

Evaluation of Advance Pricing Arrangement Program

FINAL REPORT

Prepared For

Canada Customs And Revenue Agency

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Project Background

- CCRA has offered the Advance Pricing Arrangement program since 1993. 87 applications (representing approximately 50 companies) have been received since the inception of the program.
- Recent published research indicates that international transfer pricing is growing in importance as an international tax issue.
- Senior CCRA officials are questioning the demands that might be made upon this program in the future as a method of dealing with transfer pricing issue disputes.
- Almost all of the applicants to the program to-date have been very large multinational companies.

Project Summary

- The primary objectives of this project was to assess the attitudes and opinions of current APA program users (Qualitative Phase) and to determine the potential future use of the APA program (Quantitative Phase).
- Focus Groups and personal interviews were used to solicit opinions from external tax advisors and current / former participants in the APA program.
- A quantitative telephone survey was conducted with external tax advisors and tax executives from large and small corporations in Canada.

Qualitative Research Objectives

Primary qualitative research objective ...

To understand attitudes and perceptions of current users and their tax advisors to the Advance Pricing Arrangement program.

Secondary qualitative research objectives ...

- To understand how participants entered the APA program
- To understand general attitudes towards APA program
- To identify strengths and weaknesses of the APA program
- To obtain suggestions for changes to the program and scope of the program
- To obtain an evaluation of APA program personnel.

Quantitative Research Objectives

Primary quantitative research objective ...

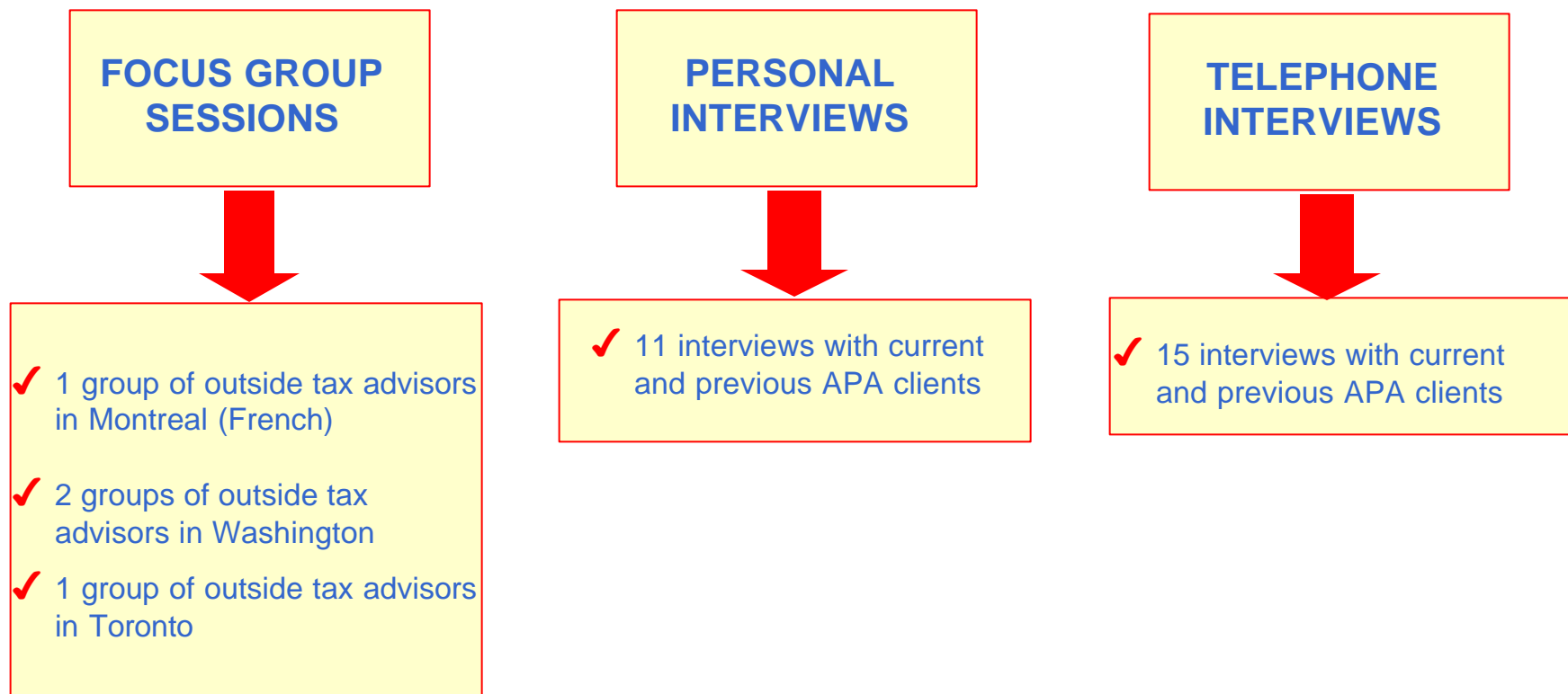
To understand the size of the potential market for the APA program offered by Canada Customs & Revenue Agency.

Secondary quantitative research objectives ...

- To understand importance of transfer pricing and other international tax issues
- To understand whether transfer pricing is gaining or losing in importance
- To assess the role of transfer pricing in an organization
- To determine the factors that shape international transfer pricing policies
- To understand level of awareness and favourability of CCRA's APA
- To determine the benefits of the APA and the general attitudes to the program.

Qualitative Research Methodology

- In order to meet the objectives of the qualitative phase of this project, a combination of focus groups and personal interviews were conducted. Current and previous clients were interviewed in person in Montreal (French) and Toronto and by telephone for all other locations. Focus groups with outside tax advisors were conducted in Montreal, Toronto and Washington.
- Field Dates: February 23, 2000 to March 13, 2000

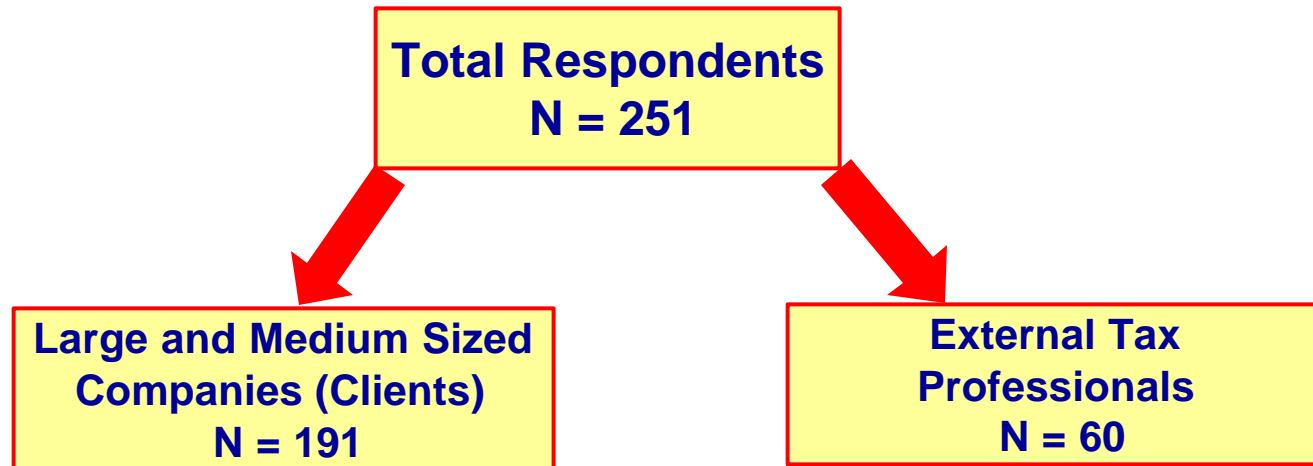


Who Was Interviewed In The Qualitative Phase?

- Representatives from 26 organizations
- One half of organizations have or had approved APA's. A number have expired APA's.
- One half are in the approvals process. One had terminated application.
- The average length of time in the approvals process for these companies was 3.5 years.
- Half of individuals interviewed were from US, others from Canada.
- Focus groups conducted with tax advisors in Washington, Montreal and Toronto.

(It is of note that very few differences of opinion or perceptions regarding the APA program and international transfer pricing exist between tax advisors and clients)

Quantitative Methodology - Sample



- In this quantitative phase of the project, telephone interviews were completed with 191 senior tax executives of corporations who are facing international transfer pricing issues.
- In addition, 60 telephone interviews were completed with outside professional tax advisors.
- The telephone calls were conducted between March 15 and March 31, 2000
- On a total basis, a sample of 251 is accurate to within +/- 5.19 percentage points; 9 out of 10 times.
 - ▶▶▶ Large & Medium Sized Companies (N=191) : +/- 5.95%; 9 out of 10 times
 - ▶▶▶ Outside Tax Professionals (N=60) : +/- 10.62%; 9 out of 10 times

Reporting Perspective

- The findings from the qualitative and quantitative phase are reported in separate sections. This approach was decided upon as they really are two very distinct and separate components of this overall research study each with their own objectives and methodology. Additionally, the sample of people interviewed was completely different in each phase. The qualitative phase addressed the attitudes and opinions of persons very familiar with CCRA's APA program. Largely, these individuals had direct previous experience with an APA. The sample for the quantitative phase was much wider. It included a number of people with limited or no previously knowledge of the APA, but who may have need for such a program as their companies have international transfer pricing issues.
- Throughout the report, circles and squares have been used to distinguish results which are statistically significant from either the total or from findings within the same data break.
- Circles signify findings which are statistically higher, whereas squares highlight those which are below the norm.
- The report highlights differences at a 90% level of confidence.
- Given the sample sizes and the resultant margins of accuracy, some results should be interpreted with caution.



PART ONE:
EXECUTIVE SUMMARY

Executive Summary - Qualitative Phase

The APA is a Great Concept But...

- The concept of an APA is great but the lengthy and costly approvals process due to insufficient CCRA staff in the past and a mindset amongst APA staff that is inconsistent with the overall objective of reaching acceptable solutions to all participants have diminished the value of the program.
- It should be of concern that there are split opinions relative to a number of the benefits that should result from an APA program.
- Despite this, most organizations need the certainty that the APA can provide and are willing to persist.
- There is a need to address the concerns of both clients and outside tax advisors in the near term and to communicate the changes that are being implemented to this very “close-knit” community of tax professionals. There is a sense from current participants that CCRA should get its house in order prior to increasing the scope of the APA.

Executive Summary - Qualitative Phase

While the APA in general is viewed as a great concept, the CCRA program is only viewed in a somewhat favourable light.

- International transfer pricing is an issue that is growing in importance for these companies.
- International transfer pricing is largely viewed as a compliance / audit issue and is not being used as a management tool to create strategic advantage for these organizations.
- APA programs are generally viewed very favourably as they are seen as a proactive approach to avoid unpleasant surprises.

Executive Summary - Qualitative Phase

CCRA is Blamed for Most of the Delays in Approvals

- Although some admit that the companies and other governments are partially to blame, the greatest portion of blame for the undue length of the approvals process is assigned to CCRA.
- There are two major reasons identified as causing these delays:
 - Lack of sufficient, well-trained staff in the APA program unit. (Some sense that the headcount issue is being resolved, but the new additions are not well trained)
 - A mindset within the CCRA program personnel that they are searching for an exact answer and not a close, acceptable answer. A number say that the APA program team members appear to be unwilling to make decisions. Others also say their mindset includes being protective of Canada's revenue sources and in some circumstances to the point of aggressively seeking new revenues.(Some say they are understanding of this)

Executive Summary - Qualitative Phase

Most Would Apply for an APA Again

- Despite the length of time and cost to obtain an APA, most respondents would make the same decision again to apply for one. There are a number of organizations who were early program participants who say they are reluctant to participate again.
- The alternatives, either a bad audit, double taxation or non-deductible penalties and interest, are less acceptable options of handling international pricing disputes for most. There are some tax advisors who feel that documentation that will hold up under Section 247 is a better alternative given the delays and costs associated with an APA.
- Once approved, the certainty of treatment provided by an APA is a benefit that outweighs the time, frustration and cost of the application process.
- The APA Program enhances users impressions of CCRA as a whole.
- There is split opinion as to whether or not the process is much too expensive relative to the benefits achieved.

Executive Summary - Qualitative Phase

Many Would Recommend To Others, But With Conditions...

- Many would recommend to others but usually under certain specified conditions.
 - »»» *“Not unless being audited”*
 - »»» *“Yes, if they can afford”*
 - »»» *“If they have complex issues or a specific need for certainty”*
 - »»» *“When CCRA develops more of a positive track record”*
 - »»» *“Not practical for smaller companies”*. This opinion varies by country with US tax advisors being more positive about the value than an APA can provide to a medium sized company.

The Search for Certainty is Driving the Desire for APA's...

- The APA is geared primarily to the elimination of double taxation
- The main benefit is the “certainty of treatment” provided to the stakeholders in each organization and the resulting comfort level for all stakeholders

Executive Summary - Qualitative Phase

The Value and Benefits of an APA are Being Diluted...

- Each of the following statements receive mixed agreement and should be some cause for concern:
 - The APA is much too expensive relative to the benefits achieved
 - The APA provides my organization with a discipline by providing a forum to present arguments regarding transfer pricing issues
 - The APA staff operate in a supportive fashion
 - The on-going reporting requirements greatly diminish the value of the APA for our company
 - The APA is not an adversarial approach

Executive Summary - Qualitative Phase

Many Positive Words are Used to Describe CCRA APA Staff, However, Flexible and Customer Oriented Are Not Among Them

- Applicants and outside tax advisors credit APA staff with being professional, conscientious, reliable, easy to work with and knowledgeable.
- Negative perceptions of staff include being bureaucratic, inflexible (not open to different viewpoints) and lacking in understanding of some of the industry sectors they are working in (financial services, high technology companies). Many say that APA staff are reluctant or incapable of making decisions.
- The positive words provide a good base upon which to improve those words less associated with the APA staff during the period ahead when CCRA works to reduce the length of the approvals process.

Executive Summary - Quantitative Phase

Market Potential

- The market potential for the APA in the next few years would appear to equal the number of participants that have entered the program since its inception.

International Transfer Pricing

- International transfer pricing is an issue that is growing in importance and APA programs in general are one of a number of methods of dispute resolution that are viewed reasonably favourably by clients and outside tax advisors
- Approximately one in two large companies report having international transfer pricing issues, while the incidence drops to one in five for medium sized companies

APA Program Offered By CCRA

- Six of ten of those interviewed say they are aware of the CCRA's APA program. Almost seven of ten report having a favourable overall impression of this program.
- The certainty of treatment and the avoidance of negatives (double taxation, penalties) are the primary benefits provided by an APA. Other benefits are also seen as important, including the assistance that an effective APA program can have in helping the country attract investment.
- There is however, a general sense that obtaining an APA takes far too long and is too costly.

Executive Summary - Quantitative Phase

APA Program Offered By CCRA (cont'd)

- Some key findings suggest some direction for the positioning of the APA program. The program is perceived to be a way of avoiding negatives and achieving certainty, however, it is seen by a significant minority as an adversarial approach. In addition, one in five do not feel that the program provides complete confidentiality of company information. Seven of ten outside tax advisors feel that the APA is only of use for very large companies.
- There is a general sense that the APA provides slightly more benefits to the CCRA than it does to the taxpayers.
- There is majority support for the practice of billing back travel expenses to the applying taxpayer.
- There is good support, especially with outside tax advisors, for having the APA applied to cover approximately 3 previous years.

Importance of Outside Accountants and Lawyers

- Outside tax accountants and, to a lesser extent tax lawyers, are the sources most relied upon by corporate executives for APA information. This has implications for the Agency in determining future communications strategies and plans.



Implications

IMPLICATIONS

- To date, it has been a relatively small community of organizations involved with APA programs. There does, however, appear to be a good market potential for the APA, especially with larger companies.
- There is also a reasonable market with medium sized firms. The feeling of tax advisors that the APA is only of use for large companies, while not shared by medium sized clients, may be a barrier for the program in attracting a significant number of medium sized companies.
- Prior to rolling the program out to new interested companies, there would appear to be a need to resolve some of the long outstanding applications expeditiously.
- There is a positive story for CCRA staff to hear. The program is viewed favourably, has strong benefits associated with it, a majority see the program as an asset for Canada in attracting new investment and has a market of large and medium sized companies saying they are very likely to use an APA in the next few years almost equal to the number of clients who have applied since 1993.
- This having been said, a number of improvements can be made to the operation of the program.
- There is a need to work at reducing the average time necessary to obtain an APA down from the current 3.5 years to a more reasonable time period. Steps need to be taken to address the time necessary to obtain an APA and those steps communicated to the interested stakeholders. This has implications for staffing levels and training programs for new additions to the APA program teams.
- There would appear to be a need to change the mindset of APA program personnel with respect to the preciseness with which they approach the task and with respect to the dominance they appear to assign to the task of revenue protection.

IMPLICATIONS (CONT'D)

- The key findings of this research suggest some direction for the positioning of the APA program. It is not universally seen as non-adversarial, as keeping company information confidential, or as being important for satisfying section 247 requirements or in clearing up past problems.
- Senior management of the APA group should review the detailed suggested changes made in the body of this report to determine those that could be of value in improving the effectiveness and efficiency of the program.
- Because of the importance of outside tax advisors to clients, special attention should be paid to them in any communications plan or strategy that is adopted.
- Consideration might be given to adopting a three year optional rollback of the provisions of the APA for approved applicants.
- While there is majority support for the practice of billing back travel expenses to the applying taxpayer, the feeling regarding the proportion of benefits accruing to CCRA might justify a re-think of this practice.
- Consideration might also be given to sharing the results of both the qualitative and quantitative surveys with clients, applicants and outside tax advisors. The approach of saying we asked for your comments, we have heard you and this is our plan to address these issues could be very beneficial.



PART TWO:
DETAILED QUALITATIVE FINDINGS



Attitudes Towards International Transfer Pricing

INTERNATIONAL TRANSFER PRICING IS AN ISSUE THAT CONTINUES TO GROW IN IMPORTANCE

- The increase in importance is due to a number of factors:
 - »»» Increase in attention by governments looking for revenue generation / protection
 - »»» Increasing global nature of many organizations
 - »»» Number of countries trying to keep up with US Government and OECD guidelines
 - »»» Imposition of penalties / interest by US rulings
 - »»» Increasing need to provide comfort for executives / shareholders in a global environment
 - »»» *“Looking hard for certainty”*

TRANSFER PRICING IS CONSIDERED BY MOST ORGANIZATIONS AS AN AUDIT / COMPLIANCE MATTER

- Few companies consider transfer pricing as a strategic management tool.
- From a North American point of view, taxes in both Canada and the US are viewed as roughly equal, thus eliminating any advantage that might be gained by shifting profit. *“The Canadian and US tax rates are about the same- there are no great savings”*.
- Some companies say that it would be risky or foolish to try to fool governments by making money on tax matters. Others say that they consider it their duty to pay their fair share of taxes. They don't feel CCRA looks at them in this light.
- There are more important investment decisions than transfer pricing such as labour availability and cost, market proximity, quality of life for employees and availability of raw materials.



First Contact And Expectations
- Advance Pricing Arrangement Program -

CANADA CUSTOMS AND REVENUE AGENCY HAS PROVIDED INFORMATION BUT HAS NOT SOLD THE APA PROGRAM

- Organizations have generally learned about the program from outside tax advisors, CCRA tax circulars, industry publications and conferences.
- CCRA has not taken on an aggressive marketing role of the program.
- The marketing or “participation drivers” are either outside tax advisors or parent companies.

THE DECISION TO APPLY FOR AN APA

- Usually made by parent company.
- Generally a tough sell for tax executives to convince many of their senior executives to spend money and effort for an APA. Senior executives usually have to be sold as this is generally seen as a compliance issue and most CEO's are more interested in business operations decisions that impact upon revenue or costs.
 - » *“This (recommending an APA) is not a career enhancing move for most tax executives!” In fact, some tax executives go out on a limb by encouraging their companies to enter a complex, time-consuming and expensive process.*
- The case for an APA is made a lot easier with a “bad audit”.

THE MAIN POSITIVES FOR CONSIDERING THE APA PROGRAM ARE THE AVOIDANCE OF NEGATIVES

- Few companies enter the program to achieve positive benefits.
- Rather they wanted to avoid negative consequences of reassessments (penalties / interest or double taxation).
- However, there is strong agreement that the main benefit of the APA is the positive comfort that is provided by the certainty of treatment and the corresponding lack of unpleasant surprises for management, shareholders and senior tax executives- *“The world is moving in the APA direction in search of certainty”*.

POSITIVE CONSIDERATIONS OUTWEIGH THE NEGATIVES

Positive Considerations

- »»» Certainty factor
- »»» Future or past bad audit
- »»» Faster solution than lawsuit or Competent Authority
- »»» Comfort factor
- »»» Avoidance of penalties
- »»» Avoid double taxation
- »»» Reduce future audit costs
- »»» Possible solving of past audit problems

Negative Considerations

- »»» Time to complete process
- »»» Costs
- »»» Complexity of process
- »»» No guarantee of success
- »»» Disclosure of lots of information to tax authorities that would otherwise not surface in an audit
- »»» Loss of confidentiality of information
- »»» A worry that information obtained during an application could be used against them later if an agreement is not reached



Actual Experience with the Advance Pricing Arrangement Program

THE MAJORITY HAVE A SOMEWHAT FAVOURABLE OVERALL IMPRESSION OF THE APA PROGRAM

- The favourable impression of the program is generally generated by the achieved or promised results and not by the lengthy approval process that organizations have to go through.
- ▶▶▶ *“It can be an arthritic process to get, but it is worth it”.*
- ▶▶▶ *“I can’t imagine that they (CCRA) get anything done!” “Paralysis by analysis”*
- ▶▶▶ *“There are not a lot of alternatives (to the APA).”*
- ▶▶▶ *“Happy with the way APA is handling our transfer pricing issues at present”*
- ▶▶▶ *“The most intelligent thing (APA’S)that governments have done”*
- ▶▶▶ *“An APA is a little bit better than not knowing the rules”*
- ▶▶▶ *“Anecdotal report that it will be extremely long process”*
- ▶▶▶ *“All countries came into it with same objective- A good answer for everyone”*
- ▶▶▶ *“If we don’t get APA, it will be disastrous for us!”*

“CERTAINTY OF TREATMENT” IS MOST LIKED ABOUT THE APA PROGRAM

LIKES ABOUT THE APA PROGRAM

- ✓ Certainty of treatment by tax authorities (Major benefit)
- ✓ Comfort provided to board and shareholders
- ✓ Reaches agreement on future and past
- ✓ Avoids double taxation and penalties and interest charges
- ✓ Reduces cost of future audit defenses
- ✓ Better and cleaner process than audit, litigation or CA
- ✓ Meets strategic needs for global growth
- ✓ Assists us in determining the profitability of each part of business
- ✓ Has improved overall relationships with tax authorities
- ✓ Minimizes tax exposure

THE MAJOR DISLIKE OF THE APA PROGRAM IS THE TIME REQUIRED FOR APPROVAL

DISLIKES OF APA PROGRAM

- x Lengthy approval process
- x Costs incurred (little mention of CCRA invoiced costs)
- x No guarantees at the end of the day
- x Revolving CCRA staff on file / Inexperienced CCRA staff
- x Attitude toward companies as being cheaters
- x Lack of leadership on CCRA team/ *“reluctant to pull trigger”*
- x Possibility of rolling back into past years
- x The use of secret comparables
- x Level of detail requested
- x Revealing too much
- x Lack of feedback during the approval process
- x Left out of the government to government sessions

REASONS ATTRIBUTED FOR DELAYS IN APPROVAL

- Lack of CCRA staff (Some say this is improving recently)
- Turnover of CCRA staff
- Mindset of CCRA staff (Trying to make the right / precise decision rather than obtain a good answer for everyone)
- No overall detailed time-lines established
- Appears to be no accountability on the government end
- Unwillingness or inability to make a decision at CCRA
- Lack of trained CCRA staff(business issues)
- *“Relationship between IRS and CCRA fell apart”*
- *“Expected governments to assist more”*
- General communications problems
- Not being present at government to government meetings. *“We know our business better than they do. Not being there to answer questions cost us another 3 months”*

THERE IS STRONG AGREEMENT ON SOME APA POSITIONING STATEMENTS

The APA process takes much too long to complete → This receives almost unanimous agreement from all respondents

One of the main benefits is the “certainty of treatment” provided → This is seen as the major benefit of the program

The APA is geared primarily to the elimination of double taxation

The APA program provides complete confidentiality of my company’s information → Some comment upon recent IRS ruling that was overturned regarding publication of APA approvals

THERE IS SPLIT OPINION ON MANY BENEFITS STATEMENTS

The APA is not an adversarial approach for resolving transfer pricing issues

→ By definition it is an adversarial relationship. Adversarial between IRS and CCRA. Taxpayers feel on the defensive despite this being a voluntary process.

The APA process is much too expensive relative to the benefits provided

→ Too much detail requested. Costly to obtain.

The APA provides my organization with a discipline by providing a forum to present our arguments.

The on-going reporting requirements greatly diminish the value of the APA program for us

→ Will not accept electronic copies. Want too quickly.

The APA staff operate in a supportive fashion for my organization

→ No resolution. Keep asking for information. Don't see role as being one of support.

THERE IS GOOD AGREEMENT ON OTHER ASPECTS OF THE APA

The APA is not just an enhancement or tool to help organizations meet the requirements of section 247

One of the benefits of the APA is the assistance that the process provides in meeting the requirements of section 247

The APA program provides a good forum for taxpayers to deal with transfer pricing issues in a cooperative manner

→ A number do not see the process as being cooperative, either between themselves and government or between governments.

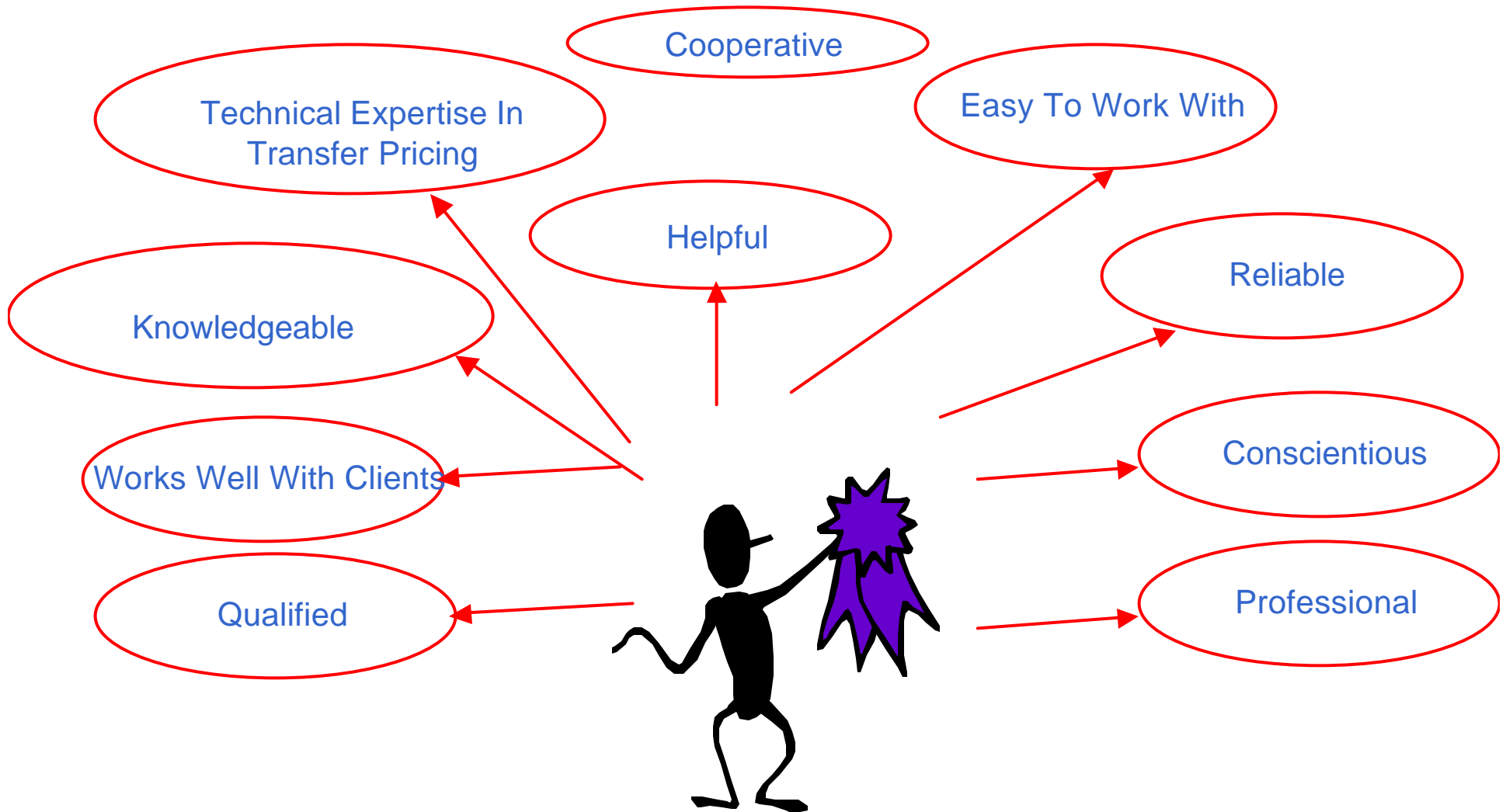
DESPITE THE ONLY “SOMEWHAT FAVOURABLE” RATINGS, THE APA IMPROVES THE OVERALL IMPRESSION OF CCRA

- Despite the operational difficulties and delays in approvals, clients and tax advisors generally say that the APA improves their overall impression of CCRA
- Clients and outside tax advisors like the proactive nature of this program
- *“It is a signal of the willingness of the government to become more competitive globally”*



Assessment Of APA Program Personnel

STRENGTHS OF PERFORMANCE OF APA PROGRAM PERSONNEL



Strengths to Leverage and Build On

WEAKER ASPECTS OF THE PERFORMANCE OF APA PROGRAM PERSONNEL

Not Able To Think Out Of The Box

Inflexible

Bureaucratic

Not Adaptable

Not forward thinking

Not Willing To Go The Extra Mile

Not Customer Oriented

Not Willing To Give And Take

Not Open To Different Viewpoints

Lack of understanding of business
and business processes



Areas Where Improvements Can Be Made



Scope Of APA Program

THERE IS LITTLE ENTHUSIASM FOR INCREASING THE SCOPE OF THE CURRENT APA PROGRAM

- There is a sense that CCRA should get its house in order prior to increasing the scope of the APA program.
- Adding customs issues and examining documentation do not generate much interest for many organizations and do not appear to be relevant to many of these companies. Permanent establishment issues could be of some interest, again provided the timing issue has been first dealt with.



Suggested Changes To APA Program

INCREASED STAFFING AND TRAINING ARE KEY SUGGESTIONS FOR CHANGE

Increased Staffing

- »»» Required to significantly reduce approvals time
- »»» There is a sense that this has been improving in recent months
- »»» Add good managers with ability to make decisions and improve empowerment
- »»» In short term hire outside consultants to address backlog and to provide training to new recruits
- »»» Hire staff with international experience and an understanding of business

Increase Training

- »»» Provide industry specific education to APA staff. Especially need to address the new knowledge-based industries
- »»» Consider structuring into industry specialist groups
- »»» Continue joint meetings and training with IRS

A CHANGE OF MINDSET AND IMPROVED COMMUNICATIONS ARE ALSO NEEDED

Change Of Mindset

- »»» Strive for close solution not exact price
- »»» Need to look at individual decisions in national interest- there could be potential loss of economic investment with a poor and inflexible APA program
- »»» Not an audit process- that comes later- looking for acceptable solution
- »»» Enter application process without conveying attitude that all companies are cheaters

Improved Communications

- »»» Establish a more formal communications process for each application. Establish regular reporting as to progress, people changes, meetings, etc.
- »»» Clarify role of CCRA staff at start of project
- »»» Be clear with reactions to company submissions- if a problem or disagreement - communicate that reaction
- »»» Include companies in government to government meetings as source of information

THERE IS A NEED TO FORMALIZE / INSTITUTIONALIZE THE PROCESS MORE

Formalize The Process More

- »»» Develop common information request lists with other governments
- »»» Establish detailed timelines by activity at the start of the project. Report on progress towards meeting these schedules
- »»» Increase accountability for meeting deadlines by relating to incentives, bonuses, promotions of APA staff
- »»» Streamline and reduce annual reporting requirements
- »»» Standardize requests for information
- »»» Rethink intensive documentation process
- »»» Generally institutionalize the process with rules, guidelines, case plans, etc.
- »»» Reduce compulsion to have “site” visits

MISCELLANEOUS

- Little disagreement with the team approach employed for this program.
- There is an understanding that different backgrounds are required to review the methodology.
- Comments are made that regardless of team makeup, somebody has to be in charge and be willing to make decisions.
- Some do comment that having to have all team members at meetings can cause delays in scheduling meetings.

VIEWS OF US OUTSIDE TAX ADVISORS

- Views are similar to clients on most issues. (This is a demonstration of the closeness of this community).
- Some express view that CCRA has “a chip on the shoulder attitude towards the US”.
- Support the use of the APA to help smaller companies whereas Canadian tax advisors do not. *“CCRA has not shown the same consideration for smaller companies as the IRS has” (This could be reflective of different definitions for medium sized companies in the two countries).*
- *Perceive problems for Canada if APA program is not favourably viewed.*
- *Some increasingly see Canada as an aggressive tax jurisdiction.*

VIEWS OF CANADIAN OUTSIDE TAX ADVISORS

- Views are also very similar to clients.
- Do not see APA as being of value to medium sized organizations.
- They seem to have a lack of understanding of the benefits of an APA with a number suggesting that CCRA, outside advisors and the companies all share in these benefits.



PART THREE:

DETAILED QUANTITATIVE FINDINGS

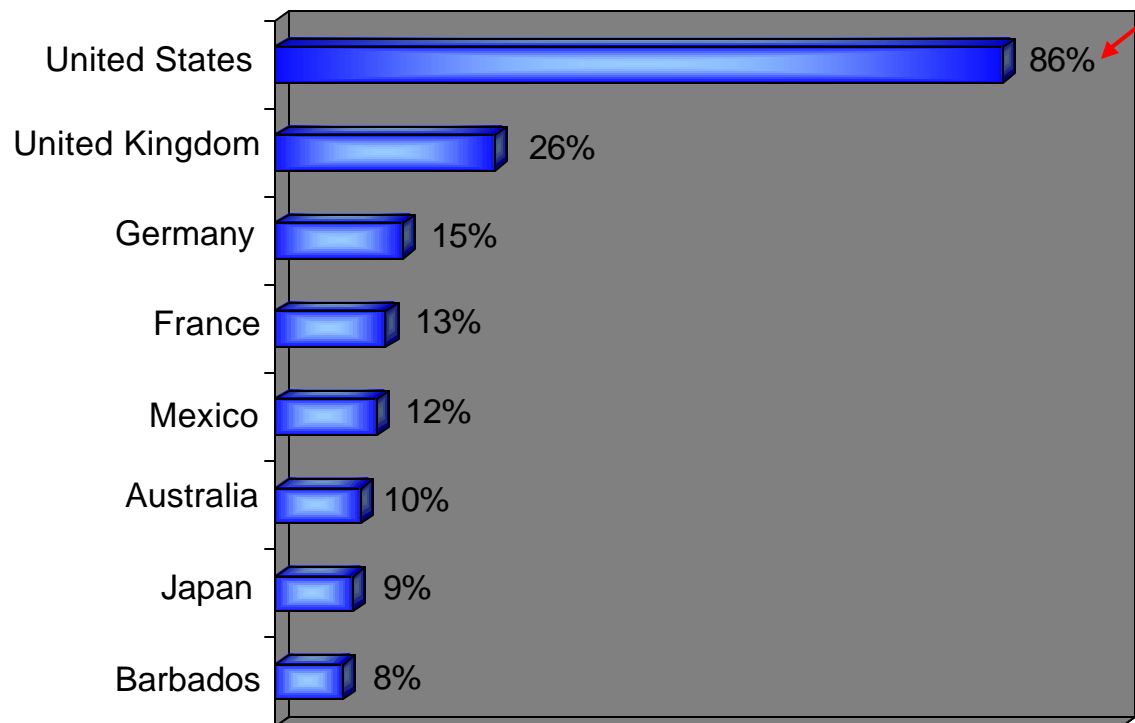


Understanding International Transfer Pricing Issues

Jurisdictions Of International Involvement

- Not surprisingly, given Canada's proximity and economic history, the vast majority of medium and large sized companies represented in the survey say they conduct non-arms length transactions with the United States. Slightly over one-quarter (26%) also say they are involved with companies based in the United Kingdom.
- Knowledge of geographic areas of involvement will become important in anticipating where the demand will come from for bilateral APAs.

Among Large/Medium Client Companies
(n=191)



Q. You indicated earlier that your organization has cross border transactions with non-arms length organizations. In which countries do you have these cross border transactions?

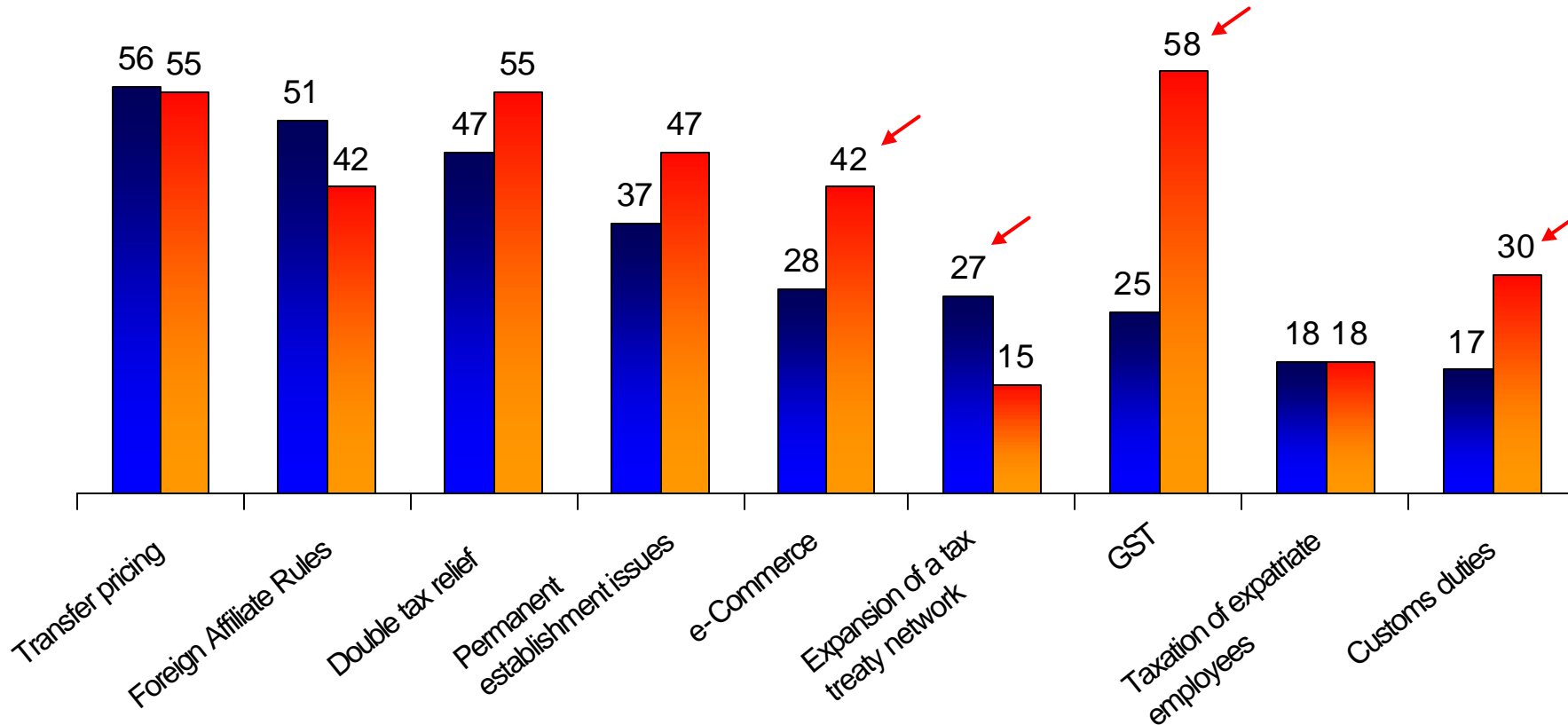
Importance of Various International Tax Issues

- A large portion of both clients and advisors give a high importance rating to: transfer pricing, Foreign Affiliate Rules, double tax relief, and to a less degree, permanent establishment issues.
- There are a few areas where the ratings of clients and advisors differ. The most remarkable difference concerns the importance of GST. Almost six in ten advisors feel this is an important area for their clients, whereas only one in four clients echo this sentiment.

% of Respondents Saying Issue Is Important
(8, 9, 10 on 10-pt. scale)

↖ = A statistically significant difference between the two groups

■ Lg./Med. Companies (n=191)
■ External Tax Professionals (n=60)



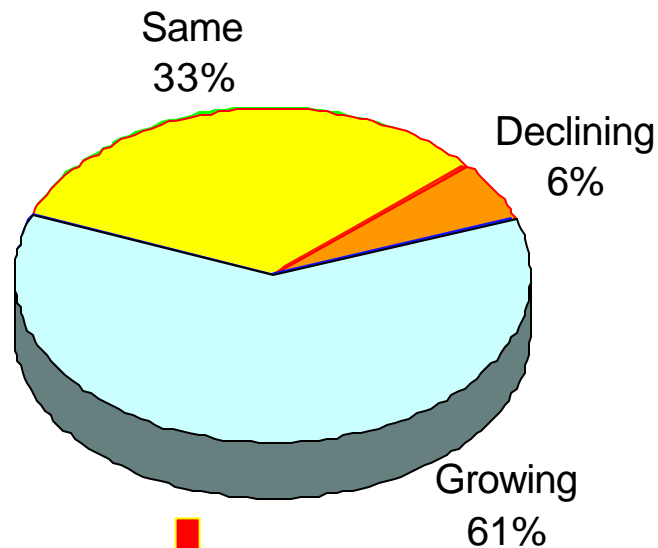
Q. Please indicate on a 1 to 10 scale where 10 means it is very important and 1 means it is not at all important, the extent to which each of the following international tax issues are considered important for your organization (your clients) in the next 1-2 years.

International Transfer Pricing Is Clearly An Issue That Is Growing In Importance

- While the majority of both clients and advisors feel that international transfer pricing issue are growing in importance, advisors are significantly more likely to feel this way.

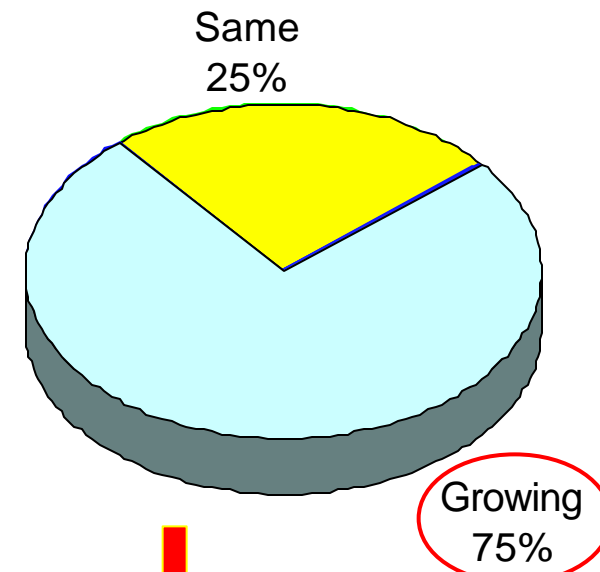
Is international transfer pricingin importance?

Among Large/Medium Companies
(n=191)



- Those most likely to say issue is "growing" in importance:
- Companies likely to apply for an APA 78%
 - High tech companies (small base) 86%
 - Resource based companies 73%
 - Subsidiaries 74%

Among External Tax Professionals
(n=60)

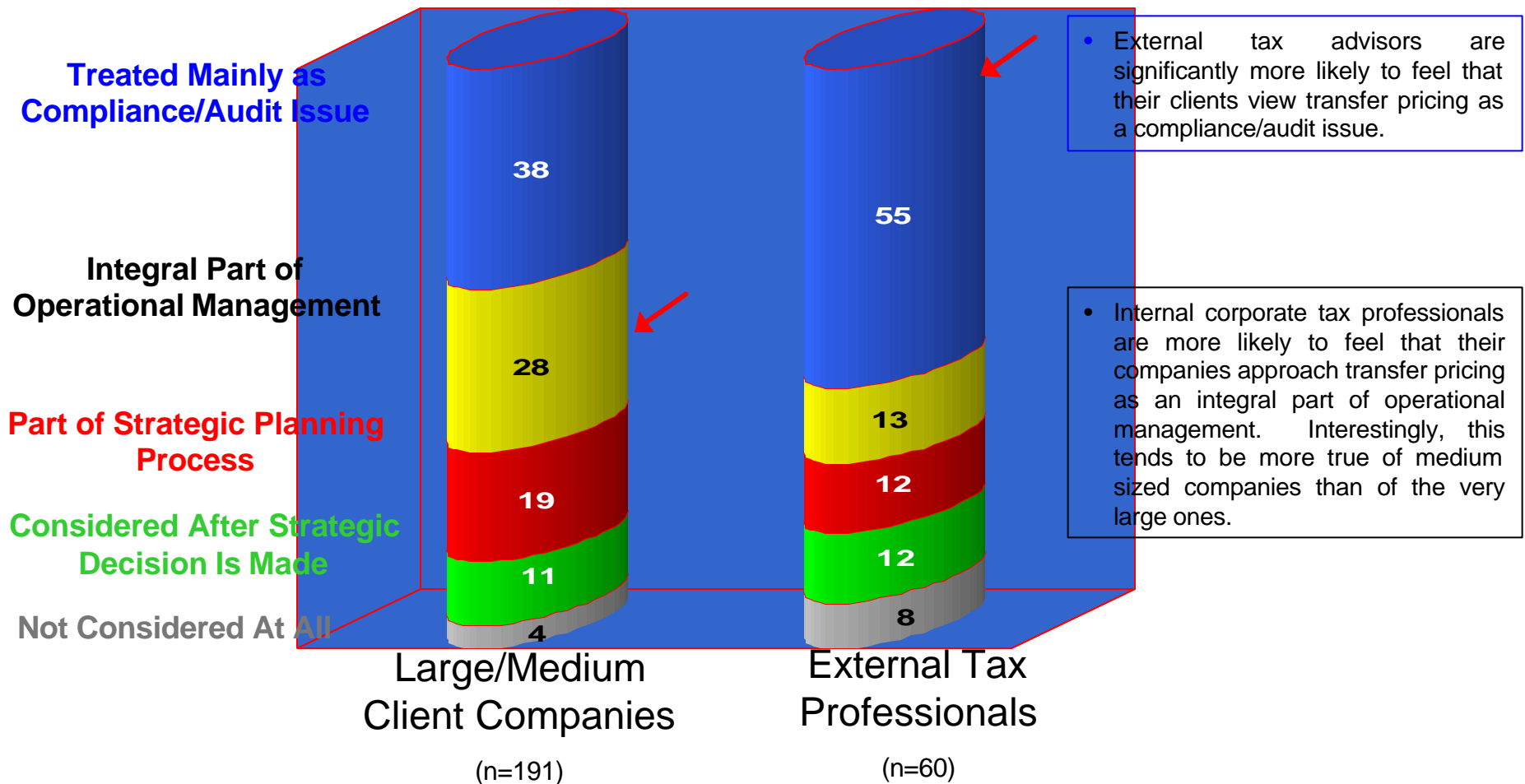


There are no significant differences within the various data breaks.

Q. Is international transfer pricing an issue that is growing in importance, staying the same in importance or declining in importance for your company (your clients)?

Tax Advisors Are More Likely To Say That Transfer Pricing Is A Compliance Issue

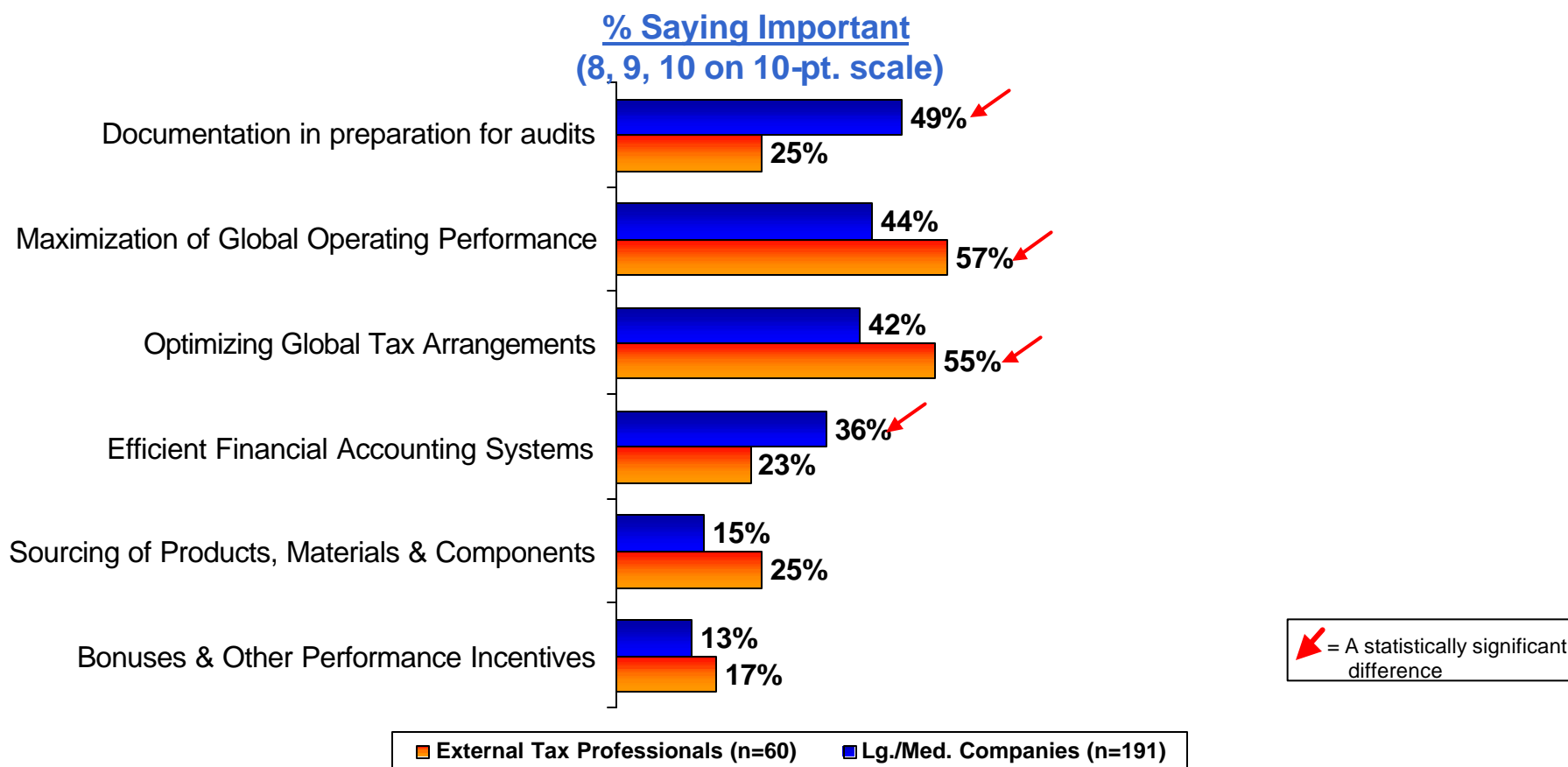
Best Describes Role of Transfer Pricing



Q. Which of the following best describes how transfer pricing is treated within your organization (your clients organizations)?
Transfer pricing is ...

Importance Of Factors in Establishing Transfer Pricing Issues

- There is a considerable disconnect between the perspectives of “clients” and advisors with regard to the importance of factors shaping transfer pricing policies.
- Clients are more likely than advisors to say efficiency of accounting systems and documentation needs to prepare for audits shape transfer pricing issues.
- Advisors, on the other hand, place more emphasis on the importance of results issues like maximizing global performance and optimizing global tax arrangements.



Q. There are a number of factors that could shape the transfer pricing policies of an organization. Could you please tell me how important each of the following are to your company (your clients) in establishing its transfer pricing policies. Please indicate on a 1 to 10 scale where 10 means it is very important and 1 means it is not important at all.



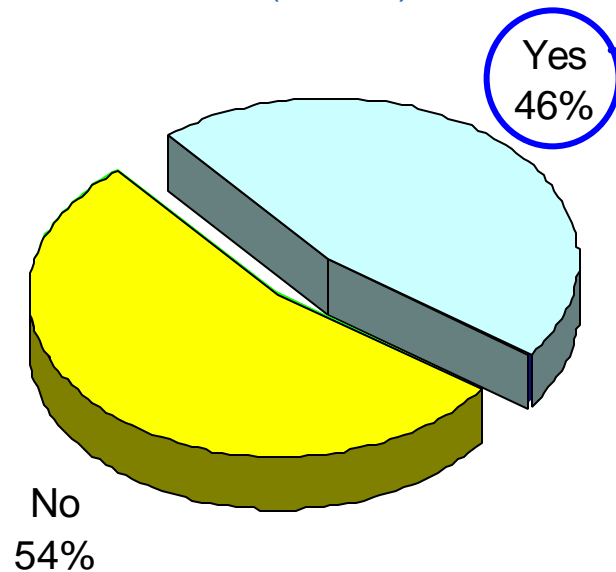
Perceptions Of Dispute Resolution Methods

Incidence Of Transfer Pricing Methodology Being Subject To Audit

- Among the large and medium sized companies surveyed, there was almost equal likelihood of them having had their transfer pricing subject to an audit or examination.

Has Your company's transfer pricing ever been the subject of an audit / examination by any tax authority?

Among Large/Medium Companies
(n=191)

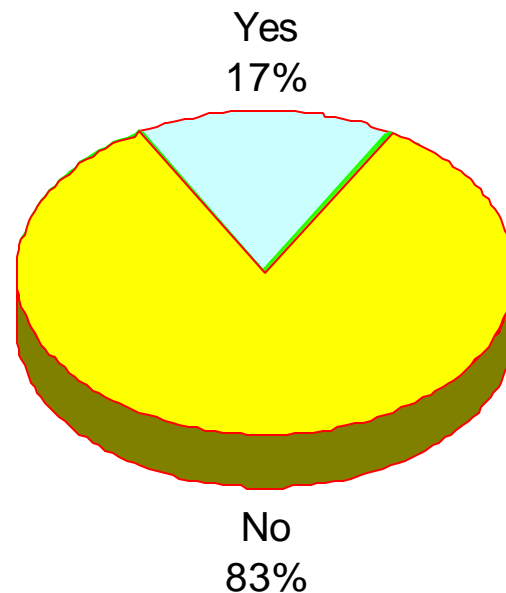


- Companies audited for transfer pricing are more likely to be:
 - ▶▶▶ Manufacturers (67%)
 - ▶▶▶ Public companies (62%)
 - ▶▶▶ Subsidiaries (68%)
 - ▶▶▶ Large companies with +\$1 billion in revenue (52%)
 - ▶▶▶ Aware of APA (53%)
 - ▶▶▶ Unfavourable impression of APA (69%)

Incidence Of Having Suffered Double Taxation Because Of Transfer Pricing

Has your company suffered any double taxation as the result of an audit or examination of your transfer pricing by any tax authority?

Among Large/Medium Companies Who Have Had Transfer Pricing Audited
(n=87)



- Cross-tab analysis does not reveal any differences among different kinds of companies being more or less likely to have suffered double taxation resulting from a transfer pricing audit.

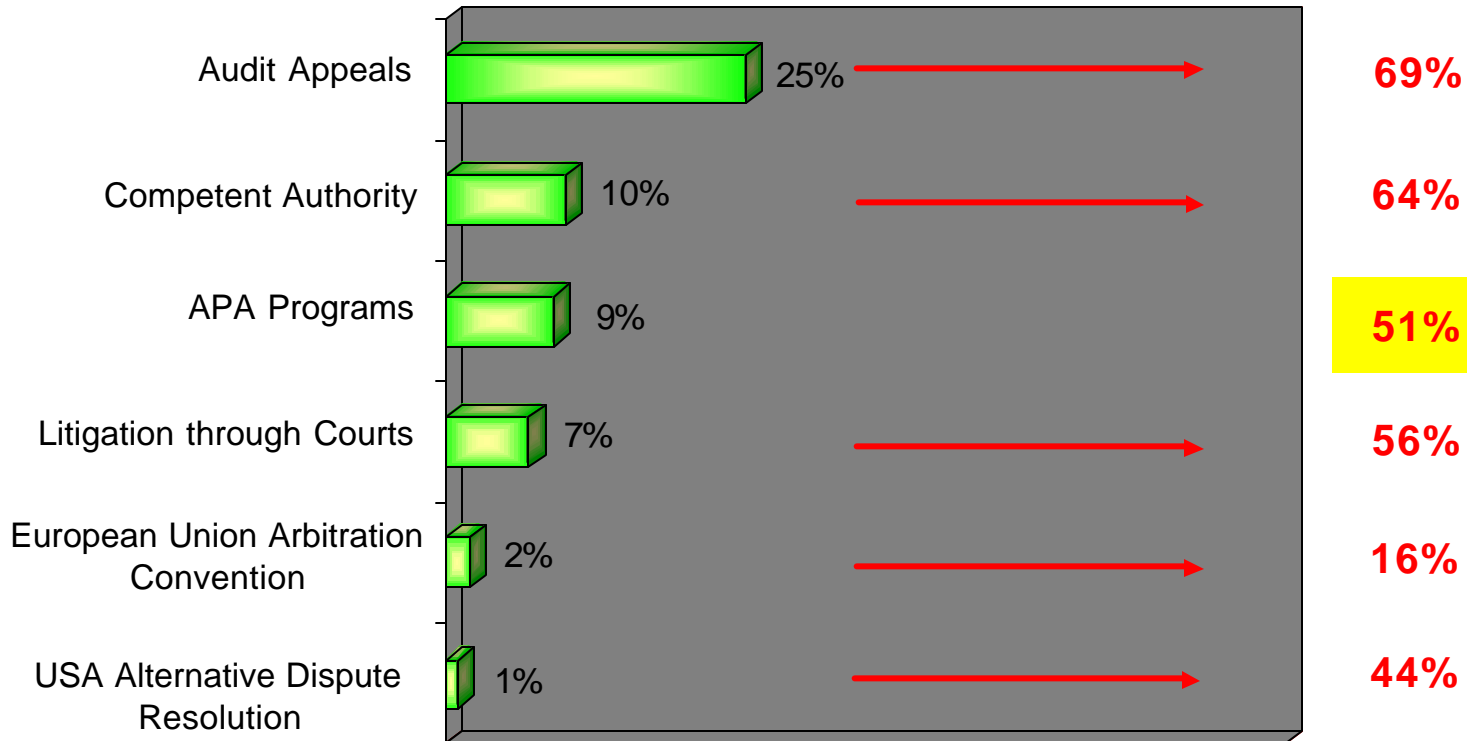
Q. Has your company suffered any double taxation as the result of an audit or examination of your transfer pricing by any tax authority?

Past and Planned Usage Of Alternative Dispute Resolution Methods

% of Large/Medium Client Companies (n=191)

Have Used Method in the Past

Willing to Use / Consider in the Future



Currently, 65% of the respondents say they have never used or applied to use any of the above dispute resolution methods.

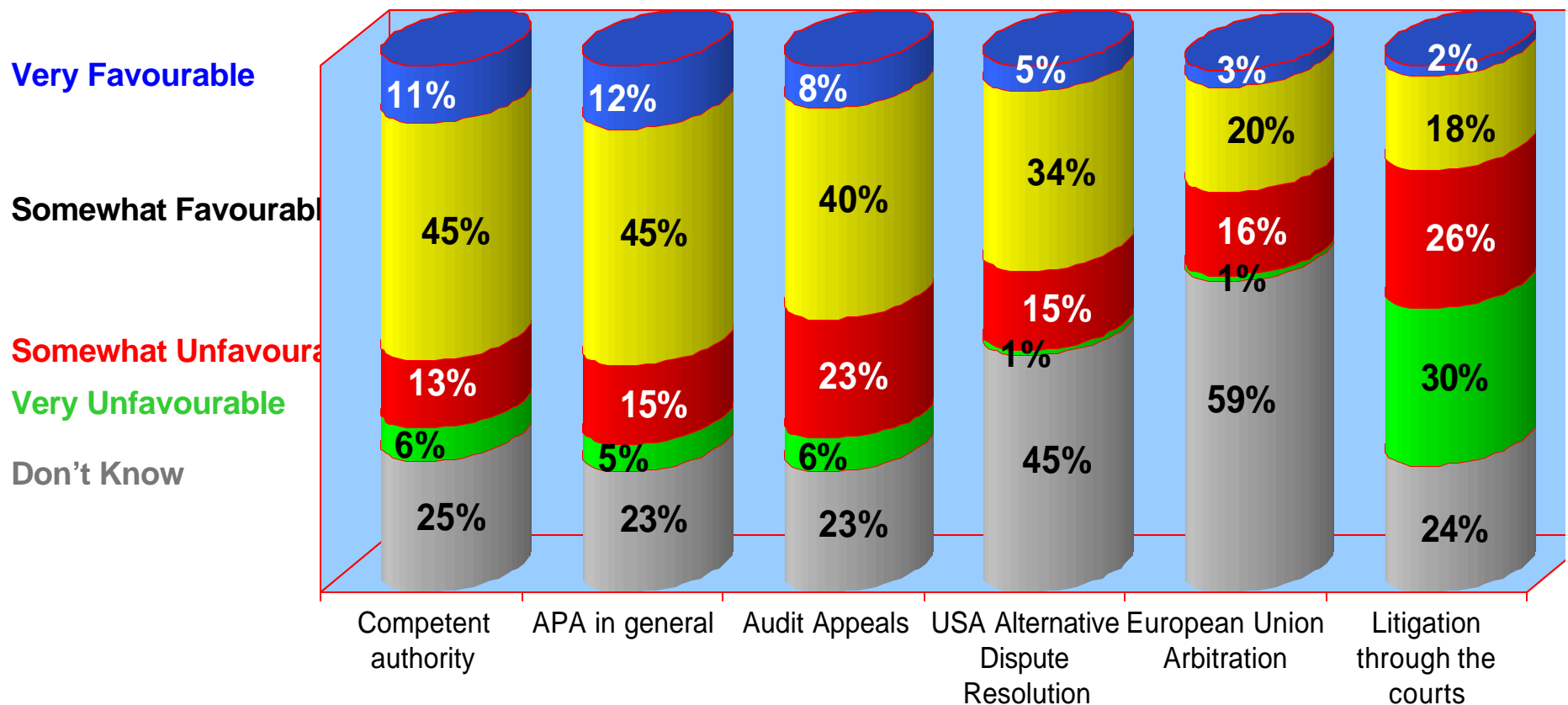
When asked which of these methods they would consider using in the future, 14% would not use any of the above mentioned methods.

Q. For each of the following dispute resolution methods, would you tell me (a) whether your company has used or applied to use, the method in the past and (b) whether your company would consider using the method in the future.

Impression of Different Methods to Resolve Transfer Pricing Disputes - Client Perspective -

- Clients tend to have favourable impressions of competent authority (56%), APAs in general (57%), and audit appeals.
- Among the dispute resolution methods tested, clearly, litigation is the least favoured with 56% saying their impression is somewhat or very unfavourable. Only one in five (20%) have an unfavourable impression of APAs in general.
- A large portion of clients are unfamiliar, and unable to comment on USA Alternative Dispute Resolution and European Union Arbitration.

Among Large/Medium Client Companies (n=191)

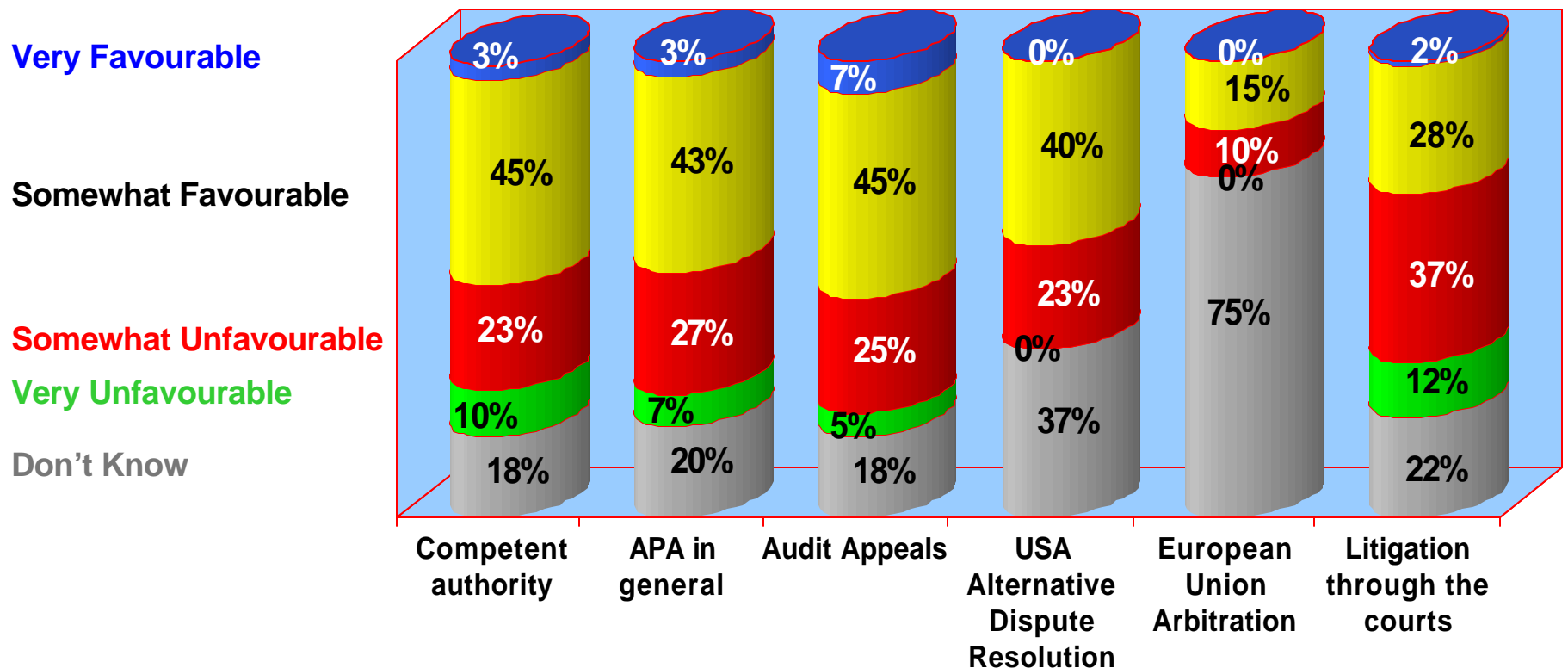


Q. There are different methods of dealing with disputes regarding international transfer pricing issues. What is your overall impression of each of the following methods of resolving disputes? Is it ... (Very Favourable, Somewhat Favourable, Somewhat Unfavourable, Very Unfavourable)

Impression of Different Methods to Resolve Transfer Pricing Disputes - Advisor Perspective -

- Advisors, like clients, are much less familiar with European Union Arbitration and USA Alternative Dispute Resolution than other dispute resolution mechanisms.
- Approximately three in ten (34%) advisors have an unfavourable impression of APAs in general.
- Similar to clients, advisors are less enthusiastic about litigation giving it a higher unfavourable impression rating.

Among External Tax Professionals (n=60)

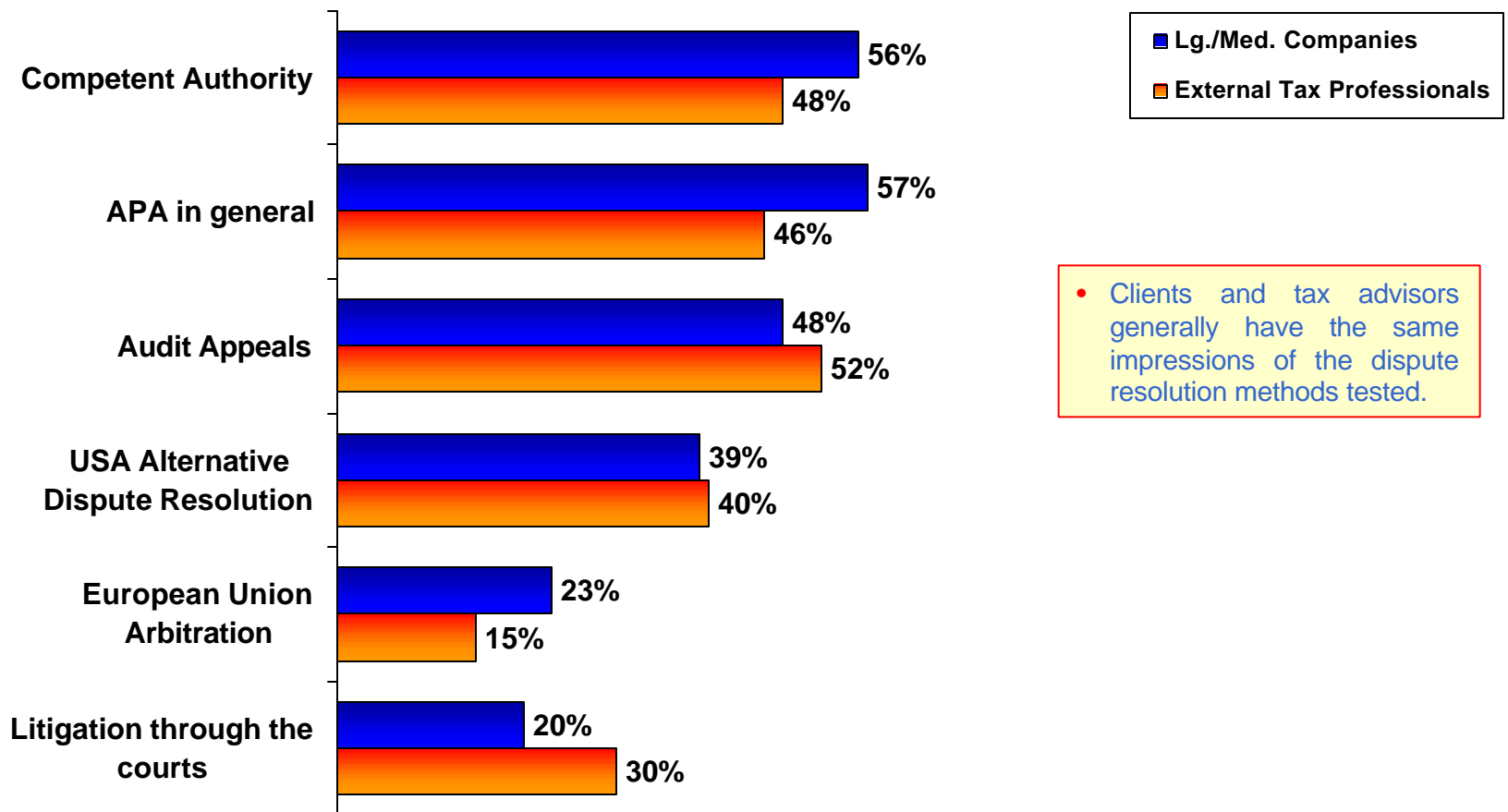


Q. There are different methods of dealing with disputes regarding international transfer pricing issues. What is your overall impression of each of the following methods of resolving disputes? Is it ... (Very Favourable, Somewhat Favourable, Somewhat Unfavourable, Very Unfavourable)

Summary Chart

Favourability of Clients vs. Advisors

% Saying "Favourable" (Very and Somewhat)



Q. There are different methods of dealing with disputes regarding international transfer pricing issues. What is your overall impression of each of the following methods of resolving disputes? Is it ... (Very Favourable, Somewhat Favourable, Somewhat Unfavourable, Very Unfavourable)

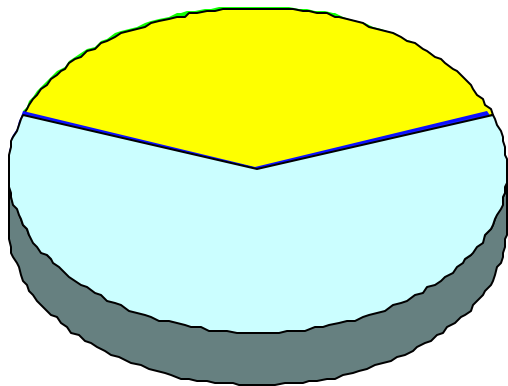


Awareness And Impression Of CCRA's APA Program

CCRA'S APA Program Has A Good Level Of Awareness With Both Clients And Advisors

Among Large/Medium Companies
(n=191)

Unaware
39%



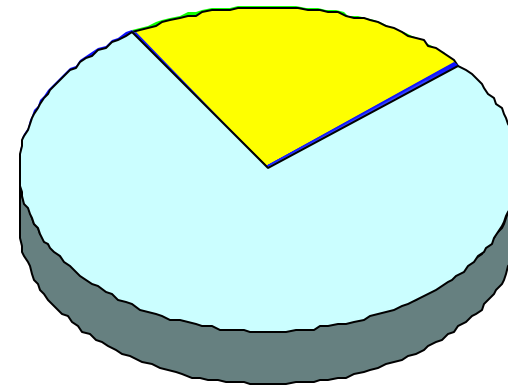
Aware
61%

Those most likely to be aware:

- Clients whose transfer pricing has been subject to audit (72%)
- Larger companies (68%)
- Companies with +\$1B Revenue (67%)

Among External Tax Professionals
(n=60)

Unaware
23%



Aware
77%

Those most likely to be aware:

- Advisors from larger tax firms (93%)
- Advisors who feel that international transfer pricing is a growing issue (82%)

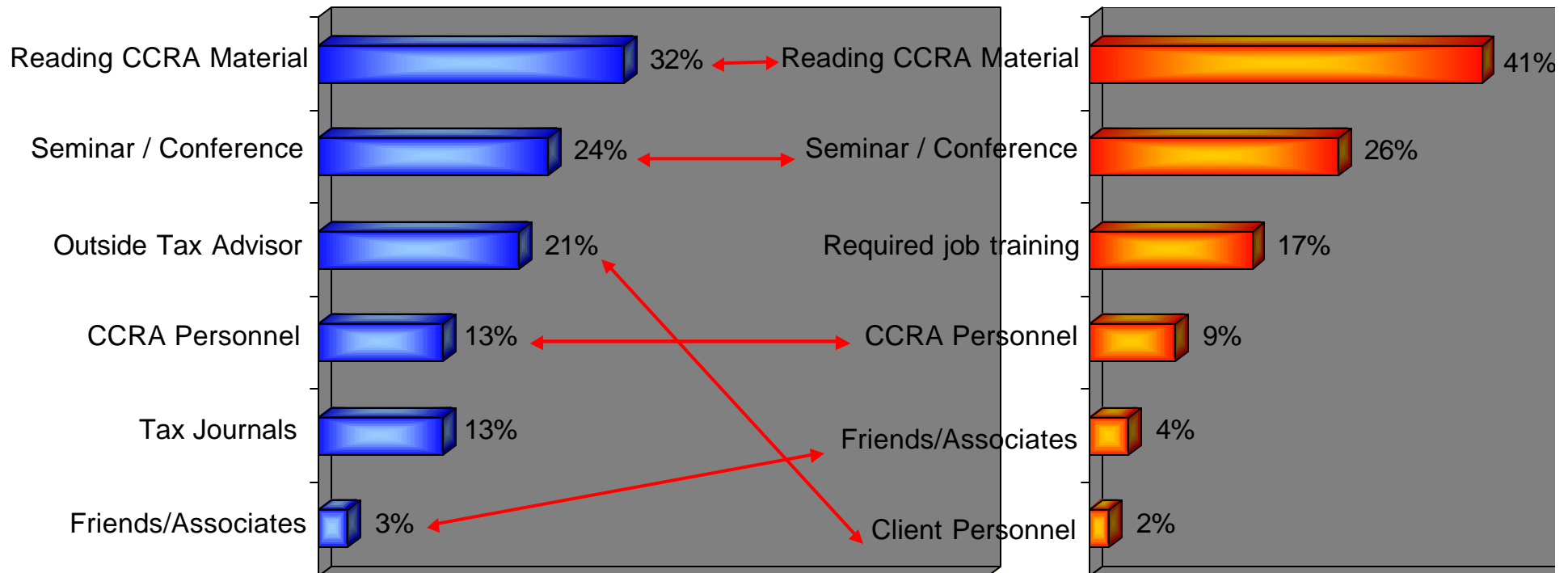
Q. Are you aware of the APA program operated by the Canada Customs and Revenue Agency?

Information Sources Creating An Awareness of CCRA's APA Program

- The arrows linking the two graphs below show that clients and advisors became aware of the APA program largely through similar means. CCRA materials and personnel play a significant role in creating awareness of the APA program.

Among Large/Medium Client Companies

Among External Tax Professionals

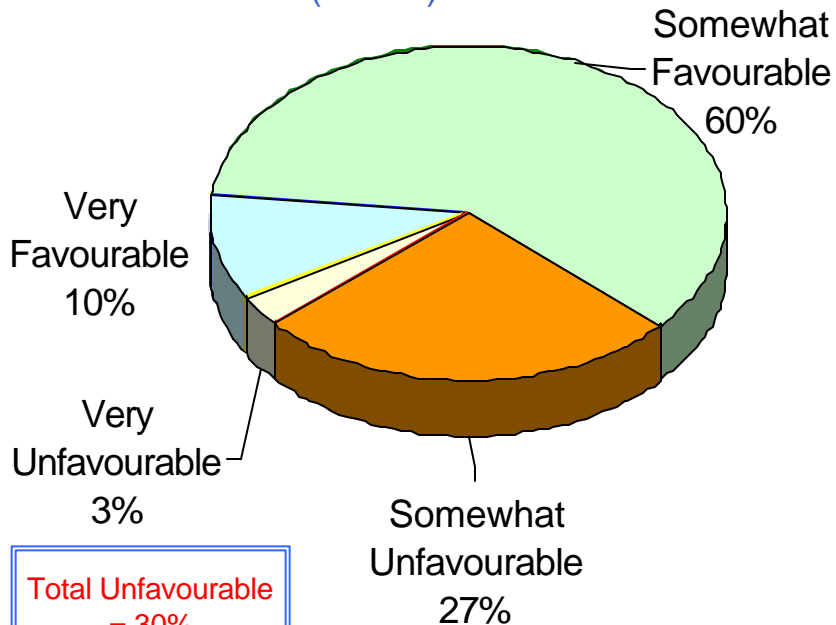


Q. How did you become aware of the APA program?

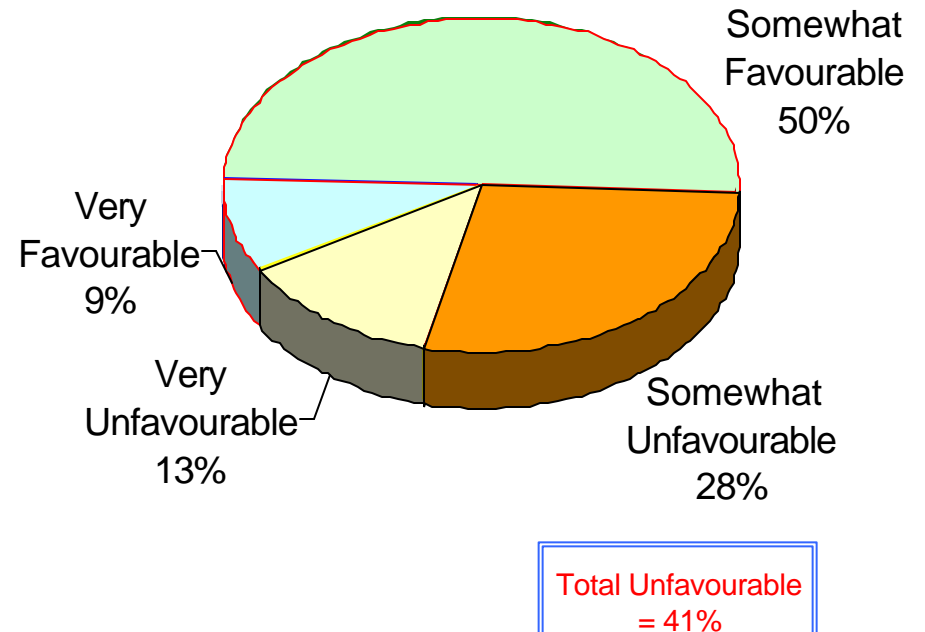
Clients And Tax Advisors Have A Somewhat Favourable Impression Of The CCRA APA Program

Overall Impression of CCRA's APA Program

Among Large/Medium Companies
who are aware of the Program
(n=117)



Among External Tax Professionals
who are aware of the Program
(n=46)



Those most likely to have a negative impression of the program:

- Those who have had their transfer pricing audited 38%
- Those who are unlikely to apply for an APA 37%
- Those who are unlikely to recommend it to others 73%
- Larger companies (+\$1Billion) 35%

There are no significant differences within the various data breaks.

Q. Based upon what you know or have heard, what is your overall impression of the APA program offered by CCRA? Do you have a very favourable, somewhat favourable, somewhat unfavourable, very unfavourable impression of the APA program?

Unaided Rationale for Favourable / Unfavourable Impressions of the APA

Reasons for Having a Favourable Impression

Among Large/Medium Client Companies...

- ✓ Advanced ruling / predefined (13%)
- ✓ Sound like a fair / reasonable solution (13%)
- ✓ Feel more confident / certainty (12%)
- ✓ Good long term solution to settlements (7%)
- ✓ Have heard good things about the program / good reputation (7%)

*Among External Tax Advisors... (*Small Base)

- ✓ Sounds like a fair / reasonable solution (48%)
- ✓ Have heard good things about the program / good reputation (22%)
- ✓ Faster / Quicker process (7%)
- ✓ Less rigid / more flexible (7%)
- ✓ Too new / lack experience to make it work smoothly (7%)

Reasons for Having an Unfavourable Impression

Among Large/Medium Client Companies...

- ✗ Time consuming / lengthy process (46%)
- ✗ Cumbersome/too much hassle/paperwork(13%)
- ✗ Price / too expensive (17%)
- ✗ Too complicated / difficult (14%)
- ✗ Risky divulging sensitive information (14%)

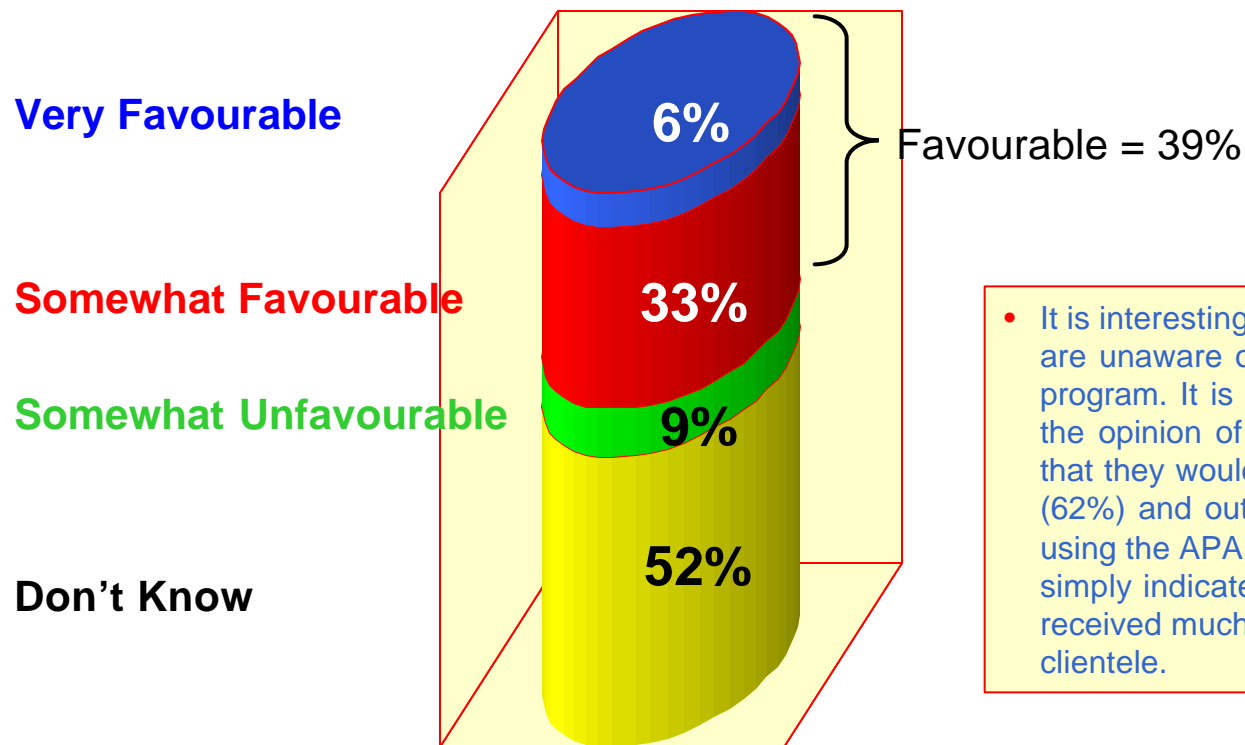
*Among External Tax Advisors... (*Small Base)

- ✗ Time consuming / lengthy process (47%)
- ✗ Cumbersome / too much hassle / paperwork (32%)
- ✗ Too complicated / difficult (21%)
- ✗ Poor philosophy / mindset of CCRA officials (11%)
- ✗ Price / too expensive (11%)

For the Most Part, Clients Are Unaware of How Their Advisors Feel About The APA Program

Client's Perception of How Their Outside Tax Advisors Feel About the APA

Among Large/Medium Companies
(n=191)



- It is interesting that such a large portion (52%) of clients are unaware of how their advisors feel about the APA program. It is simply not a case that they do not value the opinion of outside professionals. The majority say that they would rely most upon outside tax accountants (62%) and outside tax lawyers (25%) for advice about using the APA program. Consequently, this finding may simply indicate that the APA is not a topic that has yet received much “air time” between tax advisors and their clientele.

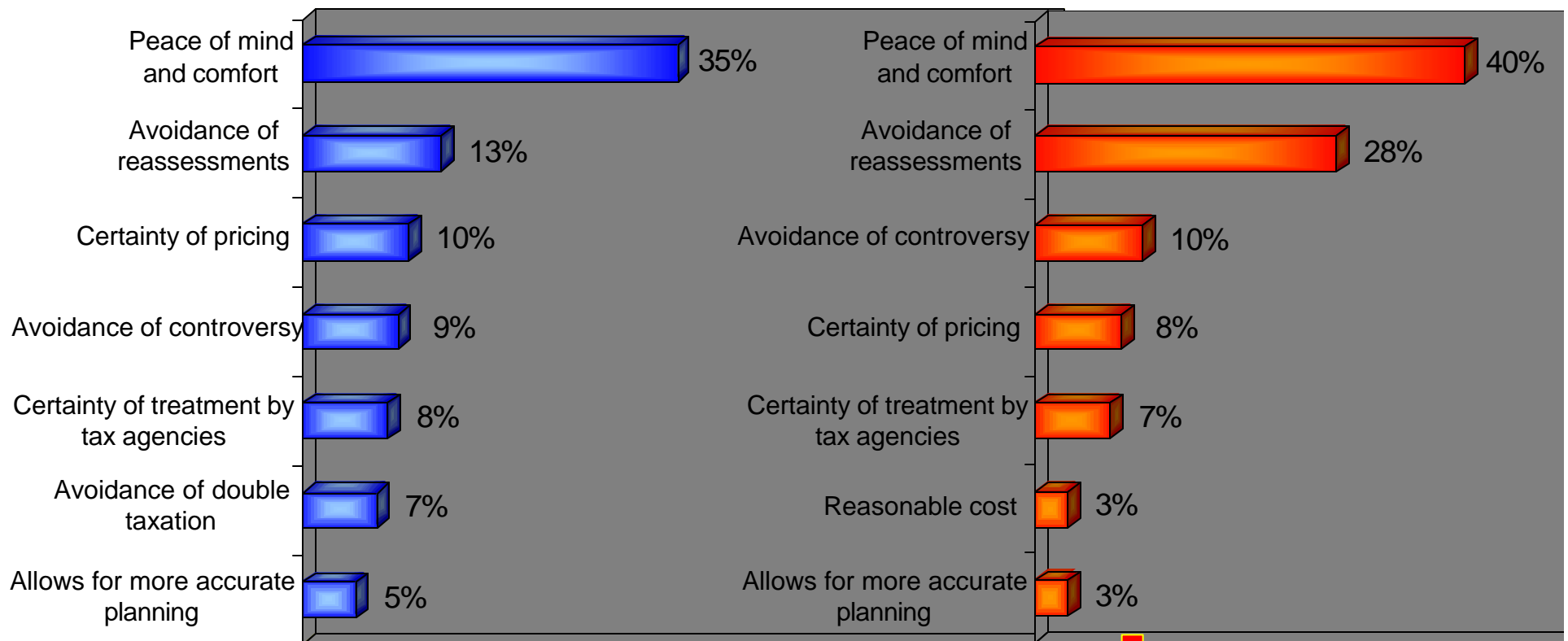
Q. (Asked only of Large/Medium Companies) Thinking about the outside tax advisors who provide your company with its main source of tax advice, what is their overall impression of the APA program offered by CCRA? Do they have a very favourable, somewhat favourable, somewhat unfavourable or very unfavourable impression of the program?

Top-of-Mind Benefits Associated With An APA

- Total Mentions, Unaided -

Among Large/Medium Client Companies (n=191)

Among External Tax Professionals (n=60)



Of note, 15% specifically say that there are no benefits of an APA for their company. An additional 12% are unable to respond to the question.

Significantly fewer (5%) advisors than clients (15%) feel that the APA has no benefits.

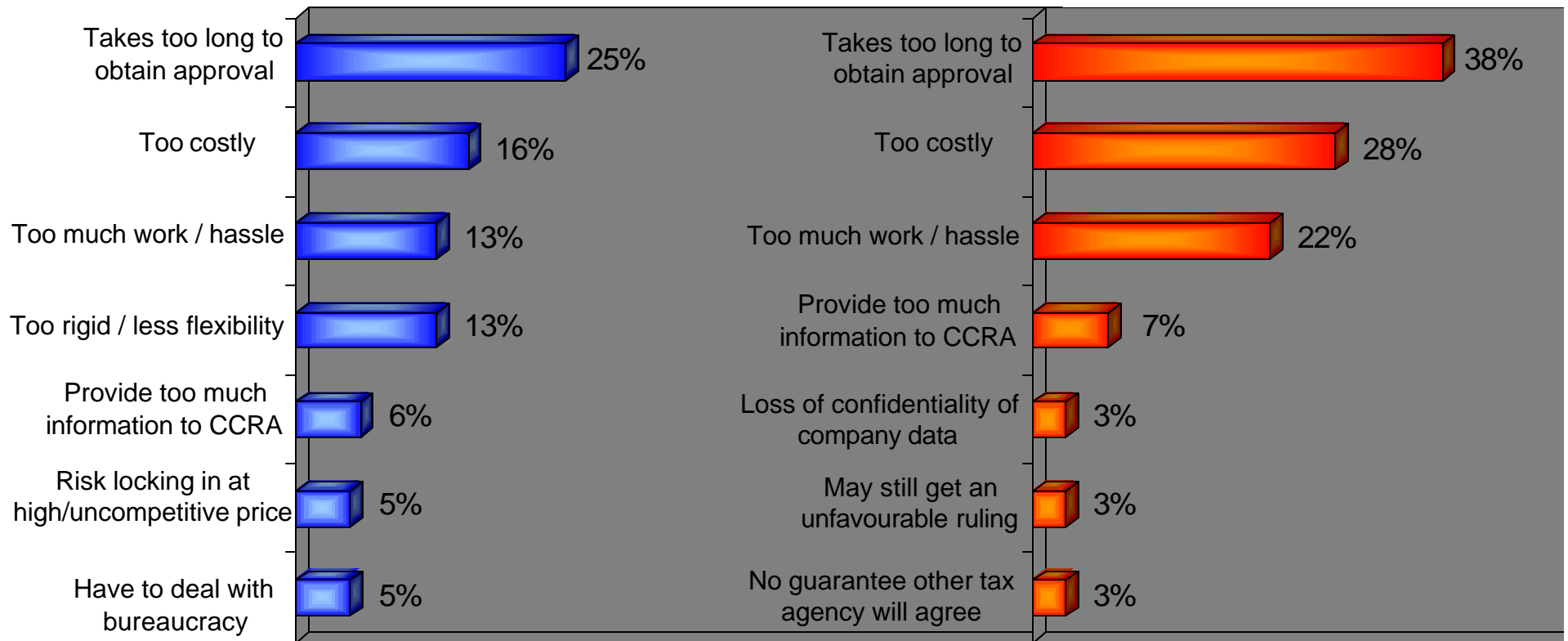
Q. In your opinion, what is, or what would be, the benefits of an Advance Pricing Arrangement (APA) for your company (your clients)?

Top-of-Mind Drawbacks Associated With An APA

- Total Mentions, Unaided -

Among Large/Medium Client Companies (n=191)

Among External Tax Professionals (n=60)



6% say they are not familiar with any disadvantages / drawbacks associated with the APA.

5% say they are not familiar with any disadvantages / drawbacks associated with the APA.

Q. In your opinion, what would be the drawbacks or disadvantages of an Advance Pricing Arrangement (APA) for your company (your clients)?

Avoidance Of Double Taxation, Reassessments And Penalties, And Certainty Of Treatment Are The Most Important Benefits Associated With An APA

- There are few significant differences in attitudes between clients and advisors.

Importance of Benefit	% Saving Important (8, 9, 10 on Scale of 1-10)	
	Large / Medium Clients (n=191)	External Tax Professionals (n=60)
Avoidance of double taxation	71	70
Avoidance of Reassessments and Penalties	69	78
Certainty of Treatment By CCRA and Other Tax Authorities	67	80
Avoidance of Controversy and Legal Challenges	56	67
Peace of Mind and Comfort for Senior Executives	46	50
Reduced Audit Defense Costs In Future	42	43
Satisfies Requirements Under Section 247	37	48
Ability to Use APA to Clear Up Past Problems	30	35

Q. In your opinion, what is or what would be, the benefits of an Advance Pricing Arrangement for your company (your clients)?
(Unaided)

Overview Of Agreement Statements By Clients

Among Large/Medium Client Companies (n=191)

	% AGREE	% DISAGREE	NET SCORE
One of Main Benefits is Certainty of Treatment	85	5	+80
APA Process Takes Much Too Long	59	9	+50
APA is Geared Primarily to Elimination of Double Taxation	68	24	+44
An Effective APA Program Would Assist Canada In Attracting Investment	60	31	+29
The APA Provides Complete Confidentiality of Company Information	49	23	+26
The APA is Only of Use For Very Large Companies	52	37	+15
I Would Generally Recommend The APA Program to Other Companies	44	29	+15
The APA is an Adversarial Approach For The Resolution of Pricing Issues	38	47	-9

Q. Based upon what you know or may have heard, please indicate the extent to which you agree with each of the following statements as it relates to the APA program offered by Canada Customs and Revenue Agency. Do you agree strongly, agree, disagree, or disagree strongly with the following statements?

Overview Of Agreement Statements By Tax Advisors

Among External Tax Professionals (n=60)

	% AGREE	% DISAGREE	NET SCORE
One of Main Benefits is Certainty of Treatment	83	7	+76
APA Process Takes Much Too Long	80	3	+77
The APA is Only of Use For Very Large Companies	72	13	+59
APA is Geared Primarily to Elimination of Double Taxation	75	17	+58
The APA Provides Complete Confidentiality of Company Information	65	17	+48
I Would Generally Recommend The APA Program to Other Companies	57	28	+29
An Effective APA Program Would Assist Canada In Attracting Investment	57	32	+25
The APA is an Adversarial Approach For The Resolution of Pricing Issues	40	45	-5

Q. Based upon what you know or may have heard, please indicate the extent to which you agree with each of the following statements as it relates to the APA program offered by Canada Customs and Revenue Agency. Do you agree strongly, agree, disagree, or disagree strongly with the following statements?

Comparison Of Attitudes Of Clients And Advisors To APA Program

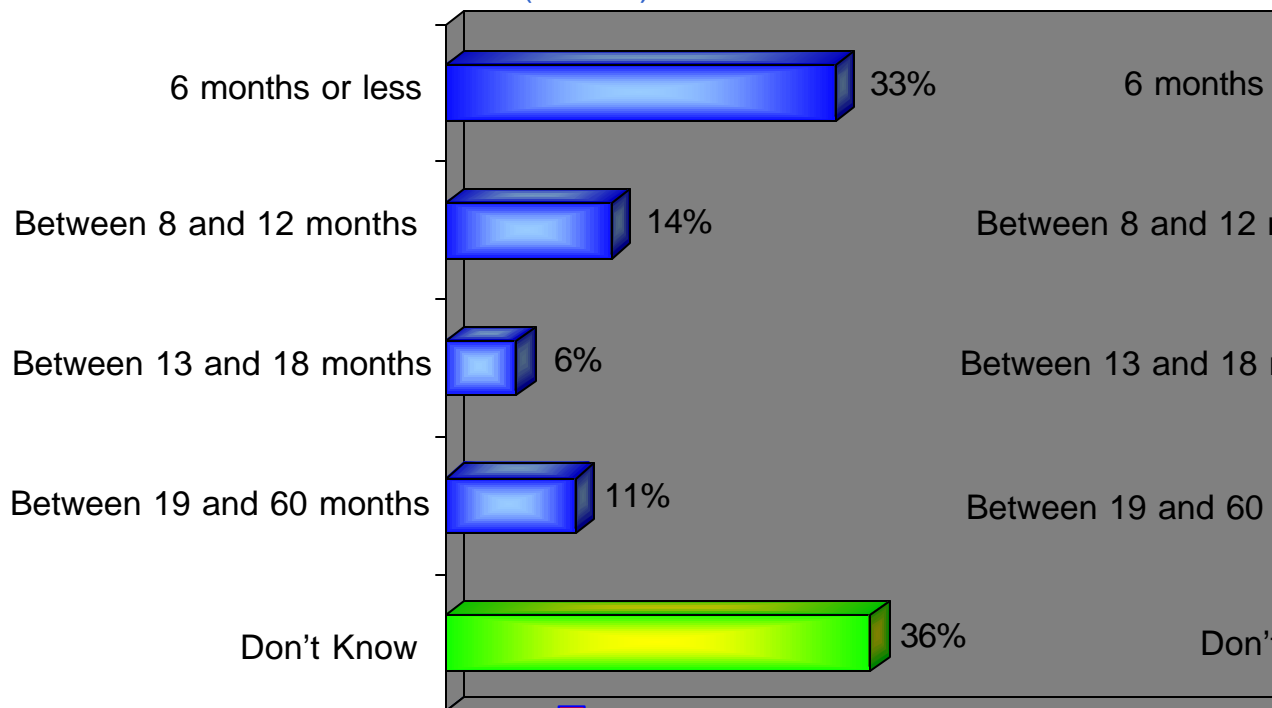
- Certainty of Treatment is seen as the strongest benefit of the APA program by both clients and tax advisors.
- There is very high agreement among both groups that the APA takes much too long to complete, and that it is geared primarily to the elimination of double taxation.

	Net Score Clients (n=191)	Net Score Advisors (n=60)
One of Main Benefits is Certainty of Treatment	+82	+76
APA Process Takes Much Too Long	+72	+77
APA is Geared Primarily to Elimination of Double Taxation	+66	+58
An Effective APA Program Would Assist Canada In Attracting Investment	+55	+25
The APA Provides Complete Confidentiality of Company Information	+45	+48
The APA is Only of Use For Very Large Companies	+39	+59
I Would Generally Recommend The APA Program to Other Companies	+24	+29
The APA is an Adversarial Approach For The Resolution of Pricing Issues	-14	-5

On Average, Clients and Advisors Perceive That An APA Takes Between 12 and 15 Months To Complete

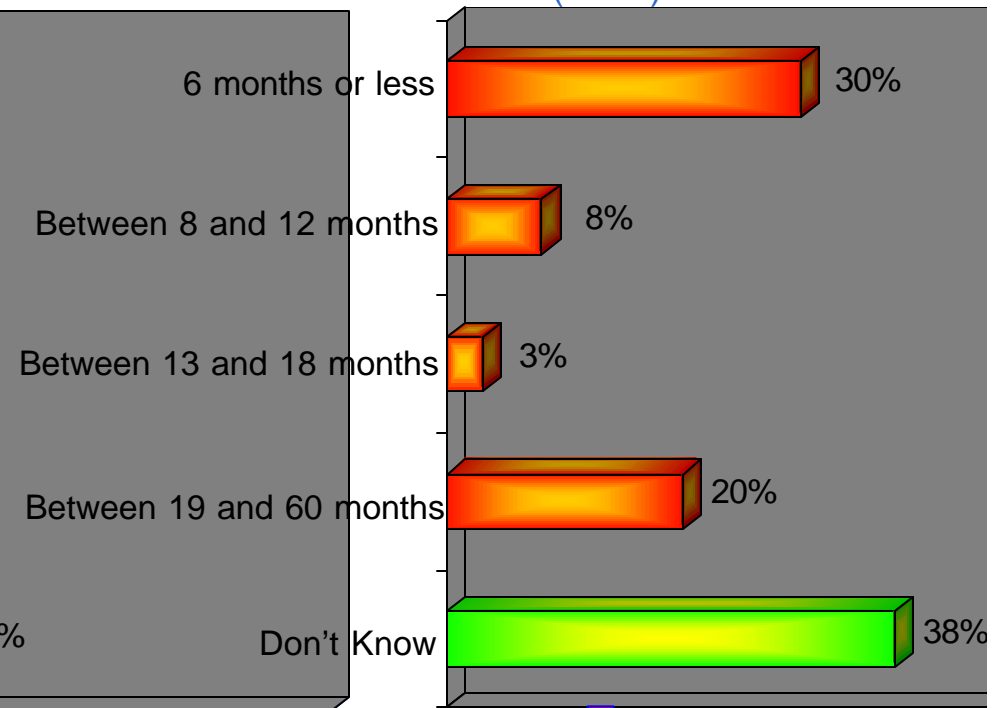
Perception of Length of Time to Complete an APA (months)

Among Large/Medium Client Companies
(n=191)



Average = 11.5 months

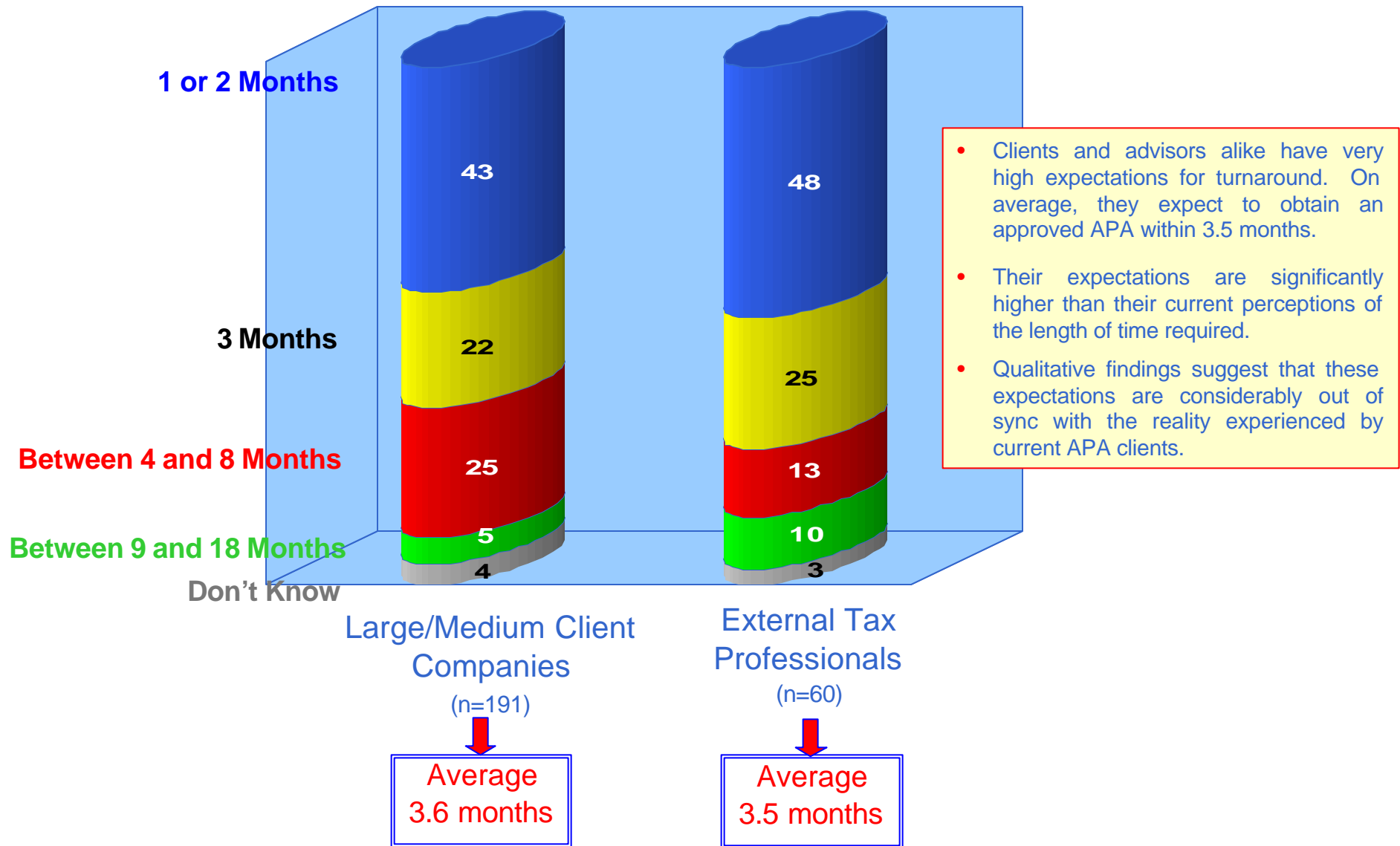
Among External Tax Professionals
(n=60)



Average = 14.8 months

Clients and Advisors Have Very Demanding Expectations For APA Turn-Around

Expectation of Length of Time to Obtain an APA (months)



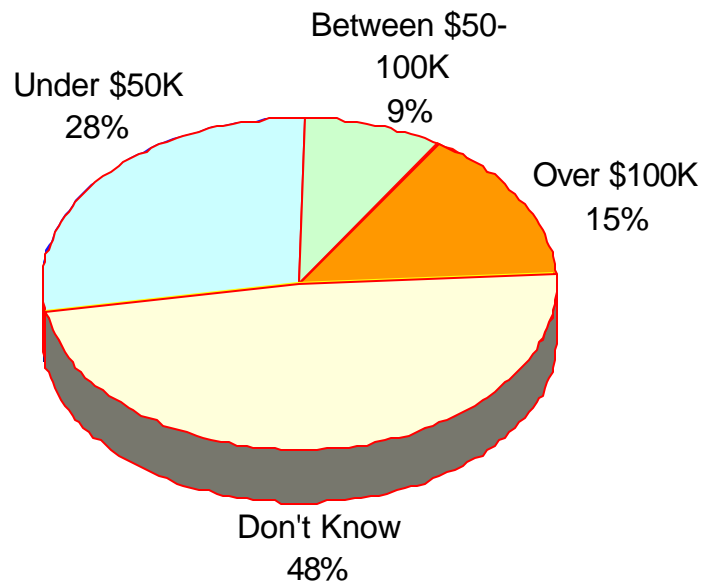
Q. How many months (years) would you expect it should take to obtain an approved APA?

Most Have No Perception Of The Costs Associated With Obtaining An APA

- A large proportion of both clients and advisors have no perception of the internal and external costs associated with obtaining an APA.
- Of those who do have a perception, most tend to feel it costs under \$50,000. A small number of clients and advisors perceive the costs to be several million dollars. These individuals are responsible for pulling up the overall average.

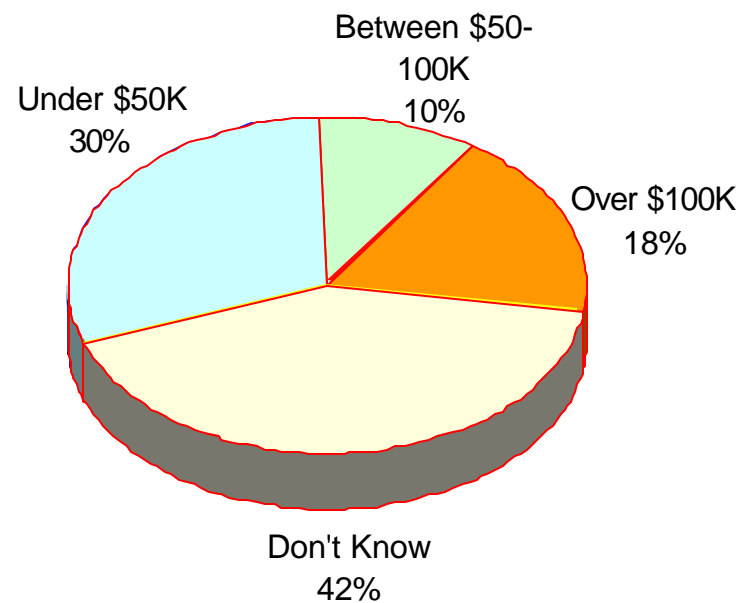
Perception of Internal & External Costs to Complete an APA (\$)

Among Large/Medium Companies
(n=191)



Average
\$288.4K

Among External Tax Professionals
(n=60)



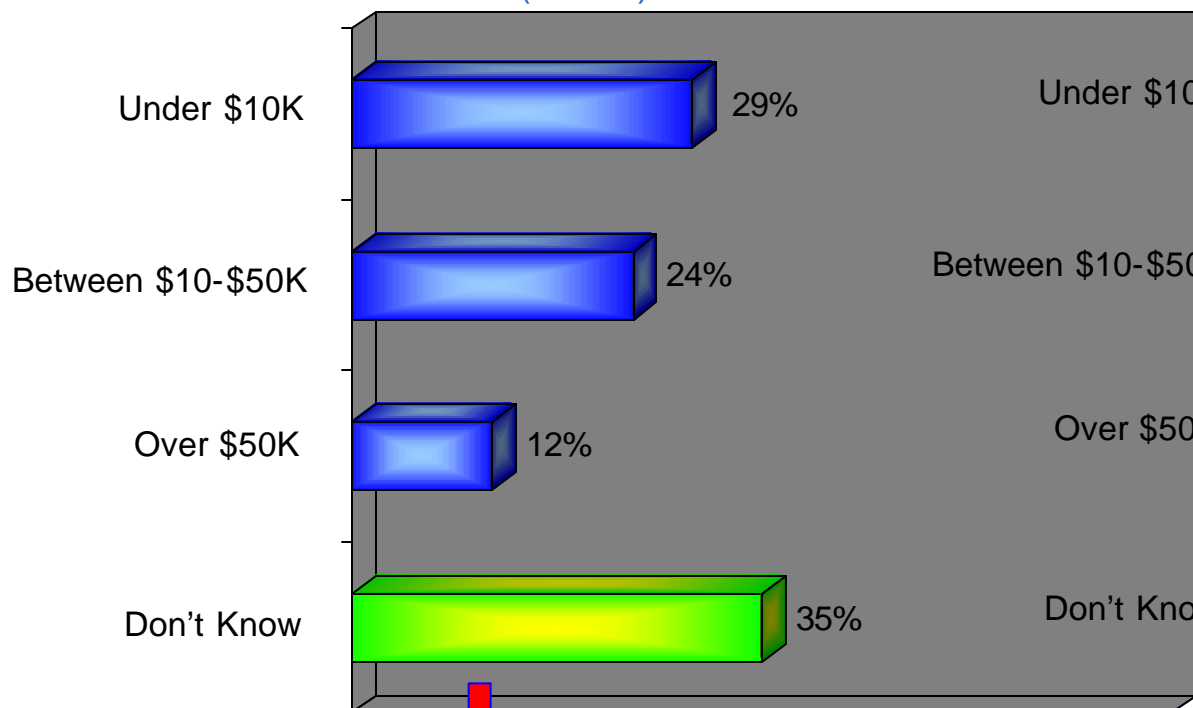
Average
\$250.5K

Current Cost Perceptions Are Considerably Higher Than Cost Expectations to Complete an APA

- For both clients and advisors, current costs perceptions are considerably higher than cost expectations to complete an APA.
- A hand full of advisors are pulling up the overall average for expected costs such that it is considerably higher than the costs expected by clients. This having been said, the largest proportion of advisors say costs should be below \$10K.

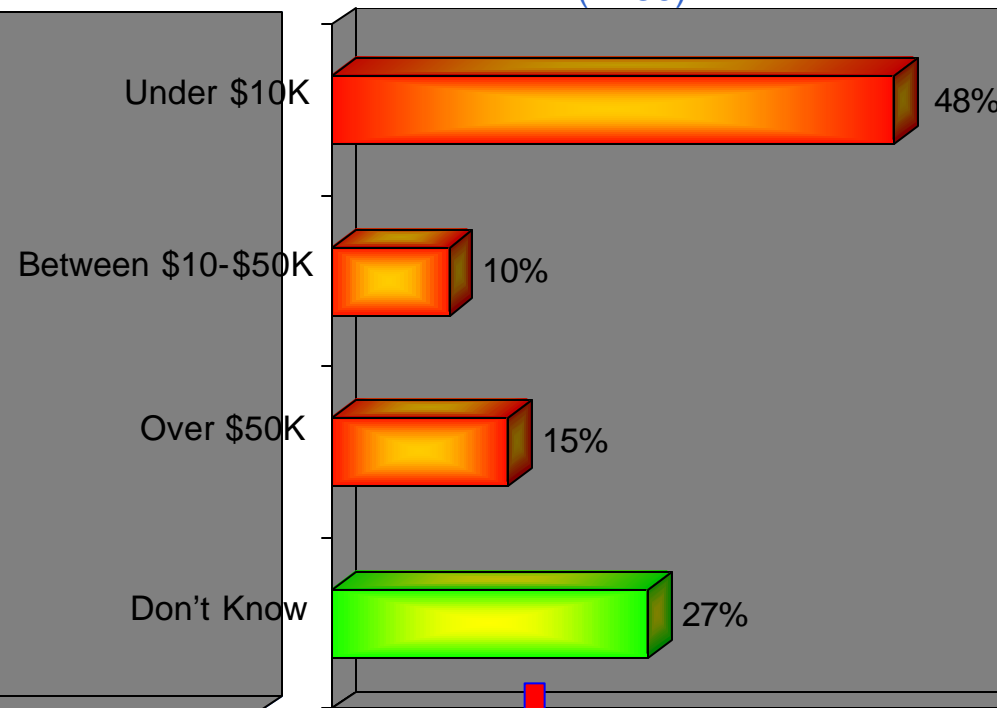
Expectation of Internal & External Costs to Complete an APA (\$)

Among Large/Medium Client Companies
(n=191)



Average
\$65.8K

Among External Tax Professionals
(n=60)



Average
\$88.5K

Q. What would you expect that it should cost to obtain an approved APA?

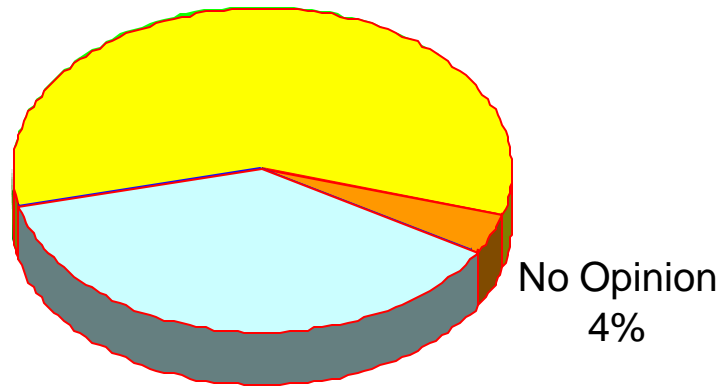
Clients And Advisors Approve Of Practice Of Billing Client For Travel Expenses

- External tax professionals are significantly more likely to approve of the practice of CCRA billing back associated travel expenses at cost. This may be related to the fact that, as external consultants, they are more familiar with the concept of billing clients back for out-of-pocket costs associated with projects.

Among Large/Medium Companies

(n=191)

Approve
58%



Disapprove
38%

No Opinion
4%

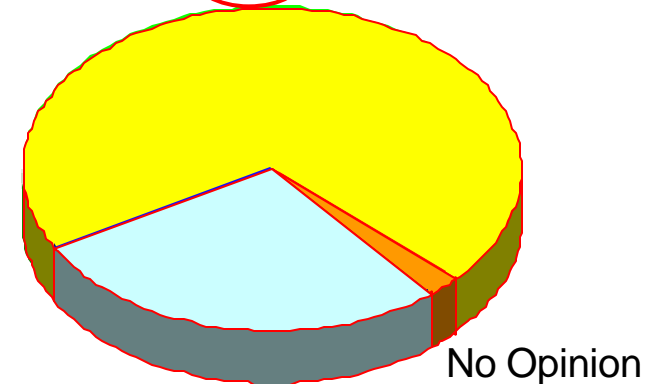
Those most likely to disapprove of charging back:

- Clients who feel that CCRA is the primary beneficiary of the APA program (63%)
- Companies with +\$1B Revenue (43%)
- Subsidiaries (55%)

Among External Tax Professionals

(n=60)

Approve
70%



Disapprove
28%

No Opinion
2%

Those most likely to disapprove of charging back:

- Advisors from smaller firms (43%)

Q. The current practice of the Agency while undertaking the travel necessary to pursue an APA is to follow the user pay principle and bill the applying company for those expenses. Do you approve or disapprove of this practice?

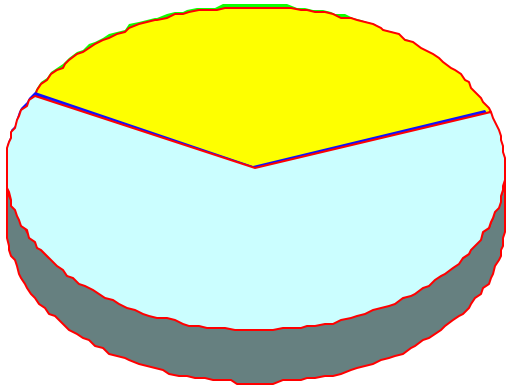
Terms And Conditions Of APA Should Be Applied To Cover 3 Previous Years

- External tax professionals are significantly more likely than clients to feel that the terms and conditions of an APA should be applied to cover previous years. Both groups feel that 3 years is a reasonable period for which the conditions should be applied back to cover.

Among Large/Medium Companies

(n=191)

No
37%



Yes
63%

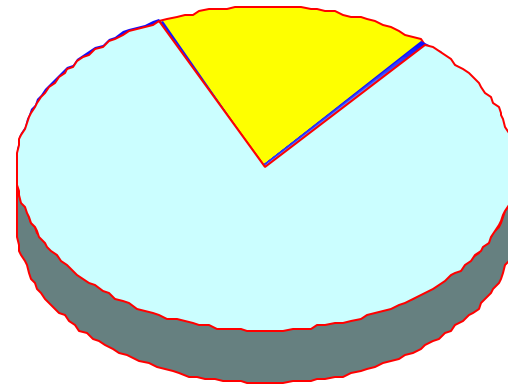


On average, clients feel that the terms and conditions of the APA should be extended back for a period of 3.5 years.

Among External Tax Professionals

(n=60)

No
18%



Yes
82%



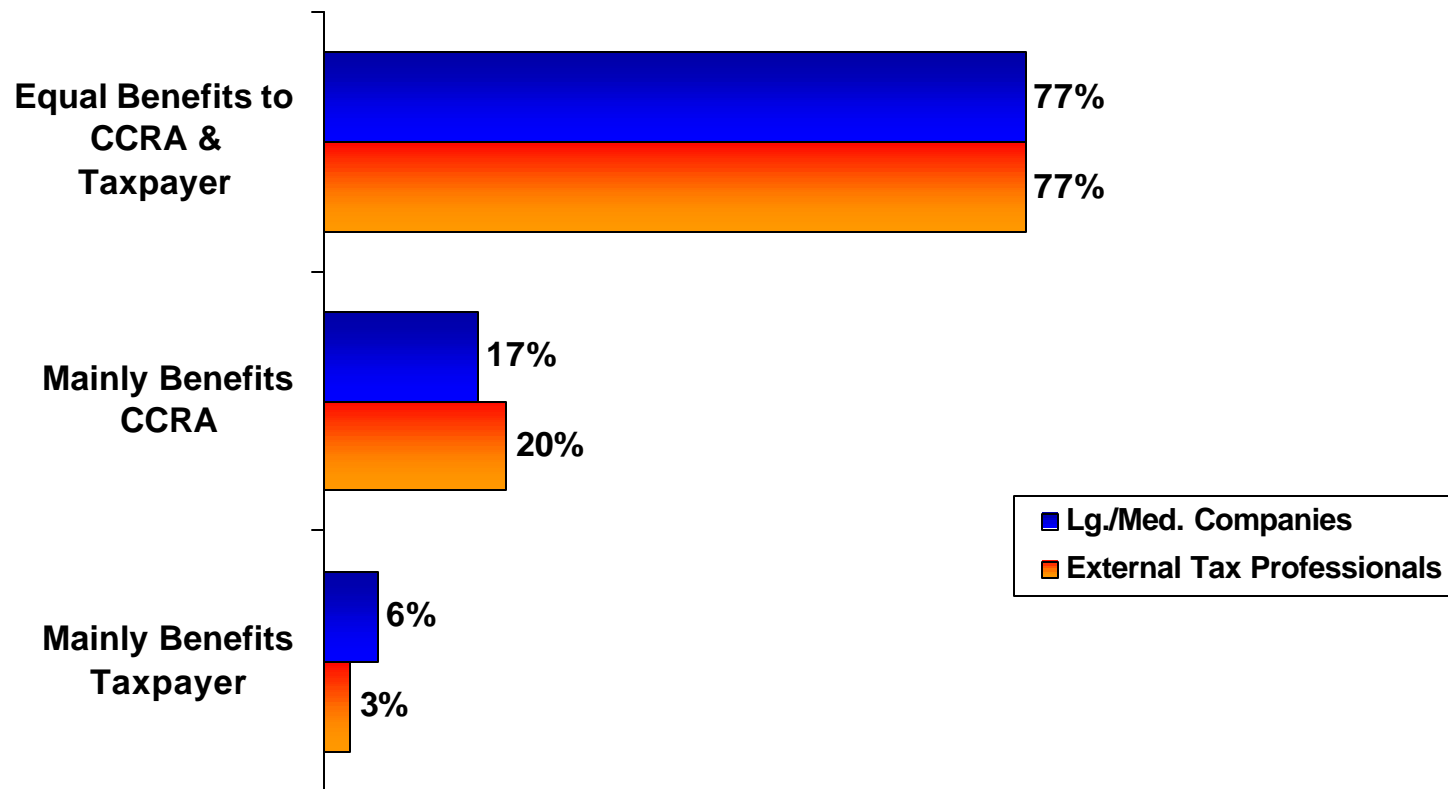
On average, advisors feel that the terms and conditions of the APA should be extended back for a period of 3.3 years.

Q. Once an APA is approved would you like to see the terms and conditions of the APA applied to cover previous years?

The APA Program Provides Equal Benefits To The Taxpayers And CCRA

- The vast majority of both groups feel that the APA equally benefits the taxpayer and CCRA. There is, however, approximately one in five who feel that a disproportionate share of the benefit goes to the tax authority. This suggests that a segment of potential applicants needs to be better informed about how their companies can benefit from the program.
- It is interesting to note that those respondents who have an unfavourable opinion of the APA program tend to be more likely to feel that CCRA gets the lion's share of the benefits.

Statement Closest To How They Personally Feel



Q. Which of the following statements regarding the benefits of an APA program with CCRA is closest to how you personally feel?

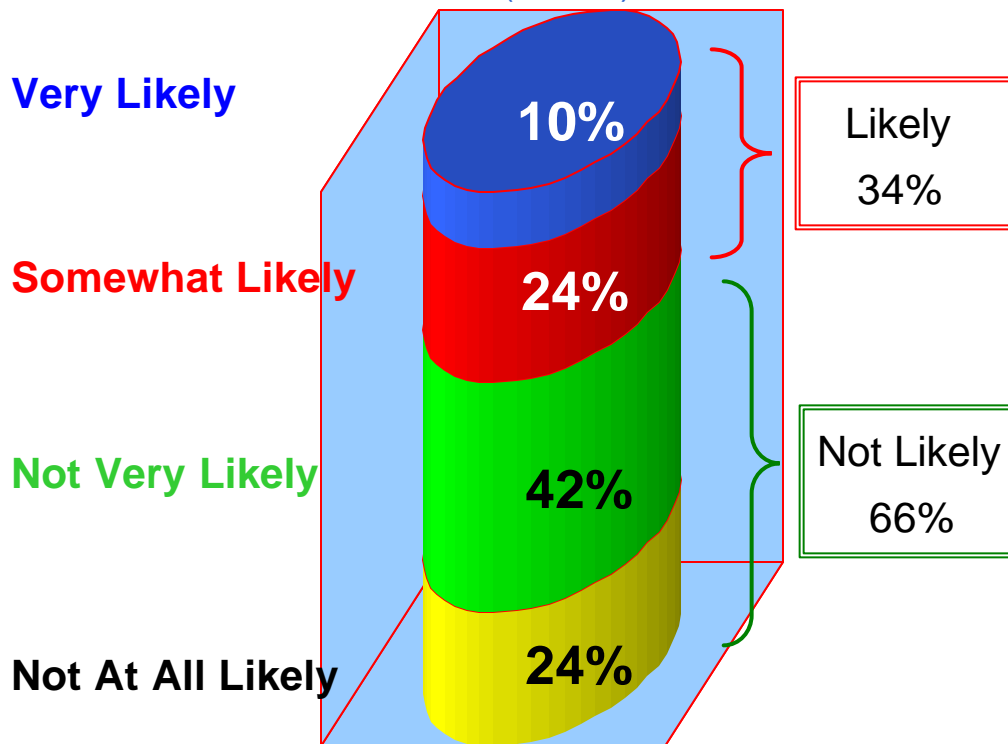


Potential Size Of APA Market

Likelihood of Medium and Large Companies Applying For An APA (Next Few Years)

Likelihood of Medium and Large Companies Applying for An APA
(Next Few Years)

Among Large/Medium Companies
(n=191)



Those who say 'Likely' tend to be:

- Companies previously unaware of the APA program (46% compared to 26% among those aware of APA)
- Companies with a favourable impression of the APA (33% compared to 9% among those with an unfavourable impression)
- Companies with less than \$1B in revenue (46% compared to 29% among those with revenues exceeding \$1B)
- Companies who feel transfer pricing is growing in importance

Q. How likely would it be that your company might apply for an APA within the next few years? Is it ... (Very likely, Somewhat likely, Not very likely, Not at all likely)

Stated Reasons For Being Likely / Unlikely To Use APA in the Future

Among Large/Medium Client Companies

Arguments for Being Likely to Use APA (n=64)

- ✓ Future security / certainty / insurance (20%)
- ✓ Heavily involved with international business (14%)
- ✓ Sounds like a good idea (11%)
- ✓ We are experiencing growth (11%)
- ✓ It would be beneficial (general mention) (9%)
- ✓ To avoid double taxation (3%)
- ✓ We have transfer pricing issues (3%)

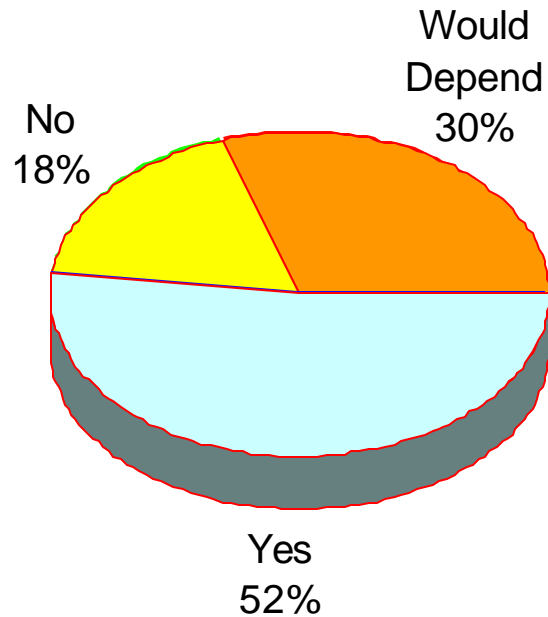
Arguments for Being Unlikely to Use APA (n=127)

- ✗ Can handle issues internally (18%)
- ✗ Unnecessary for a small company like ours (11%)
- ✗ No benefits for our company (10%)
- ✗ Too expensive (9%)
- ✗ Don't know enough about the program (9%)
- ✗ Our transfer pricing issues are simple (8%)
- ✗ Comfortable with our current methodology (6%)
- ✗ Time consuming / inefficient (6%)
- ✗ Not a priority / Have other more pressing issues (6%)

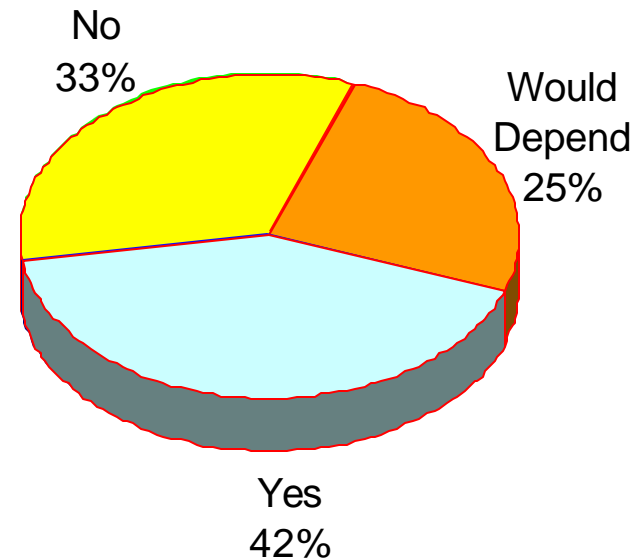
Incidence of Advisors Recommending APA

Among External Tax Professionals
(n=60)

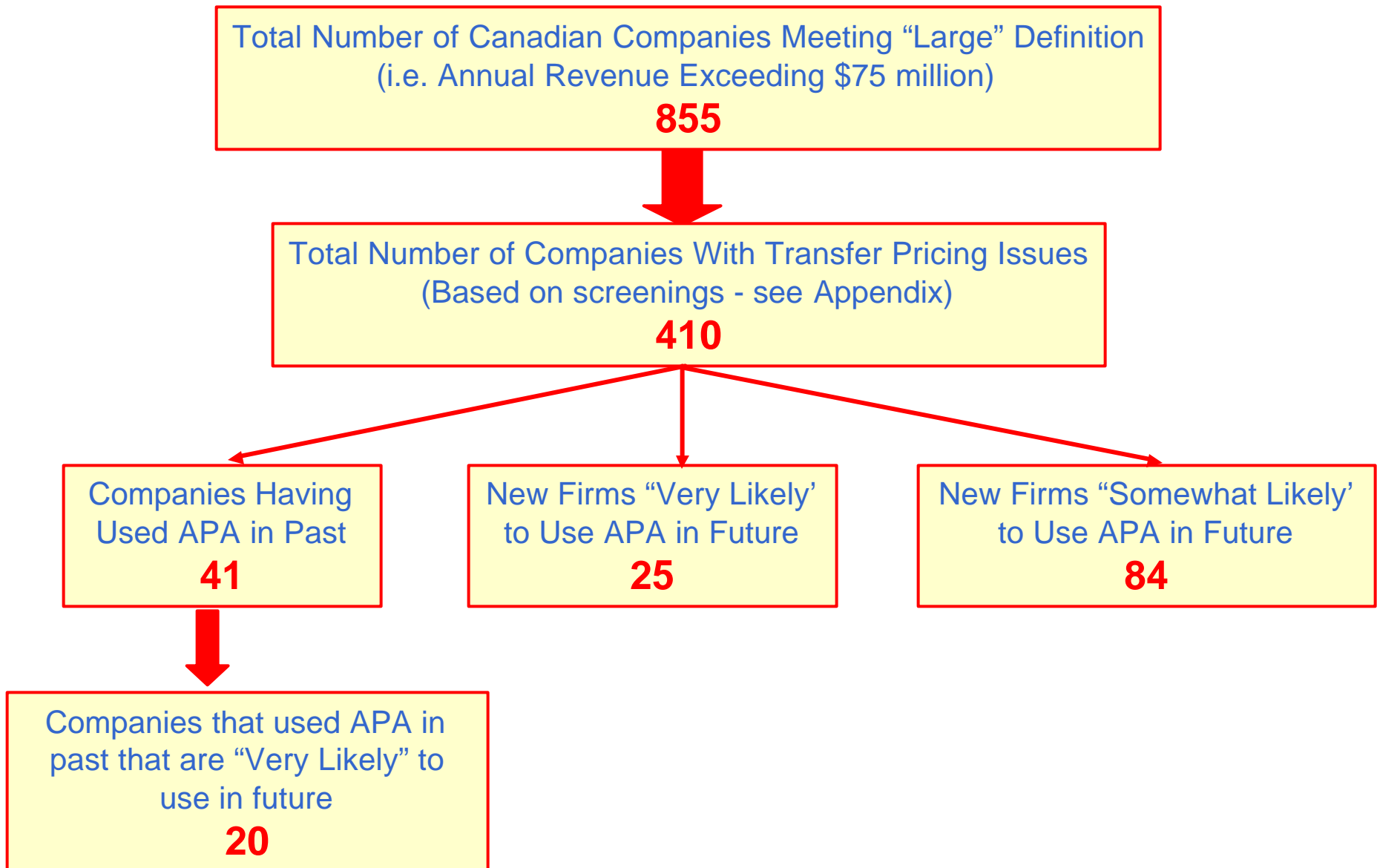
Would you recommend an APA to a **large company** with international transfer pricing issues?



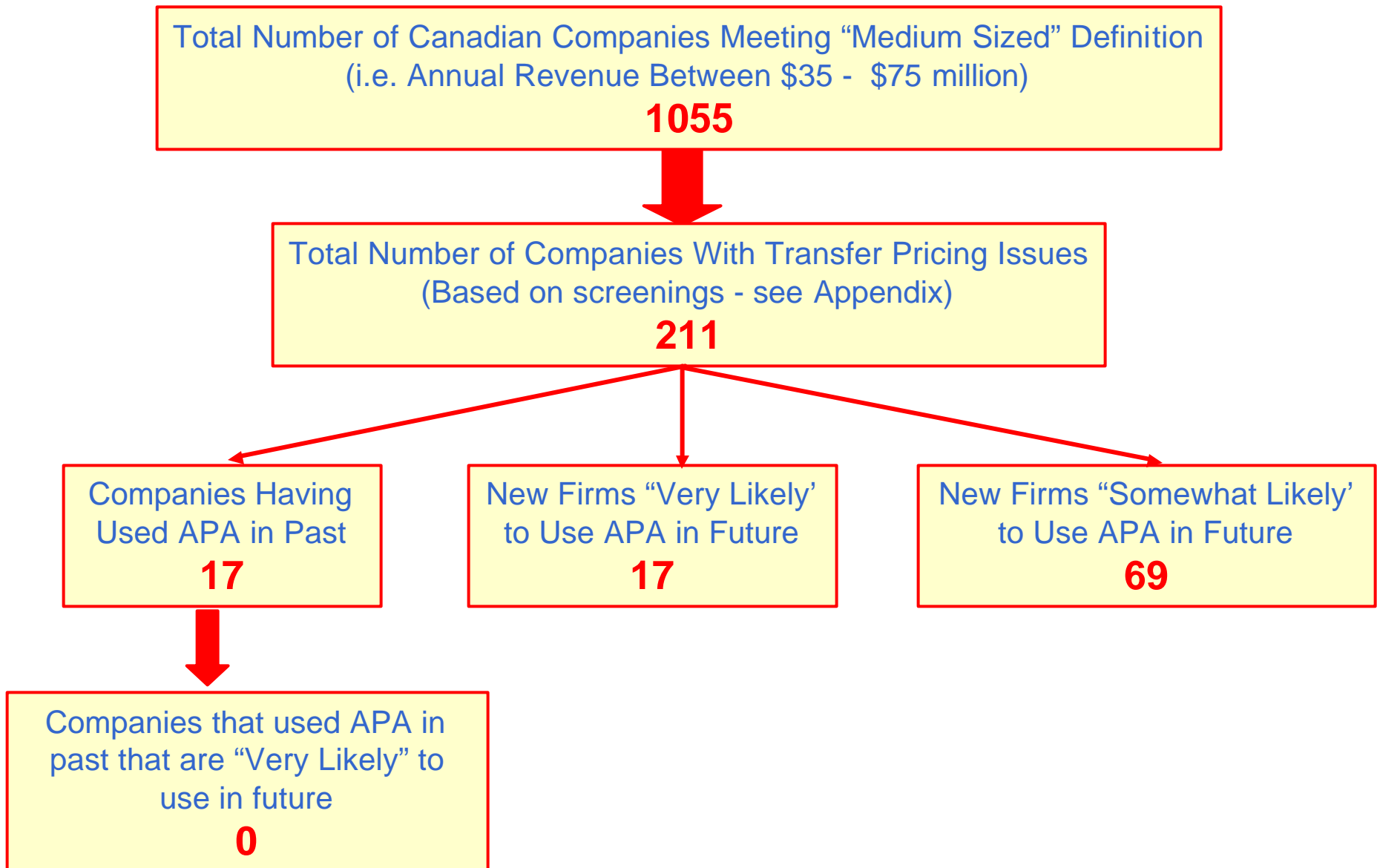
Would you recommend an APA to a **medium sized company** with international transfer pricing issues?



Estimated Size of Market For APA In Next Few Years - Large Companies -



Estimated Size of Market For APA In Next Few Years - Medium Companies -



Profile Of Respondents

“Firmographics”

Among Large / Medium Companies

Industry Sector

Manufacturing	→	24%
Resources	→	21%
Financial Services	→	15%
High Technology	→	14%
Utilities	→	4%
Communications	→	4%
Pharmaceuticals	→	2%
Refused	→	16%

Public vs. Private Company

Public	→	82%
Private	→	18%

Parent Company vs. Subsidiary

Subsidiary	→	20%
Parent	→	80%

Revenue

Under \$1 Billion	→	31%
Over \$1 Billion	→	69%

Among External Advisors

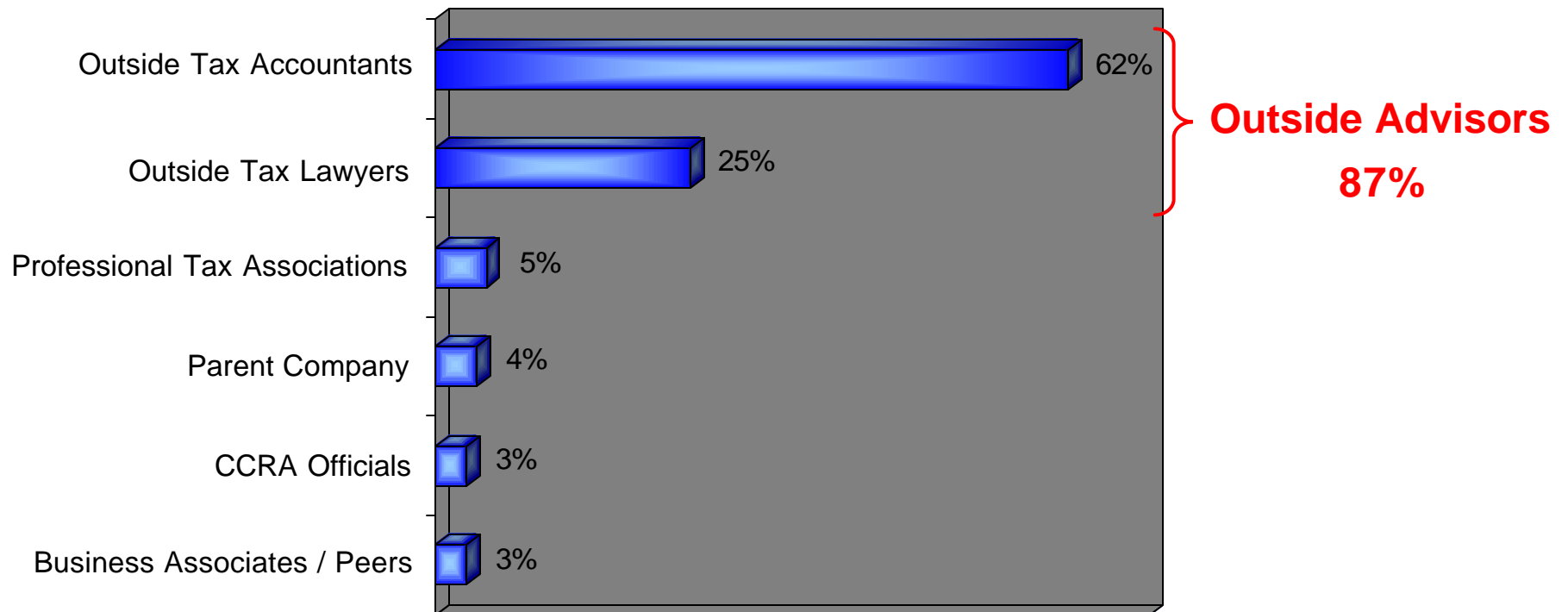
No. of Advisors in Firm (Canada wide)

Under 5 advisors	→	50%
Over 5 advisors	→	50%
<i>Average</i>	→	<i>67.3</i>

Groups / Individuals Clients Most Rely Upon for APA Advice

- The overwhelming majority of clients say they would seek APA advice from outside advisors. This speaks to the importance of CCRA keeping advisors on-side, and well versed about the APA so that they act as advocates rather than opponents.

Among Large/Medium Client Companies
(n=191)





Appendices