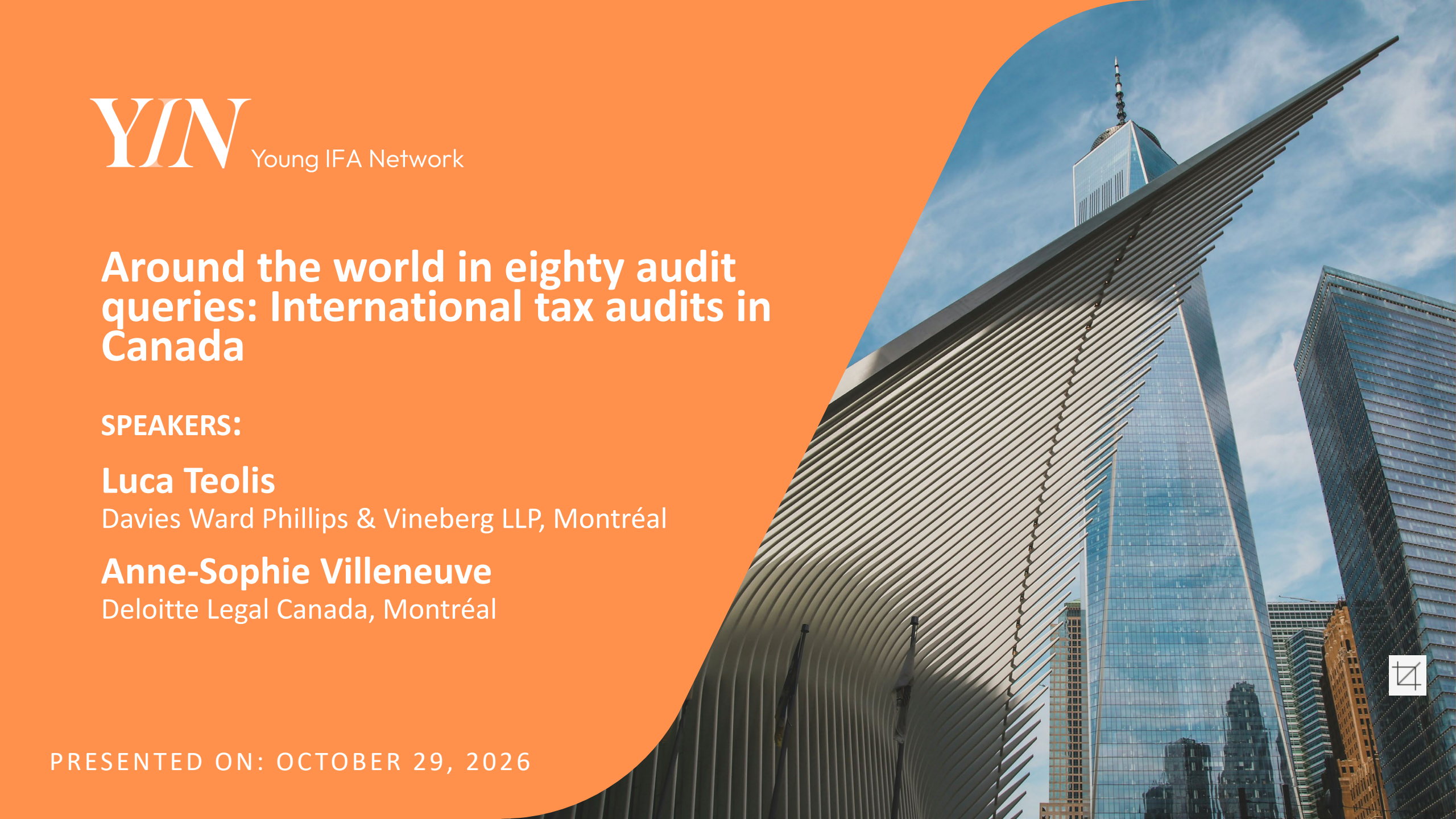
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Around the world in eighty audit queries: International tax audits in Canada



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PRESENTATION OUTLINE

- Transfer pricing update
  - Transfer pricing overview
  - MAP process
  - APA and BAPA processes
  - New transfer pricing rules
- Information requests and international exchanges of information
- International collection mechanisms & issues



1. TRANSFER PRICING UPDATE

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TRANSFER PRICING OVERVIEW

- Transfer pricing rules are outlined in section 247 of the *Income Tax Act (*ITA).
- The purpose of the rules is to ensure that transactions between Canadian-resident corporations and non-arm's-length non-resident entities are entered into on an arm's-length basis.
- The arm's-length transfer price is determined with reference to comparable transactions entered into between arm's length parties.
- Guidelines of the Organization for Economic Co-operation and Development (OECD) must also be considered.

MUTUAL AGREEMENT PROCEDURE (MAP)

- A MAP is a dispute resolution mechanism that allows authorized Canada Revenue Agency (CRA) officials to interact with foreign tax administrations to resolve issues of double taxation and taxation not in accordance with a convention.
- The Competent Authority Services Division (CASD) within the CRA is responsible for the MAP in Canada.
- Residents of either country can request assistance under the MAP to resolve an issue and request relief under their convention.
- Can be an alternative to litigation (objection and appeal).
- Confidential proceeding.

SITUATIONS WHERE A MAP MAY BE AVAILABLE

- Where a Canadian taxpayer is subject to additional tax because of a CRA adjustment in respect of a transaction with a related party in a treaty country, the taxpayer may request a corresponding adjustment for the related party in the treaty country.
- Where a Canadian-resident taxpayer is also considered resident in a treaty country.
- Where a taxpayer in a treaty country is subject to additional tax due to an adjustment in respect of a transaction with a related party in Canada, the Canadian taxpayer could request a corresponding deduction in Canada.
- Where a branch of a Canadian resident taxpayer operating in a treaty country is subject to additional tax due to an adjustment by that country of the income allocated to the branch, the Canadian taxpayer could request an increased foreign tax credit in Canada.

SITUATIONS WHERE A MAP MAY BE AVAILABLE

- Where a Canadian taxpayer subject to tax in Canada on worldwide income, including income from carrying on a business in a treaty country, is taxed in that country on the business income earned there despite not having a permanent establishment.
- Where tax is withheld by a treaty country on a payment to a Canadian resident at a rate exceeding the rate stated in the applicable treaty.
- Where there is uncertainty as to whether a treaty covers an item of income arising in another jurisdiction, the CASD could provide clarification.

MAKING A MAP REQUEST

- Where a request is made to the CASD, the CASD will first attempt to resolve the situation unilaterally, if the relief requested is entirely within the scope of Canadian tax laws
  - If the CASD is not in a position to resolve the situation unilaterally, it will do so by mutual agreement with the foreign authority
- Most MAP requests are bilateral, but a taxpayer may request a multilateral MAP (involving more than two jurisdictions).
- A MAP request must be initiated by written application, within the applicable time limit specified in the treaty.

MAPs AND THE AUDIT AND APPEALS PROCESSES

- The CASD does not have authority over cases where an audit is pending or in process.
- Taxpayers can file an objection and keep it in abeyance during the MAP process, to protect their right of appeal to the Tax Court and keep the year open for reassessment.
- Waivers of objection or appeal rights granted as part of the settlement of an audit or objections process do not prevent taxpayers from seeking relief from double taxation under the MAP.
- Taxpayers can resume a MAP or submit a MAP request if double taxation remains after an objection or appeal.

NEGOTIATION OF THE MAP

- The MAP is negotiated between the Canadian competent authority and the foreign competent authority.
- Taxpayer involvement in the process is minimal:
  - Taxpayers can present their views and assist in providing and understanding the facts.
- Where a MAP request is accepted regarding a CRA adjustment, the CASD will prepare a position paper to be exchanged with the foreign competent authority.
- Where the adjustment is made by a foreign authority, CASD will request a position paper from the foreign competent authority.

MAP IMPACT ON COLLECTIONS, INTERESTS AND PENALTIES

- The CASD operates independently from Collections.
- Acceptance of a MAP request does not depend on compliance with CRA collections policies.
- A MAP request does not suspend CRA collection actions or the requirement to pay the tax and interest.
- Treaties do not cover interest and penalties assessed as a result of an adjustment to an international transaction.
- The CASD cannot waive or negotiate interest and penalties as part of a MAP request.

ACCELERATED COMPETENT AUTHORITY PROCEDURE (ACAP)

- An ACAP allows for the application of a MAP settlement to taxation years that are in the preliminary stages of an audit, or which could be considered for audit review.
- An ACAP request must be included with a MAP request or made before the conclusion of MAP negotiations.
- Both competent authorities must accept the ACAP request for it be considered as part of the MAP.
- An ACAP will not preclude the CRA's right to examine a taxpayer's books and records or to address issues covered by the ACAP.

ADVANCE PRICING ARRANGEMENTS (APA)

- An APA is a prospective agreement establishing how certain cross-border transactions between related parties will be priced for Canadian tax purposes, and which transfer pricing methods will be applied.
- APAs can be:
  - unilateral (between the taxpayer and the CRA)
  - bilateral (between the taxpayer, the CRA and a foreign tax administration)
  - multilateral (involving more than one foreign tax administration)
- The purpose of an APA is to provide taxpayers with certainty with respect to their transactions with non-arm's-length non-residents, and to prevent costly audits and treaty disputes.
- APAs can also be rolled back to prior taxation years.

CONDITIONS FOR ELIGIBILITY TO AN APA

- Taxpayers may be eligible to apply for an APA if:
  - they are subject to the transfer pricing rules in section 247 ITA;
  - they carry on business through a permanent establishment in Canada or in a treaty jurisdiction;
  - they are party to other international transactions with related parties.
- The CRA is most likely to enter into an APA with respect to cross-border transactions that:
  - are recurring and well documented;
  - for which the parties' functions, assets, risks, legal arrangements, and business conditions are stable;
  - are supported by an appropriate transfer pricing method.

CHALLENGES OF PURSUING AN APA

- Lengthy and resource-intensive process:
  - An APA requires an economic analysis, contracts, comparables and responses to CRA information requests. Site visits and functional interviews may be conducted.
- Foreign authority coordination:
  - A bilateral APA requires agreement between the competent authorities; the CRA does not control the foreign authority's resources, position or timetable.
- Ongoing compliance:
  - Consistent application of the agreed method, annual APA reports and disclosure of material changes. A failed critical assumption may lead to revision or cancellation.

TIMING OF APAs AND IMPACT ON INTEREST

- No statutory deadline:
  - The CRA is not required to conclude an APA within a set time; timing depends on complexity, information quality and, for a bilateral APA, the foreign competent authority.
- The CRA reported, in 2024, an average completion time of:
  - 40.8 months for bilateral APAs
  - 36.8 months for unilateral APAs
- Exposure while the APA is pending:
  - An APA request does not suspend an audit, collection action or the accrual of arrears interest.

NEW TRANSFER PRICING RULES

- Bill C-15 received Royal Assent on March 26, 2026. The revised rules apply to taxation years and fiscal periods beginning after November 4, 2025.
- The focus moves from the legal form of the arrangement to the substance of the transaction.
  - This means that the parties' actual conduct and the economically relevant characteristics are analyzed.
- The contractual terms remain relevant to the extent they are consistent with the actual conduct.

FORMER VERSUS REVISED SECTION 247

- Adjustment rule:
  - Former section 247 had separate rules for pricing adjustments and recharacterization; revised section 247 uses a single adjustment rule.
- Recharacterization:
  - The *bona fide* non-tax purpose test is removed; arm's-length conditions may contemplate a different transaction or no transaction at all.
- OECD Guidelines:
  - The OECD guidelines were formerly persuasive but not binding. Section 247 must now be interpreted to best achieve consistency with the OECD Guidelines.

IMPACT OF NEW TRANSFER PRICING RULES ON AUDITS

- Contemporaneous documentation must be prepared by the documentation due date and updated for material changes.
- The taxpayer has 30 days to provide documentation following a written CRA request (formerly three months).
- If the taxpayer fails to comply with the request, it is deemed not to have made reasonable efforts for the purpose of the subsection 247(3) penalty.
  - The penalty is 10% of the amount by which the net adjustment exceeds the lesser of 10% of gross revenue and $10 million (formerly $5 million).

2. INFORMATION REQUESTS AND INTERNATIONAL EXCHANGES OF INFORMATION

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THREE WAYS TO EXCHANGE INFORMATION

- **On request**
  - For a specific case.
- **Spontaneous**
  - A State shares information it believes is of interest to another State.
- **Automatic**
  - Under a pre-established protocol.

ON REQUEST - BILATERAL TAX TREATIES

- **Framework:** OECD Model Tax Convention on Income and on Capital
  - 94 bilateral treaties in force in Canada (per Finance Canada).
  - Aim: avoid double taxation and prevent tax evasion.
- **Purpose of the information:**
  - Must serve to apply the treaty or domestic tax law.
- **Standard:** "foreseeable relevance" (OECD Model since 2005)
  - No "fishing expeditions".
  - No requests for information unlikely to be relevant.
- **Caution:**
  - The relevance standard could vary (e.g., "necessity" or "relevance").

ON REQUEST - BILATERAL TAX TREATIES

LIMITS:

- **Exhaustion:** the requesting State must first use all usual domestic sources.
- **Confidentiality:** the information must be treated as confidential.
- **Reciprocity:** no State must go beyond its own laws or administrative practice, nor provide information the requesting State could not itself obtain.
- **Trade secrets and privileged information:** may be refused.

ON REQUEST - TAX INFORMATION EXCHANGE AGREEMENTS (TIEAs)

- **Framework:**
  - OECD Model Agreement on Exchange of Information on Tax Matters.
- **Scope:**
  - States with no bilateral tax treaty with Canada, mainly low- or no-tax jurisdictions.
  - 24 TIEAs in force (per Finance Canada).
- **Main Differences with OECD Model Tax Convention:**
  - Applies only to the taxes listed by the parties (usually income tax).
  - The requesting State must provide specific information to establish foreseeable relevance.

ON REQUEST - MULTILATERAL CONVENTION

- **Convention on Mutual Administrative Assistance in Tax Matters**
  - Covers all forms of administrative cooperation in assessment and collection.
  - Applies to all taxes except customs duties, unless a party opts out.
  - Canada signed in 2004 and ratified in November 2013.
- **Reach:**
  - 152 signatory States (other than Canada).
- **Arts. 4 and 5 – exchanges on request:**
  - Same "foreseeable relevance" standard.
  - The requested State must take "all necessary measures": broadly worded, leaving it more latitude.

ON REQUEST – RELEVANT CASELAW

- *Canada as requesting state*
  - *Rémillard v. Canada (National Revenue)*, 2022 FC 338
  - *Levett v. Canada (Attorney General)*, 2022 FCA 117
- *Canada as requested state*
  - *Blue Bridge Trust Company Inc. v. Canada (National Revenue)*, 2021 FCA 62
  - *Canada (National Revenue) v. Shopify Inc.,* 2025 FC 968
- *Domestic application*
  - *Canada (National Revenue) v. Zeifmans LLP*, 2026 FCA 147
  - *Canada (National Revenue) v. Liang*, 2026 FC 1102
  - *Canada (National Revenue) v. Chad*, 2024 FC 460
  - *Canada (National Revenue) v. Schreiber*, 2024 FC 729

ON REQUEST - CANADA AS THE REQUESTING STATE

RÉMILLARD v. CANADA, 2022 FC 338

- **Context:**
  - CRA residency audit (2013–2017) of a Quebec businessman claiming to have emigrated to Barbados.
  - Information exchange requests sent via JITSIC to the U.S., Switzerland and Barbados (2019).
- **Foreseeable relevance:**
  - Assessed primarily by the requesting State, presumed to act in good faith.
  - "Reasonable possibility" the information will be relevant; for residency, "everything is relevant".
- **Exhaustion:**
  - "All reasonable means", not all available means.
  - Five T-997 requests sufficed; no section 231.2 requirement or section 231.7 order needed first.

ON REQUEST - CANADA AS THE REQUESTED STATE

Blue Bridge Trust Company Inc. v. Canada (National Revenue), 2021 FCA 62

- **Context:**
  - France requested information from Canada under article 26 of the Canada – France Tax Convention on French residents under audit. The CRA issued requests for information under subsection 231.2(1) ITA to the Canadian trustee.
- **Standard:**
  - Information must be "foreseeably relevant"; article 26 aims to encourage exchange to the maximum extent possible.
- **Limited CRA review:**
  - No duty to thoroughly analyze the requesting State's facts and law; treaty-compliance concerns are left for the MAP stage.
- **Outcome:**
  - The FCA upheld the subsection 231.7(1) compliance order requiring the trustee to produce settlor information, balance sheets and asset inventories.

SPONTANEOUS EXCHANGES

- **OECD Model Tax Convention on Income and on Capital**
- **OECD Model Agreement on Exchange of Information on Tax Matters**
- **Multilateral Convention**
  - Article 7
  - Exchanges occur notably where:
    - A State has grounds for supposing a loss of tax in the other State.
    - A tax reduction or exemption in one State would increase tax in another.
    - A State has grounds for supposing artificial profit shifting within groups of enterprises that reduces tax.

AUTOMATIC EXCHANGES

- **OECD Model Tax Convention on Income and on Capital**
- **OECD Model Agreement on Exchange of Information on Tax Matters**
- **Multilateral Convention**
  - Article 6: possibility to make agreements regarding automatic exchanges.
- **FATCA (U.S. law):**
  - Automatic exchanges with the U.S.
  - Part XVIII ITA (since July 1, 2014): financial institutions identify and report accounts held by U.S. persons or U.S.-owned entities.
- **Common Reporting Standard (CRS):**
  - Developed by the OECD at the G20's request (2014).
  - Multilateral Competent Authority Agreement.
  - Reported: account holder identity and date of birth, account and institution numbers, year-end balance, interest, dividends and other income.
  - Part XIX ITA (since July 1, 2017);Canada exchanging since 2018.

AUTOMATIC EXCHANGES

- **Country-by-Country Reporting:**
  - OECD Base Erosion and Profit Shifting (BEPS) project, also under the Multilateral Competent Authority Agreement.
  - Section 233.8 ITA (2016): ultimate parent entity of an MNE group with consolidated revenue over €750 million.
  - Reports, by jurisdiction: revenue, profit, tax paid, capital, retained earnings, employees, tangible assets and main activities.
  - First exchanges in June 2018; about 70 participating countries.
- **No relevance standard for automatic exchanges:**
  - Information need not relate to a specific audit or to applying tax laws.
  - Used upstream, for risk assessment and audit selection; otherwise stored in databases.

OTHER CANADIAN INITIATIVES

- **JITSIC (OECD Forum on Tax Administration):**
  - Forum on effective ways to counter tax avoidance.
  - Focus on high net-worth individuals.
- **Joint Chiefs of Global Tax Enforcement (J5):**
  - Canada, Australia, Netherlands, U.K. and U.S. (since 2018).
  - Joint criminal investigations and intelligence sharing: tax crimes, money laundering, cybercrime.

3. INTERNATIONAL COLLECTION MECHANISMS AND ISSUES

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THE REVENUE RULE

- **Principle:**
  - Courts will not enforce, directly or indirectly, the tax laws of another State.
  - Adopted in Canada: *United States of America v. Harden*, [1963] S.C.R. 366.
- **Rationale:**
  - Tax collection is an exercise of sovereign power that stops at the border.
  - A long-standing rule, described in *Harden* as enforced for some 200 years.
- **Practical result:**
  - Absent a treaty, a foreign tax authority cannot sue in Canada to recover a tax debt, and the CRA cannot do so abroad.
- **Scope:**
  - Covers direct and indirect enforcement.

TREATY COLLECTION ASSISTANCE

- **Multilateral Convention:**
  - Canada is a party but reserved on the collection-assistance provisions.
  - Canada prefers to negotiate collection assistance bilaterally.
- **Bilateral treaties:**
  - Exception to the revenue rule.
  - The foreign tax claim is treated as a Canadian tax debt.
  - Constitutionality upheld: *Chua v. M.N.R.*, [2001] 1 F.C. 608.
- **Canadian treaties with collection assistance:**
  - U.S. (since 1995), Netherlands (1997), Germany (2001), Norway (2002), United Kingdom and Spain (2014), New Zealand.

WHICH TAX CLAIMS ARE COVERED?

- **Broad scope:**
  - Generally, taxes of every kind.
  - "Tax" is defined by the law of each State.
- **On the Canadian side, the claim must be collected by or on behalf of Canada:**
  - Federal income tax, Goods and Services Tax and provincial taxes collected by the CRA.
  - Québec taxes collected by Revenu Québec are generally excluded.
- **Finality:**
  - The claim must be finally determined for collection purposes.

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