The Institute of Chartered Accountants' of India's

Western India Region Council's Mulund CPE Study Circle

Basics and Issues in Transfer Pricing Audit
24 October 2020
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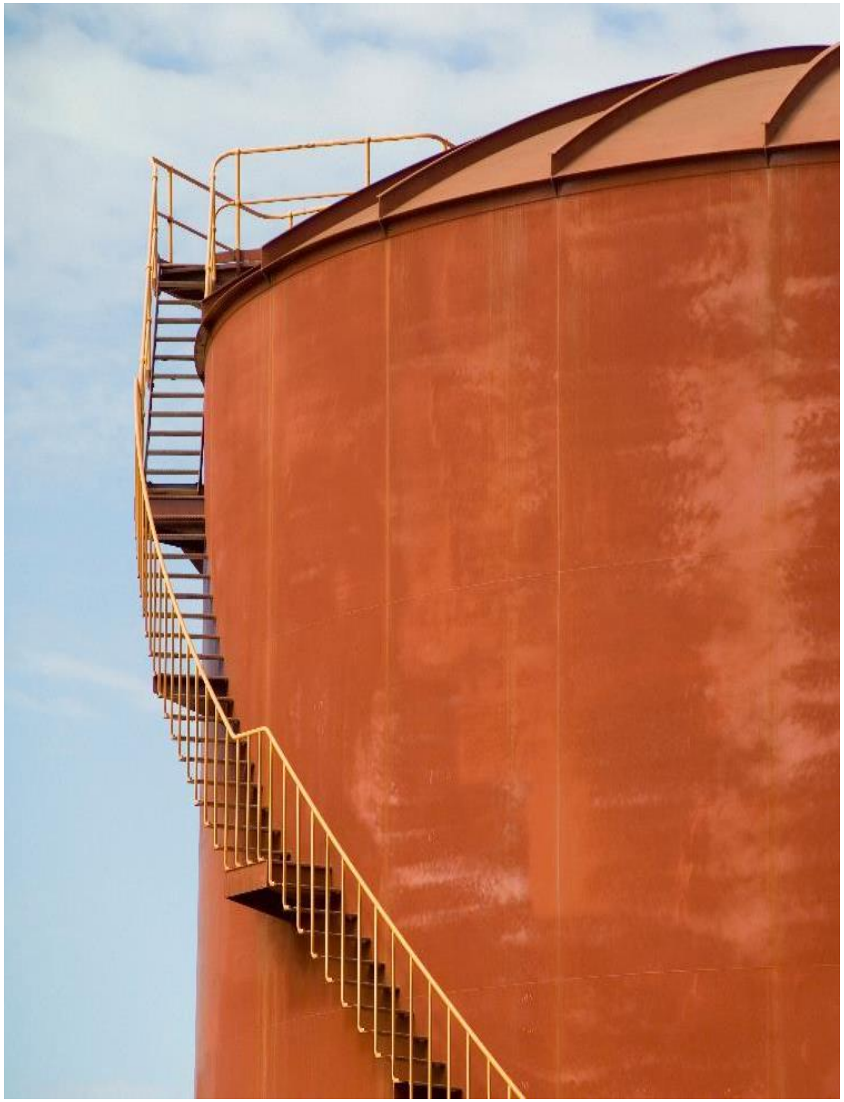
Contents



What is transfer pricing (TP) & history

Exercise – 1

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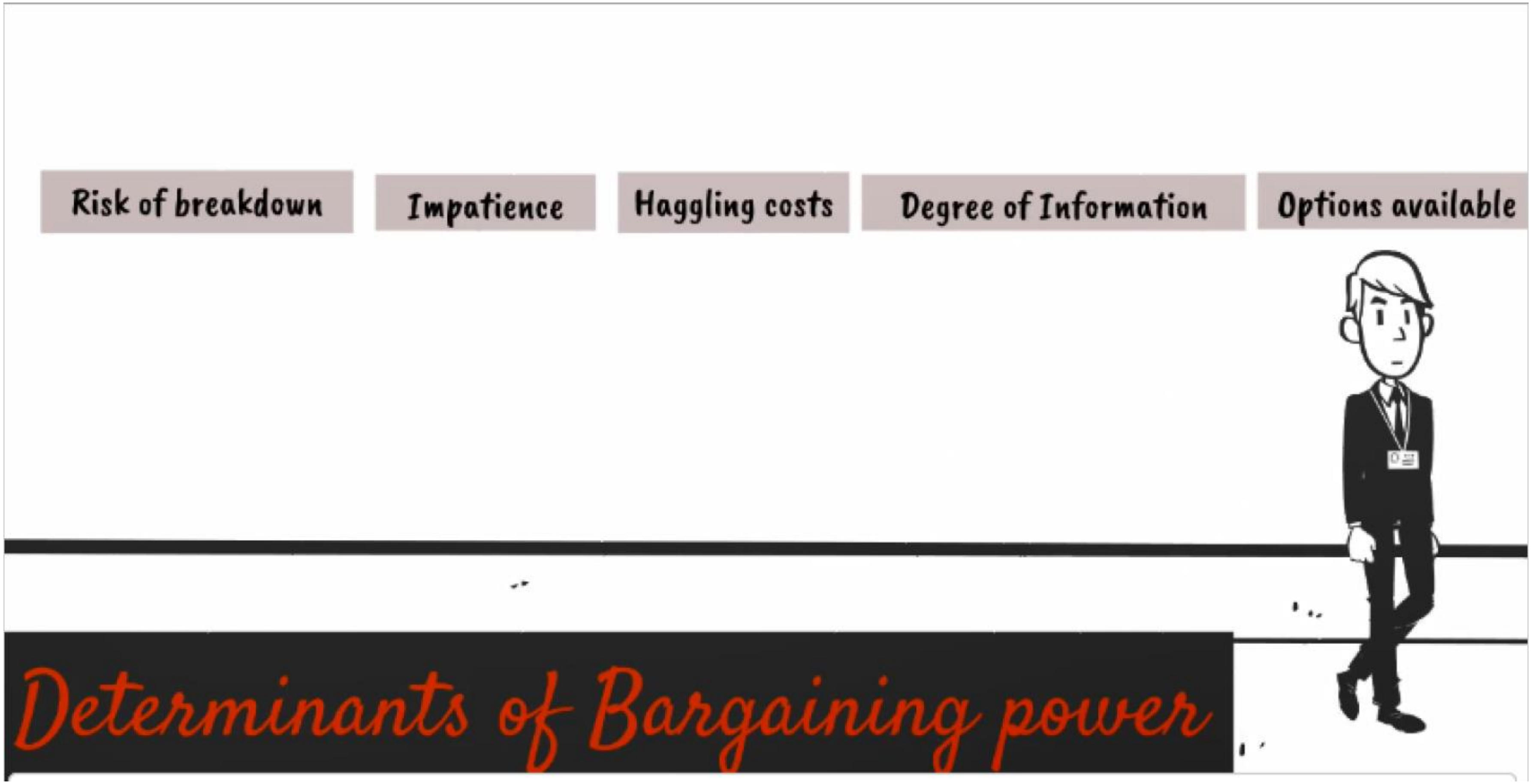
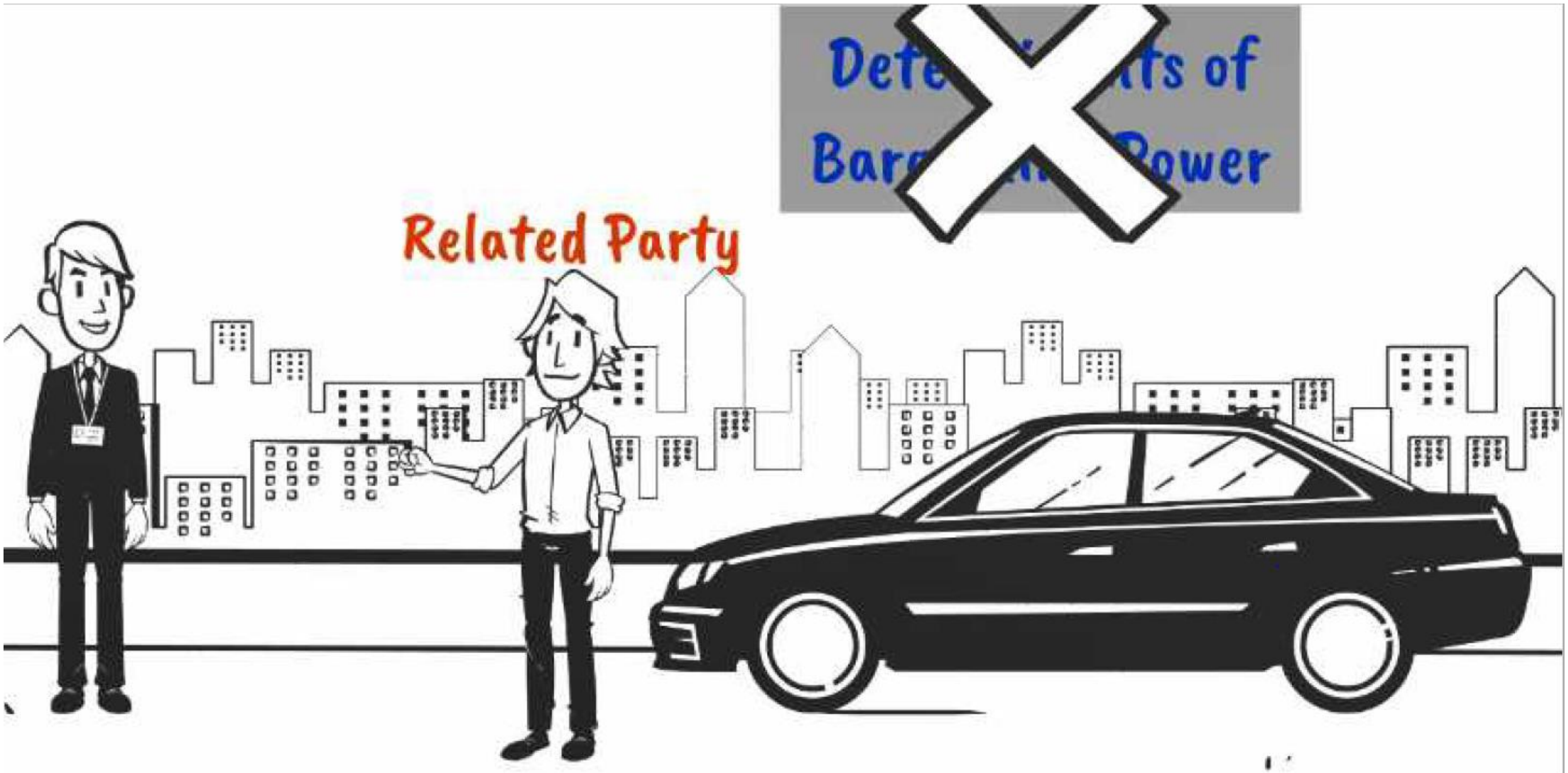
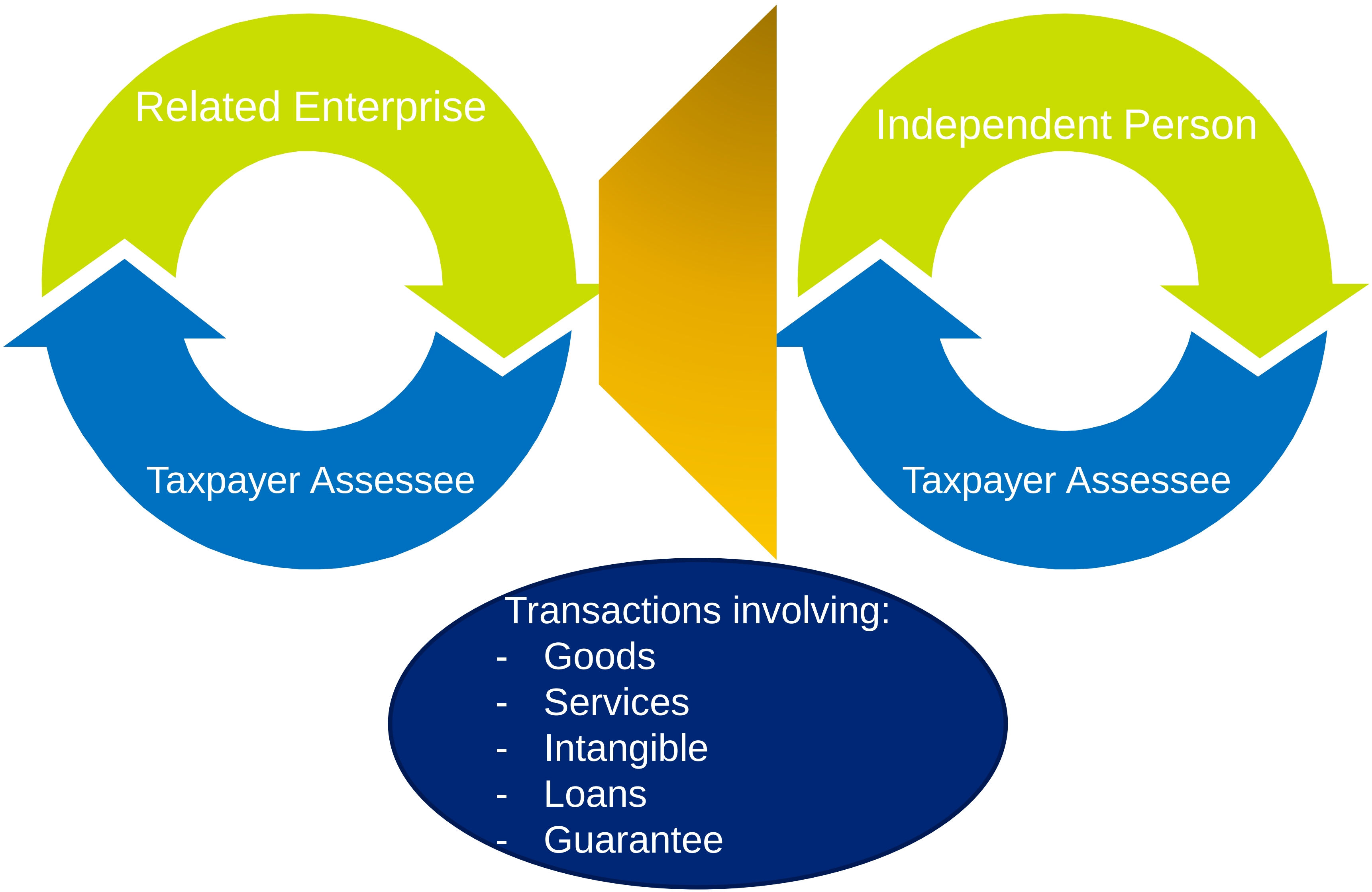


Risk of breakdown
Impatience
Haggling costs
Degree of Information
Options available
Determinants of Bargaining power

Exercise – 1



What is transfer pricing



Historical background of Transfer Pricing

- Prevent erosion of Government’s tax base
- 60% of international trade is carried on with AEs
- To counter the effect of transfer of profits, many developing and developed countries introduced Transfer Pricing Regulations
- Increased the burden of proof on taxpayers
- Transfer Pricing adjustment by Revenue for computing tax liability

Historical background of Transfer Pricing

- Complex issue requiring knowledge of multiple disciplines:
  - ✓ Taxation
  - ✓ Accounting
  - ✓ Economic
  - ✓ Legal
  - ✓ Statistical

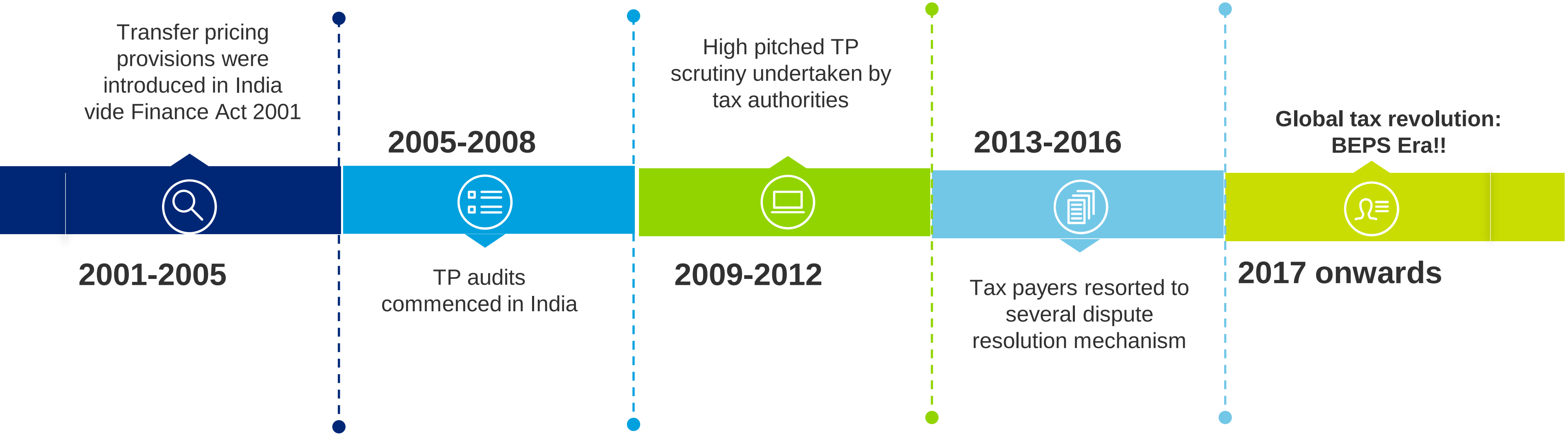
- Becoming more and more of mathematical and statistical issue – involving comparables and their mark-ups

- Organization for Economic Co-operation and Development (“OECD”)’s views on transfer pricing:

Transfer pricing can deprive governments of their fair share of taxes from global corporations and expose multinationals to possible double taxation. No country - poor, emerging or wealthy - wants its tax base to suffer because of transfer pricing. The arm's length principle can help

Historical background of Transfer Pricing in India

Story so far….



Legislative Evolution of Transfer Pricing in India

Significant Legislative Changes

- **2001**– detailed framework for transfer pricing introduced in India
- **2009** – formation of **Dispute Resolution Panel (DRP)**
- **2012** – **APA program** introduced in India
- **2013 – Safe Harbour Rules (SHR)** announced
- **2014** – definition of **'deemed international transaction**' amended to expressly include domestic third party transactions
- **2016** – revised internal circular for reference of cases for transfer pricing scrutiny
- **2017** – **secondary adjustments** brought in to remove the imbalance between cash profit and actual profit as a result of transfer pricing adjustments
- **2017** – revised safe harbor rates for **IT/ IT enabled Services (ITeS) transactions** and **SHR** introduced for **Low value added Intra Group Services (IGS)**

Major Global Alignment Measures

- **2015** – computation of Arm's Length Price (ALP) streamlined:
  - Introduction of **range concept**
  - Use of **multiple year data**
- **2017** - introduction of **Country-by-Country (CbC) reporting and Master File** requirements
- **2017** – introduction of **interest deduction limitations**

Exercise – 2

Scenario : 1 Particulars	India	Singapore	Remarks
Selling Price of India / Singapore	1600	1300	Total tax amount for the Group = 77
Purchase cost of goods	1300	1200	
Selling cost in India	100	-	
Profit	200	100	
Tax rate	30%	17%	
Tax amount	60	17	

Scenario : 2 Particulars	India	Singapore	Remarks
Selling Price of India / Singapore	1600	1400	Total tax amount for the Group = 64
Purchase cost of goods	1400	1200	
Selling cost in India	100	-	
Profit	100	200	
Tax rate	30%	17%	
Tax amount	30	34	

Insights of Base Erosion and Profit Shifting (“BEPS”)

Global Tax Revolution – Base Erosion Profit Shifting !

Currently MNCs are facing a number of new challenges including:

- **Perception that MNCs are not paying fair share of taxes**
- **Loss of trust between tax authorities and businesses**
- **Loss of trust between tax authorities in different countries**

This new global tax environment has resulted in the following actions – a Global Tax Revolution:

- **Change in tax authorities' approach to interpretation of tax laws and tax treaties**
- **OECD's BEPS project**
- **Unilateral actions**

Discourage MNCs that are aggressive in tax planning and make them a little bit more moderate and measured

Base Erosion and Profit Shifting (BEPS) Program

- Refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits

- Over 100 countries and jurisdictions are collaborating to implement the BEPS measures and tackle BEPS under the inclusive framework

- BEPS program's 15 Actions are based on three (3) key pillars:
  - Coherence in domestic laws
  - Substance requirements
  - Improving transparency

- The Government is equipped with instruments to address tax avoidance, ensuring profits are taxed where economic activities generating the profits are performed and where value is created

Base Erosion and Profit Shifting – 15 Actions

Actions	Action Name	Action Objective
1	Digital economy	Rework existing tax rules to deal with digital economy. May involve introduction of VAT on digital goods, virtual PE rules, WHT etc.
2	Hybrid mismatch arrangements	To curb abuse of hybrid instruments / entities, may involve ordering rules to specify primary and defensive rules with respect to the deduction and the exemption
3	Controlled Foreign Company (CFC) Rules	Curb tax deferral through parking of profits to low/new tax jurisdictions. May involve identification of best practices and likely a proposal for some form of minimum standard for CFC rules
4	Limit base erosion via interest deductions	Address thin capitalization issues. Group wide approach and fixed ratio approach being evaluated
5	Counter harmful tax practices	Curb tax competition among countries to attract investments e.g., UK Patent Box, Dutch Innovation Box, low/ reduced CTX rates
6	Prevent treaty abuse	Objective of treaty is not to create double non-taxation. May involve introduction of US style LOB or UK style GAAR (principle purpose test) Rules
7	Prevent artificial avoidance of PE	Amending PE article in tax treaties to remove loopholes in PE clause and address artificial avoidance arrangements

Base Erosion and Profit Shifting – 15 Actions

Actions	Action Name	Action Objective
8	TP aspects of Intangibles	Ensuring that profits associated with the transfer and use of intangibles are appropriately allocated in line with value creation
9	Risks and capital	Substance over form w.r.t. capital contribution or allocation of risks
10	Other high risk Transactions	Develop rules to prevent BEPS involving transactions which would not (or would only very rarely) occur between third parties. e.g., intra group services, management fees, etc.
11	Analyze data on BEPS	Analyzing economic impact of actions taken to address BEPS on ongoing basis (taxpayer confidentiality, compliance costs and burdens on taxpayers and tax administrations)
12	Disclosure of aggressive tax Planning	Develop mandatory disclosure rules for aggressive or abusive transactions, arrangements or structures
13	Re-examine TP documentation	Introducing three tiered documentation consisting of Master file, Local file and CbC reporting template
14	Dispute resolution	Improving effectiveness of MAP and arbitration provisions
15	Multilateral instrument	Develop multilateral instruments which would be signed by all countries to agree upon common treaty arrangements

Base Erosion and Profit Shifting – Action 8 Intangibles

An intangible is:

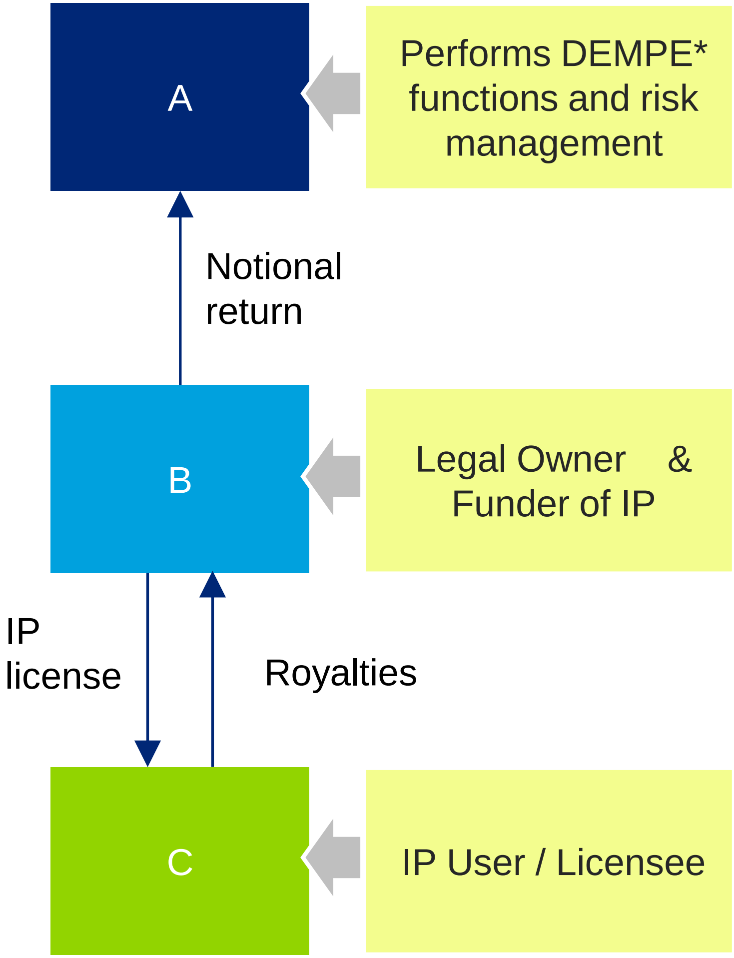
- Not a physical asset or a financial asset
- Capable of being owned or controlled for use in commercial activities
- Whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances

Examples	
Intangibles for TP Purposes	Not Intangibles for TP Purposes
Patents	Group Synergies
Know-how and trade secrets	Market specific features
Trademarks, trade names and brands	Assembled workforce
Rights under contracts and government license	
Licenses and similar limited rights in intangibles	
Goodwill and ongoing concern	

Finance Act, 2012 India has adopted (retrospectively from AY 2002-03) an expanded definition of 'intangible property' covering ten different kinds of intangibles - marketing, technology, artistic, engineering, customer, location, human capital and a few others - and as if that was not enough, a residual clause covering 'any other item deriving its value from intellectual content' is also provided

Base Erosion and Profit Shifting – Action 8 Intangibles

Example:



TP outcomes from this example under the new TP Guidelines:

- As legal owner of the IP, B receives royalties from C, in return for granting C the right to use the IP
- A is entitled to a notional return from B – the legal owner – for the performance of DEMPE functions and risk management
- If B only funds the IP and assumes no control over A's DEMPE functions **or risk management (including funding risk)**, B is only entitled to a risk-free return
- For transfer pricing purposes, A is entitled to all of the returns from exploitation of the IP above the risk free return

*DEMPE = Development Enhancement, Maintenance, Protection, Exploitation

Base Erosion and Profit Shifting – Action 8 Intangibles

Practical challenges:

- What is value creation ?
- More than one entity performing DEMPE function
- DEMPE analysis will put pressure on defining the correct intercompany pricing
- Difficult to find comparable independent parties undertaking DEMPE function
- Undertaking price adjustment in case of non availability of independent comparable companies
- Legal owner of intangible to earn risk free return – Whether the same is comparable to loan transaction?
- Circular 6/2013 – Allocation of routine cost plus – whether arm's length?
- Divergent views in relation to treatment of intangibles as international transaction
- Hard to value intangibles – Practical application?

Base Erosion and Profit Shifting – Action 10 Low Value Intra-Group Transactions

1. Characteristics

- Intra-group services are:
  - Supportive in nature
  - Not a part of core group business
  - Can be principal business activity of the service provider
  - Do not require unique/ valuable intangibles
  - Do not lead to creating of unique/ valuable intangibles
  - Do not involve or give rise to significant risk

2. Examples

- Accounting & auditing
- Processing and management of debtors/ creditors
- Activities in connection with human resources
- Information technology support services
- Internal and external communications and public relations support
- Legal, administrative, tax compliance and other clerical services

3. Exceptions

- Services constituting core group business
- Research & development
- Manufacturing and production
- Purchasing, sales, marketing and distribution
- Financial transactions
- Extraction, exploration or processing of natural resources
- Insurance/ reinsurance
- Services of Corporate Senior management

Cautions that if a company's activities do not qualify for the simplified method, it should not be assumed that such activities should generate high returns

Base Erosion and Profit Shifting – Action 13 Three Tier Documentation

Evolution of existing transfer pricing documentation requirements

Master File

- Group wide description including supply chain, value drivers, main markets, high level functional analysis, details of business changes
- High level description of IP strategies, IP location and R&D management and location
- High level description of group financing arrangements
- Consolidated group accounts
- Description of APAs or other rulings

Local File

- Transactional/entity specific;
- Local management structure, detailed functional analysis, economic analysis and reconciliations of TP to accounts.
- Local documentation nuances continue?

A new requirement

Country-by-Country

- Revenue
- Profit before tax
- Cash tax paid
- Current Tax Accrual
- Capital and retained earnings
- Net Book Value of tangible assets
- Number of employees
- Complete list of entities and PEs for each country, with activity codes to be attached to template

Compliance

Policy | **Calculate** | **Process** | **Monitor** | **Document** | **Defend**

Base Erosion and Profit Shifting – Action 13 Tree Tier Documentation

Overview of CbC reporting

What is CbC reporting?

CbC reporting is part of the OECD's BEPS Action 13. In essence, large MNEs have to provide an annual return, the CbC report, that breaks down key elements of the financial statements by jurisdiction

Who is impacted?

CbCR will apply to MNEs with a combined group revenue of Euro 750 million or more and who prepare or would be required to prepare the consolidated financial statements. The ultimate parent entity may nominate alternate reporting entity to prepare and file the CbCR

What is the governing principle to determine the constituents of an MNE group for CbC reporting?

The governing principle to determine an MNE Group for the purpose of CbC reporting is to follow the accounting consolidation rules governed in the tax jurisdiction of the parent entity

When does it take effect?

This depends on when countries implement CbC report into their own legal system, but the intention is that reports will be required for the fiscal years starting on or after the 1st of January 2016 (FY16) and should be filed within 12 months of the relevant year end

Base Erosion and Profit Shifting – Action 13 Tree Tier Documentation

Where is a CbC report filed?

CbC reports are primarily to be filed where the parent company is headquartered (HQ). If the HQ country has not implemented CbCR, MNEs should file in the country with CbC reporting where their most significant activities occurs

Which jurisdictions will have access to the CbC report filed by the parent company?

The countries participating in the BEPS project will exchange CbC report through Multilateral Competent Authority Agreement/bilateral tax agreements for exchange of CbC report

With respect to confidentiality, the participating countries have agreed to have in place and be prepared to enforce legal protections of the confidentiality of the information in the CbC report equivalent to those under the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, a tax information exchange agreement (TIEA) or a tax treaty

Why are CbC reports needed?

CbC template is intended to be used for risk assessment purposes only and is not a conclusive evidence on whether transfer prices are appropriate or not. CbCR should not be used as a substitute for a detailed TP analysis of individual transactions and prices based on a complete functional and comparability analysis

Article 9 of OECD / UN TP Model

Arm's Length Principle

Article 9 of OECD / UN Model Tax convention deals with Associated Enterprise and the concept of transfer pricing in taxability.

Para (1) determines the relationship

"*1. Where:*

(a) An enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or

(b) The same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly"

Arm's Length Principle

While Para (2) determines the taxability:

"2. Where a Contracting State includes in the profits of an enterprise of that State-and taxes accordingly-profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other state shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjustment, due regard shall be had to the other provisions of the Convention and the competent authorities of the Contracting States shall, if necessary, consult each other."

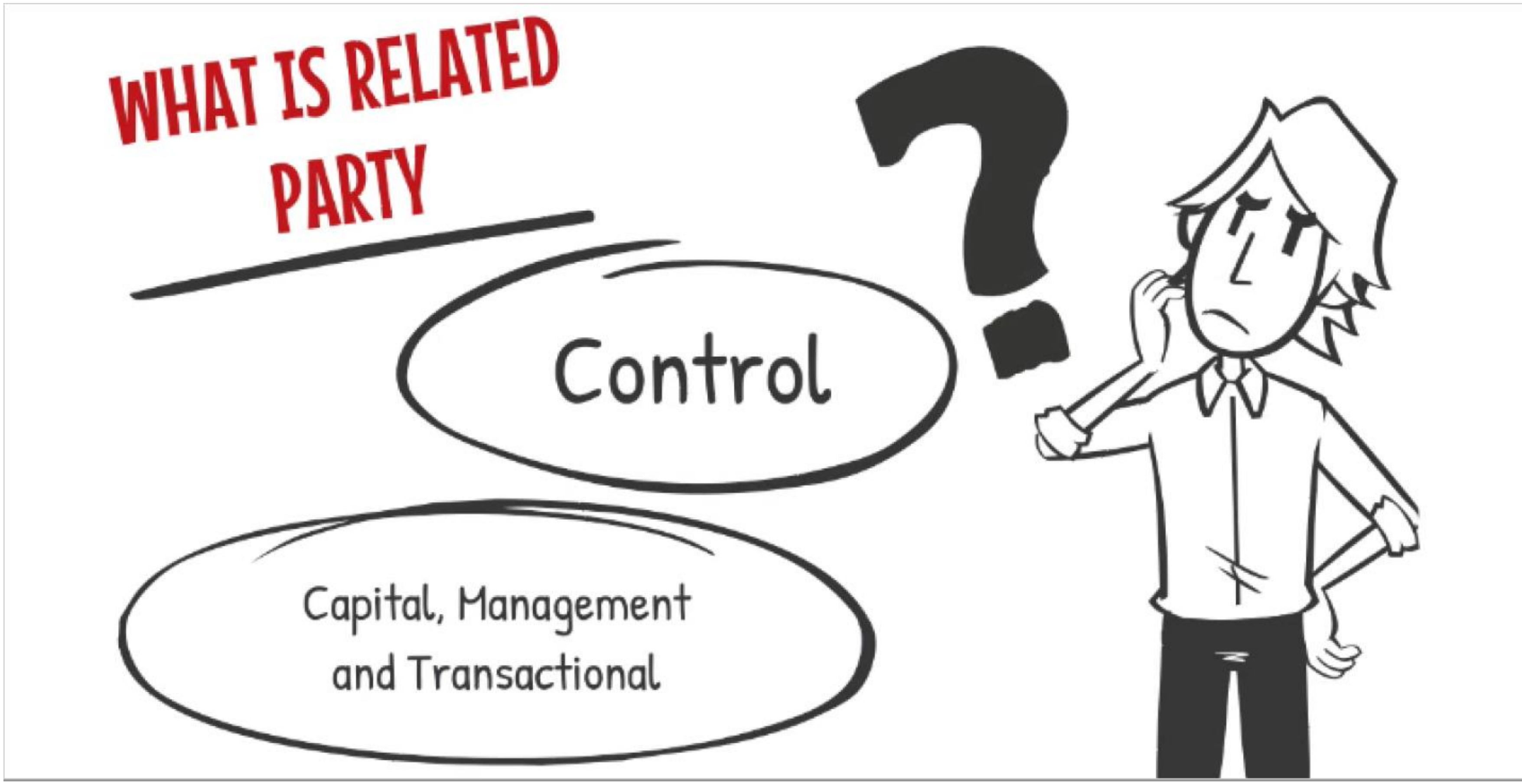
Associated Enterprise as per Income-tax Act, 1961

Indian Transfer Pricing Regulations

Sections 92 to 92F of the Act govern the Indian transfer pricing provisions.

Section & Rules	Provisions
92	Computation of income having regard to ALP
92A	Meaning of Associated Enterprise
92B	Meaning of International transaction
92BA	Meaning of specified domestic transactions
92C (1) (Rule 10B, 10C)	Methods of computation of ALP *Rule 10AB – Any other method for determination of ALP
92CA	Reference to Transfer Pricing Officer (TPO)
92CB	Safe harbour rules
92CC	Advance Pricing agreement
92CD	Effect of advance pricing agreement
92D (Rule 10D)	Maintenance of information and documents by persons entering into an international transaction or specified domestic transaction
92E (Rule 10E, Form 3CEB)	Accountant's Report entering into an international transaction or specified domestic transaction
92F (Rule 10A)	Definitions: Accountant, ALP, Enterprise, PE, Specified date, Transaction *

Associated Enterprise Relationship



Associated Enterprise Relationship

Section 92A defines the meaning of the term associated enterprise

Equity / Debt

- Directly or indirectly holds $\geq$ 26% of voting power in another;
- One entity holds $\geq$ 26% of voting power in each of two enterprises;
- Book loan $\geq$ 50% of the book value of total assets;
- Guarantee $\geq$ 10% of the value of total borrowings;
- 10% interest in Firm / AOP / BOI.

Management

- Appointment of $\geq$ 50% of Directors / one or more Executive Director by an enterprise;
- Appointment by same person in each enterprise.

Activities

- 100% dependence on use of intangibles for manufacture / processing / business;
- Direct / indirect supply $\geq$ 90% of raw material under influenced prices and conditions;
- Sale under influenced prices and conditions.

Control

- One enterprise controlled by an individual and the other by himself or his relative or jointly;
- One enterprise controlled by HUF and the other by a member or his relative or jointly.

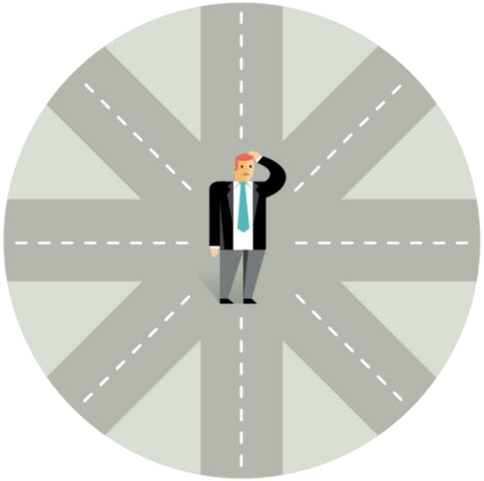
International Transactions as per Income-tax Act, 1961

International Transactions

Section 92B defines the meaning of the term international transaction

- Transaction between two or more associated enterprises, either or both of whom are non-residents

- In the nature of -
  - 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 such enterprises,
  - Any mutual agreement or arrangement on allocation or apportionment or any contribution of cost or expenses
  - Business restructuring or reorganization irrespective of whether it has impact on profit, income, losses or assets



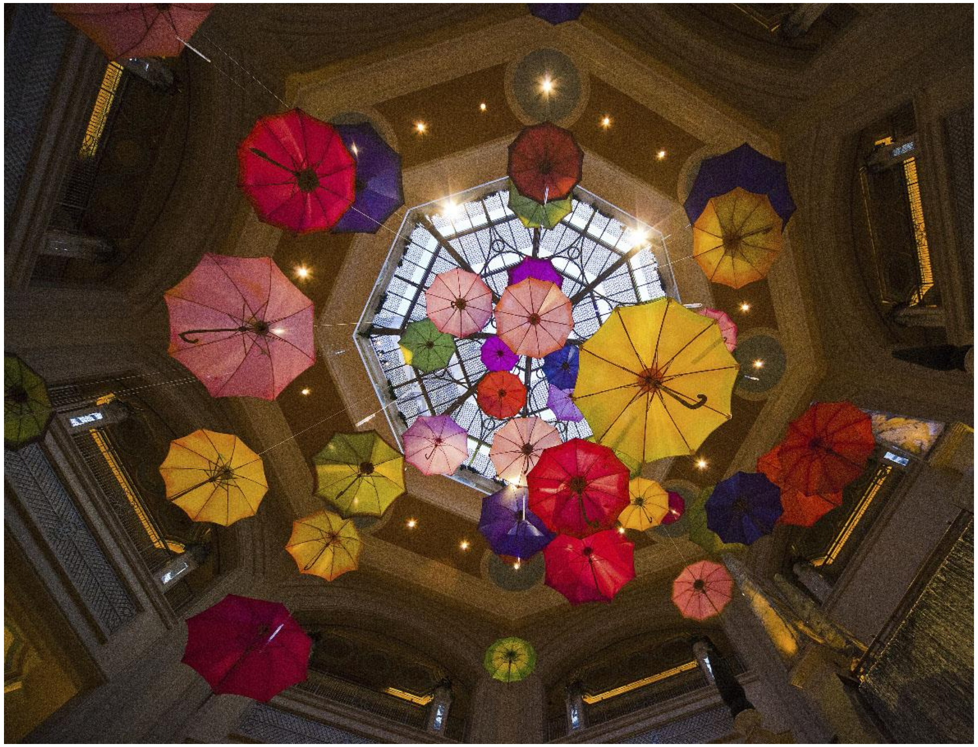
International Transactions

Explanation to Section 92B

International Transaction	Includes
Tangible Property	• Purchase, Sale, Transfer, Lease / Use of property / Article / Product / Thing • Includes Building, Vehicle, Machinery etc.
Intangible Property	• Purchase, Sale, Transfer, Lease / Use of Intellectual Property • Includes Transfer of ownership/use of rights/other commercial right, etc.
Capital Financing	• Long/short term borrowing / lending • Guarantee • Purchase / Sale Securities • Advances / receivables, Payments / any debt, etc.
Provision of Services	• Market Research / Development • Technical Service • Scientific Research • Legal / Accounting Service etc.
Business Restructuring	• Transaction of Business restructuring / reorganization with AE irrespective of bearing profit / income / loss or assets – at the time of transaction / future date.

International Transactions

- The term "intangible property" includes the following categories of intangibles:
  - Marketing
  - Technology
  - Artistic
  - Data processing
  - Engineering
  - Customer
  - Contract
  - Human capital
  - Location
  - Goodwill
  - Methods, programmes, systems, procedures, surveys, studies, forecasts, customer lists, technical data etc.
  - Any other item that derives value from its intellectual content



Deemed International Transaction

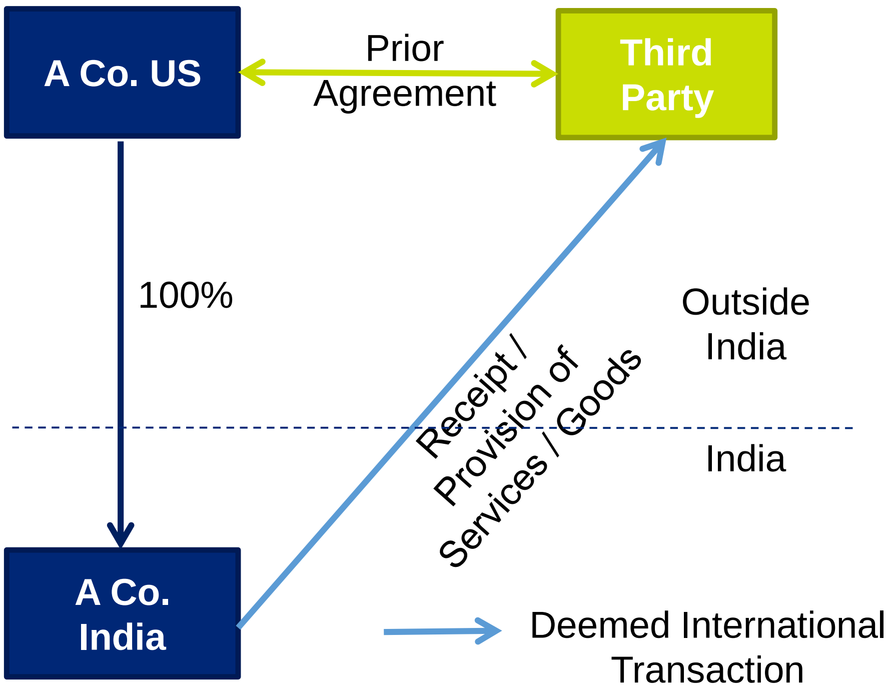
Provisions and Interpretation upto FY 2013-14:

Transaction with a person other than an AE shall be deemed to be a transaction entered into between two AEs if

- A prior agreement exists between the AE and third party

  Or

- Terms of the transaction are determined in substance by the AE and third party



Certain judicial pronouncements favored the position that the third party had to be non-resident for this deeming provision to trigger

Deemed International Transaction

Provisions and Interpretation w.e.f. FY 2014-15

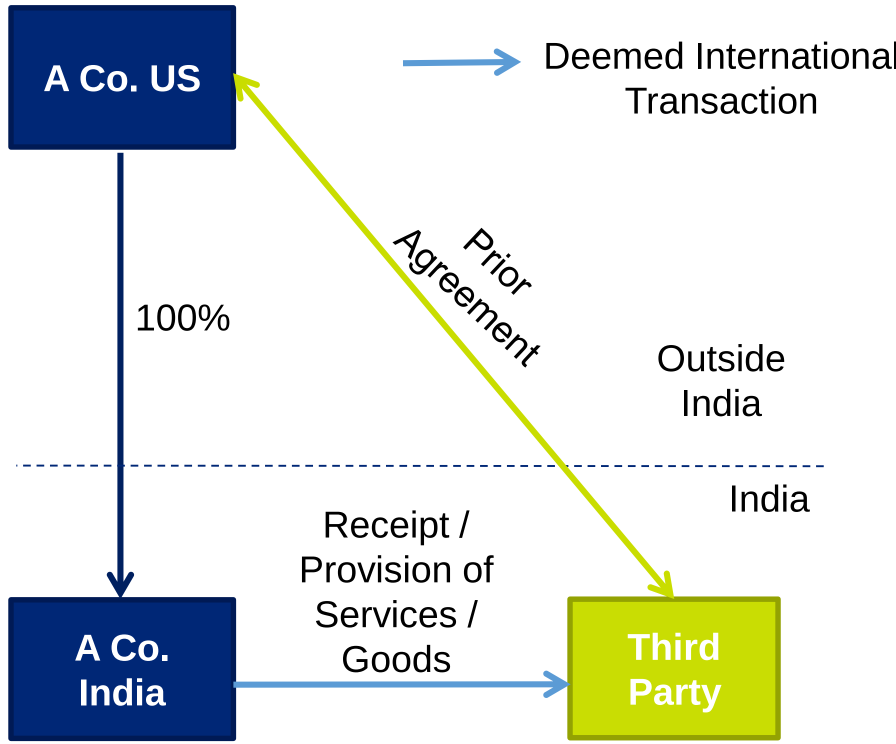
Transaction with a person other than an AE shall be deemed to be an international transaction entered into between two AEs if

- A prior agreement exists between the AE and third party

  Or

- Terms of the transaction are determined in substance by the AE and third party

Irrespective of whether the third party is resident or not



Tax residency of third party is irrelevant

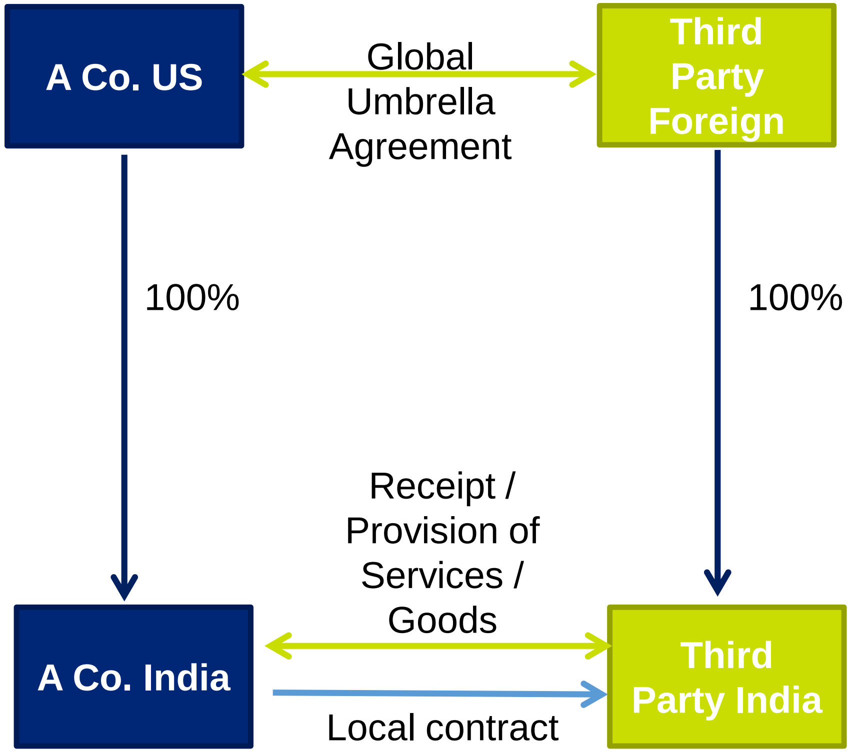
Deemed International Transaction

Quadrilateral :

Two views possible on applicability of deeming provision for the transaction between A Co., India and the Third party in India:

1. **Not applicable -** Since no prior agreement directly between foreign AE and third party in India.

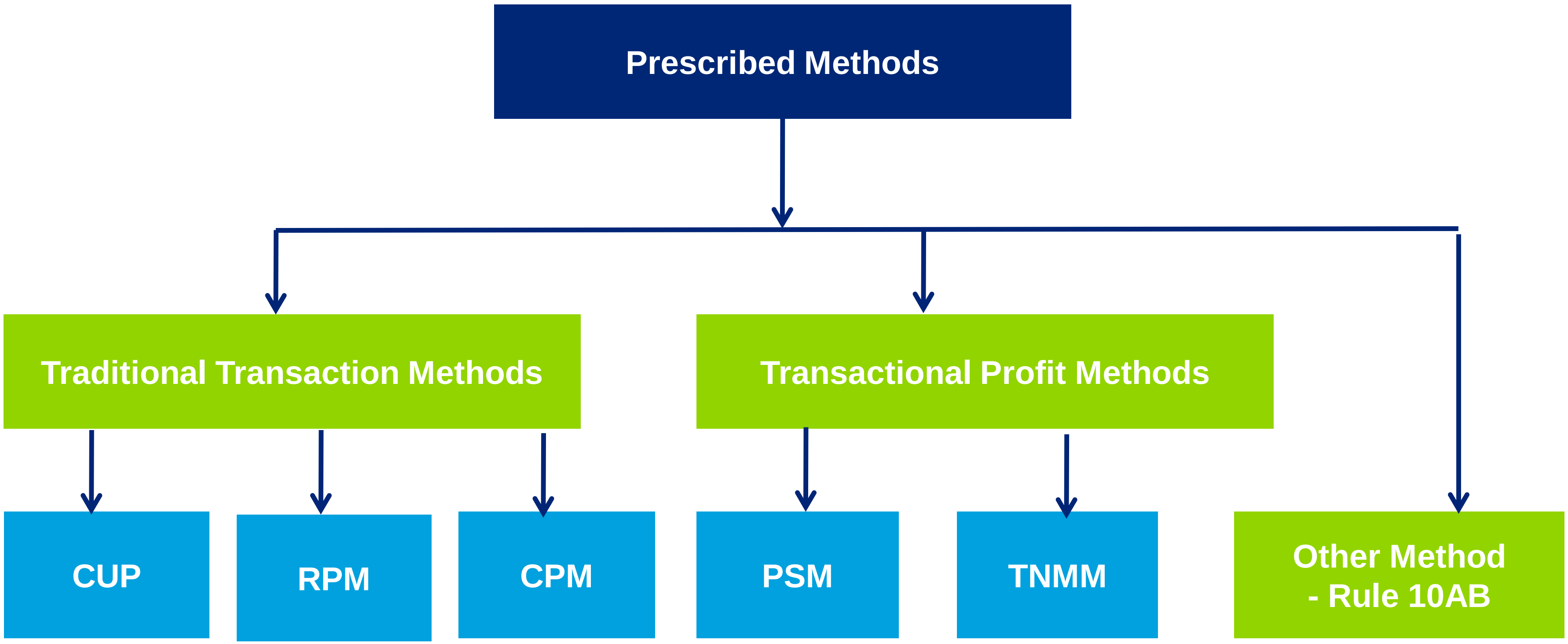
2. **Applicable –** Arguably, intention of the law is to cover all transactions with any party where terms of agreement are not determined by the taxpayer on a standalone basis but are determined by its AE



In case the legal view (i.e. View 1 - transaction does not qualify as deemed international transaction) is taken, it is important that adequate disclosures, with an appropriate note, are made in the annual TP certificate filed in Form No. 3CEB, from a penalty protection perspective.

Methods & Benchmarking

Methods



No hierarchy or preference of methods prescribed under the Act

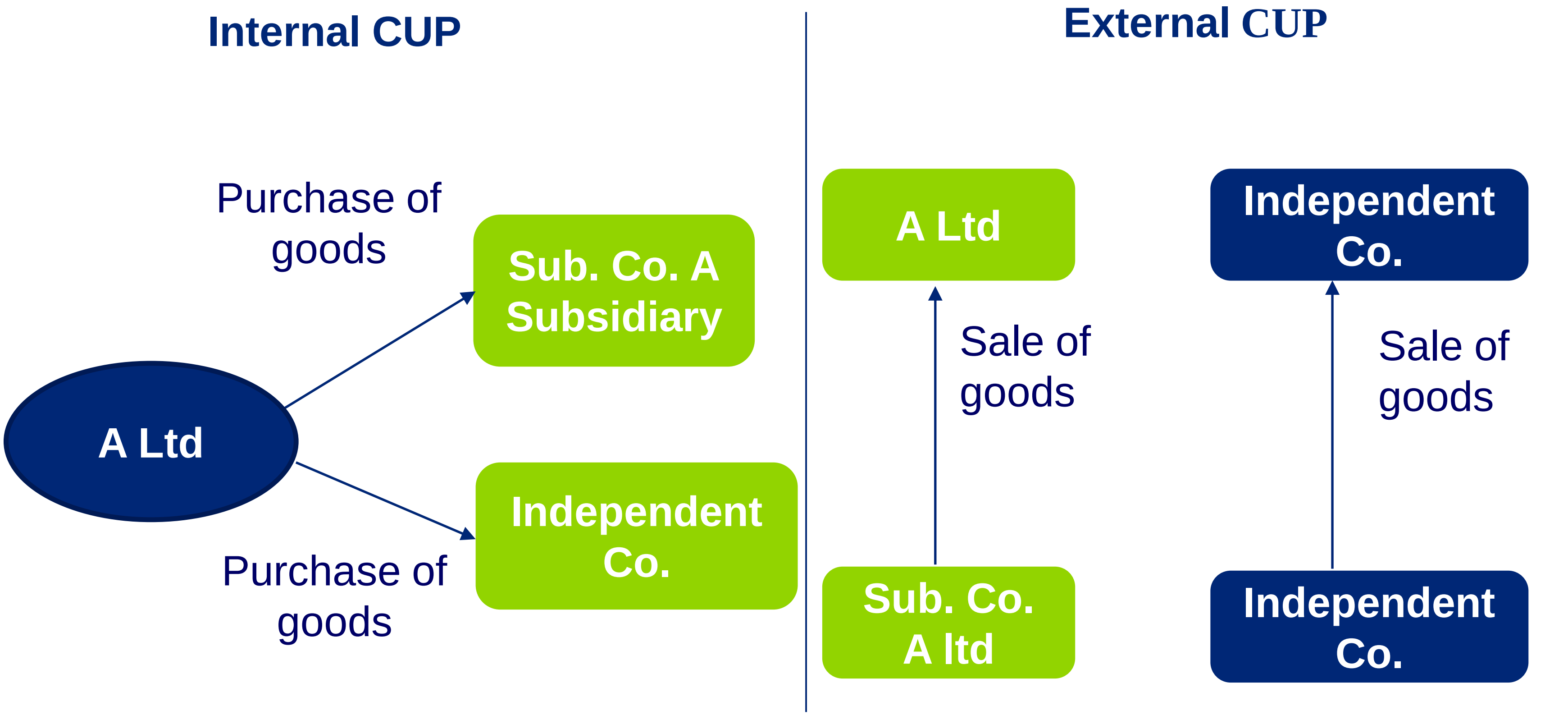
Methods

Comparable Uncontrolled Price ("CUP") Method:

- Most Direct Method
- Prices are benchmarked without any reference to the profits
- Requires strict comparability in products, contractual terms, economic terms, etc..:
  - ✓ Strong similarity of products and services
  - ✓ Geography of markets
  - ✓ Functions and Risks
  - ✓ Business strategy
  - ✓ Contractual terms
  - ✓ Timing of the transaction
  - ✓ Volume
- Two types of CUPs available –Internal CUP & External CUP
- Typically Internal CUP is preferred over External CUP due to higher degree of comparability

Methods

Example of CUP:



Internal CUP is preferable

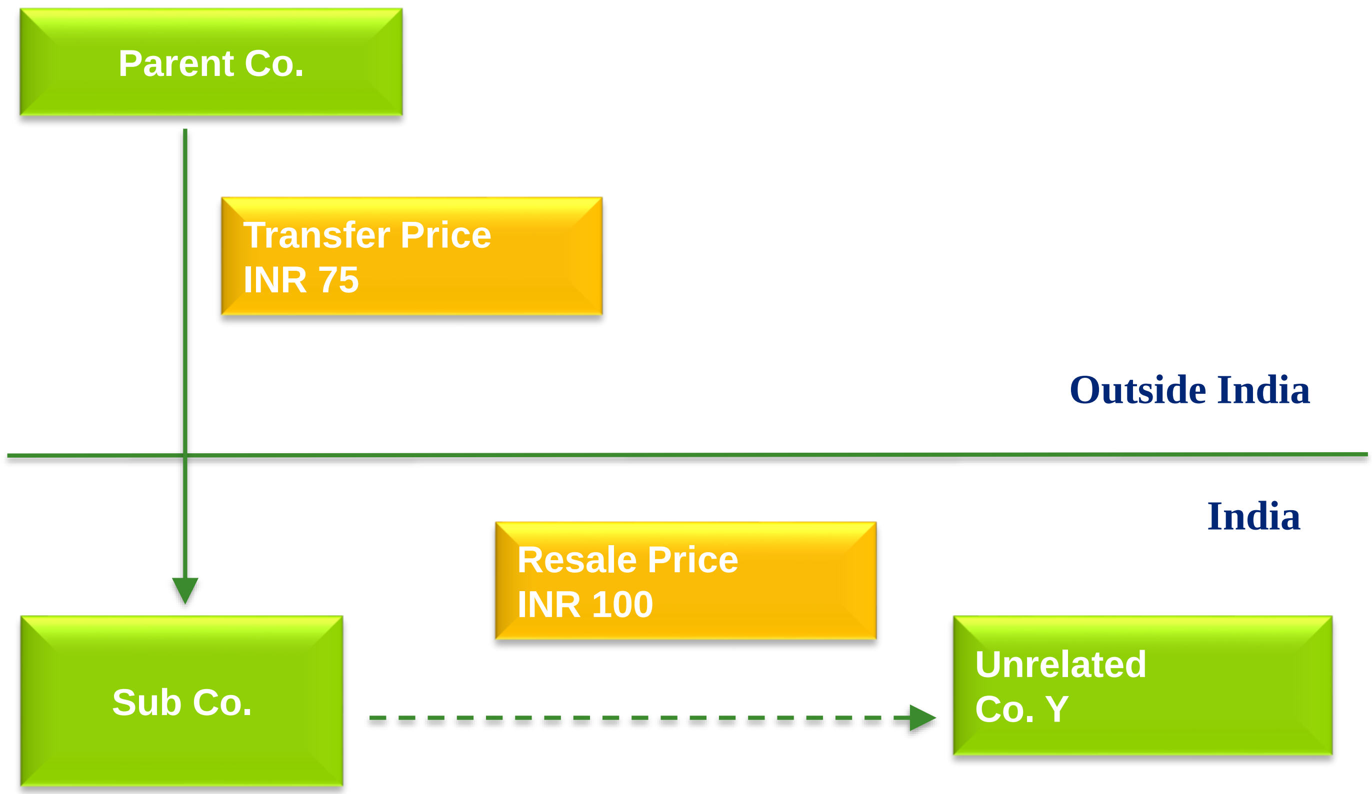
Methods

Resale Price Method ("RPM"):

- Preferred method for a distributor buying purely finished goods from a group company (if no CUP available)
- Ordinarily used in cases involving the purchase and resale of tangible property
- Reseller has not added substantial value whether tangible or intangible
- Packaging, labeling, or minor assembly are acceptable
- Difficult to apply where goods are further processed before resale
- Comparability is relatively less dependent on strict product comparability and additional emphasis is on similarity of functions performed & risks assumed

Methods

Example of RPM:



Price paid by Sub Co. to AE is at arm's length if the 25% resale margin earned by Sub Co. is more than margins earned by similar Indian distributors`

Methods

Cost Plus Method ("CPM"):

- Compares and identifies mark-up earned on direct and indirect costs of production incurred with that of comparable independent companies

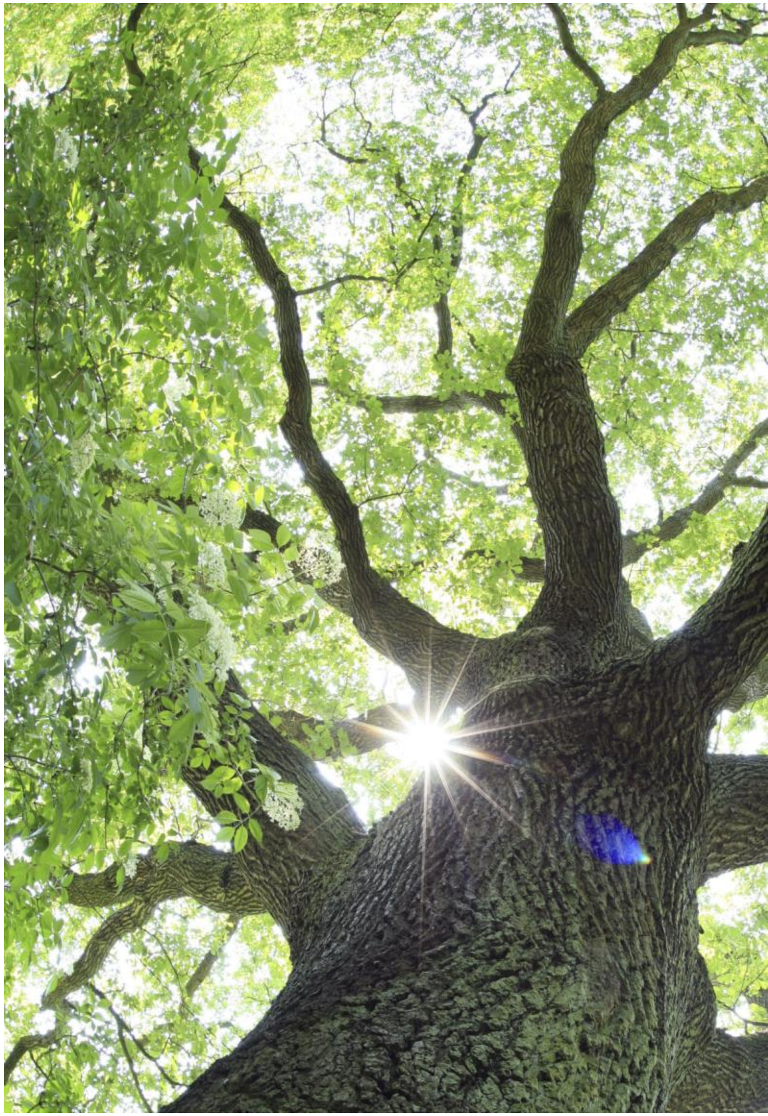
- Preferred method in case -

  - Semi-finished goods sold between related parties
  - Contract manufacturing agreement
  - Provisions of services on contract basis

- To be applied in cases involving manufacture, assembly or production of tangible products or services that are sold /provided to AEs

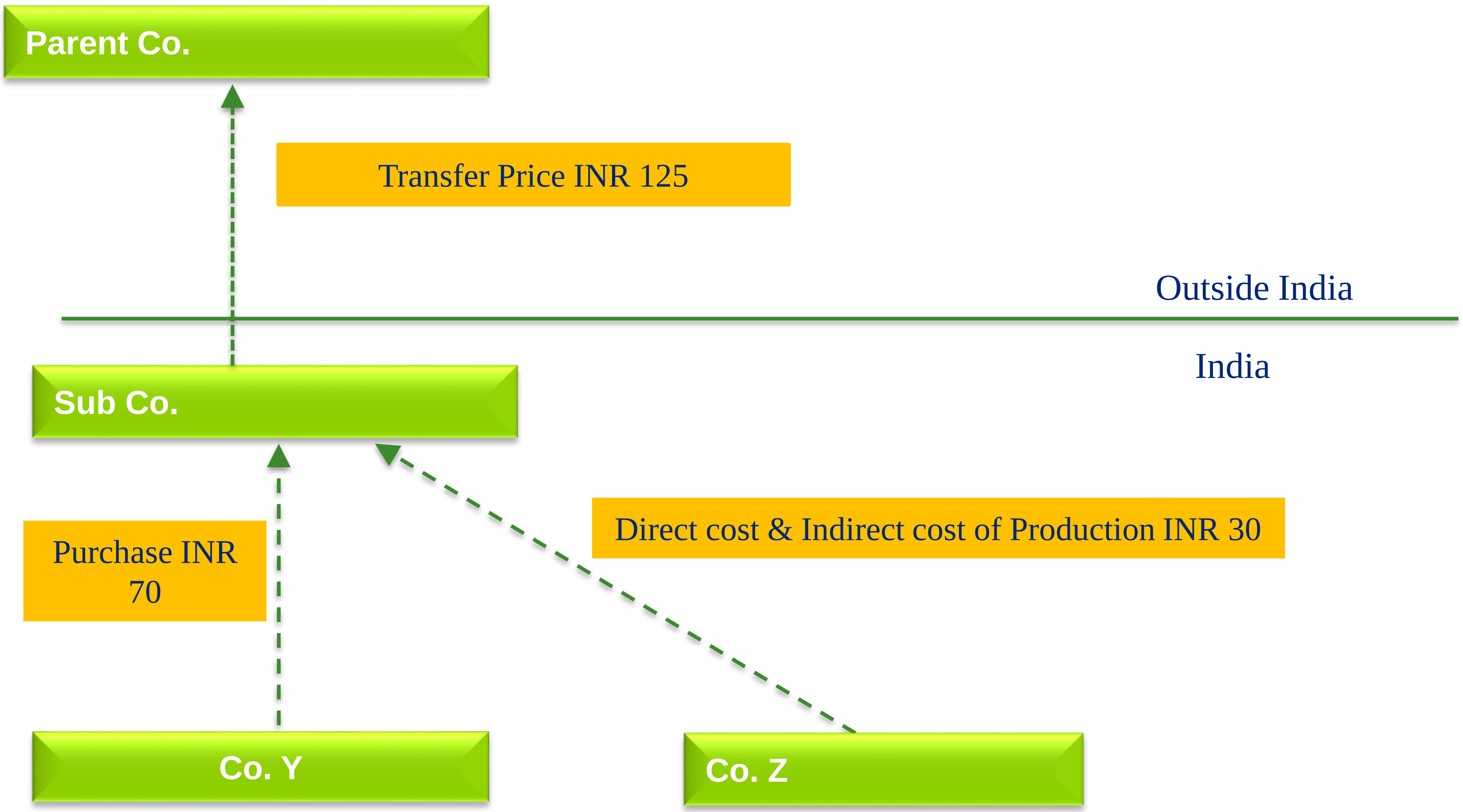
- Comparability under this method is relatively not as much dependent on close physical similarity between the products

- Larger emphasis on functional comparability



Methods

Example of CPM:



Price charged by Sub co to AE is at arm’s length if the 25% mark up on cost is more than that of similar Indian assemblers

Methods

Profit Split Method (“PSM”)

- Applied in cases involving-
  - transfer of unique intangibles or
  - in multiple international transactions that cannot be evaluated separately

- Calculate the combined operating profit resulting from an inter-company transaction based on the relative value of each AEs’ contribution to the operating profit

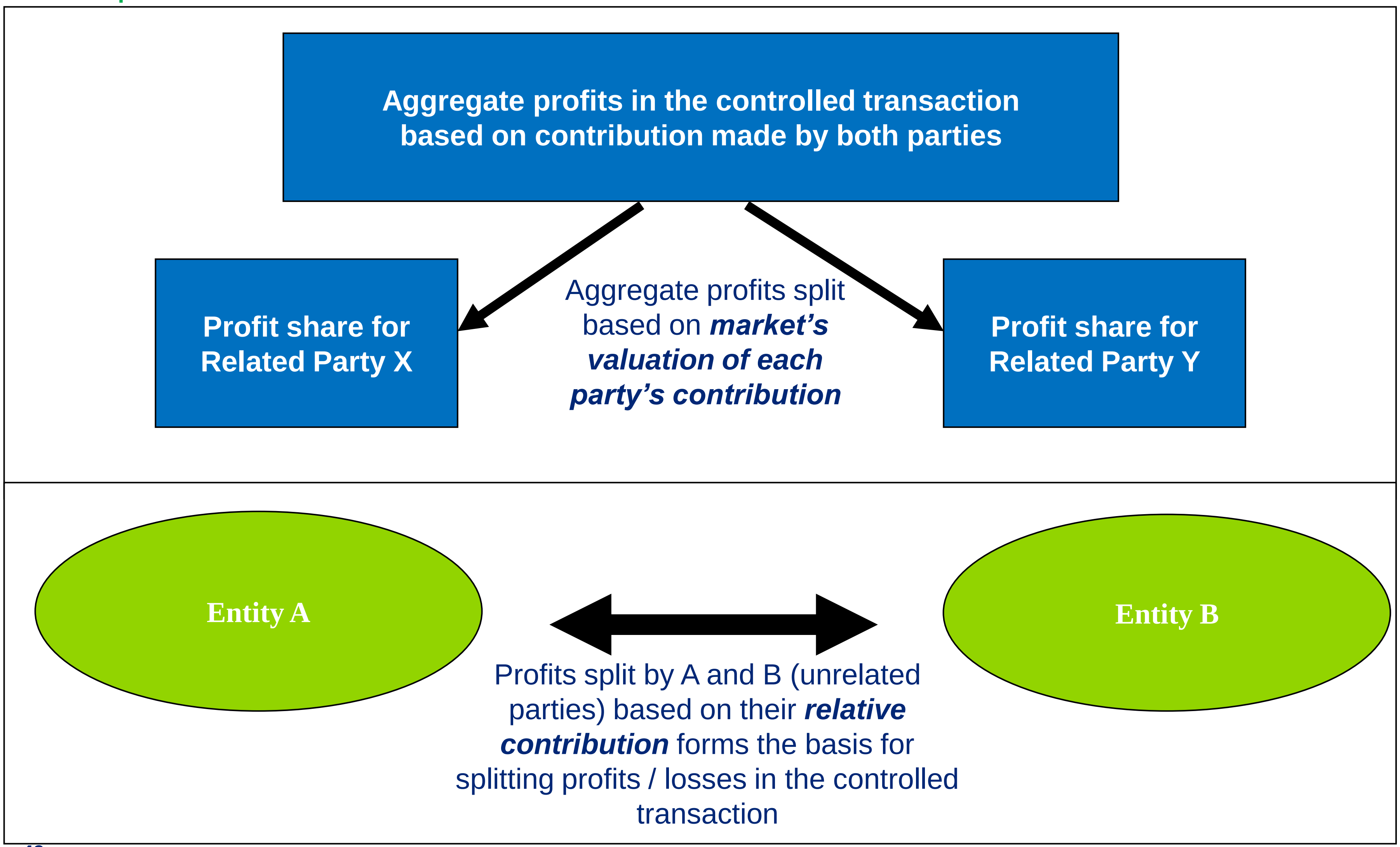
- Evaluates allocation of combined profit / loss in controlled integrated transactions

- Contribution made by each party is based upon a functional analysis and valued, if possible, using external comparable data

- Allocation methods:
  - Combined profit split method; and
  - Residual profit split method

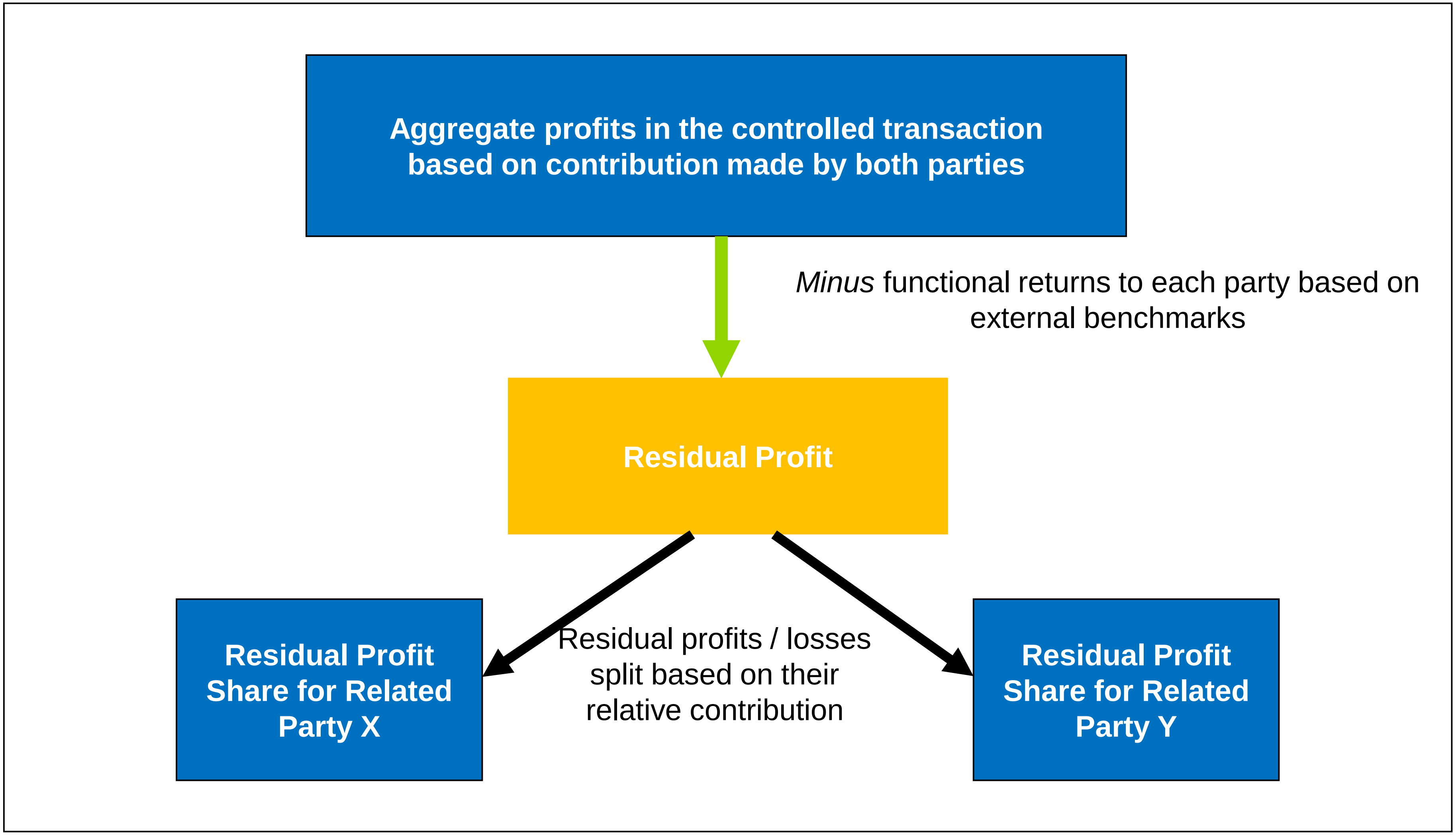
Methods

Example of PSM:



Methods

Example of PSM:



Methods

Transactional Net Margin Method ("TNMM")

- Most frequently used method, due to lack of availability of data for application of other methods

- Examines net operating profit from transactions as a percentage of a certain base (can use different bases i.e. costs, turnover, etc.)

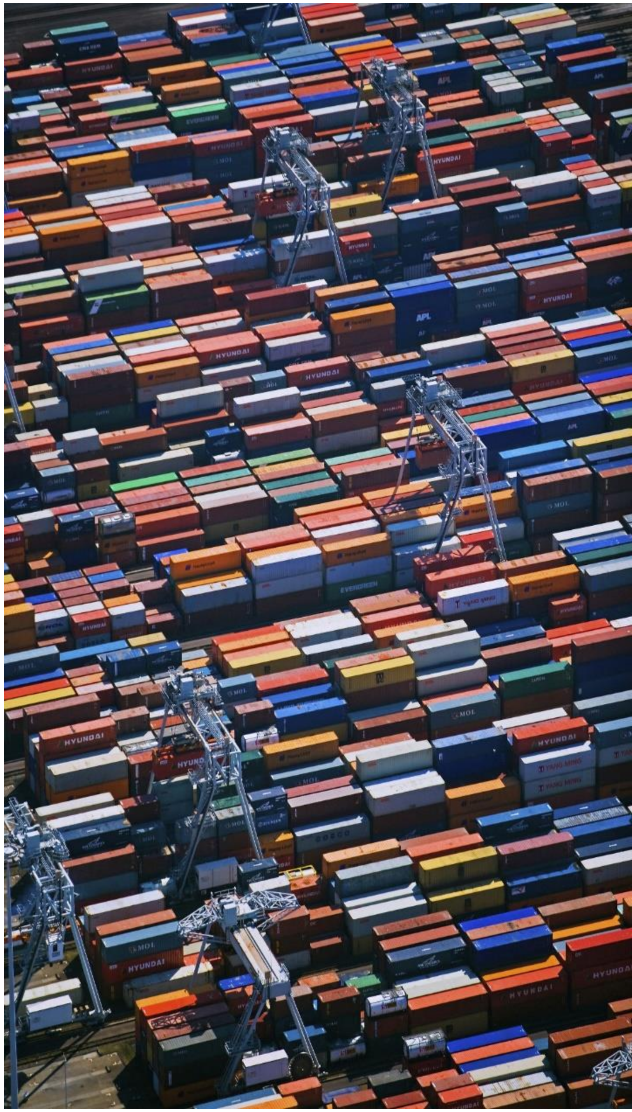
- Both internal TNMM and external TNMM are possible

- Broad level of product comparability and high level of functional comparability

- Applicable for most categories of transaction and often used to supplement analysis under other methods

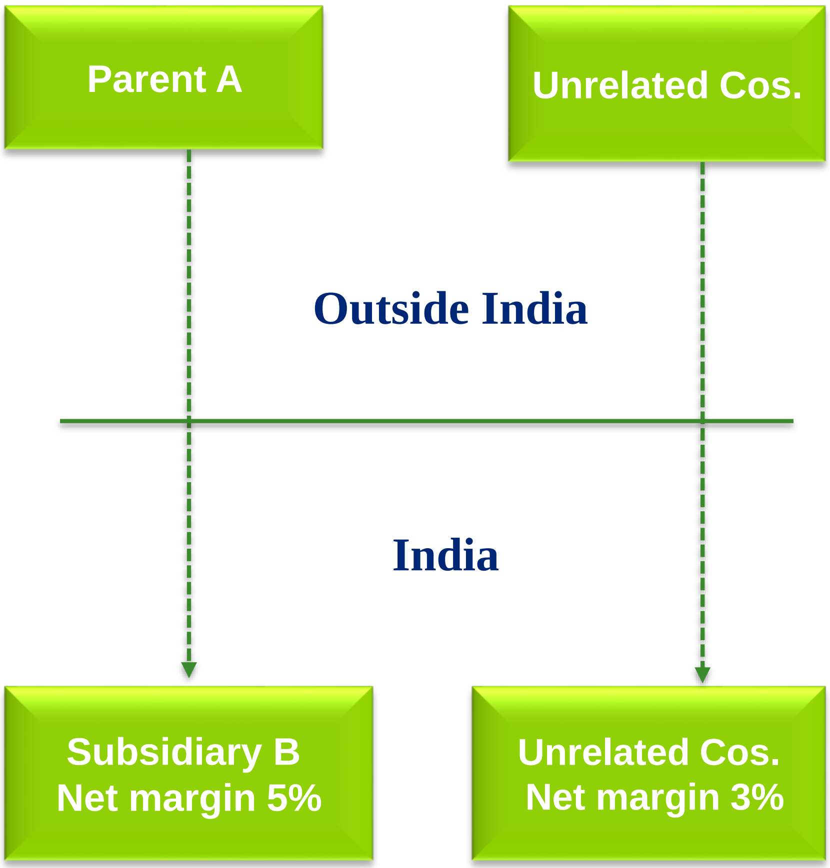
- Grouping of transaction - Relevant controlled transactions require to be aggregated to test whether the controlled transaction earn a reasonable margin as compared to uncontrolled transaction

- Usually regarded as an indirect and one-sided method, but is most widely adopted



Methods

Example of TNMM:



Methods

Other Method as per Rule 10AB:

- CBDT has notified the “Other method” vide a Notification
- Applicable from FY 2011-12:
- Rule 10AB - *“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-associated enterprises, under similar circumstances, considering all the relevant facts.*"
- Effectively this implies that “quotations” rather than “actual prices” charged or paid can also be used
- To maintain proper documentation specifying the rejection reasons for non-application of other five methods and appropriateness of the “other method”
- Other Method can be used for following transactions:
  - Valuation of shares
  - Reimbursements

Choice of Most Appropriate Method

Method	Transaction Type
CUP	Loans, Royalties, Service fee, transfer of tangibles
RPM	Marketing operations of finished products, where distributor not performing significant value addition to product
CPM	Raw material or semi-finished goods are sold, assembly, contract manufacturing
PSM	Transactions involving provision of integrated services by more than one enterprise or involving unique intangibles
TNMM	Provision of services, distribution of finished goods where applicability of RPM is inappropriate

The regulations do not define any priority of Methods

TP Documentation – Country by Country Reporting; Master File and Local File

CbC Reporting – India Perspective

- Requirement introduced with effect from AY 2017-18 (FY 2016-17)
- Apply to an international group *(i.e. group operating in two or more jurisdictions)* having consolidated revenue exceeding the prescribed threshold
- OECD mandated threshold is € 750 million equivalent to INR 5500 crores
- The threshold would be determined based on the consolidated revenues of the group in the immediately preceding year.

Example – CbC reporting for an international group having Indian parent, for the previous year 2017-18, shall apply only if the consolidated revenue of the international group in previous year 2016-17 exceeds INR 5500 Crores

- Exchange rate as on the last day of the previous year.
- Stringent penalty norms prescribed
- Every parent entity or an alternate reporting entity, resident in India, would need to furnish CbC report in Form No. 3CEAD
- Intimation under Form no. 3CEAC has to be filed by every constituent entity resident in India, of an international group, the parent entity of which is not resident in India

CbC Reporting – India Perspective

- For high-level TP risk assessment purposes, the CbC report may be useful
- Tax administrations may also use it to evaluate other BEPS related risks and for economic and statistical analysis
- The information in the CbC report is not be used as a substitute for a detailed TP analysis of individual transactions and prices based on a full functional analysis and a full comparability analysis
- The information in the CbC report on its own does not constitute conclusive evidence that transfer prices are not appropriate
- The information in the CbC report may be used as a basis for making further enquiries into the MNE's tax structure and allied matters
- However, it should not be used by tax authorities to propose TP adjustments based on a global formulary apportionment of income.

Master File – Applicability in India

- Each of the Indian Constituent Entities of International Group will be required to file the Master File in Form 3CEAA

- No threshold requirements are provided for Part A, thus, all Constituent Entities need to file it

- The CEs are also required to file Part B of Master File (Form 3CEAA) provided:

    - The consolidated revenue of IG exceeds INR 500 crores in the reporting accounting year; **and**

    - The aggregate value of international transactions exceeds INR 50 crores **or** international transactions related to intangibles exceed INR 10 crores in the reporting accounting year

- Applicable from FY 2016-17

Various forms and due dates – considering FY 2019-20

Requirement	Purpose of Form	Relevant Form	Due date for FY 2019-20
CbCR*	CbCR filing	Form 3CEAD	31 March 2021*
	Notification by Inbounds	Form 3CEAC	60 days prior to the due of filing CbCR**
	Filing for designation of Indian Constituent entity	Form 3CEAE	Not Specified
Master File	Master File filing	Form 3CEAA	30 November 2020
	Filing for designation of Indian Constituent entity	Form 3CEAB	30 days prior to the due of filing Master file i.e. 31 October 2020

**Due date under Section 286(4) [i.e. multinational group's having non-resident parent entities] has been prescribed as 12 months from end of the financial year.*

***Due date of the parent entity's jurisdiction to be considered.*

Transfer Pricing Documentation – Local

Rule 10D provides the list of mandatory documents to be maintained by an enterprise undertaking international transaction or a specified domestic transaction.

Entity related

- Ownership structure
- Profile of multinational group
- Business description / Profile of Industry

Price related

- 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
- Details of transfer pricing adjustment(s) made (if, any)

Transaction related

- Any other information e.g. data, documents like invoices, agreements, price related correspondence etc.

Transfer Pricing Documentation – Local

- Detailed documentation not required in case aggregate transaction value is less than INR 1 crore
- Contemporaneous data requirements
- Need to obtain Accountant's report (under Form 3CEB) to be filed along with the return of income
- Documents to be retained for a fixed period

Accountants’ Report – Section 92E

Accountants' Report – Section 92E / Rule 10E

- Obtained by every person entering into an international transaction and SDTs
- To be filed by the due date for filing return of income (e-filing mandatory)
- Opinion whether prescribed documents have been maintained the particulars in the report are "true and correct"
- Verification can involve:
  - Related party ledgers extracts
  - Related party Schedule under AS-18
  - Sample Invoices / Vouchers / Debit Notes / Credit Notes
  - Relevant intra-group agreements
  - Information on comparability

Practical issues in Form 3CEB verification and filing

- Reconcile transactions in Form No. 3CEB with audited accounts (related party disclosure, notes to accounts)
- Identify transactions with deemed associated enterprises
- Transaction not having effect on profits, income, losses and assets should it be reported by way of note or disclosed as an international transaction
- To identify unreported transactions *e.g. Guarantees given on behalf of subsidiaries, interest free loan, loan taken and repaid in the same year,* etc.
- Reimbursement of expenses – Kindy check whether any markup element is involved
- Interest on receivables – Kindly analyze the company's policy. Receivables outstanding beyond a stipulated period of time can be regarded as loan advanced to the AE
- Management Representation Letter and Appendices thereto
- DSC of client needs to be registered
- Business restructuring disclosure

Penalties

Penalties for non-compliance

Sr. No	Particulars	Default	Penalty
CbC report			
1.	Non-furnishing of CbC report by Indian parent or the alternate reporting entity resident in India	Each day up to a month from due date	INR 5,000 per day
		Beyond a month from due date	INR 15,000 per day for period exceeding a month
		Continuing default beyond service of penalty order	INR 50,000 per day from date of service of penalty order
2.	Non-submission of information	Beyond expiry of the period for furnishing information	INR 5,000 per day
		Continuing default beyond service of penalty order	INR 50,000 per day from date of service of penalty order

Penalties for non-compliance

Sr. No	Particulars	Default	Penalty
CbC report			
3.	Provision of inaccurate information in CbC report	Knowledge of inaccuracy at time of furnishing the report but fails to inform the prescribed authority	INR 500,000
		Inaccuracy discovered after filing and fails to inform and furnish correct report within fifteen days of such discovery	
		Furnishing of inaccurate information or document in response to notice issued	
Master File			
1.	Non-furnishing of information and documentation	Failure to furnish the information and document to the prescribed authority	INR 500,000

Key Take Aways

- What's transfer pricing?
- BEPS – 15 Action points
- Associated enterprise – Section 92A
- International transactions – Section 92B
- Most appropriate method
- Determine arm's length price
- Three tier documentation
- Accountants' report
- Penalties

Questions

Thank you

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