Base Erosion & Profit Shifting (BEPS) Implementation in India in Building Transfer Pricing Capacity

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BEPS Project

- ✓ World-wide concern over double non-taxation or less than single taxation.
- ✓ Challenges posed by the changing business models, digital economy, inadequacy of the definition of PE, transfer pricing outcomes not in line with value creation, etc.
- ✓ The G-20 Finance Ministers called on the OECD to develop an Action Plan to comprehensively tackle BEPS.
- ✓ 15 point Action Plan announced in 2013 and Reports on all 15 issues released and approved in 2015.

BEPS Through Transfer Pricing

- ✓ Generally, the Transfer Pricing rules, based on the Arm's Length Price or Arm's Length Principle (ALP), are able to align economic activities with income and pricing.
- ✓ However, the ALP principle is sometimes mis-used to artificially segregate income from economic activities and shift such income to low-tax jurisdictions.
- ✓ Contractual transfer of risks or allocation of excessive capital to low tax jurisdictions also results in shifting income to such jurisdictions.

Transfer Pricing Regime in India

- ✓ Transfer Pricing provisions introduced in India in 2001 w.e.f. Financial Year 2001-02.
- ✓ The OECD model of transfer pricing was adopted with some modifications.
- ✓ One of the significant modification was adoption of Arithmetic Mean of comparable companies' profit margins instead of a range or median.

Transfer Pricing Regime in India

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- ✓ The founding principle of transfer pricing provisions in India is to compute income arising from an international transaction having regard to the arm's length price.
- ✓ Arm's length price is the price that would prevail in transactions between two unrelated parties – in other words, the market price.
- ✓ TP provisions apply to transactions between Associated Enterprises (AEs).

Transfer Pricing Regime in India

- ✓ Computation of income from international transactions to be made as per section 92 of Income Tax Act, 1961.
- ✓ Meaning of Associated Enterprise prescribed in Section 92A of Income Tax Act, 1961.
- ✓ Meaning of International Transaction prescribed in Section 92B of Income Tax Act, 1961.
- ✓ Subsequently, certain Specified Domestic Transactions have also been included under our TP provisions w.e.f. 01/04/2013.

Transfer Pricing Regime in India

- ✓ ALP to be determined after carrying out a FAR (Functions, Assets, Risks) analysis.
- ✓ Based on the FAR analysis, most Appropriate Method to be chosen from the following 6 methods:
- ✓ Comparable Uncontrolled Price Method (CUP)
- ✓ Resale Price Method (RPM)
- ✓ Cost Plus Method (CPM)
- ✓ Profit Split Method (PSM)
- ✓ Transactional Net Margin Method (TNMM)
- ✓ Any Other Method

Transfer Pricing Regime in India

The Organisational Structure

- ✓ The TP regime in India is administered across the country through 14 Commissionerates. Each Commissioner of Income-tax (Transfer Pricing) has 3 Additional/Joint Commissioners working under him/her.
- ✓ Each Additional Joint Commissioner, in turn, has 2 Deputy/Assistant Commissioners working under him/her.
- ✓ Oversight on all the Commissionerates is exercised by 3 Chief Commissioners of Income-tax.

Transfer Pricing Regime in India

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Recent Developments:

- ✓ Adoption of an Arm's Length Range in addition to the Arithmetic Mean.
- ✓ Use of Multiple Year data to decide the ALP.
- ✓ Risk-based selection of cases for TP audit instead of monetary threshold.
- ✓ Secondary Adjustment.
- ✓ Limitation of interest deduction.

Transfer Pricing Regime in India

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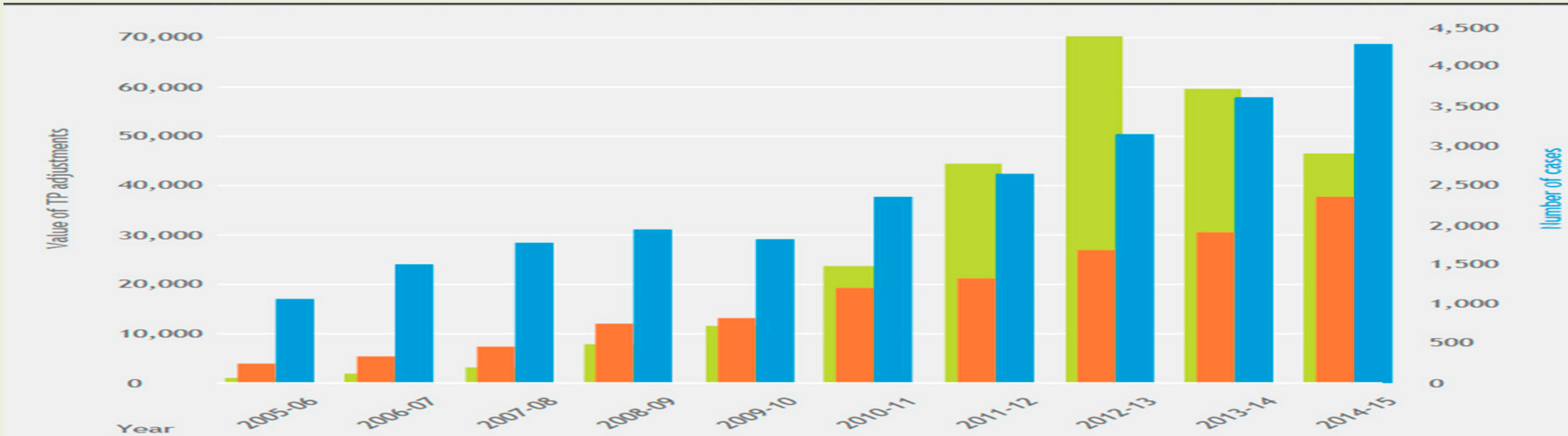
Number of Audits and Amount of Adjustments



Year	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Amt. of Adjustments (in cr.)	1,220	2,287	3,432	7,754	10,908	24,111	44,532	70,016	59,602	46,466
No. of TP audits completed	1,061	1,501	1,768	1,945	1,830	2,368	2,638	3,171	3,617	4,290
No. of adj.cases	239	337	471	754	813	1,207	1,343	1,686	1,920	2,353

Amt. of Adjustments (in cr.) No. of TP audits completed No. of adj.cases

Transfer Pricing Regime in India

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- ✓ For Resolution of TP disputes and reducing litigation arising from TP audit, the Government has taken a number of steps in the recent past, such as:
- ✓ Setting up of 9 Dispute Resolution Panels (DRP) with 3 Commissioners on each panel to take a final view on TP adjustments proposed by the Transfer Pricing Officer
- ✓ Advance Pricing Agreement (APA) Scheme with Rollback provisions
- ✓ Safe Harbour Rules for certain transactions

Implementation of TP Elements of BEPS Project in India (1/5)

- ✓ Actions 8,9,10 and 13 of the BEPS Project deal with transfer pricing.
- ✓ Actions 8,9 and 10 primarily rewrote rules and guidance that seek to align value creation with transfer pricing outcomes so as to ensure that appropriate remuneration is given to value creating activities in the jurisdiction where such activities take place.
- ✓ India has always supported this notion and hence, the revised TP guidelines issued by OECD have been broadly accepted.

Implementation of TP Elements of BEPS Project in India (2/5)

- ✓ Except the recommendation on low value-added intra-group services, India has endorsed all the recommendations arising from the new transfer guidelines based on Actions 8,9 and 10 of the BEPS Project.
- ✓ Action 13 of the BEPS Project pertains to a new 3-tiered documentation regime for transfer pricing with a Master File for the entire Multinational Enterprise (MNE) group; a Local File for the local subsidiary; and a Country-by-Country (CbC) Report for the MNE group's performance in all jurisdictions.

Implementation of TP Elements of BEPS Project in India (3/5)

- ✓ India has implemented the new documentation regime in full measure with legislative amendments in the Income-tax Act, 1961 to usher in provisions for filing and sharing of CbC Reports [Section 286] and filing of Master File [Proviso to Section 92D(1)].
- ✓ India has also signed the Multilateral Competent Authority Agreement (MCAA) and a Bilateral Agreement (with USA) to automatically exchange CbC Reports with various countries.

Implementation of TP Elements of BEPS Project in India (4/5)

- ✓ Even prior to BEPS, India had a robust Transfer Pricing regime with a large network of TPOs doing a number of TP audits every year
- ✓ Transfer Pricing audit was seen as an important instrument to prevent profit shifting from India
- ✓ Aggressive TP structures were carefully analysed by TPOs and appropriate remedial actions were taken

Implementation of TP Elements of BEPS Project in India (5/5)

Challenges Ahead:

- ✓ With transfer pricing issues becoming more complex by the day, constant up-gradation of skills of officers is needed.
- ✓ Litigation management.
- ✓ Balancing tax certainty with the need to curb BEPS through TP is the real challenge!

Thank You