; Website at http://travel.state.gov/visa/temp/types/types_2664.html

**United States Citizen and Immigration Services:** http://www.uscis.gov/portal/site/uscis