

Surprise! The Impact of Transfer Price Adjustments on Canadian Customs Valuation and Compliance

Did you know that an importer may be required to amend its customs filings to reflect transfer price adjustments to import prices made for income tax purposes by a parent or other related company? Even if not required, the importer may wish to voluntarily amend the import price to claim a duty refund where a transfer pricing adjustment decreases the import price of dutiable goods.

In the modern global economy, many corporations carry on business domestically in their home countries, but transact business with other countries through related affiliates. For income tax purposes, these related companies must ensure that pricing between related entities reflects arm's-length transactions, in accordance with the OECD Guidelines (which have been incorporated into the *Canadian Income Tax Act*). In many cases, these obligations are satisfied through periodic transfer price adjustments. These adjustments are generally recorded as paper/electronic transactions in corporate accounting records, with no actual transfer of funds involved.

The practice of many corporations entering into international transactions is to establish a selling price at the start of a fiscal year. This price is often based on a previous year's arm's-length pricing. Periodically during the year, or generally at least on an annual basis, the pricing will be re-examined to determine whether this pricing actually did reflect arm's-length transactions. Transfer price adjustments may be made by reference to expected

returns at certain trade levels, or more accurately to actual sales to non-related purchasers.

It may come as an unpleasant surprise to a foreign vendor and its importing affiliate to learn that the affiliate may have a legal obligation in Canada to amend customs filings to reflect import prices after transfer price adjustments have been made. The obligation to amend customs documents may arise whether prices are increased or decreased (although those resulting in duty refunds do not generally impose an obligation, but rather may be voluntarily requested to be adjusted by claiming duty refunds). Where transfer prices are increased, the situation becomes more problematic because there may be additional customs duties and sales/value-added taxes (such as GST) payable.

In the event that the CBSA discovers a failure to amend customs documents to reflect subsequent transfer price adjustments, an importer may be subject to assessments of duties, taxes, interest on overdue amounts and Administrative Monetary Penalties ("AMPs"). Interest generally compounds daily. The importer might also be required to correct up to four years of customs entries.

Any required amendment should be made within 90 days of when the importer acquired "reason to believe" that the original valuation declaration is incorrect. The Canadian International Trade Tribunal upheld the Canada Border Services Agency's ("CBSA")'s position in *Jockey Canada Co. v President of the CBSA* (2013), AP-2011-008.

There is generally no such obligation to correct the value for duty ("VFD"), and no related risk of AMPs for not correcting the VFD, where a transfer pricing decrease would result in a duty refund. Nevertheless, the importer may wish to voluntarily file an adjustment to the import price to claim a duty refund within the four-year claim period permitted by law.

In testimony described in *Jockey Canada*, the CBSA advised that its standard practice is to allow amendments to lower the VFD as the result of downward year-end transfer pricing adjustments.

This testimony represents an apparent change in position. The CBSA had previously advised that such downward pricing adjustments should be ignored as post-import price reductions pursuant to paragraph 48(5)(c) of the *Customs Act*. The decision in *Jockey Canada* should assist importers in pursuing duty refund claims made on the basis of downward transfer price adjustments.

To calculate the VFD under the transaction value method, the CBSA starts with the transfer price for income tax purposes to determine the price paid or payable for goods that are imported into Canada. Once any transfer pricing adjustments are taken into account, the resulting transfer price generally constitutes the transaction value of the imported goods. The transaction value may be subject to further adjustments as set out in section 48 of the *Customs Act*.

The CBSA has in recent years been conducting extensive customs compliance audits to examine issues such as VFD, rules of origin and tariff classification. Where there are transactions between a Canadian importer and a related foreign vendor/exporter, CBSA has been looking at transaction price adjustments as part of the VFD review, to ensure that appropriate revisions to customs documentation are being made to reflect transfer price adjustments.

Importers receiving goods from related parties abroad need to be advised in a timely manner of all transfer price adjustments affecting the customs value of their imported goods, so that the appropriate amendments can be made to customs filings. To amend entries in a timely manner, there needs to be prompt communication of these adjustments to the Canadian customs compliance team.

In the event that there has been a failure in the past to file such amendments, one potential avenue to protect against AMPs would be to take advantage of the CBSA's voluntary disclosure process. If the importer wishes, the importer could initiate the voluntary disclosure on an anonymous basis through legal counsel to seek CBSA's opinion that it would approve the voluntary disclosure

upon completion of the necessary steps. As part of the voluntary disclosure, the incorrect VFD declarations would generally need to be corrected (up to four years). Although AMPs may be avoided as a result of CBSA accepting the voluntary disclosure, any overdue duties and taxes would generally be required to be paid, along with any prescribed interest accruing thereon. Another potential advantage of the voluntary disclosure is that CBSA would impose interest at the prescribed rate, rather than the punitive specified rate (6% per annum higher than the prescribed rate).

Summary

The Canada Border Services Agency (CBSA) may require that amendments to customs valuation declarations be made by an importer, whose reported value for duty (VFD) is changed by way of a subsequent transfer price adjustment made by a related vendor for income tax purposes. If the importer does not make the amendments in a timely manner, then the importer may need to take proactive steps to correct the entries, and to revise customs practices going forward.

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[a cautionary note](#)

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