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TP Niche

A spectrum of transfer pricing issue

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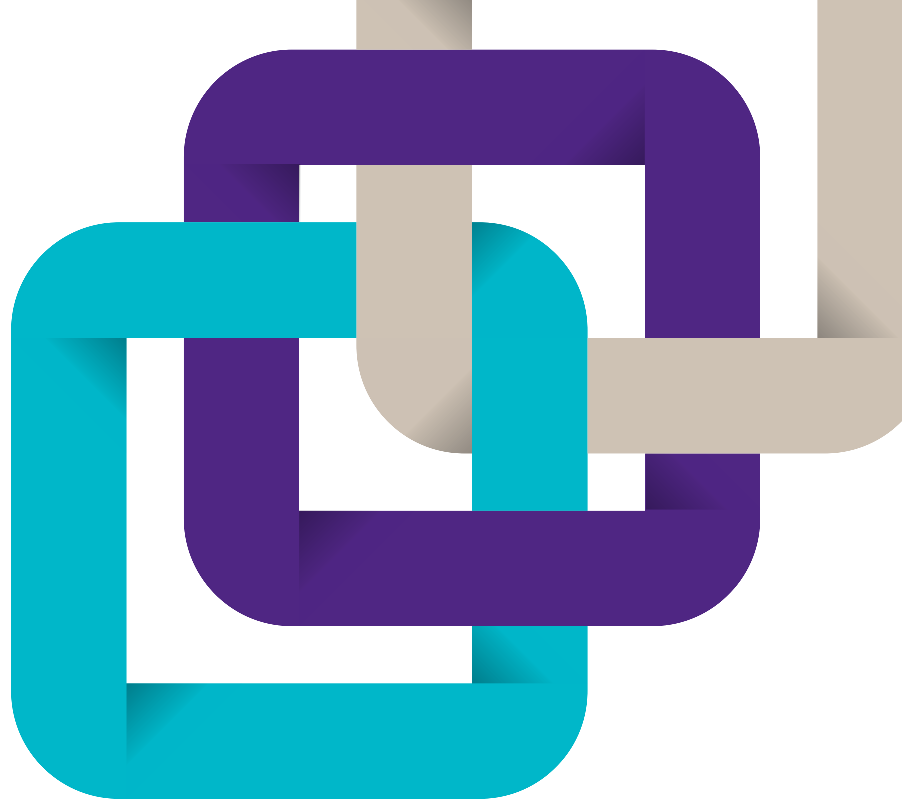

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Foreword

Arun Chhabra

Director

Grant Thornton Advisory Private Limited

Dear Readers,

With our quarterly publication TP Niche, the main objective is to share our firm's experience on emerging transfer pricing aspects and provide valuable insights to the readers on the evolving transfer pricing landscape in India.

This issue of TP Niche covers a wide range of transfer pricing topics categorised under five Sections viz. 'Perspective', 'Our experience', 'From the judiciary', 'Tracker' and 'Global corner'. The Perspective section of this edition covers evolution of jurisprudence in relation to attribution of profits to Permanent Establishments in India. 'Our Experience' section captures our firm's experience in innovative transfer pricing planning assignments. Our planning services ensure that a robust policy is put in place for clients' intragroup arrangements. These ex-ante exercises safeguard clients before actual implementation of intragroup arrangements and assesses potential risk exposure, if any. With so many decisions being pronounced by the Tribunal and High Courts on Transfer Pricing issues on regular basis, it is challenging to keep track of fundamental positions emerging from such decisions on peculiar issues. The publication captures some key rulings reported in the last quarter.

'Tracker' section lists key developments in the form of notifications, circulars and other publications touching different legislative and practical aspects of transfer pricing. 'Global Corner' is a section designed to highlight key developments in the global TP arena. In this edition, readers get to know of recent developments in TP regime in Singapore. This section also provides a gist of the prominent ruling by Australian Federal Court on intragroup financial arrangements. Readers may also read about other global updates from OECD in relation to BEPS in this section.

Hoping that you will find this TP Niche edition highly informative and useful. In case you have any comment, query or feedback, please reach out to us.

Perspective

This Section provides a perspective on the attribution of profits in case of permanent establishments with reference to Indian jurisprudence.

Introduction

The existence of nexus between 'income' and the 'taxing state' is a prerequisite for the right to tax. The fundamentals of international tax revolve around the existence of two forms of taxation i.e. residence based taxation and source based taxation. In residence based taxation, a person is taxed on his global income in the state of residence. While, he may also get taxed in the source country on the income arising therein on the basis of source based taxation.

Increased globalisation has resulted in multi-national enterprises (MNE) operating in multiple jurisdictions, thus giving rise to disputes on profit allocation. The tax authorities, especially in developing nations, are concerned about erosion of their due share of revenue resulting from significant operations of foreign entity in their country. A correct and just allocation of profits between the residence and source jurisdiction is hence imperative.

On global and domestic fronts, there is guidance available on determination of taxable presence of a MNE in a source state through formation of a Permanent Establishment (PE). However, absence of systematic, clear and detailed rules on attribution of profits to a PE is a cause of concern. In such situations, transfer pricing ('TP') has a pivotal role to play to ensure appropriate attribution of profits to PE. The discussion below throws light on the ensuing issue. A gamut of case laws have been analysed to present a comprehensive outlook and to reflect the evolution of Indian jurisprudence in the context of attribution of profits to PE.

Definition of Permanent Establishment

Article 5 of the Organisation for Economic Cooperation and Development Model Tax Convention on Income and on Capital ('OECD Model') and Section 92F(iii)(a) of the Income Tax Act, 1961 ('the Act') define the term PE to mean "a fixed place of business through which the business of an enterprise is wholly or partly carried on."

Determination of the existence of PE and the resulting attribution of profits to PE are concepts widely debated in the Indian Courts. However, the focus of this column shall be restricted to the concept of attribution of profits to PE.

Basic Principles on Attribution of Profits to Permanent Establishment

Guidance under OECD Model

Attribution of profits to PE arises on existence of PE as stipulated in Article 5 of the OECD Model. Thereafter, Article 7(1) of the OECD Model on 'Business Profits' comes into force. It clearly focusses on the concept of attribution stating:

"The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in that other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in that other State but only so much of them as is attributable to that permanent establishment."

Further, for the purpose of attribution of profits, Article 7(2) of the OECD Model necessitates PE to operate as if it were a:

"separate and independent enterprise taking into account the functions performed, assets used and risks assumed ('FAR')."

Guidance under Indian jurisprudence

Following are the key principles laid down by Indian courts in the context of attribution of profits to PE:

- **Evaluating PE's role in the economic value chain**

Profits are attributed to PE of the MNE on account of PE's participation in the economic life of the host country. This view was established in ZTE Corporation where the Delhi bench of Income Tax Appellate Tribunal ('ITAT') held:

"the most important aspect to be kept in mind is the level of PE's participation in the economic life of the source country. It is primarily nexus between the source country and PE's activities which produce the taxable income" to the taxpayer".

The above judgment clearly laid emphasis on the presence of economic connection between the source country and the PE of the foreign enterprise operating in the source country.

- **PE is a separate and independent legal entity**

It is an established fact that profits are computed on the assumption that PE is distinct and separate enterprise dealing independently with the enterprise of which it is a PE. This view was reiterated in M/S Seagate Singapore International as:

"For the purpose of computation of profits of the PE, it should be treated as a separate and distinct enterprise wholly independent of the enterprise of which it is a PE".

This separate entity approach has also found support in Section 92F of the Act that defines the term 'enterprise'.

- **Attribution in accordance with Arm's Length Principle**

The other underlying principle requires attribution to be governed by the Arm's Length Principle ('ALP'). In this regard, Central Board of Direct Taxes ('CBDT') vide Circular No. 5/2004 (dated 28th September 2004) provided for tax treatment of PE in case of non-resident entity having business connection with resident Indian entity. It clarified that:

"profits to be attributed to a PE are those that PE would have made if, instead of dealing with its Head Office, it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the arm's length principle."

Hence, it is seen that the concept of attribution is in approbation with the basic fundamental principle of transfer pricing i.e. ALP.

Indian provisions on Attribution of Profits

Explanation 1(a) to Section 9(1)(i) of the Act provides basic framework for attribution of profits owing to 'business connection' in India as below:

"in case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India"

Expected benefits of these initiatives:

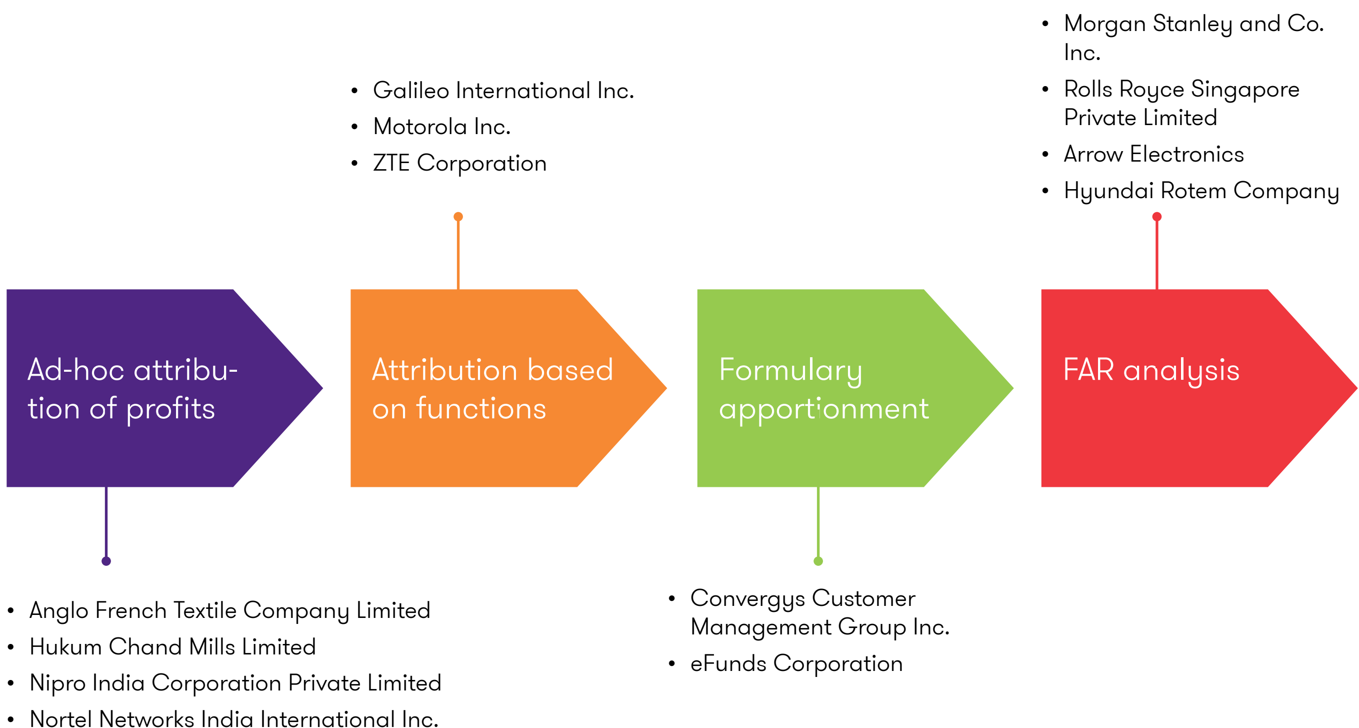
In absence of specific provisions on estimation of profits attributable to PE, the Act provides for general clauses for determination of income of non-residents. In this regard, Rule 10 of the Income Tax Rules ("the Rules") lists methods for determination of income of non-residents. It states that, "If

This view has been established in varied cases in the Indian judiciary including, Rolls Royce Singapore Private Limited (Delhi High Court Judgment), M/S IJM (India) Infrastructure Limited (Hyderabad Bench) etc.

the Assessing Officer ('AO') is of the opinion that the income accruing or arising to the non- resident, whether directly or indirectly, through or from any business connection in India cannot be definitely ascertained, the amount of such income may be calculated:

- At such percentage of the turnover so accruing or arising as the AO may consider to be reasonable, or
- On any amount which bears the same proportion to the total profits or gains of the business of such person as the receipts so accruing or arising bear to the total receipts of the business, or
- In such other manner as the AO may deem suitable.

Flow of attribution of profits in judicial context: The observed transition



Flow of attribution of profits in judicial context: The observed transition

Anglo French Textile Company Limited v. CIT is one of the early rulings by Indian Judiciary on attribution dating to the year 1952. The assessee was a non-resident company manufacturing textiles in India. In the course of its business, it bought cotton from, and sold textiles in British India (being the taxable territory) and partly outside British India (Madras). The entire profits from outside of British India were being received in British India. The issue before the court was whether income received in British India could be said to wholly arise in India and whether allocation based on business operation was required.

On the issue of profit attribution, the Supreme Court ('SC') stated that "there should be allocation of income between various business operations of the assessee demarcating the income arising in the taxable territories (British India) in the particular year from the income arising without the taxable territories in that year". Accordingly, the figure of 10 per cent on British Indian sales was considered reasonable for attribution of profits on the basis of extent of operations carried out in British India.

Similar view was upheld in Hukum Chand Mills Limited v. CIT. The appellant company manufactured textiles in its mills at Indore outside British India and sold its goods to merchants in British India. The sales were made through brokers and agents in British India. On the basis of facts of the case, 15 per cent allocation was considered reasonable for the operations relating to contracts undertaken in British India. In arriving at the figure of 15 per cent, emphasis was laid on then Rule 33 of the Income Tax Rules, 1922. Rule 33 has now been replicated as Rule 10 of the Income Tax Rules that has been explained above. Excerpts from the judgment stated, "The question as to what proportion of the profits of the sales arose or accrued in British India is essentially one of fact depending upon the circumstances of the case. In the absence of some statutory or other fixed formula, any finding on the question of proportion involves some element of guess work. The endeavour can only be to be approximate and there cannot in the very nature of things be great precision and exactness in the matter."

In the recent past, rulings pertaining to profit attribution were pronounced considering Rule 10 of the Rules together with specific provisions in the Act. In DDIT v. Nipro Asia Pte Ltd the assessee was a company incorporated in Singapore operating with a Branch Office ("BO") in India. In computing the assessee's profit from sales in India, the AO, in absence of any correct transfer pricing study report, adopted provisions of Rule 10 of the Rules using 'selective financial figures' from publicly available websites. ITAT rejected AO's computation (negating using of publicly available data) and assessed income based on Section 44BB and 44BBB of the Act which provides for presumptive profit rate of 10 per cent. Accordingly, ITAT calculated assessee's profit at 10 per cent of total sales in India. Similar view was upheld in Nortel Networks India International Inc. and GE Energy Parts Inc.

In the case of Motorola Inc., ITAT allocated 20 per cent profits to the PE on the contention that the PE played role in negotiation and conclusion of contracts and supply of equipment in India. Similarly, in Galileo International Inc., 15 per cent profit attribution was considered sufficient owing to the role played by PE in negotiating contracts. Decisions on similar basis were upheld in case of Rolls Royce Plc., ZTE Corporation etc.

Formulary Apportionment in attribution of profits

In 2013, in case of Convergys Customer Management Group Inc. v ADIT formulary apportionment was used as the basis of allocation. It was ascertained that the assessee had a fixed place PE in India following the India-US Double Taxation Avoidance Agreement (DTAA) and to attribute profits, AO adopted head count as basis for allocating revenue and expenses. However, the tribunal rejected the approach of the AO and used end customer revenue as base to which a global operating income percentage was applied to arrive at profits attributable to the Indian operations. The residual profits were than apportioned between the US (Head Office) and the Indian PE.

Further, to allocate the residual profits the Delhi Tribunal relied on decision in Anglo French Textile Company Limited v. CIT and Hukum Chand Mills Limited v. CIT discussed above. The higher figure of 15 per cent was applied to the instant case to meet the 'ends of justice.'

Yet another case (eFunds Corporation v. ADIT) was decided by ITAT in light of formulary approach that placed importance on a methodological procedure for profit attribution. The total profits

[2] AY 2003-04 Pronounced on 16/02/2017

attributable to India were worked out in proportion of Indian assets to global assets.

Although a deviation from the conventional ALP approach, the Tribunal had resorted to formulary apportionment in the above-mentioned case. A pre-determined formula for determination of profits attributable to PE (global formulary apportionment) disregarded FAR Analysis. This concern has also been acknowledged by the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ('OECD TP') stating:

"predetermine formulae are arbitrary and disregard market conditions, management's own allocation of resources, thus producing an allocation of profits that may bear no sound relationship to the specific facts surrounding the transaction. A formula based on a combination of costs, assets, payroll and sales implicitly imputes a fixed rate of profit per currency unit, regardless of differences in functions, assets, risks and efficiencies among members of the MNE group."

In India, the current provisions for attribution of profits as defined under Rule 10 are akin to the formulary approach. However, globally, there has been no agreement on the use of global formulary apportionment owing to practical difficulties

Importance of FAR analysis in Arms-Length attribution of profits.

Landmark decision by the SC in DIT (International Taxation), Mumbai v. Morgan Stanley and Co. Inc. throws light on the importance of transfer pricing analysis in attribution of profits to PE. The company, a US-based leading investment bank, outsourced a wide range of high-end support services to Morgan Stanley Advantage Services Private Limited (MSAS) in India. To obtain clarity on taxation of its Indian outsourcing operations, the question was filed with AAR, "If it is held that there is a PE in India, would there be anything further attributable to the PE if the PE was compensated on an arm's length basis?" The Supreme Court upheld the AAR and pronounced as below:

"The impugned ruling is correct in principle insofar as the 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 the PE."

Further, it was established that the situation would have been different if transfer pricing analysis did 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 the PE for those functions/risks that have not been considered. Therefore, it is imperative that the transfer pricing analysis of the taxpayer exhaustively captures the FAR for attribution of profits.

Similarly, in Rolls Royce Singapore Private Limited, it was emphasised that profit attributable to the PE in India will need to be prepared with regard to the functions performed, risk assumed and assets used by the PE in India. The assessee was incorporated in Singapore and rendered repair and maintenance services along with supplying spares to customers in India. The assessee contended that the business income arising from supply of spares was not taxable on account of absence of PE in India. The AO, Commission of Income Tax (Appeals) and the ITAT, however, took the view that the assessee had 'dependant agent PE in India' and accordingly profit was to be attributed to the PE in India and taxable in India. The AO held that 25 per cent of the profits on sale of spare parts was chargeable to tax which was reduced to 10 per cent by CIT(A) and ITAT. To substantiate the reduction in the profits attributable it was clearly laid, "The risk assumed by PE in India is very limited. It (ANR) is only performing the functions of soliciting contracts for sale of assessee's products or promoting the sales. All other main or core activities regarding the arrangements or acquisition of products supplied by the assessee company to the Indian customers are performed in Singapore. Therefore, the profit attributable to PE in India shall be confined to the marketing activity carried out within India to solicit orders and promoting the sale of assessee's products. The activity carried out in India to promote the sale of the assessee's products and then to soliciting order would lead to attributable profits to PE in India at best to the extent of 10 per cent of the profit earned from the activities of sale of spares by the assessee company to the Indian customers."

Also, for the above attribution, reliance was placed on two cases namely, Ingersoll Rand Company and Annamali Timber Trust and Company where attribution of 10 per cent was justified owing to trading/ negotiation and soliciting operations carried out in India. Hence, the Tribunal has ascribed significance to the TP Study and therefore undertaking a detailed transfer pricing analysis for the purpose of attribution of profits to PE is imperative.

Further in Hyundai Rotem Company, the approach principally accepted by the Tribunal also laid considerable reliance on TP Study. The study exhibited detailed analysis on the functions performed, assets employed and risk assumed. The taxpayer, a project office of Hyundai Rotem Company (Korea) provided liaisoning, coordination and administrative support services to its head office on a cost plus basis. The AO did not accept the cost plus methodology and instead determined the income attributable basis Rule 10 provided in the Rules. The CIT (A) upheld the approach adopted by AO. On appeal before the Tribunal, it was held that Rule 10 was to be applied in cases where the income of the PE could not be definitely ascertained. This fact was to be demonstrated by the AO before proceeding with Rule 10. Where TP Study already existed, it was warranted to first reject the TP Study on sufficient and reasonable grounds before computing attribution as per Rule 10. As discussed above, this approach was also witnessed in Nipro Asia Pte Limited where TP Study was rejected on account of various deficiencies. Hence, the AO invoked provisions of Rule 10 of the Rules to determine the income of the taxpayer.

In a recent decision in case of Arrow Electronics India Limited - Arrow Asia Pac Ltd., Hong Kong had set up a company in Singapore, Arrow Electronics India Limited. This Singapore based company had opened a liaison office ("LO") in Bangalore after obtaining relevant approvals from the Reserve Bank of India. However, Arrow Group, in December 2002 incorporated a fully owned subsidiary in the name of M/S Arrow Electronics India Private Limited. The LO was established to be the Indian PE.

To attribute profits, AO placed considerable reliance on FAR analysis. It was held, "there is no mathematical formula for working out profits of Indian operations and that of Singapore operations. Functions, Assets and Risk analysis is the best way to arrive at profits". The allocation of weights was in terms of different functions performed by the LO. The final quantification upheld by the Tribunal was attributable as 40:60 to the LO and the HO on the basis of following methodology.

The OECD Base Erosion and Profit shifting ('BEPS') allows profits to be taxed where value is created and also where economic revenue generating activities are performed. From the above case, it is clear that attribution of profits were in line with 'value creation' as advocated by the OECD BEPS report.

Parameters	**Functions**	**Assets**	**Risks**	**Total**
Sectoral Weightage	50%	25%	25%	100%
Intra Sectoral weightage (LO:HO)	70:30	10:90	10:90	100
Weighted Average (LO:HO)	35:15	2.5:22.5	2.5:22.5	40:60
Weighted Average (LO:HO)	35:15	2.5:22.5	2.5:22.5	40:60

Concluding remarks

When a business embarks on the idea of going global, permanent establishment is the cause of concern. As discussed, while rules on determining existence of PE are clearly laid down, estimation of attribution of profits to PE has been a matter of continuous debate before the Courts/ Tribunal. As has been established in abundant case laws, it is purely a matter dependent on the facts and circumstance of each specific case.

However, cases where existence of PE has been confirmed by the taxpayer, the PE is under obligation to maintain its book of accounts for tax purposes. It aids in attributing revenue and costs to the different activities of the PE. It was established in the case of CIT v. Hyundai Heavy Industries Co. Ltd. that in absence of the books of PE, the revenue and costs attributable to the installation activities of a PE were determined on the basis of the generally acceptable principles of accounting.

Subsequently, transfer pricing compliance also becomes imperative. Attribution of profits in that case, will have to be undertaken as per the arms - length principle. Hence, the PE is required, to comply with the provisions under the Indian regulations to file an accountant's report in Form 3CEB and maintain supporting transfer pricing documentation as required under the Act. Also, the associated penalty in respect of non-maintenance of prescribed transfer pricing documents and failure to furnish the accountant's report gets attracted in case of PE.

Our experience

This Section narrates Grant Thornton India LLP ("Grant Thornton"/ "GTILLP")'s experience in formulating effective Transfer Pricing planning studies.

Client A:

Background:

The top management of the Group based out of Singapore, extends requirement based management support services to its AEs based out of India, Malaysia and Philippines. The top management includes:

a. CEO – Providing the overall direction at every point of development

b. Sales Head – Marketing and promoting the services and supporting the individual entity in identifying the targets, guiding the AEs in the negotiation process and in concluding the project

c. Finance Head – Support in establishing and strengthening the internal control mechanism, monitoring the progress on a regular basis, monitoring and ensuring that the invoices are raised in accordance with the terms of contract, collating data for internal financial reporting, etc.

We were engaged to provide advice to the client regarding the most appropriate transfer pricing framework for recharging the above mentioned management support services.

Our Approach:

The basis recommended for determining the quantum of management charges to be recovered was unique, as it involved recommending a model, which would capture the efforts put in by the individual members of the management team and translate the time cost into a cost pool for allocating the same on a dynamic model by considering the following:

(a) Direct costs- the cost attributable directly to an entity,

(b) Common costs – allocated on the basis of efforts and value of business generated.

We analysed each of the cost head to substantiate its allocation and also back it up with viable allocation key. While recommending the cost allocation keys we relied on the principles laid down in "OECD Transfer Pricing Guidelines" and "UN Practical Manual on Transfer Pricing" for intra-group services.

Also given the stringent litigation surrounding management costs, we made sure that the management captured evidences of provision of such services, and all relevant documents to support the rationale of incurring such costs and related benefits availed as a result.

Receipt of low value added services have been covered under the Safe Harbour scheme w.e.f AY 2017-18. In light of this development, taxpayers opting for this safe harbour would be required to maintain appropriate documentation. Further assessee would be required to obtain certification from an accountant pertaining the following:

- Method of cost pooling
- Exclusion of shareholder and duplicate costs from the cost pool
- Reasonableness of cost allocation keys

Client B:

Background:

The client, engaged in providing software development and marketing support services to its parent company/ AE in Canada, proposed to commence software distribution activities in India. We were requested by the client to recommend an appropriate TP model for the proposed transaction of software distribution.

- The AE develops and sells software products for the transportation and infrastructure sector.
- Since Indian customers prefer to pay in INR, the client in India would enter into a contract with the end customers on behalf of the AE, for the sale of software licenses in India. However, the end-user license agreement ("EULA") would be between the customers and the AE (which is the owner of all intellectual properties).

We were engaged to provide advice to the client regarding the most appropriate transfer pricing framework for recharging the above mentioned management support services.

Our Approach:

We carried out a detailed FAR analysis of the client and proposed various operational models. On evaluation of models, we advised the client to operate as a limited risk distributor instead of a commission based model.

We recommended the client to maintain an appropriate profit margin both at the net level and at the gross level to ensure ALP from an Indian TP perspective. Our recommendation was also within the inter-percentile range of the PLI of comparable companies to ensure ALP adherence from the Canadian TP perspective.

- Based on the recommended PLI, we suggested the client to forecast their direct and indirect costs in order to determine the purchase price of the software licenses being purchased from the AE for sale in India.
- Since the client operates in three different segments, we also recommended appropriate cost allocation to be maintained between the segments and the basis of cost allocation.

In addition to our recommendations on the TP policy, we also advised the client in respect of drafting an exhaustive inter-company agreement which validates its characterisation as a limited risk distributor. We highlighted that the client should cover aspects such as credit risk, invoicing, etc. in its intercompany agreement.

Client C:

Background:

The client is a leading hotel asset management company incorporated in India for the purpose of construction, development and management of hotels in India and has partnered with various large global hotel operators.

Apart from developing and operating hotels for itself, the client is also engaged in assisting group companies in India in developing hotels which are then managed by respective group entities.

Further, it is also assisted in providing administrative, management and strategy related support services to its group companies that do not possess the requisite expertise to perform the above management, strategic and administrative related functions in respect of their business operations.

The client had been charging the cost pertaining to the above mentioned services from the group entities without charging any markup. However, these services being value adding services, the client approached us to recommend a pricing model that would take into account the revenue of its group entities.

Our Approach:

Based on our discussions with the management and detailed analysis of the business operations and the entire flow of function, asset and risk, we determined that the abovementioned services performed by the client are value adding services and are critical to the business operations of group entities. Any independent third party performing comparable services would have cross-charged not only the cost of such services, but would have earned a remuneration linked with the revenue or profits of group companies.

We assisted the client by suggesting the appropriate price range which the Client should adopt for different services rendered to the group entities. This included:

- Understanding and documenting detailed functional analysis for each department / service line of the client;
- Identifying key value-adding functions performed by the Client and assisting in arriving at an appropriate pricing model for each function;
- Analysing comparable agreements for similar revenue/ profit linked pricing models;
- Suggesting appropriate price range which the Client can adopt for its different services / functions.

Our efforts also involved an extensive analysis of large number of agreements to ascertain comparability.

Based on thorough analysis of the clients operations and regular meetings with the management we were able to estimate the remunerations under various pricing models based on revenue projections. After critical analysis and evaluation of each model we suggested an appropriate pricing model that would take into account the functions performed and risks assumed by the client.

From the judiciary

This Section focusses on some of the interesting case laws reported on transfer pricing during the quarter, April-June 2017

Luxottica India Eyewear Pvt Ltd vs. ACIT

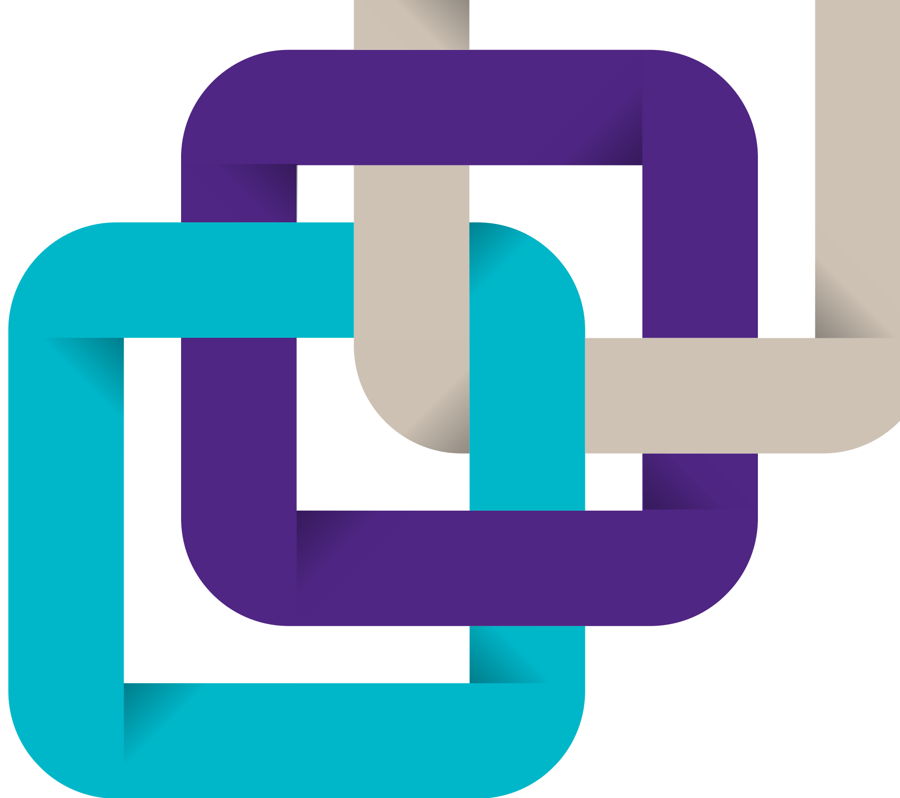
AY: 2010-11 & 2011-12, Delhi ITAT Bench

Facts of the case:

- The assessee is a part of Luxottica group which is a leader in design, manufacture and distribution of sun glasses and prescription frames in mid and premium price categories.
- The assessee entered into international transactions relating to purchase of goods and reimbursement of expenses to and from AEs. The TPO considered AMP expense as a separate international transaction and subsequently benchmarked it using BLT. Resultantly an adjustment was proposed for AY 2010-11 and AY 2011-12.
- The assessee initially argued that AMP expense is not an international transaction and hence there is no question of making adjustment relying on the judgments of Maruti Suzuki India Ltd (2015) 129 DTR 25 (Del) and Whirlpool of India Ltd (2015) 94 CCH 156 Del – HC.
- The DR on the other hand relied on the Delhi HC judgment of Sony Ericson Mobile Communications (India) Pvt. Ltd. (2015) 374 ITR 118 (Del) wherein the matter was restored for ALP determination after considering AMP expense to be a separate transaction. Further the DR also relied on jurisdictional HC in Yum Restaurants (India) Pvt Ltd (2016) 380 ITR 637 (Del) wherein the matter was restored for determining whether AMP expense is an international transaction. Also even in assessee's case for the preceding year, the matter was restored for fresh adjudication. In light of above and several other cases it was pleaded that the matter be restored for a fresh adjudication.
- Further, the Assessee representative ("AR") contended that the TPO for AY 2012-13 has not made any adjustment on account of AMP expenses but has factored in the AMP intensity adjustment in the profit margin of the comparables. The AR pleaded that instead of remitting the matter for deciding the existence of an international transaction and then determining the ALP, the matter should be remitted with a direction to carry out AMP intensity adjustment in line with the view taken by TPO in AY 2012-13.

ITAT observation and ruling:

- The Tribunal was not convinced with the proposition of AR regarding AMP intensity adjustment. Additionally, the facts of the instant appeals were similar to the assessee's own case of preceding year. Hence considering the same, the matter was remitted back to AO/TPO for fresh adjudication in light of directions given by the Tribunal in its order for the immediately preceding year.



For AY 2012-13

Facts of the case:

- The TPO has not considered AMP expense as a separate transaction in AY 2012-13, instead an adjustment was made in the international transaction relating to 'Import of finished goods' on account of AMP expense which was referred to as AMP intensity adjustment.
- The Ld. TPO argued that there was creation of marketing intangibles in favour of the AE by carrying out huge AMP expenses whereas the comparables selected by the assessee were carrying out low or negligible marketing functions. The excess intensity of AMP expense in assessee's case as compared to the comparables was sought to be adjusted by carrying out an AMP intensity adjustment in the following manner. First AMP intensity adjustment was carried out in the profit margin of comparables through which an adjusted average margin of 6.03 per cent was computed. Then the arm's length cost was calculated in a backward manner. Thereafter the difference between arm's length cost and actual cost was proportionately allocated to the AE segment on the basis of purchase of material.
- The assessee accepted TPO's approach of carrying out AMP intensity adjustment in the profit margin of comparables. However, the assessee objected computation of TP adjustment by contending that total operating expenses including indirect costs should be used as denominator instead of total cost of material consumed only.
- The TPO proposed that TNMM should be applied as the most appropriate method instead of RPM whereas the assessee relied on the judgment given in its own case for AY 2009-10 wherein RPM was selected as the most appropriate method by the TPO.

ITAT observation and ruling:

- With regard to AMP intensity adjustment, assessee's contention was rejected by pointing that the components of numerator and denominator have to remain same. Since the numerator consists of purchase cost of materials from AEs (which is not disputed by assessee), denominator cannot be any figure other than purchase cost of material consumed, purchased from both AEs as well as non AEs.
- With regard to selection of MAM, in AY 2009-10, TPO considered AMP expenditure as a separate transaction, therefore there was no need to subsume the AMP function in the determination of ALP. In the present year, RPM should be applied as the MAM provided it appropriately encompasses the effect of AMP intensity adjustment.

Hyundai Motors India Limited vs. DCIT

AY 2009-10, 2010-11 & 2011-12, Chennai ITAT Bench

Facts of the case:

- The assessee is a fully owned subsidiary of Hyundai Motor Company ('HMC'). It is engaged in manufacturing cars in India under the brand name 'Hyundai', which is legally owned by HMC. The TPO opined that due to usage of trademark Hyundai in every vehicle manufactured by it, there was development of the brand name in India. This brand development in India led to accretion in the brand value of Hyundai globally which benefitted HMC, being the legal owner of the brand.
- The assessee did not receive any compensation from HMC towards accretion in brand value and hence an adjustment was made by the TPO.
- On an appeal before DRP the adjustment amount was reduced
- A total of six appeals and one cross objection was filed before the Tribunal which were taken up in unison. A cross objection filed by the assessee for the AY 2011-12 was not maintainable by the Tribunal for the reason that the cross objection was filed against the order of the AO. The Tribunal invoked the provisions of Sec 253(4) and held that a cross objection can only be filed to challenge the order passed by the CIT (A).
- The twin issues in question before the Tribunal were whether:
  - The assessee was obligated to use the brand name Hyundai for promoting the same or for benefitting from the reputation of the same.
  - The incidental benefit accruing to HMC due to accretion in the brand value can be considered to be an international transaction

ITAT observation and ruling:

- It is a settled position that the assessee is not incurring excessive AMP expense in comparison to its competitors, hence the rulings of LG's special bench and Maruti Suzuki India are not applicable in this case as the facts are materially different.
- The increase in brand value is not due to any conscious efforts taken by the assessee but is instead triggered from sale of cars as it creates more brand visibility. While AMP expense is a conscious effort for increasing brand value, in this case the increase in brand value is a by- product of the economic activity undertaken by the assessee i.e. selling cars with 'Hyundai' logo.
- The obligation to use the brand name as per the technology agreement is essential to protect the intellectual property owned by AE and even in arm's length method, transaction is fully justified. Moreover, the brand enjoyed a favourable global reputation, which was leveraged by the assessee in India.
- Accretion in the brand value was viewed from following three aspects to analyse whether the same falls under the purview of international transactions:
  - In the nature of purchase, sale or lease of tangible or intangible property: Accretion of brand value did not result in purchase, sale, transfer, lease or use of intangible property. Even the extended definition does not cover 'accretion to value of intangible'.
  - In the nature of provision of service: Provision of service requires conscious efforts rather than a passive exercise. Use of brand name is allowed as a privilege to the assessee and a privilege to the assessee cannot be a service by the assessee. Hence accretion in brand value cannot be classified as a service transaction.
  - In the nature of any other transaction having a bearing on profit, incomes, losses or assets of such enterprises: Unless a transaction affects profits, losses, income or assets of both the enterprises, it cannot be termed as an international transaction. Further, accretion in value of brand owned by HMC neither results in any specific cost nor does it have any impact on income, expenditure, losses or assets of the assessee, thus the transaction does not fall even in this category.
- Following its noting, ITAT upheld assessee's contentions for deletion of adjustment on account of increase in value of brand as it fails to classify as an international transaction.

Pangea3 & Legal Database Systems Pvt. Ltd. Vs Income Tax Officer

AY: 2009-10, Mumbai ITAT Bench AY: 2009-10, Mumbai ITAT Bench

Facts of the case:

- The taxpayer, a registered STPI unit with Software Technologies Parks of India, is engaged in rendering ITeS services in the nature of legal support services, data processing, legal database, and other administrative support services to its AE. The taxpayer selected TNMM as the MAM and OP/OC as PLI.
- While computing the PLI, the taxpayer excluded foreign exchange loss of INR 3.41 crores and determined its operating margin at 15 per cent.
- The TPO recast the PLI at 2.83 per cent claiming that the taxpayer had wrongly treated forex loss as non-operating item of expense and proposed an adjustment of INR 8.64 crores. On an appeal to the DRP, the adjustment was reduced to INR 5.26 crore. Aggrieved, the taxpayer and revenue filed cross appeals before the Tribunal.
- Before the Tribunal, the taxpayer argued that, in contrast to the comparables, the taxpayer's loss was abnormal. In majority of the comparables, due to unavailability of data in the public domain relating to the forex gain/loss, it was difficult to carry out reasonable accurate adjustments in the margins of the comparables. Accordingly, the adjustment should be carried out in the PLI of the tested party.

ITAT observation and ruling:

Issue	TPOs Argument	Tribunal's Ruling
Adjustment in tested party	Comparability adjustment to weed out any differences can only be made in case of comparables and not in case of the tested party.	• ITAT ruled that in absence of reliable data for a particular cost or profit, reasonable accurate adjustment in the hands of tested party may throw fruitful results. • Adjustment can be made in two kinds of situations: – Between the international transaction and third party comparables, or – Amongst the transactions between the AEs. • Referring to 10B(e) ITAT held that "Nowhere the rule suggests that the adjustment which materially affects the price or cost or profit should be made only to the uncontrolled transaction, that is, comparables and not to the 'tested party' whose transactions is being compared". • Hence, the Tribunal concluded that adjustment can be made in the comparables as well as the tested party.
Nature of foreign exchange loss/gain	• When transactions are entered in foreign currency and the taxpayer is maintaining books in Indian currency, the forex loss/gain forms a part and parcel of such transaction and cannot be separated and given a different treatment • The Tribunal has consistently held that forex gain/loss arising out of international transaction is in the nature of operating profit/cost.	• It was held that, when international transactions are entered into with an AE, one of whom is a resident of other contracting state and the transactions are in foreign currency, then any gain or loss on account of forex is inherent item of cost or profit. • Foreign exchange loss is always an operating item as it is closely related with the underlined transaction
Adjustment on account of loss on cancellation of foreign exchange contracts	• Once an item is appearing as an operating cost, then any part of the cost cannot be excluded in the garb of making comparability adjustment. • Risk on account of forex would be similar between taxpayer and the comparables. • Placing reliance on OECD commentary, the revenue argued that hedging loss has to be necessarily given the same treatment as the loss or gain on the underlined transaction.	• In case of any difference or abnormality or any extraordinary item which materially affects the cost base or profit, PLI needs to be adjusted to eliminate the material effect of such difference. • Risk assumed by comparables and the taxpayer may be similar in nature but differ in quantum and scale. The material differences affecting the cost or profitability need to be eliminated.

Principal Commissioner of Income Tax vs. Kusum Health Care Private Limited

AY: 2010-11, Delhi High Court

Facts of the case:

- Kusum Health Care Private Limited ('Kusum Health Care' or 'assessee') is a company engaged in manufacturing and trading of pharmaceutical products with its overseas AE and third parties.
- During FY 2009-10, the assesse reported two international transactions namely export of manufactured medicines and export of traded medicines to its AE in Ukraine.
- In its transfer pricing documentation, the assesse determined the ALP of the above mentioned international transactions by selecting TNMM as the MAM for the manufacturing and trading segment and OP/TC as the PLI.
- During tax assessment, assessee's case was referred to the TPO for determination of :
  - ALP. The TPO accepted the above transactions to be at arm's length using TNMM. However, he imputed interest (@ SBI prime lending rate + 300 basis points) on the receivables outstanding from AE for a period exceeding 180 days as agreed in the inter-company agreement and made an adjustment.
  - The assessee filed its objections against the adjustment before the DRP which principally upheld the TPO order, however directed the TPO to apply interest on outstanding receivables @ SBI prime lending rate + 150 basis points.
  - Aggrieved by the order of AO/ TPO, assessee appealed before the ITAT.

ITAT observation and ruling:

S.No	Assessee's Main Contentions	ITAT's Observations/ruling
1	• WCA takes into account the impact of outstanding receivables on the profitability: • Reliance placed on OECD which opines that WCA is an attempt to adjust for differences in the time value of money between the tested party and comparables. • Placed reliance on various supporting case laws wherein the principle of undertaking WCA was upheld	• Appropriate adjustments need to be considered to bring parity in WC investment of the assesse and the comparables rather than looking at the receivable independently. • WCA takes into account the impact of outstanding receivables on the profitability. • If the pricing/ profitability of the assesse are more than the WCA margin of the comparables, the imputation of interest on outstanding receivables is not warranted. • Major reliance placed on the decision of Ahmedabad ITAT in the case of Micro Ink Ltd.
2	• Principle of aggregation is a well-established rule in the transfer pricing analysis. The principle seeks to combine all functionally similar transactions for determination of ALP: • Reliance placed on OECD guidelines for aggregation of transactions: • Placed reliance on various supporting case laws wherein the principle of aggregation was upheld.	• Relying on the ratio laid down by Delhi HC in the case of Sony Ericsson Mobile Communication India Pvt. , ITAT held that the approach by the assesse of aggregating the international transaction pertaining to sale of goods to AE and receivables arising from such transactions is in accordance with established TP principles.
3	• No interest has been charged on the overdue balances from unrelated third parties as well	• No specific finding on this contention.
4	• Re-characterisation of a transaction and imputing notional interest on a fictional transaction in not permissible under the Act	• No specific finding on this contention

Based on the above, the ITAT held that the higher profit margins earned by the assessee in comparison to the working capital adjusted margins of the comparable companies more than compensated the assessee for the credit period extended to the AE. Accordingly, the case was decided in favour of the assessee and the adjustment made by the AO/ TPO was deleted.

High Court Ruling:

Aggrieved by the decision of the ITAT, the revenue filed its appeal before the Hon'ble Delhi HC on the ground that the ITAT overlooked the fact that the expression "international transaction" as defined in Explanation (i)(c) to Section 92B of the Act includes "payments or deferred payments or receivable or any other debt arising during the course of business" and accordingly they separately constitute an international transaction.

HC affirming the ITAT order in principle ruled as below:

- The expression 'receivable' in the explanation to Section 92B of the Act does not mean that
- de hors every item of receivable arising from the dealings with foreign AEs would automatically be characterised as an international transaction. Further, the HC observed that a delay in collection of money may be due to different reasons and require investigation on a case to case basis.
- What needs to be analysed is the pattern that may emerge from the receivables over a period of time which indicate that the arrangement of parking huge receivables with the related parties reflects an international transaction with underlying intent to benefit the AE.
- In the present case, since the assessee had already factored in the impact of receivables on its pricing/ profitability by way of undertaking WCA to comparable companies' profit margins; any further adjustment for outstanding receivables would distort the picture and re-characterise the transaction.
- Relying on Delhi HC ruling in the case of EKL Appliances Ltd. (2012) 345 ITR 241(Delhi), the HC held that characterisation of a transaction is impermissible in law.

Tracker

I. Notifications/ press releases

India Signs the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("BEPS")

On June 7, 2017 India signed the multilateral convention to implement measure to BEPS Action Plans. The MLI covers measures relating to following Action plans:

- **Action 2 -** Neutralising the effects of hybrid mismatch arrangements
- **Action 6** - Preventing the Granting of Treaty Benefits in Inappropriate Circumstances
- **Action 7** - Preventing the Artificial Avoidance of Permanent Establishment Status
- **Action 14** - Making Dispute Resolution Mechanisms more effective

India has listed its treaties with 93 countries in the provisional list of Covered Tax Agreements. This represents virtually all its comprehensive tax treaties.

CBDT issues revised Safe Harbour Rules w.e.f. April 2017

The notification moderates the safe harbour for all industries except auto and introduces safe harbour for low value adding services. The revised rules are applicable from AY 2017-18 and have reduced the exercise period of the safe harbour from 5 years to 3 years.

CBDT notifies rules for Secondary Adjustment

The rules provide that the excess money should be repatriated to India within 90 days from the relevant date. In case of failure to do so, interest would be imputed at:

- Marginal Cost of lending rate of SBI+325 basis points where the transaction is denominated in Indian currency
- 6 month LIBOR rate+300 basis points, in case of foreign currency denominated transaction

Tolerance Range For AY 2017-18 and 2018-19

The Govt. has retained tolerance range for AY 2017-18 and AY 2018-19 at 1 per cent for wholesale traders and 3 per cent for all other taxpayers vide notification dated 9 June 2017.

United Nations Transfer Pricing Manual 2017

On April 7, second edition of the UN transfer pricing manual was released. The 2017 edition, divided into four parts, includes new chapters on cost contribution agreement and treatment of intangibles. The revised manual also takes into consideration the developments of OECD/G20 BEPS project.

II. Advance pricing agreement ("APA") updates

India's Advance Pricing Agreement regime Moves Forward with Signing of More APAs by CBDT

S.No	APAs signed till date
Bilateral APA	• 12
Unilateral APA	• 150

CBDT releases Advance Pricing Agreement Annual Report: 2016-17

As the APA programme enters into its 6th year, the CBDT has released an Annual Report on the APA Programme providing key insights on its progress in the first five years of its implementation (i.e. from FY 2012-13 to FY 2016-17) in a single report. The report states that a total of 815 Applications have been filed in 5 years, out of which 152 agreements have been signed.

CBDT amends clauses 3 and 4 of Form No. 3CED (Application for APA)

As per the notification, taxpayers will now be required to specify name, address, country of residence and unique identification number of the AE. Further, disclosure regarding immediate as and ultimate parent companies of applicant is also required.

III. Grant Thornton Publications

Navigating the Revised Indian Safe Harbour Rules

The article analyses the Safe Harbour scheme in India in light of the revised safe harbour rules.

IV. Grant Thornton News Flashes:

- APA Annual Report
- High Court ruling in case of Kusum Healthcare Pvt. Ltd
- Revised Safe Harbour Rules

Global corner

This Section narrates Grant Thornton India LLP ("Grant Thornton"/ "GTILLP")'s experience in formulating effective Transfer Pricing planning studies.

A. Updates from Singapore:

I. Evolving Transfer Pricing regime in Singapore

- **2006-2009**

The Inland Revenue Authority of Singapore ("IRAS") issued the first set of transfer pricing guidelines in 2006. These were supplemented by subsequent circulars and enacted in law as follows:

- Administrative guidance on APAs in 2008
- Administrative guidance on transfer pricing consultations in 2008
- Transfer pricing guidelines for related party loans and services in 2009
- A new transfer pricing provision, Section 34D was incorporated into the Singapore Income Tax Act in 2009 in respect of transactions not at arm's length

- **2015**

On 6 January 2015, the IRAS released revised transfer pricing guidelines ("2015 Singapore TP guidelines"). The new comprehensive guidelines replaced transfer pricing guidelines issued in 2006 and all previous circulars and guidelines issued in 2008 and 2009.

The publication of the 2015 Singapore TP Guidelines was considered to be the most significant development in Singapore's transfer pricing landscape since the issuance by the IRAS of its transfer pricing guidelines in 2006.

The most striking aspect of the 2015 Singapore TP guidelines was that the IRAS required the taxpayers to prepare and maintain contemporaneous transfer pricing documentation to substantiate that the related party dealings are at arm's length.

- **2016**
- On 4 January 2016, the IRAS released another revised transfer pricing guidelines ("2016 Singapore TP Guidelines"). The 2016 Singapore TP guidelines remain broadly in line with the Transfer Pricing Guidelines issued by the OECD for Multinational Enterprises and Tax Administrations ("OECD Guidelines").
- The key changes that were introduced by the 2016 Singapore TP Guidelines were centred around the APA process, MAP process and application of cost plus method.
- Further, on 10 October 2016, the IRAS released an e-Tax Guide with details on the implementation of CbC reporting for Singapore MNE groups. The guidelines issued by the IRAS are largely in line with the guidelines recommended by OECD in the final BEPS Action 13.

- **2017**

On 12 January 2017, the IRAS released yet another revised transfer pricing guidelines ("2017 Singapore TP Guidelines"). Key features include more guidance on the arm's length principle and emphasis on risks, additional information requirements to be included in transfer pricing documentation, changes to the MAP and APA programs and the introduction of an indicative margin or "safe harbour" for related party loans.

II. Transfer pricing requirements in Singapore

- **Transfer Pricing Documentation Compliance Requirements:**

The Singapore Transfer Pricing Guidelines include a requirement for taxpayers to prepare contemporaneous transfer pricing documentation when taxpayers' related party transactions exceed any of the following Singapore dollar value thresholds:

Category of related party transactions	Category of related party transactions Threshold (SGD) per financial year
Purchase of goods from all related parties	15 million
Sale of goods to all related parties	15 million
Loans owed to all related parties	15 million
Loans owed by all related parties	15 million
All other categories of related party transactions, including: Service income Service payment Royalty income Royalty expense Rental income Rental expense For the purpose of determining if the threshold is met, aggregation should be done for each category of related party transactions. For example, all service income received from related parties is to be aggregated.	1 million per category of transactions

Further to the above thresholds the 2015 Singapore TP guidelines has also provided exemption form the documentation requirements in the following situations:

- Where the taxpayer transacts with a related party in Singapore and such local transactions (excluding related party loans) are subject to the same Singapore tax rates ;
- Where a related domestic loan is provided between the taxpayer and a related party in Singapore and the lender is not in the business of borrowing and lending;
- Where the taxpayer applies the safe harbour 5 per cent cost mark-up for services that qualify as 'routine' services as defined in the guidelines ; and
- Where the related party transactions are covered by an agreement under an advance pricing agreement.

- **Definition of 'contemporaneous' transfer pricing documentation**

The IRAS defined contemporaneous to mean "documentation and information that taxpayers have relied upon to determine the transfer price prior to or at the time of undertaking the transactions."

The IRAS further clarified that it would also accept as contemporaneous TP documentation, "any documentation prepared at any time no later than the time of completing and filing the tax return for the financial year in which the transaction takes place".

- **Maintenance and update of documentation**

The IRAS requires contemporaneous transfer pricing documentation to be prepared by no later than the tax return filing date of the financial year in which the transaction takes place. Whilst the IRAS does not require taxpayers to submit TP documentation along with the tax returns, the 2015 Singapore TP guidelines stated that taxpayers have 30 days to submit the documents upon the IRAS' request.

- **Consequences of not preparing contemporaneous documentation**

In the event that documentation is not provided, or if taxpayers are unable to substantiate that their transfer prices are concluded at arm's length with their TP documentation, the following consequences could apply:

- Penalties may apply if taxpayers fail to provide TP documentation upon request by the IRAS. Such penalties will be invoked under prevailing laws concerning record keeping
- An upward adjustment may be made in the event the IRAS establishes that taxpayers have understated their profits through improper transfer pricing
- The IRAS may not support taxpayers in Mutual Agreement Procedure (MAP) discussions in the event taxpayers suffer double taxation arising from any transfer pricing audit by the IRAS or foreign tax authorities

- The IRAS may not accept the application of an APA in the absence of proper TP documentation
- The IRAS may not accept taxpayer/self-initiated transfer pricing adjustments in the absence of proper TP documentation.

III. Significant updates

- **Country-by Country ("CbC") reporting**

The IRAS has aligned its Transfer Pricing Guidelines with the IRAS' e-Tax Guide on Country-by Country Reporting issued on 10 October 2016 by incorporating the obligation of the ultimate parent entity of a Singapore MNE group to file a CbC Report), if the reporting threshold is met. This is in addition to complying with contemporaneous TP documentation requirement.

Singapore will implement CbC reporting for Singapore MNE groups from 1 January 2017 onwards. CbC reporting provisions will be applied to MNEs where:

i. The ultimate parent entity of the MNE group is a tax resident in Singapore;

ii. Consolidated group revenue for the MNE group in the preceding financial year is at least S$1,125 million; and

iii.The MNE group has subsidiaries or operations in at least one foreign jurisdiction.

CbC Report must be filed within 12 months from the end of the ultimate parent entity's financial year. The template for the information to be submitted in the CbC report consists of three tables, which are as per the BEPS Action 13 recommendation.

- **Indicative margins for related party loans**

The IRAS has for the first time introduced a safe-harbour administrative practice for related party loans not exceeding the equivalent of SGD15 million. To facilitate compliance with and adherence to the arm's length principle, the IRAS has put in place an indicative margin which taxpayers may apply on an appropriate base reference rate (e.g. LIBOR) to price the interest on their related party loans obtained or provided from 1 January 2017.

If taxpayers choose to apply the indicative margin for their related party loans, they are not expected to prepare TP documentation for these loans, and such loans will also be excluded when determining the safe harbour loan threshold of SGD 15 million.

The indicative margin will be published on the IRAS' website and will be updated at the beginning of each year, and is applicable to each Singapore-dollar or foreign currency denominated related party loan that does not exceed SGD 15 million at the time the loan is obtained or provided.

- **Disclosure of unilateral APAs in TP documentation and Adoption of BEPS Action 5 (Standards on countering harmful tax practices)**

On contents that should be included in TP documentation, the IRAS has set out for the first time its requirement that taxpayers include in their contemporaneous TP documentation, a copy of the existing unilateral and bilateral / multilateral APAs and other tax rulings to which the IRAS is not a party and which are related to related party transactions subject to the TP documentation.

On exchange of information, the IRAS will spontaneously exchange information on cross-border unilateral APAs under tax treaty or exchange of information instrument, subject to certain conditions, with:

a. Jurisdictions of residence of all related parties with whom the taxpayer enters into transactions that are covered by the unilateral APAs; and

b. Jurisdictions of residence of the taxpayer's ultimate parent entity and the immediate parent entity.

Generally, information relating to unilateral APAs issued before 1 April 2017 will be exchanged by December 2017. Those issued after 1 April 2017 will be exchanged within three months after the date of agreement.

B. News from around the world:

I. ATO's win in Chevron case

The Australian Federal Court has ruled against Chevron Australia Holdings Pty. Ltd. on inter-company financing arrangements in which the interest paid by Chevron Australia to its foreign affiliate Chevron US based on 1 month AUD LIBOR basis plus 4.14 per cent (i.e. 9 per cent) on USD 2.5 billion loan was termed to be not at an arm's length. According to the Credit Facility Agreement, there was no financial or operational covenants, neither did it have any security against the funds supplied by Chevron US to Chevron Australia nor there was any guarantee given by the UPE. The Federal Court held that interest payments to be excessive and imposed a penalty for the same.The ultimate parent entity of the MNE group is a tax resident in Singapore;

II. European Parliament passes public CBC proposal

The European parliament has approved draft proposal requiring MNEs with turnover above EUR 750 million to publicly disclose tax paid in each country by them. MNEs would be allowed to apply to authorities for exemption in member states.

III. Updates from OECD

Action 13: Country by Country Reporting

- **Further guidance on implementation of CbC reporting by OECD**

The guidance clarifies that:

- Definition of revenue to include extraordinary incomes from investments.
- To determine existence and membership of group, Local GAAP or IFRS may be applied
- Related parties are to be interpreted as Constituent entities in Table 2 of CBC report
- **CBC reporting implementation status and exchange relationships.**

The OECD released a complete list of agreements between various jurisdictions for automatic exchange of CBC reports. More than 700 automatic exchange agreements have been established and activated

Action 7: Preventing the Artificial Avoidance of PE Status

The OECD has released a discussion draft on 22 June 2017, providing additional guidance on creation of PE and the resultant attribution of profits to PE in cases as stipulated in Article 5(5) of the OECD Model Tax Convention on Income and on Capital

Action 8- 10: Transfer Pricing

- **Hard to value intangibles ("HTVI")**

The OECD released a discussion draft on pricing of HTVI. The guidance provides examples illustrating the suggested approaches and also addresses the interaction between HTVI and MAP procedures.

- **Revised Guidance on Profit Splits**

The revised draft clarifies the application of the transactional profit split method ("PSM"), by identifying indicators for its use as the most appropriate TP method. It provides additional guidance on determining the profits to be split through various illustrations.

Citations

Case law	Citation
ZTE Corporation vs ADIT	ITA 5870/Del/12 & ors
Arrow Electronics india Ltd. Vs. ADIT	I.T (TP).A Nos.209 & 210/Bang/2011 Cross Objection Nos.31 to 33/Bang/2011 I.T (TP).A Nos.617 to 619/Bang/2011
Anglo-French Textile Co. Ltd Vs. Cit	1953 AIR 105, 1953 SCR 454
GE Energy Parts Inc vs. ADIT	ITA No. 3605/De/2013
Hukumchand Mills Ltd. vs CIT	ITA No.671/Del/2011
Director of Income-tax (International Taxa-tion) v. Morgan Stanley & Co.	1968 70 ITR 450 Bom
DDIT Vs. Nipro Asia Pte Ltd.	ITA No.4078/Del/2013
Rolls Royce Singapore Pvt. Ltd.	ITA Nos. 855 to 861/Del/2009 ITA Nos. 1109 to 1113/Del/2009
Rolls Royce Singapore Pvt. Ltd Vs. Adit	ITA 1278/2010,ITA 1280/2010
Hyundai Rotem Company (Korea)	[TS-609-ITAT-2016(DEL)-TP]
Luxottica India Eyewear Pvt. Ltd. Vs Acit	ITA No.1492/Del/2015 ITA No.1205/Del/2016 ITA No.344/Del/2017 Cross Objection: ITA No.1117/Del/2015
Hyundai Motor India Limited vs. DCIT	I.T.A. No. 853/Chny/2014 and 563/Chny/2015 I.T.A. No. 739/Chny/2014 and 614/Chny/2015 I.T.A. No. 842/Chny/2016 Cross Objection: I.T.A. No. 761/Chny/2016
Pangea3 & Legal Database Systems Pvt. Ltd. Vs ITO	ITA No 2128/M/2014
ITO vs. Pangea3 & Legal Database Systems Pvt. Ltd.	ITA No 1958/M/2014

Glossary

Abbreviations	Full name
AE	Associated enterprises
ALP	Arm's length price
AMP	Advertisement Market-ing and Promotion
AO	Assessing officer
APA	Advance Pricing Agreement
AR	Assessee Representa-tive
AY	Assessment Year
BEPS	Base erosion and profit shifting
CbC	Country-by-country
CBDT	Central Board of Direct Taxes
CUP	Comparable uncon-trolled price
DRP	Dispute Resolution Panel
DTAA	Double Taxation Avoid-ance Agreement
FAR	Functions, assets and risks
FY	Financial year
GP	Gross profit
Grant Thornton/GTILLP	Grant Thornton India LLP
HC	High court
HTVI	Hard To Value Intangi-bles
IRAS	Inland Revenue Authori-ty of Singapore
IT	Information technology

Abbreviations	Full name
ITAT/Tribunal	Income Tax Appellate Tribunal
ITeS	Information technology enabled services
KPO	Knowledge Process Outsourcing
LO	Liaison Office
MAM	Most appropriate meth-od
MAP	Mutual Agreement Pro-ceedings
MNE	Multinational Enterprise
OECD	Organisation for Eco-nomic Cooperation and Development
OP	Operating profit
PE	Permanent establish-ment
PLI	Profit level indicator
RPT	Related party transac-tion
SDT	Specified domestic transactions
SGD	Singapore Dollar
The Act	Indian Income-tax Act, 1961
The Rules	Indian Income-tax Rules, 1962
TNMM	Transactional net margin method
TP	Transfer pricing
TPO	Transfer pricing officer
UPE	Ultimate Parent Entity
WCA	Working Capital Ad-justment

Contact us

To know more, please visit www.grantthornton.in or contact any of our offices as mentioned below:

NEW DELHI
National Office
Outer Circle
L 41 Connaught Circus
New Delhi 110001
T +91 11 4278 7070

AHMEDABAD
BSQUARE Managed Offices
7th Floor, Shree Krishna Centre
Nr. Mithakali Six Roads
Navrangpura
Ahmedabad 380009
T +91 76000 01620

BENGALURU
5th Floor, 65/2, Block A,
Bagmane Tridib, Bagmane Tech
Park,
C V Raman Nagar,
Bengaluru - 560093
T +91 80 4243 0700

CHANDIGARH
B-406A, 4th Floor
L&T Elante Office Building
Industrial Area Phase I
Chandigarh 160002
T +91 172 4338 000

CHENNAI
7th Floor, Prestige Polygon
471, Anna Salai, Teynampet
Chennai - 600 018
T +91 44 4294 0000

GURGAON
21st Floor, DLF Square
Jacaranda Marg
DLF Phase II
Gurgaon 122002
T +91 124 462 8000

HYDERABAD
7th Floor, Block III
White House
Kundan Bagh, Begumpet
Hyderabad 500016
T +91 40 6630 8200

KOCHI
7th Floor,
Modayil Centre point
Warriam road junction
M. G. Road
Kochi 682016
T +91 484 406 4541

KOLKATA
10C Hungerford Street
5th Floor
Kolkata 700017
T +91 33 4050 8000

MUMBAI
16th Floor, Tower II
Indiabulls Finance Centre
SB Marg, Elphinstone (W)
Mumbai 400013
T +91 22 6626 2600

MUMBAI
9th Floor, Classic Pentagon
Nr Bisleri factory, Western Express
Highway
Andheri (E)
Mumbai 400099
T +91 22 6176 7800

NOIDA
Plot No. 19A, 7th Floor
Sector – 16A
Noida 201301
T +91 120 7109 001

PUNE
3rd Floor, Unit No 309 to 312
West Wing, Nyati Unitree
Nagar Road, Yerwada
Pune- 411006
T +91 20 6744 8800

For more information or for any queries, write to us at contact@in.gt.com

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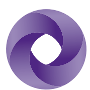

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