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Tax Alert – Canada

Department of Finance consultation on Canada's transfer pricing rules

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

On 6 June 2023, the Department of Finance released a consultation paper titled *Consultation on Reforming and Modernizing Canada's Transfer Pricing Rules*. The consultation paper, which follows through on the commitment made in the 2021 federal budget to review these rules, includes draft revisions to section 247 of the *Income Tax Act* (the Act), as well as potential administrative measures, and requests comments from stakeholders by 28 July 2023.

Shortly, EY will release a more extensive Tax Alert reviewing the content of the consultation paper in detail.

The main proposal concerns possible amendments to the transfer pricing adjustment rule in section 247 of the Act. These potential changes are intended to provide greater clarity on the application of the arm's length principle in Canada. In addition, the consultation provides stakeholders with the opportunity to provide input on administrative matters connected to transfer pricing, such as documentation and penalty provisions and the possibility of adopting more modern or simplified approaches in specific situations.

The consultation paper poses a series of 23 questions requesting specific input from stakeholders. In particular, Appendix A of the consultation paper outlines draft legislative measures, which include:

- ▶ Revised definitions to improve legislative clarity, including the addition of new definitions for “economically relevant characteristics” and “multinational enterprise group”
- ▶ Introduction of the phrase “comparable circumstances” to limit the hypothetical comparison for the delineated transaction versus what *any* two (or more) persons dealing at arm’s length would have agreed to
- ▶ Increased emphasis on the “conditions” of the delineated transaction or series to allow adjustment where the conditions are different from those that would have been included if the participants had been dealing with each other in comparable circumstances
- ▶ Replacement of the current “recharacterization” provision in paragraphs 247(2)(b) and (d) of the Act with an explicit “non-recognition” test
- ▶ Inclusion of a “consistency” provision referencing the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*.

Other administrative measures considered in the consultation paper for which input is requested include the following potentially significant developments:

- ▶ Introduction of *de minimis* transaction rules and exemptions for small taxpayers
- ▶ Provision of safe-harbour interest rates or ranges
- ▶ Potential adoption of a standardized OECD style Master File/Local File model for transfer pricing documentation
- ▶ Increased thresholds for transfer pricing penalties
- ▶ Introduction of streamlined pricing approaches for certain transactions, such as low value-adding intra-group services and distribution

The substantive elements of Canada’s transfer pricing rules have not been revised since their original introduction in 1997. The Department of Finance’s consultation paper provides an opportunity for stakeholders to have input on this very important component of Canadian tax law.

EY will review the consultation paper in greater detail and provide comments to the Department of Finance.

Learn more

To view the full Department of Finance consultation paper, visit:

[Consultation on Reforming and Modernizing Canada's Transfer Pricing Rules - Canada.ca](https://www.canada.ca/en/department-of-finance/2019/05/consultation-on-reforming-and-modernizing-canada-s-transfer-pricing-rules.html)

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