



Canada Revenue
Agency

Agence du revenu
du Canada

ADVANCE PRICING ARRANGEMENT

PROGRAM REPORT

2017

Competent Authority Services Division

International and Large Business Directorate
International, Large Business and Investigation Branch
Canada Revenue Agency

**[canada.ca/en/revenue-
agency/services/tax/international-non-
residents/competent-authority-services](https://canada.ca/en/revenue-agency/services/tax/international-non-residents/competent-authority-services)**

1. TABLE OF CONTENTS

EXECUTIVE SUMMARY	2
INTRODUCTION	3
BACKGROUND	3
APA PROGRAM: 2017	4
Applications.....	4
Production and Inventory.....	5
Intergovernmental Status	6
Completion Times	6
Intercompany Transactions.....	8
Transfer Pricing Methodologies.....	9
Participation by Industrial Sector.....	10
Participation by Country	10
Participation by Canadian Provinces.....	11
CONCLUSION	11
CONTACTS	12
HOW TO CONTACT THE COMPETENT AUTHORITY SERVICES DIVISION	13

EXECUTIVE SUMMARY

The Canada Revenue Agency's Advance Pricing Arrangement (APA) Program is administered through the CRA's Competent Authority Services Division, which is part of the International and Large Business Directorate, International, Large Business and Investigations Branch.

The APA program is a proactive service offered by the Canada Revenue Agency (CRA) to assist taxpayers in preventing transfer pricing disputes that could otherwise arise in future tax years. The main objective of the program is to provide increased certainty regarding future transfer pricing issues in a manner consistent with the Income Tax Act and guidance delivered through the CRA's information circulars and by the Organisation for Economic Co-operation and Development.

The CRA has published an annual report on its APA program since the 2001 to 2002 fiscal year. Since 2016, the annual report has been based on a calendar year, whereas the previous annual reports were based on a fiscal year. A summary of the key findings presented in this year's report is provided below:

- Based on the number of pre-file meetings held with taxpayers in 2017, the CRA had 24 applicants to the program that year.
- The year 2017 opened with an active case inventory of 90 APAs. Accepted into the program were 16 new cases, 3 cases were withdrawn, and 36 cases were completed. This resulted in a closing inventory of 67 cases for 2017.
- Of all cases in process on December 31, 2017, 88% involve taxpayers seeking an APA on a bilateral or multilateral basis, as opposed to 12% of taxpayers seeking an APA on a unilateral basis.
- The average time to conclude a bilateral APA from acceptance into the program to completion was 48.5 months.
- Cases involving transfers of tangible property made up more than half of APAs in process (58%). Cases involving intangible property represented 19%, intra-group services represented 19% and financing represented 4%.
- The transactional net margin method (TNMM) continued to be the most frequently employed transfer pricing methodology. A TNMM was proposed in 70% of APAs in process.
- APAs involving taxpayers with operations in the automobile and other transportation equipment sector represented 25% of in process APAs at the end of the year. APAs pertaining to the metals and minerals sector were the second most prevalent, representing 12% of the cases in process. APAs pertaining to the petroleum, health, and food and beverages industries each represented 9% of cases in process.
- The composition of bilateral and multilateral APAs continued to reflect the significant flow of goods and services exchanged between Canada and the United States. Although lower than the proportion historically observed, APAs involving the United States represented 52% of APAs in process.

INTRODUCTION

This year's APA report is the 16th of its kind issued by the CRA on the APA program. The report is targeted to taxpayers, tax representatives, and international tax administrations. The key objectives of the report include:

- enhancing awareness of the CRA's APA program
- notifying readers of changes to the APA program
- providing an operational status update
- identifying issues that may affect the APA program in future years

Maintaining the approach of previous publications, this year's report continues to place a heavy emphasis on statistical analysis and quantitative data, with a particular aim of providing insight to the approaches taken by the CRA and its treaty partners on difficult transfer pricing issues.

BACKGROUND

The APA program is delivered through the CRA's Competent Authority Services Division, which is part of the International and Large Business Directorate, in the International, Large Business and Investigations Branch.

The program is a service offered by the CRA to assist taxpayers to prevent prospective transfer pricing disputes. The main objective of the program is to provide increased certainty for transfer pricing methodologies to be applied to future intercompany transfer pricing transactions in a manner consistent with the Income Tax Act, as well as the guidance of the CRA's information circulars and the Organisation for Economic Co-operation and Development (OECD).

The APA process is based on co-operation and transparency with the free flow of information. The APA process differs from the CRA's audit process in that the APA process focuses on prospective or future tax years rather than tax years that have elapsed. In essence, an APA is an arrangement between a taxpayer and a tax administration that sets out an appropriate transfer pricing methodology, to be used on a prospective basis, for establishing a transfer price which is arm's length for the transactions between related parties. The establishment of a transfer price embodies the arm's length principle as described by the OECD's Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and the CRA's Information Circular 87-2, [International Transfer Pricing](#).

An APA process is started by a Canadian taxpayer through contact with the Competent Authority Services Division. For more information on the CRA's APA program, see Information Circular 94-4, [International Transfer Pricing: Advance Pricing Arrangements \(APAs\)](#).

APA PROGRAM: 2017

The following section provides an operational overview of the APA program, along with current trends, issues, and changes to the program. The following topics are addressed below:

- Applications
- Production and program inventory
- Intergovernmental status
- Completion times
- Intercompany transactions
- Transfer pricing methodologies
- Participation by industrial sector
- Participation by country
- Participation by Canadian province

Applications

A taxpayer interested in getting an APA must first send a pre-file package to the director of the Competent Authority Services Division to request an APA pre-file meeting. As much as possible, an APA request-information package should include all the information listed in Appendix I of Information Circular 94-4, [International Transfer Pricing: Advance Pricing Arrangements \(APAs\)](#). The division will review the package and, if satisfied that it is complete, will contact the taxpayer with a possible date(s) for a pre-file meeting.

A pre-file meeting, which take place between a taxpayer and the CRA, provides an opportunity for the taxpayer to learn more about the APA program and for the CRA to get clarification on the taxpayer's business, industry, and most importantly, the requested covered transaction(s). The main objective of the meeting is to explore the suitability of the taxpayer and the proposed covered transaction(s) for the APA program.

After considering the nature of the request, the availability of information, and the taxpayer's willingness to address potential issues identified during or after the pre-file meeting, a decision is then made as to whether or not the taxpayer will be accepted into the next stage of the APA process. A taxpayer invited to continue in the process has to prepare a detailed APA submission outlining the specifics of the covered transaction(s), including a detailed transfer pricing analysis and all pertinent information necessary for the CRA to review and complete its own transfer pricing analysis. After the CRA has received and reviewed the taxpayer's APA submission for completeness, a decision is made to accept or reject the taxpayer's request for an APA.

Although a taxpayer's acceptance into the APA program is not determined at the pre-file stage, the number of pre-file meetings held in a given period can provide a preliminary forecast of future years' inventory. It can also be used to gauge the current level of interest in the CRA's APA program. Historically, the CRA has averaged 24 pre-file meetings annually over the past five years. In 2017, the CRA held a total of 24 pre-file meetings.

Withdrawals from the APA process can occur during the application stage or after an acceptance of application has been granted for the program. By definition, an application withdrawal occurs when a taxpayer formally engages the CRA in an APA pre-file meeting but either chooses not to pursue an APA or is informed by the CRA that the proposed covered transaction(s) are not well suited for the APA program. An APA withdrawal occurs where a taxpayer has provided a detailed APA submission but either is unable to continue in the APA process or is informed by the CRA that they are not suited for the APA program.

To maintain transparency in the program and to ensure applicants can meet the requirements of an APA, the CRA ensures that taxpayers have the necessary feedback on their proposed transfer pricing methodologies and covered transactions. Based on this feedback, a taxpayer may decide not to pursue an APA, while in other cases, the CRA may decide that it would not be appropriate to accept or pursue an APA with a taxpayer. If the CRA declines an APA request, or chooses not to pursue an APA, taxpayers are provided with an explanation for the CRA's decision. As an example, the CRA may decline an APA request when the central issue involves a matter that is before the courts. However, in most cases, taxpayers are given an opportunity to make further representations on any outstanding issues that are preventing their acceptance into the program.

APAs are best suited for current transactions that will likely continue into the future with little to no change, and where the underlying assumptions that form the basis of an APA transfer pricing methodology do not change during the immediate pre-APA period or the APA period itself. Transactions involving one-time events, such as corporate restructurings of a significant nature, are generally outside of the scope of the APA program. Apart from a refusal by the CRA, other reasons why a taxpayer may not pursue an APA include:

- financial constraints
- significant changes in operations, such as a business restructuring
- changes in personnel

In 2017, there were 5 withdrawals from the APA process. Of these, 2 occurred during the application stage and 3 after the applications had been accepted into the program. From an efficiency standpoint, the withdrawal of an APA during the application stage instead of during the post submission stage can represent a significant saving of resources for both taxpayers and tax administrations.

On December 31, 2017, 23 applications were under consideration for acceptance to the program (that is, instances where a pre-file meeting has occurred between the CRA and a taxpayer, but a taxpayer had yet to provide the APA submission).

Production and Inventory

In 2017, 16 new cases were accepted into the program. These new cases are in addition to those cases already reflected as part of inventory from acceptances issued in years past.

Outgoing inventory, which includes APAs completed and withdrawn from the program, totalled 39 cases. Closing inventory at the end of 2017 was 67 cases.

Table 1

Application and Inventory										
Period	Pre-file meetings	Applications withdrawals	Applications pending	Opening APA balance	APAs accepted	APAs completed	APAs unresolved	APA withdrawals	Closing APA balance	Change in inventory from previous period
2017	24	2	23	90	16	36	0	3	67	-23
2016	23	2	17	107	12	26	0	3	90	-17
2015	24	2	8	109	23	21	1	3	107	-2
2015–2016	24	3	10	94	25	24	0	0	95	1
2014–2015	28	1	14	110	22	31	1	6	94	-16
2013–2014	21	8	9	99	39	25	0	3	110	11
2012–2013	24	3	35	102	21	24	0	0	99	-3

Intergovernmental Status

Of the 36 completed APAs in 2017, the majority (30) were bilateral agreements with foreign tax administrations. Since the program's inception, the majority of APAs have been bilateral APAs. Including multilateral APAs, 85% (or 273 cases) of the 322 successfully concluded cases have involved at least one other foreign tax administration. For APAs still in process, 59 (or 88%) of the 67 cases, are bilateral or multilateral. There were no multilateral APAs completed in 2017. It can reasonably be concluded that the CRA and applicants to the APA program continue to be focused on bilateral (or multilateral) arrangements in order to eliminate double-taxation and secure the highest degree of tax certainty.

Completion Times

It is the scope and complexity of a case and not the size of the covered transaction(s) or companies involved, along with other factors such as a taxpayer's co-operation and the availability of necessary quality information, that determine the length of time required to complete an APA. In some instances, cases need much more of the CRA's time and resources because they cover a particularly complex transaction(s), or because the necessary information needed to complete a transfer pricing analysis is limited in scope. Given the relatively small number of cases used to calculate the CRA's APA completion time statistics, the figures presented in the following section may not be representative due to biases resulting from the presence of extreme outliers.

After a case has been accepted into the program, the process that ensues generally requires a substantial investment in time and resources from all stakeholders. Bringing an APA from start to finish is broken down into three distinct stages. These stages are:

- due diligence
- negotiations
- post-negotiations stage

The **due diligence** stage begins once a candidate has been accepted into the program and finishes with the completion of a position paper outlining the CRA's views on the covered transaction(s). Due diligence includes reviewing materials presented by the taxpayer, undertaking site visits, issuing additional queries and/or information requests to permit the CRA to review the APA submission and complete a thorough financial and transfer pricing analysis, and concludes with the formalization of a position for competent authority negotiations.

In the **negotiations stage** (for bilateral and multilateral APAs only), the CRA engages in government-to-government negotiations with the corresponding foreign tax administration in order to establish an agreement on the approach and transfer pricing methodology to be used for the APA term. This can often require more analysis, research, and fact-finding in order to help resolve differences between the CRA's and a foreign tax administration's transfer pricing positions.

The **post-negotiations stage** pertains to the documentation and signing of a bilateral/multilateral understanding between the CRA and a foreign tax administration, and similarly the signing of a corresponding domestic APA between the CRA and the Canadian taxpayer. Depending on the complexity of the transfer pricing methodology agreed to during negotiations, the time needed to finalize an APA can vary from case to case.

Focusing on the 30 bilateral APAs closed in 2017, the CRA needed, on average, 25 months to complete its due diligence and analysis on the covered transactions. An additional 9.8 months were needed for negotiations with the corresponding foreign tax administration. And finally, 13.7 months were needed on average to draft and finalize the bilateral APA agreements. Overall, for cases completed in 2017, an average of 48.5 months was needed to move from acceptance to completion.

The total time to complete an APA does not necessarily equal to the sum of the due diligence, negotiations, and post-negotiations stages. In some instances, cases have been put on hold while the CRA waited for more information from a taxpayer. Instances of this nature generally occur when a taxpayer is reconsidering their suitability for the APA program or cannot provide the necessary information needed for the CRA to undertake a thorough financial and transfer pricing analysis. In other cases, delays are due to the APA program requiring the simultaneous exchange of position papers between tax administrations before starting negotiations. Any such delays are included in the times of completion at the respective stages of the APA process.

Table 2

Completion Times							
Period	Type	Number of Cases	Due Diligence (Months)	Negotiations (Months)	Post-Negotiations (Months)	Average Time: Acceptance to Completion (Months)	Median Time: Acceptance to Completion (Months)
2017	Bilateral/Multilateral	30	25.0	9.8	13.7	48.5	47.9
2016	Bilateral/Multilateral	24	30.2	5.9	11.3	47.3	42.7
2015–16	Bilateral/Multilateral	21	34.3	6.0	12.4	52.7	49.0
2014–15	Bilateral/Multilateral	30	31.5	5.8	11.1	48.4	48.0
2013–14	Bilateral/Multilateral	23	30.0	4.9	13.0	47.8	50.6
2012–13	Bilateral/Multilateral	21	27.9	11.6	12.0	51.5	56.8
Weighted Average		149	29.6	7.3	12.3	49.2	49.3
2017	Unilateral	6	10.0	--	2.5	12.5	12.5
2016	Unilateral	2	18.2	--	5.2	23.3	23.3
2015–16	Unilateral	3	12.2	--	2.9	15.1	15.4
2014–15	Unilateral	1	30.4	--	40.4	70.8	70.8
2013–14	Unilateral	2	31.3	--	14.9	46.2	46.2
2012–13	Unilateral	3	30.6	--	5.3	35.9	26.8
Weighted Average		18	19.3		8.9	28.3	26.8

Intercompany Transactions

Intercompany transactions can broadly be classified into four categories:

- transfer of tangible property
- transfer of rights associated with intangible property
- intra-group services
- financing

The majority of APAs continue to be for the cross-border transfer of tangible property. As of December 31, 2017, this was the breakdown of APAs in process:

- 58% for transfers of tangible property
- 18% for intangible property
- 19% for intra-group services
- 4% for financing

Table 3

	Transaction Type					
	Completed	% of total	In progress	% of total	Total	% of total
Tangible Property	24	67%	39	58%	63	63%
Intangible Property	5	14%	12	19%	17	17%
Intra-Group Services	7	19%	13	19%	20	20%
Financing	0	0%	3	4%	0	0%
	36	100%	67	100%	100	100%

Transfer Pricing Methodologies

The transactional net margin method (TNMM) continues to be the predominant methodology employed in APAs (for 80% of completed cases). At the end of 2017, the TNMM in conjunction with an operating margin profit level indicator (PLI) represented 69% of all completed cases in the APA program. The total cost plus and return on assets profitability indicators are represented in 8% and 3% of all completed cases using the TNMM, respectively.

The profit split methodology was not used in any APAs finalized in 2017 however, at the end of 2017, there were 10% of cases in progress using that methodology. That methodology is commonly used when intangible assets factor into transfer pricing. The use of the profit split methodology reflects the CRA's perspective that where both parties to a transaction are contributing to above normal profits (residual profits), a profit split will often provide a result that is more in keeping with the arm's length principle. The profit split methodology is also often used when the operational characteristics of two non-arm's length parties are highly integrated, making it difficult to identify functions performed, risks undertaken and assets owned by each party. Also, where it is appropriate and possible, all covered transactions involving the licensing of intangible property are first analyzed using the profit split methodology.

The cost plus and comparable uncontrolled price / transaction methodologies were represented in 6% and 14% of completed APAs in 2017.

If an APA is in process and the CRA has yet to finalize its position paper, the methodology reported is the methodology that is proposed by the taxpayer. Following the development of the CRA's position, where an alternative methodology has been selected by the CRA, the alternative approach may be that which is reflected in the statistics. Additionally, statistics reported for the cost plus method include service transactions and cost sharing arrangements.

Table 4

Transfer Pricing Methodology						
Transfer Pricing Methodology	Completed	% of total	In Process	% of total	Total	% of total
Comparable Uncontrolled Price / Transaction	5	14%	4	7%	9	9%
Cost Plus	2	6%	8	12%	10	9%
Resale Price	0	0%	1	1%	1	1%
Transactional Net Margin Method (TNMM) – Total *	29	80%	47	70%	76	74%
<i>PLI – Berry Ratio</i>	0	0%	2	3%	2	2%
<i>PLI – Operating Margin</i>	25	69%	36	54%	61	59%
<i>PLI – Return on Assets</i>	1	3%	2	3%	3	3%
<i>PLI – Total Cost Plus</i>	3	8%	7	10%	10	10%
Profit Split	0	0%	7	10%	7	7%

Participation by Industrial Sector

Participation in the APA program by industrial sector generally reflects the pattern of Canadian trade. More than half of the in-process APA program cases involve taxpayers with operations in the following sectors:

- automobile and other transportation equipment
- health
- computers and electronics
- metals and minerals

Participation by Country

In 2017, the CRA was engaged in bilateral or multilateral APA processes involving taxpayers from 15 different jurisdictions. After the United States, the other tax jurisdictions are United Kingdom, Switzerland, Japan, South Korea, Germany, Netherlands, Ireland, India, Sweden, China, Denmark, Chile, France, and Hong Kong.

The breakdown of bilateral and multilateral APAs by country continues to reflect the significant flow of goods and services exchanged between Canada and the United States. Since the program started, the CRA has completed 202 (or 72%) bilateral APAs with the United States of the 279 successfully completed bilateral APAs. At the end of 2017, there were 55 cases in process involving the United States. At the end of 2017, APAs involving the United States represent 53% of all APAs in process.

Participation by Canadian Provinces

The distribution of APAs across Canada broadly reflects the allocation of Canadian corporate headquarters within the country. Taxpayers located in Ontario represent more than half of all APAs in process, totalling 40 cases or 60%. There are 7 cases or 10% involving taxpayers headquartered in the province of Quebec. Representation from Western Canada (British Columbia, Alberta, Saskatchewan and Manitoba) totalled 19 APAs or 29% of cases. And there is 1 case or 1% of all in-process APAs involving taxpayers located in the Atlantic Provinces.

CONCLUSION

Since its inception in 1990, the APA program has become a key compliance tool for the CRA, while fostering a collaborative and co-operative relationship between taxpayers and other tax administrations. It has also shown that communication, transparency, and compromise permit mutually agreeable resolution of complex transfer pricing issues on a proactive basis. The program provides an opportunity for taxpayers to openly discuss the challenges they face in trying to comply with the tax laws of multiple jurisdictions. Prospective tax certainty provided through the program helps to reduce barriers to trade and contributes to the free flow of capital.

To ensure program efficiency, taxpayers have to provide a pre-file package before being granted a pre-file meeting. The package should include significantly detailed information pertaining to financial statements, business operations, and industry. The information is similar to that which taxpayers have historically been asked to provide during later stages of the APA process.

The CRA is optimistic that increased rigor in the earliest phases of the APA process will reduce the time needed to complete bilateral APAs successfully with Canada's tax treaty partners. The CRA also believes that this focus will help ensure that only taxpayers who are willing to openly work with the CRA will be permitted access to the APA program.

CONTACTS

Cindy Negus

Director

Competent Authority Services Division

Telephone: 613-946-6022

APA Managers

Section 1

Sudha Dukkupati

Manager

Telephone: 613-946-8897

Section 2

Dan Quinn

Manager

Telephone: 613-952-6960

Section 3

Chuck McSpaden

Manager

Telephone: 613-941-9281

Section 4

Brian Busby

Manager

Telephone: 613-946-6169

Technical Cases

Patrick Massicotte

Manager

Telephone: 613-946-6085

HOW TO CONTACT THE COMPETENT AUTHORITY SERVICES DIVISION

If you have comments or questions about this report or the services offered by the Competent Authority Services Division, please contact the division:

- by phone, at one of the numbers listed above
- by fax, at 613-990-7370
- by email, at MAP-APA/PAA-APP.CPB/DGPO@cra-arc.gc.ca
- by post or courier:

Director
Competent Authority Services Division
International and Large Business Directorate
International, Large Business and Investigations Branch
Canada Revenue Agency
8th floor
427 Laurier Avenue West
Ottawa ON K1A 0L5
Canada