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Increase in globalization and rise in multinational companies coming to India prompted the Indian Government to introduce transfer pricing regulations in the year 2001. The framework has since then undergone some modifications with some major amendments taking place in year 2012.

This write-up aims to provide the key features of the current position of regulatory framework in India and highlight some contemporary controversies arising there-under.
A. REGULATORY FRAMEWORK

Legal authority

Indian Transfer Pricing Regulations (TPR) adopt arm’s length principle as a basis for determining whether, India has received its fair share of tax. The provisions are embodied in Chapter X (Section 92 to 92F) of Income tax Act, 1961 and Rule 10A to 10E of the Income tax Rules, 1962.

Applicability

Transactions

TPR requires that income or expense arising from an international transaction shall be determined having regard to arm’s length price (‘ALP’). An international transaction is one which is entered into between two or more Associated Enterprises (‘AEs’) one of whom being non-resident of India. The kind of transactions that can fall under the scope of ‘international transaction’ originally included cost contribution arrangements, purchase, sale or lease of tangible or intangible property, provision of services, lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of the AEs. Owing to tax disputes surrounding intangibles, financial transactions and business restructuring the scope has recently\(^1\) been clarified to include transactions pertaining to intangibles (including customer list, marketing channel, brand, commercial secret etc.), capital financing (including standing guarantee for a debt, deferral of receivables etc.), provision of intra-group services (including market research and development, administration, legal or accounting service) and business restructuring.

Associated Enterprises

An enterprise is said to be an AE of another if it participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise or if both enterprises are so managed / controlled by same

\(^1\) Vide Finance Act, 2012
The provisions further lists out 13 prima facie cases where AE relation is deemed to exist. To illustrate, these instances include (a) where 10% or more of the borrowing of an enterprise is guaranteed by the other enterprise, (b) the business of one is wholly dependent on know-how, license etc. of another, (c) where 90% of the raw material and consumables required for manufacturing or processing are supplied by another and the price and terms of such supply are influenced by the latter.

## Methods for determining ALP

TPR requires that the ALP should be determined by any of the specified methods being the most appropriate method. The taxpayer has to select the most appropriate method to be applied to any given transaction and such selection has to be made taking into account the factors prescribed in the TPR. The prescribed methods have been listed below:

- a. Comparable Uncontrolled Price Method (‘CUPM’)
- b. Resale Price Method (‘RPM’)
- c. Cost plus method (‘CPM’)
- d. Profit Split Method (‘PSM’)
- e. Transactional Net Margin Method (‘TNMM’)
- f. Any other method (‘OM’)

TPR requires that the method selected for a particular case should be most appropriate to that case having regard to various factors including nature of transaction; nature of enterprises in the light of Functions Asset and Risk (FAR) analysis; availability and reliability of data; degree of comparability and extent to which reliable and accurate adjustments can be made for the differences.

The first five methods listed above are internationally well known and Indian TPR does not have any material departure from OECD approach in the manner of application of these methods. With a view to enable benchmarking of infrequent and intricate
transactions like dealings in shares, intangibles and cases where getting comparable financial data is a challenge, TPR introduced in year 2012 the sixth method which is referred above as ‘any other method’ (‘OM’). The rule provides that the other method for determination of the arms’ length price in relation to an international transaction shall be any method which takes into account the price which has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between Non-AEs, under similar circumstances, considering all the relevant facts. As is evident the rule permits great flexibility of considering the price that would have been charged. This method therefore makes it possible to place reliance on valuation certificates, standard rate cards, tender documents or price quotations to demonstrate arm’s length intent. However like other methods, before applying this method, one needs to demonstrate that this is most appropriate to the facts of its case.

Documentation

The provisions contained in the TPR exhaustively spell out the documentation to be maintained by a taxpayer. This includes background information on the commercial environment in which the transaction has been entered into, information regarding the international transaction, the analysis carried out to select the most appropriate method and to identify comparable transactions, and the actual working out of the ALP of the transaction. However, in cases where the value of the international transaction is below INR 10 million, the strict rules of documentation do not apply and it would be sufficient for the taxpayer to maintain such documentation and information which substantiates his claim for the ALP adopted by him. A penalty of 2% of the value of international transaction is leviable if the prescribed documentation is not maintained. The taxpayer also needs to obtain and file with tax authorities a report of an accountant certifying that the ALP has been determined in accordance with the TPR and that prescribed documentation has been maintained failing which a penalty of INR 100,000 is leviable.
Adjustments by tax authorities to the ALP as declared

The tax authorities are empowered to make adjustment to the income declared by taxpayer by modifying the ALP where the Transfer Pricing officer (‘TPO’) is of the view that the:

- a. price charged in the international transaction has not been determined in accordance with the methods prescribed, or
- b. information and documents relating to the international transaction have not been kept and maintained by the assessee in accordance with the TPR, or
- c. the information or data used in computation of the ALP is not reliable or correct, or
- d. the assessee has failed to furnish any information or document which he was required to furnish under the TPR.

Effect of adjustments by tax authorities

Besides addition to the income base, if the tax authorities find that the facts of the transaction were concealed or incorrectly stated resulting in reduction of tax base, there could be levy of penalty which can range from 100% to 300% of the difference between declared tax liability and the tax liability ascertained by tax authorities. Further since there would be deferment of tax, interest @1% per month from the end of tax year till the date of tax assessment by tax officer, would be leviable.
B. CONTEMPORARY DISPUTES RELATING TO TRANSFER PRICING

Transfer pricing in India is still in development stage and tax department is gearing up to ensure that there is no understatement of income by multinational enterprises. The disputes relating to Transfer Pricing adjustments are on rise and involve huge stakes. We have captured below some of the contemporary issues that are arising in this arena.

Capital investment as an international transaction

TP provisions are intended to apply to transactions that give rise to income or expenditure. Revenue Authorities in the recent past have extended their applicability to investments made in subsidiaries as ‘international transaction’ subject to transfer pricing. The Bombay High Court in a writ petition in the case of *Vodafone India Services*\(^2\), remanded the order of the TPO to examine if the subscription of shares resulted in any income so as to apply TP provisions to the transaction. Recently, the Hyderabad ITAT\(^3\) in the case of *Vijai Electricals Ltd*\(^4\) has also opined that subscription to shares of a subsidiary would not be subjected to Transfer Pricing regulations. Authority of Advance Ruling (‘AAR’) had also observed in *Dana Corporation*\(^5\) that in the absence of taxable income, Transfer Pricing provisions cannot be made applicable. Similar observation has been made by the AAR in *Goodyear Tire & Rubber Co*\(^6\) and *Amiantit International Holding Ltd*\(^7\). A writ petition before the Hon’ble Delhi High Court against the ruling in *Goodyear Tire* was dismissed in [2014] 360 ITR 159 (Del) as no illegality was noticed in the order of the Authority. While these rulings support the proposition that

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\(^2\) *Vodafone India Services (P.) Ltd. v UOI* - Writ Petition No 1877 of 2013, decided on 29 November 2013

\(^3\) Income Tax Appellate Tribunal (ITAT). ITAT is second level appellate authority

\(^4\) *Vijai Electricals Ltd v ACIT* - ITA 842/ Hyd/ 2012, decision dated 31.05.2013

\(^5\) [2010] 321 ITR 178 (AAR)

\(^6\) [2011] 334 ITR 69 (AAR)

\(^7\) [2010] 189 Taxman 149 (AAR)
TP regulations are not applicable on investment transactions, a robust valuation report justifying the issue price can be more effective a tool to steer clear of the controversy.

Risk adjustment for captive service providers

The comparability requirements under Indian TP regulations are similar to OECD TP Guidelines. The regulations also provide for making appropriate adjustment, for difference in transaction, enterprise, risks, working capital etc. In many cases, close comparables are not available and taxpayers seek adjustment on account of differences.

In the case of a captive service provider rendering services to its parent company alone, the Tribunal in *Intellinet Technologies*

8 held that the ‘single customer risk’ as alleged by Revenue Authority is only an ‘anticipated risk’ vis-à-vis the ‘existing’ market risk borne by independent comparables. Where a Tax Payer was receiving its remuneration in advance as against comparable companies that received their remuneration after considerable period of rendering services, the Tribunal in *Avineon Indic*

9 upheld ‘working capital’ adjustment.

In a more recent case, there were observed to be significant functional and market differences between the Tax Payer and the comparables appreciating which the Tribunal

10 ruled that risk adjustment can be computed using Capital Asset Pricing Model (CAPM), taking assistance from experts in the field of management.

Intangibles

Multinational enterprises retain trademark or brand name (hereinafter referred to as “marketing intangibles”) in one entity and allow the other group companies to use the same with or without royalty. Such group companies use these

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8 *Intellinet Technologies India (P) Ltd. v. ITO* - [2012] 53 SOT 92 (Bang.)
9 *Avineon India (P) Ltd v DCIT* - ITA No. 1606/Hyd/2010, decision dated 30 May 2014
10 *Motorola Solutions India Pvt Ltd v ACIT* - ITA No. 5637/Del/2011, decision dated 14 August 2014
marketing intangible and incur publicity expenses for marketing its products in the respective country of their operation. Issue often arises as to whether the legal owner of the intangible needs to compensate group companies using it, as per arm’s length principle, for the promotional efforts put in by such group company. Revenue authorities argue that promotional expenses enhance the value of marketing intangibles legally owned by other entity that requires application of ALP principle.

This issue was recently\(^\text{11}\) considered by a larger bench of ITAT wherein it has laid down some principles while remanding the matter back to first level tax officer to re-determine the ALP. In initial proceedings the Transfer Pricing Officer (‘TPO’) had disallowed the expenses on advertisement, marketing and promotion (‘AMP expenses’) incurred in promoting the marketing intangibles of the AE which were found to be in excess of the average AMP expenses incurred by the comparable companies. According to the tax authorities, such “excess” AMP expenditures ought to have been compensated by the AE with an arm’s length mark-up applying TNMM.

The ITAT held that there is an international transaction between the taxpayer and the AE under which the taxpayer incurred AMP expenses toward promotion of marketing intangibles legally-owned by the AE, despite the fact that there is no contractual arrangement to that effect.

The ITAT has identified following factors that need to be considered while determining the ALP for the international transaction of promotion of marketing intangibles through AMP expenses:

› Whether the Indian AE is paying any royalty to the foreign AE;
› Whether the royalty is comparable with what comparable uncontrolled enterprises would pay;

\(^{11}\text{LG Electronics India P. Ltd. vs ACIT - 29 Taxmann.com 300 (ITAT Delhi)}\)
Whether in the year under consideration the foreign AE is entering the India market or is an established brand in India;

Whether any new products are launched in India during the relevant period or the business is continuing with the existing range of products;

Whether the Indian AE is a distributor or manufacturer;

The extent of value addition made by the Indian AE;

Whether the goods sold by the Indian AE bear the same brand name as the foreign AE;

Whether the goods sold bear logo only of foreign AE or a logo which is only of the Indian AE or is it a joint logo of both the Indian entity and its foreign counterpart;

How will the brand be dealt with after termination of the agreement between AEs?

The ruling has given some directional guidelines on this burning issue however the manner in which tax authorities would apply these factors will be unfolded by the time to come. Further an important aspect that still needs deliberation is that first thing to be ascertained in such cases (even if the AMP expenses are in excess of that incurred by comparables) should be whether the real benefit of the excess AMP expenses is to the foreign AE or the taxpayer itself and whether the alleged benefit to foreign AE, if at all, is only incidental.

It has however been held in *Glaxo Smithkline*[^12], *Canon India*[^13] and other rulings that expenses on Commission, Cash Discount, Volume Rebate, Trade Discount etc. shall not be regarded as expenses incurred for improving the brand visibility of the MNE group. Further, where the Indian distributor was a limited-risk distributor, higher distributor margins earned would compensate for the marketing activities carried on by it, as held by the Tribunal in *BMW India*[^14].

[^12]: *Glaxo Smithkline Consumer Healthcare Ltd v DCIT* - 2013-TII-71-ITAT-CHD-TP
[^13]: *Canon India Ltd v. DCIT* - 2013-TII-96-ITAT-DEL-TP
[^14]: *BMW India Pvt. Ltd. v ACIT* - ITA No. 5354/Del/2012, decision dated 18 August 2013
Notional interest on unpaid receivables

The receivables in the books of an Indian enterprise on account of sales made to an AE have also been under debate recently. Tax authorities tend to argue that if a receivable is not realized in reasonable time then interest should have been earned by Indian entity thereon. In the case of Indo American Jewellery\textsuperscript{15} the TPO observed that the taxpayer had huge amount of outstanding receivables due from its AE and held that the taxpayer should have charged interest thereon. The TPO accordingly made an adjustment to the income of the taxpayer by applying 10% interest rate on the receivables due from AE. The issue, whether deferral of receivable is an international transaction necessitating its conformity to ALP principle has been statutorily settled in the favor of tax department vide Finance Act 2012. However irrespective of that the Bombay High Court in this particular case observed that the taxpayer had unrealized export receivables from unrelated entities as well on which taxpayer had not charged any interest. Based on this it held that there was no undue benefit conferred on the AE by the Indian enterprise. Accordingly the High Court accepted the plea of the taxpayer and deleted the addition to its income made by TPO.

R&D centers

Many enterprises have set up contract R&D centers in India. These entities are typically set up as captive service providers or risk mitigated entities, contractually insulated from all risks and entitled to a fixed return. The tax authorities believe that the Indian R&D center performs sophisticated and value-added activities which not only require significant investment in the physical infrastructure but also require the Indian entity to attract, train and retain highly skilled personnel. They believe that but for this function in India the profitability of foreign AE would not be as good as it is actually. In one such case\textsuperscript{16} the taxpayer was engaged in providing R&D and engineering services to its AEs and had selected comparables in the field of

\textsuperscript{15} CIT v. Indo American Jewellery - ITA 1053 of 2012, Bombay High Court
\textsuperscript{16} GE India Technology Centre Private Limited - ITA No. 789/Bang/2010 & IT Nos. 487 & 925/Bang/2011
software development for its transfer pricing documentation. The TPO observed that the taxpayer was carrying out the R&D and engineering analysis with the aid of sophisticated labs/software in various field of engineering. Therefore it held that the taxpayer was an ITeS\textsuperscript{17} Company and comparable to those providing technical consultancy, engineering services and R&D. ITAT upheld the view of the TPO on this aspect. Further the taxpayer had projected itself as a risk mitigated entity while the ITAT held that since tax payer is performing core functions that require important strategic decisions by management, it is running operational and other risks. It added that any contrary position has to be satisfactorily demonstrated by the taxpayer. Later this view was supported by circulars issued by Tax Administration. However recently the position has been reviewed by Tax Administration and recent circular\textsuperscript{18} on the subject, superseding earlier circulars, accepts that risk of R&D centre in India can be controlled remotely if certain specified parameters are met.

Guaranteeing a foreign subsidiary

A newly established foreign subsidiary will usually depend on its Indian parent for financial support. One of the means for extending such support is guaranteeing the borrowings of subsidiary. Indian Revenue Authorities claim that the guarantee extended by the Indian holding company to the foreign subsidiary would be regarded as an ‘international transaction’ and impute a fee in the hands of the Indian parent company. The IT Act was also amended by Finance Act 2012 so as to retrospectively include “capital financing, including any type of long-term or short-term guarantee” as an international transaction subjected to TP. Tribunal in the case of \textit{Bharati Airtel Ltd}\textsuperscript{19} held that unless the guarantee has a direct bearing on the profits, incomes, losses, or assets of the holding company, it cannot be regarded as an international transaction, in spite of the retrospective amendment. The position after the amendment however remains controversial.

\textsuperscript{17} Information Technology Enabled Services Company
\textsuperscript{18} Circular No. 6 dated 29.06.2013
\textsuperscript{19} \textit{Bharati Airtel Limited v ACIT} - TS-76-ITAT-2014(DEL)-TP
Selection of comparables

High turnover companies, aberrant profitability, multiple year data, etc.

Comparability analysis is yet another heavily debated issue in TP proceedings. In the undernoted case\(^{20}\) taxpayer was a captive service provider engaged by its AEs to provide financial advisory services, management consultancy services, undertake feasibility studies and diagnose operational difficulties of existing units/ advice on disinvestment. The taxpayer in its TP study had excluded certain companies as not being comparable on account of (a) such companies having marketing expenses (b) having huge fluctuations in margin (c) having high turnover and (d) having related party transactions (RPT) more than 15% of total turnover. Besides this the taxpayer had used multiple year data. The Transfer Pricing Officer disputed these criteria. The Income Tax Appellate Tribunal held that marketing expenses by service companies usually do not create marketing intangible and do not have bearing on profitability. It held that companies having RPT up to 25% can be accepted as comparable. As regards turnover filter it accepted taxpayer contention that companies having size/turnover relative to that of the taxpayer only should be taken as comparables. It also commented on use of multiple year data and held that the same should be used in exceptional cases and only where earlier year’s data is shown to have influence on the year under consideration.

Post Budget 2014, the law has been amended to provide for use of multiple year data and quartile range as against arithmetic mean used hitherto however the detailed guidelines are yet to be issued.

\(^{20}\) *Actis Advisors Private Ltd.* - ITA No. 5277/Del/2011
Start-up companies

Entering into a new market generally entails heavy set up costs due to which the margins of initial years of business are low. Tax authorities tend to disregard this fact and arrive at ALP by comparing starter companies with established players in the market. In the undernoted case the taxpayer was engaged in the business of providing Information Technology Enabled Services to its parent company and it was the first year of operations of the taxpayer. It had certain start-up costs and was yet to achieve full utilization of its capacity. In its TP study the taxpayer had claimed adjustment for under-utilization and start-up costs. During the tax assessment the Transfer Pricing Officer made adjustment to the ALP by rejecting a comparable company and also denied the adjustments sought by the taxpayer. In appeal ITAT held that necessary adjustment on the grounds of start-up costs and under-utilization of capacity are important for applying transfer pricing regulations in reasonable and fair manner.

21 Amdocs Business Services Pvt. Ltd. v. DCIT - ITA No. 1412/PN/2011
Transfer pricing (‘TP’) regulations were introduced in India in 2001 and in less than 15 years, the country finds place in top five nations on pending TP disputes. As noted in the preceding topic of ‘Transfer Pricing Regulation and Challenges in India’ the growing complexity and adjustments to income has created concern and uncertainty amongst Multinational Enterprises (‘MNEs’), about the tax impact on cross border transactions. In order to address this concern and uncertainty, Finance Act, 2012 laid down foundation for the legal framework of Advance Pricing Agreements (‘APA’) with effect from July 2012 and in August 2012, detailed Rules for executing APAs were introduced by way of Notification No. 36/2012 dated 30-8-2012. The scheme has attracted keen interest from many MNEs, with close to 250 applications having been filed since the introduction of the scheme. Five (5) agreements have already been signed and many applications are in advance stage of finalisation.

The Indian APA regime largely follows the pattern/procedure found in developed economies with some distinguishing features. The objective of this write-up is to provide an overview of the framework of APA in India and the shortcomings that need to be borne in mind while making a decision in this regard.
OECD Guidelines on Transfer Pricing for MNEs explain APA thus: “An Advance Pricing Arrangement is an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria [e.g. (a) method, (b) comparables and appropriate adjustments thereto, (c) critical assumptions as to future events)] for the determination of the transfer pricing for those transactions over a fixed period of time. While the OECD approach provides for a wide scope for which an APA can be resorted to, the Indian APA regime provides for (a) determination of Arm’s Length Price (ALP) or (b) the manner in which the ALP has to be determined, including critical assumptions. The scheme however provides that some variations to the statutory methods prescribed for determining ALP\(^1\) can also be agreed at. This is an important step towards recognition of the fact that in some unique transactions it is difficult to determine ALP within the rigid framework of statutory methods.

**SCOPE**

The APA scheme provides for unilateral, bilateral and multilateral APAs. The scheme applies to international transactions (a) which have been undertaken (ie transactions of a continuing nature from dealings that are already occurring) and (b) to international transactions which are proposed to be undertaken.

**PERIOD OF VALIDITY**

Initially, an APA was supposed to be valid for a maximum period of five (5) years from the year in which the agreement is entered into. By an amendment in 2014, an APA is now allowed to be rolled back for a period of four (4) years preceding the year of its first applicability. Roll back provisions introduced by the recent amendment is a welcome move to bring higher degree of certainty in the otherwise litigation prone environment.

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\(^1\) Indian TP regulations specify OECD authorized methods and also a sixth residuary method which is in conformity with the concept of arm’s length
CRITICAL ASSUMPTIONS

To secure the objective of APA, the scheme provides for identification of critical assumptions. As per OECD guidelines the assumptions on which the ability of the methodology to accurately reflect the arm’s length pricing of future transactions are important. Such assumptions are ‘critical’ when the actual conditions existing at the time the transactions occur could diverge from those that were assumed to exist, to the extent that the ability of the methodology reliably to reflect arm’s length pricing is undermined. Indian APA scheme does not provide any detailed guidance on this aspect hence drawing broad assumptions should be considered so that the same do not warrant re-negotiation very often.

STEPS

The process of entering into an APA involves following steps:

1. **Step 1 - Pre-filing consultation**

   The APA scheme requires that a taxpayer desirous of entering into an APA shall undertake a pre-filing consultation. The Applicant needs to file an application with the Director General of Income Tax (International Taxation) (‘DGIT’) in a prescribed form providing the prescribed particulars. In case the Applicant is seeking a bilateral or multilateral APA, the competent authority in India\(^2\) or its representative would also be involved in the pre-filing consultation. At this stage it is permissible to maintain anonymity.

   The objective of the pre-filing consultation is to determine the scope of the agreement, identify transfer pricing issues, determine the suitability of APA for the international transaction and to discuss broad terms of the agreement. Undertaking pre-filing stage does not oblige either tax authority or the taxpayer to enter into or proceed with entering into an APA.

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\(^2\) An officer authorised by the Central Government for the purpose of discharging the functions as such for matters in respect of any agreement entered into under Section 90 or 90A of the Income Tax Act relating to Double Taxation
Step 2 - Filing an application for APA

After the pre-filing consultation, if the taxpayer desires to proceed further it can file an application for an APA in the prescribed form and with all relevant documents. The application needs to be filed with the DGIT (in case of a unilateral APA) or with the Indian competent authority (in case of a bilateral/multilateral APA). One of the information to be shared with tax authorities at this stage is discussion on un-assessed tax years (Indian and foreign) and related outstanding tax, legal, and other pertinent issues. This information is apparently not relevant for determining ALP/method for the proposed transaction, hence the manner in which it may be used by tax authorities is unclear.

The application should be accompanied by prescribed fee which is based on the amount of international transaction proposed to be or entered into. For transactions up to INR 100 crores (one billion), a fee of INR 10 lakhs (one million) has been prescribed. A fee of INR 15 lakhs is payable where amount does not exceed INR 200 crores. For international transactions exceeding Rs. 200 crores, the fee payable would be INR 20 lakhs.

Step 3 - Preliminary processing of the APA application

After filing the application, the same is screened for ensuring basic compliance. If a defect is noticed in the application (including if a relevant document is not attached) or if the application is not in line with the understanding reached in pre-filing consultation then either the DGIT or the competent authority in India can serve a deficiency letter on the applicant asking it to rectify the defect or to modify the application. The deficiency letter, if any, is to be served on the applicant within one month from the date of filing of the application. The applicant can rectify the defect/modify the application within 15 days of the date of service of deficiency letter or such extended time as may be requested subject to a maximum of 30 days from the date of service of the deficiency letter.
If the DGIT or the competent authority in India are not satisfied that the deficiency has been removed by the Applicant, they can pass an order providing that the application for an APA shall not be allowed to be proceeded with. However, the applicant would be given an opportunity to be heard before such an order is passed.

### Step 4 - Processing of the APA application

Tax authorities / Competent Authority can hold meetings, call for additional documents of information or even visit the premises of the Applicant. Visits are planned with consultation of the taxpayer and are meant for gathering facts to understand the business model and not investigative in nature. Additional information can also be provided suo moto by the Applicant in connection with the application.

In case of a bilateral or multilateral APA, the authorities will, after making due enquiry, forward a draft report to the DGIT, who will in turn send it to the competent authority in India.

In case of a bilateral or multilateral APA process, the competent authority in India would enter into discussions/negotiations with the competent authority of the relevant foreign country of which the Associate Enterprise ('AE') of the applicant is a resident. The APA scheme requires that the foreign AE of the applicant initiate an APA with the competent authority of the country in which the foreign AE is a resident. Based on these discussions/negotiations, the two competent authorities would formalise a Mutual Agreement Procedure ('MAP') arrangement which would be intimated to the applicant by the competent authority in India.

In case the competent authority in India and the foreign competent authority are unable to reach an agreement, the competent authority in India would intimate the applicant of this development. At this stage, the applicant will have the option of either proceeding with the APA without the benefit of the MAP process (i.e. convert it into a unilateral APA) or withdraw the application.
Step 5 - Drafting of an APA and execution post approval

The DGIT or the Indian Competent Authority and the Applicant would then prepare a proposed mutually agreed draft of the agreement. This agreement will be entered into between the Central Board of Direct Taxes and the applicant after it receives the approval from the central government.

Post APA compliance

a) Revision of tax returns and tax assessment
APA scheme in India is not a time bound process hence it is likely that by the time an APA is entered into, one or more tax years are already over and stand scrutinised by the tax department. For that eventuality the scheme provides that the taxpayer shall file a revised return of its income for such intervening years within three months from the end of the month in which the APA is entered into. The tax assessment of such revised return is to be carried out within one year from the end of the financial year in which such revised return is furnished.

b) Filing of compliance report
The taxpayer is required to furnish an annual compliance report to DGIT for each year covered in the agreement, within thirty days of the due date of filing the revised income-tax return for that year, or within ninety days of entering into an agreement, whichever is later. Failure to file this report or filing a report containing material errors can result in cancellation of APA. The taxpayer will however given an opportunity of being heard before such cancellation.

c) Audit of the compliance report
The revised return filed after execution of the APA does not undergo a regular transfer pricing audit (for transactions covered by an APA). For covered transactions, the Transfer Pricing Officer (‘TPO’) would audit the compliance report to form an opinion on the taxpayers compliance with the terms agreed in the APA which needs to be completed within 6 months from the end of the month in which the compliance report is received by the TPO from DGIT.
Other features

\(a\) Confidentiality
The scheme does not provide for any restriction against parting with data and the possible use of the data against taxpayer.

\(b\) Withdrawal
The applicant may withdraw the application for APA at any time before the finalisation of the terms of the same however the fee paid along-with the application is not refundable.

\(c\) APA with non Treaty countries
A unilateral APA can be entered into even if the AE of the applicant is tax resident of a country with which India does not have a Tax Treaty. An official circular released by tax administration suggests that a bilateral or multi-lateral APA with a country with which India does not have a Tax Treaty or has a Tax Treaty without a clause similar to Article 9(2) of the OECD Model convention is not covered in the current APA scheme.

\(d\) APA for determining profit attribution
A foreign enterprise operating in India through a Permanent Establishment (’PE’) can also seek APA on quantification of profit attributable to the PE. Many foreign enterprises seek advance ruling from Indian Authority for Advance Ruling about whether their operations or business dealings in India create a PE. In such cases they may parallelly seek APA which may apply of the existence of the PE is ultimately upheld.
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