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SUBJECT: Advance Pricing Arrangements for Small Businesses

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## Application

The information contained herein is applicable after the official publication date. This document supplements Information Circular 94-4R, *International Transfer Pricing: Advance Pricing Arrangements (APAs)*, dated March 16, 2001.

## Summary

1. Key elements of the Small Business APA Program (the "Program") can be summarized as follows:
  - The CRA's Competent Authority Services Division (CASD) will administer the Program.
  - The Program will have a fixed non-refundable administrative fee of \$5,000.
  - Taxpayers must have gross revenues of less than \$50 million or a proposed covered transaction of less than \$10 million to be considered for the Program.
  - The Program will only cover transactions of tangible goods (which have not been bundled with non-routine intangibles) and routine services.
  - Site visits will not be performed. The only material we require the taxpayers to submit is a functional analysis.

- Only requests for a unilateral APA, without rollback, will be accepted into the Program.
- Annual reporting under the Program will be limited to stating, in writing, whether the critical assumptions have or have not been breached.

## Purpose

2. The purpose of this special release is to introduce special procedures for small business taxpayers to improve access to the CRA's Advance Pricing Arrangement (APA) Program. The APA Program is a service provided by the CRA that confirms the appropriate transfer pricing methodology to establish an arm's length price for cross-border transactions between persons that do not deal at arm's length. If the facts presented by the CRA in determining the transfer price are accurate, the taxpayer gains domestic certainty on the tax treatment of these non-arm's length transactions. An APA may be used to cover these transactions for a period of up to five years. As the taxpayer and the CRA gain comfort with the issue through the Small Business APA Program, the taxpayer may wish to renew the arrangement as a bilateral APA under the traditional APA Program.

## Background

3. Since the APA Program was introduced in July 1993, the majority of cases have addressed transfer pricing issues for large multinational corporations. However, the CRA has received a number of requests to make the APA Program more accessible to a broader group of taxpayers with non-arm's length transactions. These taxpayers contend that they have been unintentionally screened out of the APA Program for the following reasons:

- the demand for information and company time may exceed the capability of a small business to comply; and
- the fees charged by both the CRA and external advisors to pursue the APA process may be too high given the small size of the business.

To address these issues, the CRA has implemented the procedures outlined in this special release.

## Who can apply for a Small Business APA?

4. The APA Program is an administrative service offered by the CRA. The CASD will consider all requests for a Small Business APA provided the following two conditions for acceptance are satisfied:

- the taxpayer has, in the most recent taxation year prior to the request, gross revenues of less than \$50 million or, if above that threshold, proposes that the APA cover a non-arm's length transaction in a taxation year of less (or expected to be less) than \$10 million<sup>1</sup>; and
- the taxpayer proposes to cover a non-arm's length transaction that involves either the purchase/sale of tangible goods or the provision/receipt of routine services (i.e., the program will not address transfers of non-routine intangible property, tangible goods bundled with non-routine intangibles, or complex financial transactions).

If it is determined during the APA process that:

- the taxpayer's revenues or the dollar amount of the transaction, for the most recent taxation year prior to the request, exceeded the applicable threshold, thus causing the proposed transactions to fail the first condition, or
- the proposed transactions are not accurately characterized as routine in nature, thus failing to meet the second condition,

the CRA will not proceed further with the Small Business APA. Depending on the circumstances, the taxpayer can ask the CRA to restart the APA process following the procedures of the traditional APA Program or the taxpayer can withdraw its APA request.

## What are the main differences between the traditional APA Program and the Small Business APA Program?

5. To address the particular concerns of small business taxpayers, the CRA has adopted a number of procedures that are designed to reduce the time and cost of the APA process. Taxpayers applying for the Small Business APA Program must accept these procedures in their entirety and cannot opt out of one or more procedures in favour of the approach taken under the traditional APA Program.

### *Small Business APAs will not have site visits*

6. Under the traditional APA Program, APA site visits are routinely undertaken as part of the CRA's due diligence prior to establishing its position on a transfer pricing issue. Under the Small Business APA Program, site visits will not take place at all. If the taxpayer is selected for audit by the Tax Services Office (TSO), the facts relevant to the

transactions covered by the Small Business APA will be verified. Any concerns the TSO has regarding the proposed or finalized APA will be fully discussed with CASD staff prior to any action being taken. If the CRA determines that there has been a material omission or misrepresentation in the statement of relevant facts submitted by the taxpayer or the taxpayer's authorized representative, the CRA has the right to revoke the APA.

### *Small Business APAs only require a functional analysis*

7. Under the traditional APA Program, the CRA asks taxpayers to provide both a functional and an economic analysis. Under the Small Business APA Program, the CRA only requires a functional analysis. If the taxpayer has existing transfer pricing documentation which contains a complete and accurate functional analysis for the proposed covered transactions, the CRA will accept this documentation as the functional analysis for the Small Business APA request. A functional analysis must contain the records or documents listed under paragraph 247(4)(a) of the *Income Tax Act*, except for subparagraph 247(4)(a)(v) "data and methods considered."<sup>2</sup> The CRA will then perform an economic analysis based on the functional analysis provided by the taxpayer as well as responses to supplemental questions. The economic analysis determines an arm's length price for the transactions based on the most reliable data available. As part of the Small Business APA Program, taxpayers may still choose to prepare an economic analysis and may elect to submit this material to the CRA. However, the CRA will base its conclusion on its own economic analysis. The CRA will present its conclusion in draft format to the taxpayer for comment and will modify its conclusion when persuaded by factual evidence. This should not be misconstrued as a negotiation process as the CRA does not negotiate APAs with taxpayers.

### *Small Business APAs will be unilateral and without rollback*

8. Under the traditional APA Program, a taxpayer is encouraged to request a bilateral APA and may also request a rollback of the results to prior taxation years. Under the Small

<sup>1</sup> The gross revenue and transaction thresholds will be based on the taxpayer's reported prices for the most recent taxation year prior to the request and not the prices that may ultimately be determined to be at arm's length. A taxpayer can request that the APA cover multiple transactions of dissimilar products or services provided that the threshold is met for each transaction.

<sup>2</sup> For greater clarity, the taxpayer does not need to provide the information suggested in sections V and VI of the APA Submission Checklist (IC94-4R Appendix IV). The functional analysis should contain information about the proposed covered transaction, including: an organizational structure depicting the transaction flows/entities involved; the terms and conditions of the transaction; the functions performed, property used or contributed, and risks assumed by the entities involved in the transaction; the assumptions, strategies, and policies in respect of the transaction; detailed financial data for the most recent three fiscal years for the relevant entities; a history of the business; the names of direct competitors; industry background information (including critical success factors); as well as a description of transactions with unrelated parties that the CRA could potentially consider to be comparable. Please refer to paragraphs 1.20 to 1.27 and 5.16 to 5.27 of the *OECD Transfer Pricing Guidelines for Multinational Enterprises* for further information on the type of information to include in a functional analysis.

Business APA Program, the taxpayer can only request a unilateral APA and will not have the option of requesting a rollback. This policy is intended to reduce the time and cost of completing the taxpayer's APA request, and to preclude the possibility of the APA leading to unresolved double taxation in a rollback year. Should any taxation authority reassess a transaction covered by the Small Business APA, taxpayers will maintain any right to seek relief from double taxation pursuant to the pertinent provisions of the relevant bilateral Income Tax Convention.

***Small Business APAs will have a reduced cost recovery amount***

9. Under the traditional APA Program, the taxpayer agrees to cover CRA expenses for APA-related travel. Under the Small Business APA Program, there will be no site visit and no travel is required for Competent Authority negotiations as the process will be unilateral. A fixed administrative fee of \$5,000 is charged by the CRA for this Program and is to be paid when the taxpayer makes its official Small Business APA request. Once the Small Business APA request has been accepted by the CRA, the administrative fee is non-refundable.

***Small Business APAs will have a reduced reporting requirement***

10. Under the traditional APA Program, taxpayers are required to file an annual report describing the taxpayer's compliance with the terms and conditions of the arrangement. Under the Small Business APA Program, the administrative burden of preparing an annual report will be greatly reduced. All that will be required is an annual statement saying that the critical assumptions have been reviewed for the APA year and that they have or have not been breached.

## **Electronic Transmission of Information**

11. To further expedite the Small Business APA process, taxpayers and/or their authorized representatives may send their APA request and all subsequent correspondence electronically, together with an authorization for the CRA to electronically transmit correspondence related to the Small Business APA. A standard authorization for email and facsimile transmissions is included in the Appendix.

## **Time Frame for Completion**

12. The goal of the Small Business APA Program is to conclude an APA within one year of the date of receipt of the request. Every effort will be made to deal with Small Business APA requests as expeditiously as possible and taxpayers will be informed of any unusual delay.

## **Further Contact**

13. If you have any comments, feedback or questions about this special release or the services of the Competent Authority Services Division, either telephone (613) 941-2768, email us at **MAP-APA.PAA-APP@ccra-adrc.gc.ca**, fax (613) 990-7370, or write to us at the following address:

Canada Revenue Agency  
Director, Competent Authority Services Division  
International Tax Directorate  
Compliance Programs Branch  
5th floor, 344 Slater Street  
Ottawa ON K1A 0L5

## ***Appendix: Standard Authorization for Email and Facsimile Transmission***

The following authorization must be included with all requests where the requester wishes the Canada Revenue Agency (CRA) to email and/or fax correspondence:

Re: Advance Pricing Arrangement

Name: (Name of taxpayer)

I hereby authorize the CRA to email and/or fax all correspondence concerning the advance pricing arrangement request, made on behalf of the above-noted taxpayer. The correspondence is to be transmitted to email address (insert email address) and/or fax number (insert number).

I am aware that the CRA does not provide assurance with respect to the protection, confidentiality, or security of email or facsimile transmissions. I accept the risks inherent in sending information by email and/or fax. I agree not to hold the CRA or its employees liable for any damage or loss, however caused, arising out of the email and/or facsimile transmissions of correspondence related to my advance pricing arrangement request.

Check one of the following boxes:

This authorization is for correspondence by email only. ☐

This authorization is for correspondence by fax only. ☐

This authorization is for correspondence by email and fax. ☐

\_\_\_\_\_  
Requester's name

\_\_\_\_\_  
Requester's signature

\_\_\_\_\_  
Date