



Transfer pricing alert

Advance Pricing Arrangement Program Report 2017

July 20, 2018

The Canada Revenue Agency (CRA) recently released its *Advance Pricing Arrangement Program Report 2017*. The report reviews key aspects of and commentary on the CRA's advance pricing arrangement (APA) program for the 2017 calendar year, including program statistics, recent developments and current CRA practices. Highlights of the report are discussed below.

Pre-file meetings

In 2017, the CRA conducted 24 APA pre-file meetings with taxpayers.

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The CRA has averaged 24 pre-file meetings since the 2012-2013 fiscal year, when certain procedural changes were introduced. These changes require taxpayers to submit an information package in advance of being granted a pre-file meeting date, with an increase in the level and detail of information expected of taxpayers when submitting the pre-file package. The CRA had conducted 34 pre-file meetings in the 2011-2012 fiscal year.

Of note, the CRA's Information Circular IC94-4R, *International Transfer Pricing: Advance Pricing Arrangements (APAs)* - which provides taxpayers with comprehensive guidance on APAs and the process of pursuing an APA with the CRA - is being revised to include the above-mentioned changes. More specifically, the forthcoming version will include updated guidance around the pre-filing process, criteria used when accepting/rejecting APA requests, and the roles and responsibilities of taxpayers. Additionally, the updated version of IC94-4R will include updated guidance on APAs that are subject to the arbitration process under Canada's network of tax treaties, most notably the Canada-US tax treaty.

APAs completed and accepted

During 2017, a total of 36 APAs were completed by the CRA. The majority (30) were bilateral agreements with foreign tax administrations. This represents an increase over the 26 APAs completed during the 2016 calendar year and the 21 completed during the 2015 calendar year. It also represents the highest number of APA completions in the last five years.

Additionally, there was an uptick in the number of applications accepted in 2017. The CRA accepted 16 new APAs to the program in 2017, more than the 12 accepted in 2016. However, the number of applications accepted is still relatively low, considering that the last time less than 21 applications were accepted was in the 2011-12 fiscal year, when 17 were accepted. This is primarily the result of an increase in pending applications, from 17 in 2016 to 23 in 2017. Pending applications represent cases where a taxpayer had participated in a pre-file meeting but had not yet been informed of the status of the application under the APA program. Taking into consideration the withdrawal of three taxpayers previously accepted into the program, closing inventory of cases in process was 67 at the end of 2017. This is a significant decline from a closing balance of 90 in 2016, and is the lowest inventory of cases since the 2008-09 fiscal year. This can be attributed to an increased rate of APA completions relative to the decreased rate of APA application acceptances.

At year's end, 88% of cases currently in process were on a bilateral basis, as opposed to just 12% on a unilateral basis. There were no multilateral APAs completed in 2017. However, including multilateral APAs, 85% (or 277) of the 322 successfully concluded cases have involved at least one other foreign tax administration. The United States continues to be the most common jurisdiction involved in APAs in Canada, making up 52% of total APAs in process, a slight decrease from 56% last year.

Completion times up slightly

Average completion time for bilateral APAs during 2017 increased to 48.5 months from acceptance in the program to completion of the APA, up from 47.3

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months in 2016 (which was the lowest since the 2011-12 fiscal year). Similarly, the median time to completion increased to 47.9 months, up from 42.7 in 2016.

By comparison, the average completion time for bilateral APAs in the United States was 46.9 months, with a median time of 50 months¹. Average completion times for bilateral/multilateral APAs in European Union (EU) countries vary significantly – for example, the United Kingdom and France represented a lower average completion time of 25 and 26 months for APAs with non-EU, respectively, while Germany’s average completion time for APAs with non-EU countries is 52 months².

Looking at the three phases of the APA process in Canada, the average time spent on the first phase, due diligence, has dropped to its lowest since the 2012-13 fiscal year at 25.0 months in 2017. The average time spent on the second and third phases, negotiations and post negotiations, were 9.8 months and 13.7 months respectively in 2017.

Predominance of transactions involving tangible property

APAs involving transfers of tangible property remain the most common types of transaction in the APA program, making up 58% of APAs in process at the end of 2017. The balance of cases consisted of APAs involving intangible property and intra-group services, representing 18% and 19% of all cases in process respectively. Financing cases made up the smallest portion of APAs in process, at 4% at the end of 2017.

Transfer pricing methods

The transactional net margin method continued to be the most common transfer pricing method for transactions covered by the APA program, representing 70% of cases in process in 2017. The remaining balance of cases in process was made up of the cost plus (12%), profit split (10%), comparable uncontrolled price/transaction (7%) and resale price (1%) methods. In contrast with representing 19% and 7% of completed APA cases in 2016 respectively, the profit split and resale price methods were not used in any completed cases in 2017.

Participation

The CRA is currently actively engaged in bilateral and/or multilateral APA processes involving taxpayers from 15 different countries. As mentioned previously, the United States remains the most significant jurisdiction for the APA program.

Participation by industry sector generally correlates with the pattern of Canadian trade. Automobile and other transportation equipment, health, computers and electronics, and metals and minerals sectors are all common in the APA program, making up over one-half of all in process APAs.

¹ Internal Revenue Service, [Announcement and Report Concerning Advance Pricing Agreements](#), March 30, 2018, page 12.

² EU Joint Transfer Pricing Forum, [Statistics on APAs in the EU at the End of 2016](#), March 8, 2018, pages 2-4.

Closing remarks

The recent base erosion and profit shifting initiative of the Organisation for Economic Co-operation and Development, and the resulting changes in domestic legislation, will lead to increased global tax controversy in coming years and increased uncertainty around transfer pricing outcomes. As a result, taxpayers may find it advantageous to consider the APA program to achieve certainty and to manage multilateral tax controversy over a period of several years. As the CRA continues to reduce its inventory, there may be willingness and opportunity to accept more cases and continue to reduce completion times of its APAs. The APA program remains an important element in a taxpayer's overall transfer pricing strategy.

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