

Transfer Pricing Country Profile

Name of Country: Canada

Date of profile: February 2009

1	Reference to the Arm's Length Principle	<p>Subsection 247(1) of the Income Tax Act (arm's length transfer price); CRA Information Circular 87-2R International Transfer Pricing; CRA Information Circular 06-1 Income Tax Transfer Pricing and Customs Valuation; Subsection 251(1) of the Income Tax Act (arm's length) ; IT-419R2 Meaning of arm's length.</p>
2	Reference to the OECD Transfer Pricing Guidelines (if any)	<p>CRA Information Circular 87-2R International Transfer Pricing; CRA Information Circular 06-1 Income Tax Transfer Pricing and Customs Valuation; CRA Information Circular 94-4R International Transfer Pricing: Advance Pricing Arrangements.</p>
3	Definition of related parties	<p>Subsection 251(2) of the Income Tax Act defines related persons. Paragraph 251(1)(a) deems that related persons do not deal with each other at arm's length. This is the case regardless of how they actually conduct their mutual business transactions.</p> <p style="padding-left: 40px;">According to paragraph 251(2)(a), individuals connected by blood relationship, marriage, common-law partnership or adoption are related persons. Under paragraph 251(2)(b), a corporation will be related to another person (including another corporation) where:</p> <ul style="list-style-type: none"> (a) that person controls the corporation; (b) that person is a member of a related group that controls the corporation; or (c) that person is a person who is related to a person described in (a) or (b) above. <p style="padding-left: 40px;">In addition, paragraph 251(2)(c) provides that two corporations will be related if:</p> <ul style="list-style-type: none"> (i) the two corporations are controlled by the same person or group of persons; (ii) each of the corporations is controlled by one person and the person who controls one corporation is related to the person who controls the other corporation; (iii) one of the corporations is controlled by one person and that person is related to any member of a related group that controls the other corporation; (iv) one of the corporations is controlled by one person and that person is related to each member of an unrelated group that controls the other corporation; (v) any member of a related group that controls one of the corporations is related to each member of an unrelated group that controls the other corporation; or (vi) each member of an unrelated group that controls one of the corporations is related to at least one member of an unrelated group that controls the other corporation.

4	Transfer Pricing Methods	<p>The transfer pricing methods, in CRA’s Information Circular 87-2R International Transfer Pricing, are:</p> <p>Traditional transaction methods:</p> <ul style="list-style-type: none"> ○ the comparable uncontrolled price (CUP) method; ○ the resale price method; and ○ the cost plus method; <p>and</p> <p>Transactional profit methods:</p> <ul style="list-style-type: none"> ○ the profit split method; and ○ the transactional net margin method (TNMM). <p>CRA’s view is that there is a natural hierarchy in the methods. The traditional transaction methods are preferable to the transactional profit methods; and the transactional profit methods are used as methods of last resort, when the use of traditional transaction methods cannot be reliably applied or cannot be applied at all.</p>
5	Transfer Pricing documentation requirements	<p>Subsection 247(4) of the Income Tax Act details CRA’s contemporaneous documentation as follows:</p> <p>“...a <i>taxpayer</i> or a partnership is deemed not to have made reasonable efforts to determine and use <i>arm’s length transfer prices</i> or <i>arm’s length allocations</i> in respect of a <i>transaction</i> or not to have participated in a <i>transaction</i> that is a <i>qualifying cost contribution arrangement</i>, unless the <i>taxpayer</i> or the partnership, as the case may be,</p> <p>(a) makes or obtains, on or before the <i>taxpayer’s</i> or partnership’s <i>documentation-due date</i> for the <i>taxation year</i> or <i>fiscal period</i>, as the case may be, in which the <i>transaction</i> is entered into, <i>records</i> or documents that provide a description that is complete and accurate in all material respects of</p> <ul style="list-style-type: none"> (i) the <i>property</i> or services to which the <i>transaction</i> relates, (ii) the terms and conditions of the <i>transaction</i> and their relationship, if any, to the terms and conditions of each other <i>transaction</i> entered into between the participants in the <i>transaction</i>, (iii) the identity of the participants in the <i>transaction</i> and their relationship to each other at the time the <i>transaction</i> was entered into, (iv) the functions performed, the <i>property</i> used or contributed and the risks assumed, in respect of the <i>transaction</i>, by the participants in the <i>transaction</i>, (v) the data and methods considered and the analysis performed to determine the <i>transfer prices</i> or the allocations of profits or losses or contributions to costs, as the case may be, in respect of the <i>transaction</i>, and (vi) the assumptions, strategies and policies, if any, that influenced the determination of the <i>transfer prices</i> or the allocations of profits or losses or contributions to costs, as the case may be, in respect of the <i>transaction</i>; <p>(b) for each subsequent <i>taxation year</i> or <i>fiscal period</i>, if any, in which the <i>transaction</i> continues, makes or obtains, on or before the <i>taxpayer’s</i> or partnership’s <i>documentation-due date</i> for that year or period, as the case may be, <i>records</i> or documents that completely and accurately describe each material change in the year or period to the matters referred to in any of subparagraphs (a)(i) to (vi) in respect of the <i>transaction</i>; and</p> <p>(c) provides the <i>records</i> or documents described in paragraphs (a) and (b) to the <i>Minister</i> within 3 <i>months</i> after service, made personally or by registered or certified mail, of a written request therefor.”</p> <p>CRA’s Transfer Pricing Memorandum – 05 provides additional guidance.</p>

6	Specific transfer pricing audit procedures and/or specific transfer pricing penalties	<p>CRA's Information Circular 87-2R International Transfer Pricing provides guidance with respect to the application of the transfer pricing rules in section 247 of the Income Tax Act. CRA also issues Transfer Pricing Memorandums to provide further guidance on specific rules.</p> <p>Subsection 247(3) of the Income Tax Act imposes a penalty equal to 10% of the net result of certain adjustments made under subsection 247(2) of the Act calculated as follows:</p> <ul style="list-style-type: none"> • The total of the transfer pricing income and capital adjustments (upward adjustments, whether there are reasonable efforts or not); minus: • the total of transfer pricing income and capital adjustments for which a taxpayer has made reasonable efforts to determine and use arm's length transfer prices or arm's length allocations (upward adjustments for which there are reasonable efforts); and • the total of transfer pricing income and capital setoff adjustments for which a taxpayer has made reasonable efforts to determine and use arm's length transfer prices or arm's length allocations (downward adjustments for which there are reasonable efforts).
7	Relevant regulations on Advance Pricing Arrangements	CRA Information Circular 94-4R, International Transfer Pricing: Advance Pricing Arrangements (APA); CRA Information Circular 94-4RSR, Special Release - Advance Pricing Arrangements for small business.
8	Link to relevant Government Internet sites	http://www.cra-arc.gc.ca/menu-e.html http://www.cra-arc.gc.ca/tax/nonresidents/menu-e.html http://www.cra-arc.gc.ca/tax/nonresidents/common/trans/
9	Other relevant information	Canadian Income Tax case law CRA Income Tax Rulings CRA Transfer Pricing Memorandums