Case Name

***Canada v. GlaxoSmithKline Inc.*, 2012 SCC 52**

Countries

Country of decision

Canada

Other countries

The non-arm's length supplier, Adescha, was located in Switzerland.

Court

Supreme Court of Canada

Case Number

33874

Parties

Name

Her Majesty the Queen

Role

Appellant/Respondent on cross-appeal

Name

GlaxoSmithKline Inc.

Role

Respondent/Appellant on cross-appeal

Date of Decision (format yyyy-mm-dd)

2012-10-18

Income Tax Act Sections

Subsection 69(2) of the *Income Tax Act*

(Now subsection 247(2))

Taxable Years

1990, 1991, 1992, and 1993

Keywords

Transfer pricing; related non-resident; non-arm's length transfer price; reasonable arm's length price; multinational corporations; licence agreement; supply agreement; economically relevant characteristics

Summary of Facts

GlaxoSmithKline ("Glaxo Canada") is a Canadian subsidiary of Glaxo Group Ltd ("Glaxo Group"). During the taxation years in question, from 1990 to 1993, Glaxo Canada purchased ranitidine from Adescha S.A. ("Adescha"), a related non-resident company, at a rate of between $1,512 and $1,651 per kilogram. Ranitidine is the key pharmaceutical ingredient in an anti-ulcer drug, sold under the brand name Zantac by GlaxoSmithKline. During the same taxation years, two Canadian generic pharmaceutical companies purchased ranitidine from arm's length suppliers at a cost of between $194 and $304 per kilogram.

A License Agreement with Glaxo Group granted Glaxo Canada patent and trademark rights. Glaxo Canada's Supply Agreement with Adescha, a Glaxo Group clearing company, set the prices and conditions for Glaxo Canada's purchase of ranitidine.

The Minister of National Revenue reassessed Glaxo Canada under subsection 69(2) of the *Income Tax Act* (now subsection 247(2)) on the basis that the amount paid for ranitidine exceeded the price that the parties would have paid had they been operating at arm's length.

Glaxo Canada appealed to the Tax Court of Canada, which found that it was required to evaluate the Supply Agreement independently from the License Agreement and therefore could not take into account whether the License Agreement granted rights and benefits relevant in considering a reasonable arm's length price. The Tax Court of Canada upheld the Minister's reassessment with only a small revision.

Glaxo Canada then successfully appealed to the Federal Court of Appeal, which determined that the License Agreement and the Supply Agreement needed to be considered together when assessing whether the price paid was reasonable. The Federal Court of Appeal remitted the case to the Tax Court of Canada for a redetermination on the basis that Glaxo Canada had not satisfied its burden to demolish the Crown's assumptions of what constituted a reasonable price for ranitidine.

The Crown appealed the Federal Court of Appeal's decision that the License Agreement should have been considered and Glaxo Canada cross-appealed the decision to remit the case to the Tax Court of Canada.

Issues

Was the price Glaxo Canada paid to the non-resident related company for a key pharmaceutical ingredient higher than what would have been paid if the parties had been dealing at arm's length?

Did Glaxo Canada discharge its burden to demolish the assumptions of the Minister of National Revenue, or must the case be remitted to the Tax Court of Canada?

Court Decision

The Supreme Court of Canada dismissed the appeal and the cross-appeal.

The Court reviewed subsection 69(2) of the *Income Tax Act* (now subsection 247(2)), which required an evaluation of whether the transfer price paid by Glaxo Canada would have been a reasonable price between arm's length parties. To supplement subsection 69(2), which provided no specifics for the reasonableness assessment, the Court noted that OECD guidelines, while not binding Canadian law, offer several possible approaches.

The decision emphasized that relevant surrounding circumstances and, where available or relevant, other related transactions, must be considered when determining a reasonable arm's length price. The inclusion of "economically relevant characteristics" is necessary for a proper assessment. Where, as in this case, there are other agreements that grant related rights and benefits, these agreements consist of relevant circumstances to be considered in determining what an arm's length party would have paid for the goods and/or services.

The Court went on to find that the price Glaxo Canada paid for ranitidine was at least in part also compensating for rights and benefits it received under the License Agreement. Both the License Agreement and the Supply Agreement acted together to allow Glaxo Canada to acquire ranitidine, make it deliverable, and market the drug under the brand name Zantac. The License Agreement also specifically required Glaxo Canada to purchase ranitidine from either Adechsa or another source. The Court concluded that the prices paid for ranitidine by generic drug manufacturers were not sufficient comparisons without further adjustments to account for the additional rights, benefits, and obligations under the License Agreement.

As guidelines for the redetermination by the Tax Court of Canada, the Court provided a number of comments. First, the Court emphasized that transfer pricing cannot be applied with exact certainty and different assessments of a reasonable price may still fall within the appropriate range of what is reasonable. Courts can only aim as best as possible to make satisfactory and informed determinations. The Court then noted the need to consider the differing roles of Glaxo Group and Glaxo Canada and ensure that transfer pricing did not result in a misallocation of profits, noting that it will be for the Tax Court of Canada to consider whether there needs to be some adjustment for intellectual property rights. The Court also asserted that the independent interests of Glaxo Group and Glaxo Canada should be recognized. Finally, the Court highlighted the need to consider the evidence that even when operating at arm's length, some distributors have opted to purchase ranitidine from Glaxo Group.

Regarding Glaxo Canada's cross-appeal, the Court upheld the Federal Court of Appeal's decision that Glaxo Canada had not demolished the Minister's assumption that it did not pay a reasonable price for the supply. The Court remitted the case back to the Tax Court of Canada for redetermination based on the guidelines it set out.

Decision in Favour of

GlaxoSmithKline Inc., the Respondent, was successful on the appeal.

Her Majesty The Queen, the Respondent, was successful on the cross-appeal.

Editor's Notes

This was the first transfer pricing decision by the Supreme Court of Canada. While the transfer pricing provision in question, subsection 69(2), has been replaced with a new provision, subsection 247, the decision still provides important guidelines for applying transfer pricing law in Canada.

Language of Decision

Available in English and French

Full Text of Decision

In English: Judgments of the Supreme Court of Canada or CanLII

In French: Judgments of the Supreme Court of Canada or CanLII