

CRA releases revised APA guidance

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On February 21, 2024, the Canada Revenue Agency (CRA) published a revised Information Circular (Circular) on the Advance Pricing Arrangement (APA) program. The APA program offers taxpayers in multinational groups the opportunity to obtain certainty on the transfer pricing of their cross-border transactions with related parties. The changes in the Circular focus on the criteria that taxpayers must meet to be accepted into the APA program (generally requiring more information at the pre-filing stage) and how the CRA evaluates whether taxpayers and transactions are eligible for an APA to obtain certainty on their transfer pricing arrangements for future taxation years (and any rollback period).

Taxpayers seeking to address or prevent transfer pricing disputes have the option to pursue bilateral and multilateral remedies through the “competent authority” process available under Canada’s tax treaty network. This process includes mechanisms such as a Mutual Agreement Procedure (MAP), which resolves transfer pricing disputes for past years, and an APA, which offers taxpayers the opportunity to obtain certainty on their transfer pricing arrangements in advance. By proactively engaging in the APA process, taxpayers can mitigate the risk of future transfer pricing disputes and ensure compliance.

[Information Circular \(IC\) 94-4R2](#) replaces Information Circular 94-4R, issued March 16, 2001, and Information Circular 94-4RSR (Special Release), issued March 18, 2005, for small businesses. The Circular marks the first time the CRA’s APA guidance has been substantially rewritten in more than 20 years. During this period, the Competent Authority Services Division of the CRA (CASD) has developed and refined its practices. The incorporation of these evolving practices into the Circular reflects a trend in CASD’s administration of these programs to restrict, rather than expand, access, and to increase compliance burdens. This trend is unfortunate, particularly as Canada’s transfer pricing landscape is potentially changing with the proposed amendments in the [Transfer Pricing Consultation Paper](#) released on June 6, 2023.

The CRA has been consulting privately on the APA program and circulated a draft of the Circular to certain stakeholders last June. The Tax Executives Institute (TEI) provided [comments](#) on the draft Circular, raising concerns about undue compliance burdens, unreasonable filing deadlines, and additional requirements for renewing APAs. Many of these issues remain in the final version of the Circular published on February 21, 2024, although efforts appear to have been made to attenuate some of the concerns raised during the consultation.

The Circular introduces some significant changes to the written guidance on the APA

process, especially at the pre-filing stage. Taxpayers who wish to apply for an APA will now have to provide more detailed information upfront, such as a functional analysis, a description of the proposed transfer pricing methodology (TPM), and a preliminary economic analysis. CASD will use this information to assess the suitability of the APA request and to determine whether to accept the taxpayer into the program. These changes front-end-load the taxpayer burden.

The Circular includes a list of possible reasons why CASD may decide not to proceed with an APA request. These reasons include

- the CRA has concerns that the transactions involve tax avoidance or BEPS
- the business recently underwent (before the APA term) or is expected to undergo (during the APA term) a significant transformation
- aspects of the transactions are not expected to stay consistent (for reasons other than inflation or significant changes in the economic environment)
- the business has not been carried on long enough to complete an economic analysis of taxation years for which tax returns have been filed
- the taxpayer chooses not to include all cross-border intragroup transactions in their request without sufficient reasons, or where CASD believes they should be included and the taxpayer disagrees
- the legal contracts are not aligned with the “actual conduct” of the parties
- there is current litigation involving the transaction for past years
- the transaction requires a determination that does not involve a treaty article
- the taxpayer is seeking a permanent establishment (PE) determination under a treaty or the request requires allocation of profits to a PE under specific circumstances
- the transactions involve a business restructuring, shifting or eliminating functions, selling or transferring assets, closing plants or allocating extraordinary gains and losses (which may be one time in nature)
- for transactions involving intangibles, the ownership and development of the intangibles is unclear, there is no business purpose for holding the intangibles in a specific entity or jurisdiction, or the intangibles are hard to value

The CRA has indicated that these reasons are not exhaustive, and that each APA request will be evaluated on a case-by-case basis.

In the final version of the Circular, CRA removed two additional reasons for rejection into the APA program that had been included in the draft Circular. These were scenarios where (i) CASD and the taxpayer disagree on the selection of the most appropriate transfer pricing methodology (TPM) or (ii) the request is for a transaction that has not yet taken place, is hypothetical or is one-time in nature. The deletion of disagreement on the TPM is a welcome revision as it acknowledges that it is common at the outset of the APA process for there to be disagreement about the selection of the most appropriate TPM (including between CASD and the competent authority of the other jurisdiction).

The final version of the Circular also includes more qualifying language when introducing the list of common reasons why CASD may determine that a taxpayer is not suitable for the APA program. The Circular also notes that, if CRA decides not to proceed after the pre-filing meeting stage, the taxpayer will be given reasons in writing for the decision. The provision of such reasons is welcome, including because they would be relevant in a potential judicial review.

One ongoing judicial review proceeding in respect of the APA program (Court File No. T-1816-23) involves Dow Chemical Canada ULC, which is challenging CASD's refusal to accept its request for an APA with respect to certain transactions with its Swiss affiliate. CASD rejected the APA request on the grounds that it involved a post-restructuring transaction. Based on the notice of application for judicial review, it appears that the taxpayer had restructured the pricing of the relevant transactions, rather than the business itself, as the application asserts that the taxpayer changed its TPM after determining that a Canadian member was being compensated for functions it did not perform. Dow's application has not been heard by the Federal Court. A decision on this proceeding would mark the first time a Canadian court has weighed in on taxpayers' ability to access the APA program, or the sufficiency of reasons for being rejected from the program.

The Circular also addresses other aspects of the APA process, such as the roles and responsibilities of the APA team and the taxpayer, the annual reporting requirements, and the renewal and revision procedures. The Circular continues to contemplate both bilateral (BAPA) and multilateral (MAPA) APAs, and states that the CRA prefers these to unilateral APAs between a taxpayer and the CRA. While the draft Circular had strictly limited the possibility of unilateral APAs to a narrow list of circumstances, the final Circular, possibly in response to concerns expressed by TEI and other stakeholders, describes these circumstances merely as examples of circumstances in which a unilateral APA may be appropriate despite the CRA's preference for BAPAs and MAPAs.

Finally, the process for renewing existing APAs will be more burdensome under the revised guidance, which now requires a full submission in the pre-file stage and potentially a complete process at CASD's discretion. Although concerns had also been expressed about this aspect of the draft guidance, it remains unchanged in the final Circular.

In a rapidly changing international tax landscape, taxpayers are increasingly motivated to ensure compliance and avoid disputes by obtaining advance certainty regarding intercompany transfer pricing. Although the revised administrative guidance in the Circular improves modestly upon the more restrictive statements in the draft circulated last year, it continues to set a high threshold for taxpayers seeking to access that certainty through the APA program. We are nonetheless hopeful that the CRA will administer the program in a manner that reflects its potential, as noted in the Circular's introductory language, for taxpayers to "work in collaboration with the CRA and other tax administration on a constructive and co-operative basis", "openly discuss the challenges they face in trying to comply with transfer pricing requirements" and, critically, "reduce barriers to trade and investment".