



Memorandum D13-4-5

Ottawa, September 17, 2015

Transaction Value Method for Related Persons

In Brief

1. This memorandum has been reviewed in order to provide more information on the use of international transfer prices in the value for duty calculation.
2. This memorandum now includes information from the former Memorandum D13-3-6, *Income Tax Transfer Pricing and Customs Valuation*, relevant to the application of the transaction value method.
3. This memorandum also explains the Canada Border Services Agency's new policy on the treatment of downward transfer price adjustments.

This memorandum explains the treatment of sales between related persons by the Canada Border Services Agency (CBSA) in determining the value for duty of imported goods under the transaction value method (section 48 of the [Customs Act](#)).

Legislation

Sections 45 and 48 of the [Customs Act](#)

[Valuation for Duty Regulations](#)

[Imported Goods Records Regulations](#)

Guidelines and General Information

1. The definition of “related persons” is contained in subsection 45(3) of the [Customs Act](#) (the Act). For more information, refer to [Memorandum D13-3-2, Related Persons](#).
2. The primary method of valuation for imported goods is the transaction value method (refer to [Memorandum D13-4-1, Transaction Value Method of Valuation](#)). In order to apply the transaction value method, the goods must have been sold for export to Canada to a purchaser in Canada, and the price paid or payable can be determined. [The Act](#) also provides for prescribed additions and deductions to the price paid or payable.
3. If any one of the requirements of the transaction value method is not met, the CBSA will require that the value for duty of imported goods be established using an alternate valuation method.
4. The transaction value method cannot be used when the price paid or payable for goods is influenced by the relationship between the vendor and the purchaser. Paragraph 48(1)(d) of [the Act](#) provides two options for establishing the acceptability of the transaction value:
 - (a) by examining the circumstances surrounding the sale to determine whether the relationship influenced the price; or
 - (b) by the importer demonstrating that the price closely approximates a “test value”.
5. In other words, the importer must satisfy themselves that the relationship between the vendor and the purchaser had no effect on the selling price of the goods. To do so, the importer must examine how the price was determined between the related parties and maintain evidence to support their decision to use the transaction value method.

The object of the self-examination is to establish that the selling price is not significantly different from the price that would have been charged to an unrelated purchaser, given otherwise identical circumstances.

Circumstances Surrounding the Sale

6. Neither [the Act](#) nor the [international customs valuation agreement](#) adopted by the World Trade Organization (WTO), upon which the valuation provisions of the Act are based, detail the information to be used in establishing that a relationship has not influenced the price in a sale of goods for export. Regardless of how an importer chooses to establish the acceptability of the price, the importer's conclusion that the price is acceptable should be supported by factual evidence. For example, showing that the price is adequate to ensure recovery of all costs plus a profit which is representative of the firm's overall profit realized over a representative period of time in sales of goods of the same class or kind, would demonstrate that the price had not been influenced.
7. The CBSA accepts the transaction value method in most importations involving sales between related persons. It is also expected that importers will be able to assure themselves more easily and more often of the acceptability of prices between related persons than they would be able to demonstrate that the transaction value closely approximates a test value.
8. A transfer price agreement submitted by the importer may be a good source of information if it contains relevant information about the circumstances surrounding the sale. A transfer price (i.e., a price charged for the goods by the related entity) is an acceptable starting point for determining the value for duty of imported goods.
9. The Organisation for Economic Co-operation and Development (OECD) sets out several methods of pricing goods in order to achieve a price which could reasonably have been expected in similar circumstances had the vendor and the purchaser not been related. The CBSA will accept a price paid or payable which is derived from one of the methods set out by the OECD, unless there is information on prices available which is more directly related to the specific importations.
10. The following methods are other examples of ways of establishing that a price is not influenced by the relationship. It must be emphasized that this list does not contain all of the possible methods of establishing the acceptability of prices between related companies, and it is not the CBSA's intention to be restrictive in this regard:
 - (a) The vendor has sales to unrelated customers in Canada who purchase under basically the same conditions or under conditions that are different from those pertaining to the related purchaser in the sale for export to Canada. Differences in price can be justified by these differences in conditions. For example, the related purchaser is at the distributor level of trade, but the unrelated Canadian customers are at the retail level and buy in smaller quantities than the related purchaser. In this example, the importer could provide evidence to show that, although the vendor's price to the retailers is higher, the difference is accounted for by economies realized by the vendor in dispatch costs, larger production runs, selling costs, overhead costs, etc. Note that it would be necessary for the importer to obtain this evidence from the vendor;
 - (b) The vendor does not sell to unrelated purchasers in Canada and the goods sold are of types that have recognized prices established by the workings of the free market economy, e.g., commodities such as copper, zinc or sugar. The importer is able to show that information on pricing is available and that the published prices are those at which the importer did, and any other person could, buy the subject goods;
 - (c) In the event that the vendor sells only to related purchasers, the importer may be able to show that a genuine bargaining process occurs and the selling price has been established by the arm's length principle. This principle requires that related parties negotiate their transactions with each other as if they were unrelated parties, each acting in its own interest. This will normally be revealed by evidence that prices originally proposed by the related person in the position to dictate terms are adjusted as a result of the bargaining process, and that a reasonable sharing of total profits results; and
 - (d) Other methods may have to be used to meet special conditions, e.g., a sale to a related manufacturer in Canada of semi-finished products where the vendor's entire output is sold to related purchasers. It may be necessary to establish the reasonableness of the selling price by examining the level of profit of each of the related parties in relation to factors such as the capital employed, the relative risk undertaken, the effort exerted or expenses incurred, or the use of industry norms for net yield expectations.

11. In examining the effect of any differences in conditions of sale, an importer should take into consideration the factors set out in section 3 of the [Valuation for Duty Regulations](#). For example, where a related purchaser must bear the cost of advertising and warranty repairs which unrelated purchasers are not responsible for, it is reasonable to expect that the vendor will reduce the unit selling price to the related purchaser by the full unit cost of the advertising and warranty expense which the vendor does not now incur.

Test Values

12. [The Act](#) provides for a second approach that establishes the acceptability of a transaction value in a sale between related persons. In this approach, described fully in subsection 48(3) of the Act and section 3 of the [Valuation for Duty Regulations](#), the importer has an opportunity to demonstrate that the price closely approximates one of the following test values:

- (a) the transaction value of identical goods or similar goods in a sale of those goods for export to Canada between a vendor and a purchaser who are not related to each other at the time of the sale;
- (b) the deductive value of identical goods or similar goods; or
- (c) the computed value of identical goods or similar goods.

13. In order to use one of the values referred to in subsection 48(3) of [the Act](#) as a test, that value must meet two criteria:

- (a) the goods to which the test value relates must be exported at the same or substantially the same time as the goods being appraised; and
- (b) the test value used must be the value for duty of the goods to which it relates.

14. Generally, the expression “exported at the same or substantially the same time” will be taken to mean a period beginning 30 days prior to and extending to 30 days following the date of export of the goods being appraised. However, for certain transactions, such as seasonal fruit or vegetables where values fluctuate frequently, it may be appropriate to narrow the time period mentioned above. On the other hand, for certain types of goods, such as machinery or durable goods, the period of time may need to be extended.

15. The decision as to whether a difference between the transaction value of the goods being appraised and the test value is commercially significant will be made after all other relevant factors and differences, including those set out in section 3 of the [Valuation for Duty Regulations](#), have been taken into account. An assessment of the commercial significance of a difference in values would take into account that market conditions and pricing practices may vary from industry to industry. However, as a guide to importers, differences in values of 5% or less of the transaction value of the goods being appraised will not normally be considered to be “commercially significant.”

16. A difference in value greater than 5% need not preclude the acceptance of a transaction value provided the importer can demonstrate that such a difference is not commercially significant.

17. When an importer successfully demonstrates that the transaction value closely approximates a test value previously accepted by the CBSA in another importation, it is not necessary to examine the circumstances surrounding the sale of the goods being appraised.

18. The importer who uses a transfer price as the basis for the transaction value and who satisfies themselves of the acceptability of that price must retain on file the information justifying their conclusion. This information may be examined by the CBSA at any time in accordance with the [Imported Goods Records Regulations](#).

19. If the CBSA performs a review of information and evidence provided by the importer and others, and believes that the relationship has influenced the price paid or payable for the goods, the importer will, in all cases, be notified in writing of the grounds for such belief. The importer will be given ample opportunity to rebut the CBSA’s conclusion and will be allowed to submit additional information in support of the original declaration regarding the acceptability of the purchase price.

Transfer Price Adjustments

20. When a transfer price agreement between a vendor and a related purchaser exists in writing and is in effect at time of importation, the transfer price is considered by the CBSA to be the “uninfluenced” price paid or payable for imported goods.
21. For the price to remain uninfluenced, payments made to the vendor and/or adjustments to the price after importation must be declared to the CBSA.
22. There are different types of adjustments that may be made to a transfer price. For example, a compensating adjustment occurs when the actual transfer price is adjusted in order to be compliant with the terms and conditions of the agreement. This involves the price being recorded in the accounts of the importer and a debit or credit note being issued to the importer depending on whether the adjustment is upward or downward. This may occur throughout the year, at year end, or after year end.
23. Corrections to the declared value for duty must be submitted to the CBSA when the net total of upward and downward transfer price adjustments occurring in a fiscal period is identified. It is at that moment that an importer has specific information giving reason to believe that corrections to declarations of value for duty are necessary.
24. If the net total result is an upward price adjustment, a correction under the authority of section 32.2 of [the Act](#) is necessary whether or not the imported goods are subject to duties.
25. If the net total result is a downward price adjustment, a correction made under the authority of section 32.2 of [the Act](#) is necessary if the correction would be revenue neutral. If the imported goods are subject to duties, a request for refund under the authority of section 74 of the Act can be made.
26. For example, the transfer price of goods purchased by a Canadian subsidiary from its foreign parent in a fiscal period was adjusted as follows:
- (a) January to March (Q1), upward adjustment of \$10,000 (payment from the Canadian importer to the foreign parent company);
 - (b) April to June (Q2), upward adjustment of \$20,000;
 - (c) July to September (Q3), downward adjustment of \$10,000 (credit note received from the parent company);
 - (d) October to December (Q4), upward adjustment of \$30,000;
 - (e) Last adjustment to close the fiscal period (“Q5”), downward adjustment of \$10,000; and
 - (f) Net total of upward and downward adjustments: $(10,000+20,000+30,000)-(10,000+10,000) = +\$40,000$.
- Note:** The net total amount (\$40,000) must be included in the value for duty. If any other adjustments to the price paid or payable were made after importation (for example, selling commissions, design fees, etc.), these amounts must also be included in the value for duty of those goods. For more information on importer self-adjustment obligations, refer to [Memorandum D11-6-6, “Reason to Believe” and Self-adjustments to Declarations of Origin, Tariff Classification, and Value for Duty](#).
27. Paragraph 48(5)(c) of [the Act](#) precludes a decrease in the price paid or payable when a price reduction is effected after importation. Paragraph 48(5)(c) of the Act does not apply to any adjustment to a transfer price that occurs after importation but that results from an agreement that is in writing and in effect at the time the goods are imported to Canada.
28. The CBSA will examine any payment made directly or indirectly by the purchaser to or for the benefit of the vendor, or payment based on subsequent resale, disposal, or use of imported goods that accrues to the vendor, to verify whether the payment relates to reasonable identifiable services and whether that payment would normally be included in the selling price of a transaction between unrelated parties. All amounts not relating to reasonable identifiable services will be included in the value for duty of the goods. For more information on the treatment of payments or fees made after importation, refer to [Memorandum D13-4-3, Customs Valuation: Price Paid or Payable](#), and [Memorandum D13-4-13, Post-importation Payments or Fees \(Subsequent Proceeds\)](#).

Agreements

29. There are different kinds of written agreements between related parties. The process for establishing the related party price may be reflected in a transfer price agreement, study, report, or advance pricing arrangement (APA). The CBSA will not preclude the use of a transfer price as the basis of the price paid or payable if the agreement is not signed. However, the importer must demonstrate with corroborating evidence that the agreement existed and was in effect at the time of importation, and the value for duty was based on that agreement.

30. An APA is an agreement between the taxpayer and the Canada Revenue Agency (CRA). An APA stipulates a mutually acceptable transfer pricing method to be used on specified international transactions for a future period. There are various types of APAs, categorized by the number of parties involved (unilateral, bilateral or multilateral).

31. The CBSA will accept a transfer price established through an APA as the price paid or payable of imported goods and the basis for their value for duty, but may require that a correction to the value for duty be made if compensating adjustments are made to the transfer price.

Additional Information

32. For more information on transfer pricing for income tax purposes, contact the CRA.

33. For more information, within Canada call the Border Information Service at **1-800-461-9999**. From outside Canada call 204-983-3500 or 506-636-5064. Long distance charges will apply. Agents are available Monday to Friday (08:00 – 16:00 local time / except holidays). TTY is also available within Canada: **1-866-335-3237**.

References	
Issuing Office	Trade and Anti-dumping Programs Directorate
Headquarters File	79070-4-4
Legislative References	<i>Customs Act</i> <i>Valuation for Duty Regulations</i> <i>Imported Goods Records Regulations</i>
Other References	D11-6-6 , D13-3-2 , D13-4-1 , D13-4-3 , D13-4-13 International customs valuation agreement Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations issued by the Organization for Economic Co-operation and Development
Superseded Memorandum D	D13-4-5 dated November 20, 2013