

Tax Alert

Transfer Pricing



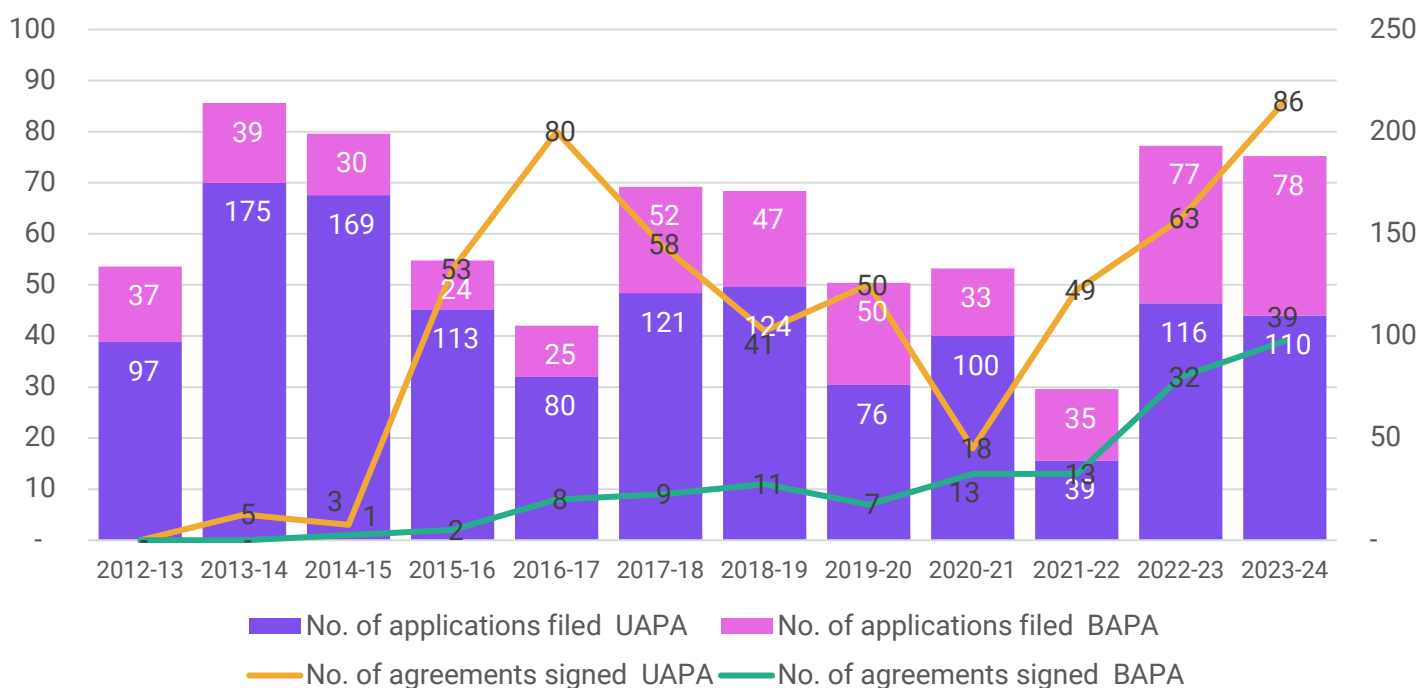
Highlights of CBDT's 6th Annual Report on APA Program

The Advance Pricing Agreement (APA) program has proven to be an effective tool for dispute resolution since its inception in 2012 in India. The Sixth Annual Report, covering FY 2023-24, clearly highlights the progress made by the Central Board of Direct Taxes (CBDT) in entering into APAs. The previous annual report, issued in September 2023, provided statistics up to

FY 2022-23, offering valuable insights into the growth and impact of the program over the years.^{1,2}

The summary of the number of applications filed and the number of agreements signed (year-wise) is given below for ease of reference:

Applications filed and agreements closed



1. <https://incometaxindia.gov.in/Lists/Latest%20News/Attachments/601/APA-Report-Final-2023.pdf>

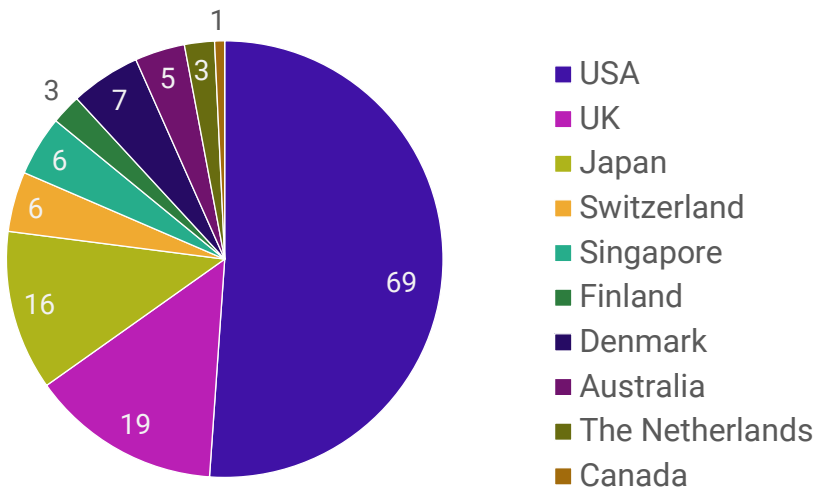
2. https://www.nexdigm.com/data/mailler/nexdigm_transfer_pricing_alert_4_September_2023.pdf

In FY 2023-24, a remarkable 125 agreements were finalized, reflecting a significant 31.58% increase compared to FY 2022-23. Notably, the trend of taxpayers opting for Bilateral Advance Pricing Agreements (BAPAs) over Unilateral Advance Pricing Agreements (UAPAs) continues to strengthen, driven by the desire for greater bilateral tax certainty. This trend is further underscored by the fact that, for the second consecutive year, the highest number of BAPAs ever recorded has been reached.

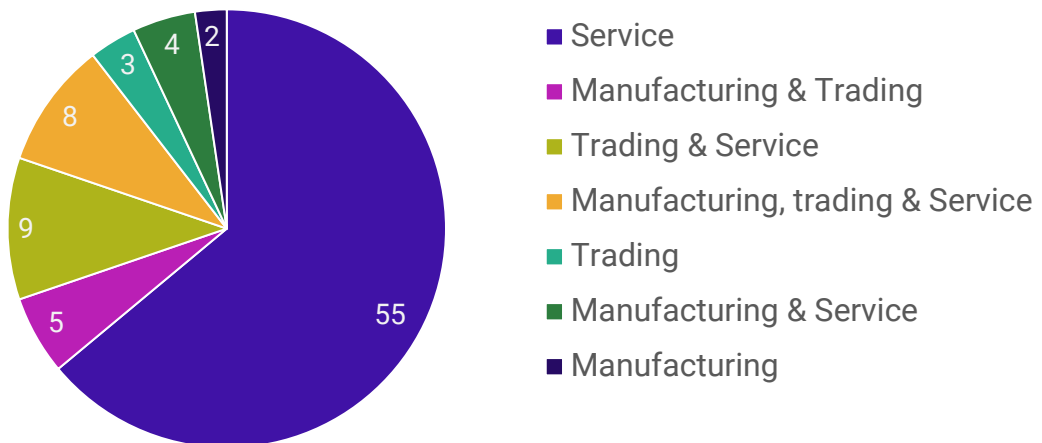
A total of 1,847 applications were filed over a span of 12 years, from FY 2012-13 to FY 2023-24. Of these, 641 applications were concluded by the end of FY 2023-24. Out of the remaining 1,206 pending applications, 348 were disposed of for other reasons. Therefore, 858 applications are still in process as of FY 2023-24. Furthermore, during FY 2023-24 alone, 188 new applications were filed, contributing to the overall number of pending applications.

A total of 39 out of the 125 agreements signed are BAPAs, with the highest number signed with the USA, followed by the UK and Japan.

Country-wise status of Agreements signed - BAPAs



Agreements signed - UAPAs



As can be seen from the chart above, the agreements signed during FY 2023-24 predominantly involve the service sector. A significant portion of these agreements pertains to captive companies engaged in software development and Business Process Outsourcing (BPO). Additionally, some of these companies also provide services in engineering design, Research and Development (R&D), and Knowledge Process Outsourcing (KPO). This trend highlights India's prominent role as an outsourcing hub for information technology and business processes, with numerous foreign multinationals establishing a presence in India's IT clusters. The pharmaceutical and chemical industries have also seen a growing representation in the APAs signed, reflecting the increasing global importance of the Indian pharmaceutical sector.

Notably, during this period, the provision of IT-enabled services/back office services and the reimbursement/recovery of expenses have been the most frequently covered transactions in the agreements, followed by software development services/IT support services and the receipt of management/corporate/other support services/intra-group services (IGS). IGS-related international transactions, totaling 18 during this period, are often subject to litigation. Their inclusion in APAs highlights the potential for harmonious resolution through collaboration between the tax department and the industry, fostering a more effective and efficient approach to resolving complex transfer pricing matters.

The Transactional Net Margin Method (TNMM) is the preferred method to conclude the determination of Arm's Length Price (ALP) of the covered transactions.

Since its launch, the APA program has successfully expedited the resolution of more complex cases. On average, the processing time for applications is approximately 45.97 months for UAPAs and 63.11 months for BAPAs. Notably, for FY 2023-24, it is interesting to note that the average duration for closing UAPA applications has reduced from 59.73 months in FY 2022-23 to 54.65 months. However, for

BAPAs, the average processing time has increased from 62.1 months to 65.61 months during the same period.

The report also provides a brief overview of the Mutual Agreement Procedure (MAP) cases that were successfully resolved during this period.

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|------------------------------------|------|
| Calendar Year | 2023 |
| Opening Inventory | 709* |
| Invocations during the year | 68 |
| Closures during the year | 115 |
| Closing Inventory | 662 |

**opening inventory is as per MAP Statistics Report*

Based on the APA Annual reports published by CBDT to date, it is evident that there has been a steady decline in both the closing inventory and the closure of MAP cases during the year.

Through its foundation on principles of mutual trust and cooperation between taxpayers and tax authorities, the program has effectively reinforced the Indian tax administration's dedication to enhancing the ease of doing business. The signed APAs have ensured certainty for approximately 3,430 assessment years (including around 804 years of roll-back), which is a significant relief in the long-drawn litigation process. The Indian Government's dedication to the program's success is evident in its recognition of challenges and assurance to continually improve the APA program.

The APA programme serves as a crucial tool in alleviating the burden on tax tribunals and the higher judiciary by preventing transfer pricing litigation. Even if it is assumed that only half of the assessment years covered by the APA program would have ended up in litigation, disputes for over 1,700 assessment years have effectively been prevented or resolved by the program.

Notably, during FY 2022-23 alone, the APA program provided tax certainty for more than 700 assessment years, further highlighting its significant role in promoting dispute resolution and tax compliance.

APAs have globally proven to be an effective mechanism for addressing transfer pricing issues. Taxpayers have successfully secured assurance on transfer pricing matters for durations ranging from 5 to 9 years. The collective impact of 641 signed APAs is estimated to have provided income certainty of approximately INR 250 billion. This has resulted in a tax and interest settlement of around INR 75 billion, all achieved without litigation or any ensuing disputes. As a result, these agreements remain litigation-free and do not give rise to appellate proceedings.

India's proposition of fostering certainty to enhance the ease of doing business is largely dependent on the success of the APA program, and it appears to be heading in the right direction. Achieving more closures of pending APA cases within shorter time frames would significantly contribute to realizing this objective. Additionally, as mentioned above, this would help reduce the litigation burden substantially, easing the strain on tax tribunals and the higher judiciary by resolving transfer pricing disputes efficiently and avoiding prolonged litigation.



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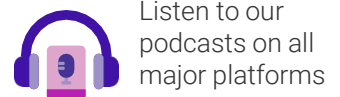
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