Transfer Pricing in Canada: 
The Advance Pricing Arrangement (APA) Program

DRTP Transfer Pricing Technical Note
No. 2014-07

Legislation

Since 1997, Canada’s transfer pricing rules have been included in section 247 of the Canadian Income Tax Act (ITA).

The Canadian transfer pricing rules are managed by the Canada Revenue Agency (CRA). In the province of Quebec, the Agence du revenu du Quebec also does transfer pricing compliance audits.

Administrative position

As stated in paragraph 8 of Information Circular IC94-4R International Transfer Pricing: Advance Pricing Arrangements (APAs), the purpose of the Advance Pricing Arrangement (APA) program is “to provide a co-operative process for resolving transfer pricing issues prospectively.”

The APA program is purely administrative in nature. There is no Canadian Income Tax Act provision that enables the creation, management or termination of this program.

An APA is defined as follows in Information Circular IC94-4R:

“An advance pricing arrangement between the Minister of National Revenue and a taxpayer. It covers certain transactions and arrangements between the taxpayer and non-resident entities. APAs confirm appropriate transfer pricing methodologies, in advance, and their application to specific cross-border non-arm's length transactions or arrangements for specified periods of time, under specified terms and conditions, for purposes of the Act. When appropriate, the Canadian competent authority may enter into a BAPA [bilateral APA] or MAPA [multilateral APA] with its foreign counterparts under the mutual agreement procedure article of the relevant income tax treaty, as described below.”
As such, APA may be unilateral [with the CRA only], bilateral or multilateral. For greater tax certainty, a bilateral APA or multilateral APA is obviously better suited than a unilateral APA.

A bilateral APA or a multilateral APA will nonetheless require more efforts from the taxpayer since it involves two or more Competent Authorities in the APA process.

The CRA has stated its preference for bilateral APA and multilateral APA since they both ensure the elimination of double taxation for the years under the APA.

In these cases, the Canadian Competent Authority will share information with the foreign Competent Authority through the mutual exchange of information procedure modelled after article 26 of the OECD Model Tax Convention on Income and on Capital during the APA process.

**Administrative steps**

An APA will relate to current and specific future transactions, not hypothetical transactions.

An APA may apply retroactively to past taxation years provided that the appropriate waivers have been filed by the Canadian taxpayer under subparagraph 152(4)(a)(ii) ITA. However, the non-resident should also take similar actions in its country of origin, as applicable.

As indicated in paragraph 10 of Information Circular IC94-4R, many administrative steps are required:

- Pre-filing meetings;
- APA request by the taxpayer;
- APA submission by the taxpayer;
- Review of the APA submission by the CRA;
- Establishment of a case plan by the CRA;
- Review, analysis, and evaluation by the CRA;
- Negotiations between the Canadian and foreign Competent Authorities;
- APA agreements;
- Post-settlement meeting with the taxpayer; and
- APA compliance.

The APA process is indeed highly procedural in nature. Many detailed and complex steps must be undertaken in order to achieve the main purpose of the program that is, ensuring tax certainty for the Canadian taxpayer in its controlled transaction with related parties.

The pre-filing meeting is attended by the taxpayer, its representative, and CRA officials. It is an opportunity to formally establish the suitability of the APA program for the Canadian taxpayer. An APA request information package must be provided to the CRA at least two weeks prior to the APA pre-filing meeting.
As the APA process moves forward, the CRA will provide the taxpayer with a “levy non-refundable user charge” to cover costs related to travel and accommodation of CRA officials involved in the APA process. However, the CRA will not charge for the time spent on the APA process.

The user charges payable to the CRA are highlighted in the APA acceptance letter, as applicable.

The APA submission must provide a detailed information package which covers the provisions included in paragraph 247(4)(a) ITA and which highlights the impacts of the proposed transfer pricing method, the critical assumptions, and the proposed duration of the APA. An APA submission will therefore discuss in greater details:

- the property or services to which the transaction relates,
- the terms and conditions of the transaction;
- the identity of the participants in the transaction;
- the functions performed, the property used or contributed and the risks assumed;
- the data and methods considered and the analysis performed to determine the transfer prices or the allocations of profits or losses;
- the assumptions, strategies and policies that influenced the determination of the transfer prices or the allocations of profits or losses;
- the impacts of the proposed transfer pricing method;
- the critical assumptions; and
- the proposed duration of the APA.

The CRA usually processes the APA submission in a similar fashion to the transfer pricing compliance audit. As such, case officers will thoroughly review the APA submission package, ask questions, meet with personnel, travel to the taxpayer premises (“site visits”), produce documentation, and ultimately negotiate with the foreign Competent Authority.

In short, the CRA will organize all the work and information requirements regarding the APA process with the Canadian taxpayer representative, the non-resident entity, the APA team, and with the foreign Competent Authority.

An APA is considered as binding on both the CRA and the Canadian taxpayer. It may nonetheless be audited, revised, revoked, or canceled by the CRA. Significant changes to the facts and circumstances which led to the APA would justify such actions, among other possibilities.

The Canadian taxpayer can always withdraw from the APA process or ultimately refuse the APA formally negotiated between the Canadian Competent Authority and the foreign Competent Authority. It may also obtain termination during the APA.
Conclusion

Although the APA program and the transfer pricing audit program are unrelated, an APA can be a good tax risk management tool for Canadian taxpayers.

Considering the upcoming changes related to the Base Erosion and Profit Shifting initiative (BEPS), an APA could provide greater certainty on current and future tax liability. An APA may also have potential use for past taxation years. Moreover, an APA could be useful to manage an actual transfer pricing audit in some instances.

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DRTP Consulting’s services are relevant to any business involved in international commerce. DRTP’s services are also relevant to accounting, legal and other types of firms which provide value to their clients.

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