

# THE POWER OF BEING UNDERSTOOD

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## WHITE PAPER

### Base Erosion and Profit Shifting

THE POWER OF BEING UNDERSTOOD



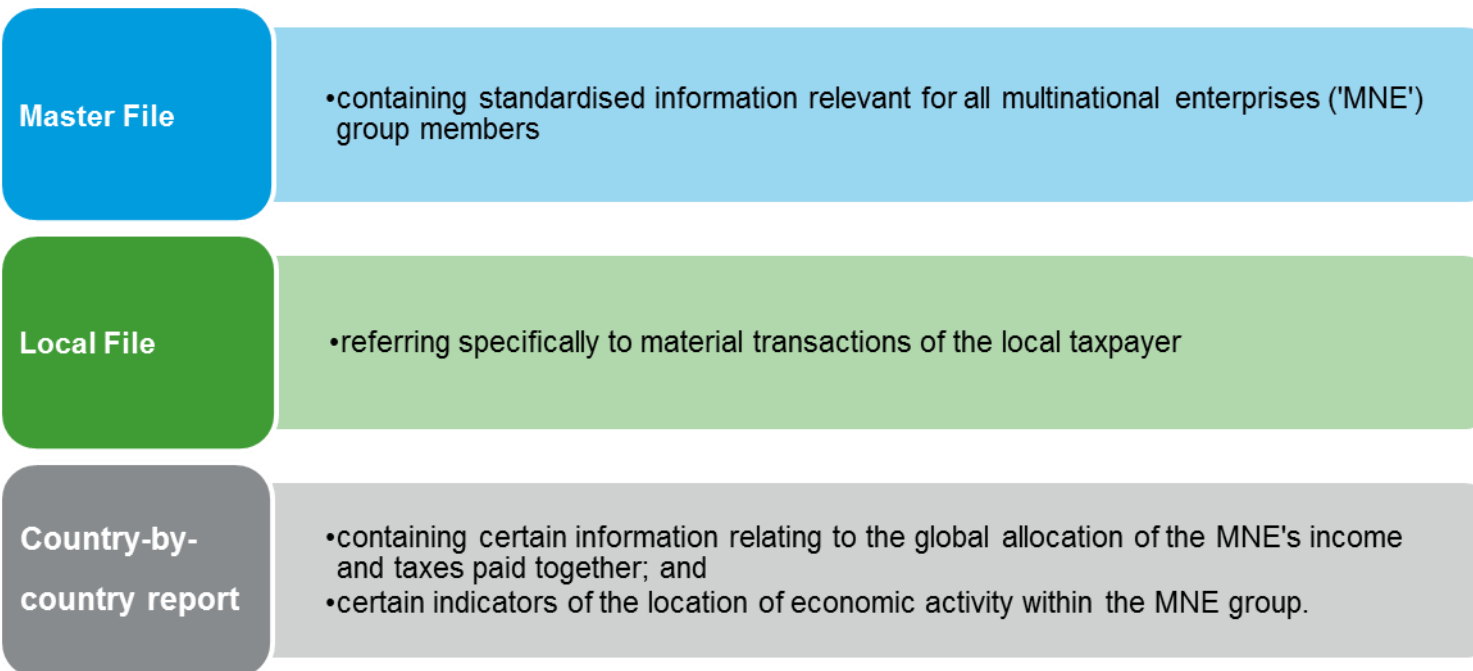


## 1.0 Background

The integration of national economies and market has increased substantially in recent years putting a strain on the international taxes, which were devised many years ago. Weaknesses in the current roles create opportunities for Base Erosion and Profit Shifting ('BEPS') requiring bold moves by policy makers to restore confidence in the system and ensure that the profits are taxed where economic activities take place and value is created. Accordingly, OECD and G20 countries adopted a 15-point action plan to address BEPS. Recently, G20 along with OECD agreed to implement recommendations of BEPS project.

With a view to align the existing Indian Transfer Pricing regulations pertaining to maintenance of documentation, the Finance Bill, 2016 proposes to adopt Action 13 of the Action Plan on BEPS ('BEPS Action Plan 13') for Transfer Pricing Documentation and Country-By-Country ('CbC') reporting by introducing an amendment to section 92D and inserting a new section 286 to the Income-tax Act, 1961 ('the Act'). These provisions will be effective from the Assessment year 2017-18 (financial year commencing 1 April 2016) and subsequent assessment years.

BEPS Action Plan 13 recommends that the countries should adopt a standardized approach to maintaining Transfer Pricing documentation. **A three-tiered structure has been mandated consisting of:**



These 3 documents will require taxpayers to articulate consistent transfer pricing positions and provide tax administrations with useful information to assess transfer pricing risks. It will facilitate tax administrations to make determinations about where their resources can most effectively be deployed, and in the event audits are called for, provide information to commence and target audit enquiries.

BEPS Action Plan 13 is proposed to be applicable from 1 April 2016. While the documentation requirement has been prescribed in line with Action Plan 13 of the OECD BEPS Action Plan; the detailed rules, pertaining to format of the report and guidelines on filing, are yet to be notified.

## 2.0 Regulations and Framework

Sections 92 to 92F of the Act contain provisions relating to Transfer Pricing regime. Section 92D of the Act provides for maintenance of prescribed information and documentation relating to the international transaction and / or specified domestic transactions.

In order to implement the BEPS Action Plan 13, essential elements of specific reporting regime in respect of CbC reporting and the master file are proposed to be introduced in the Act vide amendment to section 92D and insertion of sections 286, 271GB and 271AA of the Act. The remaining aspects, pertaining to format of the report and guidelines on filing, are to be detailed in rules which are yet to be notified.

As per the Finance Bill 2016, a proviso is proposed to be inserted in section 92D(1) of the Act to provide that a constituent entity of an international group shall be required to maintain prescribed documentation. Further, sub-section (4) is proposed to be inserted in section 92D to provide that such documentation shall be furnished to the prescribed authority on or before the prescribed date.

Further, new section 286 is proposed to be inserted in the Act, requiring CbC reporting of each entity within an international group in certain cases. This amendment proposes to introduce reporting in line with Action 13 of the BEPS Action Plan, which suggests that for each international group, CbC reporting should be undertaken in the country of residence of the parent entity of the group.

As per the proposed amendments, the CbC reporting will need to be filed with the prescribed authority in India if the parent entity of the international group is in India. Further, if the CbC reporting filed by the parent in another country, of which it is a resident, is not made available to the Indian authorities either on account of no agreement between India and that country or due to non-cooperation of that country for providing such information, then, the Indian entity will be required to file a CbC reporting in India, even if it is not a parent entity of the group.

The reporting shall be in the prescribed format, which shall be based on the Template provided by the OECD in BEPS Action Plan 13 Report.

The CbC reporting requirement shall apply wherein the consolidated revenues of the preceding year of the group, based on consolidated financial statement, exceeds the prescribed of Euro 750 million i.e. Indian currency equivalent to Rs. 5,395 crores. Therefore, CbC reporting for an international group having Indian parent, for the financial year 2016-17, shall apply only if the consolidated revenue of the international group in previous year 2015-16 exceeds Euro 750 million or about Rs. 5395 crores (the equivalent would be determinable based on exchange rate as on the last day of earlier financial year 2015-16).



The prescribed date for filing the CbC report is proposed to be the due date of filing of return of income for the relevant assessment year for which the report is being furnished. The report shall contain several parameters of each entity of the international group such as profit / loss before tax, income tax paid and accrued, capital, accumulated earnings, tangible assets, etc.

It is proposed to insert section 271GB of the Act and amendment to section 271AA of the Act for non-furnishing of the report or furnishing inaccurate

Sections under the Act	Particulars of Default	Penalty
Section 271GB Non-furnishing of Report	(a) Default not more than one month	Rs. 5,000 per day
	(b) Default more than one month	Rs. 15,000 per day for period exceeding 1 month
	(c ) Default even after service of order levying penalty under either (a) or (b) above	Rs. 50,000 per day continuing default beyond the date of service of penalty order
Section 271GB Timely non-submission of information and documents before prescribed authority	(a) timely non-submission of information before prescribed authority when called for	Rs. 5,000 per day
	(b ) Default even after service of order levying penalty under (a) above	Rs. 50,000 per day continuing default beyond the date of service of penalty order
Section 271AA Inaccurate Information in Report	(a) the entity knows of the inaccuracy at the time of furnishing the report but does not inform the prescribed authority; or	Rs. 5,00,000
	(b) the entity discovers the inaccuracy after the report is furnished and fails to inform the prescribed authority and furnish correct report within a period of 15 days of such discovery; or	
	(c) the entity furnishes inaccurate information or document in response to notice of the prescribed authority.	



### 3.0 BEPS Documentation vis-à-vis TP Documentation

#### 3.1 Information or documentation required under current Transfer Pricing regime under Rule 10D of the Rules.

Rule	Information/ documents
10D(1)(a)	Ownership structure of the taxpayer
10D(1)(b)	Profile of the multinational group
10D(1)(c)	Broad description of the business and industry
10D(1)(d)	Details of intra-group transactions
10D(1)(e)	Function, assets and risks analysis
10D(1)(f)	Supporting documents for the inter-company transactions such as agreements, official publications, reports, studies, market quotations, results of market research, letters in respect of negotiations, etc.
10D(1)(g)	Comparability analysis, including description and reason for selection of a particular TP method, along with the record of actual working carried out to determine the arm's length price
10D(1)(h)	
10D(1)(i)	
10D(1)(j)	
10D(1)(k)	Assumptions, policies and price negotiations, if any, which have critically affected the determination of the arm's length price
10D(1)(l)	Details of adjustment made to transfer prices to align them with arm's length price, if any
10D(1)(m)	Any other information/ document relevant to the determination of arm's length price



### 3.2 Comparison of Master File with Rule 10D

Constituent of Master File	Presence in Rule 10D
<b>■ Organizational Structure</b> <ul style="list-style-type: none"> <li>• Chart with Group legal &amp; ownership structure and geographical location of operating entities</li> </ul> <b>■ Description of the Group's Business(es)</b> <ul style="list-style-type: none"> <li>• Important drivers of business profits</li> <li>• Description of important business restructuring transactions</li> <li>• Description of supply chain for 5 largest products / services</li> <li>• List and brief description of important group service arrangements</li> <li>• Brief functional analysis describing the principal contributions to value creation by individual group entities</li> </ul>	<b>■</b> Broadly covered under Rule 10D(1)(a), Rule 10D(1)(b) and Rule 10D(1)(c) <b>■</b> Restricted to entities with whom transactions are entered into
<b>■ Group's Intangibles</b> <ul style="list-style-type: none"> <li>• Description of the overall strategy for development and exploitation of intangibles including Group TP policies re R&amp;D and intangibles</li> <li>• List of important Group intangibles with the list of (a) entities legally owning them and (b) important intragroup agreements</li> <li>• Important transfers of interests in intangibles within the Group</li> </ul>	<b>■</b> Not specifically covered under Rule 10D, however, intangibles relating to the Indian operations are required to be described under Rule 10D(1)(e)
<b>■ Group Intercompany Financial Activities</b> <ul style="list-style-type: none"> <li>• Group's financing arrangements and related TP policies</li> <li>• Identification of central financing entities</li> </ul>	<b>■</b> Not covered under Rule 10D
<b>■ Group's Financial &amp; Tax Positions</b> <ul style="list-style-type: none"> <li>• List of relevant APAs and tax rulings relating to the allocation of income among countries</li> <li>• Annual consolidated financial statement</li> </ul>	<b>■</b> Not covered under Rule 10D

### 3.3 Comparison of Local File with Rule 10D

Constituent of Local File	Presence in Rule 10D
<b>■ Local Entity</b> <ul style="list-style-type: none"> <li>Local organization chart and management structure</li> <li>List of key competitors</li> <li>Detailed description of the business and business strategy pursued (including business restructurings or intangible transfers)</li> </ul>	<b>■</b> Broadly covered under Rule 10D (1) (a), Rule 10D (1) (b) and Rule 10D (1) (c)
<b>■ Controlled Transactions</b> (not exhaustive) <ul style="list-style-type: none"> <li>Amount of intra-group payments and receipts involving the local entities broken down by jurisdiction of the foreign payer / recipient</li> <li>List of associated enterprises involved in controlled transactions and relationships</li> <li>Detailed comparability &amp; functional analysis with copies of all material intercompany agreements</li> <li>Indication of the most appropriate TP method selected</li> <li>List and description of selected comparable uncontrolled transactions relied on in the TP analysis and possible adjustments performed</li> <li>Copy of APAs or tax rulings to which local tax jurisdiction is not a party but impacting relevant controlled transactions</li> </ul>	<b>■</b> Covered under Rule 10D (1) (d) to Rule 10D (1) (m) - except details relating to unilateral/ bilateral APAs and similar rulings
<b>■ Financial Information</b> <ul style="list-style-type: none"> <li>Annual local entity financial accounts</li> <li>Information and allocation schedules showing link between financial data used in TP method and annual financial statements</li> <li>Summary schedules and sources of relevant financial data for comparables used</li> </ul>	

### 3.4 Comparison of CbC reporting with Rule 10D

Constituent of CbC reporting	Presence in Rule 10D
<b>■ CbC reporting by MNEs</b> <ul style="list-style-type: none"> <li>• the amount of revenue;</li> <li>• profit before income tax;</li> <li>• income tax paid and accrued;</li> <li>• total employment;</li> <li>• capital; and</li> <li>• accumulated earnings and tangible assets in each tax jurisdiction.</li> </ul>	<b>■ Not covered under Rule 10D</b>

## 4.0 Way Forward

The BEPS package of measures represents substantial overhauling of the international tax rules. Once the new measures become applicable, it is expected that the profits will be reported where the economic activities that generate them are carried out and where value is created.

The BEPS package is designed to be implemented via changes in domestic law and practices, and via treaty provisions, with negotiations for multi-lateral instrument underway and expected to be finalized in 2016.

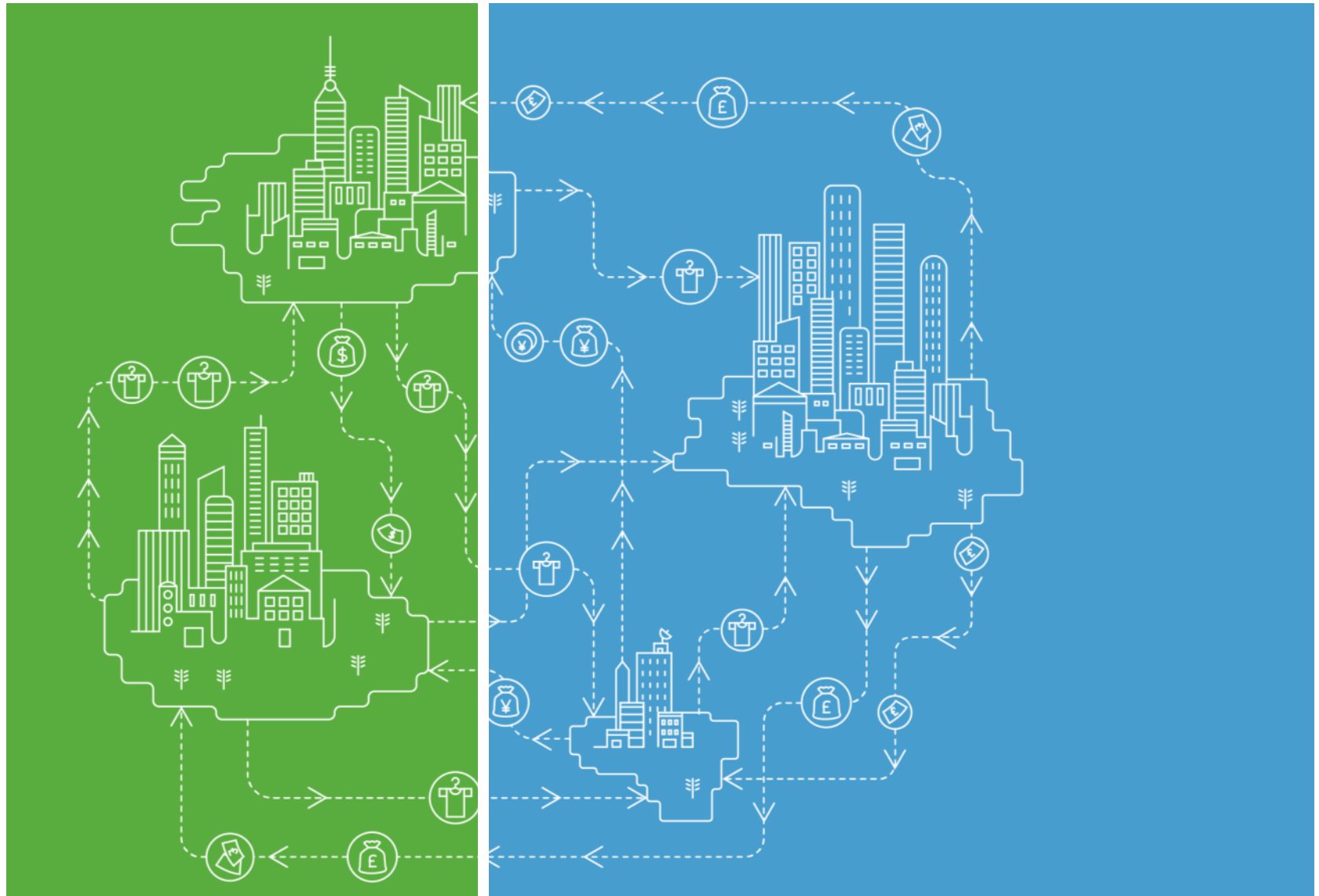
The CbC reporting under BEPS Action Plan 13 is being widely implemented by various jurisdictions across the world due to the ease of availability of information to the tax authorities, which will enable them to identify the risk areas in transfer pricing cases and get an overview of the operations of multi-national groups. The transfer pricing authorities across the globe will now have a much deeper insight in to the global operations of the group and the overall transfer pricing approach vis a vis the business aspects and economic functions performed. Their approach and analysis will not be limited to country specific operating profitability and benchmarking done.

While the amendments proposed to be introduced are with the same intention, the requirement of furnishing the same before the due date of filing return of income will be an onerous compliance burden. In addition to that, the burden of the penalties is significant, especially considering that for multinational groups having hundreds of group entities, the collation of information itself will be critical.

Some of the key actions required are:

- Analyze the new requirements and their applicability including CbC reporting in India and other countries. As this is a part of global initiative, it is expected that similar provisions are introduced in several countries this year.
- Develop templates of Master File, Local File and CbC File

- Identifying information to be maintained by each entity necessary for ensuring overall reporting
- Develop global transfer pricing policy keeping in view the BEPS and CbC requirements
- Assign responsibility for collation and compilation of information
- Ensure timely reporting



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The purpose of this White Paper ('Paper') is to provide a brief overview of the recently introduced BEPS Action Plan 13 based on our understanding of the proposed regulations as shall be applicable in India. This White Paper is subject to revision as this is a new regulation and more clarity is awaited thereon. After review of this Paper, the same should be discussed with us to determine the final course of action. No part of this Paper shall be reproduced without our prior written consent. The Paper is prepared for general use and our views as stated above would be required to be revalidated vis-à-vis the facts of each case. The Government or judicial authorities may or may not subscribe to the views expressed herein. Under no circumstances, the above should be used as any tax avoidance scheme. While we have taken steps to ensure that the White Paper is a qualitative document in all material respect, professional guidance must be sought before taking action and we are not responsible for any liability arising from any statements or errors contained in this Paper .

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