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# Global Tax Alert

News from Transfer Pricing

## India's *Finance Act, 2020* introduces amendments to transfer pricing provisions

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### Executive summary

The Finance Minister (Minister) of India presented the Finance Bill, 2020 (the Bill) as part of India's Union Budget for the Financial Year (FY) 2020-21 (Budget 2020) on 1 February 2020. The Bill, with certain amendments, was enacted as the *Finance Act, 2020* (the Act) on 27 March 2020, after receiving approval of the Parliament and the President's assent.

The Act amends certain transfer pricing (TP) provisions of the Indian Tax Law (ITL). Specifically, the Act extends the applicability of the safe harbor and advance pricing agreement (APA) provisions regarding the determination of income attributable to a business connection or a permanent establishment (PE) of a nonresident in India. The Act also amends the due date for TP compliance.

Further, the Minister announced the Government's intention to introduce a process to enable taxpayers to resolve pending tax disputes in an expeditious manner. Pursuant to the announcement, the Government introduced the Direct Tax Vivad Se Vishwas Bill, 2020 (VSV Bill) in the Parliament on 5 February 2020. The VSV Bill with certain amendments was enacted as the *Direct Tax Vivad Se Vishwas Act, 2020* (VSV Act or Direct Tax Settlement Process or the Process) on 17 March 2020, after receiving approval of the Parliament and the President's assent. The VSV Act seeks to resolve direct tax appeals pending

before various appellate forums, such as Supreme Court (SC), High Court (HC), Income Tax Appellate Tribunal (ITAT), the Commissioner (Appeals) and the Dispute Resolution Panel as on 31 January 2020. The Direct Tax Settlement Process enables taxpayers to settle appeals by paying the entire amount of the disputed tax liability or 50% of the disputed tax liability in certain situations, if the payment is made by 30 June 2020.<sup>1</sup> Beyond this date, taxpayers would need to pay the entire amount of the disputed tax liability plus an additional amount of 10% of the disputed tax. The Process is open until such time as may be notified by the Government. The Process covers all pending direct tax disputes, including TP disputes.

This Alert summarizes the key TP amendments introduced by the Act and provides an overview of the Direct Tax Settlement Process and its implications on TP disputes.

## Detailed discussion

### Expansion of scope of safe harbor and APA provisions

Attribution of income to a business connection/PE of a nonresident has been a contentious issue and has given rise to many disputes. TP safe harbor rules and the APA were introduced in the ITL to provide certainty to taxpayers for those who opt for them. While the scope of the TP safe harbor rules was limited to specified international transactions involving associated enterprises, it was not clear whether taxpayers could seek APAs on issues relating to PE profit attribution.

The Indian Tax Administration (ITA) has clarified that it is possible for a taxpayer to file an APA in relation to profit attribution to a PE, provided the taxpayer formally conceded the existence of a PE. However, in practice, no APAs have been concluded on PE issues.

To enable taxpayers to obtain certainty on this issue, an amendment has been made to the ITL to enable the ITA to notify taxpayers on the safe harbor rules or enable taxpayers to opt for APAs, for profit attribution to a business connection/PE.

The Act further provides that in the case of an APA, income attributable to a PE may be determined based on the methods prescribed under TP rules or as per the methods provided by rules made under the Act, with such variations or adjustments as required.

In the case of APAs, the above amendment will be effective for APAs entered on or after 1 April 2020, and in the case of safe harbor, the amendment will be applicable from financial year 2019-20 onwards.

### Change in due date with respect to TP Documentation (TP Doc) and Accountant's report

Currently, the due date for maintenance of TP Doc and filing of an Accountant's report in Form 3CEB is the date of filing the return of income (ROI), i.e., 30 November of the year following the relevant financial year. To enable pre-filed annual ROI, the due date has been advanced by a month. The changes made are set forth below:

TP compliance	Due date	
	As per the original provisions	As per the amended provisions
Maintenance of TP Doc	30 November of the year following the financial year	31 October of the year following the financial year
Filing of Form 3CEB		

This amendment will be effective with respect to compliance relating to the FY 2019-20 and accordingly the due date for adhering to these compliances for the FY 2019-20 would be 31 October 2020.

### Expansion in the scope of Dispute Resolution Panel (DRP)

Objections before the DRP can be filed by the eligible assessee for any variation in the income or loss returned which is prejudicial to the interest of the such eligible assessee. "Eligible assessee" means any person in whose case the variation arises a consequence of the TP order or in case of a person which is a foreign company.

The Act has also expanded the definition of eligible assessee to include non-corporate nonresidents, in addition to a foreign company. Further, objections before the DRP can be filed for any variation prejudicial to the interest of the eligible assessee, even in the absence of adjustment to income/loss (for example, orders pertaining to the levy of penalty).

This amendment will be effective for any variation made by the tax authorities on or after 1 April 2020.

## Direct Tax Settlement Process

The Process can be availed by taxpayers for appeals which are pending before the DRP, Commissioner (Appeals), ITAT, HC or SC as on 31 January 2020 or a taxpayer who has initiated any proceedings for arbitration, conciliation or mediation before 31 January 2020. The appeals or writs filed by the taxpayer, as well as by the Tax Authority, are eligible to be settled under the VSV Process, which is available until such time as may be notified by the Government.

To apply, the taxpayer should make an application in the prescribed form with the designated authority wherein upon post acceptance of the application and payment of the determined tax, the taxpayer shall be granted complete immunity from prosecution and relief from payment of interest and penalty.

The payment timelines under the Process are as follows:

Type of matter	Amount payable under the Process on or before 30 June 2020 <sup>2</sup>	Amount payable under the Process after 30 June 2020 <sup>2</sup> until the last date*
Matters involving disputed tax, interest and penalty thereof	Entire amount of disputed tax only (complete waiver of interest and penalty levied/leviable)	Entire amount of disputed tax plus 10% of disputed tax (10% being subject to aggregate amount of interest and penalty levied or leviable)
Matters involving disputed penalty, interest and fees	25% of disputed penalty/interest/fee	30% of disputed penalty/interest/fee

\* yet to be notified

In cases where an appeal or writ or SLP is filed by the tax authority on any issue before the appellate forum, the amount payable shall be 50% of the amount in the above table. Further, in the case of a taxpayer's appeal, if the taxpayer has already received a decision on any issue in its favor by the ITAT or the HC, and the same has not been reversed by any higher authority or court, the amount payable is reduced to 50% of the amount stated above.

On payment of the taxes under the Process, the matter covered by such application shall not be reopened in any other proceeding under the ITL or under any other law for the time period being in force or under any agreement (whether for protection of investment or otherwise) entered into by India with any other country or territory outside India. No proceedings shall be instituted in respect of an offense or levy of any penalty/charge/interest under the ITL in respect of tax arrears.

The VSV Act clarifies that a declaration made under the Process cannot be considered as setting any precedent for the taxpayer or the Tax Authority in relation to the issues covered under the declaration.

## Implications

Recognizing the significance of issues relating to profit attribution to a PE as well as the need to bring greater clarity and predictability, the amendment to expand the scope of the safe harbor rules and APAs to cover profit attribution to PEs is a positive development. In the past, taxpayers may have concluded APAs for activities of an Indian company by subsuming additional return/income which otherwise may be attributed to a purported PE if a tax authority were to allege one. Such an approach may enable a taxpayer to persuasively argue that since all functions/risks (and related returns) are already considered in the arm's-length remuneration of an Indian company, there should be no further profit attribution even if a PE were alleged. In light of the amendment, taxpayers may need to consider whether they can or should re-visit their existing APAs for an Indian company and consider filing new APA applications for the foreign company/PE to provide certainty and mitigate PE risk in India.

One of the key challenges faced by taxpayers in India in relation to TP enforcement and related adjustments was the time-consuming nature of the appeal process because of the number of tiers of appellate authorities and the build-up of inventory of cases at each level. The outcome of the appeals process can also be unpredictable which added to the tax risk. Therefore, given this, taxpayers should review the outstanding matters under tax litigation and evaluate feasibility of opting for the DTS Process, including the applicability of the secondary adjustment provisions which may arise on settlement of TP disputes.

Taxpayers should consider the likelihood of success under litigation given recent trends in India, availability of alternative options such as APAs and the Mutual Agreement Procedure, availability of correlative relief, impact of secondary adjustment provision and undertake a cost benefit analysis of opting for the Process vis-à-vis continuing with the existing appeals.

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## Endnotes

1. In view of the disruption caused by pandemic COVID-19, an Ordinance to provide relaxation in provisions of certain Acts and for matters connected therewith or incidental thereto was passed on 31 March 2020. Accordingly, the due date for declaration and payment of disputed tax under Direct Tax Settlement Process has been extended from 31 March 2020 to 30 June 2020, without additional payment.
2. Ibid.

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