
The 2017 OECD Transfer Pricing Guidelines reflects the objective of tackling BEPS and the establishment of the Inclusive Framework on BEPS. It also strengthens the impact and relevance of the Guidelines beyond the OECD by inviting non-OECD members to adhere to the 2017 OECD Transfer Pricing Guidelines. While India is not a OECD Member Country, the OECD Transfer Pricing Guidelines have proved to be a good reference and guidance point for Tax Authorities, Taxpayers and the Judiciary alike.

India has seen significant litigation on the transfer pricing front. While the 2017 OECD Transfer Pricing Guidelines will not fully mitigate the risk of litigation arising from ever evolving structures and the international transactions emanating therefrom, it may potentially result in reduced litigation.

Changes proposed to Chapter IV on Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes or Chapter VI on Special Consideration
for Intangibles amongst others are all aligned towards reducing litigation and providing certainty to Taxpayers.

Of particular significance are the changes to Chapter V (Documentation), where the contents of Action Plan 13 have been incorporated. This would provide significant visibility on whether the Transfer Pricing policies employed by Taxpayers are aligned to remunerate Group Companies for the value created in their respective jurisdictions.

The 2017 OECD Transfer Pricing Guidelines are a significant step forward and our publication attempts to capture the implications arising therefrom while providing insights on the next steps. We hope you will find this useful.

Dinesh Kanabar  
CEO  
dinesh.kanabar@dhruadavisors.com
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Introduction

The evolving nature of international trade together with the new-age business models have resulted in increasingly complex taxation issues (arising from the growth of cross border transactions and borderless transactions). The OECD introduced the "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration" in 1995 to deal with complex cross border taxation issues. The Guidelines were updated in 2010 ('2010 OECD Transfer Pricing Guidelines'). However, even these measures were not considered sufficient and the OECD has introduced the 2017 OECD Transfer Pricing Guidelines. The changes in the 2017 OECD Transfer Pricing Guidelines find their genesis in the Base Erosion and Profit Shifting ('BEPS') project under the aegis of G-20 and OECD.

WHAT IS BEPS?

BEPS refers to tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax jurisdictions with little or no corresponding economic activity. Today, multilateral, rather than bilateral initiatives are taking centre stage under the aegis of the G-20 and the OECD, through the BEPS project.

Measures to tackle BEPS are through implementation of the following:

- Reinforced international standards on tax treaties and transfer pricing
- Analytical reports with recommendations (Digital economy and multilateral instrument)
- Detailed reports on measuring BEPS
- Common approaches and best practices for domestic law measures
- Prescribes minimum standards
The final package of measures under the BEPS project for reforming the international tax system was released by the OECD on October 5, 2015. This is based on the BEPS Action Plan agreed to in 2013, which identified 15 action plans aimed at putting an end to international tax avoidance. The 15 action plans on BEPS released by OECD are based on 3 fundamental pillars:

- Introducing coherence in the domestic tax rules that affect cross-border activity;
- Reinforcing substance requirement to ensure that tax is aligned with the location of economic activity and value creation; and
- Improving transparency and certainty for businesses and governments.

The 15 Action plans that evolved around the 3 fundamental pillars are illustrated in the diagram below:
In the Indian context, the following actions assume greater importance, for the reasons mentioned below:

- **Action Plan 1**: Addressing the tax challenges of the digital economy. Challenges arising from a digital economy perspective are a great concern for India owing to rigid application of residence based taxation and the vast consumer market tapped by MNEs in India through Digital Media/Digital Platform. These challenges include:
  - issues relating to e-commerce arise from: difficulties of characterizing the nature of payment;
  - establishing a nexus or link between a taxable transaction, activity and a taxing jurisdiction;
  - the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

This results in stateless, non-taxable income. India has partly countered this challenge by introducing an equalization levy for payments made to non-residents using digital advertising platforms.

- **Action Plan 6**: Preventing treaty abuse. There are increasing cases of treaty abuse that are being identified by the Tax Authorities in the recent past which have resulted in double non-taxation (such as the capital gain exemption provided for in the India Mauritius treaty). This Action Plan focusses on such cases of treaty abuse and recommends introduction of measures to be followed by the participating countries through:
  - Avoiding creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including treaty shopping;
  - Introduction of specific anti-abuse rule, the Limitation of Benefits (‘LoB’) clause in tax treaties to limit the treaty benefits only to those entities that meet certain conditions; and
  - A principal purpose test that covers those cases that do not qualify the LoB clause and are still considered as transactions of treaty shopping.

India has already implemented several of the measures through re-negotiation of treaties, introduction of GAAR etc. This would necessitate Indian Multinational Enterprise (‘MNE’) Groups and MNE Group’s in general re-evaluating their structures to ensure that the primary motive of any structure is not the avoidance of tax.

- **Action Plan 7**: Artificial avoidance of Permanent Establishment (‘PE’) status. Many MNEs have been avoiding declaring taxable presence in multiple countries though they have been involved in value-creating activities in such countries without contributing in terms of profit to such countries.

In order to curb such practice, the OECD has revised the definition of PE to bring in many such MNE groups under the taxation net. In India, entities particularly involved in marketing activities have been identified by the Tax Authorities as those that avoid declaring PE status and escape taxation.

The limitation of exclusions within the scope of Article 5(4) could see greater income being liable to tax in India. Further, the recommendations provided in Action Plan 7 would provide credence to India’s contention that where agents habitually secure orders in India, there would be a PE constituted in India.

With the inclusion of GAAR in the Indian Tax Legislation, the primary concerns that were highlighted by Action Plan 6 and 7 would be addressed.

Another important aspect to consider is whether an arm’s length charge for functions performed by an entity would be sufficient to extinguish any liability towards profit attribution arising from the existence of a PE. While judicial precedents (as in the case of Morgan Stanley & Co.) have held that where functions adequately reflect the operations of an enterprise, there would be no further charge attributable other than the arm’s length charge.

- **Action Plans 8 – 10**: Transfer Pricing aspects of intangibles, Risk and Capital and High-risk transactions. The Action Plans 8-10 focus on the transactions involving intangibles, contractual arrangements, allocation of risks in line with the contractual arrangements and corresponding profits derived by the entities in the MNE Group. These Action Plans are critical from an India perspective considering that there has been substantial litigation surrounding intangibles, in particular, relating to marketing intangibles and Research and Development (‘R&D’) arrangements (owing to Indian Tax Authorities contesting that risks are borne by the Indian subsidiaries of MNEs).

1. [2007] 292 ITR 416 (SC)
The Indian Tax Authorities have issued Circular 6 of 2013, which provides guidance on when an entity would be regarded as rendering R&D services warranting a higher remuneration or share of profits. While the Action Plan and the 2017 OECD Transfer Pricing Guidelines do not necessarily deal with some of the quantification methodologies discussed in the Circular, the Circular states how Indian Tax Authorities would establish the contribution made by the so-called “Limited Risk Captive Service Provider” to the value chain of MNE Groups.

- Action Plan 13: Transfer Pricing Documentation: By providing for comprehensive documentation requirements, consisting of Master File, Local File and Country by Country Reporting (“CbCR”), Tax Authorities (including Indian Tax Authorities) would be empowered to concentrate on high-risk transactions, while having visibility on the consistency of application of transfer pricing policies across all entities of a MNE Group.

India has, vide notification dated July 28, 2017, notified the Multilateral Competent Authority Agreement. This would enable automatic exchange of CbCR with countries that are parties to the Convention.

Interplay between the 2017 OECD Transfer Pricing Guidelines and the BEPS Project

Changes to Chapters in 2017 OECD Transfer Pricing Guidelines are largely carried out to give effect to Action Plans 8-10, 13 and 14 of the BEPS Project.

Significance of the 2017 OECD Transfer Pricing Guidelines – an India perspective

In addition to OECD Member Countries, India (as a representative of the G20 countries) played an important part in the BEPS Project. While India is not a OECD Member Country, the OECD Transfer Pricing Guidelines have proved to be a good reference and guidance point. In the case of Sony Ericsson Mobile Communications India Pvt. Ltd2, the Delhi High Court stated that “it may not be prudent to discard or ignore the OECD TP Guidelines, without adequate justification and the same can be used as a supplement to the Act and the Rules, and constitute a valuable and convenient commentary on the subject. They are not binding but surely their rational and articulacy requires cogitation, if not acceptance, when warranted.”

Given that India formally participated in the BEPS Project, the OECD Transfer Pricing Guidelines are more relevant than ever for us in India today (more specifically on contentious issues like intangibles, business restructuring etc.). Further, various changes made in the tax legislation relating to intra-group services, documentation requirements (introduction of CbCR, maintaining local file, master file etc.) are in line with the overall direction of the 2017 OECD Transfer Pricing Guidelines.

Given the above backdrop, it is imperative that MNEs operating from/ in India, examine their TP Policy/ Documentation to ensure alignment with the Indian Transfer Pricing Regulations while also being cognizant of the specific guidelines/ guidance provided in the 2017 OECD Transfer Pricing Guidelines.

OECD and United Nations (‘UN’) Model Tax Conventions (Similarities, Differences and Recent Developments)

The OECD and the UN Model Tax Conventions have similar goals i.e. eliminating double taxation and preventing base erosion of profits arising from evolution of the global economy. Even though there exist principled differences between the two models, both models play a significant role in establishing and bridging tax policies between developed and developing economies.

The UN released the revised editions of its Transfer Pricing Practice Manual ("UN TP Manual") for developing countries, providing guidance on the application of arm’s length principle with the objective of addressing base erosion risks and other issues. The convergence of UN TP Manual with the 2017 OECD Transfer Pricing Guidelines based on the BEPS project will help in bringing about consistency in the application of Transfer Pricing guidelines across the world.

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2. (ITA No.16/2014 and connected matters)
INTRODUCTION

Chapter I of the 2017 OECD Transfer Pricing Guidelines explains the arm’s length principle. The arm’s length principle is considered as an international transfer pricing standard that should be used for by Taxpayers and Tax Authorities. An authoritative statement on the arm’s length principle is provided in Article 9 of the OECD Model Tax Convention.

Section D of Chapter I, provides for the application of the arm’s length principle for transactions between Associated Enterprises (“AEs”). It seeks to compare the transactions between AEs and independent enterprises, as the transactions between AEs may not reflect the effect of external market forces on their commercial or financial relations.

REVISIONS

The 2017 OECD Transfer Pricing Guidelines recognises the dichotomy that existed between contractual agreements and operational arrangements between MNEs and their AEs. To ensure that there is coherence between the contractual and operational arrangements, substantial revisions have been undertaken following the principle of “substance over form”.

The emphasis has now, shifted from how a transaction has been labelled, to delineation of a transaction depending on its nature/ substance, rather than its label/ form. Further, such delineation should be largely in connection with risks assumed and control over such risks (including the financial capacity to assume risks), apart from the functions performed and assets used in a transaction.

The following is a summary of the significant revisions to Chapter I.

Accurately delineated transaction

In Chapter I of the 2010 OECD Transfer Pricing Guidelines, the emphasis was on examining the “actual transaction” undertaken as a whole. The revised Chapter I as contained in the 2017 OECD Transfer Pricing Guidelines, focuses on delineation of various components of a transaction (functions undertaken, assets utilised and risks assumed for each part of a transaction and not the transaction as a whole) and analysing each leg of a transaction independently, as against the 2010 OECD Transfer Pricing Guidelines which focused on the actual transaction undertaken between AEs.

The Chapter provides guidance on identifying the commercial or financial relations between AEs and accurately delineating the controlled transaction.

Guidance on risk analysis

The Chapter now incorporates a section on “Risks” (analysing risk) (as contained in Action Plans 8-10 of the BEPS project relating to aligning transfer pricing outcomes with value creation). A six-step process has been set out to accurately delineate a transaction (so as to capture the substance of a transaction), which is as follows:

<table>
<thead>
<tr>
<th>STEP</th>
<th>Identification of economically significant risks in relation to a particular transaction (basis of the likelihood and size of the potential profits or losses arising from the risk)</th>
</tr>
</thead>
<tbody>
<tr>
<td>STEP</td>
<td>Analysing contractual arrangement to determine the assumption of economically significant risks in relation to a transaction</td>
</tr>
<tr>
<td>STEP</td>
<td>Undertaking functional analysis to determine actual conduct of the AEs in relation to the assumption and management of risks in relation to a transaction</td>
</tr>
<tr>
<td>STEP</td>
<td>Confirm consistency between contractual arrangement and conduct on ground (as seen from step 2 and 3)</td>
</tr>
<tr>
<td>STEP</td>
<td>Guidance on allocating risks amongst parties to the transaction, in case, the party identified in the steps above do not control such risks or do not have the financial capacity to assume such risks</td>
</tr>
<tr>
<td>STEP</td>
<td>Determination of arm’s length price based on financial and other consequences of risk assumption as documented and understood between points 1 to 5 above</td>
</tr>
</tbody>
</table>
Certain important terms mentioned in the above steps have been elaborated below:

**Assumption and allocation of risks**

<table>
<thead>
<tr>
<th>Control &amp; Authority</th>
<th>Risk Management Function</th>
<th>Financial &amp; Technical Capability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Decision to accept risk-bearing opportunities;</td>
<td>Decision to accept risk-bearing opportunities;</td>
<td>This includes the access to funding to take on or lay off a risk, pay for risk mitigation functions and bear the consequences if the risk materializes</td>
</tr>
<tr>
<td>Decision to respond to risks; and</td>
<td>Decision to respond to risks; and</td>
<td></td>
</tr>
<tr>
<td>Performance of actual functions</td>
<td>The capability to mitigate risks</td>
<td></td>
</tr>
</tbody>
</table>

Therefore, it is clear that a party which controls the risk should be compensated for such functions. Where an AE only provides funding, but does not control the risk, such AE should be remunerated only for the financing cost and no risk premium should be paid to such an AE.

In cases where a party contributes to the control of risk but does not assume the risk, then the potential upside or downside on taking risk, should be shared basis its contribution on control.

The concept of control and the financial capacity to assume risks is illustrated through the explanation below:

Company A does not:
- evaluate the financing opportunity,
- consider the appropriate risk premium; and other issues to determine the appropriate pricing of the financing opportunity, and
- does not evaluate the appropriate protection of its financial investment.

In these circumstances, Company A would not be entitled to any more than a risk-free return as an appropriate measure of the profits it is entitled to retain, since it lacks the capability to control the risk associated with investing in the financial asset.

The risk will be allocated to the enterprise which has control and the financial capacity to assume the risk associated with the financial asset, which is Company B. Company C assumes the utilization risk by exploiting the asset and marketing the asset’s capabilities and negotiating with customers.

**Location Savings:**

The 2017 OECD Transfer Pricing Guidelines specifies that the principles in relation to location savings as provided in Chapter IX of the said Guidelines are generally applicable even to transactions other than business restructuring. It provides specific guidance on the sharing of location savings between two or more enterprises which are as follows:

- Identify if location savings exist
- Quantification of location savings
- Retention of location savings within the MNE Group or passing on the same to ultimate customers
- If location savings not passed to end customers, then allocation of such savings amongst group entities
Assembled workforce and secondment of employees:

The Chapter also provides guidance on determination of an arm’s length price for transfer of assembled workforce and for secondment of employees.

It is important to note that transfer or secondment of employees may result in transfer of valuable know-how or other intangibles from one AE to another. For example, an employee from Company A seconded to Company B may have knowledge of a secret formula owned by Company A and may make that secret formula available to Company B for its commercial operations. In such cases, the provision of know-how should be separately analysed under the provisions of Chapter VI of 2017 OECD Transfer Pricing Guidelines.

There is specific guidance provided explaining circumstances which may warrant an arm’s length compensation for transfer of assembled workforce.

Significance from an Indian Transfer Pricing perspective

Guidance on risk analysis:

Indian Transfer Pricing Legislation does not provide for detailed guidance on risk analysis. However, the approach as proposed in Chapter I of the 2017 OECD Transfer Pricing Guidelines (i.e. delineation of international transactions) has been followed by Tax Authorities in the course of Transfer Pricing Audits in India.

The Indian Tax Authorities could now use the guidance on risk analysis as provided in Chapter I during the course of audit to determine whether an international transaction undertaken by a Taxpayer is in conformity with the arm’s length principle (whether the contractual arrangement is in line with the operational arrangement).

The guidance is a significant departure from the guidance provided under the 2010 OECD Transfer Pricing Guidelines. Accordingly, Taxpayers are required to evaluate and ensure that their arrangements and transfer pricing documentation are harmonious and in keeping with the conduct between the transacting AEs.

An analysis of the risks assumed and management of such risks in connection with a Taxpayer’s international transaction would be a critical point for:

- determining an arm’s length price for various constituents of an international transaction and
- benchmarking of the profitability of the various AEs who would be part of such an international transaction.

Further, an evaluation of Indian operations of the MNE Group should be undertaken as the for compliance with the conditions as provided in Circular 6 of 2013. The Indian Tax Authorities while relying in the Circular would also draw useful references from 2017 OECD Transfer Pricing Guidelines while undertaking transfer pricing audits.

Location Savings:

Indian Transfer Pricing Legislation includes location savings and assembled workforce as part of the definition of intangibles.

However, no guidance has been provided on allocating the benefit arising from location savings amongst various AEs participating in the transaction or for determining an arm’s length consideration for transfer of assembled workforce from one AE to another.

From an Indian Transfer Pricing perspective, location savings mostly constitute labour costs as labour costs are comparatively low in India when compared to developed countries. MNEs take advantage of the low labour costs in India and avail benefit of location savings. Taxpayers should ensure that the guidance as provided in this Chapter for determination of an arm’s length price is considered in relation to transactions involving location savings.

Further, a specific analysis should be undertaken to evaluate whether the comparable companies identified would factor for the location savings while determining the arm’s length price. Taxpayers should document any specific finding to mitigate any risk that may arise during the course of a transfer pricing audit.

There have been various judicial rulings that have adjudicated on the issue of location savings. The findings are summarised below:
In the case of M/s Watson Pharma Private Limited\(^3\), it was held by the Honourable Income Tax Appellate Tribunal ("Tribunal"), Mumbai, that "the Assessee as well as the AE operate in a perfectly competitive market and the Assessee does not have exclusive access to the factors that result in the location specific advantages. As a result, there is no super profit that arises in the entire supply chain. Thus, there is no unique advantage to the Assessee over competitors."

Further, in the case of GAP International Sourcing (India) Private Limited\(^4\), it was held by the Honourable Tribunal, Delhi, that "the arm's length principle requires benchmarking to be done with comparables in the jurisdiction of tested party and the location savings, if any, would be reflected in the profitability earned by comparables which are used for benchmarking the international transactions. Thus, in our view no separate / additional allocation is called for on account of location savings."

Though there is no guidance on allocating benefit arising from location savings in Indian Transfer Pricing Legislation, judicial precedents considered relevant factors such as competitive market, availability of local comparables, unique advantages, passing-on of the location specific advantages to the end-customers, etc., while adjudicating on this issue.

Further, in connection with location savings, it is imperative that MNEs also document the incremental costs associated (cost of transport etc.) with the movement of functions, assets and risks to India and location savings subsisting after catering to such incremental costs only be considered by Tax Authorities.

**Assembled workforce**

Employees transferred from one entity to another may have technical knowledge which may be critical for the conduct of the core activity of the MNE. Therefore, Taxpayers should also ensure that, while undertaking any transfer of assembled workforce or secondment of employees with significant know-how in relation to the core operations of the MNE, the guidance as provided in this Chapter for determination of an arm’s length price is considered.

Indian MNEs who second/ transfer employees outside/ to India would also have to evaluate whether such secondment/ transfer would merit a consideration, following the principles as contained in the 2017 OECD Transfer Pricing Guidelines. Further, where Indian MNEs who transfer work out of India to AEs for availing comparatively lower labour costs would also have to be cognisant to recognise location savings in accordance with the principles as contained in the 2017 OECD Transfer Pricing Guidelines.

While Indian Transfer Pricing Legislation recognises assembled workforce as an intangible, the 2017 OECD Transfer Pricing Guidelines also recognise that compensation for such transfers are warranted even if the employees transferred are not contributing anything other than routine services. Given, the same, one must evaluate whether local comparables engaged in similar activities would already factor assembled workforce as a factor for determination of the arm’s length price.

Accordingly, it would be important that companies document the reasons for employee transfers. The documentation should capture whether any intangible could be assigned or the transfer would be a routine transfer, the cost of which would have already be in built into the arm’s length price so determined.

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\(^3\) ITA 1423/Mum/2014 & ITA 1565/Mum/2014

\(^4\) ITA Nos. 5147/Del/2011 & 228/Del/2012
INTRODUCTION

Chapter II of the 2017 OECD Transfer Pricing Guidelines provides guidance on selection of the Most Appropriate Transfer Pricing Method (‘MAM’) for determination of the arm’s length price for an international transaction. The five methods advocated by OECD are categorized under two broad heads:

**Traditional Transaction Methods**
- Comparable Uncontrolled Price Method (“CUP”)
- Resale Price Method (“RPM”)
- Cost Plus Method (“CPM”)

**Transactional Profit Methods**
- Comparable Uncontrolled Price Method (“CUP”)
- Resale Price Method (“RPM”)
- Cost Plus Method (“CPM”)

**REVISIONS**

**CUP to benchmark commodity transfers:**

Considering the practical challenges in benchmarking commodity transfers, CUP may be the most appropriate method to benchmark such transactions.

Specific guidance has been provided about the use of quoted prices available on commodity stock exchanges as a CUP for benchmarking commodity transfers and how adjustments may be required to be made to such prices obtained from the commodity indices.

Some of the key characteristics that are required to be considered while benchmarking commodity transactions are:
- Pricing date;
- Physical features and quality;
- Contractual terms (period of contract, time and terms of delivery, transport costs, insurance, foreign currency terms, volume traded etc.).

Differentiating Transfer Pricing guidelines as per OECD and UN: The UNTP Manual for developing countries considers benchmarking commodity transactions using a separate method called as the ‘Sixth method’ or ‘the Commodity Rule.’ This Method is being used in various developing countries in many variations for arriving at the arm’s length price of import and export transactions of commodities such as grains, oil and oilseeds, oil and gas, mining and fishing products.

**Discussion Draft on revised guidance on TPSM**

As against the 2010 OECD Transfer Pricing Guidelines, the TPSM now considers control and assumption of risks for allocating profits to the entities in the MNE Group. This provides additional guidance to Taxpayers while applying TPSM between AEs. A discussion draft on Action Plan 10 of the BEPS project with respect to revised guidance on profit splits has been released by OECD for public comments.

**Significance from an Indian Transfer Pricing perspective**

**Updates to CUP**

The Indian Transfer Pricing Guidelines provide for the application of ‘any other method’ (apart from the detailed guidance provided on the five methods) to benchmark international transactions, provided, none of the five methods as specified the 2017 OECD Transfer Pricing Guidelines are suitable to benchmark the international transaction.

Though the Indian Transfer Pricing legislation does not specifically provide for the inclusion of benchmarking of commodity related transactions under the CUP method, the provision relating to application of any other method provide for flexibility. Further, owing to the use of the word “price charged” or “paid” in the
Indian Transfer Pricing Legislation for application of CUP, there has been protracted litigation on whether a quote would find acceptability for use as CUP. The guidance provided on use of a “quote” for benchmarking an international transaction may enable taxpayers (including those engaged in commodity trade) to have a useful reference point while dealing with protracted litigation arising from use of quotes while benchmarking international transactions.

**Update to TPSM**

**NEED FOR UPDATED GUIDANCE:** Given that the updated guidelines provide for delineation of transactions and remunerating contracting entities for value creation, updates to the guidance on application of TPSM is the need of the hour.

**PROVISION FOR LOSS SPLITS:** Indian Transfer Pricing Legislation does not specifically provide for loss splits, unlike the OECD 2017 Transfer Pricing Guidelines which provide for loss splits as well as profit splits. It would be interesting to see, if detailed guidelines are provided by the OECD for application of loss splits, (Currently, the discussion draft provides for loss splits) whether the same would be incorporated in the Indian Transfer Pricing Legislation.

**REVIEW OF CURRENT DOCUMENTATION:**
The MNE Groups ought to evaluate their current documentation to verify the applicability of TPSM as the MAM given the guidance provided in Chapter I on risks of the 2017 OECD Transfer Pricing Guidelines. The review should include review of agreements, operations and whether the revised guidance on TPSM is applicable in the facts of the case.

In the event TPSM is applicable, suitable factors (i.e. intangibles, costs savings etc.) ought to be considered while deciding on the parameters for the application of TPSM.

A summary of the various methods provided under the OECD, UN and Indian Transfer Pricing legislation is captured in the diagram below:
INTRODUCTION

Chapter III provides general guidance on the methodology to be adopted while undertaking comparability analysis. There are no significant changes that have been incorporated in this Chapter. However, given that the Chapter has references to other Chapters (i.e. Chapter I, Chapter VI, Chapter IX etc.) it would be important that a harmonious reading be undertaken while carrying out a comparability analysis.

The key contents of the chapter relate to:

- Providing guidance on the steps undertaken while doing a comparability analysis; and
- The approach to accepting or rejecting of comparable companies to the tested party identified.

The same has been captured below in the diagrams below:

**TYPICAL PROCESS FOR UNDERTAKING COMPARABILITY ANALYSIS**

- Interpretation of data collected
- Determination of years to be covered
- Possibility of comparability adjustments
- Identification of potential comparables
- Selection of most appropriate method to benchmark transactions
- Determination of available sources of information for external comparables
- Identification and review of internal comparables
- Understanding the controlled transaction
- Analysis of taxpayer’s facts

**Approaches to Identify Comparable Companies**

**Additive approach**
Companies first identified based on some information available with taxpayer and data collected subsequently

**Deductive approach**
Systematic search process undertaken to identify dataset and then quantitative and qualitative filters applied to identify comparable companies - more transparent than additive approach
Significance from an Indian Transfer Pricing perspective

The guidance provided for comparability analysis under the 2017 OECD Transfer Pricing Guidelines is largely similar to the Indian Transfer Pricing Legislation.

The guidance provided for comparability analysis under the 2017 OECD Transfer Pricing Guidelines is largely similar to the Indian Transfer Pricing Legislation.

- Use of additive approach: Indian Transfer Pricing Authorities are not open to the use of the additive approach to identify comparable companies as is accepted under the 2017 OECD Transfer Pricing Guidelines.
- Use of foreign comparables: Use of foreign comparable companies is not accepted by Indian Tax Authorities.

Given the above, it would be important to evaluate the use of additive approach or foreign comparables where suitable local comparable companies are not identified using the deductive approach. Further, use of guidance on qualitative and quantitative techniques prescribed by the OECD should be considered while maintaining transfer pricing documentation.
CHAPTER IV

Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes

INTRODUCTION
Chapter IV of the 2017 OECD Transfer Pricing Guidelines examines various administrative procedures that could be applied to:

- Minimize transfer pricing disputes; and
- Resolve any disputes that arise between Taxpayers and Tax Authorities or between different Tax Authorities.

Member countries of the Inclusive Framework on BEPS have agreed to a minimum standard with respect to treaty related disputes. Accordingly, some significant changes have been incorporated in Chapter IV of the 2017 OECD Transfer Pricing Guidelines:

Access to MAP:
Chapter IV of the 2017 OECD Transfer Pricing Guidelines now addresses the concern of Taxpayers in connection with denial of access to MAP in transfer pricing cases with treaty partners. Member countries have agreed to comply with the minimum standard of providing access to MAP in transfer pricing cases.

REVISIONS
Revisions to Chapter IV of the 2017 OECD Transfer Pricing Guidelines align with Action Plan 14 of the BEPS report. The introduction of measures to tackle BEPS should not lead to uncertainty for Taxpayers and unintended double taxation. Accordingly, the recommendations of Action Plan 14 find place in Chapter IV to help improve the dispute resolution mechanisms.

The primary concerns of taxpayers that are to be addressed vide changes to Chapter IV are:

- Lack of guidance on invoking MAP
- Denial of MAP
- Limited taxpayer participation
- Time limit under domestic law vis-à-vis treaty
- Suspension of demand collection
- Time taken for sentiment of disputes

The Chapter also addresses other general concerns of Taxpayers relating to the denial of access to MAP. These include:

- Provide access to MAP, whether or not:
  - the application of a treaty anti-abuse provision has been met; or
  - the application of an anti-abuse provision in the domestic law conflicts with the provisions of a treaty.
- Publish rules, guidelines and procedures regarding MAP (including guidance on specific information and documentation that a taxpayer is required to submit);
• Clarify that audit settlements between Tax Authorities and Taxpayers do not preclude access to MAP; and

• Commitment to ensure that both Competent Authorities are made aware of requests for MAP assistance.

India is not a signatory to the binding arbitration process. Accordingly, as of now, India has not committed to resolution of MAP cases within a specified timeframe.

Time limit:
The maximum duration prescribed for completion of MAP under the Chapter is 24 months. This will ensure speedy resolution of disputes between Taxpayers and Tax Authorities.

Suspension of collections:
The Chapter emphasises on the need for suspension of collections of disputed taxes and accrual of interests on filing of MAP for ensuring that the MAP negotiations may happen on a free and fair basis.

Secondary adjustment:
The OECD Transfer Pricing Guidelines recognise secondary adjustments in three forms:

• Constructive dividend;

• Constructive equity contribution; and

• Constructive loans.

The use of secondary adjustments by Tax Authorities in one country would mean that there is a possibility of double taxation unless correlative relief is provided by Tax Authorities of the other jurisdictions.

While the OECD Model Tax Convention is silent on secondary adjustments, the 2017 OECD Transfer Pricing Guidelines suggest that Tax Authorities should levy such secondary adjustments where it can be proved that the Taxpayer intended for disguising such pay-outs as dividend, loan or equity.

Multilateral/ Bilateral Safe Harbours:
The Chapter provides for the adoption of and guidance in relation to Multilateral or Bilateral Safe Harbour provisions. Though the implementation of Unilateral Safe Harbours have many benefits attached to them, the implementation of the same in one country may lead to taxable income being reported in another country which may not satisfy the arm's length principle resulting in double non-taxation or taxation.

Significance from an Indian Transfer Pricing perspective

Though the Indian government has taken several measures (risk based assessments, introduction of range concept, APA program etc.) to reduce litigation arising from transfer pricing the following merit attention:

• Introduction of time limit for settlement of disputes under MAP as proposed under the 2017 OECD Transfer Pricing Guidelines;

• Given the quantum of litigation in India arising from Transfer Pricing cases, MAP is frequently invoked. Accordingly, the need for strengthening this process with a view to making it more efficacious is often felt. There is currently no time limit for settlement of MAP disputes (except in the context of UK and US where a two-year period has been agreed upon), which often leads to significant delays in resolution of MAP applications. Given that India has not opted for mandatory binding arbitration to resolve transfer pricing disputes under MAP, there is an urgent need to take administrative steps to ensure that MAP process becomes more efficacious and timely.

• As of now, Taxpayers should evaluate their current disputes in place which could be covered as part of a bilateral MAP settlement.

• Consider negotiating Bilateral and Multilateral Safe Harbour for various activities to ensure ease of doing business in India;

• Introduction of provisions to stay collections under MAP with all treaty partners. At present, stay of collection under MAP is only applicable for MAP applications with limited treaty partners.

India has taken the first step in this regard by signing the Multilateral Instrument Accord in Paris.

• Secondary Adjustments: Another important aspect for Indian Tax Authorities to consider is the treatment of secondary adjustment. As of now, Indian Tax Authorities only recognise the concept of a secondary adjustment in the form of a constructive loan and levying of interest for non-remittance of amounts pertaining to secondary adjustments. Given the practical challenges arising from imposition of secondary adjustments and the double taxation arising therefrom, the Indian Tax Authorities may consider implementing some of the guidance provided by the OECD in this regard.
CHAPTER V
Documentation

INTRODUCTION
This Chapter provides guidance for Tax Authorities in developing rules and procedures on documentation to be maintained by Taxpayers and information to be sought during the course of transfer pricing audits. It also provides guidance to assist Taxpayers in identifying documentation to substantiate their transactions satisfying the arm’s length principle and Tax Authorities in facilitating tax examinations.

The 2010 OECD Transfer Pricing Guidelines emphasised the need for reasonableness in the documentation process from the perspective of both Taxpayers and Tax Authorities. However, the 2010 OECD Transfer Pricing Guidelines did not provide for a list of documents to be included in a transfer pricing documentation package nor did it provide clear guidance with respect to the link between the documentation process, administration of penalties and the burden of proof.

In order to balance the usefulness of data available to the Tax Authorities for transfer pricing risk assessments and the increased compliance burden on Taxpayers, the need for reconsidering the rules in relation to documentation was strongly felt. The revisions to Chapter V of the 2017 OECD Transfer Pricing Guidelines align with Action Plan 13 of BEPS Report.

REVISIONS
Risk-based Assessment:
The Chapter emphasises the importance for Tax Authorities to effectively utilize limited resources at their disposal to accurately identifying, evaluate and assess only those cases that warrant an in-depth review. Effective risk assessment becomes a pre-requisite for a focused and resource efficient audit.

Adoption of three-tiered approach to TP documentation:
In order to achieve the objective of usefulness of data to Tax Authorities with no increase in compliance burdens on the Taxpayers, guidance has been provided on adoption of a three-tiered documentation approach, which consists of:

MASTER FILE:
The Master file provides an overview of the MNE Group business. The Master file would assist Tax Authorities in evaluating the presence of significant transfer pricing risk while providing the Taxpayer an opportunity to satisfy the Tax Authorities without furnishing excessive amounts of information. The information contained in the master file is as follows:
- Nature of the MNE Group’s global business operations,
- Overall transfer pricing policies,
- Global allocation of income and economic activity;
- MNE group’s organisational structure;
- Description of the MNE’s business;
- Intangibles owned by the MNE;
- MNE’s intercompany financial activities; and
- MNE’s financial and tax positions.

LOCAL FILE:
The local file supplements the master file and focuses on information:
- relevant to the transfer pricing analysis related to transactions undertaken between the Taxpayer and its AEs in different countries and
- which are material in the context of the Taxpayer’s country’s tax system.

Such information would include relevant financial information regarding the specific transactions undertaken by the Taxpayer with its AEs, comparability analysis, and the selection and application of the MAM for each international transaction.

CbCR:
CbCR requires information relating to
- the global allocation of the income;
- taxes paid; and
- indicators on the location of economic activity among tax jurisdictions in which the MNE Group operates.

Additionally, it also requires a listing of all the Constituent Entities for which financial information is reported, including the tax jurisdiction of incorporation (if it is different from the tax jurisdiction of residence), as well as the nature of the main business activities carried out by that Constituent Entity.

All the above documentation is to be maintained by the Taxpayers on a contemporaneous basis.
Review and updation of Documentation:
The Chapter provides Documentation to be reviewed and updated annually to determine the accuracy and relevance of the functional and economic analysis while confirming the transfer pricing methodology.
However, the Chapter also provides relaxation for maintenance of documentation should the local legislation requirements provide for review and updation of the documentation every three years (except for updating financial data of comparable companies), where operating conditions remain unchanged.

Materiality threshold:
The CbCR requirement is for fiscal years commencing on or after January 1, 2016. The monetary threshold for CbCR is where the Group revenue equals to or exceeds EUR 750 million.

Confidentiality, Consistency and Appropriate use:
The Chapter prescribes conditions (i.e. confidentiality, consistency and appropriate use) to be satisfied by Tax Authorities for information obtained from Taxpayers during the course of an audit.

Information exchange:
The Chapter discusses information exchange between Tax Authorities in jurisdictions where the MNEs operate and it is applicable only between countries that are a party to the Convention on Mutual Administrative Assistance in tax Matters.

Significance from an Indian Transfer Pricing perspective

Risk based assessment
The Indian Tax Authorities have implemented a risk based assessment program. This has resulted in few cases being selected for scrutiny via audits while providing the field officers a greater opportunity to examine high risk cases in detail. The changes proposed in the 2017 OECD Transfer Pricing Guidelines only support the process which has been put in place by the Indian Tax Authorities.

Three-tiered documentation:
A three-tiered approach (Master file, Local file and CbCR) with respect to the documentation has been adopted by India, (aligning with Action Plan 13 of the BEPS project and Chapter V of the 2017 OECD Transfer Pricing Guidelines). Although India has supported the documentation recommendations, there is requirement for greater clarity in connection with the documentation details to be provided for as part of CbCR in India. Given that the first year of application of the three-tier documentation is Financial Year 2016-17, a notification in this regard from the Indian Tax Authorities is the need of the hour.

Taxpayers should evaluate the documentation requirements for:
- Applicability of maintenance of three-tiered documentation;
- Adhering to the minimum standards of documentation (details to be maintained) as per the Indian Transfer Pricing legislation or the 2017 OECD Transfer Pricing Guidelines (whichever documentation is more stringent) till specific guidelines have been issued in this regard by the Indian Tax Authorities;
- Identification of details as required under the three-tiered approach to ensure adequate details are available for compliance with the due date requirements;
- Review of the complete documentation to ensure that arm’s length price determination is aligned with the Transfer Pricing Guidelines keeping in mind the requirement of Substance over Form. Any deviation from policy would be apparent owing the multitude of data available with the Tax Authorities.

Information exchange:
India was a party to the Convention on Mutual Administrative Assistance in Tax Matters that was signed on May 12, 2016. India has also issued a Notification on July 28, 2017 wherein it notified the Multilateral Competent Authority Agreement on the Exchange of Information for CbCR.

Confidentiality of information
India is required to bring in more stringent laws on confidentiality of information obtained from the three-tiered documentation structure or through exchange of information.
INTRODUCTION
Chapter VI of 2017 OECD Transfer Pricing Guidelines provides guidance on determination of an arm’s length consideration for transactions involving the use or transfer of intangibles between AEs. Chapter VI is aligned with the BEPS Action Plans 8-10 (aligning transfer pricing outcomes with value creation).

Article 9 of the OECD Model Tax Convention seeks to determine the arm’s length nature of the transactions between AEs. It does not focus on the specific labels assigned to such transactions but rather focusses on the conditions within which such transactions have taken place.

Revisions to Chapter VI include items or activities that convey economic value whether or not they constitute an intangible. The revised Chapter focuses on the economic contributors to a transaction rather than lay emphasis on the labels ascribed to the various components of the chapter by the AEs (i.e. examine the substance of the transaction rather than focus on the form). The focus of the Chapter is to ensure that development, enhancement, maintenance, protection and exploitation (‘DEMPE’) functions of intangibles are appropriately rewarded.

REVISIONS

Definition of ‘Intangible’ and its identification:
The 2017 OECD Transfer Pricing Guidelines define the term intangible as “intended to address something which is not a physical asset or financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.”

Further, the 2017 OECD Transfer Pricing Guidelines have clarified the following, with respect to identification of intangibles:

- The existence of legal, contractual or other forms of protection may affect the value and returns of an intangible. However, the existence of such a contract does not necessitate the characterisation of an intangible for transfer pricing purposes but may provide a useful reference point.

Guidance on risk:
This Chapter provides guidance on risk in connection with intangibles, which requires harmonious reading with Section D of Chapter I of the 2017 OECD Transfer Pricing Guidelines.

Differentiates intangibles and local market conditions:
The Chapter distinguishes between an intangible and local market conditions. If local market conditions are not under the control of an entity, then such local market condition would not constitute an intangible for the purposes of Chapter VI of the 2017 OECD Transfer Pricing Guidelines.

All intangibles do not warrant a compensation:
The emphasis of the analysis is whether use/exploitation of an intangible provides a premium return or not? Where an intangible offers a premium return vis-à-vis the service or product being offered without the intangible, compensation is warranted for use or exploitation of the intangible.

Registration of an intangible is not a determining factor for ascertaining whether an intangible warrants remuneration. Only when an intangible has an ascertainable benefit on exploitation, can a remuneration be offered for it.

Further, in case of bundled intangibles one would have to examine there exists benefit for each intangible and only then a compensation could be provided for use or exploitation of the intangible.

Framework on analyzing transactions involving intangibles:
A six-step process on analysing transactions involving intangibles has been provided under Chapter VI of the 2017 OECD Transfer Pricing Guidelines. This process is consistent with the guidance for identifying the commercial or financial relations as provided in Chapter I of 2017 OECD Transfer Pricing Guidelines.
In analysing transactions involving intangibles, specific guidance is provided in this Chapter in respect of the following types of intangibles:

- Intangibles that are self-developed by a multinational group and transferred between AEs while still under development;
- Acquired or self-developed intangibles that serve as a platform for further development; or
- Other aspects, such as marketing or manufacturing which are particularly important to value creation.

Outsourced research and development:

This Chapter provides guidance on how to determine ownership, control and management in connection with outsourced research and development. If the legal owner performs none of the DEMPE functions, the benefits from the intangible should accrue to the entity undertaking outsourcing. This is in line with Chapter I of the 2017 OECD Transfer Pricing Guidelines which mentions that an entity should be entitled to the functions it actually performs, the assets it actually uses and the risks it actually assumes.

Funding of intangibles:

Funding and risk-taking are inter-related, i.e., the funding party contractually assumes the risk of loss of funds. However, the economically significant risk in an investment would be funding risks and operational risks cumulatively and not on an independent basis. The party assuming only financial risks, without assuming control over any other specific risk should only expect a risk-adjusted return on its funding.

The determination of an arm’s length consideration for funding of intangibles, including funding used for project finance, is currently being examined by the OECD and guidance in this regard would be provided in due course.

Guidance on assumption of various types of risks:

While undertaking a functional and risk analysis for intangibles some aspects which merit consideration have been discussed in the Chapter and guidance has been provided thereon as follows:

The six-step process is summarized below:

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<th>STEP</th>
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<td>01</td>
<td>02</td>
<td>03</td>
<td>04</td>
<td>05</td>
<td>06</td>
</tr>
<tr>
<td>Identification of economically significant intangibles with specifications</td>
<td>Analysing contractual arrangement to determine legal ownership, rights and obligations of entities in relation to intangibles</td>
<td>Undertaking functional analysis to determine actual conduct of parties on ground</td>
<td>Confirm consistency between contractual arrangement and conduct on ground</td>
<td>Delineate the controlled transaction based on conduct of parties</td>
<td>Determination of arm’s length price based on FAR of each entity</td>
</tr>
</tbody>
</table>

In analysing transactions involving intangibles, specific guidance is provided in this Chapter in respect of the following types of intangibles:

- Intangibles that are self-developed by a multinational group and transferred between AEs while still under development;
- Acquired or self-developed intangibles that serve as a platform for further development; or
- Other aspects, such as marketing or manufacturing which are particularly important to value creation.
Guidance on comparability of intangibles or rights in intangibles:

- Transactions involving transfer of intangibles or rights in intangibles: Guidance has been provided in relation to comparability factors for determination of an arm’s length price for an intangible – (i.e. exclusivity, extent and duration of legal protection, geographic scope, useful life, stage of development, rights to enhancements, revisions and updates, expectation of future benefits, etc.).

- Transactions involving the use of intangibles in connection with the sale of goods or the provision of services: In connection with the sale of goods or provision of services, the 2017 OECD Transfer Pricing Guidelines clearly state that there may not necessarily be a transfer of intangibles. However, the intangible may be exploited in the course of rendering services or sale of goods. Accordingly, an appropriate remuneration should be provided for the same while determining the arm’s length price for the international transaction being reviewed.

  - E.g. A car manufacturer uses valuable proprietary patents to manufacture cars for sale to associated distributors. The patents contribute significantly to the value of the cars. The patents and the value they contribute should be identified and taken into account in the comparability analysis of the transaction consisting in the sales of cars by the car manufacturer to its associated distributors, in selecting the most appropriate transfer pricing method for the transactions, and in selecting the tested party. The associated distributors purchasing the cars do not, however, acquire any right in the manufacturer’s patents. In such a case, the patents are used in the manufacturing and may affect the value of the cars, but the patents themselves are not transferred.

- Partially developed intangibles: The OECD Transfer Pricing Guidelines 2017, discourages cost based valuations generally as there is no correlation between the costs of developing an intangible and their value or transfer price once it is developed. Cost based valuations are valid only in certain cases such as intangibles used for internal business operations, particularly where the intangibles used are not unique and valuable.

- Hard to Value Intangibles (‘HTVI’): Transactions involving HTVI exhibit one or more of the following features:

  **HARD TO VALUE INTANGIBLES**

  - Intangible is only partially developed at the time of transfer
  - The intangible itself is not standalone a HTVI but has to be seen together with other intangibles
  - The exploitation requires a novel approach which at the time of the contract is untested
  - Intangible is used in connection with or developed under a Cost Contribution Arrangement or other similar arrangements
  - Transferred on a lump-sum basis

  In case of HTVI, as it is uncertain to determine the actual outcomes at the time of entering into the transaction, it is important to consider the anticipated remuneration (i.e. ex-ante – future benefit expected to be derived by a member of the MNE Group at the time of a transaction) and actual remuneration (i.e. income actually earned by a member of the MNE Group through exploitation of the intangible).

  The Tax Authorities would have to consider ex-post outcomes and evaluate the appropriateness of the ex-ante arrangements. Adjustments should be made, if the pricing undertaken at the inception of the transaction (ex-ante) is considered inappropriate.

  Adjustments are not necessary if the difference between ex-ante and ex-post outcomes does not have the effect of increasing or decreasing the compensation for the HTVI by more than 20%. Therefore, a tolerance band of 20% is permissible.

  In cases where the deviation in the ex-ante and ex-post outcomes is more than 20% for the HTVI, the 2017 OECD Transfer Pricing Guidelines provide that no adjustment should be made to the ex-ante price, where the Taxpayer is able to justify the
reasonableness of the assumptions adopted while determining the pricing of such transactions.

Significance from an Indian Transfer Pricing perspective

Detailed guidance on determination of arm’s length price for international transactions involving intangibles has not been provided in Indian Transfer Pricing Regulations. Only the term intangible has been defined in the Indian Transfer Pricing Regulations.

The Tax Authorities in India have been contesting the transfer pricing aspects relating to intangibles for several years. Some of the key factors deliberated by Indian Tax Authorities relate to the assumption and control of risk in connection with intangibles, valuation of partly developed intangibles, determination of arm’s length compensation for outsourced research and development services.

A few of the contentions and how the 2017 OECD Transfer Pricing Guidelines deal with such contentions is discussed below:

Royalty:

MNEs often enter into agreements for licensing brands, trademarks, know-how, design, technology, etc. with their AEs in India. Payments for licensing of intangibles is made in lump sum or by way of periodic payments or a combination of both types of payment. Intellectual property, which is owned by one entity and used by another entity, generally requires a royalty payment as consideration for its use. The key consideration in this regard has been the determination of an arm’s length charge of royalty, finding comparables in the public domain with sufficient information for undertaking a comparability analysis.

Specific guidance has been provided in the OECD TP Guidelines, explaining, when is payment for royalty justified for exploitation of an intangible provided by an AE (i.e. only when use of the intangible provides some quantifiable benefit to the licensee).

Further, Taxpayers should consider the detailed guidance provided for identification of comparable companies in connection with the intangible licensed. This would provide a platform for Taxpayers to justify the pricing and need for payment of royalties in connection with the intangible licensed.

Taxpayers should evaluate the guidance and review their documentation to ensure that their transfer pricing policy is aligned to remunerate entities engaged in value creation.

Contract Research & Development (‘R&D’) activities and other outsourced services:

Indian Tax Authorities have contested whether outsourced R&D centres in India truly operate as risk mitigated and limited function centres. The issues examined in arriving at conclusions generally relate to:

Whether the Indian subsidiary bears economically significant risks and performs control and research functions independently and whether the Indian Subsidiary has been remunerated with an appropriate return for the functions performed and risks assumed.

Considering the revision in Chapter I and Chapter VI as contained in the 2017 OECD Transfer Pricing Guidelines, an Indian Subsidiary of an MNE Group ought to undertake a detailed analysis of the risks borne and functions undertaken by it vis-à-vis its AE. In the event that there is any discrepancy between the current contractual and operational structure, suitable steps should be taken to align the arrangement and the transfer pricing policy in connection with such services.

In an Indian context, the Indian Tax Authorities have issued Circular 6 of 2013 which clarifies when an entity would be regarded as rendering R&D services warranting a higher remuneration or share of profits in the Indian context.

While BEPS Reports and the updated 2017 OECD Transfer Pricing Guidelines do not necessarily deal with some of the quantification methodologies discussed in the Circular, the Circular states how Indian Tax Authorities would establish contribution of the so-called “Limited Risk Captive Service Provider” to the value chain of MNE Groups. Accordingly, Taxpayers should necessarily revisit the impact of the said Circular given the guidance provided in the 2017 OECD Transfer Pricing Guidelines.
Marketing Intangibles – Application of Bright line concept:

Transfer Pricing aspects of marketing intangibles have been a focus area for the Indian Tax Authorities. Many revisions that have currently taken place in the 2017 OECD Transfer Pricing Guidelines have been questioned by the Tax Authorities in India.

The functions carried out by Indian subsidiaries of an MNE Group relating to marketing, market research and market development, have been the subject matter of transfer pricing adjustments in India. The expenditure incurred on marketing functions has been subjected to litigation on the premise that the Indian Taxpayers were incurring these expenses for and on behalf of their parent companies outside India, and:

- such expenses promoted the brands/ trademarks that are legally owned by foreign parent AEs;
- such expenditures created or developed marketing intangibles in the form of brands/ trademarks, customer lists, dealer/ distribution channels, etc. even though the Indian company may have had no ownership rights in these intangibles.

Accordingly, Indian Tax Authorities contended that the functions carried out in India, were in the nature of development of intangibles owned by the AEs and hence the Indian company deserved a compensation for such services rendered.

The UN TP Guidelines also mention that the above functions result in the below mentioned benefits:

- Direct Benefit: By way of increased revenue from the territory on account of Sale/ Royalty/ Fee for Technical Services etc. In many of the cases, such functions may have an impact on revenue enhancement of the AEs in other parts of the world. For example, sponsorship of events or sports watched in many countries, launching of brands developed in India in other parts of the world etc.
- Indirect Benefit: Development of Market: AEs of the Indian company, who are owners of intangibles, obtain an advantage in terms of development of market for themselves. While this kind of advantage builds over a period of time, it is manifested in different ways. For example, when the AE enters into an agreement with a third party for directly selling goods in India. It is observed in many cases that agreements are concluded in India by the foreign AEs with retail chain companies or e-sellers or large corporate houses, etc. Here, the awareness about the trade intangibles owned by the AE, which were not well-known in the Indian market, is enhanced by the marketing efforts made by the Indian company, thus adding value to the intangibles.

Some of the contentions of the Tax Authorities now find acceptance by the OECD and hence Taxpayers should undertake an analysis of whether they are creating any marketing intangibles for their AEs in India.

However, judicial precedents in connection with marketing intangibles clearly spell out that indirect benefit and conduct of parties both in terms of contract and operations should be considered while determining whether an intangible has been created or not.

It would be interesting to keep a close eye on the future judicial pronouncements given that the OECD has partly provided credence to approach of the Tax Authorities in India.

Hard to Value Intangibles

Given the clarity that has been provided in the 2017 OECD Transfer Pricing Guidelines, the Taxpayers should ensure/ revisit their valuation of HTVIs to ensure that the documentation for justification is in compliance with the methodology prescribed.

While justifying any deviation in the ex-ante price and ex-post price, the documentation that was maintained contemporaneously (i.e. at the time of entering into the transaction) would have to present sufficient credible evidence that any material differences between the projections and the actual profits were due to unforeseeable developments or the realization of properly identified and priced risks.

Given the treatment of HTVIs, Taxpayers may also implement checks that independent parties use to mitigate the risk arising from uncertainty in valuing intangibles, such as contractual provisions. In situations with high uncertainty, Taxpayers may want to cap the time frame of the agreement or include clearly defined price adjustment clauses that determine a new price.
CHAPTER VII

Special consideration for Intra-Group Services

INTRODUCTION

Chapter VII discusses issues in relation to intra-group services, i.e.,

- whether a service has been rendered by one group entity to another; and
- determination of an arm’s length price in connection with such services rendered (including whether any compensation is warranted at all).

MNE Groups generally make arrangements for one or more entities to perform certain functions on behalf of the Group (i.e., to obtain benefits from centralization of functions within the Group). Such services are typically in the nature of administrative, technical, financial and commercial services. Such services are known as intra-group services in the transfer pricing context.

It is important to note that MNE Groups operating on a non-centralised model would not be offering intra-group services and only centralised services would be covered within the ambit of the Chapter.

How to identify if an intra-group service has been provided?

“Benefits test” is an approach through which an intra-group service can be identified. Intra-group service is said to have been provided by one AE to another if:

- such service benefitted the recipient AE with economic or commercial value to enhance or maintain its business position; and
- an independent enterprise would have been willing to pay for such service or whether the entity would have performed the activity in-house itself.

REVISIONS

The revisions in this Chapter encompassed the need to determine whether an intra-group service has enhanced the economic value of the AEs through provision of services. In this regard, the 2017 OECD Guidelines have also considered other variances that MNE Groups may have in their business models that may or may not give rise to intra-group services particularly.

Duplication of services:

Duplication services are those that are provided by one group member to another member, where such services are also performed by the recipient entity or are availed from a third party by such recipient entity.

EXCEPTION: TEMPORARY Duplicative SERVICES

The 2017 OECD Transfer Pricing Guidelines also carve out the exception for temporary duplicative services. For example, there would be no intra-group services if an MNE Group is reorganizing to centralize its management functions. Another example would be the case where an MNE Group undertakes to duplicate services to rectify a wrong business decision (i.e., by getting a second legal opinion on a subject).

Concept of viable economic alternative discussed in relation to whether a profit charge is warranted or not for intra-group services rendered.

In cases where the cost of rendering such intra-group services by an AE to the recipient AE is higher than what could have been locally procured by the recipient AE, the 2017 OECD Transfer Pricing Guidelines carve out an exception and state that no mark-up should be charged in such cases.

Low-Value adding intra-group services:

This Chapter:

- identifies certain low-value adding intra group services that do not warrant high profit mark-ups owing to the routine nature of such services; and
- provides guidance on documentation of low value adding services which would reduce the compliance burden.

Characteristics of low-value adding intra-group services are:

- Such services are of a supportive nature;
- Such services are not part of the core business of the MNE group, i.e., not profit earning activities or contributing to economically significant activities;
- Such services do not use or lead to the creation of unique or valuable intangibles; and
- Such services do not involve the assumption or control of substantial or significant risk by the service provider including the creation go significant risk.
Examples of low-value adding intra-group services as provided in the 2017 OECD Transfer Pricing Guidelines are provided below:

**SUMMARY OF EXAMPLES OF LOW-VALUE ADDING INTRA-GROUP SERVICES**

| Accounting and Auditing | Accounting and Auditing |
| Human resource activities | Activities with regard to tax obligations |
| Information technology services | General services |
| Internal and external communications and public relations support | |

**LIST OF ACTIVITIES THAT DO NOT QUALIFY FOR A SIMPLIFIED APPROACH ARE**

- Services constituting the core business of the MNE group
- Services of corporate senior management (other than management supervision of services that qualify as low value-adding intra-group services)
- Insurance and reinsurance
- Research and development services (including software development unless falling within the scope of information technology services as provided in the above paragraph)
- Manufacturing and production services
- Purchasing activities relating to raw materials or other materials that are used in the manufacturing or production process
- Extraction, exploration, or processing of natural resources
- Financial transactions
- Sales, marketing and distribution activities
What is a simplified approach? A simplified approach is one that is suggested to be adopted in the case of low-value adding intra-group services. The approach can be explained as follows:

- **Benefit test not to be applied:** The Chapter suggests that the Tax Authorities should avoid applying the benefit test to low-value adding intra-group services as this would require more efforts than the benefits from investigating such services.

- **Determination of cost pools:** The costs incurred by all the members of the MNE Group in providing intra-group services should be pooled. Such pooling of costs should consist of direct and indirect costs of rendering the service while disregarding costs that are directly incurred by one member on behalf of another.

- For example, in creating a pool of payroll costs, if group company A provides payroll services solely to group company B the relevant costs should be separately identified and omitted from the pool. However, if group company A performs payroll services for itself as well as for company B, the relevant costs should remain within the pool.

- Allocating low-value adding service costs: For the allocation of low-value adding service costs, the members should use appropriate allocation keys in light with Chapter II of the guidelines.

- Guidance on cost build-up for intra-group services: The Chapter recommends a mark-up of 5% of the low-value adding service costs in the pool of costs except for pass-through costs, irrespective of the categories of services mentioned above.

- Withholding taxes: The Chapter recommends that withholding taxes to be levied by countries only on the profit element of the low-value adding intra-group services and not on the entire cost-plus. This would mean that if the cost of the services is INR 100 and mark-up there on is INR 5, the total value of the service is INR 105. Presently, withholding taxes are charged on INR 105 and not INR 5 as is proposed by the OECD.

- Guidance on documentation requirements: An MNE Group opting for the simplified approach as mentioned above, is required to maintain the documentation and information provided below:

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<tr>
<th>SERVICES RELATED</th>
<th>CONTRACTUAL RELATED</th>
<th>OTHERS</th>
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<tbody>
<tr>
<td>Description of the categories of low value-adding intra-group services provided</td>
<td>Written contracts or agreements for the provision of services</td>
<td>Documentation and calculations showing the determination of the cost and of the mark-up applied thereon, in particular a detailed listing of all categories and amounts of relevant costs, including costs of any services provided solely to one group member</td>
</tr>
<tr>
<td>Identity of the beneficiaries</td>
<td>Any modifications to those contracts and agreements reflecting the agreement of the various members of the group to be bound by the allocation rules of this section</td>
<td>Calculations showing the application of the specific allocation keys</td>
</tr>
<tr>
<td>Reasons justifying that each category of services constitute low value</td>
<td>Rationale for the provision of services within the context of the business of the MNE</td>
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</tr>
<tr>
<td>Confirmation of the mark-up applied</td>
<td>Reasons justifying that each allocation keys produce outcomes that resonably reflect the benefits received</td>
<td></td>
</tr>
<tr>
<td>Documentation and calculations showing determination of the cost and of the mark-up applied thereon, in particular a detailed listing of all categories and amounts of relevant costs, including costs of any services provided solely to one group member</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Description of the selected allocation keys</td>
<td>Description of the benefits or expected benefits of each category of services</td>
<td>Such written contracts or agreements could take the form of a contemporaneous document identifying the entities involved, the nature of the services, and the terms and conditions under which the services are provided.</td>
</tr>
</tbody>
</table>
Significance from an Indian Transfer Pricing perspective

The Indian Tax Authorities have embraced the new chapter on intra-group services.

Benefits test approach:
The Indian Tax Authorities have historically contended the need for a benefits test approach for determining an arm’s length remuneration for intra-group services. With the changes as contained in 2017 OECD Transfer Pricing Guidelines, it would be advisable that the Taxpayers review their documentation to ensure adequate details are maintained capturing the nature, benefits of and arm’s length charge for such intra-group services.

Revised Safe Harbour Rules:
The 2017 OECD Transfer Pricing Guidelines are aligned with Indian Transfer Pricing Legislation for low-value added services, which is captured within the ambit of the revised Safe Harbour Guidelines. The arm’s length charge for such services has been capped at 5 percent of cost.

Applicable to Indian MNEs and Shared Service centers in India of MNEs
The 2017 OECD Transfer Pricing Guidelines do not distinguish between low-value added services rendered by Headquarter companies or Shared Service Centers. Accordingly, the Guidelines are equally applicable to Indian MNEs and Shared Service Centers based out of India.
CHAPTER VIII

Cost Contribution Arrangements

INTRODUCTION
This Chapter discusses the cost contribution arrangements between AEs and determination of an arm’s length consideration for the same.

What is a Cost Contribution Arrangement?
A Cost Contribution Arrangement (‘CCA’) is defined in this Chapter as
- a contractual arrangement among business enterprises
- to share the contributions and risks involved in the joint development, production or the obtaining of intangibles, tangible assets or services
- with the understanding that such intangibles, tangible assets or services are expected to create benefits for the individual businesses of each of the participants.

REVISIONS
The revised Section D of Chapter I provide detailed guidance on the application of arm’s length principle not based only on the functions performed or assets utilised but also on the risks assumed and on the financial capacity to assume such risks. Basis this, Chapter VIII required a significant change with respect to distributing contributions of the profits obtained from the CCA between participants who perform significant functions and have control over risks of undertaking the CCA.

Types of CCAs

Current contributions to the development of intangible to be valued at cost.
Contributions to a CCA would take the form of:

Disregards entities that do not control and assume risks in the CCA for the purpose of profit sharing:
In line with Section D of Chapter I (i.e. application of arm’s length principle), this Chapter also specifies that those participants to the CCA that:
- do not have control over the economically significant risks and
- do not have the financial capacity to assume risks
would not be entitled to a share in the profits arising out of the CCAs. Such participants would only be entitled to a routine return.

Current contributions to the development of intangible to be valued at cost.
Contributions to a CCA would take the form of:

All contributions should be valued and accounted for in a CCA. Based on the contributions made by the participants, the expected benefit would also be shared amongst the participants.

In valuing contributions, distinctions should be drawn between contributions of pre-existing value and current contributions.
For administrative purposes, it is recommended that the current contributions be valued at cost for the purposes of this Chapter.

In this case, the pre-existing contributions should recover the opportunity cost of the ex-ante commitment (at the time of entering into the CCA) to contribute resources to the CCA.

If the differences between value and cost of current contributions are insignificant, then for practical reasons, the current contributions can be valued at cost in services CCAs.

Significance from an Indian Transfer Pricing perspective

Importance of control over risks

The Chapter signifies that all participants should have control over risks and functions in connection with their contribution to the CCA. This has been the historical stance of the Tax Authorities in India. Accordingly, adequate documentation should be maintained in this regard.

The requirement for all contributors to CCA having control may be onerous given that only one party maintains control over the operations of the CCA. Taxpayers should review whether adequate documentation can be maintained in this regard to justify such payments.

Documentation requirements

The documentation requirements would be consistent with the requirements as contained in Chapter V and VI of the 2017 OECD Transfer Pricing Guidelines. Taxpayers should evaluate whether sufficient documentation has been maintained justifying the contributors to the CCA and in the event adequate documentation has not been maintained, the same should be maintained.
INTRODUCTION

Business restructurings are typically accompanied by a reallocation of profit potential among the members of the MNE Group. The objective of the chapter is to ensure that reallocation of profit potential is consistent with the arm’s length principle and its applicability with business restructurings. Business restructuring broadly includes termination or substantial renegotiation of existing arrangements.

REVISIONS

The changes proposed to the 2017 OECD Transfer Pricing Guidelines largely align with the changes proposed in Action Plans 8-10 and 13 of the BEPS Project.

Delineation of a transaction

The first step in analysing the TP aspects of a business restructuring is to accurately delineate the transactions that comprise the business restructuring. The aspects meriting attention are commercial or financial relations and the conditions attached thereto.

The delineation should assist in determining the following which concluding whether a charge is warranted for Business Restructuring:

- Identification of commercial and financial relationships between MNE AEs who are part of the restructuring;
- Understanding the conditions attached in connection with delineation of the transaction;
- Documentation of business rationale for the proposed restructuring; and
- Pre and post analysis of the functions, assets and risk to understand how the same has changed pre and post restructuring.

Guidance on valuation for business restructuring

The determination of an arm’s length compensation for business reconstruction would not be an aggregation of the components of the business restructuring. In particular, if the transfer of an ongoing concern comprises multiple contemporaneous transfers of interrelated assets, risks, or functions, valuation of those transfers on an aggregate basis may be necessary to achieve the most reliable measure of the arm’s length price for the ongoing concern. Valuation techniques that are used, in acquisition deals, between independent parties may prove useful to valuing the transfer of an ongoing concern between associated enterprises.

Significance from an Indian Transfer Pricing perspective

The following is an indicative list of documents that should be maintained as part of the restructuring exercise:

- Commercial rationale for re-structuring;
- Documentation regarding roles and responsibilities of various Group entities pre and post the restructuring;
- Benchmarking analysis to justify the arm’s length pricing of the restructuring;
- Documentation of the realistically available options;
- Substance of the Taxpayer to assume the risk associated with the restructuring.

Exit charge an Indian context

Section F of Chapter IX deals with indemnification of the restructured entity. However, in an Indian context following are the important plans for consideration:

- The arm’s length principle does not require compensation for a mere decrease in the expectation of an entity’s future profits or for a mere transfer of FAR.
- Exit charge arises only where there is a transfer of something of value or a termination or substantial renegotiation that would be compensated between independent enterprises in comparable circumstances.
- The following factors to be seen to determine whether exit charge is payable or not:
  - Whether there is a written or formal arrangement for indemnification in case of termination or renegotiation?
  - Whether the terms of the arrangement and the existence or non-existence of an indemnification (as well as the terms of such a clause where it exists) are arm’s length.
  - Whether another party dealing at arm’s length would have been willing to indemnify the one that suffers from the termination or renegotiation of the agreement?
Way forward

The revisions in the OECD Transfer Pricing Guidelines are largely aligned to the Indian Transfer Pricing Legislation. Accordingly, it is important for Taxpayers, to consider the following:

Review of current operational structure:
Taxpayers should evaluate whether their contractual arrangements are in line with their operational arrangements (i.e. substance and form of international transactions are aligned).

The review should encompass a review of the risks assumed by various constituents of the international transaction (including the ability to finance, manage and assume such risks).

Review of current disputes:
It is important that Taxpayers review their current disputes. As part of the review, the Taxpayers may consider whether the additional guidance provided in the 2017 OECD Transfer Pricing Guidelines would mitigate the risk.

Given that the timelines provided for resolution of MAP, Taxpayers should re evaluate invoking MAP for dispute resolution.

Documentation requirements:
There are no specific guidelines provided by Indian Tax Authorities as regards the content to be maintained as part of the Master file, Local file and CbCR. In the absence of any specific guidance, Taxpayers could consider the 2017 OECD Transfer Pricing Guidelines as the minimum documentation to be maintained.

Intangibles:
A detailed analysis of the intangibles owned by the Group should be undertaken considering the DEMPE functions. The benefits enjoyed by the Group owing to the exploitation of intangibles should be apportioned basis the contributors to the DEMPE functions.

Another significant point for consideration is whether a charge is required for licensing or transfer of an intangible. Unless any specific advantage is received by the licensee/transferee of the intangible no charge should be paid for use of such intangibles. Adequate documentation should be maintained to explain the benefit to the licensee/transferee from use of the intangible.

Benefits tests analysis for intra-group services:
In respect of intra-group services availed/provided by the Indian entities, it is important to review and evaluate the benefits that have arisen from the availing of/provision of such intra-group services. Adequate documentation should be maintained justifying any charges.

Review of data captured in CbCR:
Evaluation of data captured as part of the CbCR is a significant activity to be undertaken by Taxpayers. Attention should be given to jurisdictions which are subjected to low or no taxes to ensure that there is adequate substance in such organisations which would align with the profits retained by Group Companies in such jurisdictions.
Comparison of 2017 OECD Transfer Pricing Guidelines vis-à-vis 2010 OECD Transfer Pricing Guidelines and Indian Transfer Pricing Guidelines

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<tbody>
<tr>
<td>I – The Arm’s Length Principle</td>
<td>• Arm’s Length Principle is the international transfer pricing standard to be used for tax purposes.</td>
<td>• Arm’s Length Principle is the international transfer pricing standard to be used for tax purposes.</td>
<td>• Indian Transfer Pricing Legislation is based on the arm’s length principle.</td>
</tr>
<tr>
<td>Guidance on Risks:</td>
<td>• Section D of the Chapter has been updated in conformity with Action Plan 9 of the BEPS report. The key components/plans in this regard have been provided below:</td>
<td></td>
<td>• Guidance on Risks:</td>
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<td></td>
<td>• Focus on contractual terms now extended to include examination of conduct between AEs in connection with their dealings.</td>
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<td>• Indian Transfer Pricing Legislation does not provide for the detailed guidance on risk analysis. However, the approach as proposed in</td>
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<td>• Provides guidance on risk analysis – i.e. (i) identification of risk (ii) contractual assumption of risk (iii) evaluation of AEs who actually control and mitigate risk (iv) confirm whether entity assuming risk actually controls/mitigates the risks (v) delineation of transactions based on relevant characteristics of the transaction and pricing according to the same.</td>
<td></td>
<td>• Chapter I of the 2017 OECD TP Guidelines has been followed by Tax Authorities in the course of Transfer Pricing Audit.</td>
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<td>Accurately delineated transaction:</td>
<td>• Focus now on “accurately delineated transaction” vis-à-vis “actual transaction” i.e. propagates evaluation of each leg of a transaction independently vis-à-vis aggregated approach.</td>
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<td>Location Savings:</td>
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<td>• Guidance on how to share benefits of locational savings between AEs.</td>
<td></td>
<td>• While the Indian Transfer Pricing Legislation includes location savings as part of the definition of intangibles, no guidance has been provided for determining an arm’s length remuneration for transfer of such locational savings.</td>
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<tr>
<td>Assembled Workforce:</td>
<td>• Guidance on determination of an arm’s length compensation for transfer of assembled workforce and secondment of employees.</td>
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<tr>
<td>II – Transfer Pricing Methods</td>
<td>• Provide guidance on the selection of the Most Appropriate Transfer Pricing Method and describes the traditional and transactional profit Methods.</td>
<td>• Changes to the Chapter are summarised below:</td>
<td>• Indian TP Regulations provide for detailed guidance on the various transfer pricing methods</td>
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<tr>
<td>Comparable Uncontrolled Price (‘CUP’) Method:</td>
<td>• This is largely aligned with earlier provisions. However, specific guidance has been included to benchmark commodity related transactions while utilizing the CUP Method</td>
<td>Comparable Uncontrolled Price (‘CUP’) Method:</td>
<td>Comparable Uncontrolled Price (“CUP”) Method:</td>
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<td></td>
<td>• TPMS is to consider the control and assumption of risks for allocating profits to the entities in the MNE Group which provides additional guidance while applying PSM between AEs.</td>
<td></td>
<td>• Indian TP Regulations provide for the selection of “Other Method” for determining the arm’s length price. This provides for flexibility in terms of benchmarking commodity related transactions</td>
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<td></td>
<td>• A discussion draft on Action 10 of the BEPS project with respect to revised guidance on profit split has been released by OECD for public comments.</td>
<td>Transactional Profit Split Method (‘TPSM’):</td>
<td>Transactional Profit Split Method (‘TPSM’):</td>
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<td>• Updated guidance is required on the application of TPSM in line with the delineation of transactions and remuneration of contracting entities for value creation</td>
<td>• While the OECD TP Guidelines provide for loss split as well as profit splits, Indian Transfer Pricing Legislation does not provide for loss splits</td>
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<td></td>
<td></td>
<td>• While the OECD TP Guidelines provide for loss split as well as profit splits, Indian Transfer Pricing Legislation does not provide for loss splits</td>
<td>Review of current documentation, involving review of agreements, on ground operations also for the applicability of TPSM,</td>
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<tr>
<td>III – Comparability Analysis</td>
<td>Provides general guidance on the methodology to be adopted while undertaking comparability analysis</td>
<td>No significant changes have been incorporated in this Chapter. However, given that the Chapter has references to other Chapters (i.e. Chapter I, Chapter VI, Chapter IX etc.), it would be important that a harmonious reading be undertaken while carrying out a comparability analysis.</td>
<td>The guidance provided for comparability analysis under the 2017 OECD Transfer Pricing Guidelines is largely similar to the Indian Transfer Pricing Regulations.</td>
</tr>
<tr>
<td>IV – Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes</td>
<td>Examines various administrative procedures that could be applied to minimize transfer pricing disputes.</td>
<td>Mandatory Binding Arbitration: Member countries of the Inclusive Framework on BEPS have agreed to a minimum standard with respect to treaty related disputes.</td>
<td>Mandatory Binding Arbitration: India has not opted for mandatory binding arbitration.</td>
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<td>Access to MAP: Provides guidance as regards the concern of Taxpayers for denial of access to MAP in TP cases with treaty partners.</td>
<td>Time Limit: Currently there is no time limit for settlement of disputes under MAP.</td>
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<td>Time Limit: Maximum duration prescribed for completion of MAP is 24 months.</td>
<td>Suspension of collections: Stay of collection under MAP currently is only applicable for MAP applications with limited treaty partners. Similar relief could be invoked for MAP with other treaty network countries.</td>
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<td>Suspension of collections: Emphasis on suspension of collections on filing of the MAP.</td>
<td>Secondary Adjustments: Currently, the Indian TP legislation recognises the concept of secondary adjustment in the form of a constructive loan and interest is levied for non-remittance of amounts pertaining to secondary adjustment.</td>
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<td>Secondary Adjustments: Tax Authorities should avoid levying secondary adjustments unless proved that the taxpayer intended for disguising such payouts as dividend, loan or equity.</td>
<td>Multilateral / Bilateral Safe Harbours: Indian TP Regulations provide for only Unilateral Safe Harbour provisions.</td>
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<td>Multilateral / Bilateral Safe Harbours: Adoption of and guidance in relation to Multilateral or Bilateral Safe Harbour provisions.</td>
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<tr>
<td>V – Documentation</td>
<td>Provides general guidance for Tax Administrations in developing rules and procedures on documentation to be maintained by Taxpayers and information to be sought in connection with transfer pricing enquiries.</td>
<td>Changes in this Chapter align with Action plan 13 of BEPS Report. A summary of the changes has been provided below:</td>
<td>Risk-based assessment: Indian Tax Authorities have also adopted a risk based approach to transfer pricing audits.</td>
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<td></td>
<td>Risk-based assessment: Guidance on risk based assessment to be undertaken by Tax Authorities.</td>
<td>Three-tiered documentation: The Indian Transfer Pricing Regulations have been updated to include the three-tier structure for documentation to be maintained.</td>
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<td>Adoption of three-tiered approach to TP documentation: Three-tiered approach to TP documentation- Master file, Local file and CbCR.</td>
<td>Information exchange: India was a party to the Convention on Mutual Administrative Assistance in tax Matters that was signed on May 12, 2016. India has also issued a notification on July 28, 2017 wherein it notified the Multilateral Competent Authority Agreement on the Exchange of Information for CbCR.</td>
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<td>Review and updation of Documentation: Documentation to be maintained contemporaneously and update either yearly or periodically based on local legislation requirements.</td>
<td>Confidentiality of information: India is required to bring in more stringent laws on confidentiality of information.</td>
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<td>Materiality threshold: Materiality threshold prescribed for maintenance of documentation.</td>
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<td>Confidentiality, Consistency and Appropriate use: Prescribes conditions to be satisfied by Tax Authorities as regards information obtained from Taxpayers during the course of audit (i.e. confidentiality, consistency and appropriate use).</td>
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<td></td>
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<td>Information exchange: Introduces the concept of information exchange between Tax Authorities in jurisdictions where the MNEs operate.</td>
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<td>VI – Special Consideration for Intangibles</td>
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<tr>
<td>• Discusses the special considerations that arise in seeking to establish whether conditions made or imposed in transactions between AEs involving intangible property transactions reflect arm’s length.</td>
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<td>• Changes in this chapter align with Action plans 8-10 of the BEPS Report. A summary of the changes has been provided below:</td>
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<tr>
<td>• Guidance on risk: Provides specific guidance on risk in connection with intangibles – requires harmonious reading with Section D of Chapter I.</td>
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<tr>
<td>• Differentiates intangibles and local market conditions: Highlights the difference between an intangible and local market conditions – no control or ownership over local market conditions would not constitute an intangible.</td>
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<tr>
<td>• All intangibles do not warrant a compensation: Highlights that not all intangibles warrant a compensation – similar to the contention of the Indian Tax Authorities that unless an intangible provides an ascertained benefit the same warrants no compensation.</td>
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<td>• Framework provided for analysing transactions involving intangibles: A six-step process on analysing transactions involving intangibles has been provided.</td>
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<tr>
<td>• Outsources research and development: Provides specific guidance on how to determine ownership, control and management in connection with outsourced research and development (i.e. if legal owner performs none of the DEMPE functions, the benefits from the intangible should accrue to the entity undertaking outsourcing).</td>
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<td>• Funding of intangibles: The determination of an arm’s length consideration for funding of intangibles is being worked and further guidance would be shared on the same.</td>
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<tr>
<td>• Guidance on assumption of various types of risks: Some aspects that merit consideration while undertaking a functional and risk analysis for intangibles have been provided.</td>
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<tr>
<td>• Guidance on comparability of intangibles or rights in intangibles: Includes guidance on comparability factors for determination of an arm’s length price for intangibles or rights in intangibles.</td>
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<tr>
<td>• Use of intangibles with sale of goods or provision of services: Provides guidance with respect to transactions that involve use of intangibles exploited in the course of rendering of services or sale of goods.</td>
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<td>• Partially developed intangibles: Discourages cost based valuations in respect of partially developed intangibles.</td>
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<tr>
<td>• Hard to Value Intangibles: Provision of tolerance band of 20% with respect to pricing of Hard to Value Intangibles (‘HTVI’). Also states that where the deviation is more than 20% in case of pricing of HTVI, no adjustment should be made where the Taxpayer is able to justify the pricing of the HTVI and the assumptions adopted.</td>
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<tr>
<td>• Detailed guidance on Intangibles: Has not been provided in Indian Transfer Pricing Regulations. The term intangible has been defined in the Indian Transfer Pricing Regulations and no other specific guidance (i.e. identification, pricing etc.) has been provided.</td>
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<td>• Historical contentions: Indian Tax Authorities have historically contended that not all intangibles warrant a charge and in the event that the entity to whom work has been outsourced undertakes all significant DEMPE functions, the profits arising from the intangibles should accrue to the entity to whom the work has been outsourced.</td>
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<td>VII – Special consideration for Intra-Group services</td>
<td>• Discusses issues in relation to intra-group services (i.e. whether a service has been rendered and determination of an arm’s length price in connection with such services)</td>
<td>• Duplication of services: Deals with the treatment for duplication of services – also carves out an exception for temporary duplicative services.</td>
<td>• Indian Transfer Pricing Regulations do not provide for detailed guidance on intra-group services.</td>
</tr>
<tr>
<td></td>
<td>• Concept of viable economic alternative: Concept of viable economic alternative discussed in relation to whether a profit charge is warranted or not for intra-group services rendered.</td>
<td>• Concept of viable economic alternative: Concept of viable economic alternative discussed in relation to whether a profit charge is warranted or not for intra-group services rendered.</td>
<td>• Benefits test approach: The Indian Tax Authorities have historically contended on the need for benefits test approach for determining arm’s length remuneration for intragroup services.</td>
</tr>
<tr>
<td></td>
<td>• Low-value adding intra-group services: Definition and treatment of low-value adding intra-group services. Suggestion that no benefits test to be applied for low value added services.</td>
<td>• Low-value adding intra-group services: Definition and treatment of low-value adding intra-group services. Suggestion that no benefits test to be applied for low value added services.</td>
<td>• Revised Safe Harbour Rules: The 2017 OECD Transfer Pricing Guidelines are aligned with the Indian Transfer Pricing Legislation for low-value added services, which is captured within the ambit of revised Safe Harbour Rules.</td>
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<tr>
<td></td>
<td>• Guidance on cost build-up: Guidance on cost build-up for cost recharges in connection with intra-group services.</td>
<td>• Guidance on cost build-up: Guidance on cost build-up for cost recharges in connection with intra-group services.</td>
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<td></td>
<td>• With-holding taxes: Suggestion that withholding taxes to be levied only on the profit element of the low-value adding intra-group services.</td>
<td>• With-holding taxes: Suggestion that withholding taxes to be levied only on the profit element of the low-value adding intra-group services.</td>
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<td></td>
<td>• Documentation requirements: Guidance on documentation requirements in case of intragroup services.</td>
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<tr>
<td>VIII - Cost Contribution Arrangements (‘CCAs’)</td>
<td>• Discusses the cost contribution arrangements between AEs and the arm’s length consideration for the same.</td>
<td>• Types of CCAs: Specifies the types of CCAs – services vs. intangibles.</td>
<td>• Indian Transfer Pricing Regulations do not provide any specific guidance on CCAs.</td>
</tr>
<tr>
<td></td>
<td>• Control and Assumption of risks: Disregards entities that do not control and assume risks in the CCA for the purpose of profit sharing.</td>
<td>• Control and Assumption of risks: Disregards entities that do not control and assume risks in the CCA for the purpose of profit sharing.</td>
<td>• Documentation: Taxpayers should evaluate that their documentation is sufficient justifying the contributors to the CCA.</td>
</tr>
<tr>
<td></td>
<td>• Current contributions to be valued at cost: Current contributions to the development of intangible to be valued at cost.</td>
<td>• Current contributions to be valued at cost: Current contributions to the development of intangible to be valued at cost.</td>
<td></td>
</tr>
<tr>
<td>IX – Transfer Pricing aspects of Business Restructuring</td>
<td>• Discusses the transfer pricing aspects of business restructuring, including cross-border deployment by an MNE of functions, assets or risks.</td>
<td>• Revisions to Chapter IX to conform the guidance on Business Restructuring introduced by the 2015 BEPS Reports on Actions 8-10 and 13.</td>
<td>• Business Restructuring has been covered as an international transaction within the Indian Transfer Pricing Regulations. However, no detailed guidance has been prescribed in this regard.</td>
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<td></td>
<td>• Accurate delineation of the transactions forming part of the business restructuring is an important aspect of benchmarking a business restructuring.</td>
<td>• Accurate delineation of the transactions forming part of the business restructuring is an important aspect of benchmarking a business restructuring.</td>
<td>Exit charge:</td>
</tr>
<tr>
<td></td>
<td>• Controlling risk and financial capacity to assume risk with respect to the restructuring.</td>
<td>• Controlling risk and financial capacity to assume risk with respect to the restructuring.</td>
<td>• Warrants exit charge in respect of transactions involving business restructuring.</td>
</tr>
<tr>
<td></td>
<td>• Guidance on transfer pricing documentation to be maintained in case of a business restructuring</td>
<td>• Guidance on transfer pricing documentation to be maintained in case of a business restructuring</td>
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Dhruva Advisors LLP is a boutique tax and regulatory services organization, working with some of the largest multinational and Indian corporate groups. We bring a unique blend of experience, having worked for the largest investors in India, advising on the largest transactions and on several of the largest litigation cases in the tax space. We work closely with regulators on policy issues and our clients on tax advocacy matters. We believe in thinking out of the box, handholding our clients in implementation and working to provide results.

Key differentiators:
- Strategic approach to complex problems
- In-depth, specialised and robust advice
- Strong track record of designing and implementing pioneering solutions
- Trailblazers in tax controversy management
- Long history of involvement in policy reform
- Technical depth and quality

Dhruva has presence in Mumbai, Ahmedabad, Bengaluru, Delhi, Singapore and Dubai. The key industries that the team advises on include financial services, IT and IT-enabled services (ITES), real estate and infrastructure, telecommunications, oil and gas, pharmaceuticals, chemicals, consumer goods, power, as well as media and entertainment.

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- Dhruva Advisors has also been awarded the Best Newcomer of the Year 2016 - ASIA by the International Tax Review.
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