International Tax Planning

Co-Editors: Nick Pantaleo and C. Andrew McAskile*

RETHINKING THE CANADIAN INBOUND BUSINESS MODEL: PART 1

Marc Darmo and Steve Dunk*

Multinational enterprises (MNEs) are abandoning their traditional organizational structures in favour of arrangements organized by economic functions rather than by legal entity. This article presents a comprehensive analysis of such an arrangement where an entrepreneurial entity in a lower-tax jurisdiction would oversee the development, production, and sale of goods in Canada.

Part 1 of this two-part article begins with a discussion of the various tax and non-tax issues associated with the location, design, and operation of the entrepreneurial entity. Part 1 then introduces several possible approaches an MNE might employ to distribute tangible goods into Canada when departing from a full-fledged Canadian distribution model. These distribution approaches are distinguished primarily by how they avoid the creation of a Canadian “agency permanent establishment” for the entrepreneurial entity. Considerations relevant to selecting the optimal distribution approach under this new business model are discussed in detail. These include avoiding controlled foreign corporation rules applicable to the MNE in its home country, establishing an appropriate and defensible transfer pricing for the lower reward earned by the Canadian subsidiary, and minimizing any negative commodity tax implications of the conversion. **Keywords:** Organizational change; multinationals; distribution; downsizing; transfer pricing; permanent establishment.

* Of PricewaterhouseCoopers LLP, Toronto. We would like to acknowledge the important contribution of Alan Ross of PricewaterhouseCoopers LLP to the preparation of this article. We would also like to thank several other colleagues, including Eric Lockwood, Richard Marcovitz, Oscar Tevnissen (New York), and J.D.B. Oliver (London) for their valuable comments on earlier drafts of the article. Finally, we would like to thank Maria Lopes of PricewaterhouseCoopers LLP for her excellent research assistance. Any omissions or errors are solely our own.