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# CURRENT ISSUES IN TRANSFER PRICING



#### 1. Outstanding Receivables

a. Whether outstanding receivables is an international transaction by itself?

Tally Solutions Pvt. Ltd. v. ACIT [2016] 73 taxmann.com 70 (Bangalore - Trib.)

Open Text Technologies India (P.) Ltd V. DCIT 105 taxmann.com 163 (Hyderabad - Trib.)

- As per Explanation to section 92B, inserted by Finance Act, 2012, interest on outstanding receivables is an international transaction
- b. Whether it would amount to capital financing?

Pegasystems Worldwide India Pvt. Ltd v. ACIT [2015] 64 taxmann.com 470 (Hyd - Trib.)

Hexagon Capability Center India (P.) Ltd. V. ACIT [2019]102 taxmann.com 461 (Hyd - Trib.)

 held that outstanding receivables on account of services could not be equated with capital financing.

c. If there is delay in realization, whether adjustment of imputed interest is justified?

GSS Infotech Ltd vs. ACIT [2016] 70 taxmann.com 356 (Hyderabad - Trib.)

 RBI itself allowed an year for amounts to be realised if they are in foreign exchange, so no interest could be levied from assessee for delay in realization of receipts from AEs

Dhanush Infotech (P) Ltd TS-1193-ITAT-2018(Hyd) TP

Bisazza India (P) Ltd TS-1095-ITAT-2018(Ahd) TP

 Where assessee applied TNMM as MAM which takes care about all cost including notional interest on receivables, TPO could not apply CUP to determine notional interest to be charged from associated enterprise on outstanding unrealized sale amount.

c. If there is delay in realization whether adjustment of imputed interest is justified?

Axis Risk Consulting Services (P.) Ltd. v. DCIT [2018] 92 taxmann.com 103 (Delhi - Trib.) CIT v. Indo American Jewellery Ltd., [2014] 44 taxmann.com 310 (Bombay - HC)

 In case where there is a delay in realization from unrelated customers also, it could be concluded that on basis of internal CUP, transaction with related party i.e. AE, met arm's length requirement vis-à-vis transactions with unrelated third parties.

#### 2. Corporate Guarantee

a. Is it not a shareholder activity?

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Micro Ink Ltd Vs. ACIT [2015] 63 taxmann.com 353 (Ahmedabad - Trib.)
ITO v. Cadila Health Care Ltd. [2017] 78 taxmann.com 330 (Ahd. - Trib.)
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b. Is it an international transaction at all?

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Bharti Airtel Ltd. v. Addl. CIT [2014] 43 taxmann.com 150/63 SOT 113 (Delhi - Trib.)

Marico Ltd. v. Asstt. CIT [2016] 70 taxmann.com 214 (Mum. - Trib.)

Redington (India) Ltd. v. Jt. CIT [2014] 49 taxmann.com 146 (Chennai - Trib.)

EIH Ltd [TS-1020-ITAT-2018 (Kolkata- Trib.)]

CCL Products (India) (P.) Ltd V. DCIT [2019]106 taxmann.com 11 (Visakhapatnam - Trib.)
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c. Corporate guarantee is different from bank guarantee.

GVK Power & Infrastructure Ltd. Vs. ACIT [2018] 94 taxmann.com 415 (Visakhapatnam - Trib.)

BS Ltd. Vs. ACIT [2018] 94 taxmann.com 346 (Hyderabad - Trib.)

Glenmark Pharmaceuticals Ltd Vs. ACIT [2014] 43 taxmann.com 191 (Mumbai - Trib.)

JE Energy Venture (P.) Ltd V. ACIT 108 taxmann.com 418 (Delhi - Trib.)

- d. Whether corporate guarantee is resulting in any benefit in the hands of AE in terms of lowering of interest rate.
  - Yield approach

Guidance issued by the HMRC in the UK: INTM502040 - Intra group funding

#### 3. Dispute in respect of comparables-

whether inclusion / exclusion of a company as comparable is a question of fact ?

PCIT Vs Softbrands India (P.) Ltd [2018] 94 taxmann.com 426 (Karnataka HC)

Saipem India Project Limited [TS-66-SC-2019-TP] (Supreme Court)

Citrix R&D India Pvt Ltd [TS-137-SC-2019-TP] (Supreme Court)

- Held that unless the finding of the Tribunal is found ex facie perverse, the Appeal u/s. 260-A of the Act, is not maintainable. There is no question of law, not to speak any substantial question of law, involved in the appeal and hence, HC has dismissed the revenue's appeal.
- Supreme Court has dismissed the SLP filed by Revenue.

#### 3. Dispute in respect of comparables-

whether inclusion / exclusion of a company as comparable is a question of law?

#### Pyramid IT Consulting (P.) Ltd. vs. ACIT Delhi HC [2019] 105 taxmann.com 281

Since the entire TP Adjustment has hinged only on one comparable, the objection to the inclusion of which by the Assessee required a detailed consideration. The Court remanded the entire issue of determining the TP adjustment if any in respect of the Assessee to the TPO for a fresh determination.

#### 4. Remanded matters to AO/TPO- Draft Order

a. If TPO proposes an adjustments in the remanded proceedings by ITAT, AO is under an obligation to pass a draft order again.

Cyient Ltd Vs. DCIT [2018] 89 taxmann.com 309 (Hyderabad - Trib.)

JCB India Ltd. Vs. DCIT [2017] 85 taxmann.com 155 (Delhi-HC)

b. Whether same principle is applicable, when AO is passing rectification Order under section 154?

Talent Anywhere Services Pvt Ltd (formerly known as QSG Resources Management India Pvt Ltd) [TS-549-ITAT-2019(Ahd)-TP]

 Held that once the DRP has given its directions, the order passed in pursuance of such directions, or rectification order in respect thereof, can only be appealed before the Tribunal. Whether the directions of the DRP have been correctly implemented or not cannot, at any stage, be challenged before the DRP.

#### 4. Remanded matters to AO/TPO- Draft Order

c. Whether adjustment made under MAP shall be added to total income despite the final assessment order is quashed for not passing draft-order?

Yazaki India Private Limited (Formerly known as Tata Yazaki AutoComp Limited) [TS-669-ITAT-2019(PUN)-TP]

Held that as per rule 44H(4) when a resolution has been made on an issue under the MAP proceedings, which assessee has accepted, the same attains finality and binds the assessee. Having accepted the MAP order, the assessee cannot agitate such an issue in the appellate proceedings.

5. Routing money through AE for acquisition of distribution rights from third-party, not a 'international-transaction'

# KSS Limited (formerly known as K Sera Sera Productions Ltd) [TS-1379-HC-2018(BOM)-TP]

Held that the transaction did not result into diversion of income of the assessee to its AE. Also, upholds ITAT's observation that in order to attract the provisions of Chapter X, there must be a transaction or arrangement between two or more AEs which gives rise to the income or benefit in the hands of at least one of them, observes that in the present case the advance was not given to the AE but to the third parties for the purpose of acquisition of rights of distributorship.

6. Whether TP Provisions are applicable to income covered under Tonnage Tax Scheme?

Van Oord India Private Limited [TS-440-ITAT-2019(Mum)-TP]

Mumbai ITAT ruled that TP-provisions [Chapter X] do not apply to income taxed under Tonnage Taxation Scheme (TTS) under Chapter XII-G of the IT Act. Held that TTS is a separate code by itself in as much as it provides a selfcontained charging provision as well as 'method of computation of income in the chapter.

- 7. Whether Foreign AEs can be taken as a tested party?

  IDS Infotech Ltd [TS-58-ITAT-2019(CHANDI)-TP]

  WNS Global Services Pvt. Ltd. [TS-278-ITAT-2019(Mum)-TP]
  - Held that foreign AE can be taken as tested party for the purpose of benchmarking the transactions.

#### Carraro India Private Limited [TS-124-ITAT-2019(PUN)-TP]

Held that the exercise of considering foreign AE renders the substantive Sec. 92 otiose and definition of 'international transaction' u/s 92B and Rule 10B redundant which is patently an unacceptable proposition having no sanction under the Indian transfer pricing law.

8. Whether TPO is under an obligation to apply Turnover Filter for exclusion of comparables?

#### **Speridian Technologies Private Limited (TS-962-ITAT-2019(COCH)-TP)**

 Held that if other filters are within the parameters and only on account of turn over, the comparables cannot be excluded.

# DCIT v. FIS Global Business India (P.) Ltd. [2018] 94 taxmann.com 344 (Delhi - Trib.)

- When average PLI of comparables, consisting of companies having similar or high or low turnover, is considered for benchmarking, effect of different volumes of turnover is automatically ironed out. Therefore, simply excluding the comparable because turnover of this company is more than Rs.100 crore is not a proper reason.

Cadence Design Systems (India) (P.) Ltd. v. DCIT [2018] 89 taxmann.com 443 (Delhi - Trib.)

8. Whether TPO is under an obligation to apply Turnover Filter for exclusion of comparables?

However, Turnover Filter has been upheld by-

CIT v. Pentair Water India (P.) Ltd. [2016] 69 taxmann.com 180 (Bombay)

Infor (India) (P.) Ltd. v. DCIT [2019] 109 taxmann.com 435 (Hyderabad - Trib.)

Northern Operating Services Vs. DCIT [2019] 108 taxmann.com 451 (Bangalore - Trib.)

9. Whether cash PLI (PBDIT) can be taken for the purpose of benchmarking the margin of the Assessee? i.e. Whether depreciation adjustment can be made for the purpose of calculating OP/OC?

Qual Core Logic Ltd. v. DCIT [2012] 22 taxmann.com 4 (Hyd-Trib)

M/s. International Specialty Products (India) Pvt. Ltd. v. ACIT I.T.(TP)A. No.1279/Mum/2017 -Trib

Snecma HAL Aerospace Pvt Ltd [TS-456-ITAT-2019(Bang)-TP]

- "Directs AO/TPO to accept cash profits as PLI and directs assessee to furnish the details to prove that there was substantial variation in the manner of charging depreciation".

9. Whether cash PLI (PBDIT) can be taken for the purpose of benchmarking the margin of the Assessee? i.e. Whether depreciation adjustment can be made for the purpose of calculating OP/OC?

#### INA Bearings India Pvt. Ltd [TS-540-ITAT-2019(PUN)-TP]

- ITAT held that the effect of all the individual higher or lower items of expenses or incomes is subsumed in the overall operating profit margin, ruling out the need for any adjustment on comparison of one-to-one items resulting into the determination of the operating profit margin. Held that depreciation adjustment is called for only when there is a difference on account of different rates of depreciation and not for different quantum of depreciation simplicitor.

10. Whether LIBOR + basis points can be taken as benchmarking rate when the compulsorily convertible Debenture s ('CCDs') are issued in Indian currency?

Hyderabad Infratech Pvt Ltd [TS-982-ITAT-2019(HYD)-TP]
PCIT v. India Debt Management (P.) Ltd. [2019] 106 taxmann.com 55 (Bom -HC)
CIT v. Tata Autocomp Systems Ltd. [2015] 56 taxmann.com 206 (Bom-HC)

- we agree with the assessee's contentions that the CCDs cannot be categorized as a loan and LIBOR plus two hundred basis points benchmark cannot be accepted on the facts of the case.
- ALP in the case of loans advanced to Associate Enterprises would be determined on the basis of rate of interest being charged in the country where the loan is received/consumed.

11. Investment in preference shares shall not be considered as loan unless the transaction is sham.

#### Aegis Limited [TS-65-HC-2019(BOM)-TP]

The facts on record would suggest that the assessee had entered into a transaction of purchase and sale of shares of an AE. Nothing is brought on record by the Revenue to suggest that the transaction was sham. In absence of any material on record, the TPO could not have treated such transaction as a loan and charged interest thereon on notional basis.

#### Cairn India Ltd [TS-1151-ITAT-2018(DEL)-TP]

Same view upheld by Hon'ble Delhi ITAT.

12. Benchmarking under CUP method - Quotations from internet are not reliable

#### JSL Limited (Now known as Jindal Stainless Ltd) [TS-1231-ITAT-2018(DEL)-TP]

Rejects Chinese market quotation downloaded from internet adopted by the assessee for applying CUP method as not substantiated by any authentic and reliable material, notes that a reliable quoted price would include prices obtained from recognized and transparent price reporting or governmental price setting agencies or an international or domestic commodity exchange market.

13. Whether Internal TNMM ('AE and NON-AE') can be applied even though the there is no segmental reporting in the financial statements?

#### Netguru Ltd [TS-383-ITAT-2019(Kol)-TP]

Held that assessee's ALP computation based on segment report duly verified and certified by the independent Statutory Auditor was in compliance of Rule 10B(1)(e) which provides for comparison of net profit margin realized by taxpayer from an international transaction with that realized by an unrelated enterprise from a comparable uncontrolled transaction.

Birlasoft (India) Ltd. v. DCIT [2014] 49 taxmann.com 312 (Delhi - Trib.)

Destination of the World (Subcontinent) (P.) Ltd. v. ACIT [2011] 12 taxmann.com 310 (Delhi),

Lummus Technology Heat Transfer BV v. DCIT [2014] 42 taxmann.com 342 (Delhi -Trib.)

14. Whether Persistent loss making companies can be included in comparables?

NOKIA SIEMENS NETWORK INDIA P LTD [TS-733-HC-2019(DEL)-TP]

Upheld the ITAT findings which say that there was a general trend in the industry of either loss-making or declining revenues. Further, Hon'ble High Court by noting the ITAT views which say that loss making companies should not be excluded only on that basis when they are functionally similar to that of the assessee, held that comparable company shall not be excluded.

#### Asahi Glass Ltd. v. DCIT [2016] 69 taxmann.com 32 (Delhi - Trib.)

 Where a company was not a consistent loss making company and losses were due to extraordinary circumstances which were only case specific, it could not be excluded from list of comparables.

- 1. Change in Cl.No.4 nature of business or activities of the Assessee (classification of business nature)
  - became narrow compared to earlier years.
  - difficulty in classifying under "Others" more so when we apply TNMM as Most Appropriate Method (MAM).

#### **Example:**

Company A Ltd is into <u>animation business</u>, however at the time of classification of business in Form 3CEB we will find it difficult as the same or similar nature of business is not available in the given list of nature of businesses.

- 2. Nature of relationship with the Associated enterprise as specified in Cl.No.10 is to be determined appropriately.
  - All the related parties as disclosed in RPT schedule of financials may not become Associated enterprises as specified in sec. 92(A) of the IT Act.
  - Possibility of litigation.

3. All the transactions during the year with the Associated enterprises may not be reported in some of the circumstances

#### **Example:**

- The transactions of loans given or taken during the year may not be reported, whereas interest charged or paid in relation to the loan given or taken shall be reported under Cl.No.14.
- The amount on which guarantee given or taken during the year may not be reported, however, commission charged on guarantee shall be reported under Cl.No.15.

- 4. With respect to reporting under Cl.No.19 only receivables shall be reported whereas payables may not be reported as per Explanation to sec.92B.
- 5. The aggregate value of international transactions as per books of accounts as specified in Cl.No.8 may not include the receivables amount as reported under Cl.No.19.
- 6. What is a deemed international transaction as per sec.92B(2)? How to do reporting under Cl.No.20

7. How to report Cl.No.10, details of associated enterprise when there is a deemed international transaction.

- 8. Shall we report the transactions with persons specified u/s 40A(2)(b) under Cl.No.21?
  - due to amendment in Finance Act,2017, transactions with parties covered under sec.40A(2)(b) will not be considered as a specified domestic transactions as per Sec.92BA
  - however in form 3CEB in Cl.No.21 one may select "Not Applicable" in the drop down provided.

- 9. How to report transaction with other enterprise which has close connection with the assessee as defined in section 80 IA (10)?
- 10. When foreign AE is filing return of income in India as per the Income Tax Act, is it mandatory to file Form 3CEB by such foreign AE?

# Sec.92BA-Specified Domestic Transaction (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 refereed 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** 

# Sec.92BA-Specified Domestic Transaction (SDT)

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

# Tax Holiday Units Taxable Units of Company

- 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.

# Sec.92BA-Specified Domestic Transaction (SDT)

- 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

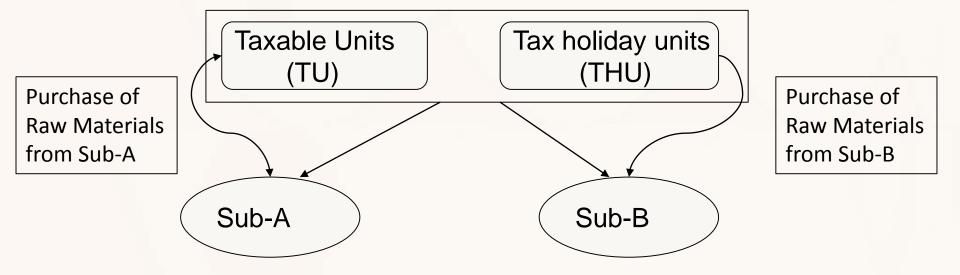
- How to benchmark inter-unit transfers between tax holiday unit and taxable units of the entity?
  - Can we consider CUP method as a Most Appropriate Method ("MAM") when there are similar transactions with unrelated domestic parties.
  - Can we consider Cost Plus Method ("CPM") as MAM instead of CUP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

- A new section 92CE has been inserted in Income Tax Act through the Finance Act, 2017.
- Secondary adjustment means an adjustment in the books of account of the assessee and its associated enterprise to reflect that the actual allocation of profits between the assessee and its associated enterprise are consistent with the transfer price determined as a result of primary adjustment, thereby removing the imbalance between cash account and actual profit of the assessee.

- However, Secondary adjustment is not applicable if,—
  - (i) the amount of primary adjustment made in any previous year does not exceed one crore rupees; **OR**
  - (ii) the primary adjustment is made in respect of an assessment year commencing on or before the 1st day of April, 2016:

- If the excess money is not repatriated to India within a period of 90 days, the excess money available with the AE shall be treated as loan given by the assessee to such AE and interest shall be calculated at the rate prescribed in rule 10CB of Income Tax rules. (Rule 10CB has been amended by Notification No.76/2019)
- the excess money or part thereof may be repatriated from any of the associated enterprises of the assessee which is not a resident in India. (New Proviso-Inserted by Finance Act 2019 –No.2)
- where the excess money or part thereof has not been repatriated within the prescribed time, the assessee may, at his option, pay additional income-tax at the rate of 18% on such excess money. (Sub. Sec 2A -Inserted by Finance Act 2019 No.2)

- The tax on the excess money or part thereof so paid by the assessee under subsection (2A) shall be treated as the final payment of tax in respect of the excess money or part thereof not repatriated and no further credit therefor shall be claimed by the assessee or by any other person in respect of the amount of tax so paid. (Sub. Sec 2B -Inserted by Finance Act 2019 No.2)
- No deduction under any other provision of this Act shall be allowed to the assessee in respect of the amount on which tax has been paid in accordance with the provisions of sub-section (2A). (Sub. Sec 2C -Inserted by Finance Act 2019 No.2)
- Where the additional income-tax referred to in sub-section (2A) is paid by the assessee, he shall not be required to make secondary adjustment under sub-section (1) and compute interest under sub-section (2) from the date of payment of such tax.] (Sub. Sec 2D -Inserted by Finance Act 2019 No.2)

# "THANK YOU"