Nangia Andersen LLP

Communiqué

Your Quarterly TP Tabloid

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Foreword

In this unlock phase of world's exceptional battle against coronavirus, we hope for your good health and well-being. Despite numerous efforts by the Governments across the globe to provide various relaxations in the current pandemic, the major economies continue to witness double-digit de-growth in their GDP, the economic slump has left a bigger dent than anticipated by anyone across the globe.

Meanwhile, with an endeavour to keep you updated with the current developments in the Transfer Pricing (TP) landscape at both Indian and global fronts, we have come up with this quarterly issue.

At India level, we have discussed the launch of 'Transparent Taxation' platform by our Hon'ble Prime Minister (PM) on August 13, 2020, the release of final version of the Guidance Note on Section 92E of the Income Tax Act, 1961 (the Act) by the Committee on International Taxation of the Institute of Chartered Accountants of India (ICAI). Further, we have discussed the detailed Guidance on Mutual Agreement Procedure (MAP) resolution that has been released by Central Board of Direct taxes (CBDT), which is aimed towards making MAP a more promising alternate dispute resolution mechanism. Furthermore, we have discussed significant Indian rulings pronounced in the previous quarter.

At global level, the Organisation for Economic Co-operation and Development ("OECD") has released the outcome of the third phase of BEPS Plan 13 which analysis Country-by-Country (CbCR) implementation by member nation and indicates strong global progress in efforts to improve the taxation of Multinational Enterprises (MNEs) worldwide. Further, significant TP centric news in different countries and significant TP rulings across the globe have also been discussed in this issue.

Accordingly, towards our objective of being your value-added partners, we discuss the above significant events/ happenings in this quarterly issue as tabulated below:

We hope that our publications are beneficial and help you in understanding the potential impact (if any) of the changes with respect to your business in India. We look forward to your suggestions or feedback that you would like to share with us, at query@nangia.com. Kindly note that information contained within this issue is of general nature and reliance on the same should not be placed without seeking professional advice, especially on litigation matters.

Stay safe and remain healthy.

Rakesh Nangia

Chairman,

Nangia Andersen India Pvt. Ltd

PM unveils 'Transparent Taxation' Platform

The government is putting in relentless efforts for reforming and simplifying the tax system. On August 13, 2020 Hon'ble PM Narendra Modi launched 'Transparent Taxation' platform surrounding faceless assessments, faceless appeals & taxpayers' charter. Through this platform, the Government emphasised on shift from "banking the unbanking, securing the unsecured, funding the unfunded" to "Honouring the Honest" by applying the principal of 'Minimum Government, Maximum Governance'. As part of this scheme, the Government will make extensive use of technology, digital analytics and even artificial intelligence to ease compliance burden, minimise the physical interface between the taxpayers and the tax officials to achieve the objective of providing a seamless, painless and faceless tax administration. The Hon'ble PM also highlighted the need to introspect on low base of taxpayers despite growth in tax filers and the decrease in complexity/ taxation/ litigation and increase in transparency/ compliance/ trust.

The details of the Taxpayers' Charter, faceless assessments, faceless appeals can be viewed in our NewsFlash that can be accessed through the link stated below:

https://bit.ly/3l8ggwh

In the initial scheme of things, considering the complexities involved, cases pertaining to search and seizure, international tax, etc. were not covered.

However, draft of the Taxation and Other Laws Bill, 2020 that was released on September 18, 2020 entirely changes the landscape for Transfer Pricing (TP) assessments as well, as it brings TP litigation also within the folds of faceless assessments scheme. Although conceptually the faceless assessment scheme is a giant step in the history of income tax litigation, it will have to overcome the customary hiccups and implementation challenges considering the intricacies and complication of TP. Some of the key ones are listed below:

- Success of this scheme is directly dependent on quality of written submission along with evidence submitted by the taxpayers without having any opportunity to personally explain and articulate the lengthy submissions in a hearing.

- Success would also directly dependent on the competency of the tax officer to raise pertinent queries in order to elicit correct information on an issue instead of resulting in deluge of irrelevant details or resorting to rowing and fishing. Further, the quality of involved officers would also impact the extent to which submission/ details are understood properly. More so, with TP being always under a specialists officer, the level of understating of complex transactions and business models has to be to the desired benchmark!

- In case these assessments result in high pitched assessments/ ad-hoc adjustments made by tax authorities in absence of proper submissions/ explanations or any gap in understanding of actual facts, then more efforts would be required at first appeal level to set out the correct facts and getting unwarranted additions/ adjustments deleted. With first level appeal also under faceless, the problems can compound if not handled with aptly.

- If such faceless assessment orders are challenged and decided in faceless appeals, with positions being applied with the same paint brush, then the bottleneck could happen at the Tribunal level and we can expect a spate of cases being remanded back. This may thereby increase litigation and pendency of cases.

- The taxpayer would not know the tax officer but the tax officer would know which Company is being assessed. How much impact would this have, that only time will confirm.

Therefore, the success of the scheme lies in its implementation and it becomes imperative for the Government to ensure the same and to make practical modifications, in order to mitigate hardships on the taxpayers. Also, there arises a need to bring out structural change in the mindset of tax authorities, impart the requisite knowledge through trainings and upskilling of the concerned officers in TP, as well as substantially rebuild the infrastructure, including providing adequate IT and administrative (devising of standard operating procedures, etc.) infrastructure system to handle the enormous data, to ensure data confidentiality and to weed out operational challenges.

In sum, the new scheme looks good and ambitious, especially coming at a time when everything is going online. However, it would be important to understand that for the scheme to be successful and to achieve its aim of reducing subjectivity, discretion and to facilitate doing business in India, the key would be in its efficient and smooth implementation in the long run.

ICAI releases Final Section 92E Guidance Note

On August 21, 2020, ICAI's Committee on International Taxation released the Final Guidance Note on report under Section 92E pursuant to draft Guidance Note released in June 2020. It subsumes amendments made by Finance Acts 2019 and 2020 pertaining to secondary adjustment and enhanced scope of Advance Pricing Agreement (APA) including income Under Section 9(1)(i) of the Act relating to profit attribution to permanent establishment (PE) and Rules 10DA and 10DB of the Income Tax Rules, 1962 (the Rules). The Guidance Note also captures the CBDT Notification dated May 20, 2020 for extending applicability of Safe Harbour Rules notified earlier to AY 2020-21, etc.

The Guidance Note released by ICAI can be accessed using the link below:

https://www.icai.org/new_post.html?post_id=16763

CBDT releases detailed MAP Guidance

On August 7, 2020, CBDT's Foreign Tax and Tax Research (FT&TR) division released a detailed MAP Guidance[1]. This is an important step that the authorities have taken to transparently laydown the MAP process for its taxpayers as per the minimum standard obligation under OECD's Base Erosion and Profit Shifting Action Plan 14.

The MAP Guidance is presented in 4 main parts as discussed below:

- **Part A – Introduction and Basic Information**

  This part details on what is MAP, India's treaty network, the broad procedure of filing a MAP application in India along with a comprehensive list of documentation / information to be filed has been provided to avoid multiple subsequent requests later on. Further, it clarifies the interpretation of "Commitment of endeavouring to complete the MAP case within 24 months".

- **Part B – Access and Denial of Access to MAP**

  Access to MAP

  Elucidates the circumstances where MAP can be accessed by Indian and overseas taxpayers. Key examples for tax issues to be covered are:
  - TP Adjustments.
  - Determination of existence of a PE.
  - Attribution of profits to PE, whether admitted or not by the taxpayer.
  - Characterisation or re-characterisation of an income or expenses (like royalty or fees for technical services or interest).

[1] The details on recent amendment to MAP provisions have been captured in our previous issue of the TP Tabloid which can be accessed through the below link: https://bit.ly/3fzeP9d

Further, specific clarification has been provided in certain circumstances as stated below:

- Access to MAP is granted even where domestic anti-abuse provisions are invoked by Indian tax authorities.
- Where order is passed towards default in tax withholding (under Section 201 of the Act)
  - MAP application can be filed however discussion will be taken up only if the regular tax assessment order is passed against the non-taxpayer.

Additionally, it also lists down the few circumstances where India would provide access to MAP but Competent Authority (CA) of India would not negotiate any other outcome than what has already been achieved in such circumstances. It includes Unilateral APA entered by an Indian or foreign taxpayer with the CBDT, where Indian Safe Harbour for TP have been availed and tax return filed accordingly and where an order is passed by Income-tax Appellate Tribunal (ITAT or Tribunal) in respect of the same disputes that are also being examined under MAP.

Denial of Access to MAP

Explains situations where access to MAP is denied such as:
- Expiration of 3 years from the date of notification of action.
- Incomplete MAP applications/ documents/information and errors are not remedied within reasonable time limits.
- If the CAs of India conclude that the objection raised by the taxpayer on the action taken by tax authorities is not justified.
- Where a settlement order has already passed on the same issues by Income-tax Settlement Commission, where Authority of Advance Ruling has ruled on the same issues under a MAP application.

Apart from the above situations, no MAP access shall be provided in respect to issues that are purely governed by India's domestic law and arises due to the implementation of India's domestic legal provisions.

- **Part C – Guidelines on Procedural Technicalities**

Key issues of MAP that have been touched upon in this part of the Guidance Note are:

- MAP resolution cannot go below the returned income and in transfer pricing cases it needs to be in accordance with provisions of sub-section (3) of Section 92 of the Act.
- It covers only the tax to be paid and does not cover disputes on interest and penalties.
- Further, the CAs of India may resolve recurring issues over the years on the same principles but, they do not have power to ensure conformity by the tax authorities to prior MAP resolutions.
- The CAs of India would be obligated to make secondary adjustments part of the MAP resolution in respect of cases pertaining to financial year 2016-17 or thereafter.
- Where bilateral/ multilateral APA has been filed and accepted, it is not admissible to file MAP application.
- The disputes relating to collection of tax demand under MAP to be suspended where India has specific Memorandum of Understanding (MoU) with counter party countries, otherwise regular procedure for stay of demand is to be followed as per domestic law.

- **Part D – Guidelines on Implementation of MAP**

Intimation of acceptance of MAP resolution by taxpayer to be made in 30 days. Resolution to be provided by tax office within one month from the end of the moth in which he receives the letter of the CAs of India having jurisdiction over the case providing the details of the resolution.

The MAP outcomes cannot be implemented in MAP cases where an order of the ITAT (for the same assessment year that has been resolved under MAP) comes to the knowledge of the CAs of India after the MAP has been resolved or is pronounced after the MAP has been resolved but not yet implemented, and the CAs of India would inform their counterparts about the outcomes of the ITAT order and request them to provide correlative relief for the adjustments sustained by the ITAT, if any.

Although, there still remain additional unaddressed aspects such as whether issuance of “show cause notice” or TP order can suffice as a trigger for MAP application or not, etc. But this being the first guidance of the kind in India is certainly a welcomed move that brings out clarity to the various stakeholders by ushering in a more efficient and effective dispute resolution mechanism.

Rulings on impairment of assets and amortization of goodwill

1. Imsofer Manufacturing India Pvt. Ltd. vs DCIT – ITA No. 5158/Del/2015 (AY 2009-10) & ITA No. 1049/Del/2016 (AY 2010-11)

ITAT, New Delhi has upheld the contention of the appellant (engaged in manufacturing of chocolates and other confectionery) by embracing provision for impairment of assets as non-operating expenditure while calculating the operating cost of the Assessee for Assessment Year (AY) 2010-11. The Assessee submitted that the machine purchased for its production was kept as capital work in progress at the year-end as production could not be started and subsequently, the Assessee decided to discard the production-line and sell the machine as scrap. The Assessee further submitted that it created the provision for impairment of losses to reflect the carrying amount of the asset at market price. Considering these facts, the ITAT held that accounting treatment given by the appellant is in confirmation with the Accounting Standards issued by the Institute of Chartered Accountant's of India (ICAI) and opined that provision for impairment of loss is neither a depreciation charge nor amortization on fixed asset but, rather an adjustment made to carrying amount which is reversible in nature. Delhi ITAT further held that provision for impairment of loss is not an operating expense as its neither recurring in nature nor its related to business operation. Further, the Tribunal took reference of provision of Section 92(1) of the Act where income/expense in relation to the international transaction shall be computed at arm's length and in the Tribunal opinion provision for impairment of assets is not an international transaction. On a separate note, the Tribunal, for AY 2009 10, upheld that when the Assessee has incurred significantly higher non-cen-vat-able custom duty as compared to the Assessee, adjustment of custom duty ought to be allowed. Aside from these issues, the Tribunal also adjudicated on capacity utilization adjustment, exclusion/inclusion of potential companies as comparable in favor of the Assessee for AY 2009-10 & AY 2010-11.

Nangia Andersen LLP's Take

Considering the current economic and market conditions, items such as provision for impairment of assets, provision for stock obsolescence, etc. would be forming part of income statement of many taxpayers. Hence, a clarity on the treatment of these for TP Profit Level Indicator (PLI) computation purposes would be required. Though Section 92CB of the Act, i.e. the Safe Harbor provisions does provide the definition of operating revenue and operating cost, it can act only as a guiding principle and is applicable only on eligible Taxpayers who opt for it. The ruling may take us back to the basics for developing the reasons for considering any item as operating or non-operating for PLI computation, however, there is no concrete guidance on factors to be considered and it all boils down to the taxpayer to maintain the detailed documentation around the reasoning for considering any expense item as extraordinary in nature for excluding from the TP-PLI computation.

Detailed analysis of ruling can be accessed at: **https://bit.ly/3l8JWcF**

2. Symantec Solutions Private Limited vs DCIT – ITA No. 565/Mum/2016 & 1907/Mum/2017

Mumbai ITAT has arbitrated on the treatment of amortization of goodwill as non-operating expense in respect of Assessee being a captive service provider engaged in rendering marketing support services, general and administrative services (reported as technical support services) and software development services to the overseas Symantec Group entities for AY 2011-12 and AY 2012-13. The Tribunal observed that the Assessee has reported amortization of goodwill in the Profit & Loss Account, however, has not claimed the same as expenditure while computing the taxable income and disallowed the expenditure suo motto. Assessee placed various ruling on record which dictates that the expenses disallowed cannot form part of the operating expense. Further, the Tribunal acknowledged that in the Assessee' s own case in AY 2013-14, the Dispute Resolution Panel (DRP) has ruled in the favor of the Assessee. Persuaded by the Assessee contention, the Tribunal directed the Transfer Pricing Officer (TPO) to consider amortization of goodwill as non-operating item. Aside this issue, the Tribunal also upheld Assessee's contention that Infosys Limited be excluded from the final set of comparable companies selected by the TPO based on turnover and size.

Nangia Andersen LLP's Take

The treatment of amortization of goodwill in the TP analysis will depend on the detailed Functional, Assets and Risk (FAR) analysis including evaluation of the impact that such goodwill may have on the business of the Taxpayer along with accurate valuation of goodwill, treatment of such goodwill by the Taxpayer and allowance of the amortization of the same by the tax authorities. While there is no current concrete guidance on treatment of amortization of goodwill on a consensus basis on TP side, it boils down to some of the inherent factual factors which needs to be analyzed to take a position for TP analysis.

▪ Rulings on re-characterization of international transaction

3. Essar Power Ltd. vs ACIT – ITA No. 5450/Mum/2018

Mumbai ITAT scrapped the TP adjustment made by the TPO (which was confirmed by the DRP also) with respect to the interest computed on money advanced by Assessee, engaged in power generation, towards share application money to its Associated Enterprise (AE) for AY 2014-15. Mumbai ITAT held that the amount advanced where in fact towards share application money and that the shares have indeed been allotted within a period of six months. The Tribunal relied on its order in the Assessee's own case for AY 2013-14 and also relied on a series of other Tribunal orders of various jurisdiction holding that TPO/ Assessing Officer (AO) does not hold any power to re-characterize the advance given for share application money and allotment of shares as loan transaction, unless supported by any evidence to prove otherwise. Accordingly, the Tribunal deleted the TP adjustment made by the TPO. The Tribunal also ruled on interest charged on outstanding receivable by directing the AO to compute interest on the outstanding receivable from its AE at LIBOR plus 0.5% by applying the LIBOR rate of the country of the AE.

Nangia Andersen LLP's Take

The Income Tax Act doesn't vest any authority upon the TPO/AO to question the commercial expediency of the Assessee or re characterize the underlying transaction unless any material evidence is placed on record to substantiate that substance is different from form. To circumvent any unwarranted re characterization, it becomes crucial for the Assessee to maintain requisite documents such as approvals obtained from RBI for remitting foreign currency, share certificates issued, minutes of any meetings, resolutions, etc. for substantiating the delay for allotment, if any, and issuance of shares. Guidance can also be sought from other statues like Companies Act, FEMA Act, RBI guidelines and from other domestic laws of the country of which the shares are to be subscribed.

▪ Ruling on benchmarking of outstanding receivable

4. Kusum Healthcare Pvt. Ltd. vs ACIT – ITA No. 3717/Del/2017

Delhi Tribunal agreeing with the contention of the Assessee (engaged in manufacturing and sale of pharmaceutical medicine/goods) deleted the TP adjustment performed by the TPO (confirmed by the DRP) by re-characterizing the outstanding AE receivable beyond the period of 180 days as unsecured loan and thereby calculating the notional interest @ LIBOR plus 400bp for AY 2013-14. The Tribunal opined that a mere re-characterization of outstanding receivable into unsecured loan by the TPO on account of delay in realization of receivable cannot be considered as international transaction and that the arm's length price (ALP) determination is required only for actual transaction. Tribunal adhered to the coordinated bench ruling in Assessee own case for AY 2010-11 (upheld by the jurisdictional HC) wherein, it was adjudged that the international transaction pertaining to sale and receivable arising therefrom should be analysed under aggregation approach as both are interlinked. Tribunal further reiterated the observations of aforementioned rulings in Assessee's case that the sales price already takes into account the delayed credit period, notional imputation of interest is unwarranted, and that working capital adjustment nullifies the impact of outstanding receivables on profitability.

Nangia Andersen LLP's Take

As per explanation to definition of international transaction under Section 92B of the Act, outstanding receivables has been included. However, the key debate has been on the interlinked nature of such outstanding to the principal transaction. There have been divergent views from Tribunals all over the country, on whether such outstanding can be considered to be an international transaction. The current ruling highlights an important aspect that outstanding receivables are linked to the principal transaction and further, any effect of such outstanding will be automatically be reflected in the working capital adjustment analysis to determine the profitability/ALP. Nevertheless, as a best practice, It would be advisable to consider and document the factors such as industry practice, market conditions, comparison of credit period extended to AEs and third party customers, financial position backed with establishing arm's length nature of international transaction post working capital adjustment.

Ruling on benchmarking of FCCD denominated in Indian currency

5. Assotech Moonshine Urban Developers Pvt. Ltd. vs DCIT – ITA No. 1749/Del/2017

Delhi ITAT embracing the contention of the Assessee, has rejected the TPO's benchmarking of interest with LIBOR based rate (upheld by the DRP) on Fully and Compulsorily Convertible Debentures (FCCD) denominated in Indian currency issued by the Assessee to its AE for AY 2012-13. The Tribunal observed that the investment agreement and the details filed with RBI clearly indicated that the subscription money has been received by the Assessee for FCCD in INR to be converted into equity shares of the Assessee and also to be repaid in INR. Considering these facts, Delhi ITAT held that, the interest rate should be the market driven interest rate applicable to the currency in which the loan has to be repaid. The Tribunal also noted that the DRP, in the Assessee own case for AY 2014-15, had accepted the plea of the Assessee and held that the interest rate should be benchmarked using the Indian rate and not LIBOR. Thus, the Tribunal allowed the plea of the Assessee and directed that SBI prime lending rate + 300 basis points be considered as the ALP for the purpose of benchmarking the interest transaction. ITAT followed the ruling in the case of Cotton Naturals India Pvt. Ltd. in arriving to its conclusion.

Nangia Andersen LLP's Take

Across the Indian TP litigation landscape, it has been a consistent stand to benchmark the financial transaction denominated in foreign currency at LIBOR based interest rate and Indian PLR (especially SBI) in case of INR denominated transaction. Guidance can be drawn from Rule 10CB of the Rules which states that, for computing the interest income pursuant to secondary adjustment under Section 92CE of the Act, SBI lending rate plus basis point should be adopted in case the international transaction is denominated in Indian currency and likewise LIBOR plus basis point, if the said transaction is denominated in foreign currency. Similarly, Safe Harbor provisions under Rule 10TC of the Rules, mandates use of SBI marginal cost of fund lending rate in case where the intra group loan is denominated in INR. Accordingly, it becomes vital for the AE's to determine the currency in which underlying financial transaction should be undertaken.

Ruling on effect of APA resolution on earlier year litigation

6. Springer India Pvt. Ltd. vs ACIT – ITA No. 6708/Del/2016

Delhi ITAT, in the second round of proceeding, adjudicated that the 'Other Method' as adopted in the APA be adopted as the most appropriate method (MAM) in respect of for AY 2012-13, a year not covered under APA, for the Assessee engaged in publishing, reprinting and distribution of books and journal. In the first round of proceedings, the Assessee had approached the Tribunal disputing the application of Transactional Net Margin Method (TNMM) as the MAM by the TPO against the 'Other Method' applied by the Assessee. Consequently, the Tribunal remanded the matter to the TPO with a direction to decide on the applicability of MAM.

Aggrieved by the decision, Assessee appealed before the jurisdictional HC, who in turn remanded the matter back to ITAT to decide afresh. Subsequently, the Assessee entered into APA under Section 92CC of the Act, with the CBDT wherein 'Other Method' was agreed to be the MAM for all transactions and was applicable for the previous assessment years 2016-17 to 2020-21 and also for roll back period comprising of previous years 2012-13 to 2015 -16. Tribunal after examining the aforementioned facts and also various ITAT decisions, opined that the methodology provided in APA for determination of ALP of international transaction may be adopted for the uncovered year if the FAR analysis remains akin to the covered years. Accordingly, Delhi ITAT directed the TPO to evaluate the resemblance of FAR analysis of the year under consideration to the covered years and upon affirmation, adopt the same methodology.

Nangia Andersen LLP's Take

APA agreements are entered between the Assessee and CBDT the APA authorities based on constructive deliberation on FAR analysis and all other related aspects considered exhaustively. Further, given the FAR analysis being a cornerstone of TP study, it seems reasonable to allow the application of methodology agreed in APA for the period outside the purview of APA as well, provided, provided the FAR analysis and nature of transactions is analogous to the covered period.

Ruling on domestic inter-company loan transaction

7. Regus Business Centre Pvt. Ltd. vs ACIT – ITA No. 6847/Mum/2018

Mumbai ITAT, relying on the coordinate bench ruling in respect of Assessee's own identical case for AY 2012-13, arbitrated in favour of the Assessee on account of intra-company loan transaction and Intra Group Services (IGS) for AY 2014-15. In case of inter-company loan transaction, Mumbai ITAT rejected the TPO's treatment of invoking deemed international transaction under Section 92B(2) of the Act and characterizing the loan advanced by the Assessee to its other fellow domestic subsidiary company as an international transaction.

The Tribunal observed that, Sub-section 92B(2) of the Act got amended via Finance Act 2014 w.e.f. 01/04/2015 by substituting the word 'deemed to be a transaction' with ' deemed to be an international transaction', however, also noted that, the said amendment doesn't impact the concerned AY and thus provision applicable prior to amendment shall continue to apply. Accordingly, the Tribunal held that Section 92B(2) would have to be analyzed in conjunction with Sub-section (1) wherein to qualify the definition of international transaction, either or both of the AE has to be a non-resident and in the instant case, the loan has been advanced by the Assessee to its fellow subsidiary that are domestic entity resident in India. On the issue of IGS, the Tribunal rejected the 'benefit test' applied by the TPO holding that the ALP of IGS cannot be determined at NIL as the benefit test has become redundant, thus restoring the matter back to TPO for fresh adjudication.

Nangia Andersen LLP's take

The current ruling opines on the applicability of the deeming provisions prior to the date of amendment. On the TPO's approach of triggering Section 92B(2) of the Act, with the advent of deeming provision under Section 92B(2) of the Act vide FA 2014 applicable from 01.04.2015, there has been an increased focus on the analysis of such transactions which are not prima facie visible from the financial statements or related party definition perspective. Considering transactions like centralized vendor appointment on a world-wide basis, acquisitions at local level arising of global arrangement, etc. are typically present in most multinational set up, a robust analysis should be undertaken to identify and unearth such contracts and payments which could get covered under such deeming provisions, failing to report and benchmark such transactions will attract substantial penalty. These may be more prevalent during the pandemic period due to changes in supply chain and realignment with vendors on global basis. Thus, this would require careful analysis to avoid any protracted litigation in future.

▪ Rulings on validity of assessment proceedings

8. Mavenir India Pvt. Ltd. vs DCIT – ITA No. 203/Del/2020

Delhi ITAT has ruled in favour of the Assessee for AY 2015-16 by pronouncing that the Draft Assessment Order (DAO) issued under Section 143(3) r.w.s 144C of the Act, in aggregation with demand notice and simultaneous issuance of penalty notice will instigate all succeeding proceedings and order as null and void. The Tribunal observed that provision under Section 144C of the Act contains chronological steps to be followed to conclude the proceedings. It further explained that the provision under Section 144C of the Act requires the AO to initially issue DAO only and shall complete the proceeding under Section 144C of the Act, under Sub-section (3) or Sub-section (13) basis the response from the Assessee either accepting the variation or raising objection before DRP. However, in the instant case the AO has by passed the relevant Sub-section (3) and Sub-section (13) and issued not only DAO but also served demand notice causing to terminate the further proceedings. Delhi ITAT relied upon the coordinate bench ruling in the case of Perfetti Van Melle India Pvt Ltd in ITA 9116/Del/2019 while reaching to its conclusion.

Nangia Andersen LLP's take

Non-obstante clause contained under Section 144C(1) Sub-section gives an overriding effect to other provisions thus making the procedure to be followed in compliance with the provision of Section 144C Sub-section mandatory. Circumventing the mandatory provision is not a mere irregularity but a non-curable defect. Besides, there are also plethora of ruling in the set aside proceedings, wherein the assessment order has been annulled if the AO fails to comply with Section 144C. Such acts have been concluded to be illegality of law, being ultra-virus, rather than being irregularity of the law whereby the defect can be cured.

9. Firemenich Aromatics (India) Pvt. Ltd. vs ACIT – ITA No. 348/Mum/2014

Mumbai Tribunal for AY 2009-10 deliberated on the maintainability of the Revenue's appeal filed against DRP direction in the light of Sub-section (2A) of Section 253 of the Act being omitted by the Finance Act 2016 while examining the effect of 'repeal' and 'omission' to the provision. The Tribunal has admitted the Assessee objection on the validity of Revenue's appeal filed regardless of failing to file the cross objection for the same. In understanding the implication of repeal/omission to a provision, the Tribunal examined Section 6, 6A and 24 of General Clauses Act. The Tribunal stated that, where Central Act or Regulation repeals any enactment then unless the repeal indicate a different intention, it shall not affect any investigation, legal proceedings, remedies etc. which was available under such enactment as if such repeal never existed. Further, Section 6A of General Clauses Act reveals that repeal can also be enacted by the expression 'omission'. In pronouncing its judgement, Tribunal relied on Hon'ble Supreme Court ruling in the case of Fibre Boards Pvt. Ltd and Shree Bhagwati Steel Rolling Mills wherein the apex court opined that omission would amount to repeal and accordingly any action taken pursuant to the currency of such enactment shall continue to be stand valid. Tribunal thus discounted the contention of the Assessee that omission shall deemed as it never existed in the statue and held that appeal filed by the Revenue during the lifetime of Section (2A) of 253 of the Act shall stand legal. Further, the ITAT distinguished the ruling in case Texport Overseas Private Limited relied on by the Assessee, stating that the judgement was pronounced without considering the SC decision in the case of Fibre Boards and Bhagwati Steels.

Nangia Andersen LLP's Take

Complex or vexed as it may get, repeal and omission appear to be the two sides of the same coin. Section 6A of the General Clauses Act puts the dilemma of differentiating between repeal and omission to an end. It provides that the repeal to a provision can be done either by the expression of omission, insertion or substitution. Thus, making it amply clear that the omission will also be a repealed. Repeal may take any form and so far, any statue or part of it get obliterated will be captured under the expression repeal.

Ruling on transaction with AE relationship for part of the year

10. Lonsen Kiri Cheminal Industries Ltd. vs DCIT - ITA No. 1116/Ahd/2015

Ahmedabad ITAT adjudicated in determining the ALP on account of export of goods by the Appellant to its AE's i.e. Well Prospering Ltd and Dyestar Group of companies (Dyestar) for AY 2011. During the concerned year, on 4th February 2010, the Assessee Company was incorporated in the form JV between Well Prospering Ltd. and Kiri Dyes and Chemicals Ltd (belonging to Dyestar). Thus, Dyestar formed an AE relationship with Assessee during later part of the year (i.e. on 4th February 2010). The Assessee while determining the ALP in respect of goods exported to its AEs by application of Comparable Uncontrolled Price (CUP) method, considered the average price charged by the Assessee to Dyestar prior to 4th February 2010, as uncontrolled transaction. In this regard, the Tribunal arbitrated on whether an AE formed during the part of the year can be considered as comparable for benchmarking. The Tribunal took cognizance of Section 92A(2) of the Act which states that two enterprises shall be deemed to be AE for the entirety of the financial year, if, the companies are AE at any time during the previous year. Further, the Tribunal referred to Rule 10A(ab) of the Rules r.w.s 92A(2) of the Act where it states that uncontrolled transaction means transaction between enterprises other than AE. Hence, Tribunal opined that once the company becomes an AE to the Assessee during any part of the concerned year, the transactions with such company cannot be taken as comparable. Tribunal also relied on Gemstone Glass Pvt. Ltd. in arriving at its conclusion. Separately, Tribunal also upheld the TP adjustment made by the TPO by comparing the average price of the comparable invoices with each individual related party invoices raised by the Assessee, instead of the average of related party invoice prices adopted by the Assessee. Tribunal relied in the case Tilda Riceland (P) Ltd. to support its decision and held that aggregation of comparable uncontrolled transaction is permissible but not for international transaction, taking reference from Rule 10B(1)(a)(i) of the Rules.

Nangia Andersen LLP's Take

Determination of AE is an intricate process, as there can be different scenarios emerging from a particular business decision. In the instant case, Tribunal, going by the condition of anytime during the year, has come to a conclusion of establishing AE relationship for the whole part of the year. Taxpayer would need to keep this aspect in mind while analysing the international transaction as there can be differences arising from accounting standards definitions of related party transactions vis-a- vis considering actual value of the international transaction, if the AE is to be considered for full part of the year. Also, keeping in mind the stringent penties for non-reporting or under-reporting of a transaction in the Accountant's Report.

Ruling on considering budgeted cost for ALP determination

11. GE Power India Limited vs DCIT/ACIT/ITO – ITA No. 1727/Mum/2015, 1956/Mum/2015, 1585/Mum/2016, 2065/Mum/2016, 2228/Mum/2016 & 956/Mum/2018

Mumbai ITAT rejected the Assessee's contention of treating the unabsorbed power production overhead, under recovered selling & administrative (S&A) overhead and one-time technical assistance fee as extra ordinary expenditure in respect of its transportation segment. Tribunal held that production overhead and S&A overhead are regular expenditure incurred during the normal business operation year after year and cannot be termed it as a discrete expenditure. Tribunal also held that mere comparison of actual expenditure with the budget and difference being termed as non-recurring is not sustainable. Further, the Tribunal held that the Assessee failed to show that similar corresponding adjustment has been provided for comparable companies.

Tribunal also observed that in pursuant to accounting standard, extra-ordinary item should be captured as a separate line item in the financial which was missing in the Assessee's financials. Similarly, for one-time technical assistance fee Tribunal held that the same is regular normal expenditure. However, accepting with the Assessee argument, Tribunal stated that TP adjustment in respect of international transaction with AE should be made pertaining to transport segment only and not entity wide. Further, the Tribunal deleted the ad hoc determining of ALP as NIL by the TPO for royalty paid on trademark and held that where the Assessee has provided the bench-marking study and the TPO has rejected such benchmarking study, the onus is on the TPO to determine the ALP of such transaction instead of just making ad hoc adjustment. Also, the ITAT expunged the DRP direction of determining the ALP in respect of royalty payment on technology license @ 1% without the application of the prescribed method.

Nangia Andersen LLP's Take

Treatment of extra-ordinary nature of expenses is a fact specific exercise. Under the Indian TP guidelines, the costs will typically be considered from the actual expenses recorded in the books of account. Adequate documentation and back data need to be maintained leading to claim of non-recurring/extra-ordinary nature. This detailing becomes even more relevant in the pandemic period where there will be instances of abnormality arising due to lockdowns and demand impacts. Hence, maintenance of robust documentation is imperative in such cases and as rightly held by this Tribunal, be supported by financial statements as well, where possible.

Rulings in relation to AMP adjustments

12. The Himalaya Drug Company vs ACIT – IT(TP)A No. 1385/Bang/2017

Bangalore ITAT deleted the TP adjustment proposed by the TPO in respect of AMP expenditure incurred by the Assessee, being a partnership firm (engaged in manufacturing and sale of ayurvedic medicament and consumer beauty products), for AY 2013-14. TPO observed that the ownership of brand name of 'Himalaya' transferred from the Assessee to its AE, Himalaya Global Holdings Ltd (HGHL) and also the logo underwent a change during 2003 and accordingly, the TPO determined that excess expenditure incurred by the Assessee over and above the routine expenditure incurred by the comparables as non routine expenditure to promote the brand and logo, legally owned by HGHL. Tribunal relying on coordinate bench ruling in the Assessee's own case for AY 2010-11 & 2011-12 held that, in the absence of any specific agreement between the Assessee and it AE to incur the AMP expenditure, the same cannot be termed as international transaction as, it is the Assessee which has developed all the products and trademark and is exclusively entitled to exploit the same. On a separate note, TPO also made TP adjustment in nature of royalty on the ground that the Assessee has allowed its AE, to use product registration/license to market its product in the respective country, which was mandatory for the Assessee to obtain in compliance of the respective country regulation. TPO held that such product registration/license is an intangible asset of the Assessee and it should charge royalty for exploiting the same. In this regard, the Tribunal held that the Assessee has exported finished goods to its AEs located in various countries who in turn sold such finished goods in respective markets and that charging of royalty from distributors over and above selling price is not commercial trade practice. Further, the Tribunal acknowledged that that the underlying goods relate to drugs and beauty products that need product license in each of the country where the products are sold and, obtaining such license cannot be considered as exploitation by the AE, as AE also has to independently obtain separate license for trading in pharma products. Distinguishes the ITAT ruling in the case of Dabur India Ltd where the AEs were manufacturer of the products under the brand 'Dabur' who also used to receive technical expertise. Thus, Tribunal upheld the contention of the Assessee and deleted the TP adjustment.

Nangia Andersen LLP's Take

The marketing intangiles issue finds itself on a new spectrum every time since there is no one size fit all formula here. It can be seen from many ruling that different approaches are struck down but, no approach has been suggested as the yardstick. Having said this, the onus has always been placed on the Assessee to collate and present evidence to substantiate that such expenditure has been incurred for the benefit of the Assessee only. No material has been placed on record by the Department to substantiate their claim or to solidify an approach to determine the quantitative TP adjustment. The roller coaster ride would continue till the Hon'ble Supreme Court presides over the matter.

Ruling on considering customs database data for CUP analysis

13. Dow Chemical International Pvt. Ltd. vs ACIT – ITA No. 1786/Mum/2016

The Mumbai ITAT relied on the coordinate bench ruling in the Assessee's own case for AY 2010-11 and AY 2014-15 to determine the ALP of raw materials imported by the Assessee from its AEs for AY 2011-12 by adjudicating on the MAM to be used, the database to be used to determine the comparable transactions and the comparable transactions to be considered to determine the ALP of raw materials imported by the Assessee from its AEs. While adjudicating the MAM, the Tribunal acknowledged that CUP should be adopted as MAM being the direct method and being a traditional transaction method which should be preferred over traditional profit method such as RPM and TNMM. Tribunal further held that when the CUP method using ICIS software covers 68% of the total transactions that too being a direct method and a traditional transaction method, the DRP ought to have accepted the same. The Tribunal also accepted the additional comaprables as additional evidences produced by the Assessee before the Tribunal using TIPS Data Base which covers even more higher percentage of total value (more than 90%) of import transactions from the AEs and remitted the issue back to the TPO, directing that CUP be adopted the MAM and the additional comparable transaction be evaluated to determine the ALP of international transaction. The Tribunal also added that TIPS Data Base maintained by the Customs Department has also been accepted by the Delhi Tribunal in the case of Tilda Riceland Pvt. Ltd. vs. ACIT reported in 161 TTJ 213. The Tribunal further upheld that while comparing the data at or near to the relevant date of transactions with the comparable prices using TIPS Data Base, portfolio approach ought to be adopted to take both the prices that are favourable to Assessee as well as that are adverse to Assessee, consequently, dismissing the cherry picking done by Revenue of those transactions which are favouring, based on the decision of same jurisdictional Tribunal in the case of Boskalis International Dredging C.V vs. DDIT reported in 67 SOT 118, subsequently approved by Hon'ble Jurisdictional High Court reported in TS-1310-HC-2018.

Nangia Andersen LLP's Take

In the instant ruling, Tribunal has adopted customs data to import prices for TP analysis. Historically, there has always been a difference between customs value benchmarking vs TP analysis as the objectives of both analyses are completely divergent. Nevertheless, with all stakeholders working on harmonization between TP and customs, allowance of adding Customs database results while undertaking TP analysis is a welcome move and a step in right direction.

Taiwan

On the 18 August 2020, Taiwan Ministry of Finance released draft amendment in TP rules placing emphasis on examining the actual conduct and capacity to assume/ manage the risks of the related party. Further, the amendments effective from 1 January 2020, provides detailed definition and DEMPE (Development, enhancement, maintenance, protection, and exploitation) analysis in respect of the Intangible assets to be undertaken to determine the actual contribution made and adequate remuneration for all the related parties in a group.

Poland

On 6 August 2020, Poland's Minister of Finance clarified dividends are not considered as controlled transaction, therefore, not requiring TP documentation.

On 4 September 2020, Poland proposed draft bill to extend the application of TP rules and documentation requirement in cases where beneficial owner is located in "tax haven" jurisdiction.

South Korea

On 11 September 2020, Korean legislation assembly proposed amendment in APAs and MAP rules.

Under the revised provisions, the roll back period has been revised for bilateral APAs (from five to seven years) and unilateral APAs (from three to five years) for APAs filed post 1 January 2021.

Further, proposed amendment would allow the Taxpayer to initiate MAP even after the final court decision is rendered. Additionally, as per amendment, in order to reach MAP the taxpayer would have to accept the MAP and withdraw any tax appeal for the relevant issue. Furthermore, the amendment bill provides an option to the Taxpayer to get the matter resolved by the arbitration committee, in case the MAP is unable to address the issue.

Further, on 27 August 2020, Korean National Tax Service announced tax audit initiation of 43 MNCs suspected of transferring huge income earned in Korea to other countries without due tax payment.

Cyprus

On 4 September 2020, Cyprus Ministry of Revenue issued clarification in respect of the Bilateral Competent Authority Arrangement (CAA) with the US for exchange of Country-by-Country (CbC) Reporting that is expected to be effective for Reporting Fiscal Years starting 1 January 2020. Detailed notification can be accessed at:

https://bit.ly/33k0yIC

Philippines

Philippines' Bureau of Internal Revenue (BIR) has published guidance to clarify the newly issued BIR Form No. 1709 - "Information Return on Transactions with Related Party". The said form contains details of the related-party transaction (both foreign and domestic), to be filed with the taxpayer's income tax return. BIR further explained that the said form shall be used as primary foundation for tax department to conduct TP risk assessment/ audit of a particular entity or transaction.

Japan

Effective July 2020, Japan's National Tax Agency (NTA) reorganize their tax audit teams into single unit to cover domestic and international tax issues, with TP being key focus area.

USA

On 24 August 2020, United States of America's (US) IRS issued notification regarding implementation of arbitration arrangement between the competent authorities of the US and Switzerland that can be accessed at:

https://bit.ly/3q1Tjie

Hong Kong

On 15 July 2020, Hong Kong's Inland Revenue Department published revised TP guidance on APAs. The revised DIPN No. 48 published introduces application for unilateral, bilateral and multilateral APAs in Hong Kong apart from specifying the thresholds for APA applications. Revised DIPN 48 can be accessed at:

https://bit.ly/3fzenYB

Australia

On 15 July 2020, Australian taxation Office (ATO) issued guidance on TP treatment of the JobKeeper payments to provide employment related relief in response COVID-19. The ATO expects Australian entities to retain the benefit of JobKeeper payments that they receive and not to shift the benefit of the government assistance to offshore related parties. Detailed guidance can be accessed at:

https://bit.ly/2HIBPGo

In August 2020, ATO published draft practical compliance guideline outlining practical compliance guidance for taxpayers involving outbound interest-free loans between cross border related parties, process of self-assessment, evidence required to be documented to substantiate self-assessment undertaken against the risk factors, and to calculate risk zone using practical instances. For details, please refer link:

https://bit.ly/369nEnb

Further, detailed analysis on the subject can be accessed at: **https://bit.ly/3q6qykC**

Singapore

The Inland Revenue Authority of Singapore (IRAS) updates its COVID-19 Support Measures and Tax Guidance to address taxpayers' APA related queries and provide guidance in relation to TP documentation to be maintained to substantiate the arm's length nature of the transaction in COVID-19 period. Detailed guidance can be accessed at:

https://bit.ly/3m9uYET

Further, detailed analysis on the subject can be accessed at: **https://bit.ly/2JfkYuY** and **https://bit.ly/3799SQB**

OECD Updates

- On 24 September 2020, Organisation for Economic Cooperation and Development (OECD) has released the outcomes of the third phase of peer reviews of the BEPS Action Plan 13 i.e. Country-by-Country reporting (CbCR) initiative as of April 2020, which analyses CbCR implementation by member nations and indicates strong global progress in efforts to improve the taxation of Multinational Enterprises (MNEs) worldwide. The review also discussed about India's CbCR requirements, highlighting and seeking clarifications for the deviation from BEPS AP 13, recommending Indian authorities to implement standard procedures and to ensure the exchange of information (EOI) is been conducted in a consistent manner, within the EOI framework issued by the OECD.

- On 31 July 2020, OECD and Brazil's tax authorities launched a public survey seeking inputs on the development of safe harbors and other framework for tax certainty in Brazil.

- On 9 July 2020, OECD published Corporate Tax Statistics Database (2nd edition), which provides aggregated information on the global tax and economic activities of nearly 4,000 multinational enterprise (MNE) groups headquartered in 26 jurisdictions and operating across more than 100 jurisdictions worldwide which was collected with the help of CbCR implemented by all the countries. The detailed statistics can be accessed at:

  https://bit.ly/2V5MVbj

Global BattleGround

Dutch Appeals Court ruling on adoption of Profit Split Method for benchmarking on the basis of the FAR for business sale transaction

Assessee was engaged in the activity of zinc smelting and performed functions including procurement of raw materials, production planning, undertaking smelting process, sales and other operational activities. On 1 July 2010, the Assessee completed the transfer of all of its functions except production (smelting) process to its AE, for which the Assessee was compensated on cost+ 10% basis.

Dutch Tax Authority contended that the production function performed by the Assessee is the core group function involving use of Intellectual Property (IP). Moreover, the activities of the AE also involves use of unique intangible in the Group value chain. Since the activity(s) performed by both the AEs are closely inter-linked and involves unique intangibles, routine cost plus remuneration for the Assessee was not justified and profit split method (PSM) should be considered to arrive at arm's length remuneration for the Assessee.

Dutch Court of Appeal held that "The functions left by the interested party (assessee) after the transfer… include more than that of a pure wage producer" and it did not amount to function limited to routine activities. Court adopted PSM to be the most appropriate method for determining arm's length remuneration for the AEs, stating a direct connection between the established profit split percentage based on the FAR of the Assessee and the calculated value of the portion of the business that was transferred to the AE. Copy of the translated judgement can be accessed at:

https://bit.ly/3q5dP1e

Canadian Tax Court's TP ruling on not re-characterizing service agreement as sham in case of AgraCity Ltd.

AgraCity Ltd. (Taxpayer) act as logistics services provider in Canada under the Service Agreement with its Barbados-AE for sale of AE's herbicide to Canadian farmers, earning cost plus remuneration. The Tax Court of Canada, placing reliance on the judicial precedence, rules in favor of the Taxpayer, disregarding the contentions of the Canadian Revenue Agency (CRA) for considering the service agreement of the Taxpayer as sham on a ground that mere "confusing, incomplete or inadequate records ….are not, on their own, evidence of a sham". Court observed the validity of the contractual agreement which in turn sets out and measures the roles of the parties and remuneration of the Taxpayer. In absence of any evidence to establish existence of any sham transactions or any deceptive window dressing, the CRA ruled that the transaction(s) under the Service Agreement entered by the Taxpayer with its AE is not sham and at arm's length price (ALP).

Further, Court rejected the CRA's attempt to use TP-recharacterization provision and explained that "One of the express requirements for recharacterisation is that *non-arm's length parties must be participants in a transaction or series of transactions that would not have been entered into between arm's length persons"*; Thereafter, Court accepts the expert's opinion/ evidence that the taxpayer's returns under the Services Agreement were within the range of comparable cost plus returns and holds that the taxpayer, "has met its initial onus to "demolish" the Respondent's (CRA) assumptions". Copy of judgement can be accessed at:

https://bit.ly/33A22Pd

Canadian Federal Court ruling for reallocation of AE's profits to Cameco Corporation

Canadian Federal Court of Appeal affirms Canadian Tax Court's decision of reversing TP adjustments made by Revenue on sale of Uranium by Cameco Corporation (Assessee) to its Swiss subsidiary/AE. Court while rejecting the Revenue's plea - seeking reallocation of profits earned by the Swiss AE to Assessee, on the premise that Assessee would not have entered into such long term contract with any third party. Court explained the legal ground provided in the tax statute needs to be fulfilled before making such adjustment. Court held that Swiss AE was assuming Uranium product price risk and is therefore entitled to favourable movement in its market price. Court further observed that the legal tax legislature would not permit the Revenue to ignore the separate legal existence of Assessee and AE. Court also rejected Revenue's contention of disregarding Assessee's group structure on premise that it was planned to evade Assessee's tax liability in Canada. Court, placing reliance on OECD Guidelines, observes that the structure adopted by the Assessee did not impede determination of appropriate transfer price and accordingly rejects CRA's attempt to reallocate the profit of the Swiss AE to the Assessee.

Canadian Court ruling on power/ right of the Revenue to gather information

Revenue during TP audit of Bayer Inc. (Assessee) demanded copy of agreements entered between any Bayer Group entity with third party(s) w.r.t. pharmaceutical product. Assessee challenged the relevance of Revenue's audit request in Court. Court, while ruling in favor of Revenue, stated that Revenue may reasonably sought an information even if it ultimately turns out to be irrelevant, provided rational connection exits between the information sought and provision of the Tax legislature in force. Court further clarified that the Assessee is protected from abusive use of the provision by the Revenue through the power of a judge to review the requirement. Copy of judgement can be accessed from the given link:

https://bit.ly/3l65CpZ

Zimbabwean High Court Ruling on taxing related party transactions in case of CRS

CRS Pvt Ltd, Zimbabwe (Assessee) entered into the lease agreement with its South African AE for lease of its fleet of transportation vehicles. A fixed rate billing per trip for the lease of vehicles was agreed between the parties and the AE was required to bear all the operating expenses involved in using the vehicles. Zimbabwe Revenue Authority (Revenue) contends that the pricing under the lease agreement was low and not as per the industry standard. Revenue contends that transaction entered was primarily to avoid or reduce tax liability by the Assessee and by invoking the deeming provision provided in the tax legislature made an addition in the notional income.

High Court of Zimbabwe (HC) upheld the Revenue's contention and stated that such an arrangement wouldn't have happened in third-party scenario, thereby the transaction was not undertaken at arm's length and was deliberately designed for tax avoidance by the Assessee.

It is pertinent to note that the said ruling by HC relates to financial year prior to introduction of detailed TP regulations in Zimbabwe; thereby, HC only relied on deeming provision governing Tax Avoidance Arrangements by the Assessee. With TP regulations in place, the HC might have considering the FAR and other economic substances involved in the transaction undertaken by the Assessee. Copy of judgement can be accessed at:

https://bit.ly/3nVFkIS

Zambia Tribunal ruling of re-characterization of Nestle as Limited Risk Distributor

On 28 March 2019, Zambia's Tax Appeals Tribunal (TAT) ruled in favor of Nestle Zambia Trading Limited except upholding Revenue's contention of Assessee's charaterisation as limited risk distributor (LRD). TAT held that Assessee's Group Company exercises significant control over it through its functions like strategic management, sales, marketing, finance, accounting, HR, IT, legal, procurement and supply chain management services, which were performed by the group. TAT further observed that as per the License Agreement, know-how remained the exclusive property of foreign AE and were never transferred to the Assessee, which ultimately resulted in foreign AE retaining the ownership of products resold by the Assessee in Zambia. Thus, TAT held that the ultimate risks in marketing, distribution, storage and/or selling of products were assumed by foreign AE and not Assessee. Therefore, TAT concluded that Assessee was operating as LRD and not full-fledged distributor. Copy of judgement can be accessed at:

https://bit.ly/2JbFk8v

Danish Tax Court ruling on discretionary valuation of intangible assets in case of Software A/s

Software A/S (Assessee) operated as full-fledged distributor of software and related services provider till 2010 when its operations restructured to commissionaire for newly established Swiss sales and marketing hub. In absence of TP documentation during restructuring, Danish Revenue made discretionary assessment, contending that additional tax from intangibles transfer in 2010 to Swiss-AE has to be determined by applying DCF valuation model, which was struck by Danish Tax Court. Court observed that Assessee has adequately analysed the FAR and prepared comparability analyses for transactions undertaken before and after restructuring in its TP Study. Court however noted that Revenue had rightly stated that the pricing of intangible transfer during restructuring to be done in accordance with Danish TP provisions. Court applied the DCF valuation model prepared by Revenue, restricting the expected useful life of assets to only 10 years – and not indefinite as determined by Revenue – resulting in lower tax adjustment. Copy of translated judgement can be accessed at:

https://bit.ly/2V2VZOh

Italian SC ruling of allowability of losses attributed to Italian PE of the US Parent in case of Citibank

Italian SC reversed regional tax court judgment and ruled in favour of Citibank NA (Assessee), US based banking company with PE in Italy. SC explained *Para 3 of Article 7 of the Italy-US DTAA* provides conditions for allowability of expenses incurred by PE stating that Italian PE's expenses can be considered as non-deductible only if expenses incurred are attributable to the banking operations carried by US parent outside the territory of the State (Italy) and not through the PE. Court further states that PE is a distinct independent entity from its parent company whose profit is taxable as per the applicable Tax Legislation. Given the losses were incurred on the loan agreements entered with Italian clients, thus SC held that such losses were deductible in the P&L of the Italian PE and should not be attributed to the parent irrespective of the financial capacity of the PE to assume the risk. Copy of judgement can be accessed at:

https://bit.ly/3fy8kUa

Finnish SC ruling on re-characterization of intra-group financial restructuring

Finnish Supreme Administrative Court (SC) provided ruling in favour of the Assessee holding that Revenue is not entitled to re-characterize legal transactions between group companies u/s 31 of Tax Procedure Act. Assessee reorganized its internal financing function, establishing a new financing company in Belgium. Assessee further transferred its intra-group unsecured loan and interest income to the Belgian AE in exchange of shares. Revenue authorities while disregarding the legit reorganisation of the group financing function by the Assessee, made TP adjustment on the premises that the Assessee still conducts significant functions while assuming the significant risks on the intra-group financing activities and the AE only provides routine financial management, payment and reporting services to the Assessee. SC observed that Revenue has ignored the legitimate reorganisation of Assessee's functions, which is not valid under the Finnish tax legislation.

SC further held that the TP adjustment is not sustainable by re-characterizing the transaction in the absence of any information suggesting that the financial operations were conducted for the purpose of tax avoidance. SC held that only when transactions are in contravention of General Anti-Avoidance Rule, the Revenue is entitled to re-characterize the transaction and assess tax consequences, not otherwise. Furthermore, SC clarified that it is not possible to interfere with the cash flows between the inter-company transactions, but only with the pricing or other terms of such transaction. SC also ruled that while OECD TP Guidelines provides for the reclassification under exceptional circumstances; however, this is used merely as a source of interpretation and ruling is limited to Finnish domestic law in force. Copy of judgement can be accessed at:

https://bit.ly/3q3cCYA

▪ Polish Supreme Administrative Court's ruling on fact based comparability analysis

Assessee operates as a group of agricultural producers, wherein the Assessee purchases fruits from the producers who were also the Company's shareholders under the provisions governing producer groups in Poland.
Polish Revenue authority alleged that the Assessee purchase the agricultural produces at inflated prices from its shareholders *(agricultural producers)* vis-à-vis market prices. Since agricultural producers' income were not subject to taxation, the Assessee reduced its tax liability by shifting substantial profit from the sales of the product to its shareholder. Revenue further alleged that due to lower margins of the Assessee, recovery of cost of materials, energy consumption, depreciation and other costs was not possible, resulting in overall losses for the Assessee. On these premises, the Revenue made TP adjustment by comparing the margins of the Assessee with the selected comparable independent companies.

Supreme Administrative Court (SC) in response to Assessee's appeal held that Revenue, before conducting comparability analysis, should be considerate about the agricultural producer status of the Assessee. SC observed that the specific nature of the entity, the principles and essence of the group's operation, the scope of goals that it pursue, the strategy of the producer groups, the use of aid measures, the issue of the group's market strategy should be the basic foundation and essence for undertaking the comparability analysis. SC observed that the Revenue did not apply practically the provisions on the issue of comparability analysis, thereby quashing the TP assessment and remitting the case back to the Revenue.

▪ EU General Court ruling in case of Apple

EU General Court in a decade long dispute ruled in favour of Apple Group (Assessee) holding that European Commission (EC) is not successful in establishing the selective economic advantage provided by Irish Revenue in previous two tax rulings passed in favour of subsidiaries of Apple (namely ASI and AOE engaged in sales and marketing and manufacturing in Ireland respectively). Court highlighted the necessity of carrying objective factual analysis while conducting assessment. Accordingly, Court emphasised that EC should first focus to identify the 'activities' performed, assets deployed and risks assumed by branches of the Apple subsidiaries operating in Ireland, before determining the value of such activity. Court disregarded EC's contention to allocate Apple Group's IP licenses to ASI and AOE's branches and proposing to tax the branches' trading income, without conducting any actual detailed analysis.

Furthermore, Court observed the EC has not been successful to demonstrate any methodological errors which would have led to reduction in ASI and AOE's chargeable profits in Ireland or to prove that the contested tax rulings were the result of discretion exercised by the Irish Revenue, thereby providing any selective advantage to ASI and AOE.

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