



Transfer Pricing in India

Basic principles, major issues of dispute, and
role of High Court

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Outline

- Basics of transfer pricing
- Background of TP legislation in India
- TP regulations as per the Income-tax Act, 1961
- Domestic TP law and Treaty interplay
- Thin Capitalization
- AMP Expenses
- Other issues

Basics of transfer pricing

What is transfer pricing?

- Transfer pricing, for tax purposes, is the pricing of inter-company transactions that take place between affiliated businesses.
- The transfer pricing process determines the amount of income that each party earns from that transaction.
 - An exercise largely carried out for Tax Minimization across the group
 - As long as group is controlling the funds, it does not matter where they are parked
- Taxpayers and the taxing authorities focus exclusively on related-party transactions, which are called *controlled transactions*, and have no direct impact on independent party transactions, which are termed as *uncontrolled transactions*.

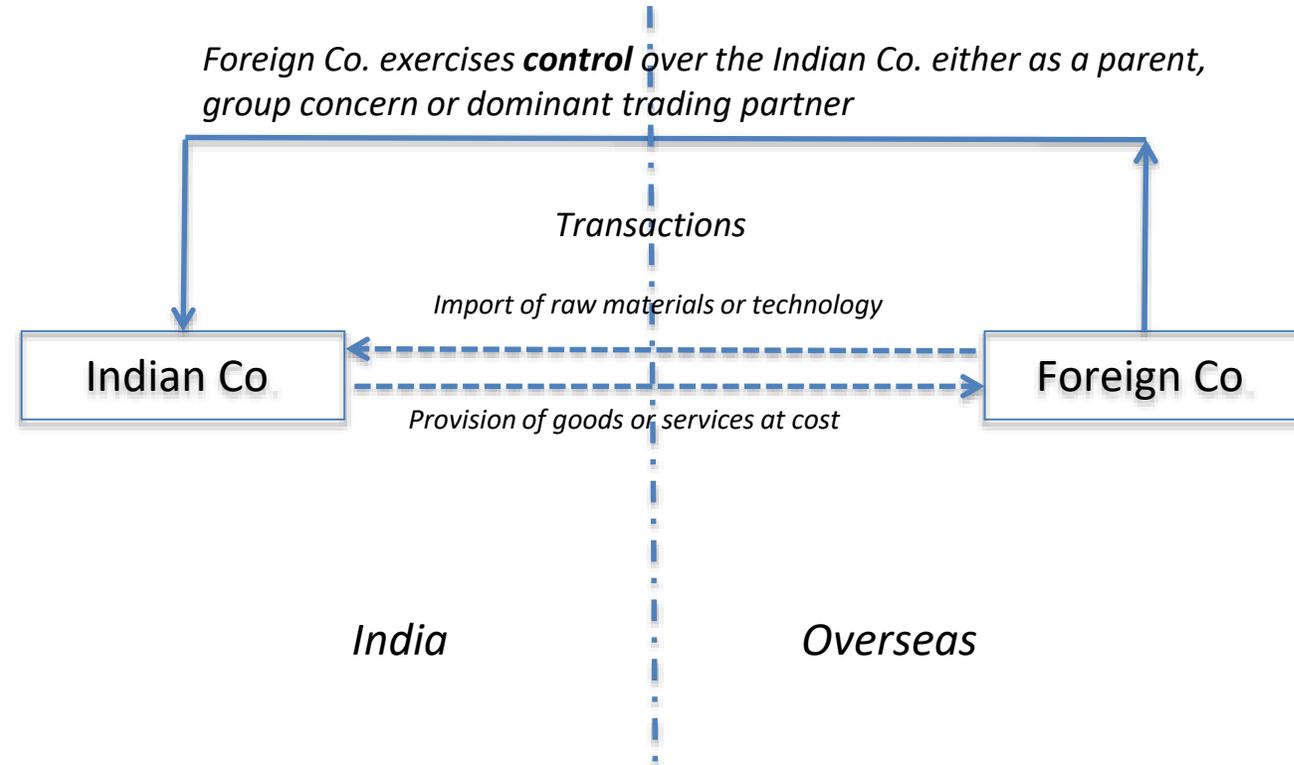
What is transfer pricing ... *contd.*

- The OECD defines “Transfer Pricing” as the pricing at which an Enterprise transfers physical goods and intangible goods and provides services to Associated Enterprises.
- Since the Transfer Price within the Group may not necessarily be driven by market forces and the Group’s Interest may precede over market consideration, it is possible that the Transfer Pricing may differ from the prices that would have ordinarily fetched in similar transaction from an independent Enterprise under similar circumstance.
- Transactions between Associated Enterprises (AEs) is referred to as “Controlled” transactions as distinct from “uncontrolled” transactions between companies that are not associated and can be assumed to operate independently on Arms Length Basis in arriving at the prices of such transactions.

Rationale

- The concept of an international corporate headquarters of a multinational corporation that uses transfer pricing to minimize worldwide taxation is no longer viable.
- The tax authorities are intent on their own revenue maximization by thwarting the taxpayer's tax minimization plans.
- In a globalized economy there has been an emergence of Multi National Enterprises, wherein the parent company may be in one country while its various subsidiaries and Branches/Associated Enterprises will be spread over in different countries.
- This has led to increasing volume of transactions within an MNE Group, which are also called Intra Group Transactions. Since, these Intra Group Transactions are not purely governed by market forces but are driven by the Group Companies' common interests, the pricing of such Intra Group Transactions often becomes a subject of controversy.
- MNE/MNCs try to distribute their profits amongst the various Companies within the Group located in different Countries.

Scenarios: Cross-border transactions



Scenario 1

*Indian Co. is treated as **Permanent Establishment** of the Foreign Co., profits attributable to it are taxed*

Scenario 2

Independent streams of receipts by Foreign Co. are made subject to withholding tax requirements

Scenario 3

Transactions between Indian Co. and Foreign Co. are subject to transfer pricing

Scenarios: Analysis

- Scenario 1
 - **Indian Co. is treated as Permanent Establishment of the Foreign Co.**
 - Permanent Establishment as a concept is contained in the relevant DTAA;
 - Certain objective criterion have to be demonstrated before an entity can be taxed as a PE of a Foreign Co.;
 - Case Study - Assistant Director of Income-tax-1, New Delhi v. E-Funds IT Solution Inc. [2017] 399 ITR 34 (SC)
- Scenario 2
 - **Independent streams of receipts by Foreign Co. are made subject to withholding tax requirements**
 - Individual stream of receipts would have to be categorised under a head subject to TDS under either the Income Tax Act, 1961 or the DTAA. Royalty and FTS are major dispute areas;
 - Offshore supply of goods is not taxable [Ishikawajma-Harima] and hence not subject to withholding;
 - Case Study - Centrica India Offshore (P.) Ltd. v. Commissioner of Income-tax [2014] 364 ITR 336 (Delhi)

Scenarios: Analysis ... contd.

- Scenario 3
 - **Transactions between Indian Co. and Foreign Co. are subject to transfer pricing**
 - Indian Co. is required to satisfy the Revenue that the transactions with the Foreign Co. were undertaken on prices which were at Arm's Length;
 - Contemporaneous documentation is maintained for data from other comparable entities and a prescribed method is applied by the Indian Co. to demonstrate that the price of the transactions undertaken was at Arm's Length;

Morgan Stanley (SC)

- DIT (International Taxation) v. Morgan Stanley & Co. Inc., (2007) 7 SCC 1 at page 28
 - “The impugned ruling is correct in principle insofar as an associated enterprise, that also constitutes a PE, has been remunerated on an arm's length basis taking into account all the risk-taking functions of the enterprise. In such cases nothing further would be left to be attributed to PE. The situation would be different if transfer pricing analysis does not adequately reflect the functions performed and the risks assumed by the enterprise. In such a situation, there would be a need to attribute profits to PE for those functions/risks that have not been considered. Therefore, in each case the data placed by the taxpayer has to be examined as to whether the transfer pricing analysis placed by the taxpayer is exhaustive of attribution of profits and that would depend on the functional and factual analysis to be undertaken in each case. Lastly, it may be added that taxing corporates on the basis of the concept of economic nexus is an important feature of attributable profits (profits attributable to PE).”

Glossary of TP terms

- AMP - Advertising, Marketing and Promotion
- ALP- Arms' Length Price
- APA- Advance Pricing Agreement
- BEPS- Base Erosion and Profit Shifting
- CPM - Cost Plus Method
- CUP- Comparable Uncontrolled Price
- CUT- Comparable Uncontrolled Transaction
- DRP- Dispute Resolution Panel
- DTAA- Double Taxation Avoidance Agreement
- FAR- Function, Assets and Risks
- MAM- Most Appropriate Method
- MAP- Mutual Agreement Procedure
- MNE - Multinational Enterprise
- OECD- Organisation for Economic Co-operation and Development
- PE- Permanent Establishment
- PLI- Profit Level Indicator
- PSM- Profit Split Method
- RPM- Resale Price Method
- TNMM -Transactional Net Margin Method
- TP - Transfer Pricing
- TPO- Transfer Pricing Officer

Concepts in transfer pricing

- The effort of all tax authorities is to determine the correct value of taxable income which becomes difficult when the tax payer is involved in Intra Group Transactions.
- Article 9 of the OECD Model Convention provides for the concept of the Arm's Length Principle wherein the profits of Enterprises of MNE is based on transactions between the independent Enterprise under similar conditions and circumstances.
- Arm's Length Principle seeks to ensure that the variations in the transfer price between members of an MNE (the Controlled Transactions), which may be based on special relationship between the enterprises, are either eliminated or reduced to large extent.

Background of TP in India

Background of TP in India

- 1991 – Liberalization, privatization, and globalization:
 - Indian started attracting interests of Multinational Enterprises (MNEs)
 - Similarly, several Indian companies also steadily emerged as global players by either making offshore acquisitions or by setting up overseas subsidiaries
- Standing Committee in March 1991 – the existing provisions of the Act were inadequate to deal with tax minimisation through transfer pricing
- Expert Group of CBDT – recommended complete overhaul of section 92 of the Act. Section 92, as it then stood, read:

Income from transactions with non-residents, how computed in certain cases.

292. Where a business is carried on between a resident and a non-resident and it appears to the Assessing Officer that, owing to the close connection between them, the course of business is so arranged that the business transacted between them produces to the resident either no profits or less than the ordinary profits which might be expected to arise in that business, the Assessing Officer shall determine the amount of profits which may reasonably be deemed to have been derived therefrom and include such amount in the total income of the resident.

Background of TP in India ... *contd.*

Other provisions in the Income-tax Act

- Rule of Commercial Expediency' – not open to Revenue to contest the commercial need for a transaction – judicial doctrine usually applied in disallowances made under **Section 37**
- Nonetheless, certain statutory provisions regulate the amount of payments, Example:
 - Disallowance under **Section 40A** for payments made an assessee to a category of closely connected persons, which are deemed to be excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of the assessee or the benefit derived by or accruing to him therefrom;
 - Re-Computation of consideration under **Section 80-IA** for transfer of goods and services between the eligible undertaking and an ineligible unit, if the consideration, for such transfer as recorded in the accounts of the eligible business does not correspond to the market value of such goods or services as on the date of the transfer;
 - Similar provision in **Section 10A** for transactions between eligible and ineligible units;

Background of TP in India ... *contd.*

- The Finance Act, 2001 introduced transfer pricing regulations in India by substituting existing Section 92 of the Act and introducing new sections 92A to 92F w.e.f. 01.04.2002 (AY 2002-03)
- Finance Minister's speech at the time of introducing TP regulations:
 - “The presence of multinational enterprises in India and their ability to allocate profits in different jurisdictions by controlling prices in intra-group transactions has made the issue of transfer pricing a matter of serious concern. I had set up an Expert Group in November 1999 to examine the issues relating to transfer pricing. Their report has been received, proposing a detailed structure for transfer pricing legislation. Necessary legislative changes are being made in the Finance Bill based on these recommendations.”
(Mr. Yashwant Sinha, Finance Minister, February 28, 2001)

Domestic Transfer Pricing

- CIT v Glaxo SmithKline Asia (P) Ltd. (2010) 236 CTR 113 (SC):
 - “... in order to reduce litigation occurring in complicated matters, the question of extending Transfer Pricing regulations to domestic transactions require expeditious consideration by the Ministry of Finance and the CBDT may also consider issuing appropriate instructions in that regard”.
- Finance Act, 2012 – introduced domestic transfer pricing for ‘specified domestic transactions’ from AY 2013-14

TP regulations as per the Income-tax Act

Section 92 – Income to be computed having regard to ALP

- Section 92(1) provides that any income arising from an international transaction shall be computed having regard to the arm's length price.
 - 'having regard to' – refers to the scheme laid down in the subsequent sections e.g. section 92 provides for the computation of the arm's length price, while section 92CA provides for adjustments to income on the basis of ALP determined
- Section 92(2) covers cost contribution arrangements
- Section 92(3) provides that the application of the transfer pricing provisions should not result in reducing the income computed on the basis of books of account
 - Effectively, it means that the TP adjustment should not result in reducing the returned income
 - “Corresponding adjustments” – not possible because of section 92(3) read with section 92C(4) (both provisos) ?
- Explanation provides that it applies to any expense and Interest arising from an IT – needed because expenses may not be income

Section 92 ... contd.

Key issues

- Issue of shares at a premium by assessee to its non-resident holding company does not give rise to any income from an admitted international transaction and, thus, there is no occasion to apply Chapter X in such a case
 - Vodafone India Services (P.) Ltd. v. Union of India [2014] 50 taxmann.com 300/[2015] 228 Taxman 25 (Bom.)
 - Shell India Markets (P.) Ltd. v. Asstt. CIT [2014] 51 taxmann.com 519 (Bom.)
- Income not defined in the TP regulations. ALP and International Transaction are defined. Debate is whether income is as per section 2(24). That being an inclusive definition should context govern its scope. Is income only commercial profits? Should IT control income or vice versa? Does sec rule out capital transactions?

Section 92A – Associated Enterprise

- Two or more enterprises are associated enterprises if:
 - One of them participates in the management, control, or capital of another, or
 - There is common management, control, or capital exercised by some persons
- Section 92A(2) provides an illustrative list of situations for AEs, e.g.:
 - Shares carrying 26% or more voting power in one enterprise are held by another
 - Loan given by one enterprise to another which constitutes not less than 51% of the book value of the total assets of the other enterprise
 - One of them guarantees not less than 10% of the borrowings of another

Section 92A – Associated Enterprise ... *contd.*

- Interplay between sub-sections (1) and (2)
 - Prior to amendment in 2002, sub-section (2) opened as: “Two enterprises shall be deemed to be associated enterprises if, at any time during the previous year, ...”
 - Now – “For the purposes of sub-section (1)” has been inserted
 - Does that make the participation in management, control, and capital as provided for in sub-section (1) mandatory?
- Tested Party – The OECD TP Guidelines defines 'tested party' as "the one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparable can be found.

Section 92B – International transaction

- International transaction is a transaction:
 - Between two or more AEs
 - Either or both of whom are non-residents
 - In the nature of purchase, sale or lease of property or provision of services
 - Or lending or borrowing money
 - Or any other transaction having bearing on profits, income, losses, or assets
 - Includes cost contribution arrangements
- Sub-section (2) provides that if a transaction is entered into between an AE and a third person, where there is a prior agreement between such person and the AE, it shall be deemed to be an international transaction
- Explanation provides for an inclusive definition of ‘international transaction’, and ‘intangible property’
 - Transactions in capital assets, intangibles, lending and borrowing, corporate guarantee, capital financing and business restructuring are now specifically included as international transactions.

International transaction – issues

- Deferred receivables:
 - **CIT v. Kusum Healthcare Pvt Ltd.** 2017 398 ITR 66 has held that an adjustment made by TPO on account of outstanding receivables cannot be an International Transactions.
 - **Mckinsey Knowledge Centre India Pvt. Ltd. v. PCIT** 2018 407 ITR 450 (Delhi) has applied the retrospective amendment introduced to Explanation to Section 92B holding that any delay in a realization of trade debt arising from the sale of goods or services rendered in the course of carrying on the business is a liability to be visited with Transfer Pricing adjustment on account of interest income short-charged or uncharged.
- Where the Revenue has been unable to demonstrate some tangible material that there is an international transaction involving AMP expenses between Indian subsidiary and foreign parent, the Revenue cannot proceed to determine ALP of AMP expenses by inferring the existence of an international transaction based on the bright line test
 - **CIT v. Whirlpool of India Ltd.** [2015] 64 taxmann.com 324 (Delhi)

Arm's Length Price (ALP)

- ALP is found in paragraph 1 of article 9 of the OECD MC which reads as under:
 - “Where conditions are made or imposed between the two associated 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 accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.”
- The principle laid out above in the UN Model has also been reiterated in the OECD Model Tax Convention and the OECD Guidelines as supplemented and amended. Source: UN Transfer Pricing Manual 2017

Arm's Length Price (ALP) ... *contd.*

- Sec. 92F(ii) "arm's length price" means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions;
- The term 'transaction' includes an arrangement, understanding or action in concert, whether or not in writing and whether or not intended to be enforced in legal proceedings. A transaction includes a number of closely linked transactions.
- An 'uncontrolled transaction' means a transaction between enterprises other than associated enterprises, whether resident or non resident.

Section 92C – Computation of ALP

- ALP shall be determined by any of the six methods, being the most appropriate method (MAM)
- The six methods include:
 - (a) comparable uncontrolled price method;
 - (b) resale price method;
 - (c) cost plus method;
 - (d) profit split method;
 - (e) transactional net margin method;
 - (f) such other method as may be prescribed by the Board ('other method')

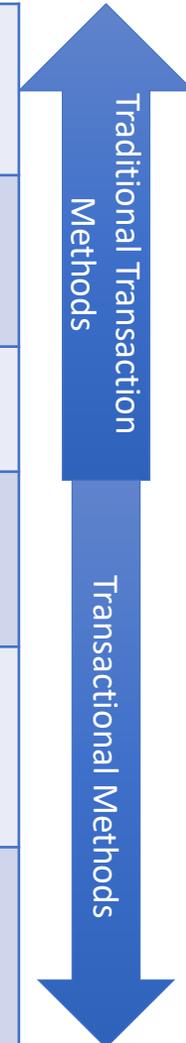
Section 92C – Computation of ALP ... *contd.*

Key features of section 92C:

- Concept of most appropriate method.
- Arithmetic mean.
- No adjustment to income if variation within 5% of the transaction value.
- Whether the 5% safe harbour is available as standard deduction?
- No exemption under sec 10A or 10B or under chapter VIA on the addition to income due to adjustment to ALP.
- Value of IT can be disturbed only if :
 - (a) ALP not determined as MAM.
 - (b) Information not maintained as per sec 92D.
 - (c) Information used is not reliable.
 - (d) Failure to furnish information as per sec 92D(3).
- Based on ALP determined of an Assessee, no refund to its AE even if TDS on such transaction.

TP Methods

Comparable Uncontrolled Price	The price charged or paid for property transferred or services provided in a comparable uncontrolled transaction + <u>Adjustments</u>
Re-sale Price	[Re-sale Price charged by the tested party for the goods or services obtained from the AE to the unrelated party minus the normal uncontrolled gross profit and the expenses incurred by the assessee] + <u>Adjustments</u>
Cost Plus	A sum of direct and indirect costs incurred and [normal uncontrolled gross profit + <u>Adjustments</u>]
Profit Split Method	Employed in transactions involving transfer of unique intangibles. The combined net profit of the AEs in a transaction are compared to their relative contribution to arrive at apportioned transfer price profit
Transaction Net Margin	The net profit of the tested party is determined against costs incurred, sales affected or assets employed or any other relevant base and the same is compared against the net profit of comparables determined against the same base + <u>Adjustments</u>
Other method	Any scientific or rational basis of proving that the transfer price was at arm's length



Most appropriate method (MAM)

- The Income Tax Act, 1961 does not provide any specific hierarchy of methods for transfer pricing. It insists on applying the 'Most Appropriate Method' (MAM).
- Rule 10C of the Income Tax Rules specify factors for determining the Most Appropriate Method
- Similar factors stated in the OECD guidelines as well:
 - Functional analysis
 - Availability of reliable information (in particular, on uncontrolled comparables)
 - Degree of comparability between the controlled and uncontrolled transactions
 - Reliability of comparability adjustments that may be needed to eliminate material differences between them
- Traditional / direct methods more preferred over transactional / indirect methods
- Other method is also a direct method - Toll Global Forwarding India (P.) Ltd. v. DCIT— [2015] 167 TTJ 57 (Del-Tri)

Section 92CA – Reference to TPO

- Reference to be made if necessary and expedient.
- Board's Instruction no 3 of 2003 explains the procedure in detail. This Instruction has been upheld by the Delhi HC.
- Reference with the approval of CIT. The Delhi HC in Sony and Gujarat HC in Veer Gems held that there was no need to give opportunity to assessee at this stage. **Bombay HC** in the case of **Vodafone** has held that where assessee contends that TP provisions do not apply in its case, Assessee should be given an opportunity before making reference.
- New provisions relating to transactions not disclosed by the assessee which come to the notice of the TPO, deemed to have been referred.

Section 92CE – Secondary Adjustments

- OECD definition
 - “adjustment that arises from imposing tax on a secondary transaction in transfer pricing cases”
 - Secondary transaction is a constructive transaction resulting from a primary adjustment.
 - Purpose – to make the actual allocation of profits consistent with the primary adjustment
 - Example: Deferred receivables
- Illustration:
 - SubCo (India) purchases goods from HoldCo (USA) for Rs. 100
 - ALP = Rs. 60
 - Excess payment = Rs. 40
 - This could be treated as: (i) Loan, or (ii) Dividend payment

Section 92CE – Secondary Adjustments ... *contd.*

- Section 92CE requires secondary adjustment to be done if a primary adjustment has been made:
 - By the assessee suo motu
 - By the Assessing Officer
 - By an Advance Pricing Agreement (APA) or Mutual Agreement Procedure (MAP)
 - As per the Safe Harbour Rules
- Deferred receivables
 - Excess money available with the AE, if not repatriated to India, deemed as an advance and interest to be computed on the same as prescribed
- Secondary adjustment – will it be an international transaction?

Other provisions

- Documentation:
 - Section **92D** provides for maintenance of documents as prescribed. This is essential to make determination of ALP. Rule 10B details the documents to be maintained.
 - Section **92E** requires an assessee to obtain an audit report of the IT in the prescribed form(Form 3CEB).
- Measures to reduce disputes:
 - Safe Harbour Rules- Section 92CB.
 - Advance Pricing Agreements- Section 92CC and Section 92CD.
 - Dispute resolution Mechanism- Section 144C.
- Section **92F** contains some definitions. Important among them are of 'ALP' and 'Transaction'.

Steps involved in transfer pricing as per the Act

1. Maintenance of TP study report
2. Reference to a TPO
3. Transfer Pricing Order
4. Draft Assessment Order
5. Reference to Dispute Resolution Panel
6. Directions of DRP
7. Final Assessment Order

Domestic TP law & Treaty interplay

Article 9 – OECD MC

Art. 9(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 accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

Article 9 – OECD MC ... *contd.*

Art. 9(2):

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 this Convention and the competent authorities of the Contracting States shall if necessary consult each other.

Article 9 – OECD MC ... *contd.*

- The Article provides for the basis of transfer pricing law within treaty law.
- Pre-2001 situation: Article 9 was present in most Indian treaties, but the Transfer Pricing provisions were not yet enacted in the Act
 - Refer: Discussion under treaty law that treaty cannot create a charge or levy!
- Article 9 and Article 11 illustration

Thin capitalization

Thin Capitalization

Earlier position:

- Interest on debt capital borrowed from shareholders resulting in abnormally high debt-equity ratio, cannot be disallowed in absence of any thin capitalization rule – **DIT v. Besix Kier Dabhol SA** [2012] 26 taxmann.com 169 (Bom.)

What is thin-capitalization?

- A company is said to be thinly-capitalized when it has high debt compared to its equity (skewed debt-equity ratio – the % would vary from vertical to vertical. For example, in infrastructure companies, a high debt would be acceptable, but the same won't be the case with a software company.)
- AE from Low Tax Jurisdiction lending money to Indian Sub, far in excess of need and capacity to repay
 - Interest paid claimed as deduction by Indian Sub
 - Lender taxable at lower rate when interest received

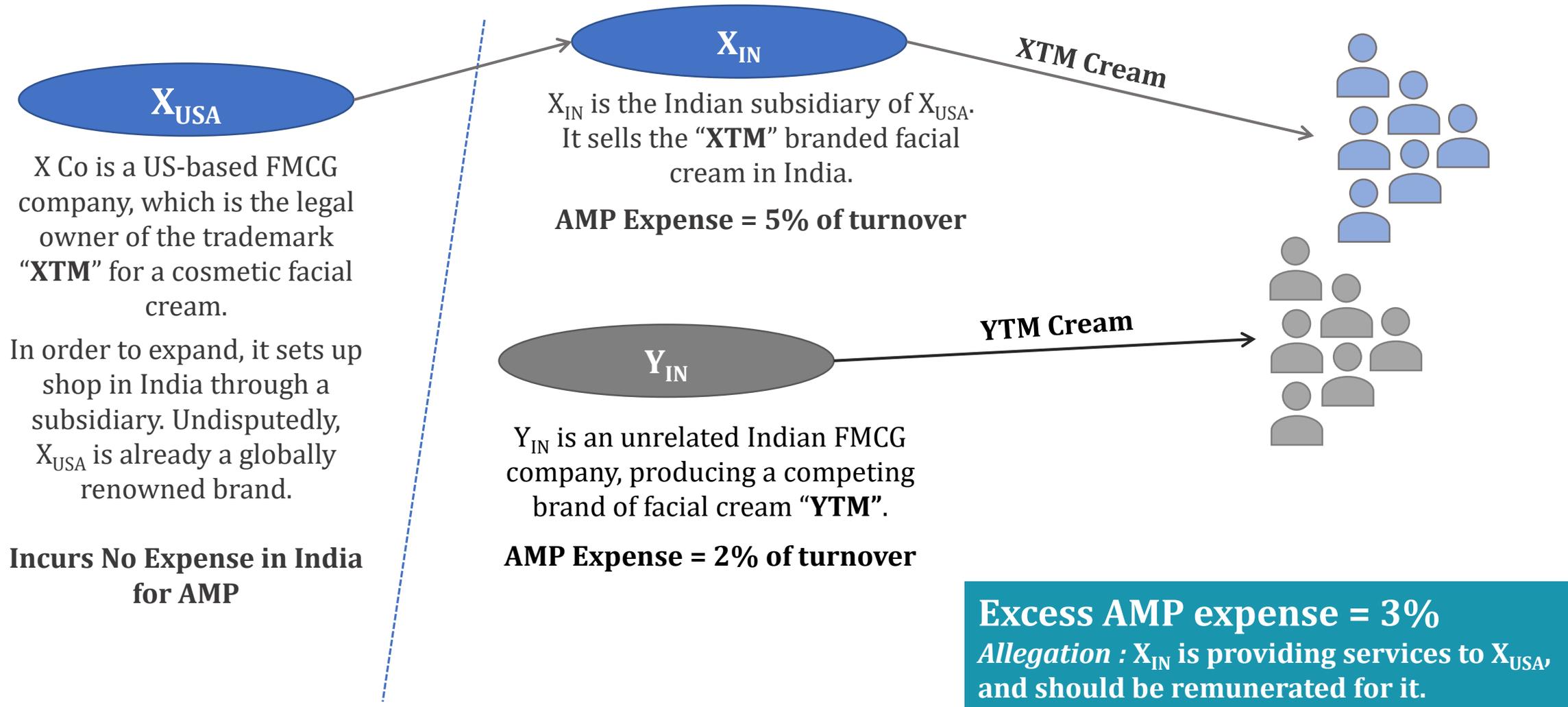
Thin Capitalization – section 94B

Section 94B:

- Interest on loan from AE would not allowed as deduction
 - In excess of 30% of EBIDTA
 - Even if the payment is at ALP, dis-allowance would apply
 - Dis-allowed sum allowed to be carried forward for 8 years
- Applicable even on loans taken from third parties where
 - Loan is guaranteed by AE
 - Secured by deposit from AE
- No corresponding adjustment permissible
- Significant dis-advantage to loss making Indian Sub
 - Better to give capital subsidy - Siemens SC can be relied upon

AMP Expenses

AMP Expenses – the issue



AMP Expenses ... *contd.*

- Para 6.2 of OECD guidelines states that the terms “Intangible Property” includes rights to use International Assets such as patents, trademark, trade name and design, Models, literary and artistic works, copyright and other intellectual property rights.
- Section 92B which define International Transactions was also amended to clarify that it included “Intangible Properties”
- Revenue has been making adjustment on account of Advertisement, Marketing and Promotion (“AMP”) expenses incurred by Indian Companies using the Trademark of overseas associated Enterprises for nil or little consideration for the purpose of rendering Brand Development Services to the Associated Foreign Enterprises.
- The Delhi High Court in the case of Sony Ericsson Mobile Communication India Private Limited Versus Commissioner of Income Tax (374 ITR 118) has held that the AMP expenses incurred by Assessee therein constitute an International Transaction. The Court had rejected the application of Bright Line Test holding that it has no statutory basis.
- In the subsequent decisions of Maruti Suzuki India Limited (381 ITR 117) and Whirlpool India Limited (381 ITR 154) the High Court has held that the existence of International Transactions in AMP may not be presumed and the same is needed to be demonstrated on the basis of evidence.

AMP Expenses – Court rulings

[Sony Ericsson Mobile Communications India \(P.\) Ltd. v. CIT \[2015\] 55 taxmann.com 240 \(Delhi\)](#)

- i. The fact that AMP is an international transaction cannot be disputed because the assessee itself contended that it has been remunerated as part of the distribution function.
- ii. The High Court, however, rejected BLT as a method to benchmark the transaction or determine the compensation receivable by the assessee.
- iii. The High Court held that the distribution function and the AMP function are closely linked and should, therefore, be benchmarked together.
- iv. The High Court further held that the Revenue cannot accept the value of the import price and at the same time hold that AMP has not been remunerated.
- v. For benchmarking the combined transaction, comparables should function under a similar distribution arrangement and not be brand owner.

AMP Expenses – Court rulings ... *contd.*

[Sony Ericsson Mobile Communications India \(P.\) Ltd. v. CIT \[2015\] 55 taxmann.com 240 \(Delhi\)](#)

- vi. Segregated approach can be followed only when no comparable is found that is similar to the assessee's distribution arrangement with the AE. But setoff has to be given as section 92(3) does not prohibit the same.
- vii. The High Court held that both TNMM and Profit Split Method would be appropriate to benchmark the AMP function along with the distribution function.
- viii. Brand is created and enhanced not only through advertisement but also through goodwill and superior quality of goods and services consistently provided. Advertisement alone does not create brand.
- ix. Recognizes the concept of economic ownership i.e. a transaction is recognized only when a person is deprived of economic ownership and the person is entitled for compensation for such deprivation.

AMP Expenses – Court ruling ... *contd.*

Maruti Suzuki India Ltd. v. CIT [2015] 64 taxmann.com 150 (Delhi)

- i. It followed the decision of Sony Mobile and held that BLT is not a prescribed method under the IT Act to determine the compensation for AMP function.
- ii. It held that in order to determine a compensation, the Revenue has to show the existence of an international transaction on account of AMP function.
- iii. In the absence of any agreement for performing the AMP function, the Court held that the Revenue has to establish that the assessee performed the AMP function at the behest of the AE. Since the Revenue could not show that the assessee performed these functions on the direction of the AE, the Court held that there was no international transaction.
- iv. The Court further held that there was no machinery under the IT Act to determine the benefit to the AE in terms of enhancement of its brand value. The Court held that none of the methods under sec.92C(1) could be used for this purpose.
- v. e) In the absence of machinery, it was held that even if there is an international transaction on account of AMP function, no compensation for the same is determinable- B.C. Srinivasa Shetty's case.

Other issues

Recharacterization of transactions

- Delhi High Court in the case of EKL Appliances (345 ITR 241) held that ordinarily the Revenue shall not restructure/re-characterize the actual transaction legitimately entered into between the contracting parties. It observed: “barring exceptional cases, the tax administration should not disregard the actual transaction or substitute other transactions for them and the examination of a controlled transaction should ordinarily be based on the transaction as it has been actually undertaken and structured by the associated enterprises.”
- The High Court, following the OECD guidelines on transfer pricing held that the Revenue may recharacterize the transaction in two circumstances namely (i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner.

Share transfer without consideration

- USA Holding Company (HoldCo) has an Indian Subsidiary (SubCo)
- HoldCo transfers the shares in Indian SubCo to another Singapore Co. (SingCo) without any consideration.
- Whether the transfer would be attracting TP provisions or not?
- Venenburg Group B.V., In re [2007] 159 Taxman 219 (AAR – New Delhi)
 - Section 9, read with sections, 195, 139 and 92 to 92F, of the Income-tax Act, 1961 - Income - Deemed to accrue or arise in India - Whether where an applicant, a non-resident company incorporated in Netherlands, in course of its corporate reorganization of its group companies, proposed transfer of its entire shares held by it in its Indian subsidiary company to another of its 100 per cent subsidiary company incorporated in Netherlands, in view of provisions of the Act read with provisions of DTAA between India and Netherlands, no taxable capital gains in respect of said transaction would arise in India - Held, yes - Whether since no tax will be payable in India, no tax will be required to be deducted under section 195 - Held, yes - Whether, consequently, applicant will not be required to file any return under section 139 in respect of transaction in question and provisions of sections 92 to 92F will also not be attracted - Held, yes

Thank you. Questions?