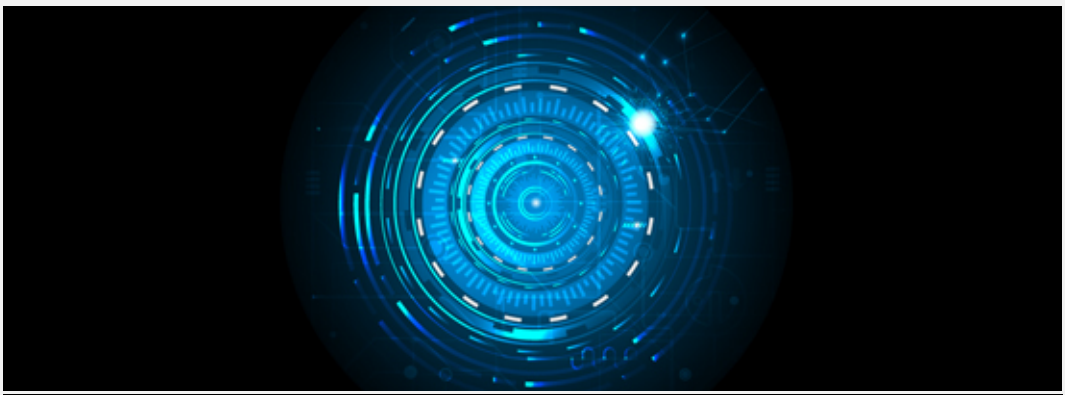

Canada's 2019 budget introduces transfer pricing measures

Global Transfer Pricing Alert 2019-015

Canada's 2019 federal budget, released March 19, proposes two new measures concerning the relationship between the transfer pricing rules in the Income Tax Act (ITA) and other provisions of the ITA. The budget also provides commentary on the ongoing base erosion and profit shifting (BEPS) project.

A summary of the transfer pricing-related measures contained in the budget is provided below.

Transfer pricing measures

The two budget measures related to transfer pricing include the order of application of the transfer pricing rules and the definition of transaction for extended reassessment period.

Order of application of the transfer pricing rules
The government proposes amending the ITA to clarify that the transfer pricing rules in Part XVI.1 (s. 247) should have priority of application over other provisions in the ITA. The budget notes that this change may have various implications and provides an example on the calculation of transfer pricing penalties imposed under Part XVI.1 of the ITA.

The budget notes that the current exceptions to the application of transfer pricing rules that pertain to Canadian resident corporations that have amounts

owing from controlled foreign affiliates, or guarantees of amounts owed by controlled foreign affiliates, will continue to apply.

The order of application measure will apply to taxation periods that begin on or after March 19, 2019.

Definition of transaction for extended reassessment period
The government also proposes to amend the ITA to ensure that the term "transaction" has the same meaning in both the transfer pricing rules and the applicable reassessment rules.

As background, an extended three-year reassessment period applies to reassessments made as a consequence of a transaction involving a taxpayer and a nonresident with whom the taxpayer does not deal at arm's length. The budget notes that this reassessment extension is intended to apply in the transfer pricing context, but that the expanded definition of "transaction" used in the transfer pricing rules does not apply for purposes of the extended reassessment period. As such, the change in definition of transaction for reassessment purposes is intended to better align the transfer pricing rules and the extended three-year reassessment period.

The change to the definition of "transaction" for purposes of the extended reassessment period will apply to taxation periods of taxpayers for which the normal reassessment period ends on or after March 19, 2019.

Update on the BEPS project

The budget reiterates that the Canadian government continues to cooperate and actively participate in the Organisation for Economic Co-operation and Development (OECD) project known as the BEPS initiative.

Multilateral instrument
The budget notes that the Canadian government is taking the necessary steps to enact the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) into Canadian law and to ratify the MLI as needed to bring the tool into force.

Country-by-country reporting
In addition, the budget notes that Canada is currently participating in an OECD review of the information being collected in the country-by-country reports to ensure that they provide tax administrations with information that facilitates accurate assessment for

transfer pricing and other BEPS risks. This review is scheduled to be completed in 2020.

For further details, see the Ministry of Finance's budget website.

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