

## Central Board of Direct Taxes (CBDT) issues final rules on “range concept” and “multiple year data”

27 October 2015



### INTRODUCTION

The CBDT had issued the draft scheme of Rules on 21 May 2015 on “range” concept and “use of multiple year data” for determination of arm’s length price (ALP) in relation to international and specified domestic transactions undertaken

on or after 1<sup>st</sup> day of April 2014. The Rules were in continuance to the budget speech announced by the Finance Minister in 2014. The CBDT followed the process of consultation before issuing final Rules and gave opportunity to

stakeholders to provide their concerns and recommendations on the proposed scheme.

After receipt of comments and suggestions, CBDT has finalised the Rules and has notified the same on 19 October 2015. Based on such notification, CBDT has amended Rule 10B(4) of the Income-tax Rules, 1962 ('Rules') and has introduced Rule 10CA.

## KEY HIGHLIGHTS OF THE AMENDED RULES

### Range concept and Multiple year data

- The existing transfer pricing guidelines provided for "arithmetic mean" of the arm's length prices (ALPs) where more than one ALPs were determined.
- Further, only single year data (i.e. financial year in which transactions were entered into) was allowed to be used for margin analysis of the comparable companies, with the exception that data of prior 2 years could also be considered only if such data revealed facts which could have an influence on the determination of transfer prices in relation to the transactions being compared.
- Now, with the new Rules, the 'range' concept has been introduced to be allowed in cases where the ALP is determined by using any method prescribed under section 92C of the Income-tax Act, 1961.

- For the mechanism to work, following are the requirements:
  - a) A data set is required to be constructed in which the ALPs would be arranged in an ascending order
  - b) For arriving at the ALPs – weighted average of the prices would be computed after assigning weights to the quantum of appropriate indicator (e.g sales, costs, assets employed etc.) based on the method applied and the same would be considered for arriving at respective prices
  - c) Where data for the financial year in which transactions have been entered into (referred to as current year) is available at the time of furnishing the return of income, a weighted average of 3-years of comparable uncontrolled data would be used to construct the data set including current year data. However, where data for current year is not available at the time of furnishing the return of income, data of 2 preceding years out of 3 years would be used. Further, a comparable company is to be rejected for all years in case if it is not comparable in the current year in which the taxpayer undertakes the transaction
  - d) A data set with minimum 6 entries is to be constructed where the ALP is determined based on method other than Profit Split Method (PSM) and Other Method
  - e) The data points lying within the 35<sup>th</sup> to 65<sup>th</sup> percentile of the data set of series would constitute the range.

- If the transfer price of the tested party falls outside the range as constructed above, the “median” of the data set would be taken as ALP and adjustment to transfer price shall be made accordingly.
- Cases where the ‘range concept’ cannot be applied, the existing arithmetic mean concept shall continue to apply in the same manner as it applied along with benefit of tolerance range.
- In a scenario where current year data is not available at the time of filing of return of income by taxpayers, current year data can be used during the transfer pricing audit by both the taxpayer and the department if it becomes available at the time of audit.

#### Dhruva comments

- The data points lying between 35<sup>th</sup> to 65<sup>th</sup> percentiles would constitute ALP range and hence, the loss making and high profit making companies will not be selected. However, in certain cases the ALP determined by range concept may not work in favour of the taxpayer as against ALP arrived at by applying arithmetic mean.
- The number of comparables considered for comparison would play an important role in application of range concept.
- It will be important to understand whether the range or mean concept adopted by the taxpayer for arriving at the ALP at the time of furnishing the return of income is not disturbed by the tax authorities during TP audits. For instance, if during TP audit, 1 or more comparable entities are additionally thrown up by the database making total comparable set of 6,

the TP officer may consider applying range concept as against arithmetic mean considered by the taxpayer.

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