DRAFT GUIDANCE NOTE ON TRANSFER PRICING REPORT – SECTION 92E

AUTHOR :EDITOR

ICAI Releases Exposure Draft Guidance Note On Report Under Section 92E Of Income-Tax Act, 1961 (Transfer Pricing) Based on the law as amended by Finance Act, 2022

EXPOSURE DRAFT GUIDANCE NOTE ON REPORT UNDER SECTION 92E OF THE INCOME-TAX ACT, 1961 (TRANSFER PRICING)

[Based on the law as amended by the Finance Act, 2022]
(Revised 2022)

(Last date for Comments: 1st August, 2022)

Committee on International Taxation
The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

Following is the Exposure Draft of the Guidance Note on Report under section 92E of the Income-tax Act, 1961 (Transfer Pricing), issued by the Committee on International Taxation of ICAI for comments. Changes have been made to the extent of amendments made by the Finance Act, 2022.

The Committee invites comments on this Exposure Draft. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide suggestions for alternative wording.

How to comment:

Comments can be sent to citax@icai.in so as to be received not later than 1st August, 2022.

Chapter 1

Introduction

Legislative Framework

1.1 In an era of liberalization and globalization of trade and investment and the emergence of digital economy, the perceptible results have been – increase in the number of cross-border transactions and the complexity and speed with which global business can be transacted.

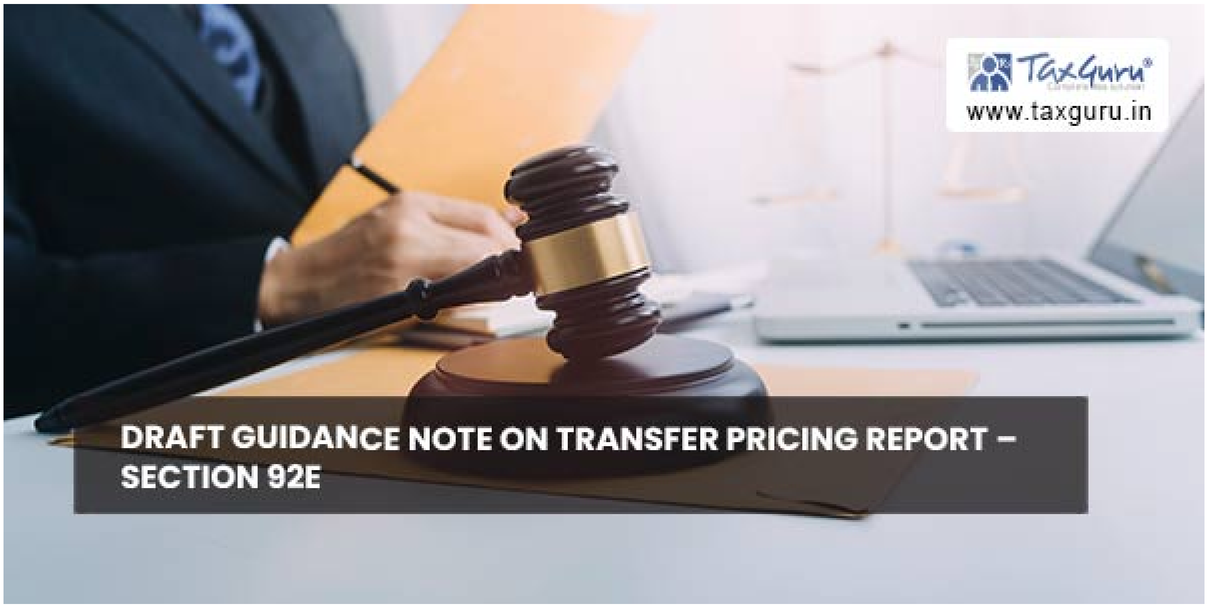
1.2 When transactions are entered into between independent enterprises, the consideration therefore is determined by market forces. However, when associated enterprises deal with each other, it is possible that the commercial and financial aspects of the transactions are not influenced by external market forces but are determined based on internal factors. In such a situation, when the transfer price agreed between the associated enterprises does not reflect market forces and the arm?s length principle, the profit arising from the transactions, the consequent tax liabilities of the associated enterprises and the tax revenue of the host countries could be distorted.

1.3 The existence of different tax rates and rules in different countries offers a potential incentive to multinational enterprises to manipulate their transfer prices to recognise lower profit in countries with higher tax rates and vice versa. This can reduce the aggregate tax payable by the multinational groups and increase the after tax returns available for distribution to shareholders.

1.4 In India, the Act for a long time did not deal with this problem in a detailed manner. The erstwhile section 92 sought to determine the amount of profits which may reasonably be deemed to have been derived from a business carried on between a resident and a non-resident which, owing to the close connection between them is so arranged that it produced, to the resident, either no profits or less than the ordinary profits which might be expected to arise in that business in case the transaction would have been entered into between two entities having no close connection. Besides, sections 40A(2); 80IA(10) and 80IB(13) of the Act provide powers to the Assessing Officer to interfere with the pricing or costing of certain transactions in certain cases in order to determine the correct quantum of deduction permissible.

1.5 The Finance Act, 2001, recognised that international transactions between Associated Enterprises may not be subject to the same market forces that shape relations between two independent firms, and therefore introduced a set of provisions in Chapter X of the Act under the title “Special Provisions relating to avoidance of tax”. The statutory framework attempts to monitor transfer prices for goods, facilities and services in order to determine that they confirm to the “arm’s length principle”. Not only has section 92 of the Act been completely recast but new sections 92A to 92F have also been introduced to meet the desired objective of ensuring that the local tax base of a taxpayer is fair.

1.6 The relevant provisions contained in Chapter X (sections 92 to 92F) of the Act and the provisions dealing with the levy of penalties for noncompliance thereof are reproduced in **Annexure** I. The Finance Act, 2002 made certain changes to the provisions contained in sections 92A, 92C, 92F and 271F. The Finance Act, 2006 further amended section 92C. Further, the Finance Act, 2007 inserted sub-sections (3A) and (4) in section 92CA. Finance Act 2009 amended the proviso to section 92C, provided for constitution of the dispute resolution panel and empowered the Board to formulate safe harbour rules. Finance Act 2011 amended the allowable variation as per second proviso to section 92C(2) to be notified by the Central Government, and made changes to Section 92CA. The Finance Act 2012 has introduced significant amendments including inter alia clarifying the coverage of the term „international transactions’, expanding the scope of transfer pricing provisions to specified domestic transactions (Section 92BA) and providing an Advance Pricing Agreement framework (Section 92CC and Section 92CD) empowering the transfer pricing officer to determine arm’s length price of an international transaction noticed during the course of proceedings before him, even if the said transaction has not been referred by the Assessing Officer, provided such transaction has not been reported by taxpayer as per requirement of Section 92E of the Income Tax Act, 1961 [Section 92CA(2B)] and expanding the scope of penalties and amending Section 147 of the Act to provide that non-reporting of transaction in report as per Section 92E would be deemed to be case of escapement of income.



Further, changes specifically in respect of arm's length price determination were introduced vide Finance (No. 2) Act 2014 and the Finance Act 2015. The Finance Bill 2014 introduced the use of multiple year data and the Finance Act (No. 2), 2014 introduced range concept for determination of arm's length price and roll-back mechanism for APA. The final rules in relation to the range concept and use of multiple year data were notified by the Central Board of Direct Taxes in October, 2015.

1.7 Further, section 92B extended application of transfer pricing provisions to transaction entered by an Indian entity with a resident independent third party under specified circumstances. The Finance Act 2015 increased the threshold limit for the applicability of specified domestic transaction from INR 5 crores to INR 20 crores with effect from Financial Year 2015-16.

1.8 The Finance Act 2016, in line with recommendations of the BEPS Action Plan 13, inserted section 286 for furnishing of country-by-country report and inserted proviso to section 92D(1) for maintenance of Master File, with effect from Financial Year 2016-17. Further, relevant rules and forms for country-by-country and Master File were notified on 31 October, 2017.

1.9 Further, the existing penalty provisions have been rationalised along with insertion of additional penalties for non-furnishing/ maintenance of country-by-country report and Master File.

1.10 The Finance Act 2017, amended the applicability of specified domestic transactions compliance by excluding expenditure made to person referred to in Sec. 40A(2)(b) of the Act, from the ambit of the definition.

1.11 Provisions regarding secondary adjustments and limitation on interest deduction were introduced and inserted as new sections (92CE and 94B respectively) vide Finance Act, 2017.Finance Act 2017 also introduced section 271J for levying penalty on accountants for furnishing incorrect information in reports or certificates furnished under any provisions of the Act or the rules made thereunder.

1.12 The Finance (No. 2) Act, 2019 made amendments to section 92CD, 92CE, 92D and 286 of the Act. These amendments are as follows:

- Section 92CD (3) was amended to clarify that in cases where assessment or reassessment has already been completed and modified return of income has been filed by the tax payer under sub-section (1) of section 92CD, the Assessing Officers shall pass an order modifying the total income of the relevant assessment year determined in such assessment or reassessment, having regard to and in accordance with the APA. This amendment is applicable from 1 September, 2019.

- Section 92CE was amended to give clarification with regard to applicability of provision of secondary adjustment and to give an option to assessee to make one-time payment (discussed in detail at Para 1.31 of this chapter)
- Section 286 of the Act was amended to give clarification regarding definition of the "accounting year" so as to provide that the accounting year in case of the alternate reporting entity („ARE') of an international group, the parent entity of which is not resident in India, shall be the one applicable to the parent entity of ARE. The said amendment will take effect retrospectively from the 1st April, 2017 and will, accordingly, apply in relation to the assessment year 2017-18 and subsequent assessment years.

1.13 The Finance Act, 2020 made certain amendments to sections 92CB, 92CC, 92F and 94B. These amendments are as follows:

- Section 92CB and 92CC of the Act was amended to include attribution of profits to the PE of a non-resident under clause (i) of sub-section (1) of section 9 of the Act.
- Section 92F of the Act amended the definition of term "specified date" to mean the date one month prior to the due date for furnishing the return of income under sub-section (1) of section 139 for the relevant assessment year.
- Section 94B of the Act was amended to exclude interest paid or payable in respect of a debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking.
- On 17 June 2022, Central Board of Direct Taxes („CBDT') has issued **Notification No. 66 /2022**/F. No. 370142/26/2022-TPL. Vide this Notification; the CBDT has extended the Safe Harbour Rules („SHR') to Assessment Year („AY') 2022-23 relevant to the previous year 2021-22.

1.14 Faceless Assessment: The Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 amended section 92CA of the Act and inserted clause (8) to (10) w.e.f from 1.11.2020 to extend the provision of faceless assessment to transfer pricing also.

Sub-section (9) of the said section further provides that for the purposes of giving effect to the aforesaid scheme, the Central Government may by notification in the Official Gazette direct that any of the provisions of the Act shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified. It was provide that no direction shall be issued after the 31st day of March, 2022.

By virtue of Finance Bill, 2022, the last date for issuing directions/notification for faceless determination of arm's length price under section 92CA, faceless Dispute Resolution Panel under 144C, Faceless appeal/proceedings before the Appellate Tribunal under section 253/section 255 of the IT Act have now been extended from March 31, 2022 to March 31, 2024.

1.15 Non filing of repetitive appeals – A new section 158AB has been inserted after section 158AA by the Finance Act, 2022 in order to prevent filing of repetitive appeals.

These amendments are also included in the Annexure. The Rules prescribed in this regard by the Central Board of Direct Taxes are reproduced in **Annexure II**. The relevant extracts from the Memorandum explaining the provisions of the Finance Act, 2001, Finance Act, 2002, Finance Act, 2006, Finance Act, 2007, Finance Act, 2009, Finance Act, 2011, Finance Act 2012, Finance (No. 2) Act 2014, Finance Act 2015, Finance Act 2016, Finance Act, 2017, Finance (No. 2) Act, 2019 Finance Act 2020, The Taxation And Other Laws (Relaxation And Amendment Of Certain Provisions) Act, 2020 and Finance Act, 2022 are given in **Annexure III**. The Central Board of Direct Taxes has issued Circulars explaining the provisions and clarifying certain related aspects. These circulars are given in **Annexure IV.**