



EMERGING TRENDS & RECENT JUDICIAL PRECEDENCE -TRANSFER PRICING

OUR SCHEDULE

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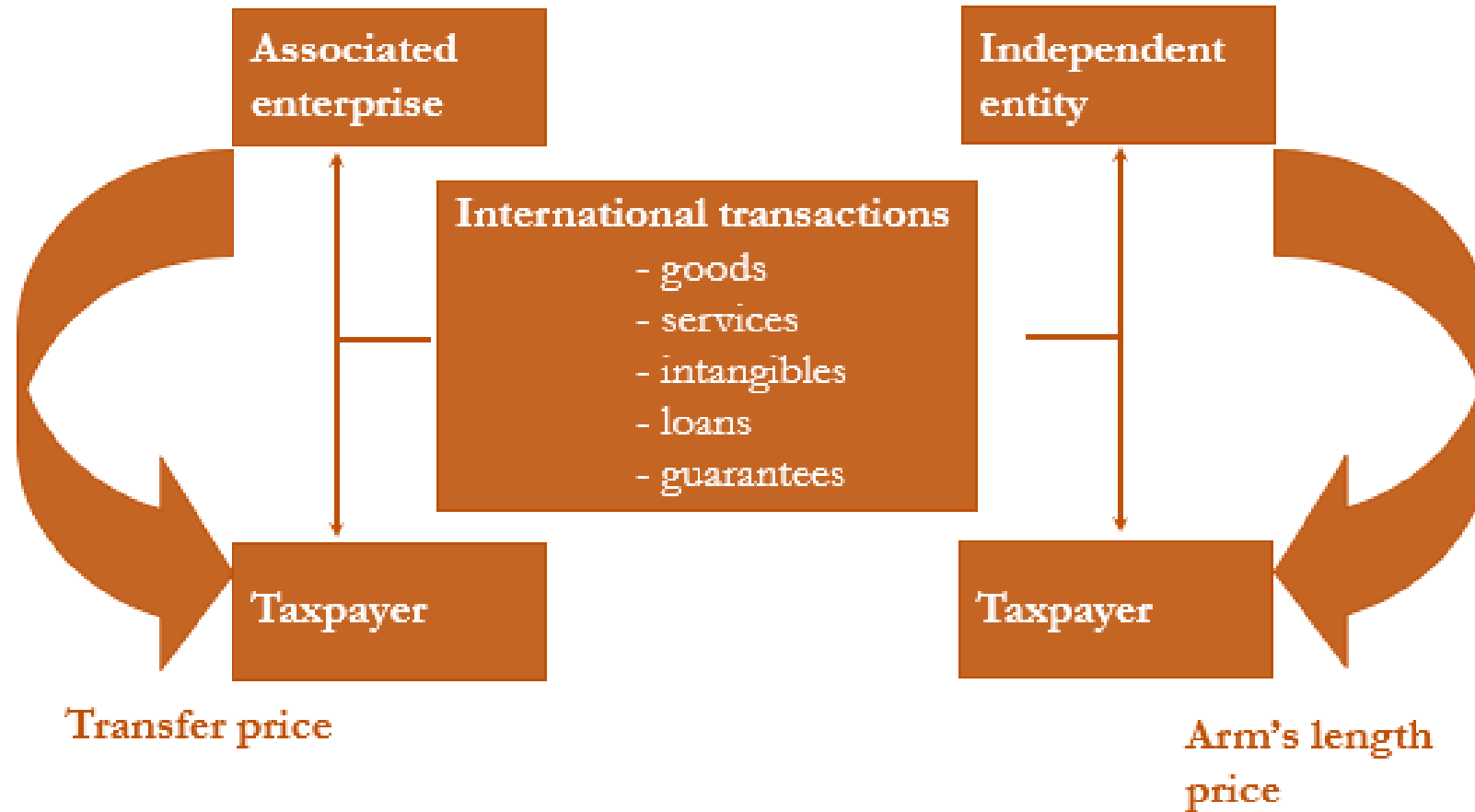
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CONCEPT OF TRANSFER PRICING

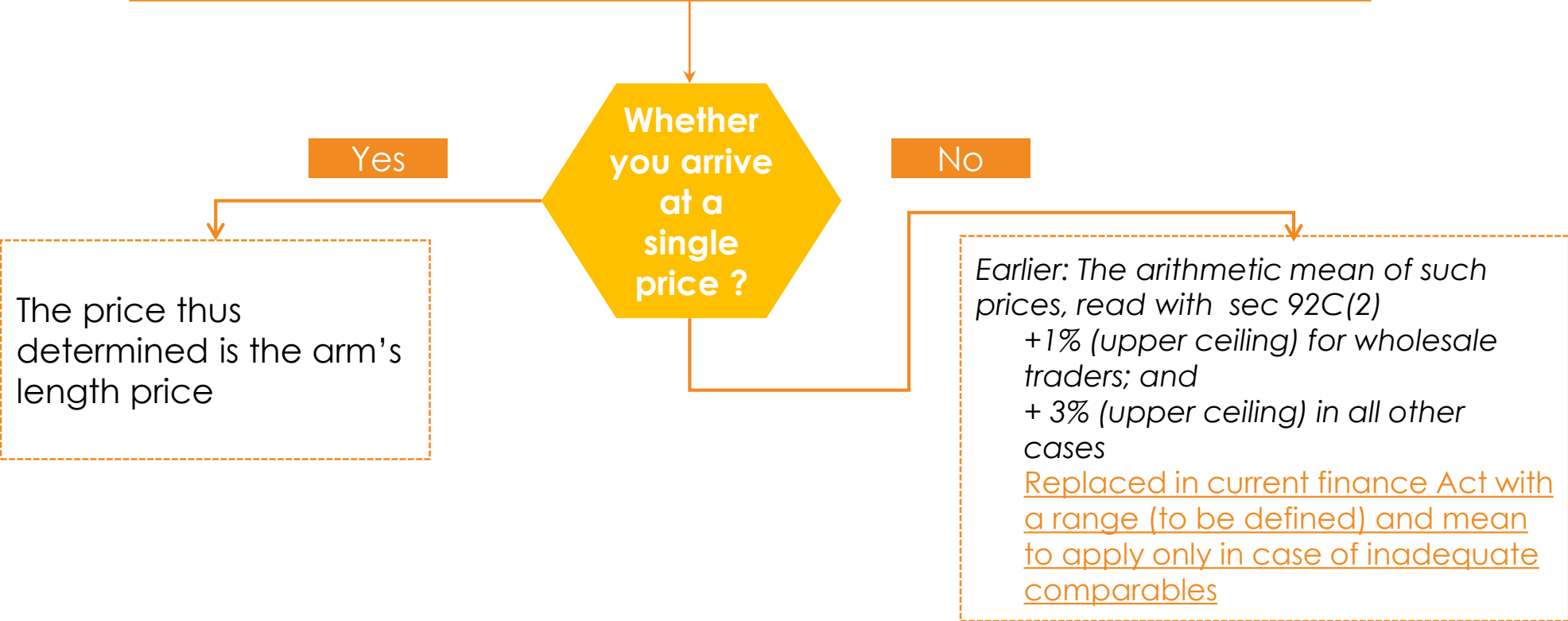
INTRODUCTION TO TRANSFER PRICING



ARM'S LENGTH PRICE

Price applied or proposed to be applied in a transaction between persons other than AEs, in uncontrolled conditions

Determination of arm's length prices using one of the Prescribed methods



APPLICABILITY

- The provisions of **Section 92 to 92F** of the Act are applicable only if:
 - There are two or more enterprises (defined in Sec 92F); and
 - The enterprises are **AEs** (defined in Sec 92A); and
 - The enterprises enter into a transaction (defined in Sec 92F); and
 - The transaction is an **International transaction** (defined in Sec 92B).
- Further w.e.f. 1 April 2012, TP provisions shall also apply to specified domestic transactions (SDTs) (defined in Sec 92BA) - where domestic related parties have claimed any special tax holiday deductions u/s 10AA/80A/80IA/favourable corporate tax rate u/s 15BAB
- Consequences of these provisions:
 - Computation of **income/ allowance of expenses** having regard to the **Arm's length price** [Section 92]
 - Maintenance of prescribed **Documentation** (Section 92D & Rule 10D)
 - Obtaining of **Accountant's report** (under Form 3CEB) (Section 92E)
 - To ensure compliance with the arm's length principle, stiff **Penalties** have been prescribed

APPLICABILITY

- **Section 92(1) –**

Any income arising from an **international transaction** shall be computed having regard to the **arm's length price**

Explanation - the allowance for **any expense or interest** arising from an international transaction shall also be determined having regard to the **arm's length price**

- **Section 92(3) –**

The provisions are not intended to be applied in case determination of arm's length price reduces the income chargeable to tax or increases the loss as the case may be

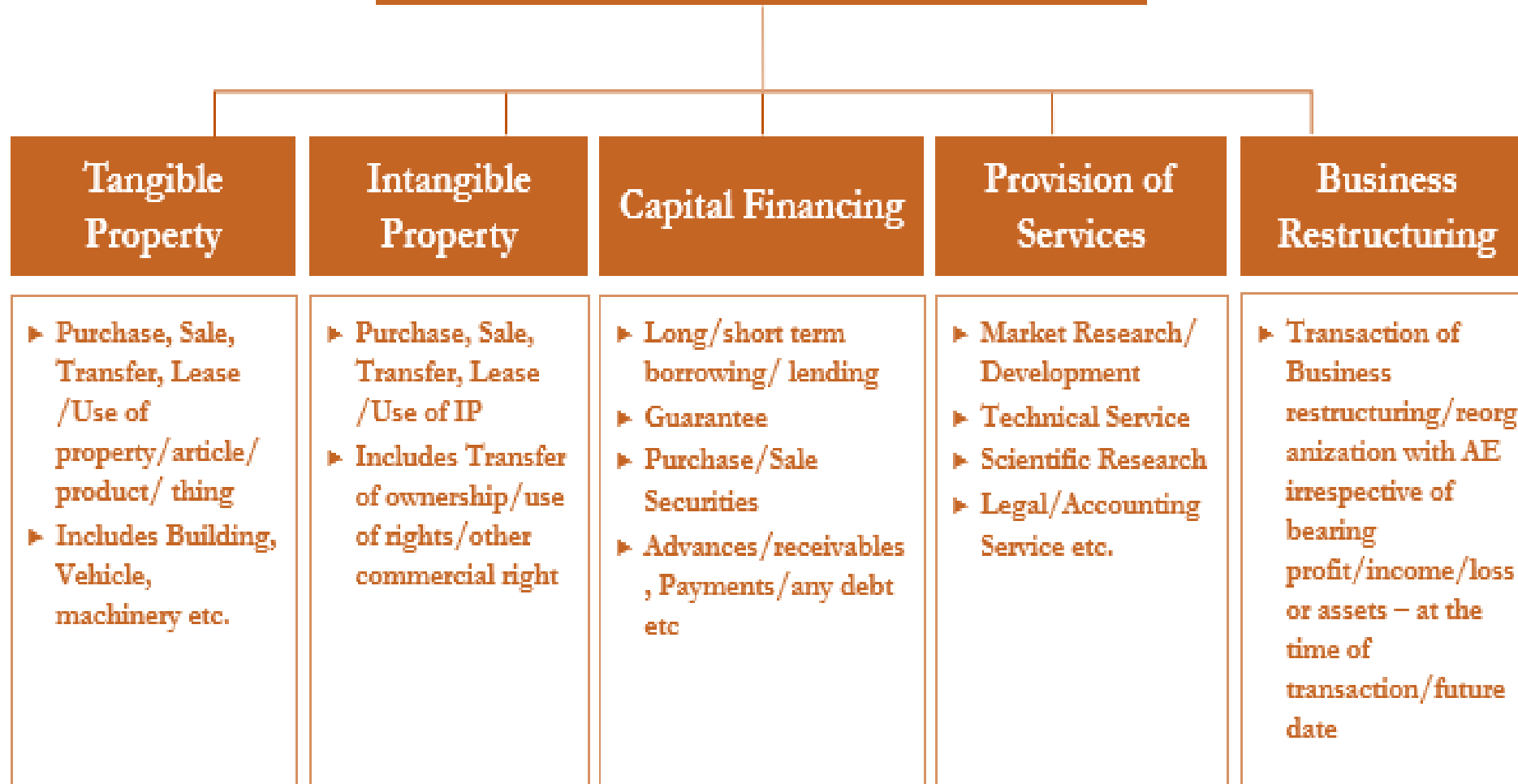
International transaction (Sec 92B)

- Transactions between two or more AEs, **either or both** of whom are non-residents
- Transaction relates to:
 - Purchase, sale or lease of tangible or intangible property; or
 - Provision of services; or
 - Lending or borrowing money; or
 - Any other transaction having a bearing on the profits, income, losses or assets of the enterprises; or
 - Mutual agreements or arrangements for allocation or apportionment of, or any contribution to, any cost or expense incurred; or
 - Business restructuring or reorganization irrespective of fact that it has bearing on the profit, income, losses or assets

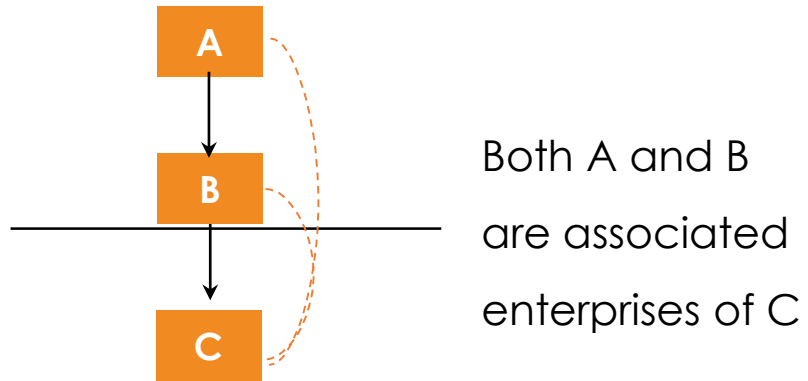
As per Section 92F(V):

- “transaction” includes an arrangement, understanding or action in concert –
 - (A) whether or not such arrangement, understanding or action is formal or in writing: or
 - (B) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceeding.

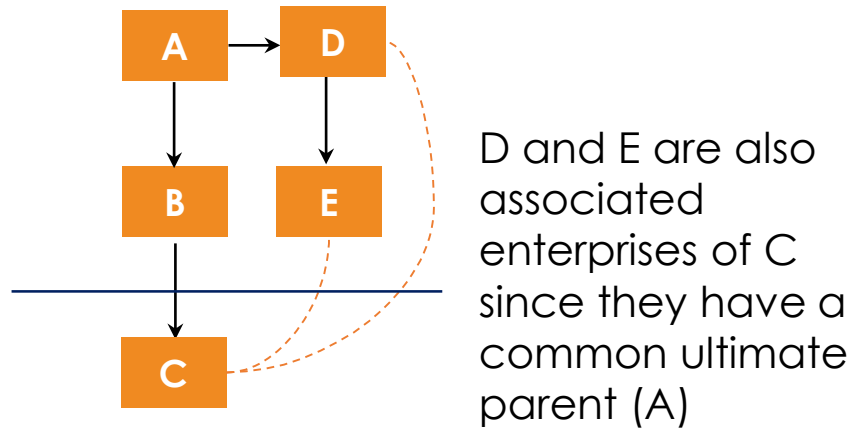
International Transaction



MEANING OF ASSOCIATED ENTERPRISES (Sec 92A)



Both A and B are associated enterprises of C



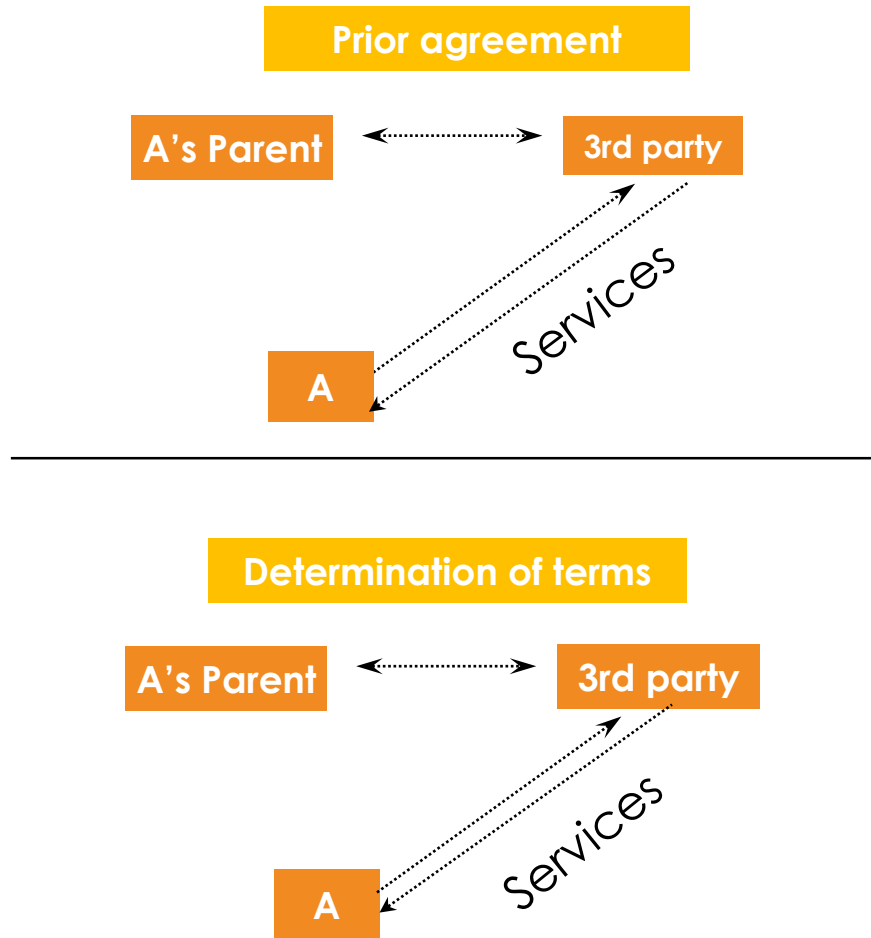
D and E are also associated enterprises of C since they have a common ultimate parent (A)

Direct or indirect participation (through one or more intermediaries) in management, control or capital

DEEMED ASSOCIATED ENTERPRISES (Sec 92A(2))

HOLDING	MANAGEMENT	ACTIVITIES	CONTROL
<p>1. $\geq 26\%$ direct / indirect holding by enterprise</p> <p><u>OR</u></p> <p>2. By same person in each enterprise</p> <p>3. Loan $\geq 51\%$ of Total Assets</p> <p>4. Guarantees $\geq 10\%$ of debt</p> <p>5. $> 10\%$ interest in Firm / AOP / BOI</p>	<p>6. Appointment $> 50\%$ of Directors / one or more Executive Director by an enterprise</p> <p><u>OR</u></p> <p>7. Appointment by same person in each enterprise</p>	<p>8. 100% dependence on use of intangibles for manufacture / processing / business</p> <p>9. Direct / indirect supply of $\geq 90\%$ Raw Materials under influenced prices and conditions</p> <p>10. Sale under influenced prices and conditions</p>	<p>11. One enterprise controlled by an individual and the other by himself or his relative or jointly</p> <p>12. One enterprise controlled by HUF and the other by</p> <ul style="list-style-type: none"> - a member of HUF - his relative or - Jointly by member and relative

DEEMED INTERNATIONAL TRANSACTION- Sec 92B(2)

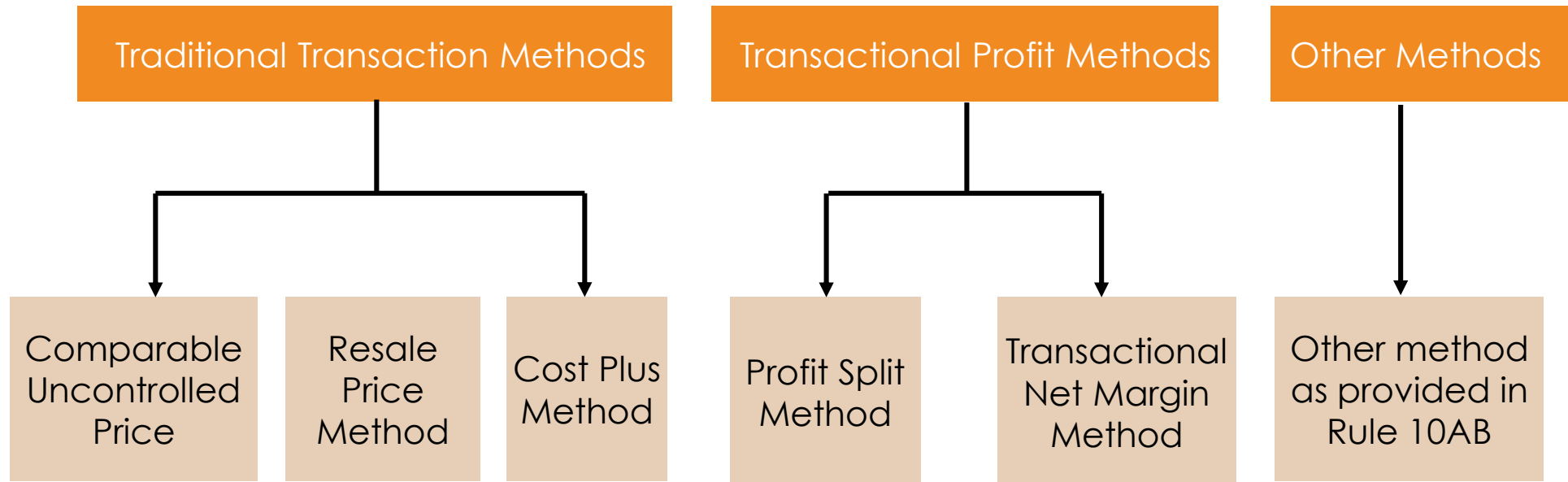


- ▶ An transaction with an unrelated company (3rd party) is deemed to be an international transaction and subject to transfer pricing regulations if
 - ▶ a **prior agreement** exists between A's AE and 3rd party in relation to services rendered by A to the 3rd party; or
 - ▶ **terms of transaction** are determined in substance by A's AE and 3rd party

SPECIFIED DOMESTIC TRANSACTION – Sec 92(2A)

- ▶ Scope of TP provisions expended w.e.f. AY 2013-14 by including “SDT” if aggregate value of such transaction exceeds INR 50 Million (INR 5 Crores) [*Finance Bill 2015 has proposed to increase this threshold to INR 20 Crores*]
- ▶ Applicability of TP regulations (including procedural and penalty provisions) to specified transactions between domestic related parties and payments made to related parties.
- ▶ Section 92BA - “**Specified Domestic Transactions**” in case of an Assessee means any of the following transactions, not being an international transaction, namely -
 - i. Any expenditure in respect of which payment is made or to be made to a person u/s 40A(2)(b);
 - ii. Any transaction referred u/s 80A;
 - iii. Any transfer of goods/services u/s 80-IA;
 - iv. Any business transaction u/s 80-IA(10);
 - v. Any transaction under Chapter VI-A or u/s 10AA – to which provisions of Sec 80-IA (8) or (10) applies;
 - Va. Any business transacted between the persons referred to in sub-section (6) of section 115BAB;] or
 - vi. Any other transaction as may be prescribed.

PRESCRIBED TRANSFER PRICING METHODS



- ▶ Tax payer may apply any of the above methods that is considered most appropriate for a transaction. There is no preference of one method over another

COMPARABLES

- ▶ All methods require comparables
- ▶ Transfer price is set/ defended using data from comparable companies
- ▶ Comparable company should be independent and similar to an associated enterprise.
- ▶ Comparability Criteria (Rule 10C(2)):
 - nature of transactions undertaken (i.e. type of good, service etc.)
 - company functions
 - risks assumed
 - contractual terms (i.e. similar credit terms)
 - economic and market conditions



COMPARABLE UNCONTROLLED PRICE METHOD -Rule 10B(1)(a)

- The price charged or paid for property transferred or services provided in a comparable uncontrolled transaction or a number of such transactions are identified.
- Such price is adjusted for differences, if any, between the international transaction/SDT and the comparable uncontrollable transactions or between the enterprises entering into such transactions, which could materially affect the price in open market.
- The adjusted price arrived above is to be taken as the arm's length price.

COMPARABLE UNCONTROLLED PRICE METHOD

▶ Internal CUP

Manufacturer A

Related party - B

Non-related party

▶ External CUP

Non-related party A

Non-related party B

RESALE PRICE METHOD- Rule 10B(1)(b)

- ▶ Compares the resale gross margin earned by associated enterprise with the resale gross margin earned by comparable independent distributors
- ▶ An arms' length gross margin should be sufficient for a reseller to cover its operating expenses and make an appropriate operating profit (in light of its functions and risks)
- ▶ Preferred method for a distributor buying purely finished goods from a group company without any value addition (if no CUP available)



RESALE PRICE METHOD- Rule 10B(1)(b) - Process

- Identification of resale price by tested party
- Resale price reduced by normal gross profit with reference to uncontrolled transaction(s)
- Such price reduced by expenses incurred (customs duty etc.) in purchase of the product/ services.
- This price may be adjusted to account for functional and other differences if any
- Adjusted price arrived above taken to be arm's length price

COST PLUS METHOD - Rule 10B(1)(c)

- ▶ Compares the gross profit on costs the associated enterprise earns with the gross profit on costs earned by comparable independent companies
- ▶ Preferred method for:
 - ▶ manufacturer supplying semi-finished goods
 - ▶ company providing services

Manufacturer A
(Indian)

Cost + 40%

Related
Manufacturer
B (US)

US Market

COST PLUS METHOD Rule 10B(1)(c) - Process

- Identification of direct and indirect costs of production incurred in tested party transactions
- Identification of normal gross profit with reference to uncontrolled transaction(s)
- Normal gross profit adjusted to account for functional and other differences if any
- Adjusted gross profit added to total costs identified in step 1
- Sum arrived above is taken to be arm's length price

PROFIT SPLIT METHOD-Rule 10B(1)(d)

- ▶ Appropriate for transactions which are not capable of being evaluated separately
- ▶ Calculates the combined operating profit resulting from a whole inter-company transaction based on the relative value of each associated enterprise's contribution to the operating profit
- ▶ The contribution made by each party is determined on the basis of a division of functions performed, valued, if possible using external comparable data
- ▶ Applicable for analyzing tangible, intangible or services issues

PROFIT SPLIT METHOD-Rule 10B(1)(d) - Process

- Determination of combined net profit of the associated enterprises arising out of international transaction
- Evaluation of relative contributions by each enterprise on the basis of functions performed, risks assumed and assets employed
- Profit thus apportioned to the tested party is used to arrive at the arm's length price
- Splitting of combined net profit amongst enterprises in proportion to their relative contributions

TRANSACTIONAL NET MARGIN METHOD-Rule 10B(1)(e)

- ▶ Examines net operating profit from transactions as a percentage of a certain base (can use different bases i.e. costs, turnover, etc.) in respect of similar parties
- ▶ Ideally, operating margin should be compared to operating margin earned by same enterprise on uncontrolled transaction
- ▶ Can compare to “comparable transactions” between independent parties
- ▶ Applicable for any type of transaction and often used to supplement analysis under other methods
- ▶ Most frequently used method in India, due to lack of availability of comparable uncontrolled prices and gross margin data required for application of the comparable uncontrolled price method/ cost plus method/ resale price method

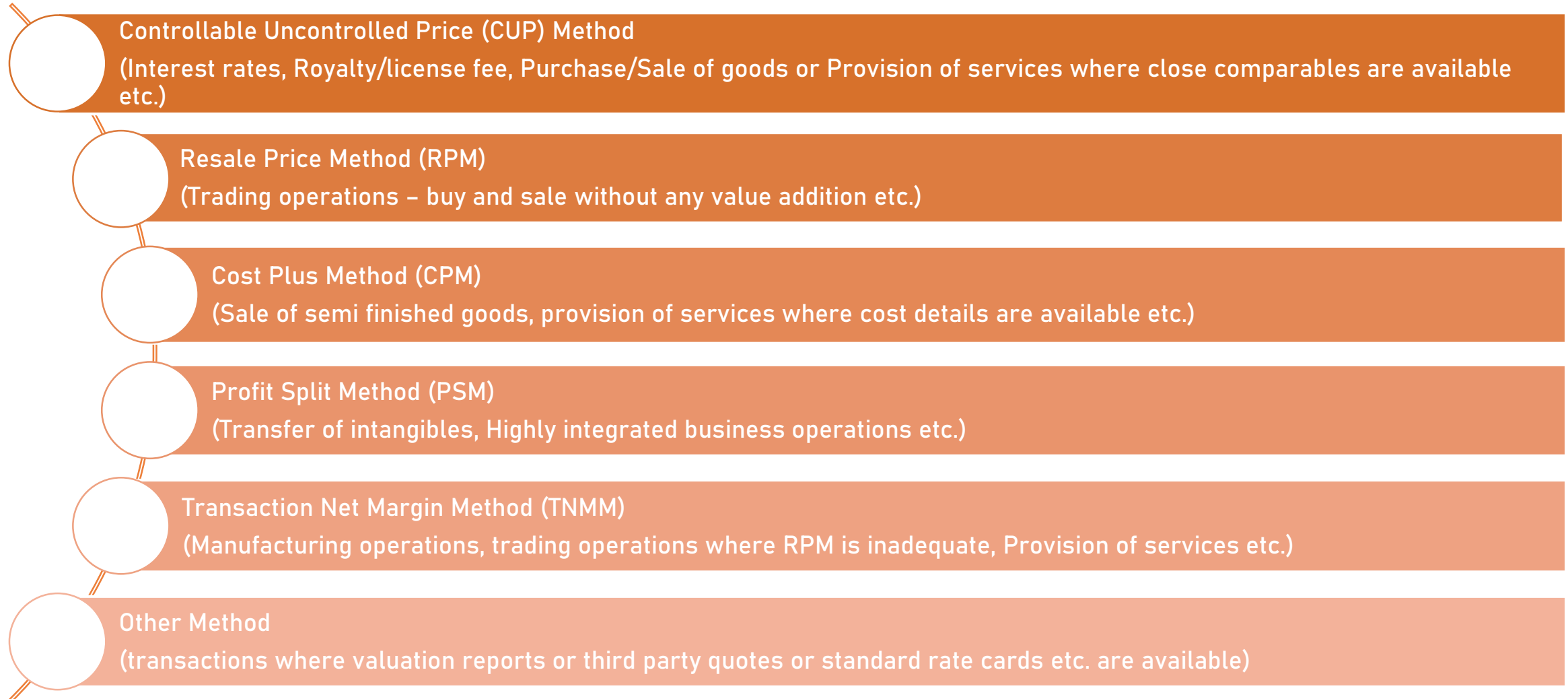
TRANSACTIONAL NET MARGIN METHOD - Process

- Computation of net profit as a percentage of a certain base realised from the international transaction.
- Computation of net profit realized by the tested party or an unrelated enterprise in a comparable uncontrolled transaction
- Net profit from uncontrolled transaction adjusted to account for differences if any
- The net profit thus established is taken into account to arrive at an arm's length price for the international transaction

OTHER METHOD : (Rule 10AB)

- Other Method or the sixth method allows the use of 'any method' which takes into account:
 - (i) the price which has been charged or paid or
 - (ii) would have been charged or paid for the same or similar uncontrolled transactions, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts.
- The various data which may possibly be used for comparability purposes could be:
 - (a) Third party quotations;
 - (b) Valuation reports;
 - (c) Tender/Bid documents;
 - (d) Documents relating to the negotiations;
 - (e) Standard rate cards;
 - (f) Commercial & economic business models; etc.

Brief on TP Methods* for determining Arm's Length Price



**TP methods as prescribed in Rule 10B of Income-tax Rules, 1962 and their broad application/ usage*

92 C(2) – TOLERANCE RANGE REDUCED: Notification 23/09/2014

- The Central Government notified that where the variation between the arm's length price determined under section 92C and the price at which the international transaction or specified domestic transaction has actually been undertaken does not exceed:
 - **1% of the latter (TP) for wholesale traders (Explained) and**
 - **3% of the latter (TP) in all other cases,**
- The price at which the international transaction or specified domestic transaction has actually been undertaken shall be deemed to be the arm's length price for assessment year 2014-2015.

****Wholesale Trading means an international transaction or specified domestic trading in goods, which fulfils the following conditions:***

- 1. Purchase cost of finished goods is 80% or more of the total cost pertaining to such trading activities: and***
- 2. Average monthly closing inventory of such goods is 10% or less of sales pertaining to such trading activities***

INTRODUCTION OF 'RANGE' CONCEPT

- “**Range**” concept followed internationally; also propounded by OECD
- Use of inter-quartile range is amongst the globally accepted best practice and also closer to economic realities wherein prices, and or margins, are compared to those within a range and not at to a particular point.
- In order to align the transfer pricing regulations in India with the international best practices, "range" concept is proposed to be introduced for determination of arm's length price.
- However, arithmetic mean concept will continue to apply where number of comparable is inadequate
- Relevant excerpts from the FM's speech

“In order to align Transfer Pricing regulations in India with the best available practices, I propose to introduce **range concept** for determination of arm's length price. However, the arithmetic mean concept will continue to apply where number of comparable is inadequate. The relevant data is under analysis and appropriate rules will be prescribed”

CBDT Notification No S.O. 2860 (E) dated 19 Oct 2018 - 'RANGE' & 'MULTIPLE YEAR DATA'

- Budget 2014 made an announcement that 'range concept' would be introduced, where there are adequate number of comparables for determination of ALP
- Consequently, section 92C(2) was amended to prescribe for manner, in which the arm's length basis of the international or domestic transactions will be undertaken
- In light of the above announcements, the CBDT announced application of range concept and use of multiple year data

Applicable for international transaction or domestic transaction undertaken on or after April 1, 2014. (i.e. from Assessment Year 2015-16)

RANGE CONCEPT APPLICABILITY & METHODOLOGY

METHOD	Only under TNMM, RPM or CPM
COMPARABLES	Minimum 6
PERIOD	Weighted average of 3 year data of each company to construct the data set (In certain circumstances, data of 2 years could be used out of the 3 years)
PLI COMPUTATION	Numerator and denominator of the chosen PLI to be aggregated for all the years for every comparable
RANGE	Data Points lying within 35 th and 65 th percentile off the data set

If the transfer price of the tested party falls outside the range computed, the 'median' of the range would be taken as ALP and adjustment to transfer price shall be made.

USE OF MULTIPLE YEAR DATA

- Multiple year data allowed only where determination of ALP is done using TNMM, RPM or CPM.
- Data would comprise of three years including the current year.
- Data of 2 years also permitted in case of non-availability of data for 3 years for following reasons:
 - ❑ Data of the current year of the comparables not be available by the due date;
 - ❑ A comparable fails to clear a quantitative* filter in any one year; and
 - ❑ Comparable commenced operations only in the last two years or closed down operations during the current year.

Data of the current year can be used during the transfer pricing audit by both the taxpayer and the department, if it becomes available at the time of audit.

**** The notification in the present form is silent on the definition of quantitative filter. Further there is no reference to any qualitative filter.***

TRANSFER PRICING DOCUMENTATION

A detailed list of mandatory documents are given in Rule 10D(1) of the Rules.

- ▶ Ownership Structure
- ▶ Profile of multinational group
- ▶ Business description/ Profile of industry

- ▶ Nature and terms (including price) of international transactions
- ▶ Description of functions performed, risk assumed and assets employed (functional analysis)
- ▶ Records of economic and market analysis (economic analysis)
- ▶ Record of budgets, forecasts, financial estimates
- ▶ Any other record of analysis (if, any) to evaluate comparability of international transaction with uncontrolled transaction(s)
- ▶ Description of method considered with reasons of rejection of other methods

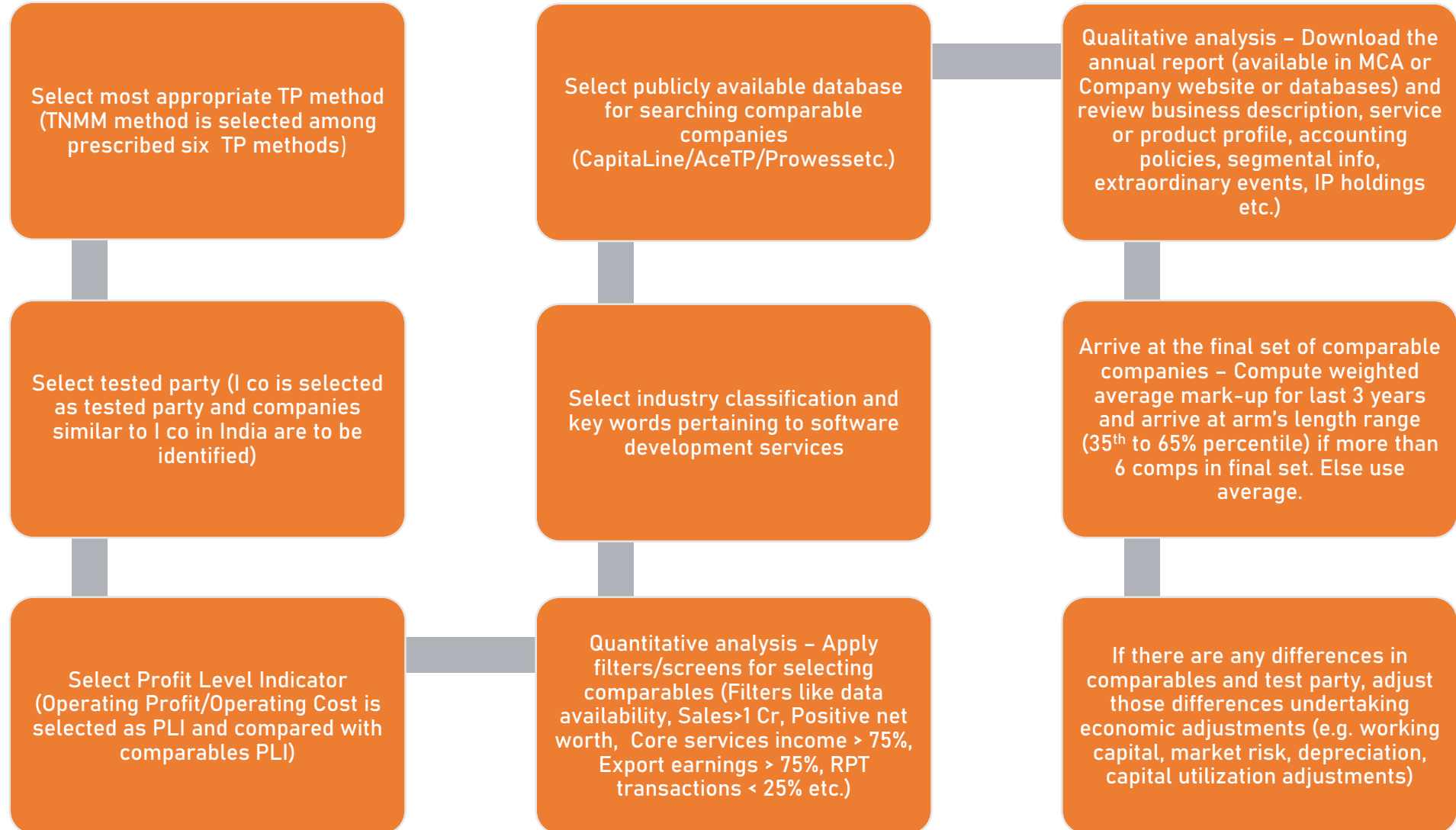
Entity Related

Price Related

STEPS FOR DETERMINATION OF COMPARABLES

Case study:

- > Indian resident entity - I co. is engaged in providing software development services to its holding company in US - F co.
- > I co. is earning a mark-up of cost plus 15% for the services rendered to F co.
- > We have to evaluate mark-up of 15% earned by I co from the International transaction of Provision of software development services from an arm's length stand point.
- > Here are the steps involved in the benchmarking analysis undertaken to arrive at the arm's length mark-up earned by comparable companies engaged in similar software development services in India.



TRANSFER PRICING DOCUMENTATION

- ▶ Details of transfer pricing adjustment(s) made (if, any)
- ▶ Any other information e.g. data, documents like invoices, agreements, price related correspondence etc.
- ▶ Detailed documentation not required in case aggregate transaction value is less than **INR 1 Crore**
- ▶ List of supporting documents are also provided in the law
- ▶ Contemporaneous data requirements
- ▶ Documents to be retained for a fixed period from end of the assessment year
- ▶ Need to obtain Accountant's report (under Form 3CEB) to be filed along with the return of income

Transaction Related

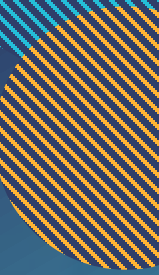
ACCOUNTANT'S REPORT (Form 3CEB) - Rule 10E

- Obtained by every taxpayer filing a return in India and having international transaction or SDT
- To be filed by due date for filing return of income
- Essentially comments on the following:
- whether the taxpayer has maintained the **transfer pricing documentation** as required by the legislation,
- whether as per the transfer pricing documentation the prices of international transactions are **at arm's length**, and
- certifies the value of the international transactions as per the books of account and as per the transfer pricing documentation are **"true and correct"**

Form 3CEB is bifurcated into following 3 parts:

- ❑ **Part A: Details of taxpayer**
- ❑ **Part B: Details of International Transactions**
- ❑ **Part C: Details of Specified Domestic Transactions**

EVOLUTION OF TRANSFER PRICING



EVOLUTION OF TRANSFER PRICING

FY 2012-13	
S No	Particulars
1	Section 92 was amended by introducing sec 92A to 92F
2	Definition under Sec 92B was amended retrospectively w.e.f 01.04.2012
3	Sec 92BA was introduced for SDT(5CrS)
4	Sec 92CC and CD was introduced-APA
5	Safe harbour rules introduced for FY 2012-13 to 2016-17
FY 2013-14	
S No	Particulars
1.	Tolerance range of 3% was introduced w.e.f FY 2013-14
FY 2014-15	
S No	Particulars
1	APA-Rollback was introduced
2	Use of multiple year data introduced-CBDT Notification No. 83/2015 [F.No.142/25/2015-TPL]dated 19 October 2015

EVOLUTION OF TRANSFER PRICING

FY 2015-16	
S No	Particulars
1	Threshold limit for triggering the provisions of SDT increased from INR 5 Cr to INR 20 Cr from FY 2015-16 through CIRCULAR NO.- 19 /2015
FY 2016-17	
S No	Particulars
1	Sec 92BA was amended-Sec 40A(2)b was excluded
2	Adopted Action point 13 of BEPS-Introduced Master file and CBCR
FY 2017-18	
S No	Particulars
1	CBDT issued revised SHR for FY 2016-17 to 2018-19
2	Sec 94B was introduced for restriction of Interest payments
3	Sec 92CE-Secondary Adjustment was introduced
4	Introduced few clauses in Tax Audit report
	<ul style="list-style-type: none"> • clause 30A-Primary adjustment and repatriation of the same. • clause 30B-Limitation of Interest payments u/s 94B • clause 43(a)- CBCR

EVOLUTION OF TRANSFER PRICING

FY 2018-19	
S No	Particulars
1	Modification order for past years in case of APA
2	Clarification with respect to provisions of secondary adjustment
3	Clarification regarding definition of the "accounting year" in section 286 of the Act
4	Rationalisations of provisions relating to maintenance, keeping and furnishing of information and documents by certain persons
FY 2019-20	
S No	Particulars
1	Preponement of Form No. 3CEB compliance timeline
2	Non-residents other than FCs can file now file objections before DRP
3	Rationalizing the thin capitalization ('TC') regulations
4	Inclusion of attribution of profits to Permanent Establishment ('PE') in APA and SH
5	Penalty for false entry or omission

SECONDARY ADJUSTEMENT u/s 92CE

Secondary adjustment has been defined to mean an adjustment in the books of accounts of the taxpayer and its AE to reflect the actual allocation of profits between the taxpayer and its AE consistent with the transfer price determined as a result of primary adjustment.

- **Secondary Adjustment Provisions u/s 92CE are attracted in the following cases:**
 - Suo – Moto Adjustment by Assessee
 - Adjustment by Assessing Officer u/s 92CA
 - Safe Harbour Rules u/s 92CB
 - Advance Pricing Agreement u/s 92CC
 - Mutual Agreement Procedure (Article 25)
- **Exemptions to Secondary Adjustment:**
 - Amount of Primary Adjustment is not exceeding Rs. 1 Crore.
 - Primary Adjustment is made prior to AY 2016-17 (FY 2015-16).

Time Limit and Applicable rate of Interest

Type of Primary adjustment	Time Limit for repatriation	Consequences for imputation of delayed receipts
Adjustment made by the Indian Tax Authority and accepted by the taxpayer	On or before 90 days from the date of relevant order	For rupee denominated transactions: 1-year MCLR* + 325 basis points *MCLR of State Bank of India as of 1 April of the relevant FY
Suo-moto adjustment by the taxpayer	On or before 90 days from the due date of filing return of income under Section 139(1) of the Act or (in case of APA, the due date of filing of modified return of income)	For foreign currency denominated transactions: 6 months LIBOR* + 300 basis points *LIBOR as of 30 September of the relevant FY Or
Adjustment pursuant to APA, Safe Harbour or MAP		Additional income tax of 18% on such excess money

MASTERFILE AND CBC REPORT



MASTER FILE

- The master file (MF) is a document which contains high level information about the global business operations and TP policy of an MNE group. The MF will usually include standardized information about the group's organizational structure; significant value drivers; main geographical locations; description of the business activities of members of the group (i.e. products, services, supply chain etc.); information about the group's intangibles; financing activities within the group (including external funding); and financial and tax positions of the MNE group.
- In an attempt to achieve more transparency on the transfer pricing policies applied by MNEs, the OECD updated in 2015 the documentation requirements in Chapter V of the OECD Guidelines. Since then, MNEs are expected/required to document their transfer pricing information in the form of a Master File and a Local File.
- The Guidelines provide that the master file should be made available to all relevant tax authorities in the jurisdictions where the members of the group are resident. Further, the MF may be prepared for the group as a whole or on a line of business basis, provided all centralized functions and transactions are described thoroughly in the MF.

APPLICABILITY OF MASTERFILE

- Part A of Master File (Form 3CEAA) – Part A comprises of basic information relating to the International Group (“IG”) and the constituent entities of the IG operating in India (such as name, permanent account number and address). The final rules have clarified that Part A of the Master File will be required to be filed by every constituent entity of an IG, without applicability of any threshold;
- Part B of Master File (Form 3CEAA) – Part B comprises of the main Master File information that provides a high-level overview of the IG’s global business operations and transfer pricing policies. Every constituent entity of an IG that meets the following threshold will be required to file Part B of Master File: –
 - A. The consolidated group revenue for the accounting year exceeds INR 5,000 million and**
 - B. For the accounting year, the aggregate value of international transactions exceeds INR 500 million, or aggregate value of intangible property related international transactions exceeds INR 100 million.**
- The Master File has to be furnished by the due date of filing the income-tax return i.e. 30 November following the financial year. IGs with multiple constituent entities in India can designate one Indian constituent entity to file the Master File in India, provided an intimation to this effect is made in Form No. 3CEAB, 30 days prior to the due date for filing the Master File in India.

COUNTRY-BY-COUNTRY ('CBC') REPORT

Under BEPS Action 13, all large multinational enterprises (MNEs) are required to prepare a country-by-country (CbC) report with aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which it operates. This CbC report is shared with tax administrations in these jurisdictions, for use in high level transfer pricing and BEPS risk assessments.

Requirements:

- The CbC report requires each MNE to provide key financial information on an aggregate country basis with an activity code for each member of the MNE. CbC report is a new concept for the international tax world and represents the biggest change to the existing Guidelines. The provision of the CbC report to the tax authorities is a 'minimum standard' requirement, and the report makes clear that countries participating in the BEPS project are expected to commit to and adopt this measure. It will provide tax authorities with global information for the purposes of risk assessment.

COUNTRY-BY-COUNTRY ('CBC') REPORT

- The elements relating to CbC reporting requirement shall apply in respect of an international group having consolidated revenue, based on consolidated financial statements, exceeds the threshold. The current international consensus is for a threshold of INR 6,400 Crores.
- The CbC report requires MNEs to report annually and for each tax jurisdiction in which they do business; the amount of revenue, profit before income tax and income tax paid and accrued. It also requires MNEs to report their total employment, capital, accumulated earnings and tangible assets in each tax jurisdiction. Finally, it requires MNEs to identify each entity within the group doing business in a particular tax jurisdiction and to provide an indication of the business activities of each entity.

Applicability of ('CbC') report

Rule 10DA of the Income tax Rules, 1962 ("the Rules") (as amended) provides that the provisions of furnishing of CbC Report to the Income tax department is applicable only if the consolidated revenue of International Group is more than Rs. 5,500 crores as reflected in the consolidated financial statements for the preceding accounting year.

Forms – MASTERFILE AND (“CBC”) REPORT

Form	Description
Form 3CEAA (Part – A)	All CE s of International Group, Irrespective of whether Satisfying the threshold Limits or Not
Form 3CEAA (Part – B)	All CE s of International Group, Crossing the Master File threshold Limits Notified
Form 3CEAB	Subsidiaries of Designated CE i.e case more than 1 entity in India is crossing the Master File threshold limits Notified
Form 3CEAC	Intimation of the Indian CE being alternate reporting entity or that the Parent entity is filing CbCR
Form 3CEAD	Filing of CbCR by <ul style="list-style-type: none"> • Indian Parent Company • Indian Alternate reporting entity • CE resident in India satisfying 286(4) (No Agreement for Information Exchange)
Form 3CEAE	Instruction where CbCR is being Filed by Designated CE where <ul style="list-style-type: none"> • 2 or More CE s Resident of India are falling under 286(4) categories. (No Agreement for Information Exchange; or • Resident CE s of Group having Indian Parent

Forms – MASTERFILE AND ('CBC') REPORT

Form	Due dates
Form 3CEAA (Part – A)	Due date for filing of return 30 November
Form 3CEAA (Part – B)	Due date for filing of return 30 November
Form 3CEAB	30 days prior to the due date for filing form 3CEAA – 31 st October.
Form 3CEAC	2 Months prior to the due date for filing form 3CEAD – 30 th September.
Form 3CEAD	Due date for filing of return 30 November
Form 3CEAE	Due date has not been mentioned, comparatively filing could be done by March 31 of next Assessment year.

CbC reporting – key definitions – section 286(9)

Term	Definition
Group	<ul style="list-style-type: none"> ▶ Group includes parent entity and all the entities in respect of which a consolidated financial reporting for financial reporting purposes is prepared or would have been prepared (if in case equity shares would have been listed on stock exchange)
International group	<ul style="list-style-type: none"> ▶ Two or more enterprises which are resident of different countries/territories or ▶ Enterprise being resident of one country/territory carrying on business through permanent establishment (PE) in other countries/territories
Parent entity	<ul style="list-style-type: none"> ▶ Entity of the group holding directly or indirectly an interest in one or more of the other entities of the group such that it is required or would have required (if in case equity shares would have been listed on stock exchange) to prepare consolidated financial statements as per laws in force/accounting standards of country/territory of which entity is resident
Constituent entity	<ul style="list-style-type: none"> ▶ Any entity of international group <ul style="list-style-type: none"> ▶ that is included in consolidated financial statement ▶ that is excluded from consolidated financial statement on the basis of size or materiality ▶ that is PE of any separate business entity and such PE prepares separate financial statement for financial reporting, regulatory, tax reporting or internal management control purposes
ARE	<ul style="list-style-type: none"> ▶ A constituent entity that has been designated to furnish CbC report in place of parent entity in country or territory in which such constituent entity is resident

OECD model CbC report template

Table 1:

Tax jurisdiction	Revenues			Profit (loss) before income tax	Cash Tax Paid (CIT and WHT)	Current year tax accrual	Stated capital	Accumulated earnings	Tangible assets other than cash and cash equivalents	Number of employees
	Unrelated party	Related party	Total							

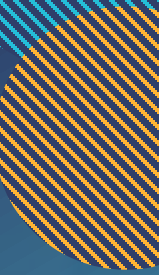
Table 2:

Tax jurisdiction	Constituent entities resident in the tax jurisdiction	Tax jurisdiction of organization or incorporation if different from tax jurisdiction of residence	Main business activity(ies)													
			R & D	Holding or managing IP	Purchasing or procurement	Mfg or production	Sales, marketing or distri.	Admin., Mgmt or support services	Provision of services to unrelated parties	Internal group finance	Regulated financial services	Insurance	Holding shares or other equity instruments	Dormant	Other	

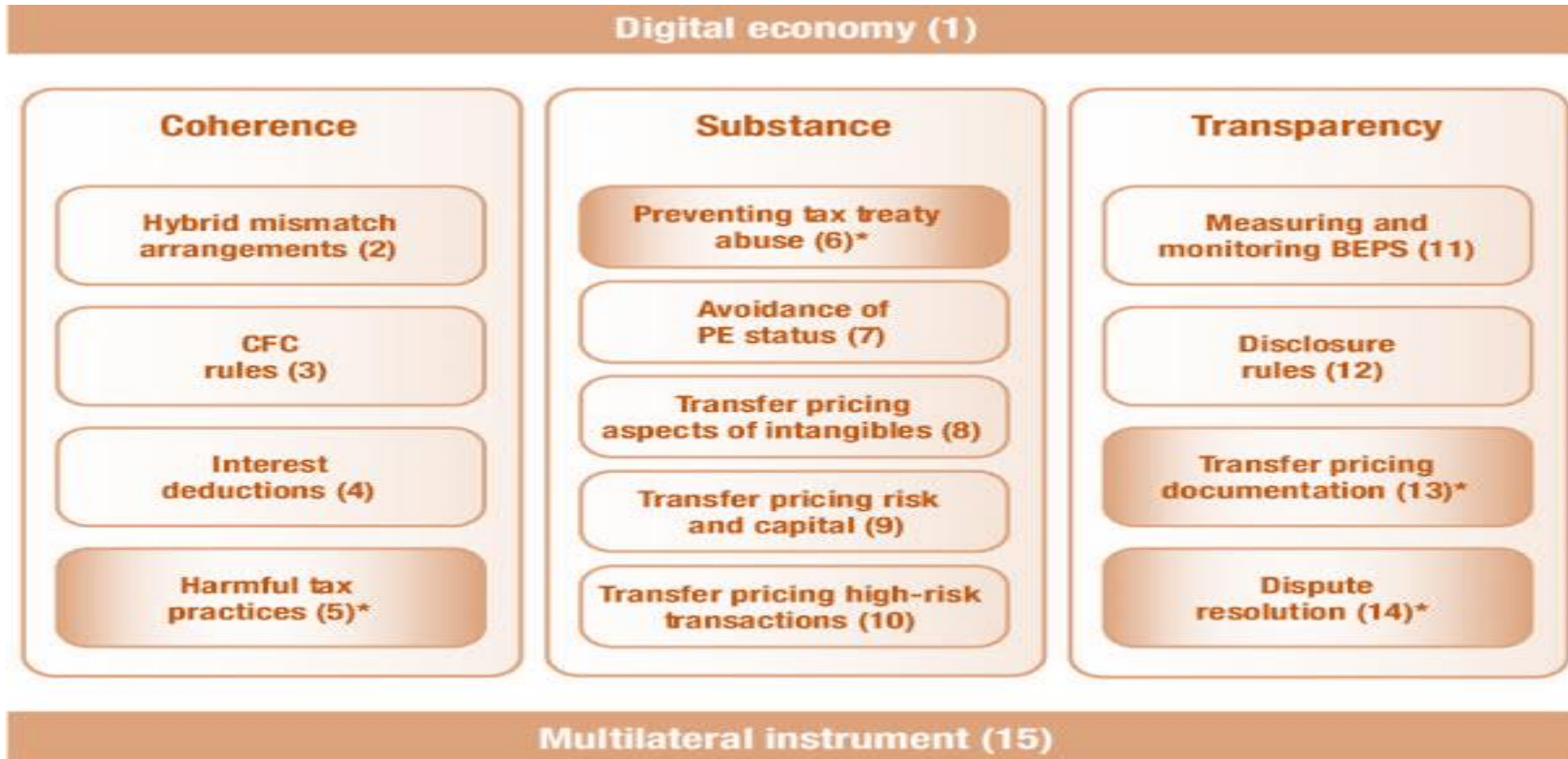
Master File – information required

Organization structure	Business description	Intangibles	Intercompany financial activities	Financial and tax positions
Structure chart:	Important drivers of business profit	Overall strategy description	Financing arrangements for the group	Annual consolidated financial statements
<ul style="list-style-type: none"> ▶ Legal ownership ▶ Geographic location 	Supply chain of: <ul style="list-style-type: none"> ▶ 5 largest products/services by turnover ▶ Products/services generating more than 5% of turnover 	List of important intangibles and legal owners	Identification of financing entities	List and description of existing unilateral Advance Pricing Agreements (APAs) and other tax rulings
	Main geographic markets of above products	List of important intangible agreements	Details of financial transfer pricing policies	
	List and brief description of important service arrangements	R&D and intangible transfer pricing policies		
	Functional analysis of principal contributions to value creation by individual entities	Details of important transfers		
	Business restructuring/ acquisitions/ divestitures during fiscal year			

BEPS - BASE EROSION & AND PROFIT SHIFTING



BEPS - Base Erosion and Profit Shifting



*Minimum standards

Point 4: Limit base erosion via interest deductions and other financial payments

- The goal of Action 4 is to ensure that net interest deductions are directly linked to the level of economic activity. The economic activity is determined based on taxable earnings, before deducting net interest expense, depreciation and amortization (EBITDA).
- The final report on Action 4 recommends an approach based on a fixed ratio rule which limits an entity's net interest deduction to a percentage of its EBITDA. As a minimum, this rule should apply to entities in multinational groups. The recommended approach proposes a range of possible EBITDA ratios between 10% and 30%.

Point 13: Re-examine transfer pricing documentation

- Action 13 contains a three-tiered standardized approach to transfer pricing documentation, including a minimum standard on CBCR.
- First, the guidance on transfer pricing documentation requires MNEs to provide tax administrations with high-level information regarding their global business operations and transfer pricing policies in a Master File.
- Second, it requires that detailed transactional transfer pricing documentation be provided in a Local File specific to each country, identifying material related-party transactions, the amounts involved in those transactions, and the company's analysis of the transfer pricing determinations they have made.
- Third, large MNEs are required to file a Country-by-Country Report that will provide annually and for each tax jurisdiction in which they do business the amount of revenue, profit before income tax, income tax paid and accrued, and other indicators of economic activity

Point 14: Make dispute resolution mechanisms more effective

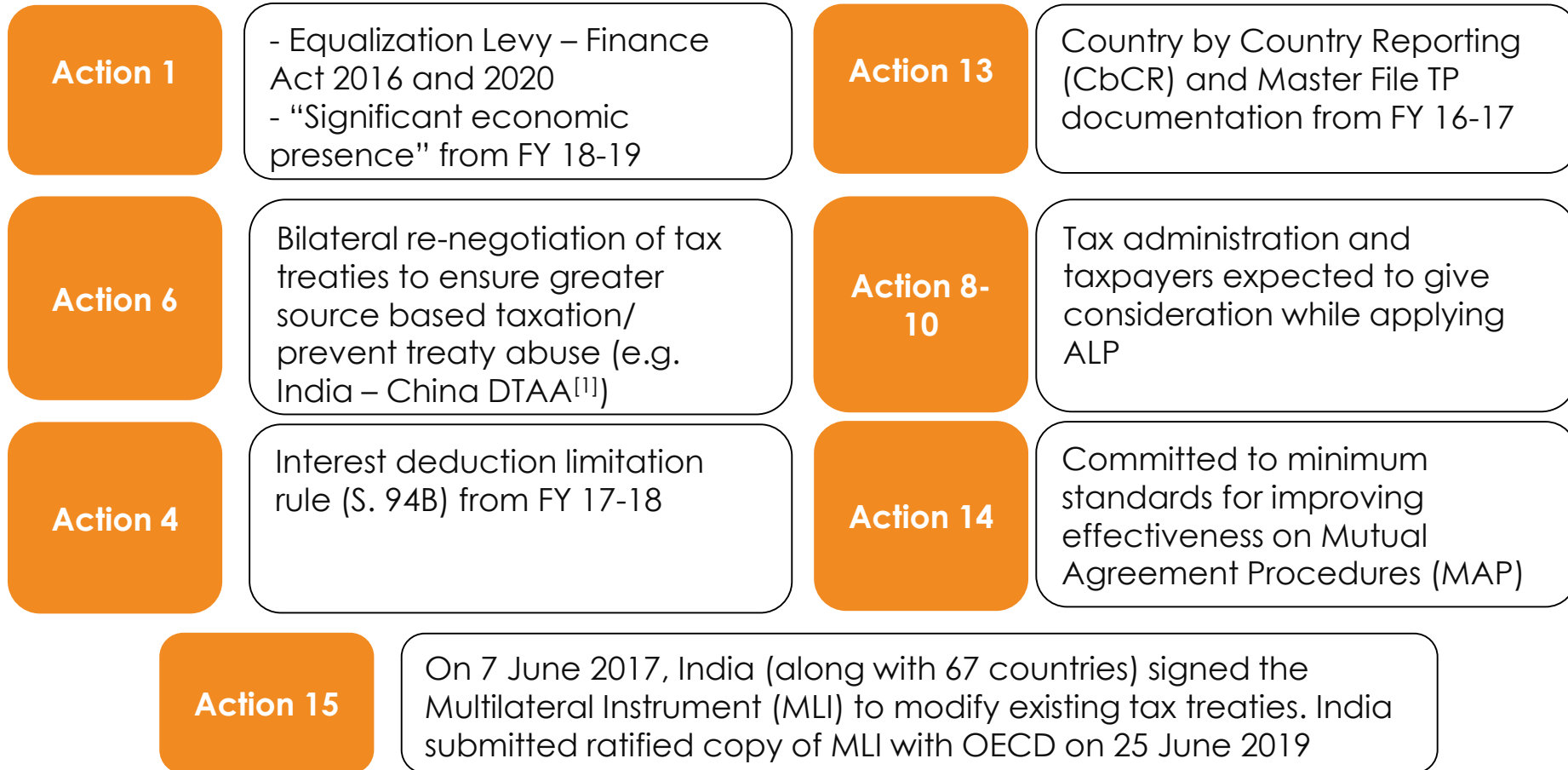
- It might happen that two jurisdictions seek to tax the same transactions or activities. Generally, tax treaties directly resolve most such cases. However, two jurisdictions might disagree on the interpretation or application of a tax treaty. The mutual agreement procedure (MAP) article of a tax treaty provides a mechanism to resolve these cross-border tax disputes.
- The goal of Action 14 is to address obstacles that prevent countries from solving treaty related disputes under MAP.

BEPS Action Points:

Point 15: Develop a multilateral instrument

- Most countries have Double Tax Treaties (DTT) in place with other countries. These DTT's provide clarity as to where a company has to pay taxes, if activities are spread over two or more countries.
- Although a lot of these treaties are based on the OECD Model Tax Treaty, almost all treaties are the result of bilateral negotiations. If BEPS is to be implemented correctly, these treaties have to be renegotiated one by one. This would take ages.
- Instead, Action point 15 aims to develop a Multilateral Instrument (MLI). The MLI is expected to be adopted by 100 countries. This MLI allows countries to swiftly modify their bilateral treaties to implement BEPS measures.
- The MLI, gives countries the flexibility to specify which treaties are covered. They can decide how they meet the minimum standards. If desired, they can opt out of all or part of the provisions which extend beyond the minimum standard.

Implementation of BEPS Actions in India:



[1] Provisions influenced by MLI/ BEPS- Principal purpose test (PPT), competent authority rule as tie-breaker test for dual resident entities, narrowing the permanent establishment definition

RESTRICTION ON DEDUCTION OF INTEREST u/s 94B

- CBDT has introduced provisions similar to thin capitalisation in the Finance Act 2017 by insertion of Section 94B under the Act. Thin capitalisation refers to a situation in which a company is financed through a relatively high level of debt compared to equity, which significantly affects the amount of profit it reports for tax purposes
 - The section is triggered when interest or similar consideration paid to the AE exceeds INR 1 crore.
 - The interest amount that will be disallowed as deduction in computation of income is defined as lower of:
 - The total interest amount in excess of 30% of earnings before interest, taxes, depreciation and amortization;
 - Interest paid or payable to Associated Enterprise
- The provisions are not applicable to Indian company or PE of Foreign Company which is engaged in the business of banking or insurance
 - The provisions are not applicable in respect of debt issued by lender which is PE in India of a non-resident bank
 - If the interest expenditure is not wholly deducted, the balance shall be carried forward to the subsequent assessment years not more than 8 years

TAX ORDINANCE AMENDMENT – Reduced Corporate tax rate

The government has introduced a favourable tax regime for new manufacturing companies. The **Taxation Laws (Amendment) Ordinance, 2019 passed on 20 September 2019** has inserted Section 115BAB offering a low tax rate of 15% (plus surcharge and cess) to new manufacturing companies, which are covered by section 115AB.

Transfer Pricing Applicability:

The definition of the Specified Domestic Transaction (SDT) contained in Section 92BA of the IT Act is amended to bring the Companies opting to be covered by section 115BAB within the ambit of Transfer Pricing. Thus, any transactions entered into by newly set up manufacturing company, opting for reduced rate of 15%, with any of its related parties (domestic or otherwise) are to be at Arm's Length. This amendment shall be effective from fiscal year 2019-20.

Although the SDT definition is redefined by the Finance act, if any manufacturing entity on undertaking the reduced corporate tax rate scheme shall have to comply with the transfer pricing provisions irrespective of the value of transactions with the related party (domestic or international).

The existing tax rates are analysed with an illustrative example (With Surcharge taken at 0%, 7% and 12%)

Particulars	Company (Existing Tax rate @25%)	Company (Existing Tax rate @25%)	Company (Existing Tax rate @25%)	Company (Existing Tax rate @30%)	Company (Existing Tax rate @30%)	Company (Existing Tax rate @30%)
Corporate Tax Rate	25%	25%	25%	30%	30%	30%
Applicable Surcharge	0%	7%	12%	0%	7%	12%
Applicable Cess	4%	4%	4%	4%	4%	4%
Effective Tax Rates	26%	27.82%	29.12%	31.20%	33.38%	34.94%

The Companies who wishes to avail the Tax incentives can continue with existing Tax rate. However, the MAT rate has been reduced to 15% (before surcharge and cess) from 18.5%. Post expiry on Tax incentives the Companies can opt for revised Tax rates mentioned below.

The newly proposed tax rates*

Particulars	Company (New Tax rate @22%)
Corporate Tax Rate	22%
Applicable Surcharge	10%
Applicable Cess	4%
Effective Tax Rates	25.17%

Conditions

- After expiry of tax holiday period, the companies can avail tax rate
- Once the option to avail the reduced rate is exercised, the same cannot be withdrawn
- Companies should not claim any incentive
- Losses brought forward on account of such incentives shall considered as already utilized

The newly proposed tax rates**

Particulars	Company (New Tax rate @15%)
Corporate Tax Rate	15%
Applicable Surcharge	10%
Applicable Cess	4%
Effective Tax Rates	17.16%

Conditions

- Company Should be Incorporated on or after 01 October 2019
- Does not avail any exemption/ incentive
- Companies should commence production on or before 31 March 2023

Applicability of IND AS



APPLICABILITY OF IND AS

Applicability of IND AS

On 16 February, 2015, the MCA notified the rules which lay the Ind AS roadmap:

- **Voluntary Phase:** Early adoption of Ind AS is permitted from financial year beginning on or after 1st April, 2015.
- **Mandatory Phase I** (adoption from 1st April, 2016 with comparatives for 2015-16)
 - Listed company or Unlisted company having net worth in excess of Rs. 500 Crores or more
 - Holding, subsidiary, joint venture or associates of these companies
- **Mandatory Phase II** (adoption from 1st April, 2017 with comparatives for 2016-17)
 - All listed companies not covered under the mandatory phase I
 - Non-listed companies with net worth of INR 250 Crores or more and not covered in the mandatory phase I
 - Holding, subsidiary, joint venture or associates

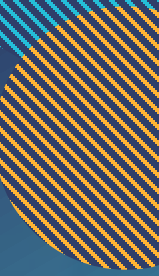
APPLICABILITY OF IND AS

- Definition of related party under Ind AS 24 is broader and will cover increased number of related party relationship and has clear principles of identification of related parties.
- If, based on the Ind AS 24 definition, one party is identified as related to the second party; the definition would treat the second party as related to the first party, by symmetry.

Ind AS 24	AS -18
Includes any director	Excludes non-executive directors
Includes close members of family of KMP	Includes only relatives of KMP
An entity discloses that terms of RPT are equivalent to those that prevail in arm's length transactions, only if such terms can be substantiated	No such stipulation on substantiation of RPT when the same is disclosed to be on arm's length
KMP remuneration disclosure to include post employment benefits	Does not have such requirement

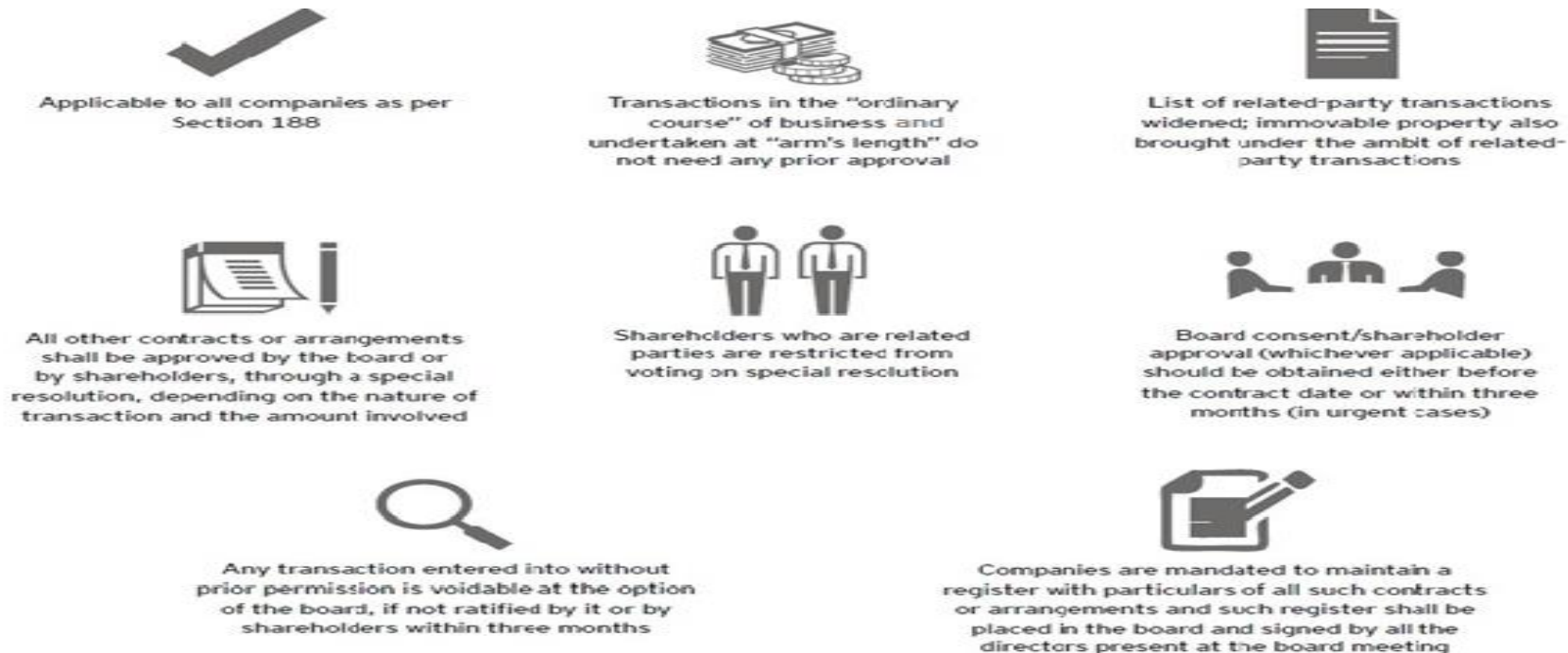
COMPANIES ACT 2013

TP INTERPLAY

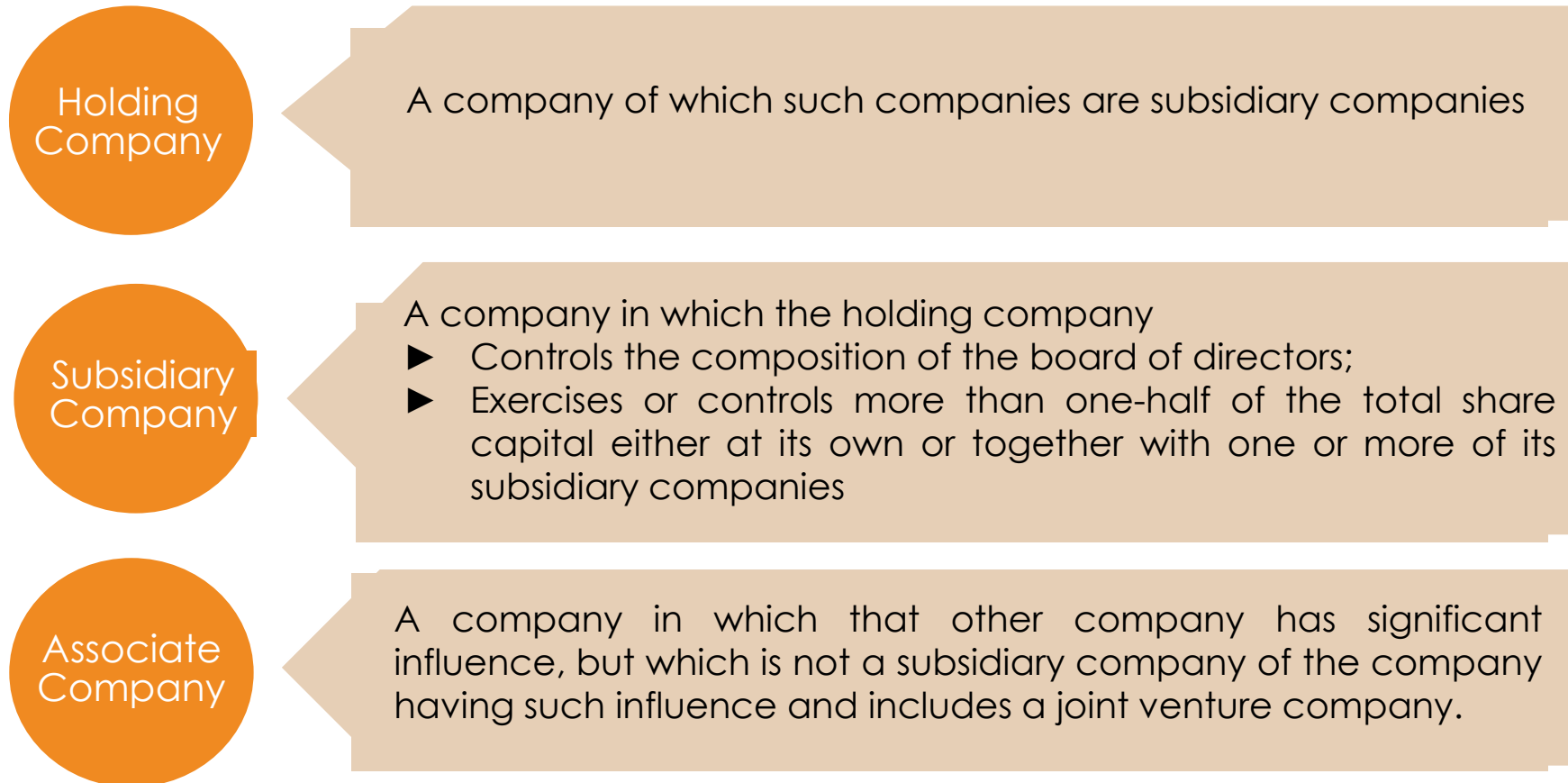


KEY COMPLIANCE REQUIREMENTS

- With the growing participation of investors and other stakeholders in companies, the question of transparency in deals with related parties has often been a topic of much debate and discussion. With the objective to usher increased degree of transparency in such transactions, section 188 has been introduced in the Act placing the onus on the Board of Directors to review, approve and explain such transactions to shareholders and in some cases seek their approval. The following are the key compliance requirements for related party transactions under the Act:

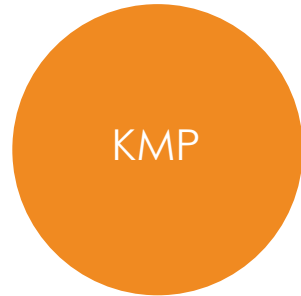


Companies Act, 2013 Definitions



Significant influence means control of at least twenty percent of the total share capital, or of business decisions under an agreement;

Companies Act, 2013 Definitions



- ▶ The Chief Executive Officer or the managing director or the manager;
- ▶ The Company Secretary;
- ▶ The Whole-time director;
- ▶ The Chief Financial Officer;
- ▶ Such other officer as may be prescribed



- ▶ Members of a HUF
- ▶ Husband and wife
- ▶ One person is related to the other in such manner as may be prescribed (includes father, mother, son, daughter, son's wife, daughter's husband, brother, sister)



An individual who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole, or substantially the whole, of the affairs of a company, and includes a director or any other person occupying the position of a manager, by whatever name called, whether under a contract of service or not.

Companies Act 2013 Related Party Transactions - Definition

The Companies Act, 2013 has laid down certain restrictions on the related party transactions if those transactions are not in the ordinary course of business or at arm's length. However, these restrictions are limited to specified transactions mentioned under section 188 of the Companies Act, 2013. These specified transactions are:

- | |
|--|
| ▶ Sale, purchase or supply of any goods or materials; |
| ▶ Selling or otherwise disposing of, or buying, property of any kind; |
| ▶ Leasing of property of any kind; |
| ▶ Availing or rendering of any services; |
| ▶ Appointment of any agent for the purchase or sale of goods, materials, services or property; |
| ▶ Appointment of any related party to any office or place of profit in the company, its subsidiary company or associate company; and |
| ▶ Underwriting the subscription of any securities or derivatives thereof, of the company. |

Latest SEBI Update dated 22nd November 2021

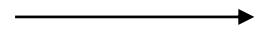
1. SEBI Vide Circular No : SEBI/HO/CFD/CMD1/CIR/P/2021/662 dated 22^o November 2021 amended Vide notification dated November 9, 2021 mandating listed entities that have listed specified securities to submit to the stock exchanges disclosure of Related Party Transactions (RPTS) in the format specified by the Board from time to time.
2. Further, it has been decided to prescribe the information to be placed before the audit committee and the shareholders for consideration of RPTs.
3. Accordingly, the following provisions shall apply to entities that have listed specified securities on a Recognized Stock Exchange.

Latest SEBI Update dated 22nd November 2021

4. Information to be provided by the management of the Listed entity to the audit committee and the shareholders.
 - a. Type, material terms and particulars of the proposed transaction
 - b. Name of the RPT and its relationship
 - c. Tenure of the proposed transaction
 - d. Value of proposed transaction
 - e. . The percentage of the listed entity's annual consolidated turnover, for the immediately preceding financial year, that is represented by the value of the proposed transaction (and for a RPT involving a subsidiary, such percentage calculated on the basis of the subsidiary's annual turnover on a standalone basis shall be additionally provided);
 - f. If the transaction relates to any loans, inter-corporate deposits, advances or investments made or given by the listed entity or its subsidiary:
 - Details of source of funds
 - Purpose for which the funds will be utilized
 - applicable terms, including covenants, tenure, interest rate and repayment schedule, whether secured or unsecured; if secured, the nature of security
 - g. where any financial indebtedness is incurred to make or give loans, intercorporate deposits, advances or investments
 - nature of indebtedness;
 - cost of funds; and
 - tenure

Latest SEBI Update dated 22nd November 2021

5. Audit committee



Shall review the above-mentioned information and also the status of long term (more than one year) or recurring RPTs on an annual basis before giving approval.

6. Shareholders



Shall review the above-mentioned information in addition to the requirements under the companies act 2013 as a part of explanatory statement.

Latest SEBI Update dated 22nd November 2021

7. Format for reporting of RPTs to the Stock Exchange

The listed entity shall make RPT disclosures every six months in the format provided by

[Clicking here](#)

8. The Circular shall come into force with effect from April 1, 2022.

9. The Circular is issued in exercise of the powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with Regulation 101 of the LODR.

RISK PARAMETERS

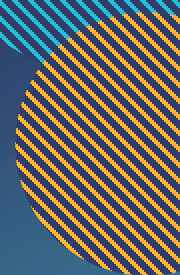


RISK PARAMETERS

CBDT vide instruction 3/2016 dated 10th March 2016 has issued guidelines for implementation of transfer pricing provisions by replacing instruction no 15/2015. The said guidelines are applicable for both IT as well as SDT. The key features of the guidelines are as under:

Selection Criteria	Action to be taken
All cases selected under Computer Assisted Scrutiny Selection (CASS) system or under the compulsory manual selection system	Mandatorily referred to the TPO by the AO after obtaining approval of the PCIT or CIT.
All cases selected under non-transfer pricing risk parameters referred to the TPO only in the following circumstances:	Where the taxpayer has entered in to and IT or SDT, however the taxpayer has not filed Form No. 3CEB or has not disclosed all the IT's or SDT's in the report so filed.
	Where there has been a transfer pricing adjustment of INR 10 crores or more in any earlier assessment year which has been upheld by the judicial authorities or is pending in appeal. Where, in the search and seizure or survey operations, findings have been recorded by the investigation wing or AO regarding transfer pricing issues.

Recent Developments – TP Impact



1. Characterization of Comparables – Cherry picking of Comparable Companies.

A. Issue

- The crux of arm's length price determination is comparability analysis, where a controlled transaction or price is compared with the independent uncontrolled comparables. Given this, comparability, including selection of appropriate comparable is at the heart of transfer pricing analysis, and death of comparability could well mean the death of transfer pricing
- Ever since the formal transfer pricing (TP) regulations were introduced in India in 2001, the maximum amount of dispute and litigation in the field of TP have revolved around the issue of comparability or economic analysis, namely selection/ rejection of comparables.
- There was an underlying reason or logic for the genesis of such controversy i.e. profitability and functionality of any selected comparable.

EMERGING ISSUES IN TP

1. Characterization of Comparables – Cherry Picking of Comparables

B. Judicial Pronouncements

- It was held by the Delhi Tribunal in **ITW India Limited V/s ACIT 1(1), Gurgaon (2015 53 Taxmann.com 531)**, that no side (the TPO nor the assessee) can be allowed cherry-picking. The view has also been supported in the following cases:
- **Lubrizol Advance Materials India (P) Limited (2014 42 taxmann.com 263 (Ahd- Tribunal)**
- **Toshiba India Private Limited V/s ACIT (Delhi Tribunal)**
- **Phillips Software Centre Private Limited V/s ACIT (2008 26 SOT 226)**

Pr. CIT vs. M/s Softbrands India Pvt Ltd (Bangalore High Court) (AY 2006-07)

Any appeal before High court would not be entertained either by Revenue or the Assessee unless it involves substantial question of law and the exercise of fact finding or Arms Length Price determination or 'Transfer Pricing Adjustments' by ITAT is final as it is the final fact finding Authority.

EMERGING ISSUES IN TP

2. Domestic TP's deemed omission from Inception

A. Issue

- Disputed the ALP of managerial remuneration paid by taxpayer, by virtue of coverage under section 92BA(i) of ITA. The introduction of SDT caused considerable challenge to the taxpayer, in establishing the ALP of certain transactions such as managerial remuneration given that the roles/ responsibilities/ functioning of each of the directors in a particular company is unique/ different and thus may not always be comparable.
- Taxpayers had undertaken compliances in relation to SDT, such as filing of Accountant's Report in Form No. 3CEB maintenance of Rule 10D transfer pricing documentation and in certain cases, such cases also went through the rigor of transfer pricing assessments. Some cases have faced adjustments during the transfer pricing assessments and are currently in the appellate forums.

B. Judicial Pronouncements

- **Texport Overseas Private Limited Vs. Dy. CIT** (ITAT Bangalore) (Texport's case) for Assessment Year (AY) 2013-14
- Honourable Supreme Court in the case of **Kolhapur Cane sugar Works Ltd. Vs Union of India**
- Honourable Supreme Court in the case of **General Finance Co. Vs Assistant Commissioner of Income tax**
- Honourable Karnataka High Court in the case of **GE Thermometrics India Pvt. Ltd.**

EMERGING ISSUES IN TP

3. Marketing Intangibles

(a) Issues

- In case of an international transaction between taxpayer and AE under which the taxpayer incurred Advertising Marketing Promotion ('AMP') expenses towards marketing intangibles legally-owned by the AE; the issue herein pertains to allowability of such AMP expenses in the hands of the taxpayer, considering the commercial rational or the legal ownership. According to the tax Authorities, what is relevant under the transfer pricing regulations is legal ownership of intangibles.

(b) Judicial Pronouncements

- **Maruthi Suzuki India Ltd Vs CIT (ITA 110/2014)** (Delhi High Court)
- **LG Electronics India Pvt Ltd v. ACIT** (Delhi-Tribunal) (SB)
- **Sony Ericsson Mobile Communications India P. Ltd Vs CIT**

(c) Precautionary Measure:

- The necessity of transfer pricing adjustment for AMP expenses may arise
- where there is influence of an AE in advertising and marketing function of the Indian affiliate. It is advisable for the taxpayer to evaluate the TP policy in light of detailed analysis of roles / responsibilities undertaken, risks borne / reward reaped. Also, a robust documentation including legal contracts etc. has to be maintained by the taxpayer.

EMERGING ISSUES IN TP

4. Issuance of Guarantee on behalf of the AE

(a) Issues

- The Indian tax authorities are of the view that the Indian entity must charge guarantee fees for the guarantee given in respect of the borrowings of AEs.
- In the absence of any guarantee fees charged to AEs, the tax authorities may take stand that Indian entities provided an intra-group service to its AE by issuing the corporate guarantee to the loans taken by their AEs abroad, the latter are obliged to pay a service charge to the Indian entity. Accordingly, Indian entity should charge guarantee fee for provision of guarantee service.

(b) Judicial Pronouncements

- **Maruti Suzuki India (ITA 110/2014)** (DELHI HIGH COURT)
- **Siro clinpharm (ITA 2618/Mum/2014)**
- **DR. Reddys Labs (ITA No. 294, 458/Hyd/2015)**
- **Rain Cements Limited v DCIT (MA No. 32 and 33/Hyd/2017)**
- **Bharti Airtel Limited Vs. ACIT [2014],**
- **Redington (India) Limited vs. JCIT (ITA No. 513/Mds/2014),**

(c) Precautionary Measure

- Considering that the chargeability of fees on corporate guarantee provided by the taxpayer to its foreign AE is a subject matter of litigation and pursuant to the amendment in section 92B to include guarantees, it is therefore advisable to charge guarantee fees on such guarantees provided, at ALP. Reference can be drawn from the rates prescribed under the SHR.

EMERGING ISSUES IN TP

5. Charging Notional Interest for Delay in Realization of Sales Proceeds from AEs

(a) Issues

- In case of excessive credit period allowed to AEs and delay in realization of sales proceeds from AEs as compared to non AEs, the tax authorities are of the view that by giving excess credit period to AEs and delay in realizing sales proceeds from AEs as compared to non AEs, the Indian entity is passing the benefits of prolonged credit to its AE. Accordingly, an adjustment should be made in respect of excess credit period allowed to AE debtors by charging notional interest from AEs on excess amount outstanding or extended credit period.

(b) Judicial Pronouncement

- **PCIT-2 Vs. Bechtel India Pvt Ltd** (TS-591-SC-02017)
- **CIT-9 Vs Indo American Jewellery Ltd** (TS-3-HC-2013(BOM)-TP)
- **Pegasystems Worldwide India Private Limited** for FY 2009-10 (I.T.A. Nos. 1758 & 1936/Hyd/14)
- **Evonik Degussa India P. Ltd** (ITA no. 7653/Mum./2011),
- **M/s Avnet India Pvt. Ltd.** (ITA No .757(Bang.)/2011),
- **Kusum Healthcare Pvt. Ltd.** Range 5 (ITA No.6814/Del/2014)
- **BMW India** (ITA No 5354/DEL 2012)
- **Indo American Jewellery Ltd vs CIT** (ITA No. 5872/Mum/2009)

CIT vs. Aurionpro Solutions Ltd (Bombay High Court)

Transfer Pricing ALP of foreign advances: If the advances are made to a AE situated abroad, the LIBOR rate has to be considered to determine the Arms Length interest and not the interest rate in India (SBI PLR). This would be reasonable and proper in applying commercial principles

(c) Precautionary Measure

- Nevertheless, in order to avoid adjustment or litigation on this account, it is advisable that there is no excess credit allowed / prolonged credit period extended to AE debtors as compared to non AE debtors. It is advisable to maintain robust documentation to prove that the excess credit, if allowed to AE debtors is due to specific business reasons and not with the intention of passing any benefits to AEs.

EMERGING ISSUES IN TP

6. Economic Adjustments

(a) Issues

- There may be certain circumstances wherein comparables identified may require adjustments for differences in working capital, risk profile of entities, capacity utilization, etc. for determining the ALP. Such adjustments are referred to as comparability adjustments or, economic adjustments in common parlance.
- Economic adjustments have been a subject matter of litigation in India.

(b) Judicial Pronouncements

- The Chennai Tribunal in case of **Mando India Steering Systems Pvt Ltd**
- The Pune Tribunal in case of **Amdocs Business Services Private Ltd.**
- The Pune Tribunal in case of **Demag Cranes & Components (India) (P.) Ltd.**
- **Srini Pharmaceuticals Ltd**, (ITA No 1851/Hyd/2012)
- **Qual core logic** (ITA No 893/ Hyd/ 2011)
- **HSBC Electronic Data Processing Pvt. Ltd** (ITA – 420/ Hyd/ 2007)
- **Mentor Graphics (Noida) Pvt. Ltd.** (2007-TIOL-382-ITAT-Del)

(c) Precautionary Measure

- In view of the above, it is advisable that the claim on account of differences should be supported with evidence. For example, claim on account of quantity should be supported with evidence such as the commercial policy of the company, etc.

EMERGING ISSUES IN TP

7. Tax authorities cannot question the commercial rationale of legitimate business expenses incurred

(a) Issue

- In certain cases, the taxpayer makes payment to its AE for the use of brand name, in spite of perpetual loss incurred by the taxpayer in its business. The Tax Authorities generally disallow such payments considering perpetual losses suffered by the Indian entity.

(b) Judicial Pronouncement

- Delhi High Court in the case of **EKL Appliance Ltd. Vs. CIT**

(c) Precautionary Measure

- The decision highlights the fact that the tax authorities per se cannot question the commercial rationale of legitimate business expenses incurred by the taxpayer.
- However, it also becomes imperative for taxpayer to demonstrate that the transaction is at arm's length by application of the prescribed methods with proper evidences/ documentation.

EMERGING ISSUES IN TP

8. Compensation for Intra Group Services – Benefit Test

(a) Issue

- Indian tax authorities take an aggressive approach while examining the TP policies in respect of intra-group services, especially when an Indian entity is the recipient of services and management fee has been charged to Indian entity.
- The Indian tax authorities mainly seek and examine the following details in this respect:
 - Need of such services to Indian entity i.e. whether an independent enterprise in comparable circumstances would have been willing to pay for the activity if performed for it by an independent enterprise or would have performed the activity in-house for itself.
 - Whether the amount charged by AE for services commensurate with the benefit derived by the Indian entity by availing such services, whether the allocation key used by AE make sense under the circumstances, etc.
 - Whether such services have given any special advantage / commercial or economic benefit to the Indian entity or the services are just in the nature of shareholder's services i.e. services rendered to protect the interest of the AE, being the shareholder and thus, not recoverable.
 - A copy of agreement between AEs and invoices/debit notes raised by AE to examine exact nature of services rendered by AE and the basis on which the payment is made to AE.

EMERGING ISSUES IN TP

9. Compensation for Intra Group Services - Benefit Test

(b)Judicial Pronouncements

- **TNS India Private Limited vs. ACIT** (ITA No.944/Hyd/2007)
- **DCIT vs. M/s Air Liquide Engineering India P Ltd** (ITA No. 1159, 1040/Hyd /2011 & ITA No. 1408/Hyd/2010)
- **Kirby Building Systems India Ltd Pashmylaram Vs ACIT** (ITA.No.1651/Hyd/2010)
- **CIT vs Ekl Appliances Ltd** (ITA Nos.1068/2011 & ITA Nos.1070/2011)
- **GOCL Corporation Limited Vs ACIT** (ITA.No.401/Hyd/2016)
- **JT International (India) Private Limited, (Presently known as Polisetty Somasundaram Tobacco Product (I) P Ltd) Vs DCIT**

(c)Precautionary Measure

- It is advisable to design a proper Group TP policy, considering the various factors such as the nature of the activity services rendered, significance of the activity to the group, functional profiling and the characterization of the intra-group transactions involved, relative efficiency of the service supplier, any advantage that the activity creates for the group, etc. Further, it is advisable to maintain robust documentation to demonstrate the actual receipt of intra-group services and fulfillment of the benefit test i.e., to demonstrate that the consideration received by the AE for services rendered to Indian entity is proper as compared to the benefit which Indian entity received from such intra group services.

EMERGING ISSUES IN TP

10. Levy of penalty under section 271G

(a) Issue

- The TPO had called upon the assessee to submit the segmental profitability for AE transactions and non-AE transactions even though the assessee had expressed its inability to furnish details in the manner for the reason that it had not maintained separate books of accounts for AE and non-AE segments.
- The TPO accordingly proposed to levy penalty under section 271G on the assessee for its failure to furnish the said requisite details.

(b) Judicial Pronouncements

- In the case of Mumbai ITAT Ruling of **ACIT V/s M/S D. Navinchandra Exports Pvt Ltd** (ITA No. 6304/Mum/2016)
- In the case of Mumbai ITAT **DCIT Vs Laxmi Diamond P. Ltd** (ITA No.2643/Mum/2017)
- In the case of Mumbai ITAT **DCIT Vs Firestone International Pvt Ltd** (ITA No. 5304/Mum/2016)
- In the case of Delhi ITAT **Bio-Rad Laboratories (India) Pvt Ltd vs. DCIT** (ITA No.1415/Del./2017)
- In the case of Jaipur High Court **CIT Vs Gillette India Ltd.** (ITA No. 104 / 2015)
- In the case of Delhi High Court **CIT Vs Leroy Somer & Controls (India) Pvt Ltd**

(c) Precautionary Measure

- The assessee should maintain robust documentation and also document the practical difficulties if any faced by the industry it operates in as no two businesses are identical which would be helpful to the TPO at the time of assessment and may avoid litigation.

EMERGING ISSUES IN TP

10. Re-imburement of expenses

(a) Issues

- The transactions involving pure cost reimbursements also require a TP analysis (including benchmarking) for determination of ALP.

(b) Judicial Pronouncements

- Delhi High Court in the case of **Cushman and Wakefield India Pvt Ltd**
- **ADP Pvt. Ltd. Vs DCIT** (ITA No. 471/Hyd/2011)
- **AMD Research & Development Center India Private Ltd. Vs DCIT** (I.T.A. No. 86/HYD/2014)
- **M/s.Cognizant Technology Solutions India Pvt. Ltd. Vs ACIT** (ITA Nos.114 & 2100(Mds)/2011)
- **NTT DATA FA Insurance Systems (India) Private Limited Vs DCIT** (I.T(TP).A No.1311/Bang/2010)
- **NTT DATA India Enterprise Application Services P. Ltd. Vs ACIT** (ITA.No.1613/Hyd/2010)

(c) Precautionary Measure

- In view of the above, it is advisable to carefully frame the policy for re-imburement of expenses incurred on behalf of AEs. If the expenses are administrative/routine in nature, it is advisable to maintain documentation in support of expenses incurred,
- the benefit, if any, derived by the AE, rationale for incurring the expenses by Indian entity, arrangement/agreement with the AE in respect of the same, etc.
- Further, in cases where such activities are done on regular and frequent basis and continue over a period of time, it is important to look into the substance of the transaction to find whether the activities carried on by the Indian entity amounts to service rendered by the Indian entity for which it should charge appropriate amount of service fee to the AEs.



Multilateral effects of the documentation paradigm

Revision of intercompany agreements and existing transfer pricing policies of the group to renegotiate the arrangements to be done by the AEs during the current scenario. This would have an effect on pricing, credit terms, delivery and exchange rates. The positions taken ought to be documented to face transfer pricing audits in the future.



The outcome – pressure for Taxpayers or Revenue?

Benchmarking study would not accurately measure the arm's length price for 2020 and future transactions. Adjustments can be used to assist in determining ALP. Data may not be available on public domains in real time.



More issues than solutions?

Effect on APA negotiations as the effect on critical assumptions is uncertain. The terms agreed may not reflect the COVID-19 economic situation. Impact on existing APAs needs to be considered whether to honor/ revise/ cancel. Detailed documentation is required in place to discuss with Authorities on revision of APA.



Virtual workspaces – cause for controversies?

Whether decisions made through virtual world by the personnel would trigger PE risk to the companies? Work from home option given on account of social distancing requires analysis of PE risk.



Addressing the conundrum

Industry wise impact is required to be assessed to understand the effects of lockdown, demand & supply, reduced margins on competitors, market players etc. and measures taken to fight the adversities.



Transition/ temporary exit?

Temporary relocation of business functions could result in diversion of work to other locations. The FAR analysis needs to be reviewed to reflect the changes with appropriate documentation in place. Impact on benchmarking analysis on account of the above is required to be carried out.



The after-effects of lockdown

Companies would incur expenditure on account of lockdowns such as retrenchment/ layoff compensation, employee benefit expenditure on treatment of infected employees office maintenance etc. Treatment of all expenses incurred during COVID 19 as operating, non-operating/ extraordinary needs careful consideration.

Covid-19 Impact



Will borrower's confidence be shattered?

Credit profile of the borrowers is impacted due to extended period of lock downs and disruption in business operations which is a key consideration for determination of interest rates. The credit rating of companies as on 31 March 2019 would be different from that of 31 March 2020 amidst the breakout though the rating has been consistent over the years.



The HARD to VALUE pain points in the economic turmoil

The licensees of intangible assets may not earn adequate profits from exploitation of assets. Therefore, the royalties and IP payments may not be made on time or payments made may not reflect the arm's length price.



Comparability adjustments – a need of the hour?

The relationship between actual output and potential output may defer as the capacity is not being utilized in the current economic scenario due to lockdowns, work from home/ leave options to employees, existence of fixed costs such as salaries, rent, maintenance, depreciation and unutilized plant and machinery. Hence, capacity utilization for comparables vis-à-vis tested party is required to be analyzed and adjustment, if any is warranted for idle capacity costs. However, this adjustment may not be feasible for risk mitigating entities operating in India.

Equalisation levy on e-commerce operators – TP?

Overview

Taking a cue from the G20 / OECD Base Erosion and Profit Shifting (BEPS) Action 1 dealing with digital economy, India introduced an Equalisation Levy ('EL') in 2016 at the rate of 6 percent on non-resident companies engaged in online advertisement and related activities.

Key features of the new EL

Applicability – Non-resident e-commerce operators who own, operate, or manage digital or electronic facility or platform for online sale of goods or online provision of services or both and derive revenues from e-commerce supply or services made or provided or facilitated by it.

Scope of e-commerce supply or services:

- Online sale of goods owned by the e-commerce operator
- Online provision of services by e-commerce operators
- Facilitation of online sale of goods or provision of services or both by e-commerce operator
- Any combination of the above

E-commerce supply or services rendered to the following:

- A person resident in India
- A non-resident in specified circumstances
- A person who buys goods or services using an IP address located in India

Levy of 2 percent imposed on consideration received or receivable by e-commerce operators from e-commerce supply or services

Effective date: 1 April 2020

- The scope of the said provision has now been expanded to include EL of 2 percent on consideration received or receivable by an 'e-commerce operator' from 'e-commerce supply or services', and is effective from 1 April 2020.

Exclusions – Cases outside the scope of EL

- Non-resident e-commerce operators who have permanent establishments in India and e-commerce supply or services are effectively connected to those establishments
- Cases where EL is leviable on online advertisement and related activities (as these are covered by different provisions)
- Sales, turnover, or gross receipts are less than INR 20 million during the financial year

Quarterly payment and compliance

- **An annual statement needs to be furnished to the tax authorities on or before 30 June of the subsequent financial year.**

Exemption from applicability of normal income tax provisions on the revenues subjected to EL

India, US reach settlement on 2% equalisation levy

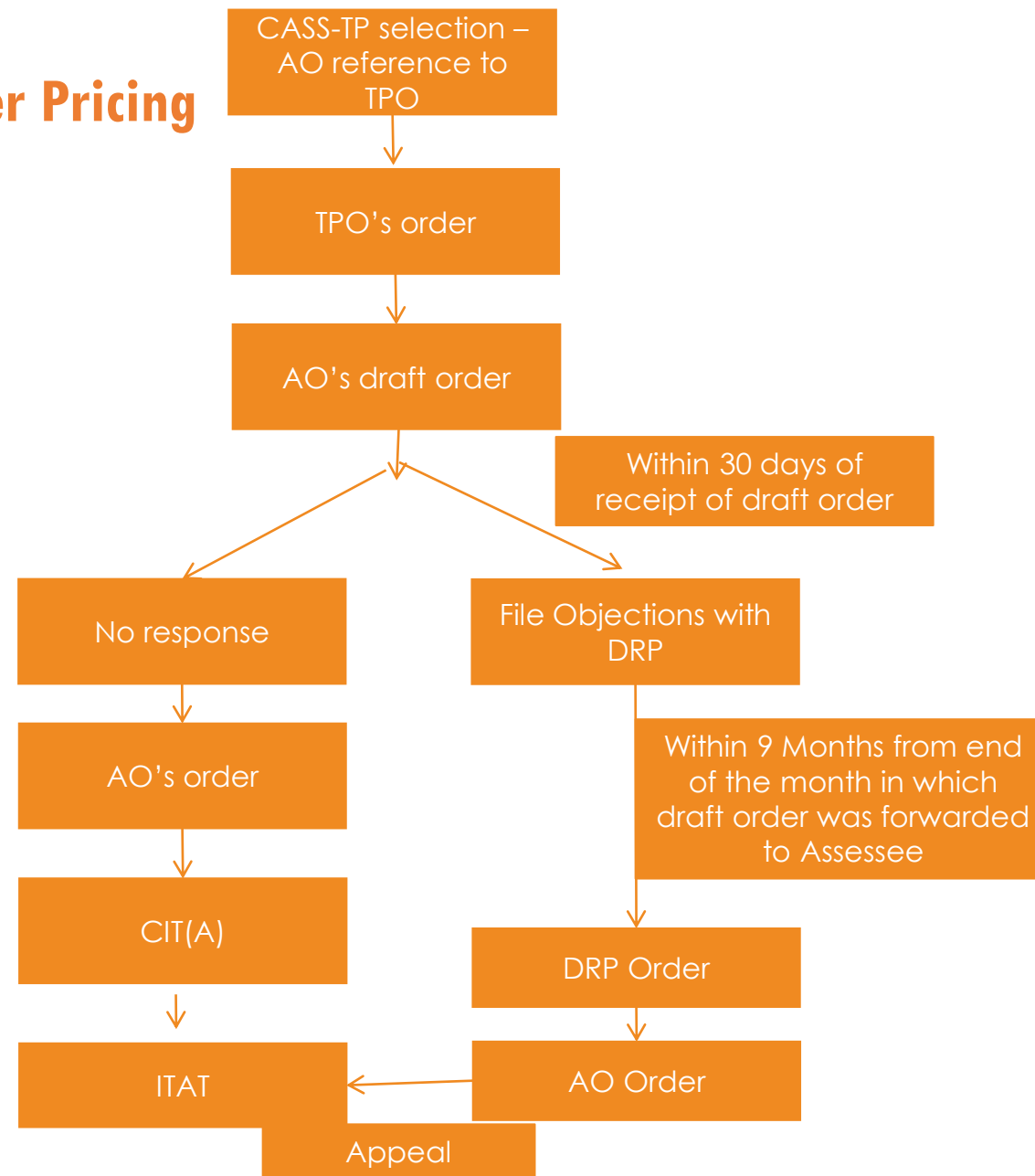
1. India and the United States have reached an agreement to settle differences relating to the 2% equalisation levy imposed by New Delhi on e-commerce operators.
 2. The settlement is based on the Unilateral Measures Compromise reached among the UK, Austria, France, Italy and Spain with the US on October 21 this year.
 3. Under the agreement
 - India will continue to impose the levy till
 - a) March 31, 2024
 - (Or)
 - b) Implementation of Pillar 1 of the OECD agreement.
- } Whichever is earlier
- The liability from India's equalisation levy on e-commerce supply of services that US companies accrue in India during the interim period will be creditable against future taxes accrued under Pillar 1 of the OECD agreement
 - The US will terminate the currently-suspended additional duties on goods of India that had been adopted in the DST Section 301 investigation.
4. The India-USA agreement on a transitional approach is beneficial to India as it can carry on with the present 2% levy with certainty until Pillar 1 takes effect
 5. Once the OECD agreement rolls out, the 2% equalisation levy will have to be withdrawn. This applies to other countries as well that have imposed a similar tax



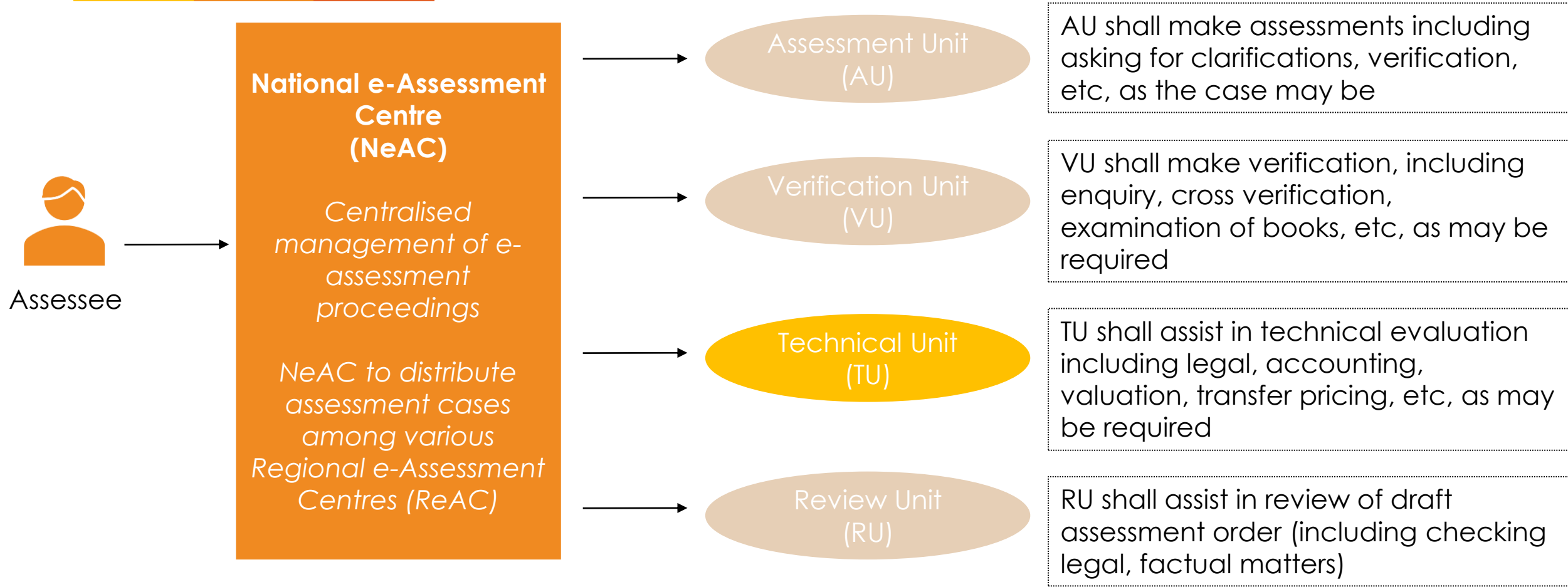
ASSESSMENT PROCEDURE



Litigation Process - Transfer Pricing



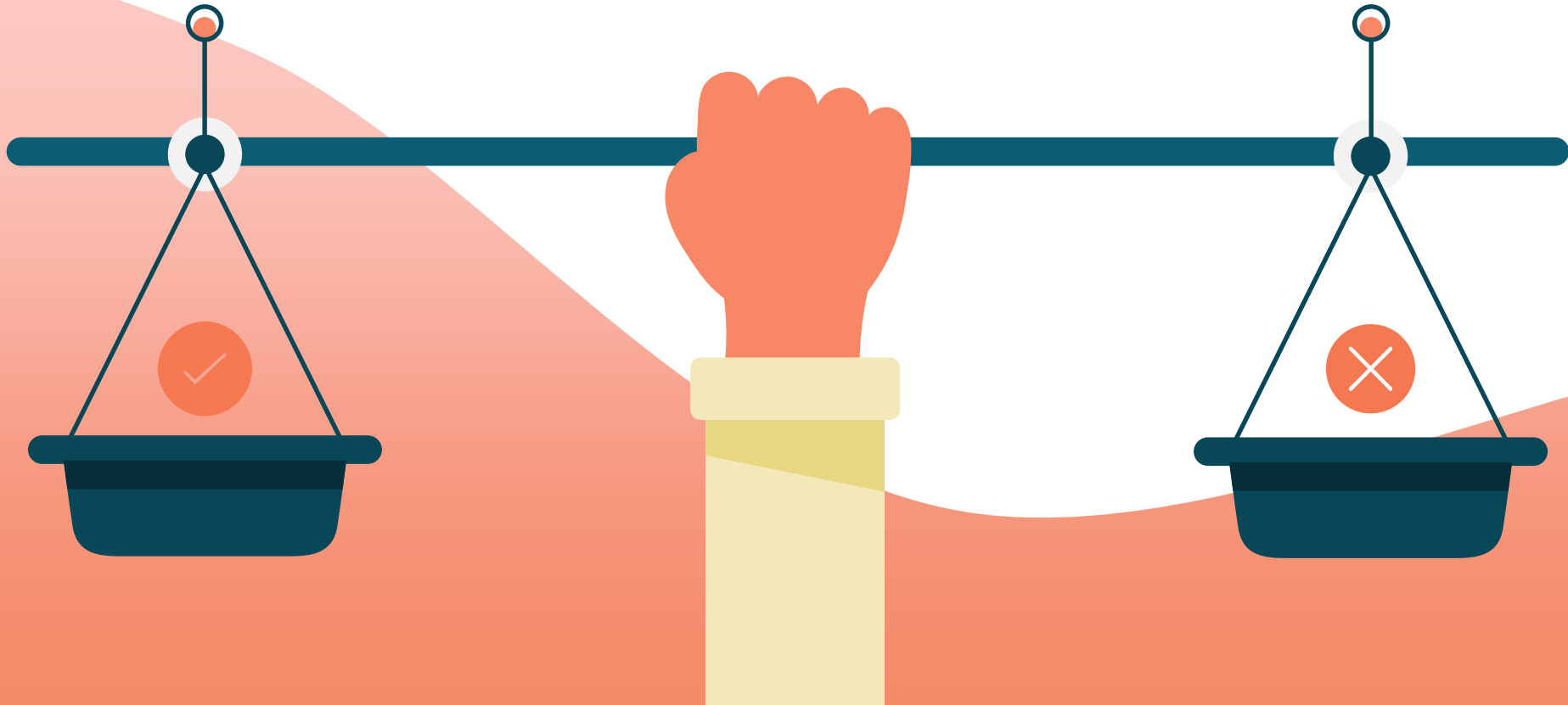
Will TP fall under Faceless Assessment?



- Whether TP will be falling under TU?
- Whether TP will continue under existing online/ manual assessment scenario?
- Whether TP will be taken care at AU level?



ALTERNATIVE DISPUTE RESOLUTION AND MITIGATION CHANNELS

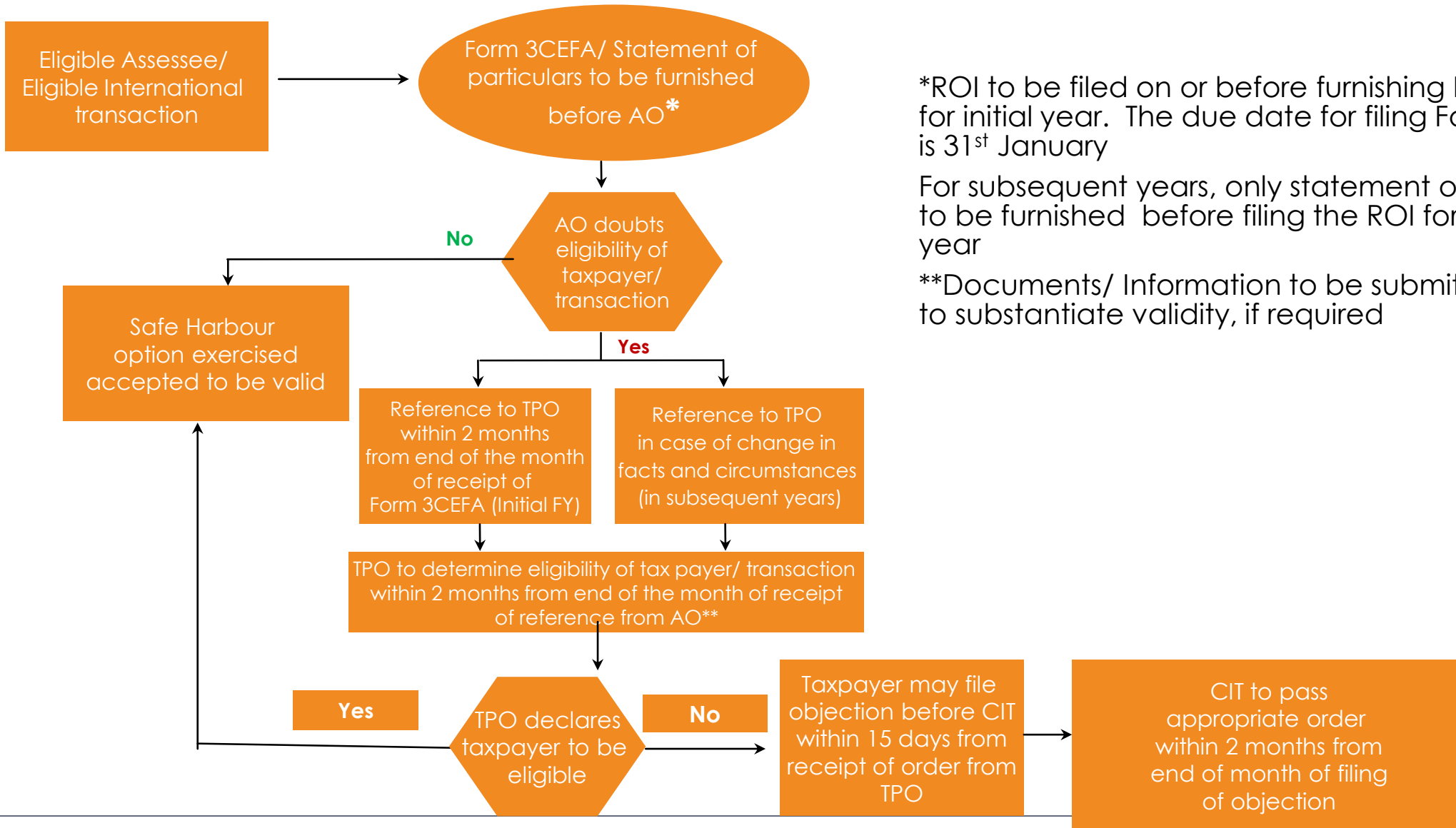


ALTERNATIVE DISPUTE RESOLUTION AND MITIGATION CHANNELS

1. Safe Harbour rules(Under Section 92CB and Rules 10TA to TG)

- A “safe harbour” is defined in the Act as circumstances in which the tax authority shall accept the transfer price declared by the assessee.
- Further, the CBDT, vide **notification 117/2021/F. No. 370142/44/2021-TPL dated 24th September 2021**, Stated that the provision of rule 10TD is extended for AY 2021-22 (*Previously only AY 2020-21 was under the purview of this rule*).
- **Compliance Requirements:**
- **FORM 3CEFA - Safe Harbour Application (International Transactions)**
- **FORM 3CEFB - Safe Harbour Application (SDT's)**

SAFE HARBOR RULES – COMPLIANCE PROCEDURE



*ROI to be filed on or before furnishing Form 3CEFA for initial year. The due date for filing Form 3CEFA is 31st January

For subsequent years, only statement of particulars to be furnished before filing the ROI for particular year

**Documents/ Information to be submitted to TPO to substantiate validity, if required

ALTERNATIVE DISPUTE RESOLUTION AND MITIGATION CHANNELS

2. Advance Pricing Agreement (APA)

- **Finance Act, 2012** had introduced the provisions of Advance Pricing Agreement ('APA') w.e.f. **1 July 2012**.
- An APA is an agreement between the CBDT and a taxpayer, which determines in advance the ALP or specifies the manner of the determination of ALP, in relation to International transactions.

(A)Types:

- Unilateral APA
- Bilateral APA
- Multilateral APA

(B)Tenure:

- The tenure of APA can be up to 5 years for onward determination of ALP.
- In case of roll back mechanism, the APA can be made applicable for a period not exceeding 4 years. Hence, the total tenure applicable for APA can be 9 years.

(C)Compliance

- APA application in Form **3CED/ 3CEDA** (for period starting from FY 2020-21)

Our Scope:

- » Framing critical assumptions during APA negotiations and collation of information and documents as per prescribed APA application form.
- » Assistance in filing the application and preparation for site visit and submission of information/ documents required from time to time
- » Conducting mock site visits
- » Follow up with the concerned authorities
- » Assisting APA negotiations and finalizing APA terms and conditions with IR.

APA— OVERVIEW OF THE PROCESS



APA – Pros and Cons

Benefits	Risks
<ul style="list-style-type: none"> ▪ Proactively avoids TP controversy - Provides certainty and enhances predictability ▪ Discussion at the “right level” ▪ Solution to complex/ difficult TP issues ▪ Eliminates/reduces risk of economic double taxation ▪ Can reduce compliance cost ▪ Concerns around domestic tax law process - Preferred means of controversy management after MAP 	<ul style="list-style-type: none"> ▪ Strain on resources for taxpayers – personnel and expenses ▪ May not provide certainty in case of a unilateral APA or if an APA involves unreliable prediction on market conditions without adequate critical assumptions ▪ Fairly detailed forms/ information request during pre-filing and application stage - normally not required in an audit ▪ Confidentiality of information submitted not clear ▪ May not always result in the desired outcome

ALTERNATIVE DISPUTE RESOLUTION AND MITIGATION CHANNELS

3. Mutual Agreement Procedure(MAP)

- MAP is an alternative available to taxpayers for resolving disputes giving rise to double taxation whether juridical or economic in nature. The agreement for avoidance of double taxation between the countries would give authorization for assistance of Competent Authorities in the respective jurisdiction under MAP. In the context of OECD Model Convention for the Avoidance of Double Taxation, Article 25 provide for assistance of Competent Authorities under MAP.

→ **Recent MAP Guidance:**

Resolution under MAP is arrived at following cases:

- Transfer Pricing adjustments
- Existence of a Permanent Establishment
- Attribution of profits to a Permanent Establishment
- Characterisation or re-characterisation of an income or expense

TP -Penalty provisions

Particulars	Penalties
(A) Documentation:	
Under-reporting and mis-reporting of income	50% - under-reporting; 200% - mis-reporting of income
In case of a post-inquiry adjustment, there is deemed to be a concealment of income u/s 271(1)(c)	100-300% of tax on the adjusted amount
Failure to maintain documents u/s 271AA	2% of the value of each International Transaction/SDT
Failure to furnish documents/report transaction u/s 271G	2% of the value of the International Transaction/SDT
Failure to furnish accountant's report u/s 271BA	Rs 100,000
Omission or false entry in books of accounts u/s 271AAD	Penalty equal to amount of such false entry

Penalty provisions [section 270A] - Finance Act 2016

(B) Master File:	
Not maintaining and filing the required information in the master file within the due date u/s 271AA	INR 500,000/-
(C) CbCR:	
Non-filing of CbC report by Indian resident parent company u/s 271GB are :	<ul style="list-style-type: none"> • INR 5,000 per day up to one month • INR 15,000 per day beyond one month • INR 50,000 per day for continuing default after service of notice
Not furnishing the information called for by the tax authority within the given time limit	<ul style="list-style-type: none"> • INR 5,000 for every day up to the service of the penalty order • INR 50,000 per day for the default beyond the date of service of the penalty order
Furnishing inaccurate particulars/not filing the corrected CbC report within 15 days	INR 500,000/-

Due Dates

TP document, Master File and CbCR Compliances for the FY 2020-21		
Particulars	Form	Due Date
TRANSFER PRICING DOCUMENTATION		
• Maintenance of Transfer Pricing Documentation u/s 92D	-	31st January 2022
• Certification and Filing of Form 3CEB u/s 92E	Form 3CEB	31 st January 2022
MASTER FILE		
• All CE s of International Group, irrespective of whatever satisfying the threshold limits or not	Part A of Form 3CEAA	28th February 2022
• All CE s of International Group, Crossing the Master File threshold Limits Notified	Part A and Part B of Form 3CEAA	
• Case more than 1 entity in India is crossing the Master File threshold limits Notified	3CEAB	29 th January 2022 (30 days prior to Filing Form 3CEAA)

Due Dates - Continuation

CbCR		
<ul style="list-style-type: none"> Intimation of the Indian CE being alternate reporting entity or that the Parent entity is filing CbCR 	3CEAC	31 January 2022 (2 Months prior to Filing Form 3CEAD)
<ul style="list-style-type: none"> This form is to specify in which country the Group is filing CbCR and is applicable only when the Parent Company of the Group is Estd in India 		
<ul style="list-style-type: none"> Indian Parent Company Indian Alternate reporting entity CE resident in India satisfying 286(4) (No Agreement for Information Exchange) 	3CEAD	31 March 2022
<ul style="list-style-type: none"> 2 or More CE s Resident of India are falling under 286(4) category. (No Agreement for Information Exchange; or Resident CE s of Group having Indian Parent 		
	3CEAE	Due Date has not been notified yet CE resident in India satisfying 286(4) (No Agreement for Information Exchange)



**G20/OECD Inclusive
Framework on BEPS:
Report on P1 and P2 Blueprint**

OECD Evolution and work so far



Action Plans on Base Erosion and Profit Shifting

AP 1: FINAL REPORT Addressing the Tax Challenges of Digital Economy

INTERIM REPORT OECD/G20 under inclusive framework; Tax Challenges arising from Digitalisation

Public consultation document and Programme of work to develop consensus

Reports on the Blueprints to Pillar 1 and 2 and invitation of comments

Public Consultation meetings

G7 Communiqué

Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy

Background of P1 and P2

- ❖ OECD and G20 countries have adopted a 15-point Action Plan to address BEPS in September 2013. The Action Plan identified 15 actions along with three key pillars:
 - Introduce Coherence in domestic rules that affect cross-border activities
 - Reinforce substance requirements in existing International Standards
 - Improve transparency as well as certainty
- ❖ The 137 members of the Framework have worked on a global solution based on a **Two-Pillar Approach**. Pillar One is focused on new nexus and profit allocation rules and ensure that the allocation of taxing rights with respect to business profits is no longer exclusively circumscribed by reference to physical presence.
- ❖ Pillar Two addresses remaining BEPS challenges and it does so via a number of interlocking rules that seek to
 - (i) ensure minimum taxation while avoiding double taxation or taxation where there is no economic profit,
 - (ii) Cope with different tax system designs by jurisdictions as well as different operating models by businesses,
 - (iii) Ensure transparency and minimize administrative & compliance costs.

Pillar 1 – Amount A

- **Amount A** is a new taxing right over a share of the residual profit of MNE groups that fall within its defined scope. The tax base is therefore determined on the basis of the profits of a group (rather than on a separate entity basis), and it is necessary to start with consolidated group financial accounts.
- A new taxing right for market jurisdictions over a share of residual profit calculated at an MNE group (or segment) level (**Amount A**)
- A fixed return for certain baseline marketing and distribution activities taking place physically in a market jurisdiction, in line with the ALP (**Amount B**)
- Processes to improve **tax certainty** through effective dispute prevention and resolution mechanisms.

Scope of Amount A

Global Threshold Limit:

MNE Groups with Global Turnover above **€20 B**
 &
 Profitability above **10%**
(PBT/ Revenue)

NEXUS: Local Revenue

1) € 1M for > €40 B GDP countries.
2) € 2.5 M for < €40 B GDP countries.

Automated Digital Services:

1. Advertisement Services
2. Sale/other Allocation of user data
3. Online Intermediation Platforms
4. Digital Content Services
5. Online Gaming

Real-Time location of User –
 Based on Indicators below:

- Geolocation
- IP Address
- Other Location Information

Consumer Facing Businesses:

1. Consumer Facing goods
2. Consumer Facing Services
3. License or Franchise

Report by Licensee or Franchisee

Place of Final Delivery of the Product or use of service

Exclusions: Extractives (non-renewable resources) and regulated financial Services

Revenue Sourcing rules –

Note: 1) **Hierarchy of Indicators** should be followed. If not, MNE should justify the reason for not availing.
 2) MNE must retain the **Documentation** of

- Internal Control Framework related revenue sourcing.
- Indicators used for Present category.

New Taxing Right

Profit Allocation:

- 1) Isolate the Routine profits & Residual profits. Threshold Limit = 10% of Revenue.
- 2) 25% fixed reallocation is used to allot appropriate share of residual profits to market jurisdictions.
- 3) Finally, Amount A is distributed based on the rules on Scope, Nexus & Revenue Sourcing.

Double Taxation Elimination:

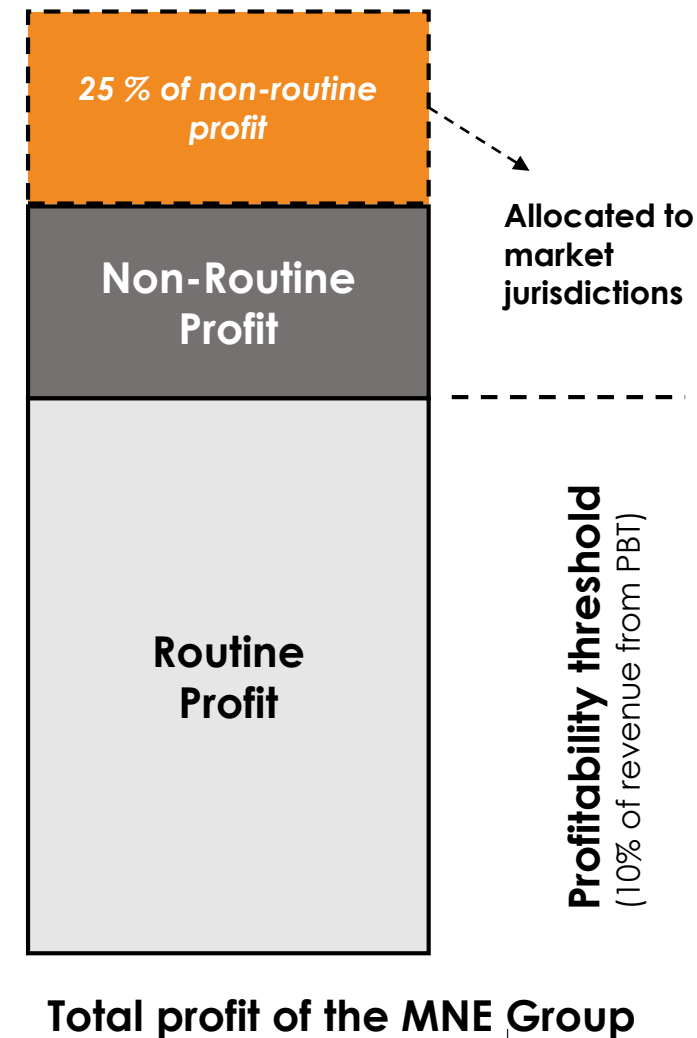
1. Identify the paying entity

- I Activities Test
- II Profitability Test
- III Market connection priority test
- IV Pro-rata allocation

2. Exemption or Credit Methods are used to eliminate double taxation.

Tax Base determination:

1. Use PBT derived from Consolidated Financial Statements.
2. Segmentation framework Threshold is yet to decide.
3. In-regime Losses can be carry forward.
4. No cross segment blending of Profits & losses are allowed



Case Study (modified as per Guidelines released by OECD in October 2021)

Facts

Group A is a large MNE group providing exclusively in-scope ADS via an online platform. It is assumed that Group A is treated as one segment for Amount A purposes and that it has the following simplified income statement:

	in million EUR
Revenue (R)	25,000
Profit before tax (P)	6,500
PBT margin (P/R)	26%

in million EUR	Local revenue (\$)	
Market 1	2,000	local subsidiary
Market 2	18,000	remote activity
Market 3	5,000	remote activity
Total	25,000	

Applying Amount A formula

Step 1: Profitability Threshold

Step 2: Reallocation percentage

Determine Group A's **residual profit (W)** by subtracting 10% from the PBT margin (P/R).

Determine Group A's **allocable tax base (A)** by multiplying residual profit (W) by 25%.

$$W = P - (R * 10\%)$$

$$A = 25\% * W$$

$$W = 6,500 - (25,000 * 10\%)$$

$$A = 25\% * 4,000$$

$$W = 4,000$$

$$A = 1000$$

10% is a threshold agreed by the IF members

25% is a threshold agreed by the IF members

Case Study (Contd)

Step 3: Allocation key

Allocation key based on the ratio of locally sourced revenue (S) to total revenue (R). This last step provides for the quantum of Amount A taxable in each eligible market jurisdiction (M), as described in the below table.

in million EUR	Local revenue (S)	Allocation Key (S/R)	Amount A (M)
Market 1	2,000	8%	$A * S/R = 80$
Market 2	18,000	72%	$A * S/R = 720$
Market 3	5,000	20%	$A * S/R = 200$
Total	25,000	100%	1000

Amount B – Introduced to simplify the TP Rules for tax administrations & Taxpayers -

The application of the arm's length principle to in-country baseline marketing and distribution activities will be simplified and streamlined, with a particular focus on the needs of low capacity countries. This work will be completed by the end of 2022.

Tax Certainty

Dispute Prevention & Resolution:

1. New mechanism Using panels.
2. Amount A allocation to be improved by panels.
3. Encourages Multilateralism in tax matters.

Dispute Resolution:

1. Mandatory binding dispute resolution mechanisms.
2. Foe countries with few MAP cases deferred from MAP peer review.

Implementation & Administration:

- Implementation of Pillar 1 require action across –
1. Domestic law
 2. Public International law
 3. Guidance on Scope , Nexus & Revenue sourcing rules to Taxpayers & Tax Administrations.
 4. Guidance could be revised & reviewed periodically

Pillar 2 – Global Minimum Tax rule

Applicability of Global Anti-Base Erosion (GloBE):

GloBE rules will apply to MNEs that meet the € 750 million threshold

Pillar 2:

Two interlocking domestic rules of GloBE –

- (i) Income Inclusion Rule (IIR): Which imposes **top-up tax** on a parent entity in respect of the **low taxed income** of a constituent entity; if that income was subject to tax at an Effective Tax Rate (ETR) that is below a minimum rate
- (ii) Undertaxed Payment Rule (UTPR): **Denies deductions** or requires an equivalent adjustment to the extent the low tax income of a constituent entity is not subject to tax under an IIR i.e., **withholding tax for a payment to a related party** if that payment was not subject to tax at or above a minimum rate.

Carve Outs and Carry forward

Carve-outs:

The GloBE rules will provide for a *formulaic substance carve-out* that will exclude an amount of income that is **5% of the carrying value of tangible assets and payroll**. In a transition period of 10 years, the amount of income excluded will be 8% of the carrying value of tangible assets and 10% of payroll.

Carve-out allows countries to continue to **offer tax incentives** to promote business activity with real substance, like building a hotel or investing in a factory.

The GloBE rules will also provide for a de minimis exclusion for those jurisdictions where the MNE's revenue is less than €10 million and profits of less than € 1 million.

Carryforward:

Excess Taxes	Losses
If excess tax paid in previous year, create an Income Inclusion Rule tax credit (IIR tax credit) (Or)	Losses in jurisdiction carryforward and allowed as deduction in computation of GloBE tax base is subsequent year from profits arising in same country.
local tax carry- forward is created, 7 year look back/Carry forward period.	Carry-forward allowed Indefinitely.

General points on P2

Entities not subject to GloBE rules:

- Government entities,
- International organizations,
- NPOs,
- pension funds or investment funds that are Ultimate Parent Entities (UPE) of an MNE Group or any holding vehicles used by such entities, organizations or funds.

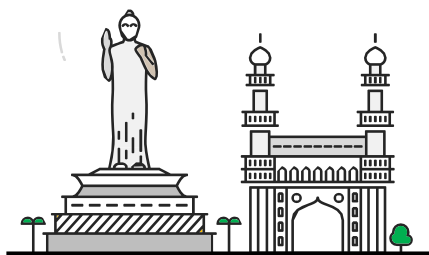
Switch-over rule (SOR):

Introduced into tax treaties that would permit a residence jurisdiction to **switch from an exemption** to a **credit** method where the profits attributable to a permanent establishment (PE) are subject to an effective rate below the minimum rate. |

Subject to tax rule (STTR):

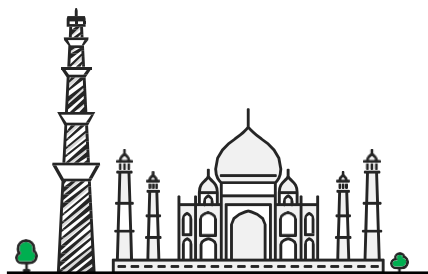
Treaty-based rule, that would complement the UTPR by subjecting a payment to withholding or other **taxes at source** and adjusting eligibility for **treaty benefits on certain items of income** where the **payment is not subject to tax at a minimum rate**. The STTR will be creditable as a covered tax under the GloBE rules. |

Contact us



HYDERABAD

Suite 5, Level 3, Reliance Cyber
Ville., Madhapur, Hitech City,
Hyderabad – 500081



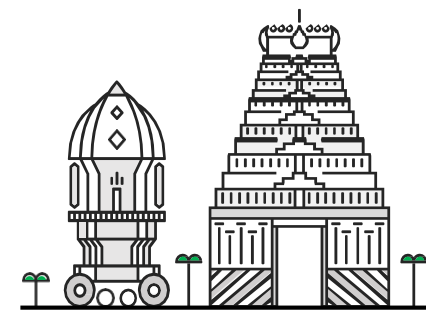
DELHI

C- 699A, 1st Floor, Sector-7, Palam
Extn., Dwarka, New Delhi, Delhi
110075



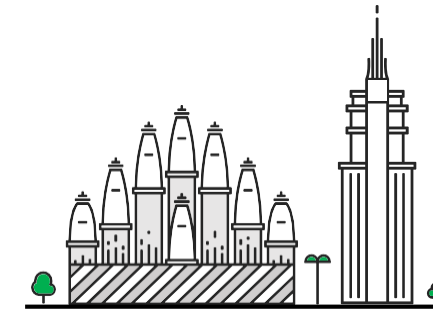
MUMBAI

Flat no.3, Plot no.226/227, Sion
East, Mumbai - 400022



CHENNAI

Old no 19, New no 13B, New
Bangaru colony first Street, KK
Nagar West, Chennai 600078



BANGALORE

90/1, 3rd Floor, Pasha South
Square, Rathavilas Road,
Basavangudi, Bangalore -
560004

Vizag: Level 3, Kupilli Arcade, Akkayyapalem, Visakhapatnam 530016,
Andhra Pradesh

Vijayawada: # 56-11-3, Sri Devi Complex, Y.V.R Street, MG Road, Patamata, Vijayawada, Andhra
Pradesh

Tirupati: H. No: 6-154/1, Syamala Nilayam, Near Water Tank, Akkarampalli, Tirupathi, Andhra Pradesh

Kurnool: #21, Top Floor, Skandanshi Vyapaar, New Bus Stand Road, Kurnool 518 003, Andhra
Pradesh



UAE Address: 2103, Bayswater Tower, Business Bay, Dubai,
UAE



USA Address: SBC LLC, 8 The Green, Suite A in the City
of Dover, Delaware - 19901

Thank You



www.steadfastconsultants.in

