



# TaxNewsFlash Canada

## Canada to Implement Country-by-Country Reporting in 2016

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Canadian parent companies of large multinational corporate groups should start developing their strategy to meet new country-by-country reporting requirements coming in 2016. The standards for these requirements, which were developed by the OECD, are intended to enhance tax transparency and to provide adequate information to conduct transfer pricing risk assessments. This reporting will be required for taxation years beginning after 2015, with the first automatic exchanges of information between governments slated to begin by June 2018.

Although Finance is expected to release draft legislation for country-by-country reporting rules shortly, the 2016 federal budget provided some important details about how Canada will implement these new requirements. These details will help companies begin to decide the most appropriate approach to develop their country-by-country report. Specifically, affected Canadian companies should now:

- Identify a cross-functional team to lead the development of a country-by-country report (e.g., include members from tax, accounting, IT, human resources and legal groups)
- Detect gaps in available data, refine the data gathering process and test the reporting processes using 2015 data as a dry run for the 2016 reporting
- Validate tax reporting results and identify potential risks and inconsistencies within the existing structure
- Identify cost-effective technology to capture, analyze and report high quality data.

### Background

Country-by-country reporting of operational and financial information is part of new transfer pricing reporting standards developed under Action 13 of the OECD's project to reduce base erosion and profit shifting (BEPS) by multinational enterprises.

The OECD released the final details for implementing a new country-by-country reporting plan in October 2015. This implementation package is intended to allow tax administrations to obtain a complete understanding of the way multinational enterprises structure their operations, while safeguarding the confidentiality of such information.

The implementation package consists of model legislation requiring the parent entity of a multinational group to file the country-by-country report in its jurisdiction of residence. The package also includes three model competent authority agreements to facilitate the exchange of country-by-country reports.

The OECD recommended a three-tiered approach to documentation that includes preparing the following:

- Country-by-country report — Financial metrics for each country in which the multinational enterprise operates, including revenue, income, taxes and indicators of economic activity
- Master file — Additional information on the operations and economic analyses of intercompany transactions including how the multinational enterprise operates and its key intra-group transactions
- Local file — Information about how the intra-group transactions of an individual entity conform to the arm's length principle for transfer pricing.

The OECD recommended that country-by-country reporting be implemented for any taxation year of the parent of a multinational group beginning on or after January 1, 2016, with a filing due date 12 months after the end of the taxation year.

Many countries, including Canada's trading partners such as the United States, United Kingdom, France, Australia and Mexico are implementing these requirements (see [TaxNewsFlash-Canada 2015-40, "U.S. Multinational Companies to Begin Country-by-Country Tax Reporting"](#)). Earlier this year, Canada joined tax authorities in 30 other countries by signing a Multilateral Competent Authority Agreement for the automatic exchange of country-by-country reports.

The 2016 federal budget confirmed Canada will implement country-by-country reporting but did not announce plans to introduce legislative changes related to master file and local file documentation requirements.

### **Who has to file?**

Canada's 2016 federal budget confirmed that Canadian parent entities of multinationals with consolidated revenues of €750 million (currently approximately CAN \$1.1 billion) or more in the preceding financial year will be required to file a country-by-country report with the CRA. This threshold is consistent with OECD's recommendation.

Under the OECD guidance, where a Canadian entity's ultimate parent is resident outside of Canada, the ultimate parent generally would not have to file a country-by-country report with the CRA. This is because the CRA will automatically obtain the report from the tax authority in the parent's foreign jurisdiction under a competent authority agreement (or another arrangement). The budget documents refer to a possible situation where a jurisdiction in which an entity

resides cannot obtain the country-by-country report from the parent's jurisdiction through the automatic exchange of information. The budget indicates that, under a secondary mechanism, a Canadian resident entity will be required to file a country-by-country report with the CRA in these circumstances.

#### **KPMG observations**

Where a foreign ultimate parent entity is not required to file a country-by-country report in its jurisdiction or there is no exchange of information agreement, it appears from the budget documents that Canada is contemplating adopting the OECD's concept of a "surrogate parent" as a secondary filing mechanism. Under this concept, a multinational enterprise may avoid having filing requirements imposed on multiple entities in multiple jurisdictions by designating one of its entities to be a "surrogate" for filing purposes. The surrogate would file the country-by-country report on behalf of the multinational group.

U.S.-based multinationals may be particularly interested in the possibility of having a surrogate parent for filing purposes given the U.S. is delaying implementation of country-by-country reporting to one year after the filing requirement in Canada and other jurisdictions. Considering its large network of tax treaties and tax information exchange agreements, Canada could well be one of the top choices for a surrogate parent jurisdiction pending the implementation of the U.S. country-by-country reporting requirements.

It is not yet clear whether the CRA will compute the €750 million reporting threshold by converting this figure to a fixed Canadian dollar amount or using a threshold derived annually at the year-end exchange rate. Some countries (e.g. the United States, Australia) have addressed this issue by setting thresholds expressed in their local currency, which will not be subject to foreign exchange fluctuations. If the threshold is fixed in Canadian dollars, changes in the value of the Canadian dollar could cause the parent entity's consolidated revenues (converted to Canadian dollars) to exceed the Canadian threshold, but to not quite exceed the threshold in the ultimate parent entity's jurisdiction, when reported in Euros or the parent entity's currency. This could create potential inconsistencies in the reporting requirements across jurisdictions.

#### **What does the report include?**

It is expected that, based on the OECD guidelines, a Canadian entity's country-by-country report will include the global allocation of the following information, by country:

- Related and unrelated party revenues
- Profit before tax
- Taxes paid
- Stated capital
- Accumulated earnings
- Number of employees

- Tangible assets
- The main activities of each of the multinational group's entities.

**KPMG observations**

Canadian entities should refer to the OECD guidance as they consider how to report some of this information in their country-by-country report. For example, entities that use a combination of contractors and employees should consider how these contractors will be treated in the reporting of the “number of employees” in the country-by-country reports. In addition, certain terms (such as tangible assets) are not necessarily well defined in the *Income Tax Act*, but are broadly defined in the OECD guidance. If there is no further guidance provided in the upcoming Canadian legislation, Canadian entities may have to provide their own interpretation of each factor, based on the current OECD guidance.

It is also unclear whether Canadian entities will have the same flexibility in determining the source of their financial information, as recommended by the OECD (i.e., Group GAAP, local statutory account GAAP, or even management reporting information).

It is expected that, once the legislation has been released, the CRA will release a prescribed country-by-country form.

Canadian entities should be prepared for the possibility that information included in their country-by-country report could become public. This is particularly important in light of recent news that the EU is considering changes to make certain country-by-country report information available to the public, both for large EU parented groups and non-EU parented groups with EU subsidiaries or branches.

**What is the filing deadline?**

According to the budget documents, ultimate parent entities that are resident in Canada will be required to file an annual country-by-country report on behalf of their multinational group within one year of the end of the taxation year to which the report relates. Affected entities will have to make reports for taxation years beginning after 2015, and the first automatic exchanges of information between governments are scheduled to begin by June 2018.

For Canadian entities with ultimate parent companies that are not resident in Canada, these entities may also have to contribute information to their ultimate parent to help complete a country-by-country report.

**KPMG observations**

Although the 2016 federal budget indicates the country-by-country report will be required for taxations years beginning after 2015, it is not yet clear how the reporting requirements will address situations where a Canadian entity has a different taxation year-end than its parent.

Although the country-by-country report will not be filed with CRA until one year after the taxation year end, taxpayers should consider completing the report—at least in draft form—before the contemporaneous transfer pricing documentation and tax return filing deadlines.

Completing the report early can help ensure that all of the information provided to tax authorities is consistent and that all potential issues are identified.

As countries across the globe implement their country-by-country reporting requirements, there may be some timing discrepancies across jurisdictions. For example, a U.S. multinational parent may not collect data for a country-by-country report until the United States enacts a country-by-country reporting requirement (expected in the 2017 taxation year). Unless the Canadian legislation provides for an exemption or deferred starting dates in the case of delayed implementation by the ultimate parent entity's tax authority, it currently appears that the U.S. ultimate parent will have to prepare the country-by-country report to meet the Canadian filing requirements based on the deadlines noted in the 2016 federal budget documents.

## We can help

KPMG can assist you at every phase of your country-by-country reporting strategy. Whether you are looking at performing a preliminary readiness assessment, a blueprinting exercise to assist in defining the scope and country-by-country factors, a strategic risk assessing analysis relying on analytics, or an end-to-end country-by-country reporting project, we can bring experience and leading practices from our national and global network. We can also assist clients on projects through the use of our proprietary technology tool KPMG LINK Country-by-Country Reporting, a web-based application to capture, analyze and report data.

For more details on these developments and their potential impact, contact your KPMG adviser or one of the following members of our transfer pricing team:

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