TRANSFER PRICING

CA. Bhavesh Dedhia, CA. Shazia Khatri,
CA. Hardik Khowala

ICAI releases revised Guidance Note on Transfer Pricing

The Institute of Chartered Accountants of India (ICAI) through its Committee on International Taxation issued the eighth edition of the Guidance Note on report under section 92E of the Income-tax Act, 1961 (Act), on 20 August 2020. Earlier in June 2020, the said Committee released an exposure draft seeking comments on the amendments proposed. The revised and updated publication incorporates amendments made by the Finance Act 2020 and CBDT notifications.

Updated Guidance Note now incorporates amendments made recently:

- Scope of safe harbor rules (u/s 92CB read with Rule 10TA to 10TF) and Advance Pricing Agreements provisions (u/s 92CC read with Rule 10F to 10T) expanded to cover profit attributable to Permanent Establishment (PE) under section 9(1)(i) of the Act;
- Change in due date with respect to transfer pricing documentation and Accountant's report (Form 3CEB);
- Relaxation to non resident banking companies from the provisions of thin capitalisation (u/s 94B);
- CBDT notification dated 20 May 2020 extending the provisions of safe harbour rules notified earlier for AYs 2017-18 to AY 2019-20 to AY 2020-21.

The Guidance Note is of immense use for all CAs practising in the area of Transfer Pricing in effectively discharging their professional responsibilities.

Reference made for Special Bench constitution to determine meaning of the term "Paid" in Tax Treaty

[Ampacet Cyprus Limited v. DCIT (ITA No. 1518/Mum/16 and 560/Mum/2017)]

The Mumbai Bench of Income Tax Appellate Tribunal (ITAT) recently made a reference to the President of Mumbai ITAT, for constitution of the Special Bench for assigning meaning to the term 'paid' used in the Article 11 on 'interest' in India-Cyprus Double Taxation Avoidance Agreement (DTAA or tax treaty).

In the facts of the case, the Appellant, a company incorporated in Cyprus, advanced loan to its Indian subsidiary. During the impugned assessment years, the Indian subsidiary had not paid interest on loan to the Appellant due to moratorium provided on interest payments in the loan agreement. However, the Transfer Pricing Officer (TPO) disregarded the moratorium and proposed an adjustment for the notional interest to the Appellant's income. Subsequently, the Hon'ble Dispute Resolution Panel (DRP) upheld the view of the TPO. Aggrieved by the action of the TPO and DRP, the Appellant challenged the adjustment on the ground that tax can only be levied under Indian-Cyprus treaty, if the interest is actually paid because of use of term 'paid' in the Article 11 of the treaty. The Appellant further placed reliance on several decisions of the ITAT, wherein it was held that the DTAA provides for taxability of interest, royalty and fees for technical services only on cash payment basis.

In this context, the ITAT observed that the term 'paid' is not defined in the Indian-Cyprus treaty, but Article 3(2) of the treaty provides that unless the context otherwise requires, the definition of the undefined treaty term should be adopted from the domestic law of the source country i.e. India in the present case. Accordingly, definition of the term "paid" under section 43(2) of the Income-tax Act, 1961 (Act) may be relevant. However, the ITAT opined that this meaning cannot be imported in the tax treaty mechanically, without any application of mind and hence, it calls for a larger bench to adjudicate whether or not this domestic tax law meaning of the expression 'paid' will be relevant. The ITAT further observed that all the decisions relied upon by the Appellant were rendered without

considering the Article 3(2) and in ignorance of the judgment passed by the Apex Court in case of Standard Triumph Motor Co Pvt Ltd v CIT (1993). Accordingly, the ITAT recommended constitution of a 3 member Special Bench to adjudicate on the issue.

In the past, similar issues have been matter of litigation before the Courts/ ITAT, wherein it was held that where the tax treaties provides for a particular income to be taxed on receipt/ cash basis, it cannot be fallaciously made chargeable to tax on accrual basis and lead to invoking of transfer pricing provisions. Further, it is a well-established principle that Section 92 of the Act, not being a complete code in itself, only provides a mechanism for computation to arrive at arm's length of the "income", which find its home in one of the substantive charging provisions being Section 4 and Section 5 read with Section 15/ Section 22/ Section 28/ Section 45/ Section 56 of the Act along with the provisions of DTAA with respective country. In view of the same, the may non-resident taxpayers (by placing reliance on the such rulings) have been adopting a position that the transfer pricing provisions are not applicable in absence of any income chargeable to tax in given year (i.e. where income has not been received in cash).

Accordingly, though there have been several judgements till date which have held that only the interest which has actually been paid/received can only be the subject matter of taxation and no transfer pricing adjustment can been made on some hypothetical payable/receivable amount, the adjudication and ruling by a Special Bench on this matter shall of significant importance and shall be awaited with great interest by the taxpayers and tax advisors.