

Transfer Pricing Accountant's report –
Important aspects
- BKESC

Divyang Thakker

15 October 2023

Transfer Provisions as per the Income-tax Act, 1961

Chapter - X

Scheme of Sections – Chapter X

- ▶ Section 92 – Computation of Income from International transaction having regards to ALP
- ▶ Section 92A – Associated Enterprise definition
- ▶ Section 92B – International Transaction definition
- ▶ Section 92BA – Meaning of Specified Domestic Transaction
- ▶ Section 92C – Computation of ALP
- ▶ Section 92CA – Reference to TPO
- ▶ Section 92CB – CBDT's power to make SHRs

Scheme of Sections – Chapter X (Cont..)

- ▶ Section 92CC – Advance pricing agreement (APA)
- ▶ Section 92CD – Effect of APA
- ▶ Section 92CE – Secondary Adjustment
- ▶ Section 92D – Maintenance of information and documents
- ▶ Section 92E – Accountant's Report in case of taxpayer entering International transaction / specified domestic transaction
- ▶ Section 92F – Definitions of certain terms

Section 92 – Income computation under Transfer Pricing

▶ When ALP to be applied

- ▶ Income arising from an international transaction
- ▶ Allowance for expense / interest arising from an international transaction
- ▶ Mutual agreement / arrangement for allocation or apportionment of any cost / expense in International transaction for benefit, service or facility between AEs
- ▶ Specified Domestic Transactions

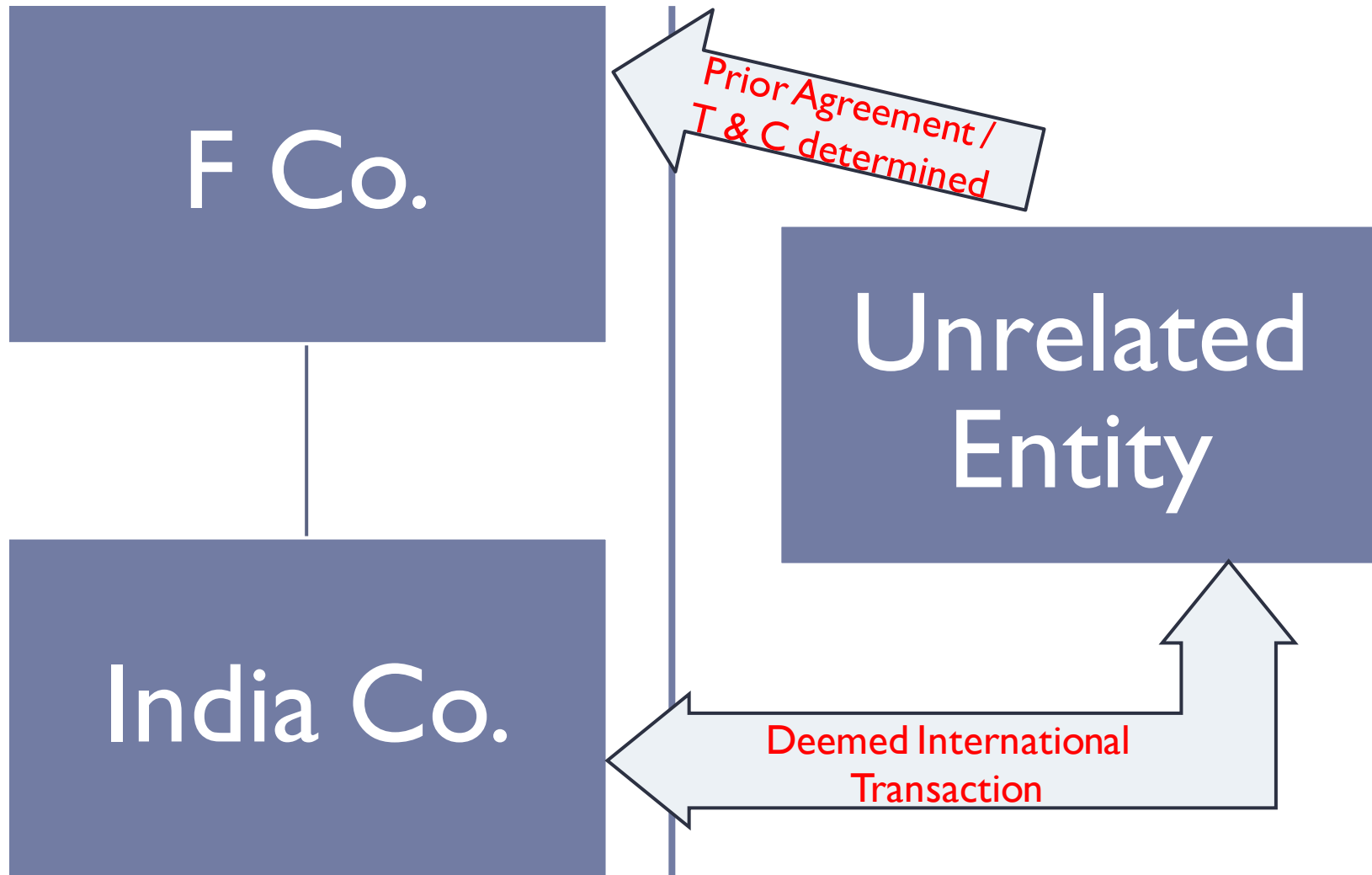
▶ When ALP not to be applied in International transaction

- ▶ Application of ALP has the effect of reducing the income chargeable to tax or increasing the loss

Section 92B – Meaning of International transaction

- ▶ “International transaction” means
 - ▶ 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, capital financing, guarantee, or
 - ▶ mutual agreement / arrangement for allocation / apportionment of any cost or expense for benefit, service or facility
 - ▶ Business restructuring / re-organization
 - ▶ any other transaction having a bearing on the profits, income, losses or assets of such enterprises, or

Section 92B(2) – Deemed International Transaction

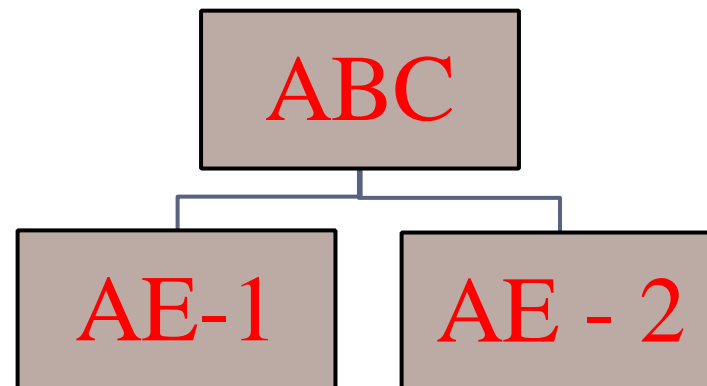
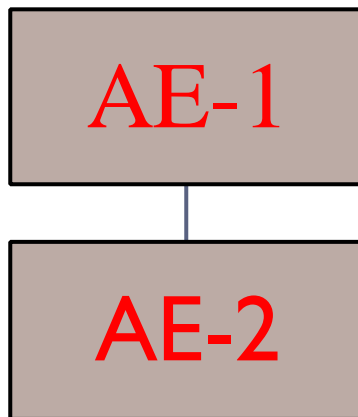


Section 92BA – Meaning of Specified Domestic transaction (SDT)

- ▶ SDT means any of the following transactions not being international transaction:
 - ▶ any transaction referred to in Section 80A;
 - ▶ any transfer of goods or services referred to in Section 80-IA(8);
 - ▶ any business transacted between the assessee and other person as referred to in section 80-IA(10);
 - ▶ any transaction, referred to in any other section under Chapter VI-A or Section 10AA, Section 80-IA(8) or 80-IA(10) of Section 80-IA;
 - ▶ any business transacted between the persons referred to in Section 115BAB(6);
 - ▶ any business transacted between the assessee and other person as referred to in Section 115BAE(4);
 - ▶ any other transaction as may be prescribed,and where the aggregate of such transactions entered into by the assessee in the previous year **exceeds** a sum of **Rs.20 crore**

Section 92A – Associated Enterprises

- ▶ “Associated enterprise” means an enterprise
 - ▶ which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or
 - ▶ one or more persons who participate, in management or control or capital of one enterprise are the same persons who participate, in the management or control or capital of the other enterprise.



Section 92A(2) – Deemed AE

- ▶ one enterprise holds, directly or indirectly, shares carrying not less than **26% of the voting power** in the other enterprise;
- ▶ any person or enterprise holds, directly or indirectly, shares carrying not less than **26% of the voting power** in each of such enterprises;
- ▶ a loan advanced by one enterprise to the other enterprise constitutes **not less than 51% of the book value of the total assets** of the other enterprise;
- ▶ one enterprise guarantees **not less than 10% of the total borrowings** of the other enterprise;
- ▶ **more than half** of the board of directors or members of the governing board, or one or more executive directors or executive members of one enterprise, are appointed by the other enterprise;

Section 92A(2) – Deemed AE (Cont..)

- ▶ **more than half** of the directors or members of the governing board, or one or more of the executive directors or members of the governing board, of each of the two enterprises are appointed by the same person or persons;
- ▶ manufacture or processing of goods or articles or business carried out by one enterprise is **wholly dependent** on the use of intangibles or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights;
- ▶ **90% or more of the raw materials and consumables** required for the manufacture or processing of goods or articles carried out by one enterprise, are supplied by the other enterprise, or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by such other enterprise;

Section 92A(2) – Deemed AE (Cont..)

- ▶ the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise;
- ▶ where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual;
- ▶ where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family or by a relative of a member of such Hindu undivided family or jointly by such member and his relative;
- ▶ where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds **not less than 10% interest** in such firm, association of persons or body of individuals;
- ▶ there exists between the two enterprises, any relationship of mutual interest, as may be prescribed.

Section 92C – Computation of ALP

▶ **Methods**

- ▶ Comparable uncontrolled price (CUP) method;
- ▶ Resale price method (RPM);
- ▶ Cost plus method (CPM);
- ▶ Profit split method (PSM);
- ▶ Transactional net margin method (TNMM);
- ▶ Such other method as may be prescribed by the Board.

▶ **ALP shall be determined by the MAM**

▶ **Rules explaining the methods**

- ▶ Rule 10B – Detailed explanation of each method
- ▶ Rule 10C – Selection of MAM
- ▶ Rule 10CA – Special cases on determination of ALP

Tolerance limit for ALP adjustment

- ▶ When more than one price is determined by MAM, the ALP shall be determined by arithmetic mean with acceptable variation not exceeding 3% (Tolerance limit)
- ▶ For AY 2023-24, tolerance limit is 1% of the wholesale trading and 3% in all other cases [CBDT Notification 46/2023 dated 26-06-2023]
- ▶ Tolerance limit to be computed with respect to the transaction price
- ▶ For Sale Transaction of Rs.10,000 and ALP of Rs.10,300. variation is 3% ($300/10,000$) w.r.t. transaction price & 2.91% ($300/10,300$) w.r.t. ALP

Definition – Wholesale Trading

- ▶ Wholesale trading means an international transaction or specified domestic transaction of trading in goods, which fulfils the following conditions, namely:-
 - ▶ purchase cost of finished goods is **80% or more** of the total cost pertaining to such trading activities; and
 - ▶ average monthly closing inventory of such goods is **10% or less** of sales pertaining to such trading activities.

Range Concept in ALP determination [Rule 10CA]

- ▶ The 'range concept' shall be applicable when:
 - ▶ The MAM is either CUP Method, RPM, CPM, or TNMM; and
 - ▶ there are at least 6 entries in the comparable dataset.
- ▶ Where these conditions are not fulfilled, 'arithmetic mean' shall continue to apply along-with the tolerance range benefit
- ▶ For determination of the range,
 - ▶ the margins in the set of comparable companies are required to be arranged in ascending order; and
 - ▶ the arm's length range would be data points lying between the 35th and 65th percentile of the set.
- ▶ **If the transaction price**
 - ▶ falls within the range, it shall be deemed to be the ALP.
 - ▶ falls outside the range, the **ALP shall be taken to be the Median** of the data set.

Illustration - Range Concept – Percentiles in decimal

- ▶ International transaction of sale of goods at USD 100
- ▶ Comparable transactions at – USD 120, USD 78, USD 110, USD 90, USD 86, USD 139, USD 102
- ▶ Arrange in ascending order
 - ▶ USD 78, USD 86, USD 90, USD 102, USD 110, USD 120, USD 139
- ▶ 7 items in data set of CUP method (conditions satisfied)

Percentile	Formula	Result	Value to be Selected
35 th	$7 \times 35\%$	2.45	3 rd Value
65 th	$7 \times 65\%$	4.55	5 th Value
Median	$7 \times 50\%$	3.50	4 th Value

- ▶ 3rd value USD 90 & 5th value USD 110
- ▶ Transaction price USD 100 falls within range and hence is at ALP

Illustration - Range Concept – Percentiles whole number

- ▶ Comparable price arranged in ascending order

Value	Price (Rs.)	Value	Price (Rs.)	Value	Price (Rs.)	Value	Price (Rs.)
1	530	6	558	11	588	16	618
2	538	7	560	12	596	17	620
3	545	8	572	13	601	18	627
4	545	9	576	14	607	19	632
5	549	10	584	15	614	20	638

- ▶ 20 items in data set of CUP method (conditions satisfied)

Percentile	Formula	Result	Value to be Selected	Price (Rs.)
35 th	20 x 35%	7	Mean of 7 th & 8 th Value	$(560+572)/2 = 566$
65 th	20 x 65%	13	Mean of 13 th & 14 th Value	$(601+607)/2 = 604$
Median	20 x 50%	10	Mean of 10 th & 11 th Value	$(584+588)/2 = 586$

Multiple Year data [Rule 10B(5)]

- ▶ For each comparable, the data of the current year is required to be considered
- ▶ In case such data is not available, data pertaining to up to two preceding financial years may be used.
- ▶ Multiple year data (of the comparable companies) is applicable only in cases where RPM, CPM or TNMM has been selected as MAM
- ▶ When using multiple year data, each comparable shall be the weighted average of the selected years.

Particulars	Year (-2)	Year (-1)	Year 0	Total	Comparable
Operating Profit (OP)	250	300	350	900	OP/TC = 900/5400 = 16.67%
Total Cost (TC)	1,700	1,800	1,900	5,400	
	14.71%	16.67%	18.42%		

Section 92CB – Safe Harbour Rules (SHR)

- ▶ ALP determination shall be subject to SHRs
- ▶ CBDT has been granted power to make and notify SHRs
- ▶ SHRs are binding on the income-tax authorities
- ▶ Rules 10TA to 10TG & Form 3CEFA – International Transactions
- ▶ Rules 10TH to 10THD & Form 3CEFB – Domestic Transactions
- ▶ SHRs applicable to eligible assessee carrying on specified business / transactions.

Section 92CC – Advance Pricing Agreement (APA)

- ▶ APAs presents a proactive measure for resolving transfer pricing disputes in a co-operative manner
- ▶ Power has been granted to CBDT to enter an APA with any person, determining the ALP or specifying the manner in which the ALP is to be determined for an international transaction to be entered into by that person
- ▶ APA can be signed after approval of the Central Government
- ▶ Once APA is signed, the ALP is determined in accordance with the APA
 - ▶ Binding on the assessee as well as the tax department
- ▶ APA shall be valid for period mentioned in it not exceeding 5 consecutive years

APA (Cont..)

- ▶ **APA can be unilateral, Bilateral or Multilateral**
 - ▶ Unilateral – Between the assessee and CBDT
 - ▶ Bilateral – Between the assessee, CBDT, AE and AE's tax administration
 - ▶ Multilateral – Between assessee, CBDT, more than one AEs and their respective tax administrations
- ▶ **APA would be applicable for existing as well as new transactions**
 - ▶ Existing transactions – make application before beginning of the year
 - ▶ New transactions – make application before starting the transaction

Section 92CC – APA Procedure

- ▶ APA scheme is covered under Rules 10F to 10T and Rule 44GA of the Income-tax Rules, 1962
- ▶ APA requires:
 - ▶ Submission of Application for a pre-filing meeting (Optional) [Form 3CEC]
 - ▶ Having a pre-filing meeting
 - ▶ Filing application for APA [Form 3CED]
 - ▶ Various hearings
 - ▶ Agreeing and signing the APA
- ▶ Once APA is signed, the assessee has to file Annual Compliance Report [Form 3CEF]
- ▶ APA can be rolled back for prior years as applied by the assessee (Maximum up to 4 years)
[Circular No. 10/2015, dated 10-6-2015]

Roll-back provisions in APA

- ▶ Roll-back is available for four previous years, preceding the first previous year covered in the APA
- ▶ Application requesting for roll back should be made in Form 3CEDA for the relevant roll back years
- ▶ International transactions covered under roll-back should be same as covered in the APA
- ▶ ROI for roll-back year ought to be furnished on or before the due date for filing return
- ▶ The manner of determining ALP in the roll back years for particular international transaction will be same as agreed in the regular APA
- ▶ Roll-back provisions shall not be provided for an international transaction if
 - ▶ the ITAT has passed an order disposing an appeal for determination of ALP of the international transaction, at any time before signing of the APA agreement; or application of roll back has the effect of reducing
 - ▶ total income or increasing the total loss.

Section 92CE – Secondary Adjustment

- ▶ Where a primary adjustment to transfer price for an amount **exceeding Rs.1 crore**
 - ▶ has been made suo-moto by the assessee in ROI
 - ▶ made by AO has been accepted by the assessee
 - ▶ is determined by APA entered into by the assessee under section 92CC
 - ▶ is made as per the SHR framed under section 92CB; or
 - ▶ is arising as a result of resolution of an assessment by way of the MAP

the assessee shall make a secondary adjustment

Section 92CE – Secondary Adjustment (Cont..)

- ▶ **Secondary adjustment computation**
 - ▶ There has been Primary adjustment to the transfer price
 - ▶ resulting in increase in the total income or reduction in the loss
 - ▶ Excess money not repatriated to India within **90 days**
 - ▶ shall be deemed to be advance made by the assessee to such AE
 - ▶ Interest on such advance to be computed at **SBI lending rate + 3.25% (transaction in INR)** or 6 month's LIBOR + **3% (transaction in foreign currency)**
- ▶ Excess money may be repatriated from any AE which is not a resident in India (may not be from same AE)
- ▶ When excess money not repatriated, assessee may pay **additional tax at 18%** of such excess money and stop year after year adjustment

Section 92D – Maintenance of information and documents

- ▶ Every person who has entered into an international transaction or SDT shall keep and maintain prescribed information and document
- ▶ Information / documents are prescribed by Rule 10D
- ▶ Such information / documentation has to be contemporaneous (exist 1 month prior to due date of filing of ROI)
- ▶ Such information to be basis of preparation of Transfer Pricing study report
- ▶ Such information / documents to be submitted to AO or CIT(A) as and when asked for (within 10 days from receipt of notice)

Three tier documentation structure

- ▶ All MNEs are required to maintain documentation containing Master File, Local File and Country-by-Country Report (CbC Report)
- ▶ Master File seeks to capture information regarding the taxpayer's global operations and their TP policies.
- ▶ Local File captures entity-specific information with reference to the related party transactions.
- ▶ CbC Report would capture key metrics of all entities in the group such as revenue, taxes paid, capital employed, headcount, etc.
 - ▶ Applicable to MNEs with annual consolidated group turnover exceeding € 750 million in preceding year

Section 92E – Accountant’s Report

- ▶ Every person who has entered into an international transaction or SDT during a previous year shall obtain a report in Form 3CEB from a Practicing Chartered Accountant
- ▶ Such report to be furnish on or before the specified date (1 month prior to due date of filing of ROI)
- ▶ The report to provide details of all international transactions and SDT and also specify if they are at ALP along-with the method adopted for determining the ALP
- ▶ ICAI has issued Guidance note on issue of Transfer Pricing Accountant’s report (Revised 2022)

Summary of Guidance Note on issue of TP Accountant's report

Institute of Chartered Accountants of India (2022)

Objective of Guidance Note

- ▶ Provide guidance to CAs in discharging their responsibilities under section 92E of the Act.
- ▶ Assist in understanding the respective responsibilities of the taxpayer and the CA;
- ▶ Guide the CA as to the nature and scope of information to be obtained from the taxpayer to enable him to conduct the examination;
- ▶ Provide guidance on the verification procedures to be adopted by the CA for giving the report and the prescribed particulars in the annexure thereto; and
- ▶ Explain the circumstances where a disclosure or qualification or disclaimer may be required from the CA while giving the report

Due diligence by CA issuing the report

- ▶ **Verify applicability of provisions of Section 92**
 - ▶ Scrutinize for all international transactions [Refer additional transactions / arrangements included by Finance Act, 2012 with retrospective effect from 1-4-2002]
 - ▶ Check for SDT [Section 92BA]
 - ▶ Check for deemed international transaction [Section 92B(2)]
 - ▶ Ensure that application of TP provisions does not result in reduction of income or increase of losses
- ▶ **Methods for ALP determination**
 - ▶ Ensure using of MAM based on nature of transactions
 - ▶ CUP is most recommended. Only when CUP not possible, look at other methods

Due diligence by CA issuing the report (Cont..)

▶ Factors to be considered for determining MAM

- ▶ nature and class of international transactions or SDTs;
- ▶ class or classes of AEs entering into the transaction and the functions performed by them taking into account the assets employed and risks assumed;
- ▶ availability, coverage and reliability of data necessary for application of the method.
- ▶ the degree of comparability existing between the international transaction or SDT and uncontrolled transaction
- ▶ the extent to which reliable and accurate adjustments can be made to account for the difference between the transactions.
- ▶ the nature, the extent and reliability of assumptions required to be made in application of a method.

Due diligence by CA issuing the report (Cont..)

- ▶ Verify if the entities fall within the definition of AE or deemed AE
- ▶ Initially apply source definition [Section 92A(1)] and then Deemed AE definition [Section 92A(2)]
- ▶ Check transactions between Head Office and PE (branch office or other fixed place of business)
 - ▶ Foreign Company & Indian branch covered
 - ▶ Indian Company & Foreign PE not covered for India TP
 - ▶ India company PE & Foreign subsidiary covered

Due diligence by CA issuing the report (Cont..)

- ▶ **Business Restructuring – to be included as International Transactions**
 - ▶ Transfer of IP rights / intangibles within the group
 - ▶ Termination or substantial renegotiation of existing arrangements (Exit Charge)
 - ▶ Conversion of full-fledged manufacturers into contractors or toll manufacturer
- ▶ **FOC transfer of goods / services**
- ▶ **Service transactions (including providing finance)**
 - ▶ Benefits test
 - ▶ Shareholder's activities – does not justify any charge
 - ▶ Capital financing – Advances received
 - ▶ Outstanding receivables beyond reasonable credit period
 - ▶ Cost contribution arrangements

Due diligence by CA issuing the report (Cont..)

- ▶ Extract the comparable companies data and apply appropriate filters to obtain relevant comparable.
 - ▶ Powess, Capitalline, TPGenie, OneSource, etc.
- ▶ Wherever applicable, check if arithmetic mean and tolerance limit is applied on comparable entities data
- ▶ When range concept is applied, check the percentile value calculation
- ▶ Check if there is any Primary adjustment in earlier years resulting in Secondary adjustment in current year

Due diligence by CA issuing the report (Cont..)

- ▶ Undertake in-depth FAR analysis
- ▶ Decide on the Tested Party – Entity whose profitability needs to be checked
- ▶ Contractual terms important – terms or delivery, payment, Volume, Incoterms, warranty, Market conditions, Geographical differences, etc.
- ▶ Analyze OECD Transfer Pricing Guidelines, wherever required
- ▶ Keeping and maintaining required information and documents – Primary responsibility of taxpayer
- ▶ Obtain a representation from the management with the list of all AEs and deemed AEs
- ▶ Management's representation that all International transactions and SDTs are duly recorded

Due diligence by CA issuing the report (Cont..)

▶ **SHRs**

- ▶ Check if taxpayer has applied for SHRs [Form 3CEFA / 3CEFB]
- ▶ If yes, in the application check the number of years that the SHRs are applicable

▶ **APA**

- ▶ Check if APA is unilateral, bilateral, multilateral
- ▶ Ensure that taxpayer seeking APA has filed application before commencement of the year for which it seeks to apply
- ▶ Check if Roll back provisions are included in the APA
- ▶ Ensure that the taxpayer has furnished Annual Compliance Report (ACR) for each year covered in the APA

Questions ?

Questions ?

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Glossary of terms

Abbreviations	Term
AE	Associated Enterprise
ALP	Arm's Length Price
AO	Assessing Officer
APA	Advanced Pricing Agreement
CA	Chartered Accountant
CbC	Country-by-Country
CBDT	Central Board of Direct Taxes
CPM	Cost Plus Method
CUP	Comparable Uncontrolled Price
FAR	Functions Assets Risks
FOC	Free of Cost
INR	Indian Rupees
LIBOR	London Interbank Offer Rate
MAM	Most Appropriate Method
MAP	Mutual Agreement Procedures

Abbreviations	Term
MNE	Multinational Enterprise
OECD	Organization for Economic Co-operation and Development
OP/TC	Operating Profit/Total Cost
PE	Permanent Establishment
PSM	Profit Split Method
ROI	Return of Income
RPM	Resale Price Method
SBI	State Bank of India
SDT	Specified Domestic Transaction
SHR	Safe Harbour Rules
TNMM	Transactional Net Margin Method
TP	Transfer Pricing
TPO	Transfer Pricing Officer
USD	United States Dollar
w.r.t.	With respect to

Divyang Thakker

tdivyang@gmail.com

<https://www.linkedin.com/in/divyang-thakker-27716620/>

+91 99 30 126622 / +91 90 22 646622

Thank You