Taxpayer Wins Convincing Decision in Landmark Canadian Transfer Pricing Case

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On September 26, 2018, the Tax Court of Canada released its long-awaited transfer pricing decision in *Cameco Corporation v. The Queen*.

Relevant to: Multinational groups with Canadian subsidiaries or a Canadian parent corporation, and other Canadian residents who engage in transactions with non-residents of Canada with whom they do not deal at arm's length.

Issue: The Tax Court of Canada has released a very important decision on Canada's transfer pricing rules under the *Income Tax Act* (Canada), which require a Canadian resident to transact with non-arm's-length non-residents on arm's-length terms for Canadian tax purposes.

On September 26, 2018, the Tax Court of Canada released its long-awaited transfer pricing decision in *Cameco Corporation v. The Queen*.

The case involved the application of Canada's transfer pricing rules in the *Income Tax Act (Canada)*, which govern transactions between Canadian residents and non-arm's-length non-residents of Canada (*e.g.*, a Canadian subsidiary and a foreign parent company or vice versa).

In this case, the Canadian taxpayer, Cameco Corporation (one of the world's largest uranium producers) had entered into long-term contracts to sell uranium to its Swiss subsidiary, and also guaranteed long-term contracts entered into by its Swiss subsidiary to purchase uranium from a third party. Following the entering into of these supply contracts, the price of uranium rose significantly. The result was that profits from sales by the Swiss subsidiary to customers outside of Canada were realized largely in Switzerland rather than Canada.

The Canada Revenue Agency (CRA) re-assessed Cameco essentially to attribute to it the profits that had been earned by its Swiss subsidiary, arguing that the foregoing purchase and sales contracts involving the Swiss subsidiary:

1. were a "sham" that should be looked through, and

2. did not meet the arm's-length standard contained in Canada's transfer pricing rules, so as to allow the CRA to either completely ignore the contracts or to revise their terms in accordance with what arm's-length parties would have agreed to.

While the case before the court involved only Cameco's 2003, 2005 and 2006 taxation year, the CRA had challenged the taxpayer's later years as well, with Cameco estimating that the total amounts potentially at stake for 2003-17 were approximately $2 billion plus interest and penalties.

Following a 65 day trial, Mr. Justice Owen of the Tax Court of Canada found in favour of Cameco in a lengthy (293 page) and detailed judgment, rejecting the Crown's arguments on both the "sham" and transfer pricing issues. The CRA was ordered to re-assess accordingly.

This ruling was described by Cameco CEO Tim Gitzel as "a clear and decisive ruling in our favour" and "a vindication of our position, our company."

Unless reversed on appeal (which the CRA has 30 days to initiate to the Federal Court of Appeal), the Cameco decision of the Tax Court of Canada will serve as very important guidance to taxpayers and tax authorities on the interpretation of Canada's transfer pricing rules, including:

1. the scope of the transfer pricing rule that allows the CRA to completely re-characterize the taxpayer's transactions (as opposed to merely repricing them), which had not previously been dealt with by the courts;
2. in cases where the Canadian taxpayer is the multinational group parent, the interpretation of Canada's transfer pricing rules within the context of the regime in the ITA governing the taxation of foreign subsidiaries of Canadian corporations;
3. the allocation of business opportunities within multinational corporate groups and the respect to be accorded to intra-group legal arrangements; and
4. how these rules do (or do not) incorporate various elements of the OECD's recent work in the transfer pricing area under its Base Erosion and Profit Shifting (BEPS) initiative).

To learn more about the implications of this decision, please contact Steve Suarez.

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