Ahmedabad

Baroda

Mumbai

Dhirubhai Shah & Co.

Chartered Accountants

Domestic Transfer Pricing

CONTACT US

Head Office

4th Floor "Aditya",
Nr. Mithakhali Six Roads,
Ellisbridge,
Ahmedabad – 380006.

Tel. No.: 079-2640 3326
Telefax: 079-2640 3325

Email : dshahco@dbsgroup.in

Foreword

We at DBS are pleased to present you a newsletter containing certain basic details on domestic transfer pricing which is a relatively new concept introduced in the Finance Act 2012. Till very recently the transfer pricing provisions were applicable only in case of cross border transactions, however with the introduction of these new provisions it would also cover those transactions which take place with a related party within India though in the normal course of business, defined as Specified Domestic Transactions.

Included in this newsletter are various - provisions in relation to such domestic transfer pricing that will give you a basic idea about domestic Transfer pricing rules and regulations.
Trust this will be useful to you.

Agenda

Applicability

- These rules come into effect from 1st of April 2012

- All assesses including sole proprietors, partnerships, companies etc incurring any kind of expenditure with a related party will be covered under the rules and regulations of domestic transfer pricing.

- Few examples of related party:
  - General relatives i.e. spouse, children, parents, siblings, etc.
  - Person of lineal ascendants or descendants.
  - Partners, directors would be classified as relatives for their relative organizations.
  - Businesses i.e. partnership, companies, etc. where substantial interest is held by the partners, directors or their relatives.
  - Two or more than two businesses i.e. partnership, companies, etc. having common shareholding/economic interest in excess of 20%.
  - Two or more than two businesses i.e. partnership, companies, etc. having common executive management/control in excess of 20%.

- The Domestic transfer pricing provisions are applicable whenever transactions between related parties exceed the minimum threshold amount of INR 50 million. All related party transactions exceeding this basic threshold limit will be subject to domestic transfer pricing provisions.

- These transactions mainly includes the related party expenditures, debit notes and credit notes sent within the group companies (which may be in respect of Interest, corporate guarantee receipt /payment, cash pooling, group funding, etc.) transfer of goods or services from/to the tax holiday undertaking to/from non-tax holiday undertaking & business transaction between the tax-holiday undertaking produces more than ordinary profits with closely connected person, etc.

- To explain these new amendments in a simpler manner – earlier all transactions even between related parties were done at a *considerable FAIR value pricing concept* whereas after these amendments transactions between related parties will have to be done *at "Arms Length Price" (ALP)*.

Methods for Determining the Arm's Length Price

- Arm's Length price (ALP) means a price that is mutually decided by two unrelated parties (having no power to influence or control another) in normal course of business.
- As per the new regulations, the transfer pricing officer (TPO) will have the power to determine the ALP.
- In case the ALP determined by the TPO is inconsistence with the pricing fixed by the assessee, then the TPO has the power to adjust the revenue/ expense accordingly which will thereby impact the taxable income of the concerned assessee.
- The ALP can be determined by any one of the following method as prescribed by Income-Tax Act, 1961:-

Sr. No.	Method	Relevant in following transactions*
1.	Comparable Uncontrollable Price Method (CUP)	Transfer of Goods Provision of services Loans, Provision of Finance
2.	Resale Price Method (RSP)	Transactions involving distribution/sale of finished products Distribution of goods involving no or little value-addition
3.	Cost Plus Method	Where comparable data from industry not available Provision of services Joint facility arrangements Transfer of semi-finished goods Long-term buying & selling arrangements
4.	Profit Split Method	Integrated services provided by more than one enterprise Multiple inter-related transactions, which cannot be separately evaluate
5.	Transaction Net Margin Method (TNMM)	When all the above method fails this method is applicable

*The above situations are indicative. Actual method determination depends on a case to case basis

Documentation

- The assesse's who are covered by the domestic transfer pricing provisions are mandatorily required to maintain the requisite information & documents as mentioned hereunder.
- The documentation is divided into three phase:- *(Indicative, would differ from case to case)*

1. Entity related
   - Brief about Industry
   - Brief about the group
   - Profile of Assessee
   - Profile of Associate Enterprise with whom the transaction takes place
2. Transaction related
   - Agreement
   - Invoices
   - Price related correspondence (Letters, e-mails, fax, etc)
3. Price Related
   - Transaction terms which should include the detailed computation of the ALP arrived by the Assessee
   - Functional Analysis (Function, Assets & Risks) which will help in deciding the margins
   - Economic Analysis (method selection, comparable benchmarking Forecasts, budgets & estimates). This information can be obtained by way of internal information, external comparable companies, public domain such as websites, Indian databases such as prowess and capital line
   - Reasons for selection of the most applicable method i.e. ALP as per the assessee

Compliance & Penalty Provisions for non compliance

Compliance provisions:-

- The assesse's have to obtain & furnish a prescribed report from Chartered Accountants in Form 3CEB.
- The Chartered Accountants reports need to be submitted to the tax authorities by the due date of filling annual return of income. At present, the due date is 30th November.
- The documentation as mentioned above is not required to be submitted along with the report, but its needs to be obtained before the due date by the assessee.
- The documentation is required to be submitted during the course of assessment as and when the Transfer Pricing Officer (TPO) demands for the same.
- A separate cell consisting of transfer pricing officer will now perform the assessments/audits of Specified Domestic Transactions instead of the regular assessing officer.
- The time limit for completion of audit at present will 4 years from the end of relevant assessment year.

A stringent penalty regime has been prescribed for non compliance:-

Sr. No.	Particulars	Penalty provisions
1	Failure to maintain documents	2% of the value of the transaction
2	Failure to maintain the Chartered Accountant's report	2% of the value of the transaction
3	Failure to Furnish the report by due date	INR 1,00,000
4	Maintaining or furnishing incorrect information or documents	2% of the value of the transaction
5	Adjustment for incorrect pricing	Penalty by way 100% to 300% of the additional tax payable.

Other Miscellaneous Points

- Adjustments to MAT profits not to be made i.e. these regulations not to impact MAT liability.
- Threshold limit of INR 50 MN will be applicable to transactions in totality with a particular specified related party and not to transactions individually.
- Tolerable limit of ± 3% has been prescribed i.e. ALP derived by the assessee can vary in the range of 3% of the ALP arrived by the TPO.
- Few concepts/transactions that are applicable as in case of International transfer pricing have been done away with in case of domestic transfer pricing such as

  A) *No requirement of maintaining advance pricing agreements (APA)*. These agreements are usually required to be maintained in case of cross border transactions between related parties. These agreements are like MOU's which basically include the price agreed for a particular related party transaction.

  B) *Few transactions are also not covered such as interest free loans, provisioning of guarantees, use of intangibles*. Usually in these kind of cross border transactions, tax department urges the assesse's in India to book notional income on such transactions and thereby levy tax on such notional income irrespective of the fact that income has been agreed to be levied or not. However, such transactions involving charging of notional income are not covered under the concept of domestic transfer pricing.

Way Forward:

It will be extremely important to map all the likely transactions that assesse's are certain to carry out with specified related persons. The assessee thereafter should analyze all transactions as to how these provisions are likely to impact them financially and from a taxation point of view. This analysis will help the assessee plan in a better way as to how to go forward in structuring the group transactions. It is extremely important to organize all relevant data in a timely manner so that necessary actions as well as compliance can take place.

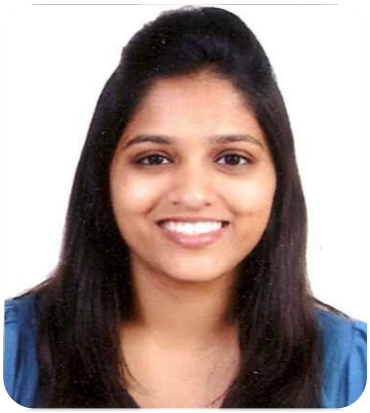
Committed to Excellence

Head Office:
4th Floor "Aditya", B/H Abhijeet -1, Near Mithakhali Six Roads, Ellisbridge, Ahmedabad (Gujarat) 380006

Vadodara Branch:
204, Sarkar Complex,
Opp ABS Tower,
Old Padra Road,
Vadodara 390015

Mumbai Branch:
1st Floor Cama Chambers,
23 Nagindas Master Road,
Mumbai 400023

Team behind this Presentation



C.A. Devanshi Ghiya

Email :devanshi@dbsgroup.in

Mobile: + 91 9428804496

Website: www.dbsgroup.in