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Outsourcing in Canada

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Canada

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Jurisdiction snapshot

Market

What is the extent of outsourcing in your jurisdiction, including the most common sectors for outsourcing activities?

Canadian businesses across various industries routinely outsource business functions. Outsourcing is common in the banking, insurance, retail, mining and telecommunications sectors, among others.

Government approach

How would you describe the government's approach to outsourcing arrangements? Are there any government-sponsored incentives for outsourcing, or restrictions on outsourcing abroad?

In Canada, outsourcing is regulated by both the federal government (based in Ottawa) and by the country's 10 provinces and three territories. Since Canada is a federal state, its legal framework for outsourcing can be somewhat complex as statutes exist at both the federal and provincial level, a consequence of a complex constitutional division of powers in this area that includes certain areas of overlap between the two levels of government. In general, federal and provincial governments favour industry-specific regulation instead of a 'one-size fits all' approach, and there are legal restrictions on outsourcing in certain contexts. Outsourcing abroad has not been as significant a political issue in Canada as it has been in the United States.

Regulation

Legislation

Is there any overarching domestic legislation governing outsourcing?

There are no laws that specifically govern outsourcing in Canada. Under the constitution of Canada, jurisdiction over contract and property law is exercised primarily by the legislatures of the provinces rather than by the federal government, so overarching legislation in this area is unlikely to emerge on a nationwide basis.

Are there any sector-specific laws or industry guidelines on outsourcing?

Several sectors have their own rules and guidelines on outsourcing. Some of the sectors are subject to sector-specific regulation. For example, financial services (eg, banks, insurance companies, trust and loan companies and credit unions/caisse populaires) that are regulated by the federal Office of the Superintendent of Financial Institutions (OSFI) are subject to specific OSFI regulations relating to outsourcing. However, not all such institutions are federally regulated.

The industries below are among those that also have sector-specific legislation:

- aviation;
- consumer credit;
- education and childcare;
- energy;
- food;
- gaming;
- healthcare;
- public services;
- transportation;
- telecommunications; and
- water and sewage.

Licences, permits and approvals

What licences, permits and/or approvals are required for outsourcing activities, if any? What are the penalties for non-compliance with these requirements?

Outsourcing, in general, does not require any specific licences, permits or approvals in Canada. Depending on the industry sector and the specific elements of an outsourcing transaction (eg, will there be a transfer of employees, technology or licences?), various aspects of a transaction may be subject to different licensing, permit or approval regimes, potentially with distinct penalties for non-compliance in each case.

Reforms

Are any legislative or regulatory reforms envisaged or underway which will affect outsourcing arrangements?

The North American Free Trade Agreement, which established a generally tariff-free trading relationship in Canada, the United States and Mexico, has been renegotiated as the United States-Mexico-Canada Agreement (USMCA). It contemplates restrictions on the parties' ability to prevent the movement of data across each other's borders. The current language allows parties to prevent the movement of data across borders to achieve a "legitimate public policy objective", but depending on the interpretation of that provision and the final language of the agreement, the USMCA in its final form may conflict with current legislation that places limitations on outsourcing.

Legal structures

Types available

What legal vehicles/structures are available for outsourcing arrangements, and what are the advantages and disadvantages of each?

Direct outsourcing
In a direct outsourcing arrangement, the customer contracts directly with a supplier. This type of arrangement – which is the most straightforward type of outsourcing – helps the customer to streamline its operations and take advantage of the economies of scale that a large supplier of the outsourced service can offer. Engaging a third party to deal with peripheral aspects of the customer's business allows the customer to focus its resources on enhancing the value delivered by its core business activities. Challenges associated with direct outsourcing vary by sector; in highly regulated industries, for example, customers must take care to ensure that outsourcing arrangements are fully compliant with statutory and regulatory requirements.

Indirect outsourcing
Indirect outsourcing is similar to direct outsourcing. The main difference is that, in an indirect arrangement, the customer appoints a supplier that immediately subcontracts to another entity.

The advantages and disadvantages of indirect outsourcing and direct outsourcing are largely the same. The main difference is that customers may find it more difficult to manage the activities of (and, where necessary, enforce their rights against) the supplier's subcontractor. Nevertheless, there are often efficiency benefits in relying on the supplier to find an appropriate subcontractor.

Multi-sourcing
In a multi-sourcing arrangement, the customer contracts with several suppliers for a range of specific services offered by each. Such arrangements can be thought of as multiple, simultaneous direct outsourcings and therefore offer most of the same advantages and disadvantages as direct outsourcings. In addition, however, they require that the customer ensure that the respective roles and responsibilities of the suppliers are clearly set out, particularly regarding their interactions with one another, in order that the service that they collectively provide is as seamless and efficient as possible and on a collective basis provides all of the services required by the customer. Achieving this can add considerable complexity, and some risk, to an outsourcing. Outsourcing agreements of this type often include provisions obliging suppliers to cooperate with one another and typically require the customer to allocate internal resources for coordination and supervision.

Joint venture or partnership
A customer and a supplier can operate as a joint venture. In Canada, a joint venture can take the form of a business corporation, a partnership or a relationship defined by a contract. In each case, each party to the joint venture makes an appropriate contribution of capital or assets, which is typically technology in the case of outsourcing.

Customers often prefer joint ventures because they allow them a greater degree of control, while at the same time giving them the advantage of direct access to the supplier's knowledge and expertise. Other benefits may include the ability to share in the profits generated by any third-party business the joint venture may conduct and smoother repatriation of the services or transition to a new supplier.

Complexity is one disadvantage of a joint venture arrangement. Like a partnership, a joint venture agreement will generally need to include provisions respecting the formation, governance, financing and dissolution of the entity, in addition to the contributions by the parties and the allocation of profits and losses, among other things.

Wholly owned subsidiary or captive entity

It is also possible for the customer to outsource to its own wholly owned subsidiary. Such an arrangement would obviously give the customer a large measure of control over the outsourced services. Such a structure can also be advantageous from a tax perspective. However, there are also disadvantages, including the cost of establishing a subsidiary with the required assets and the diminution of many of the advantages of outsourcing, such as access to economies of scale and to the expertise of large suppliers – as well as to their willingness to carry certain risks.

Cloud computing
In a cloud computing arrangement, a customer acquires the right to access IT infrastructure and services as required, typically on a subscription basis. Services are provided remotely and the infrastructure is shared with other customers of the service provider. Advantages of this model include the cost savings of not having to buy and maintain equivalent infrastructure, typically paying on an 'as required' or 'per use or user' basis and further savings resulting from the economies of scale achievable by the cloud computing service provider. Disadvantages include the possibility of non-compliance with regulatory requirements in sectors where compliance with regulations tends to require customisation of such infrastructure and, more generally, a lack of customer control, including in connection with how services are provided.

Build, operate and transfer
A customer may enter into an arrangement with a supplier to build and operate a facility that would eventually be transferred by the supplier to the customer. This type of arrangement is costly and includes significant resources to set up but generally involves limited risk for the customer.

Vested outsourcing right
Another option is for the customer to contract for a set of outcomes rather than specifically how services will be provided. The concept behind vested outsourcing arrangements is that the customer will contract for and focus on the achievement of particular goals and will not be prescriptive in specifying the process of achieving those goals. These agreements are fairly novel, focus on the 'what' rather than the 'how' and may be better suited in well-established customer-supplier relationships where an amount of trust has been built on past transactions and interactions.

Vested outsourcing agreements can be very efficient and can allow both the customer and service provider to focus on the outcome as the purpose of the relationship and avoid becoming inundated with process-based decisions. However, these agreements require the customer to give up a great deal of oversight and generally succeed only if there is a significant amount of trust between the parties.

Contractual relations

Contract forms

What are the most common contract forms for outsourcing arrangements, and what are the advantages and disadvantages of each?

The most common form of outsourcing agreement is a master service agreement (MSA). An MSA typically sets out a framework for the main terms, such as payment terms, IP ownership and service levels, and establishes a base of understanding upon which parties can quickly negotiate the future provision of services (generally via a statement of work). MSAs can be tailored to the specific needs of the industry and the outsourcing party and can also provide for flexibility to change the services provided as business needs evolve. Because an MSA is a key document governing the relationship between the customer and supplier, the process of negotiation can be very time-consuming.

As more service providers offer their software on a cloud basis, agreements governing software as a service (SaaS) products are becoming more common. The same concerns generally apply to SaaS agreements as traditional hosted products. While troubleshooting and updates are easier to facilitate with SaaS solutions, there are also inherent security risks with outsourcing physical control of data, and business continuity risks where the reliability and availability of key services are out of the control of the outsourcing party.

Due diligence

Before entering into an outsourcing contract, what due diligence is advised?

Robust due diligence should be conducted on the service provider and on the company outsourcing services. Below is a non-exhaustive list of some key areas for diligence:

- capacity and experience of the service provider and any known material subcontractor;
- data protection and security practices and certifications;
- service levels guarantees;
- price and charging method;

• flexibility regarding volume and type of service; and
• disaster recovery and business continuity plans.

Duration and renewal

What is the common duration of outsourcing contracts? How does the renewal process commonly play out?

In Canada, there are no statutory restrictions on the duration of an outsourcing agreement. Parties are free to negotiate whatever term seems appropriate to them in light of their specific circumstances. Generally speaking, most agreements have a term of between three and 10 years. Typically, the term that is agreed will take into account the amortisation term of the initial investments as well as the complexity and uniqueness of the arrangement. There is often a provision for automatic annual renewal in the absence of a notice of termination and there is usually a provision for a review and examination of charges prior to any such renewal.

Supplier selection

What procedures and criteria are commonly used to select suppliers?

Request for proposal
In a request for proposal (RFP) process, the customer develops a business plan that includes specific objectives, milestones and performance measures relating to the service that is to be outsourced. Depending on the nature of the services and, potentially, internal policies of the customer, the customer may choose to issue RFP variants such as a request for information or a request for quotation. The procurement documents will include a description of the process and the rules that govern it, the contractual terms of the prospective bid, a detailed description of the service requirements and a draft services agreement – basically, all of the information that a service provider would need to make a bid and the customer may need to assess such bid.

In the procurement process, two contracts will be created:

• the bidding contract, which establishes the rules that govern the process itself; and
• the substantive contract between the customer and the winning bidder or bidders.

Outsourcing processes initiated by governments are also informed by trade agreements and guidelines that apply to procurement by governments and quasi-governmental entities.

Invitation to tender
An invitation to tender is sometimes issued in addition to or in place of an RFP.

Service specifications

How are the service specifications agreed and monitored, and what service terms and parameters are commonly applied? Can any flexibility be provided for in these terms?

Service specifications, a key element of outsourcing agreements, can vary from sector to sector and may also be affected by applicable regulations, the confidentiality of the services in question to the customer and the degree to which they have been customised for the customer. Service specifications may also be used to assess if services have been satisfactorily performed.

The way in which service levels are described and monitored often depends on how objectively they can be measured. Service levels such as timing requirements (eg, time limits to respond to or resolve issues) are typically set out in detail in the agreement. More general service warranties are included for services that are less objectively measurable, but realistically these can sometimes be difficult to enforce. It is generally the practice in Canada to build flexibility into service level requirements.

Other things to consider with respect to service levels include:

• that, in longer-term outsourcings, customers will usually require their suppliers to improve service levels over time, on the assumption that it is reasonable to expect suppliers to actively improve their methods and technologies; and
• that it is common to agree to establish governance committees to assess supplier performance on a periodic basis.

Charging methods

What charging methods are commonly used?

Charging methods will vary with the nature of the services being provided, the exclusivity of the relationship and the manner in which risk has been allocated among the parties. In Canada, as elsewhere, there are a number of standard charging methods, including 'fixed price', 'cost plus', 'resource-based charges' and 'time and materials'. It is not uncommon for an agreement to use more than one (or even all) of these methods to price distinct elements of the transaction.

Fixed price
'Fixed price' means just that – the customer pays a predetermined price. This has the advantage of cost certainty for the customer and revenue certainty for the supplier. It is applicable primarily in outsourcings where the volume of the services provided is predictable and non-volatile.

Cost plus
A 'cost plus' method requires the customer to pay the supplier its actual cost of providing the services plus an agreed profit margin. Provisions are generally included to ensure transparency in the assessment and reporting of costs. Indirect costs, such as overhead, are included (typically on an amortised basis) in the actual costs.

Resource-based charges
'Resource-based charges' require the customer to commit to a fixed recurring charge that is calculated on the basis of a projected service volume. To determine the actual charge, the fixed amount is adjusted according to the actual volume of the relevant resource that was actually used in the most recent period.

Time and materials
The customer pays an agreed-upon unit price for specific items of service (eg, volumes of data processed, the hourly rates of applicable resources or deliveries made). The supplier may want to stipulate a minimum fee. This arrangement is often used in situations where the level and volume of services are not predictable.

Other
Complex long-term outsourcings may include mechanisms to ensure that the price paid remains competitive throughout the existence of the agreement. Examples include index-linked increases that adjust for general increases in business costs (eg, use of a consumer price index), benchmarking the supplier's charges against those of specified competitors (this is a time-consuming process that requires parties to agree typically in advance the parameters for such comparisons) and agreements about sharing cost savings from the outsourcing. In addition, the customer will often request a 'disputed fee' mechanism that suspends any obligation on its part to pay a disputed charge while the dispute is being worked out.

Warranties and indemnities

What warranties and indemnities are commonly stipulated in outsourcing contracts (for both the customer and the supplier)? Are there any mandatory or prohibited provisions in this regard?

Warranties
The warranties in a particular outsourcing agreement can depend on the type of transaction, type of services and, realistically, on the relative negotiating positions of the parties. Warranties that are found in most, if not all, Canadian agreements include:

- that the service provider has the capacity to enter into the contract and to perform its obligations;
- that the service provider will fulfil its obligations with reasonable skill and care, in accordance with good industry practice, in a timely and professional manner and in accordance with all applicable laws and regulations;
- that the material information that the service provider provided in the pre-tender and tender stages was and remains complete and accurate; and
- that the service provider has the required permits, licences, certifications and accreditations and operates in a manner consistent with specified quality assurance protocols that apply in the context of the type of services covered by the agreement.

Service providers may also warrant that the services and deliverables do not infringe or violate the IP rights of third parties and that they possess all of the rights that are required to provide the services. However, service providers can sometimes be reluctant to provide this warranty, in which case the customer may still be protected by the indemnity described below if obtained from the supplier.

Several customary warranties are mirrored by customer and supplier, including that they are authorised to enter the agreement and that they will perform their obligations under the agreement.

Sale of goods legislation implies certain conditions and warranties into outsourcing agreements. See, for example, Sections 13 and 15 of Ontario's Sale of Goods Act (RSO 1990, c S.1) (and equivalents in other Canadian provinces), which may imply conditions or warranties relating to the seller's right to sell the goods and to their quality and fitness. Corresponding provisions relating to services generally apply only if the recipients of these services are consumers (ie, individuals acting for personal reasons). Warranties and conditions implied by law can be expressly excluded by contract.

Those involved in outsourcing in Canada should also consider the impact of Canada's treaty obligations. The UN Convention on Contracts for the International Sale of Goods (CISG), for example, pre-empts provincial legislation (other than in Quebec) and may affect certain sales of goods transactions. As a consequence, parties must specifically exclude the applicability of the CISG should they wish:

- the law of a Canadian province to be the governing law of an international sales contract; or
- the specific terms of their agreement to take precedence and govern the transaction involving the sale of goods.

Indemnities
Canadian outsourcing agreements typically contain mutual indemnities with respect to property damage, bodily harm and other losses arising from wilful misconduct or gross negligence, caused by either party. They also typically include certain specific supplier indemnities, under which the customer is indemnified with respect to losses resulting from third-party IP infringement claims, employment-related claims by the supplier's employees and breaches of applicable law or of confidentiality, privacy or security obligations by the supplier.

Ending the agreement

What are acceptable grounds for terminating an outsourcing contract?

In common law jurisdictions, general common law contractual principles such as frustration and mistake may be invoked to terminate or render void a contractual relationship. However, the grounds for the termination of a contract are primarily a matter for negotiation between the parties. Termination rights as negotiated will typically allow either side to terminate in the following situations and under the conditions noted:

- material breach of the contract (on notice to the other party, if the breach is not remedied within the pre-determined cure period or immediately for certain breaches that are deemed egregious and are not capable of being cured, eg, breach of confidentiality obligations);
- consistent breaches of the contract, even if they are individually minor or not material (the type of breach and number of breaches must be defined in the contract);
- insolvency (as defined in the contract; there is no statutory termination right under Canadian insolvency legislation);
- change of control of the supplier; and
- for convenience, on prior notice.

It is important that these termination rights be described clearly in such a way as to avoid potential disputes on the availability or applicability of such termination rights.

How do contracts commonly address exit from the outsourcing contract?

Once an exit is contemplated, contractual provisions providing for termination or post-termination services will generally apply. Such provisions will generally address issues such as IP rights, confidential information and transition support.

Is there a common or mandatory notice period for non-renewal of a contract?

The parties will generally negotiate and agree on notice periods, which are not mandated by Canadian federal or provincial law. Negotiated notice periods tend to be situation-dependent; in cases of egregious breaches (at least where it is possible to do so from a practical perspective), termination without notice is often provided for.

In general, a customer will require an extended notice period in order to repatriate the services or to transition them to another service provider. In such cases, to ensure a smooth transition, the contract would typically contain transition assistance obligations of the supplier that continue either after the notice of termination has been provided or after the termination of the agreement.

General tips

What can customers do to make their outsourcing contract more successful?

To improve outcomes for outsourcing contracts, customers can take a number of steps, including:

- performing internal diligence – this allows the customer to understand its capacity and needs, helping it set clear parameters and specifications for the outsourcing project;
- understanding the business case for the outsourcing – this allows customers to better direct the process and focus on the value drivers of the outsourcing decision in the first place;
- plan internal resource use accordingly – successful outsourcing agreements require the customer to make significant resource commitments internally to monitor and ensure the outsourcing agreement is effectively performing its function; and
- clear governance structure – outsourcing agreements are more likely to succeed if the key personnel within the customer's organisation have a clear understanding of the reporting structure so that decisions can be made quickly.

Remedies and protections

Legal remedies

What legal remedies are available to the parties to an outsourcing contract in the event of contractual breach or unjust termination?

The primary remedies available in the event of a contractual breach (including a termination without cause) are damages, specific performance, injunctive relief and termination (if termination itself was not the breach).

Other remedies

What other remedies are available (eg, contractual)?

In addition to the default legal remedies, outsourcing contracts often provide for the following:

- liquidated damages;
- indemnities for certain kinds of loss;
- a right for the customer to require the supplier to re-perform services that have not been performed to the standard specified by the contract;
- a right for the customer to terminate certain aspects of the services; and
- step-in rights for the customer or a third party to take over the services.

Service level credits can often be effective as a remedial mechanism for minor breaches relating to performance services that occur within the term of the agreement. Service level credits, which incentivise the service provider to meet the agreed-upon service level requirements or other expectations, can be calculated in several ways:

- as a percentage of fees or fixed dollar amount, for any service level failure;
- as a variable percentage or dollar amount, depending on one or more factors (eg, the importance of the service level or the length of the breach); or
- by means of a 'scorecard' mechanism.

In conjunction with the above, 'earnbacks' are also an effective aspect of a service level credit mechanism, allowing a supplier to earn back a service level credit by achieving or surpassing service level requirements in subsequent measurement periods.

Liability

How can the parties to an outsourcing agreement limit or exclude their liability?

Parties to an outsourcing agreement are free to negotiate liability exclusions, although the 'public policy' and 'unconscionability' doctrines may make certain exclusions unenforceable (eg, those purporting to exclude liability for fraud). While exclusions applying to liability for negligence, wilful misconduct or for an intentional breach are not barred on those grounds, explicit wording is usually required in order for them to be effective.

Outsourcing service providers generally want to limit or exclude liability for indirect, consequential, incidental and special damages and for loss of business, profit or revenue where they constitute a direct loss. Customers will generally wish to ensure that they are able to recover, at minimum, all direct losses. If the service provider has the ability to access confidential information of the customer, or if the supplier's intellectual property is key to the provision of service, then the customer will generally try to ensure that the supplier is liable for all damages arising from any breach of the supplier's confidentiality obligations (whether direct, indirect, consequential or incidental and from any alleged infringement of third-party IP rights by the supplier).

Liability caps are also commonly negotiated, subject only to the limitations described above. The cap that is agreed upon in a given situation will generally depend on the parties' assessment of the risks that are inherent to the outsourced business.

Asset transfer and assignment

Movable and immovable property

What rules, standards and procedures govern the transfer and assignment of movable and immovable property in the context of an outsourcing arrangement?

Immovable property
Transfers of titles relating to immovable property (generally, real estate) are required to be in writing and to be registered in the appropriate land registry office. Some Canadian provinces may impose requirements for transferring immovable property, including limitations on foreign ownership in certain circumstances.

Movable property
Ownership of movables (also known as 'chattels' or 'personal property') can generally be transferred by exchanging something of value (ie, common law 'consideration') for possession of the property in question. A bill of sale can be used to evidence the transfer of title. To ensure that a title is free and clear of any liens and has been properly transferred, the parties typically arrange to search for liens in the personal property security registration systems of the relevant Canadian provinces and also under certain federal legislation.

Intellectual property

What rules, standards and procedures govern the transfer and assignment of intellectual property in the context of an outsourcing arrangement?

Transfers and assignments of intellectual property such as patents and copyright (including copyright in a computer program) must be made in writing. Moreover, any transfer of rights in a patent must be registered with the Canadian Intellectual Property Office (CIPO) and may need to meet specific formalities provided in Part I of the Bills of Exchange Act (RSC 1985, c B-4).

Under Canadian law, the author of a work retains 'moral rights' in it for as long as the work is under copyright. Moral rights include rights with respect to the work's integrity and the right to be associated or dissociated from the work, as desired. Moral rights can be waived or bequeathed, but not assigned, under the Copyright Act (RSC 1985, c C-42, ss 14.1 and 14.2).

No special or unique restrictions apply under Canadian law to outsourcing-specific IP transfers. It should nevertheless be noted that an assignment of a patent or copyright licence (including a software licence) may be prohibited by, or require consent under, the terms of the commercial agreement governing the licence. If an outsourcing agreement encompasses a transfer or licence of IP rights, sufficient due diligence should be conducted before the transaction to ensure that any needed consents or additional rights can be obtained in a timely manner.

Rights transfer

How can a customer's rights and obligations under another contract be transferred/ assigned to the supplier?

In general, a master service agreement will require the cooperation of the supplier with other suppliers or service providers of the customer. As a result, any direct transfer or assignment of rights and obligations in respect of those arrangements is not required. In a situation where rights and obligations must be transferred or assigned for the outsourcing, the parties should use a written instrument.

Data protection

Regulation

What rules, standards and procedures govern the protection and transfer of data in the context of an outsourcing arrangement? Are there any sector-specific regulations in this regard? What are the penalties for non-compliance?

Data protection legislation in Canada is composed of, on the one hand, a patchwork of broadly applicable federal and provincial laws and, on the other hand, specific industry regulations. Regulation in this area has distinct public sector and private sector components:

- Public sector – federal, provincial and municipal governmental bodies or other public sector entities (eg, government ministries and agencies; boards and commissions; schools, colleges and universities; libraries; hospitals and other health integration networks) are subject to public sector privacy legislation and regulations. The Office of the Privacy Commissioner of Canada and many of its provincial counterparts have issued guidance on compliance with the public sector legislation, including with respect to data protection, security and freedom of information requests. In addition, personal health information that originates from a health information custodian (defined as entities such as doctors, hospitals and certain quasi-private public operations such as pharmacies and assisted living facilities) can be subject to additional legislation.
- Private sector – in general, Canada's federal Personal Information Protection and Electronic Documents Act (SC 2000, c 5) (PIPEDA) establishes the regulatory framework applicable to data protection and security in the private sector. The main geographical exception is that information transfers occurring entirely within Alberta, British Columbia or Quebec are dealt with by laws in those provinces that are substantially similar to PIPEDA. In contrast, all data transfers that cross provincial borders, or that occur entirely within any of the other provinces, are subject to PIPEDA. Private sector outsourcing service providers may also be subject to public sector privacy requirements in some cases, depending on the status of their customers and on the nature of the data in their possession.

Canadian outsourcing agreements usually include a general undertaking by the parties to comply with all applicable privacy laws. In addition, there are typically confidentiality and data security obligations.

While the relevant data protection regulations do not require compliance with any particular international standard, Canada's federal and provincial privacy legislation is generally consistent with the EU General Data Protection Regulation. The European Commission has recognised that PIPEDA adequately protects personal data transferred from the European Union to Canada without the need for additional safeguards (provided that the data is, in fact, subject to PIPEDA).

When there are allegations that the privacy obligations of an organisation have been breached, the complaints process allows concerns to be raised with, and investigations launched by, the office of the privacy commissioner in an appropriate jurisdiction (either the federal jurisdiction or in one of the provinces, each of which maintains such an office). Individuals can recover damages as a result of an entity's breach of the applicable privacy legislation and the privacy commissioners of Alberta and British Columbia have order-making power.

As of 1 November 2018, private sector organisations that are subject to PIPEDA must notify the Office of the Privacy Commissioner of Canada and any affected individuals in the event of a breach of their security safeguards that creates a real risk of significant harm to the affected individuals. Customers can include by way of contract with applicable suppliers reporting, notification and cooperation obligations that would enable customers to comply with such obligations under PIPEDA.

Employment and labour

Employee transfers

What rules, obligations and liabilities apply to the transfer of employees to and from the customer and supplier (including with regard to offshoring arrangements and termination of the outsourcing contract)?

In Canada, employment and labour matters are primarily regulated by the provinces, with the exception of a small number of federally regulated industries. As a consequence, the evaluation of employment issues arising in an outsourcing will depend on whether the customer and supplier are federally or provincially regulated and, if the latter, in which province the outsourcing will take place. While employment and labour laws can differ significantly between jurisdictions, there are certain circumstances in which employees may be transferred by operation of law.

In general, employees of the customer (both unionised and non-unionised) will not transfer to the supplier by operation of law as a result of an outsourcing agreement. The employment of those individuals remains with the customer. However, if an outsourcing transaction constitutes a 'sale of business' under applicable labour relations legislation, a union's collective bargaining rights could extend to the supplier. In this case, the applicable labour legislation and the terms of the customer's collective agreement will dictate whether the customer's employees are automatically transferred to the supplier or whether they may exercise individual rights to remain with the customer.

In Quebec, an outsourcing agreement that is accompanied by the transfer of the essential elements of the business may entail a transfer of unionised employees to the subcontractor. However, a transfer of duties that is not accompanied by a transfer of the elements which characterise the business will not result in the transfer of the employees to the subcontractor.

Definition of 'employer'

How is 'employer' defined in the context of an outsourcing arrangement, and how does this affect the parties' responsibilities and liabilities?

In an outsourcing arrangement, the supplier should always be defined as the 'employer' for those individuals providing services in relation to the outsourcing arrangement. The customer, after all, does not want to be responsible for the legal obligations as an employer (ie, withholdings, benefits and liability). However, certain provincial employment standards legislation provides protections to temporary or assignment employees. As a result, it is common for the customer to negotiate an indemnity for various employment-related claims by the supplier's employees, such as:

- unpaid payroll taxes;
- employment insurance premiums;
- Canada Pension Plan or Quebec Pension Plan contributions;
- workers' compensation premiums; and
- any other amounts owing to individuals in accordance with applicable employment standards legislation.

Organised labour issues

To what extent are labour unions and works councils involved in outsourcing arrangements?

Collective agreements can be significant factors in outsourcings involving unionised businesses. Canada generally has moderate rates of unionisation outside of the government sector, with considerable variation between industries and among the provinces. Collective agreements may play an important part in determining whether a customer's employees transfer to the supplier or remain with the customer.

Works councils, in the European sense, are not a significant part of the workplace landscape in Canada.

Immigration

What immigration schemes and rules are pertinent in the context of outsourcing arrangements?

In Canada, the primary statute governing immigration is the Immigration and Refugee Protection Act (SC 2001, c 27). Individuals immigrating to Canada in support of an outsourcing agreement must be authorised to work in Canada. Authorisation to work in Canada may be supported by the customer or supplier, depending on the basis for the individual's authorisation to work in Canada.

Tax

Liability

What tax liabilities arise in the context of an outsourcing arrangement? Can these be mitigated in any way?

A transfer of assets to a supplier can give rise to federal and provincial taxes based on the proceeds of the disposition of the assets, the nature of the assets and the cost of the transferred assets. If employees are transferred to a supplier, the supplier is generally responsible for withholding and paying certain payroll taxes from the compensation paid to the employees.

Withholding tax can arise on payments to non-residents in respect of services performed in Canada and non-resident suppliers can be subject to tax if they carry on business in Canada. Tax treaties between Canada and other countries may limit applicable taxes in certain circumstances.

Transfers of assets and the provision of services can also raise sales tax issues. In Canada, there are three main types of sales tax: Provincial Sales Tax (PST), the federal Goods and Services Tax (GST) and an amalgam of PST and GST known as the Harmonised Sales Tax (HST), which apply as follows:

- HST applies only in provinces that have agreed with the federal government to integrate their former PSTs with GST as a single value-added tax (the HST) whose proceeds are divided between the federal government and the province. In those provinces – namely New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario and

Prince Edward Island – HST applies at rates between 13% and 15%, depending on the province.

- In provinces that have not agreed to integrate their PSTs with the federal GST – namely British Columbia, Manitoba, Quebec and Saskatchewan – the two types of tax (GST and PST) are charged separately. GST is always 5% while the provincial PSTs range from 6% to 8%, except in the case of the Quebec Sales Tax (QST), which is 9.975%. While the other PSTs are simple sales taxes, the QST is a value-added tax that applies in a similar manner to the GST and HST.
- In Alberta, the Northwest Territories, Nunavut and Yukon, GST of 5% applies. There is no PST in those jurisdictions.

Note that there are no city or county-level sales taxes in Canada.

Dispute resolution

Common disputes and resolution forms

What are the most common types of dispute arising from an outsourcing agreement and how are they typically resolved? Is alternative dispute resolution (ADR) common and effective?

In Canada, it is common for parties to agree to a staged approach to dispute resolution. Disagreements will initially be referred to the senior management of both parties, followed (if necessary, and if the parties agree) by non-binding efforts to mediate the dispute and then by binding or non-binding arbitration. Otherwise, the parties will have recourse to the courts.

Disputes about IP infringement issues are often carved out from any binding arbitration process that is otherwise accepted by the parties, in order to enable the allegedly injured party to pursue injunctive relief in the courts.

Recent case law

Has there been any notable recent case law which may affect the resolution of outsourcing disputes in future?

Outsourcing disputes rarely reach the courts in Canada. There have been no notable decisions specifically relating to outsourcing in recent years. More broadly speaking, the Supreme Court of Canada ruling in Bhasin v Hrynew, [2014] 3 SCR 494, established a firmer basis for affirming a duty of honesty in the performance of contractual obligations, although subsequent case law in the common law provinces has generally moved cautiously in this area (Quebec's civil law has long recognised a duty of good faith in the performance of contracts).

Law stated date

Correct as of

Please state the date as of which the law stated here is accurate.

1 November 2018.

About Stikeman Elliott

Stikeman Elliott is a global leader in Canadian business law and the first call for businesses working in and with Canada. Our offices are located in Montréal, Toronto, Ottawa, Calgary, Vancouver, New York, London and Sydney. We provide clients with the highest quality counsel, strategic advice, and workable solutions. The firm has an exceptional track record in major U.S. and international locations on multijurisdictional matters and ranks as a top firm in our primary practice areas including mergers and acquisitions, securities, business litigation, banking and finance, competition and foreign investment, tax, restructuring, energy, mining, real estate, project development, employment and labour, and pensions.

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