

OECD releases India Stage 1 peer review report on BEPS Action 14

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Executive summary

On 24 October 2019, the Organisation for Economic Co-operation and Development (OECD) released the sixth batch of peer review reports (the Report¹) relating to the implementation of the Base Erosion and Profit Shifting (BEPS) minimum standard under Action 14 (Making Dispute Resolution Mechanisms more effective). The Report covers eight countries, including India.

Overall the Report concludes that India meets half of the elements of the Action 14 minimum standard. India is now working to address several of the noted deficiencies. To be fully compliant with all four key areas of an effective dispute resolution mechanism under the Action 14 minimum standard, India needs to amend and update a certain number of its tax treaties. This is expected to take place either through the Multilateral Instrument (MLI) or via bilateral negotiations. India also has in place a bilateral Advance Pricing Agreement (APA) program, which enables taxpayers to obtain rollback of the APA.

India provides access to the Mutual Agreement Procedure (MAP) in all transfer pricing (TP) cases and cases concerning application of treaty anti-abuse provisions. However, it does not provide access to MAP for issues that do not give rise to double taxation. Further, for cases concerning the domestic anti-abuse provision, discussions during the MAP will focus on elimination of double taxation arising from such application. The Report also notes

that India does not have in place a documented bilateral consultation or notification process for situations where its Competent Authority (CA) considers the objection raised by taxpayers in a MAP request as not justified, although India intends to implement such process. India also has not yet issued comprehensive guidance on its MAP process; but expects to do so shortly. The Report highlights the absence of coordination between the MAP and India's domestic tax law appeal process which may sometimes make the MAP ineffective. The Report suggests the need for India to allocate additional resources to the MAP program to accelerate the resolution of MAP cases. The Report also provides insights into some of India's positions and approaches on MAPs/ bilateral APAs. On the arbitration clause, India has reported that it does not support the inclusion of arbitration in tax treaties as a final stage to the MAP process since India believes that such processes are against a jurisdiction's sovereignty in tax matters.

Overall the Report indicates that the experiences of the peers in handling and resolving MAP cases with India is generally positive and affirms India's commitment to make dispute resolution under tax treaties an effective and efficient process. Given the challenges with the domestic tax law appeal process, MAP/bilateral APAs would continue to be a preferred option for resolving TP disputes to mitigate double tax risk. Considering the recommendations of the OECD, the Indian Tax Administration should look at issuing detailed MAP guidance with information on India's approach to key issues and corresponding expectations of treaty partners. Further, the Indian Tax Administration needs to strengthen the teams overseeing the MAP/APA cases by providing additional resources for the efficacy of the MAP/APA programs.

Detailed discussion

Background

In October 2016, the OECD released the peer review documents on Action 14 which form the basis of the MAP peer review and monitoring process under BEPS Action 14. The peer review process assesses a member's legal and administrative framework, including the practical implementation of this framework to determine how its MAP regime performs relative to the four key areas: (i) preventing disputes; (ii) availability and access to MAP; (iii) resolution of MAP cases; and (iv) implementation of MAP agreements. The assessment methodology establishes detailed procedures and guidelines for a two-stage approach to the peer review

and monitoring process. Stage 1 involves the review of a member's implementation of the minimum standard based on its legal framework for MAP and the application of this framework in practice. Stage 2 involves the review of the measures taken by the Member to address any shortcomings identified in its Stage 1 peer review. Both of these stages are desk-based and are coordinated by the Secretariat of the Forum on Tax Administration's (FTA) MAP Forum.

Input is generally provided through questionnaires completed by the assessed jurisdiction, peers (i.e., other members of the FTA MAP Forum) and taxpayers. Accordingly, the questionnaires for the peer review process were sent to India and the peers on 29 August 2018. In total 15 peers provided input namely, Australia, Belgium, Denmark, Germany, Ireland, Italy, Japan, Netherlands, Norway, Slovenia, Sweden, Switzerland, Turkey, United Kingdom and the United States. These peers represent approximately 97% of the post-2015 MAP cases in India's inventory that started in 2016 or 2017. Furthermore, these peers represent treaty partners that have a high number of MAP cases with India as well as a more moderate caseload. Further the newly negotiated treaties or the treaties as modified by a protocol have also been considered. The period for evaluating India's implementation of the Action 14 minimum standard ranges from 1 January 2016 to 31 August 2018 (Review Period). Based on the inputs received from various parties, on 24 October 2019, the OECD released the sixth batch (Stage 1) peer review reports which include India, relating to the outcome of peer monitoring of the implementation of the BEPS minimum standard under Action 14 on improving tax dispute resolution mechanisms.

Minimum standard peer review report

The report is divided into four parts, namely: (i) Preventing disputes; (ii) Availability and access to MAP; (iii) Resolution of MAP cases; and (iv) Implementation of MAP agreements. Each part addresses a different component of the minimum standard.

Overall India meets half of the elements of the Action 14 minimum standard. India is now working to address the noted deficiencies. In order to be fully compliant with all four key areas of an effective dispute resolution mechanism under the Action 14 minimum standard, the Report recommends that India amend and update a certain number of its tax treaties. In this respect, India signed the MLI through which a number of its tax treaties will potentially be modified to meet the requirements under the Action 14 minimum standard. Where

treaties will not be modified, upon entry into force of this MLI for the treaties concerned, India has reported that it intends to update all of its tax treaties via bilateral negotiations to be compliant with the requirements under the Action 14 minimum standard and has put in place a plan as well.

India's responses/policy level considerations in relation to the four areas of the minimum standard

Preventing disputes

India meets the Action 14 minimum standard concerning the prevention of disputes. India has in place a bilateral APA program which also enables taxpayers to request rollbacks of bilateral APAs and such rollbacks are granted in practice. On the most concerning area for taxpayers, i.e., the practical application of the rollback of bilateral APAs, one of the peers has noted that India is willing to try and deal with all years where double taxation occurred in either the MAP or the APA process.

India has reported that where a tax treaty does not contain a provision that is based on or is the full equivalent of Article 25(3), first sentence, of the OECD Model Tax Convention (MTC),² there are no constraints to endeavor to reach an agreement on the general interpretation of a tax treaty. Further, the MLI, upon entry into force, will modify all such tax treaties to include the equivalent of Article 25(3), first sentence, of the OECD MTC.

Availability and access to MAP

India meets some requirements regarding the availability and access to MAP under the Action 14 minimum standard. It provides access to MAP in TP cases and cases concerning the application where treaty anti-abuse provisions are applied. Specifically, in response to some of the peers' observations and comments based on their experience in dealing with India, India has made its clarifications as follows:

- ▶ **Access to MAP and domestic remedies:** India has clarified that it grants MAP access simultaneously with domestic remedies. However, in cases where domestic remedies have been finalized, India will grant access to MAPs but will not be able to derogate from decisions of its domestic courts and thus will only seek correlative relief at the level of the treaty partner.
- ▶ **MAP access to TP cases:** India provides access to MAP in TP cases. Further India has withdrawn its reservation to Article 25 of the OECD MTC, thereby providing MAP access even in absence of Article 9(2) of the OECD MTC.
- ▶ **Requirement of final assessment order to access MAP:** MAP discussions will be started upon receipt of a final assessment order (and not after receipt of draft assessment orders or during the course of audit proceedings) to avoid devotion of time and resources on cases where the underlying tax has not been finalized or is uncertain. The key policy rationale is not to deny MAP access based on a draft assessment order, but to postpone active discussions on the resolution of the case until there is a final assessment order.
- ▶ **No MAP access in the absence of double taxation:** Most of the tax treaties are aligned with Article 25 of the OECD MTC to provide for MAP access where there is, or is a risk of, taxation not in accordance with the tax treaty and not limited to cases of double taxation. India's view is that MAP access will be granted only where there is double taxation even if it is established that there was taxation in contravention of the tax treaty. In India's view, the issue raised by the peer on the availability of MAP go beyond the terms of a tax treaty is not acceptable, as these are applied in furtherance of the treaty's preamble (setting out the treaty's purpose) and cannot go beyond that. If the treaty's purpose would not be of relevance, India questioned as to why then under BEPS Action 6 it was necessary to create a minimum standard to amend treaties' preambles.
- ▶ **MAP access for fiscally transparent entities/single member partnerships:** India's current position is that it does not provide MAP access for fiscally transparent entities that are treated under the peer's domestic legislation as disregarded from its single resident member. India's view is that MAP access to such taxpayers will require amendments to the tax treaty. India also mentioned that it is aware of the fact that the peer has a similar issue with other treaty partners for which it has entered into a protocol with one of its treaty partners to allow treaty benefits to pass through-structures. In this regard, India reported that it has proposed the same solution to the peer as well. Further, India treats this aspect as beyond the purview of the peer review of the Action 14 minimum standard.
- ▶ **MAP access to cases involving advance tax rulings:** Where a taxpayer obtains a tax ruling from an independent judicial authority (example, Authority for Advance Rulings), India's CA will not grant access to MAP. Since, such rulings can only be challenged in courts and are in the nature of judicial proceedings, MAP access cannot be granted.
- ▶ **MAP access concerning the domestic anti-abuse provision:** India provides MAP access for cases concerning application of the domestic anti-abuse provision, but the

discussion in MAP will only focus on the elimination of double taxation arising from such application and not to issues that do not give rise to double taxation or the question of whether the application of a domestic law anti-abuse provision conflicts with the provisions of tax treaty.

- ▶ **Include time limit of three years for submitting MAP request:** Where current tax treaties do not contain time limit or provide for a differing time line, the MLI will modify such tax treaties to include the required provision. However, the Report does not provide any insights on the issue of condonation of delay in invoking the MAP request.
- ▶ **MAP access in cases of audit settlements:** Where the disputes are settled by the Income Tax Settlement Commission, MAP access would be denied. However, no MAP requests involving the above situation were received by the CAs during the Review Period.
- ▶ **Submission of MAP requests to the CA of either treaty partner or introduction of a bilateral consultation or notification process:** None of the India's tax treaties allow for submission of MAP requests to the CA of either treaty partner. Also, due to India's reservation, the MLI will not modify the tax treaties to include the required provision. However, India intends to introduce a bilateral notification process to be applied in situations where its CA considers the objection raised by a taxpayer in its MAP request as not being justified.
- ▶ **Inclusion of Article 25(3), second sentence:** Where current tax treaties do not include Article 25(3), second sentence which provides for CAs to consult together for the elimination of double taxation in cases not provided for in the Convention, the MLI will modify such tax treaties. If the MLI does not modify a treaty due to specific reservation by the treaty partner, India will include in its plan for renegotiation of the respective bilateral tax treaties.
- ▶ **MAP access where sufficient information is provided:** India has not denied any MAP requests where the taxpayers have complied with India's information and documentation requirements.

Resolution and implementation of MAP cases

India meets most of the other requirements under the Action 14 minimum standard in relation to the resolution of MAP cases. India's CA operates independently from the audit function of the tax authorities and the performance indicators used are appropriate to perform the MAP function.

- ▶ **Time lines for MAP closure:** MAP cases with India were not closed within 24 months. The average time to close was 35.66 months, 34.31 months for attribution/allocation cases and 68.70 months for other cases. For attribution/allocation cases, the peers noted that India's CA sometimes became entrenched due to a preference to apply domestic TP rules over OECD TP guidelines (example preference over arithmetic/percentile range over an interquartile range and single year data over multiple year data for benchmarking analysis, however the recent experience reflects use of multiple year data). Further, for other cases India's CA preferred to rely on assertion at face-to-face meetings and did not respond to the position paper.

India's MAP inventory increased since 1 January 2016. This increase can be broken down into an increase by 9% for attribution/allocation cases and an increase of 16% for other cases. This state of play indicates that the CA is not adequately resourced to ensure that post-2015 cases are resolved within the average of 24 months (which is the pursued average for resolving MAP cases received on or after 1 January 2016). According to the statistics provided by India, its MAP caseload during this period has been as follows:

Type of case	Opening inventory 1 January 2016	Cases started	Cases closed	End inventory 31 December 2017	Average time to close cases (in months)
Attribution/ allocation cases	594	199	147	646	34.31
Other cases	101	22	6	117	68.70
Total	695	221	153	763	35.66

► **Resolving MAP cases involving fact specific issues:**

India mentioned that it does not deny MAP access in cases concerning the question of whether a permanent establishment exists. However, the burden of proof on establishing such existence differs based on the facts of the case and the peers cannot put specific conditions on India to resolve cases in a certain manner.

- **Arbitration clause:** In line with the position to the OECD MTC 2017 update, India does not support inclusion of arbitration in tax treaties as India believes that such processes are against a jurisdiction's sovereignty in tax matters.

With respect to implementation, India meets the Action 14 minimum standard and no issues have surfaced regarding the implementation throughout the peer review process. India reported that the actual implementation of MAP agreements is monitored at the level of the local tax offices. Where the local tax office is requested to implement a MAP agreement, it is also asked to report back to India's CA to confirm implementation. By doing so, India's CA can keep track on whether all MAP agreements have been implemented. India further reported that all MAP agreements that were reached on or after 1 January 2016, once accepted by taxpayers, have been (or will be) implemented. Almost all peers that provided input reported not being aware of any impediments to the implementation of MAP agreements in India on a timely basis.

Key peer inputs and OECD recommendations

The experiences of the peers in handling and resolving MAP cases with India has generally been positive. Some of them highlighted the ease of working with the contacts and the frequency of communications. Furthermore, several peers appreciated the willingness of India to resolve cases. Other peers, however, also mentioned difficulties in resolving cases with India, particularly the long time it takes to receive position papers, the interplay with domestic remedies and the fact that reaching an agreement on a principled basis is sometimes challenging. Based on the inputs received from the peers, the OECD recommendations on some of the key areas of improvements are as follows:

- **Publish comprehensive MAP guidance:** Currently, India does not have MAP guidance and domestic legislative rules are not comprehensive. Further, the effects of the statutory dispute settlement process on MAP are not addressed in the MAP guidance, since such guidance is not yet available.

In this regard, India should without further delay introduce clear and comprehensive MAP guidance. India should, when it has issued its MAP guidance, make this guidance, without further delay, publicly available and easily accessible. Further, India should, when it introduces MAP guidance, follow its stated intention to clarify the effects on MAP when the case has been resolved through its statutory dispute settlement process.

- **Provide MAP access to cases involving domestic anti-abuse as well as no double taxation:** India should change its policy to effectively allow access to MAP for issues concerning the question of whether the application of a domestic law anti-abuse provision is in conflict with the provisions of a tax treaty, and be willing to discuss such issues when being accepted into the MAP process, including where there is no double taxation but there is taxation that is not in accordance with the provisions of a tax treaty. India should seek to resolve all MAP cases that are accepted into the MAP process. In this regard, India should not refuse discussions in MAP with the other CA concerned on the grounds that there is no double taxation.
- **Increase resources for handling of MAP/bilateral APA cases:** The peers opined that with India's preference to make site visits on all cases, the time line for resolution might be extended. Hence, the peers stressed that such visits should be undertaken on a case by case basis. The peers also recommended that India should hire additional personnel to ensure that MAP cases are resolved in a timely, effective and efficient manner, which should inter alia enable India to issue position papers in timely manner and communicate more frequently and hold face to face meeting with CAs.
- **Consider adherence to OECD TP guidelines:** The peers noted that the negotiations with India's CA can sometimes become entrenched due to India's preference to apply domestic TP rules over the OECD TP guidelines, example preference over arithmetic/percentile range over an interquartile range and single year data over multiple year data for benchmarking analysis. In this regard, for attribution/allocation cases, India should provide more details explaining the acceptance or rejection of comparables and show greater willingness to adhere to OECD TP guidelines over domestic tax law to consider OECD endorsed methods in addition to cost-plus.

Implications

In a post-BEPS world, where multinational enterprises (MNEs) face tremendous pressures and scrutiny from tax authorities, the release of India's Stage 1 peer review report represents the continued recognition and importance of the need to achieve tax certainty for cross-border transactions for MNEs. While increased scrutiny is expected to significantly increase the risk of double taxation, the fact that tax authorities may be subject to review by their peers should be seen by MNEs as a positive step to best ensure access to an effective and timely mutual agreement process. In recent times, there has been a considerable amount of MAP/APA cases being delayed in resolution. As noted in the Report, due to resource

constraints, there has been some delays in the discussion and resolution of MAP/APA cases. However, the Report reinforces India's commitment to make dispute resolution an effective and efficient process. Given the challenges with the domestic tax law appeal process, MAP/bilateral APAs would continue to be a preferred option for resolving TP disputes to mitigate double tax risk. Considering the recommendations of the OECD, the Indian Tax Administration should issue detailed MAP guidance providing information on India's approach to key issues in MAP and corresponding expectations of treaty partners. Further, the Indian Tax Administration would need to strengthen the teams overseeing MAP/APA cases by providing additional resources for the efficacy of MAP/APA program.

Endnote

1. <http://www.oecd.org/tax/beps/making-dispute-resolution-more-effective-map-peer-review-report-india-stage-1-c66636e8-en.htm>.

For additional information with respect to this Alert, please contact the following:

Ernst & Young LLP (India), National Leader, International Tax and Transactions Services, Mumbai

- ▶ Pranav Sayta pranav.sayta@in.ey.com

Ernst & Young LLP (India), National Leader, International Corporate Tax Advisory Services, Bangalore

- ▶ Rajendra Nayak rajendra.nayak@in.ey.com

Ernst & Young LLP (India), National Leader, Transfer Pricing Services, New Delhi

- ▶ Vijay Iyer vijay.iyer@in.ey.com

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