

Budget 2023-24 Expectations

Transfer Pricing Perspective

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Background

The Budget 2023-24 is the last full budget of the current government before the 2024 general elections. With the current global slowdown and with India's 5 trillion economy target, this budget is key on various frontiers. The following are the expectations of the Budget 2023 announcements from a Transfer pricing perspective.

Expectations

Advance Pricing Agreement (APA): APAs have been on the forefront as a mechanism for dispute prevention with respect to Transfer Pricing. However, of late there has been increase in the inventory of pending cases with reasons including lack of allocation of sufficient manpower towards this programme by the government. In this direction, it is expected that government would provide increased resources to expedite the process.

In addition, the CBDT can also consider use of formulaic approach to conclude on the relative less complex or simple APA cases. This approach can be specific to industry having parameters relevant for respective sector or sub-sector, as applicable. Similar formulaic approaches were adopted in other instances which include conclusion of significant MAP cases by India with partner countries– where a regression-based approach / model was used to arrive at the arm's length mark-ups for captive IT/ITeS services in India, and public consultation by the OECD on Amount B of Pillar One – where mechanical pricing tool approach was considered as an output option for benchmarking of baseline marketing entities.

Further in case of routine transactions, a standard information request for the respective transactions, can perhaps be included during the application itself to facilitate quicker ingestion of information to Tax authorities, thereby lowering the time frame for conclusion of APA.

Pillar One / Two Draft Rules: India has been one of the early adopters of the BEPS (Base Erosion and Profit Shifting) program of the OECD such as three-tier documentation – Master File and Country-by-Country reporting. It can be expected that updates to the Tax legislation be introduced in the upcoming budget to implement Pillar One/Two, further considering that Pillar Two is expected to go live by 2024 globally in line with OECD. Further depending on how the model rules provided by the OECD are implemented will also decide the interplay between Pillar One / Two and transfer pricing regulations. For example, Article 3.2.3 of the model rules on Pillar Two issued by the OECD provides that intra-group transactions between group entities in different jurisdictions should be recorded at the same value and should in alignment with arm’s length principle. In this case, impact of transfer pricing adjustments made during the transfer pricing audits on the computation of GloBE income or loss will have to awaited, depending on the rules to be adopted in Indian tax legislations.

Currently South Korea has implemented Pillar Two rules in its domestic legislations.

Safe Harbour Rules (SHR): These rules were introduced as a dispute resolution mechanism to entice taxpayers entering into international transactions having relatively low value and simple nature of transactions – small taxpayers. However, it has received a lukewarm response. SHR can also aid to lower the APA inventory if the agreed arm’s length price as per the SHR are made competitive. Since there were no changes in the agreed arm’s length price during the COVID pandemic, probability of any revision is limited. Some of the expectations / recommendation on updates in SHR in the budget include:

- ▶ Introduction of royalty as a covered transaction. Royalty expenses have been one of the most litigated international transactions. Similar to low-value adding activities, certain guard rails such as upper cap on the value of royalty transactions, obtaining of Chartered Accountant certificate on the relevant aspects such computation of royalty payments can be included, etc.
- ▶ Benchmarks for intra-group loans have been benchmarked using LIBOR as per SHR. Updating benchmarks to Alternate Reference Rates (ARR), to align with foreign exchange regulations can be expected, along with appropriate adjustments for movement from LIBOR to ARR.
- ▶ Arm’s length mark-up for knowledge process outsourcing services has been linked to ratio of employee costs to total cost. Post pandemic businesses have moved to hybrid model and correspondingly there has been reduction in overheads incurred such as office rentals, transportation costs for employees and accordingly there would be an increase in the ratio even though the assessee would have been undertaking the same functions. Hence revision in these ratios can be expected.

Ease for Start-up: India’s start-up ecosystem is the second largest globally and boosting of start-ups is key from myriad aspects such as employment, growth, etc. Start-ups often explore foreign markets or at time cater to foreign markets. Hence easing of transfer pricing compliances for start-ups can aid organic growth of Indian start-up ecosystem.

Interquartile range: Arm’s length range in the Indian transfer pricing regulations is 35th to 65th percentile as against globally accepted inter-quartile range. Adoption of inter-quartile range as the arm’s length range would be a move in the positive direction, in alignment with globally accepted practice.

About us



VSTN Consultancy Private Ltd is a boutique Transfer pricing firm with extensive expertise in the field of international taxation and transfer pricing.

Our offering spans the end-to-end Transfer Pricing value chain, including design of intercompany policy and drafting of Interco agreement, ensuring effective implementation of the Transfer Pricing policy, year-end documentation and certification, Global Documentation, BEPS related compliances (including advisory, Masterfile, Country by Country report), safe harbour filing, audit defense before all forums and dispute prevention mechanisms such as Advance Pricing agreement.

We are structured as an inverse pyramid where leadership get involved in all client matters, enabling clients to receive the highest quality of service.

Being a specialized firm, we offer advice that is independent of an audit practice, and deliver it with an uncompromising integrity.

Our expert team bring in cumulative experience of over four decades in the transfer pricing space with Big4s spanning clients, industries and have cutting edge knowledge and capabilities in handling complex TP engagements.



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