

Workshop on Transfer pricing
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International Transaction (92B)
&
Specified domestic transactions (92BA)

PVSS Prasad, FCA
pvsatya.prasad@gmail.com

AGENDA

- International Transactions - Sec 92B(1)
- Deemed International Transactions – Sec 92B(2)
- Specified Domestic International Transactions- Sec 92BA

International Transactions

International transaction (Sec 92B)

- Transactions between two or more associated enterprises
- 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 in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

International Transactions

International transaction (Sec 92B) - Explanation

- The expression 'International transaction' includes -
 - a) Purchase, sale, transfer, lease or use of tangible property
 - b) Purchase, sale, transfer, lease or use of intangible property
 - c) Capital financing, any type of borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payment or deferred payment or receivable or any other debt arising in the course of business
 - d) Provisions services
 - e) Transaction of business restructuring or reorganization entered irrespective of the fact that it has a bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date

International Transactions

Examples of International Transactions:

- Sale of goods or services
- Purchase of goods or services
- Commission
- Royalty payments
- Management fee
- Issue of share capital
- Purchase of Fixed Assets
- Reimbursement of expenses

Corporate Guarantee- is an international transaction?

- Generally corporate guarantee (“CG”) can be in the following forms:
 - CG extended by Indian company on behalf of its foreign AE to **the foreign branch of an Indian bank**
 - Can it be considered as a transaction between two Indian entities?
 - CG is extended by Indian company on behalf of its foreign AE to **the AE’s foreign bank.**
 - CG is extended by Indian company **through Indian bank in the form of of *Stand-By Letter of Credit* (‘SBLC’) or *Letter of Comfort* (‘LOC’) to the bank of its foreign AE.**
- It is always a challenge to benchmark CG transactions with Associated Enterprises.

Corporate Guarantee- is an international transaction?

- What will be the best method to benchmark the transaction of 'Corporate Guarantee'
 - Third report of Rangachary Committee on Safe Harbors considered the following generally accepted economic methods for benchmarking intra-group guarantee
 - Yield Approach/Spread Method
 - Interest saving method
 - Capital infusion method
 - Risk of Loss Approach or Insurance method
 - Credit Default Swap Approach
 - Option pricing method

Corporate Guarantee- is an international transaction?

- TPO's approach in benchmarking the transaction 'corporate guarantee' is generally as follows
 - Collecting bank guarantee rates from various banks and comparing with corporate guarantee given by the assessee to its Associated Enterprises
- Judicial precedents in relation to this issue
 - Bank Guarantee cannot be compared with Corporate Guarantee
(Glenmark Pharmaceuticals- (TS-1268-SC-2018-TP)
 - Any rate between 0.25% to 0.53% as a Guarantee commission can be treated as ALP
(GVK Power & Infrastructure Ltd Vs ACIT [2018] 94 taxmann.com 415 (Visakhapatnam - Trib.))
 - If there is any agreement which provides inherent compensation benefit, if AE fails to repay the loan for which assessee provides guarantee, then that inherent benefit is considered as an appropriate consideration and no further adjustment required. **(KEC International Ltd [TS-674-ITAT-2019(Mum)-TP])**
 - CG to the third party lenders as a matter of commercial prudence to protect its interest of investment by fulfilling the shareholders obligation cannot be considered as an International Transaction if no cost is incurred by the Assessee - **[2018] 89 taxmann.com 417 (Kolkata - Trib.)**

Interest on trade receivables

- In the recent past the issue of outstanding inter-company trade receivables has been receiving special attention from the TPOs.
- It is seen that:—
 - the TPOs typically call for ageing details of trade receivables arising out of inter-company sales;
 - where such receivables are outstanding for more than the standard credit period extended to debtors (related or unrelated party) TPOs have shown a tendency to impute a notional interest;
 - the notional interest is generally the bond yield rate /SBI PLR/ Term deposit rate as the case may be.

Interest on trade receivables

■ Issues

- whether the transaction is an international transaction
- whether aggregation approach (receivables with sales) survives
- whether WCA to comparables will take into account the impact of outstanding receivables on the profitability.
- whether trade payable dues to AEs shall also be considered while computing notional interest on trade receivables.
- where assessee is a debt free company even then the adjustment of notional interest is justifiable?
- Where an assessee does not charge unrelated debtor, is it justified to impute interest on receivables from AE?

Interest on trade receivables

▪ Judicial precedents on this Issue

- To the extent of agreed credit period the sale price to AE or non-AE is inclusive of possible interest for such credit allowed to AE and therefore it cannot be said that this is an independent international transaction -
AMD India (TS-840-ITAT-2017(BANG)-TP
- The tax authorities should also give due weight to long outstanding payables before imputing interest on receivables. -
WNS Global Services (P.) Ltd. [2019] 103 taxmann.com 75 (Mumbai - Trib.)
- Delay in collection of money may be due to different reasons and requires investigation on a case to case basis
(Kusum Health Care Private Limited – ITA 765 of 2016 Delhi-HC)
- Working capital adjustment will take into account the impact of outstanding receivables on the profitability-
(Kusum Health Care Private Limited – ITA 765 of 2016 Delhi-HC)
- TP adjustment cannot be made on hypothetical and notional basis until and unless there is some material on record that there has been under charging of real income-
(Evonik Degussa India (P.) Ltd. [2016] 76 taxmann.com 313 (Mumbai - Trib.))
- When unrelated debtors are not charged any interest for delay in payments, it is justified not charging for the delay w.r.t receivables from AE this itself is an Internal CUP
(Axis Risk Consulting Services (P.) Ltd Vs DCIT [2018] 92 taxmann.com 103 (Delhi - Trib.))

Share application money

- Whether Share application money pending allotment can be treated as loan given to AE?
- In other words, whether notional interest for the period from the initial payment to the date on which the shares were actually allotted shall be considered as an International Transaction?.

Issues to be considered

- Can the above said transaction be considered as an international transaction at all
- Can it be said that payment of share application money is a capital contribution and is commercially different from a loan.
- If yes, under which method the above said transaction shall be benchmarked

Share application money

■ TPO's approach

- Re-characterizing the share application money as interest free advance and imputing notional interest.
- Share application money for allotment of shares but no shares were allotted to assessee till end of financial year and this money was available with AE of assessee for utilization, said sum would lose character of share application money and would constitute an international transaction as per provisions of section 92B as it had a direct bearing on profit and loss as well as assets of enterprises as it would constitute advance to AE
 - Upheld in ***Logix Microsystems Ltd [2017] 80 taxmann.com 39 (Bangalore - Trib.)***

Share application money

▪ Judicial Precedents

- It is not an international transaction
 - ***Hill County Properties Ltd [2015] 57 taxmann.com 400 (Hyderabad - Trib.)***
 - ***Bartronics India Ltd [2017] 86 taxmann.com 254 (Hyderabad - Trib.)***
 - ***Moserbaer India Ltd. [2018] 98 taxmann.com 457 (Delhi - Trib.)***
- It is an international Transaction
 - ***Logix Microsystems Ltd. 2017] 80 taxmann.com 39 (Bangalore - Trib.)***
- Investments in nature of equity cannot be treated as loans and advances
 - ***Prithvi Information Solutions Ltd [2014] 49 taxmann.com 176 (Hyderabad - Trib.)***
- Onus is upon Assessing officer to prove the contrary that it is an international transaction
 - ***Unitech Ltd [2019] 104 taxmann.com 165 (Delhi - Trib.)***
- a transaction of subscription of shares could not be re-characterized as loan
 - ***Aegis Ltd. [2017] 78 taxmann.com 275 (Mumbai - Trib.)***

Bad debts written off

- whether bad debts written off can be treated as a separate International Transaction?
 - As the original transaction is benchmarked in earlier years for sale of goods/services
 - If the same has to be considered as a separate international transaction then how to benchmark the transaction.
 - Writing off bad debts is common business exigency in respect of sales made both to Non AE and AE

Deemed International Transaction

Deemed International transaction (Sec 92B(2))

- Section 92B(2) of the Act creates a deeming fiction which extends the ambit of the term international transaction to include the transactions with Non-AEs (unrelated third parties) provided either of the two conditions mentioned below are fulfilled:
 - 1) There exists a prior agreement in relation to the subject transaction between the third party and the AE of the entity. (or)
 - 2) Terms of the relevant transaction are determined in substance between AE of Indian taxpayer and such third party

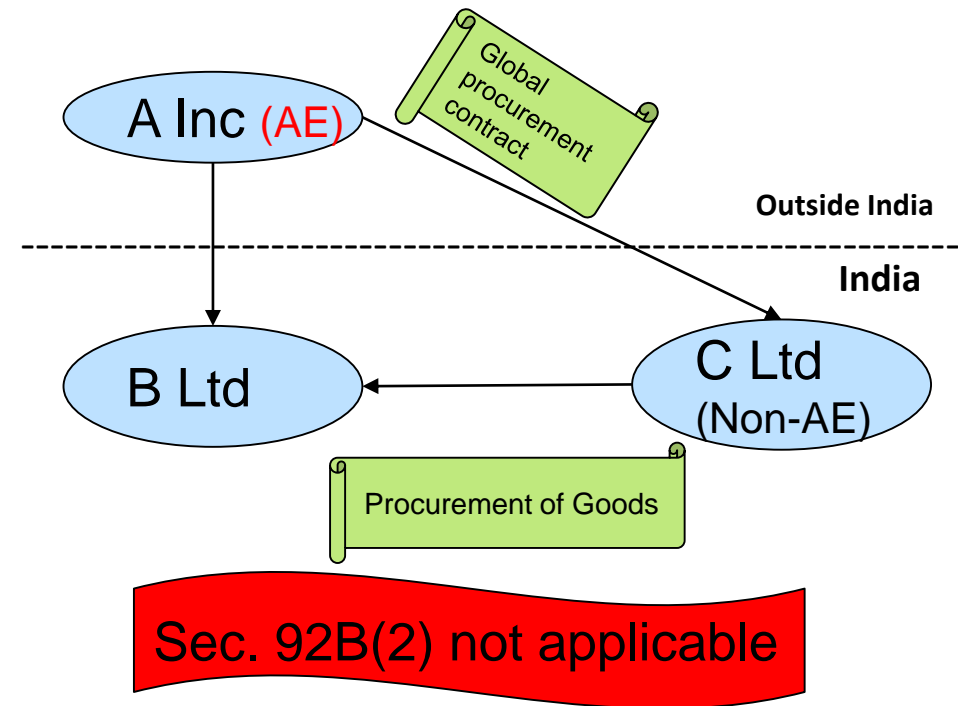
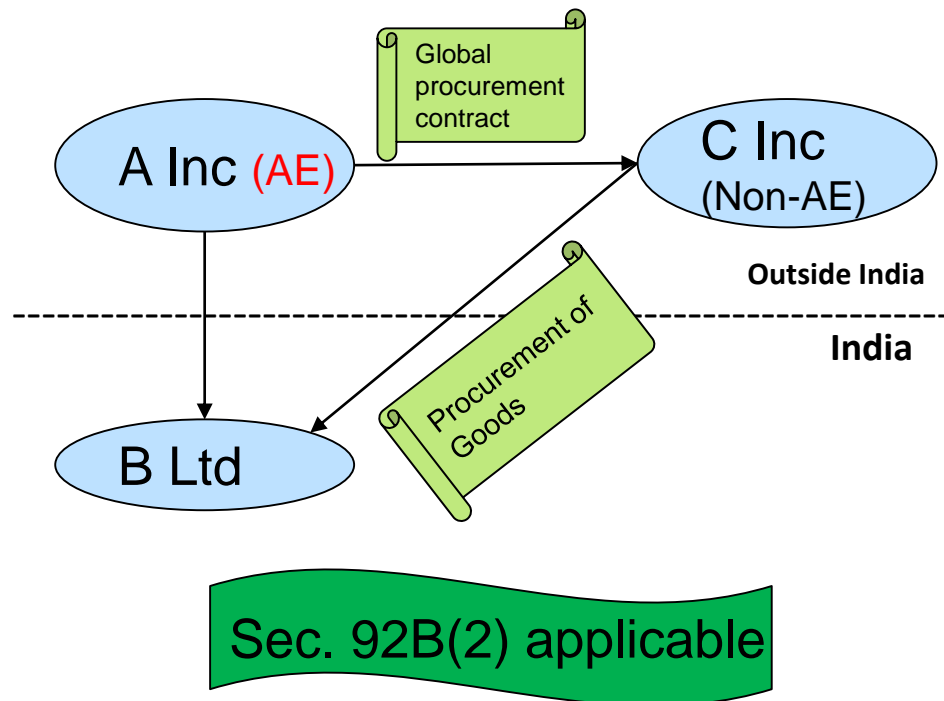
Note: The residential status of the 'third party' is not relevant to invoke the deeming fiction under clause (2) of section 92B of the Act. – (included by Finance Act 2014)

****Circular 14 of 2001 dated 22-11-2001***

Deemed International Transaction

Position prior to Finance Act 2014 amendment

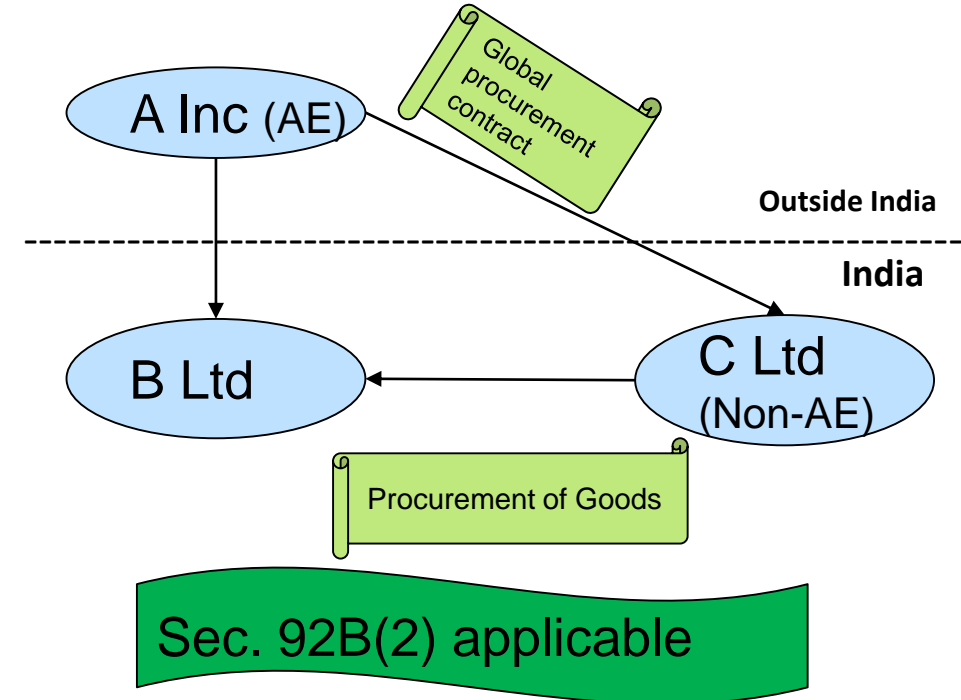
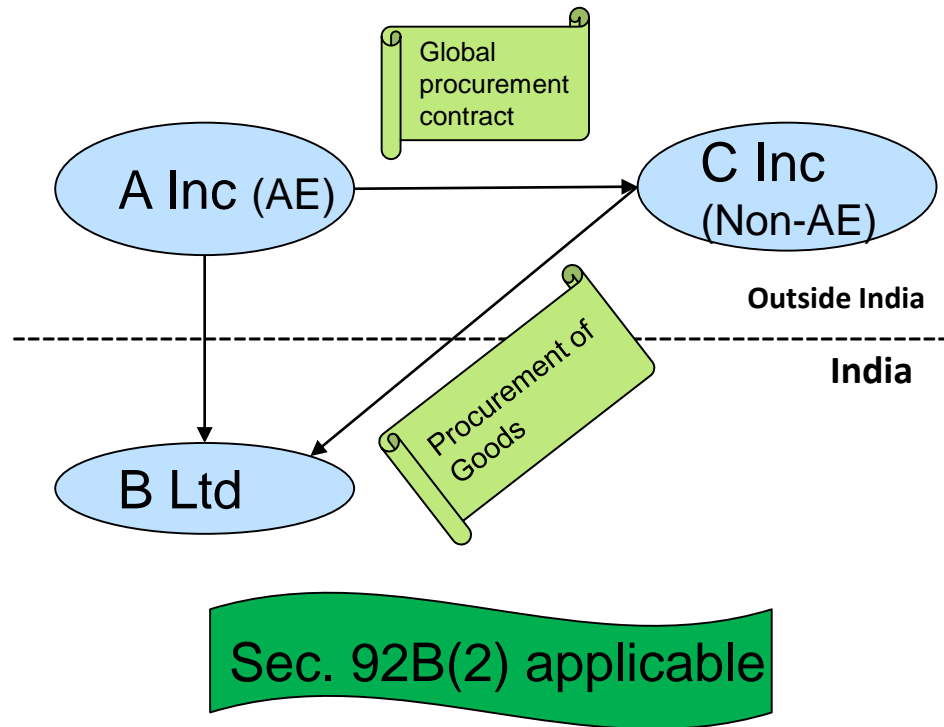
- Unlike section 92B(1), which makes it clear that at least one of the parties to a transaction must be a non-resident. Section 92B(2) does not mention whether or not the unrelated party in the transaction is required to be a non-resident.



Deemed International Transaction

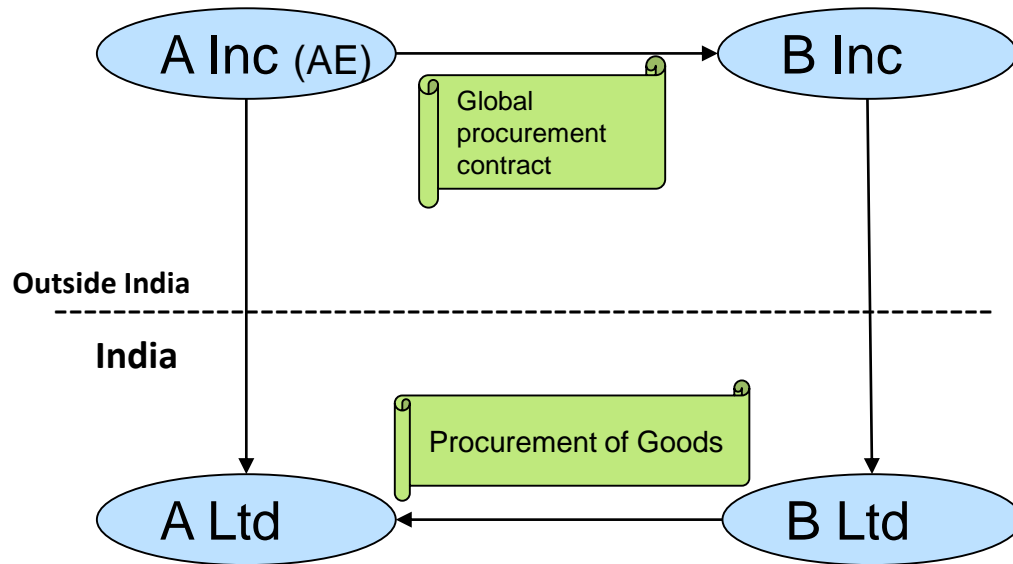
Position post amendment by Finance Act 2014

- Now, section 92B(2) applies even if third party to the transaction are residents.



Deemed International Transaction

■ CASE Study- 1 on Quadrangular Transactions

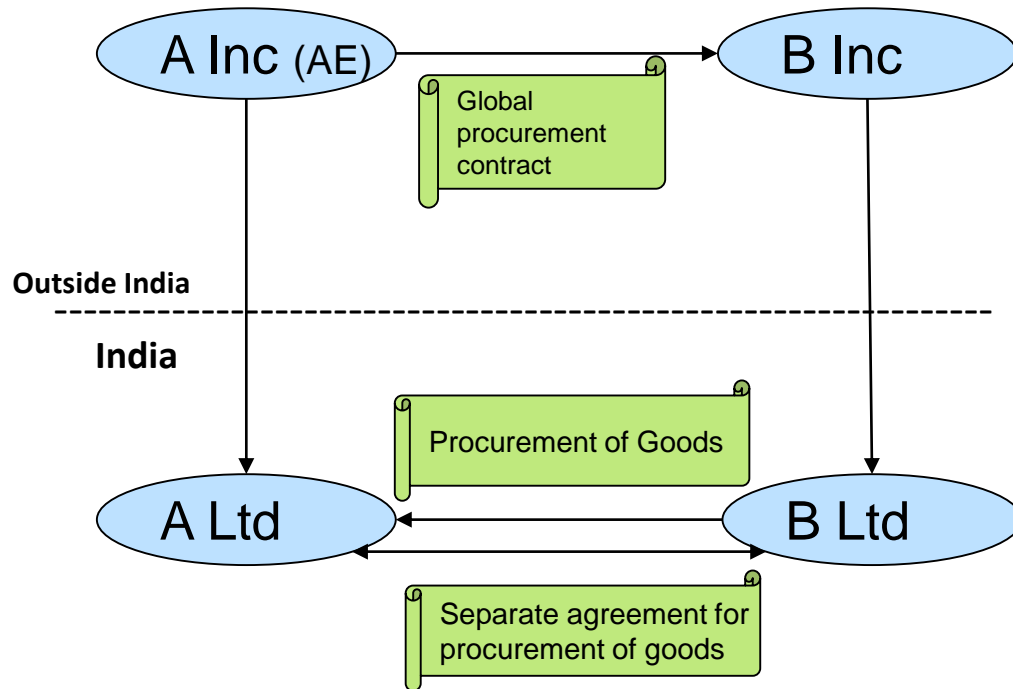


Facts of the Case:

1. Global procurement contract ("GPC") has been entered into by 'A Inc' with 'B Inc' to supply goods to its group entities.
2. As per GPC 'B Ltd' has supplied goods to 'A Ltd'
3. There is **no separate agreement** between 'A Ltd' and 'B Ltd' for the procurement of goods.

Deemed International Transaction

■ CASE Study- 2 on Quadrangular Transactions



Facts of the Case:

1. Global procurement contract ("GPC") has been entered into by 'A Inc' with 'B Inc' to supply goods to its group entities
2. 'A Ltd' has entered into another agreement with 'B Ltd' for procurement of goods by mentioning the clear terms of contract.
3. As per the above agreement 'B Ltd' has supplied goods to 'A Ltd'

Specified Domestic Transactions

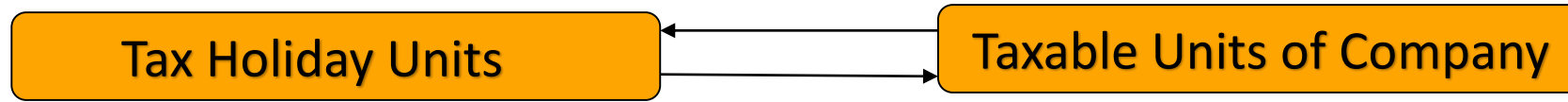
Specified Domestic transaction (Sec 92BA) ['SDT']

- Any of the specified transactions, not being any international transaction, namely
 - Expenditure in respect of which payment has been made or is to be made to person referred to in Section 40A(2)(b) ; - (omitted by Finance Act 2017)
 - Transaction referred to in Section 80A;
 - Transfer of goods or services referred to in sub-section(8) of Section 80-IA.
 - Any business transacted between the assessee and other persons as referred to in sub-section (10) of section 80-IA.
 - Any transaction, referred to in any other sections under Chapter VI-A or Section 10AA, to which provisions of sub-section (8) or sub-section (10) of section 80-IA are applicable.
 - Any other transaction as may be prescribed.

Note: Provisions of SDT would be applicable if the aggregate value of the transaction exceeds INR **20 Crore**

Specified Domestic Transactions

- In respect of tax holiday undertakings the following transactions are likely to be covered u/s 80IA(8):



- Transfer of goods
- Receipt or provision of services;
- Transfer of capital assets; and
- Further any other income and expense transactions that impact the tax holiday profits of the undertaking where the same qualify as transfer of goods and services.

Specified Domestic Transactions

- In respect of tax holiday undertakings any business transacted with entities having 'close connection' with the taxpayer will be covered u/s 80IA(10)

- **What is the meaning of 'Close connection'**

- The term 'close connection' has not been expressly defined in the Act.
- In this regard, reference could be drawn from other provisions of the Act to define 'close connection' as under
 - Substantial Interest u/s 40A(2)(b)
 - Associated Enterprise [Section 92A(2)]; and
 - Related party as per AS-18 or IndAS-24
- ***Digital Equipment India Ltd Vs DCIT (2006) 103 TTJ 329 (Bang)***

Inter-unit Transfers - Benchmarking

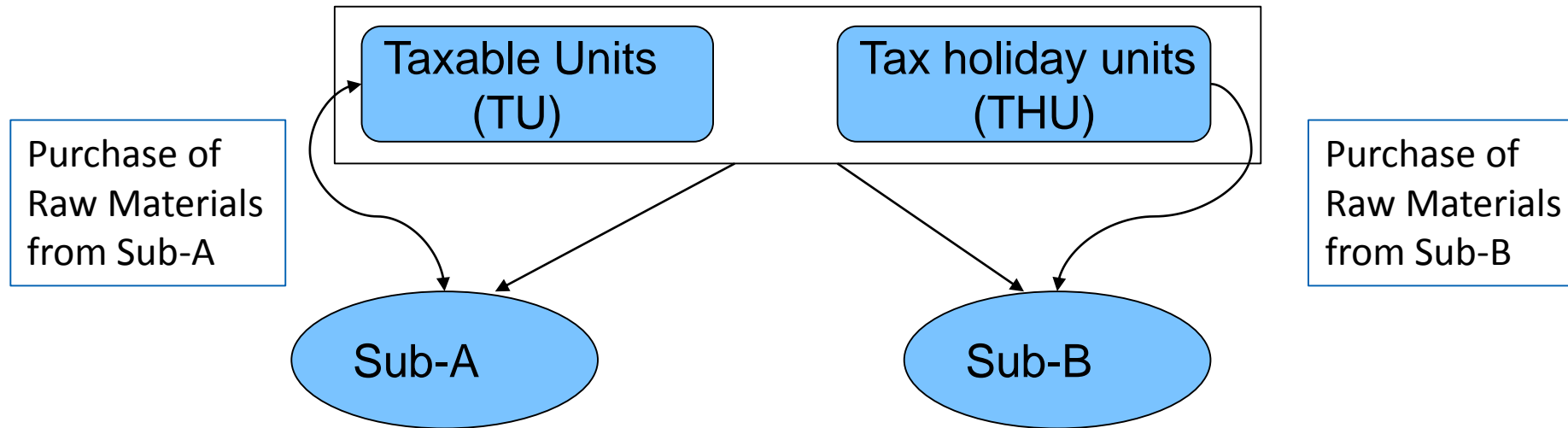
- How to benchmark inter-unit transfers between tax holiday unit and taxable units of the entity?
 - Can we consider CUP method as a Most Appropriate Method (“MAM”) when there are similar transactions with unrelated domestic parties.
 - Can we consider Cost Plus Method (“CPM”) as MAM instead of CUP method

Inter-unit Transfers - Benchmarking

- Other issues in reporting specified domestic transactions u/s 92BA
 - Is reporting of 'allocation of head office expenses mandatory? (*Ponds India (now Hindustan Lever Limited)*)- ITA 2047/Mad/88)
 - If yes, under which clause the same shall be reported.
 - What will be the basis for allocation and what type of expenses can be allocated to Tax Holiday unit
 - Whether transactions between domestic group entities and tax holiday units of the Assessee company shall be reported u/s 92BA
 - The same can be evaluated in the following case study.

Inter-unit Transfers - Benchmarking

- ABC Ltd incorporated in India conducts manufacturing activities in both of its taxable and tax holiday units. It purchases goods from its Indian Subsidiaries 'A Ltd' and 'B Ltd'
- whether these purchase transactions are required to be reported u/s 92BA



- If these transactions are required to be reported then under which method the above said transactions can be benchmarked.



THANK YOU