

India publishes detailed guidance on Mutual Agreement Procedure

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Executive summary

The Organisation for Economic Co-operation and Development (OECD) released, on 24 October 2019, the sixth batch of peer review report (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, which included a peer review of India, concluded that India met half of the elements of the Action 14 minimum standard on an overall basis. Further, the Report recommended improvements in certain areas, including the requirement to publish comprehensive guidance on India's Mutual Agreement Procedure (MAP) with information on India's approach to key issues in MAP and the corresponding expectations of treaty partners. In this regard, as a first step, India's Central Board of Direct Taxes (CBDT), on 6 May 2020, issued a notification amending the rules relating to MAP.² Following this, on 7 August 2020, the CBDT published detailed guidance (the Guidance) which is intended to provide key information on several aspects relating to India's MAP program.

The Guidance comprises of four sections, including: (A) introduction and basic information; (B) access and denial of access of MAP; (C) technical issues; and (D) implementation of the MAP process. In line with the amended MAP Rules, the Guidance also underscores India's commitment to resolve MAP cases within

24 months. In general, issuance of this Guidance will be useful and will benefit the taxpayers, tax authorities and competent authorities (CAs) of India and the respective foreign jurisdictions. The Guidance further reinforces India's commitment to make dispute resolution an effective and efficient process by reforming its MAP regime to comply with the key areas of the Report.

Detailed discussion

Background

As part of the OECD MAP peer review process, India underwent the Stage 1 peer review (based on the inputs from assessed jurisdiction, peers and taxpayers). Accordingly, on 24 October 2019, the OECD released the sixth batch (Stage 1) peer review reports which included India, relating to the outcome of the peer monitoring of the implementation of the BEPS minimum standard under Action 14 on improving tax dispute resolution mechanisms.

The Report contained recommendations from OECD on the key areas of improvements in addition to the requirements under the Action 14 minimum standard in relation to an effective dispute resolution mechanism. Issuance of comprehensive MAP guidance was one of the recommendations of the OECD as part its peer review process. Accordingly, the CBDT, on 6 May 2020, issued a notification amending the MAP Rules. Further, in line with the recommendations of OECD peer review process, on 7 August 2020, the CBDT issued the Guidance containing detailed information regarding MAP processes for the benefit of taxpayers, tax practitioners, tax authorities, the CAs of India and the respective foreign jurisdictions.

Contents of the Guidance

Overview

The MAP article contained in India's Double Taxation Avoidance Agreements (DTAAs) is largely based on Article 25 of the OECD Model Tax Convention. Through this, the CAs of the contracting states may resolve differences or difficulties regarding the interpretation or application of the respective DTAA on a mutually agreed basis. While the MAP is of fundamental importance to the proper application and interpretation of DTAAs, it has particularly emerged as a widely used mechanism for resolving transfer pricing (TP) disputes. The procedures for invoking MAP and giving effect to the MAP resolution for the granting of relief in respect of double taxation or for the avoidance of double taxation

are contained in Rule 44G the Income-tax Rules, 1962. Key highlights with respect to filing of MAP application are as follows:

- ▶ **Making a MAP application in India:** The Guidance provides details of documents that need to be part of the statutory form. The statutory form along with the documents need to be filed with the CA having jurisdiction over the MAP applications.
- ▶ **Officials responsible for India's MAP program:** At present, India has two CAs for MAP cases and they are senior officers in the Department of Revenue, Ministry of Finance (Joint Secretary, FT&TR-I and Joint Secretary, FT&TR-II). The two CAs have territorial jurisdiction over the MAP cases depending upon the location of the DTAA partner country. Joint Secretary, FT&TR-I is responsible for MAP cases with DTAA partner countries/specified territory in Europe and North America (including the Caribbean) and Joint Secretary, FT&TR-II is responsible for MAP cases with DTAA partner country/specified territory in rest of the world. The CAs of India are independent of the tax authorities who audit taxpayers and take their own decisions that are only administratively governed by an internal governance mechanism within the CBDT, Department of Revenue.
- ▶ **Computation of "24 months" timeframe for resolving MAP cases in line with the BEPS Action 14 minimum standard:** The Guidance clarifies that the period of 24 months shall be computed from the "start date" of a MAP case. In the case of a MAP invoked by foreign affiliates of the Indian taxpayer, the "start date" is determined by the home jurisdiction CAs in accordance with the MAP Statistics Reporting Framework. India notes that since at times, the CAs of India receive notice of MAP cases from the CAs of the DTAA partners much beyond the "start date," this results in delaying the endeavor to resolve such MAP cases.

Access and denial of access to MAP

1. Access to MAP

Access to MAP is granted simultaneously with domestic remedies. India provides access to MAP in the following types of cases and for the following issues, if they result in double taxation not in accordance with the DTAA: (i) TP adjustments; (ii) existence of a permanent establishment (PE); (iii) attribution of profits to a PE; and (iv) characterization or re-characterization of income or expense such as royalty/fees for technical services or interest. The Guidance specifically provides clarification on access to MAP in the following circumstances:

- ▶ **Unilateral Advance Pricing Agreement (UAPA) signed by an Indian taxpayer:** In cases where any action of the tax authorities of a DTAA partner challenges the income of a taxpayer, as determined under the UAPA entered into with India, the taxpayer shall have access to MAP. Also, MAP access can be granted during pendency of a UAPA application; but the resolution would be postponed until the conclusion of the UAPA application. In either case, the Guidance clarifies that India shall not be able to derogate from conclusions made in UAPA and thus will only seek correlative relief at the level of the treaty partner.
- ▶ **Application of the TP safe harbor rule by Indian taxpayer:** Where an Indian or foreign taxpayer opts for the Indian TP safe harbor rate on its international transactions, MAP access can be given to such foreign taxpayers in the other countries or specified territories and the Indian CA needs to be notified of the same. However, the Indian CA would not change the transfer price for the international transactions covered under the safe harbor provisions; rather, it would request the CAs of the DTAA partners to provide correlative relief.
- ▶ **Orders of Income Tax Appellate Tribunal (ITAT):** ITAT is the final fact-finding appellate body in tax matters which is independent of administrative jurisdiction of the Indian tax authorities. Therefore, in cases where the Indian taxpayer receives an order from the ITAT with respect to the disputed issues in the MAP application, while taxpayer shall have access to MAP; but India will not be able to deviate from the order of the ITAT and thus will only seek correlative relief at the level of the treaty partner. However, where the ITAT order is not conclusive and sets aside for fresh adjudication, taxpayers would be eligible for filing for MAP resolution after the fresh adjudication by the Indian tax authorities.
- ▶ **Withholding tax (WHT) order:** In situations where an obligation to withhold tax on payment to a nonresident is enforced by a WHT order on a resident payor and the same is disputed by the nonresident, MAP access would be provided to such nonresident entity anticipating an event of double taxation or taxation not in accordance with the relevant DTAA. However, such action being purely under domestic tax law and not being an order determining tax liability of the nonresident, the MAP discussion will be taken up only after an assessment order is passed in the case of the nonresident taxpayer.
- ▶ **Other matters:** India shall provide access to MAP even in a situation where the Indian tax authorities apply domestic anti-abuse provisions.

II. Denial of access to MAP

The Guidance provides that the CAs of India can deny access to MAP in certain situations as listed below:

- ▶ **Delayed MAP application:** If the taxpayer makes a MAP application to the CAs of India or to the CAs of the DTAA partners after the expiry of the time period specified in the Article relating to MAP of the relevant DTAA, the CAs of India would not provide access to MAP. This time period in most DTAA is within three years from the first notification of the action/order of tax authorities that results in double taxation. There are very few DTAA where this minimum time period is missing (e.g., India's DTAA with the United Kingdom (UK)) and certain of India's DTAA provide for an extended time limit up to five years (such as the DTAA with Brazil), whereas DTAA with the United Arab Emirates (UAE), Belgium, Canada and Italy prescribe a time limit of two years. While the DTAA with the UK, UAE, Belgium, and Canada are already amended pursuant to the ratification of the OECD Multilateral Instrument (MLI), the Guidance clarifies that efforts are on to amend those DTAA to provide for the same. This may be pursuant to ratification of the MLI or through bilateral negotiations.
- ▶ **Income Tax Settlement Commission (ITSC) and Authority for Advance Rulings (AAR):** The ITSC and AAR are independent statutory dispute resolution/prevention bodies. It is a voluntary process and is independent from the audit and examination functions of tax authorities. Once the application is accepted for settlement of disputes/advance rulings and the ITSC comes out with a settlement order or the AAR issues an advance ruling, the same is binding on both the taxpayer and the tax authorities. In such cases, MAP access would be denied by the Indian CA in respect of the issues that are included in the MAP application to the extent they are covered under the AAR/ITSC rulings/orders. However, if the ITSC/AAR refuses to issue a settlement order/advance ruling, or the ITSC issues an order without making a settlement and pursuant to this, there is double taxation on account of the Indian tax authorities' actions, MAP access shall be given to the taxpayer.
- ▶ **Other cases:** In addition, the Guidance clarifies that no MAP access shall be provided for issues that are purely governed by India's domestic tax law and arise due to the implementation of India's domestic legal provisions. Further, MAP access can be denied if it is observed that the taxpayer's objection is not justified and for this purpose, the Indian CA having jurisdiction over the case

would discuss the matter with the taxpayer and the CA of the DTAA partner. A defective MAP application can also result in the denial of MAP access, unless the defects are made good within the prescribed timelines that can range from 30 days to 90 days.

Technical issues

I. Downward adjustment

Under the Indian TP regulations, if the application of the arm's-length principle has the effect of reducing the income chargeable to tax or increasing the loss, as the case may be (i.e., computed based on the books of accounts), the TP computational provisions would not apply. In line with this, the Guidance clarifies that the Indian CAs cannot go below the income already offered to tax by the taxpayer in its tax return filings, as the same is expressly prohibited under the Indian domestic law. However, for MAP cases involving adjustments made by tax authorities of a DTAA partner, the Indian CA may go below the income already offered to tax by the taxpayer, to implement the MAP in full measure in accordance with the DTAA obligations.

II. Interest and penalties

The guidance clarifies that the consequential interest and penalties shall be administered under the Indian domestic tax law. Accordingly, the Indian CAs do not have the mandate to consider such consequential issues and negotiate disputes arising from such issues. While the amount of interest and penalties that are linked to the quantum of income, shall be varied in the same proportion as the variation in the quantum of income due to a MAP resolution, certain fixed penalties (which are not connected to the quantum of income), would not be affected by the resolution under MAP.

III. Bilateral and multilateral MAPs

The Guidance clarifies that in respect of issues for which a bilateral or multilateral Advance Pricing Agreement (APA) application has already been filed and accepted, MAP applications on the same issues for the same years should not be made by the taxpayers. Upon consultation with DTAA partners, any such MAP applications would not be admitted. However, if a bilateral or multilateral APA application fails to result in resolution for any reason, then a MAP application on the same issue and for the same years can be made and the same may be accepted by the CAs of India if it satisfies all conditions of a MAP application.

IV. Suspension of collection of taxes during the pendency of MAP

In order to avoid the unintended hardship to the taxpayers during the pendency of the MAP application, as well as for efficient management of collection of revenue, India has signed a Memorandum of Understanding regarding suspension of collection of taxes, with a few countries. These include the United States, the UK, Denmark, Sweden and South Korea. In this regard, the Guidance clarifies that the taxes whose collection can be suspended are those that have arisen from the dispute that is under discussion in MAP. In respect of MAP cases with other countries, the Indian domestic law provisions shall govern the procedures related to suspension of collection of taxes or stay of demand. This typically involves part or full payment of the tax demand as issued by the Indian tax authorities.

V. Secondary adjustment provisions

The provisions relating to the "secondary adjustments" are applicable with effect from the Indian financial year starting from 1 April 2016. These provisions are primarily intended to ensure that profit allocation between the associated enterprises is consistent with the primary TP adjustment. The said provisions envisage MAP resolution as well in order to require actual cash repatriation for the differential profit amount. Accordingly, the Guidance clarifies that Indian CAs would be obligated to make such secondary adjustments part of the MAP resolution in respect of cases pertaining to the financial year 2016-17 or thereafter.

VI. Other issues

- ▶ **Recurring issues:** While the Indian CAs may resolve recurring issues on the same principles, as adopted in a prior MAP resolution, the Guidance states they do not have the power to prevent the tax authorities from making an order that is not in conformity with prior MAP resolutions in the case of the same taxpayer and on the same issues.
- ▶ **Set-off of WHT paid by an Indian taxpayer pursuant to WHT default enquiry:** The Guidance clarifies that the WHT paid as per the demand arising from an order in WHT enquiry proceedings may be set off against the nonresident taxpayer's tax liability while implementing the MAP resolution in respect of the relevant issue.

Implementation of MAP outcomes

The Guidance clarifies that the MAP resolution shall be implemented in all cases except where an ITAT order (for a MAP covered year) is brought to the attention of the Indian CA or is passed (but not implemented) after resolution of the MAP. In such cases, the outcome of the ITAT order is applicable and thus will only seek correlative relief at the level of the treaty partner. Further, specified timelines as per amended MAP rules shall be strictly adhered to in order to ensure speedy implementation of the MAP resolution.

Further, the Guidance reiterates that following post MAP resolution and subsequent acceptance by the taxpayer, the concerned Assessing Officer in India, should send the copy of such order giving effect to the MAP resolution to the Indian CA along with the details of amount/date of payment of taxes/date of issue of refund to the taxpayer, withdrawal of appeals filed by the tax authorities, and any other relevant details.

Implications

The release of India's Stage 1 peer review report represented the continued recognition and importance of the need to achieve tax certainty for cross-border transactions for multinational enterprises. The amended MAP rules along with the Guidance provide much-needed insights and clarity to taxpayers considering the use of MAP for resolving cross-border tax disputes.

The Guidance further reinforces India's commitment to make dispute resolution an effective and efficient process by reforming the MAP regime to comply with the key areas of the Report. As noted in the Report, due to resource constraints, there have been some delays in the discussion and resolution of MAP/APA cases. Considering the recommendations of the OECD, the CBDT may also need to strengthen the teams overseeing MAP cases by providing additional resources for the efficacy of the MAP program. Nonetheless, given the challenges with the domestic tax law appeal process, MAP and APAs continue to be a preferred option for resolving/preventing cross-border tax disputes, particularly in the area of TP, to mitigate the double taxation risks.

Endnotes

1. See EY Global Tax Alert, [OECD releases India Stage 1 peer review report on BEPS Action 14](#), dated 6 November 2019.
2. See EY Global Tax Alert, [India amends Mutual Agreement Procedure rules](#), dated 20 May 2020.

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