



Advance Pricing Agreements in India: A Revolution in Taxation Law

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Abstract

Double taxation is one of the biggest challenges faced by multinational corporations, especially when the taxable transaction is between associated enterprises. The determination of transfer pricing becomes a bone of contention among the revenue authorities of different countries. One mechanism to counter this problem is to take recourse to 'Advance Pricing Agreement' (APA). An APA is an arrangement entered into between revenue authority(s) and the taxpayer to determine the transfer pricing in advance. It has a plethora of advantages and procedural benefits over the conventional methods of determination of transfer pricing. APA, which was in existence in many countries for many years, was recently introduced in India. The aim of this paper is primarily to explore the Indian law on APA in the light of the situation prevalent in other countries, and to suggest measures to improve the same. This aim shall be achieved by firstly studying the concepts pertaining to transfer pricing and the problems associated with it, which has led to the emergence of APA. Thereafter, an overview of the Indian APA regime is provided. Further, in order to evaluate the merits and demerits of Indian APA, a comparative study with the law on APA in other countries has been

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presented, while simultaneously making certain suggestions to make the Indian APA system robust. In the last part of the paper, some suggestions apart from those which were made after analyzing the comparative law have been made. If India improves upon its APA regime by taking a cue from other countries, and by implementing measures such as the creation of safe harbours, better dispute settlement mechanism, easier documentation etc., then the APA will surely bring the much desired revolution in the taxation of multinational corporations.

Keywords: Advance Pricing Agreements, Arm's Length Principle, Associated Enterprise, Safe Harbour, Transfer Pricing.

Introduction

International taxation with its growing features has presented us with not only a variety of new and hybrid instruments but also the need for regulating taxation across boundaries. Globalization has contributed to cross border trading between related entities. It is important that these statements be read along with the relevance of taxation. Taxes not only determine the economy and growth of a state but also increasing the relationship between the states. Developing nations must be more concerned about these phenomena as their dependency on tax to meet certain socialistic aspirations is higher than ever.

The Double Irish Arrangement¹ evolved by Apple Inc. is one of the examples on how companies have a tendency to evade tax on their intra-corporation and multinational transactions. These commercial entities tend to structure their transactions in such a manner that they can avoid the harsher taxing regimes, thereby paying as less tax as possible. This is because the different domestic jurisdictions have different tax regimes and the companies and other

¹ A strategy used by multinational corporation to lessen their tax liability using tools like direct sales, contract production, treaty shopping, hybrid mismatch, and transfer pricing rules. See, International Monetary Fund, *Fiscal Monitor* (October, 2013) at 47.

commercial bodies want to make as much money as possible. The structuring of a transaction to avoid tax becomes easier when the taxpayer has a multinational character. It can conveniently shift profits from one jurisdiction to another. Since, the division of the assets of a corporation among group companies does not amount to affecting the assets of the company as a whole; the companies shift their money from a higher taxing regime to a more reluctant one. The phenomenon of 'transfer pricing', thus, becomes important.

Transfer pricing generally refers to the setting of prices for transactions between associated enterprises involving the transfer of property or services.² Advance Pricing Agreements (APA) help in determining the transfer price beforehand.

This paper has three broad themes. The first theme explains the concept of 'transfer pricing', its constituents and the principles like arm's length and seeks to analyse as to how the same has led to the advent of APA. The second theme examines the legal regime pertaining to APAs in India. The last theme evaluates the pros and cons of the law relating to APA in India and tends to make suggestions for streamlining the Indian law by referring to international guidelines and practices by comparing the Indian law with the legal regime in some major jurisdictions.

The Phenomenon of Transfer Pricing

Issues Pertaining to Transfer Pricing

The current pattern of international taxation has mandated many nations to incorporate the term 'transfer pricing' high on their tax agenda. The United Nations Manual for Developing Countries³ defines it to be the general term for the pricing of cross-border, intra-firm transactions between related parties. In other words, it refers to the pricing of transactions between related entities for

² The United Nations Practical Manual on Transfer Pricing for Developing Countries", Department of Economic & Social Affairs, 2013, at ¶1.1.6. available at [http://www.un.org/esa/ffd/documents/ UN_Manual_TransferPricing.pdf](http://www.un.org/esa/ffd/documents/UN_Manual_TransferPricing.pdf) (last visited Mar. 01, 2014).

³ *Id.*

goods, services, intangible property transfers, rents and loans.⁴ The World Bank estimates that about two thirds of all business transactions take place within a group⁵ and hence involve transfer pricing. The process itself is however complicated. Several components determine a transfer price⁶; like the methods by which multinational taxpayers account for transactions among subsidiaries and divisions⁷ in different countries, documentation, local audits, expertise and so on. These practices vary widely from country to country. Thus, arriving at a transfer price is evidently not an easy process, and is a potential one for many disputes and problems. It is, therefore, expedient that the valuation of the transfer between related parties is accurate because it affects the distribution of profits among related companies and their taxable incomes.⁸ However, countries generally have no sufficient resources to perform a thorough audit of every possible transfer pricing issue.⁹ The complexity is increased by the presence of two

⁴ Marc M. Levey, C. Wrappe Steven, Steven C. Wrappe, Kerwin Chung, *Transfer Pricing Rules and Compliance Handbook* (2005), Walters Kluwer, at ¶101.

⁵ World Bank, *Transfer Pricing Technical Assistance Global Tax Simplification Program* (2011), Presentation given by Rajul Awasthi in Brussels, 24 February 2011.

⁶ A transfer price is defined by the OECD Glossary of Statistical Terms as “a price, adopted for book-keeping purposes, which is used to value transactions between affiliated enterprises integrated under the same management at artificially high or low levels in order to effect an unspecified income payment or capital transfer between those enterprises.” *available at* <http://stats.oecd.org/glossary/detail.asp?ID=2757> (Last Visited Mar. 1, 2014).

⁷ Pamela L. Kayfetz & Leo B. Helzel, *Transfer Pricing: Achieving Fair National Taxation of International Transactions*, 3 ANN. SUAV. INT’L & COMP. L. 193 (1996).

⁸ United States General Accounting Office, IRS’s Advance Pricing Agreement Program (2000), GAO/GGD-00-168, at 3.

⁹ Draft Handbook on Transfer Pricing Risk Assessment OECD, 30 April 2013, *available at* <http://www.oecd.org/tax/transfer-pricing/Draft-Handbook-TP-Risk-Assessment-ENG.pdf> (last visited , Mar. 01, 2014).

different tax jurisdictions and no accurate method exists to derive the correct price in such cases.

In order to address the transfer pricing related issues of the increasing number of multinational enterprises and their global transactions, the Organisation for Economic Co-operation and Development (OECD) developed international transfer pricing guidelines (the OECD Guidelines) in 1995. In 2010,¹⁰ these guidelines were revised to be applied to accounting periods beginning on or after April 1, 2011, and for income tax purposes for the tax year 2011-2012 and for the subsequent years. These guidelines are followed by the twenty five countries who are members of the OECD. While these guidelines do not by themselves bind the administration and the tax payers, they are useful as guiding principles and are considered even by the non member countries as a leading interpretation on the various provisions that are enshrined in the transfer pricing agreements.¹¹

Associated Enterprises

Section 92A of the Income Tax Act, 1961 defines associated enterprise as an enterprise which “(a) participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or (b) in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise”. An enterprise is associated to another enterprise if it is involved directly or indirectly through any intermediary(s) in the control, management, voting or capital of the latter. If the people involved in the previously stated affairs of the company are the

¹⁰ See OECD, *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, (OECD Publishing, Jul. 22, 2010).

¹¹ Ernst & Young, *OECD Releases Transfer Pricing Guidelines*, Issue 5 October 2010. available at [http://www.ey.com/Publication/vwLUAssets/OECD_releases_transfer_pricing_guidelines/\\$FILE/OECD_releases_transfer_pricing_guidelines.pdf](http://www.ey.com/Publication/vwLUAssets/OECD_releases_transfer_pricing_guidelines/$FILE/OECD_releases_transfer_pricing_guidelines.pdf) (last visited, Mar. 01, 2014).

same, then also they are treated as associated enterprises. Two enterprises may also be deemed to be associated by taking into account factors like shareholding, presence of equity and loans, composition of board of directors etc.¹²

The Arm's Length Principle

Despite the difficulty in determining an accurate transfer price of a transaction, the arm's length method has been given recognition both by the OECD and the United Nation. It is hence considered as an international standard to determine transfer pricing. Article 9(1) of the OECD Model Tax Convention¹³, which defines 'associated enterprises', states it to be "where conditions are made or imposed between two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxes accordingly." As per this approach, each part of the multinational entity is treated as a separate part of the economic entity (whether it is a branch or a subsidiary) and a price is substituted for taxation purposes that would have been used in the transaction had it been with an unrelated third party rather than a related party within the same multinational entity¹⁴. Hence a related party transaction (non arm's length) should be dealt with as if it is a non related party (arm's length) transaction. This principle is then applied to a pricing method specified either under the OECD guidelines¹⁵ or the country's domestic law. The OECD guidelines reflect the provision

¹² Robert Feinschreiber & Margaret Kent, *Asia - Pacific Transfer Pricing Handbook*, (John Wiley & Sons Singapore Pty Ltd., 2012).

¹³ OECD , *Model Tax Convention on Income and on Capital 2010: Full Version*, (OECD Publishing, 2012).

¹⁴ Dr. Kerrie Sadiq, *The Taxation of Multinational Banking Income : Is the Traditional Rationale Correct?* (2008) JOURNAL OF BANKING AND FINANCE LAW AND PRACTICE, 19(4), 229-248, 233.

¹⁵ The OECD Guidelines consider five methods for reaching the Arm's Length Price which are divided into traditional transactional methods and transactional profit methods.

of 'the most appropriate method'¹⁶, wherein there is no strict hierarchy of the five methods suggested by the OECD and the party can choose the one that suits the transaction. The United Nations Convention on Double Taxation¹⁷ in Article 9 also contains the arm's length principle, but does not provide further details of transfer pricing transactions. The obvious advantages of this principle are that it helps in curbing tax evasion, provides certainty of pricing, and that it is geographically neutral.¹⁸

The steps for determining the arm's length price as explained in *Ranbaxy Laboratories Ltd. v. Addl. Commissioner of Income Tax*¹⁹, are as following. Analyse the specific characteristics of the controlled transaction whether it relates to transfer of goods, services or intangibles. All the characteristics of the controlled transaction which are likely to affect its open market value must be taken into account; then after the selection of the comparables, best method of determining arm's length price is selected. Thereafter, a functional analysis is carried out to identify functions, risk and assets of uncontrolled transactions and a comparison is carried out with characteristics of the controlled transaction.

However, even while transacting at arm's length, problems can arise like the problem of uncertainty of the tax that is payable in each country and the risk that the two tax authorities will prescribe different transfer prices for the sale of goods or services and the related taxpayers will face double taxation²⁰. It is also not easy to

¹⁶ The OECD Guidelines, ¶¶ 2.2 and 2.3.

¹⁷ United Nations, *Model Double Taxation Convention between Developed and Developing Countries* (2011) available at http://www.un.org/esa/ffd/documents/UN_Model_2011_Update.pdf.

¹⁸ U.N. Manual, ¶ 1.4.6.

¹⁹ (2008) 299 I.T.R. 175 Delhi.

²⁰ Hui Zhang, *Improving the Administration of Bilateral Advance Pricing Arrangements in China*, World Bank, at 3 available at [http://lnweb90.worldbank.org/exteu/SharePapers.nsf/\(ID\)/03722265FAC1F9048525780B0051FF13/\\$File/improving_the_administration_of_bilateral_advance_pricing_arrangements_in_china.pdf](http://lnweb90.worldbank.org/exteu/SharePapers.nsf/(ID)/03722265FAC1F9048525780B0051FF13/$File/improving_the_administration_of_bilateral_advance_pricing_arrangements_in_china.pdf). (last visited , Mar. 01, 2014).

find 'comparables' from the transaction being executed to fit a price method resulting in potential disputes over pricing methods too.

To resolve the problem of uncertainty and to avoid potential transfer pricing dispute, APA has been introduced as a mechanism. An APA is basically a contractual arrangement with the tax administration of one or more countries to resolve potential tax disputes in an amicable and cooperative manner. It determines the appropriate transfer pricing method for future intercompany international transactions.²¹ The taxpayers have the obvious interest in preventing double taxation, while governments are concerned with the collection of revenue which may be detrimentally affected by under taxation²². APAs, hence provide a middle ground for the interests of both the parties.

Understanding Advance Pricing Agreement

Advance Pricing Agreement: Meaning

The OECD guidelines define an APA²³ as “an arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed period of time”. An APA is formally initiated by a taxpayer and requires negotiations between the taxpayer, one or more associated enterprises, and one or more tax administrations. APAs are intended to supplement the traditional administrative, judicial and treaty mechanisms for resolving transfer pricing issues.²⁴

²¹ Yehonatan Givati, *Resolving Legal Uncertainty: The Unfulfilled Promise of Advance Tax Rulings*, Discussion Paper No. 30 6/2009, Harvard John M. Olin Center For Law, Economics, And Business Fellows Discussion Paper Series.

²² Wickham & Kerester, D Wickham and C Kerester, *New Directions Needed for Solution of the Transfer Pricing Tax Puzzle*, 5 TAX NOTES INTERNATIONAL (1992) 399, 401.

²³ The OECD Guidelines, ¶ 5 onwards.

²⁴ Ruling of the Australian Tax Office, Taxation Ruling TR 95/23 [11].

According to the Internal Revenue Service of the United States of America (IRS-US), APAs are designed to resolve actual or potential transfer pricing disputes in a principled, cooperative manner, as an alternative to the adversarial process.²⁵ It is a binding contract between the taxpayer and the tax administration of one or more countries (unilateral APA and multilateral APA) by which the latter agrees not to seek transfer pricing adjustments for a covered transaction, provided that the taxpayer follows the agreed transfer pricing method.

Advance Pricing Agreement (APA) is “an agreement between a taxpayer and tax administration as to the transfer pricing methods that will be used to determine the arm’s length price in transactions between the taxpayers and related parties. The APA will typically set out the critical assumptions on which the agreement is based and term for which the agreement is to apply.”²⁶ An APA is unique in the sense that it does not establish a position for the taxpayer in terms of setting the transfer price, but rather, it allows for agreement on an acceptable methodology for determining transfer prices.²⁷

Introducing APA in India: Section 92 CC and 92 CD of the Income Tax Act, 1961

India has one of the highest litigation figures over the world in transfer pricing.²⁸ “The transfer pricing adjustments in the recent sixth audit cycle in India alone amounted to Rs. 44,000 crore (approximately USD 9.78 billion) which is more than the aggregate

²⁵ United States General Accounting Office, *IRS’s Advance Pricing Agreement Program*(2000), GAO/GGD-00-168, at 3.

²⁶ *IBFD International Tax Glossary* 10 (Julie Rogers- Glabush ed., 6th ed. IBFD).

²⁷ A Sawyer, *Advance Pricing Agreements: A Primer and Summary of Developments in Australia and New Zealand* 1(9) Bulletin for International Fiscal Documentation (2004) 556, 556.

²⁸ Ernst & Young, *India is the third highest jurisdiction with pending transfer pricing disputes*, as per EY Survey, 20 August, 2012. available at http://www.ey.com/IN/en/Newsroom/News-releases/Press-Release_India-is-the-third-highest-jurisdiction-with-pending-transfer-pricing-disputes. (last visited Mar, 05, 2014).

income adjustments by tax authorities in audits of previous four years.”²⁹ To answer this problem, APA was first introduced in the draft Direct Taxes Code (DTC) in 2009 and again in the DTC 2010. However, since the DTC could not be implemented, the APAs also got deferred. Later, in a phenomenal move in July, 2012, the APAs were introduced in the Finance Act, 2012 by the Ministry of Finance, in order to avoid the unnecessary litigation over transfer pricing in international transactions, such as the *Vodafone Case*.³⁰

The provision for APA is now enshrined in Section 92CC and 92CD of the Income Tax Act, 1961 (Act). Section 92CC of the Act lays down that the Central Board of Direct Taxes (Board), with the central government’s approval, may enter into an APA with any person, determining the arm’s length price or specifying the manner in which arm’s length price is to be determined, in relation to an international transaction to be entered into by that person. It is also noteworthy that section 92A(2) enlarges the scope of the term ‘associated enterprises’ by listing down a number of factors which are useful in determining the association of two enterprises, such as, voting rights, power of appointment of directors, supply of raw materials, common control etc.

The methods to compute the arm’s length price for transactions between associated enterprises can be chosen by the parties from those given under section 92C or by any other method as they deem fit, thereby facilitating party autonomy. “Section 92C provides that the arm’s length price in relation to an international transaction or specified domestic transaction shall be determined by any of the methods listed there under, being the most appropriate method, having regard to the nature of transaction or class of transactions or class of associated persons or functions performed by such persons or such other relevant factors as the

²⁹ Grant Thornton, *Indian Advance Pricing Agreement Regime: The Game Changer* (2012) at 2. available at www.grantthornton.in/.../Indian_APA_regime_The_Game_changer.pdf (last visited Mar. 05, 2014).

³⁰ *Vodafone International Holdings v. Union of India & Anr*, 341 I.T.R. 1 (S.C.) 3.

board may prescribe.”³¹ The methods listed are, comparable uncontrolled price method, resale price method, cost plus method, profit split method, transactional net margin method and such other methods as may be prescribed by the board.

Under the comparable uncontrolled price method, resale price and cost plus methods, arm’s length results are determined from the price charged in comparable uncontrolled transactions for comparable goods, or from the gross profit margins of comparable uncontrolled resellers (resale price method) or gross profit margins of comparable produces (cost plus method).³² Under the profit split method, related corporations are treated as one unit, the net profits of which then allocated among the members of the group consistent with their economic contributions.³³ The transactional net margin method compares the net profit margin in relation to an appropriate base that the assessee makes in the controlled transactions to the same net profit margins earned by it in comparable uncontrolled transactions or alternatively, by independent comparable companies.³⁴

Subsection (2) of section 92C provides that ‘the most appropriate method’ referred to in subsection (1) shall be applied, for determination of arm’s length price, in the manner as may be prescribed.³⁵ In its press release issued on June 30, 2013, the Ministry of Finance clarified that there is no hierarchy amongst the six methods and the most appropriate method has to be

³¹ CBDT Circular No. 05/ 2013, Jun. 29, 2013 & Circular No. 05/ 2013, Jun. 29, 2013.

³² H. E. Abrams, *Essentials of United States Taxation* (Kluwer Law International, 1999).

³³ *Id.*

³⁴ *Chapter 5 - Transfer Pricing Methods (Transactional Profit Methods)*, Working draft of a Chapter of the Practical Manual on Transfer Pricing for Developing Countries, available at http://www.un.org/esa/ffd/tax/sixthsession/CRP4_Ch5.pdf. (last visited Mar. 01, 2014).

³⁵ Ministry of Finance, Circular No. 5, 30 Jul, 2013. available at http://www.incometaxindia.gov.in/archive/PressRelease_Circular_5_30_062013.pdf. (last visited: Mar. 01, 2014).

determined according to what is 'best suited to the facts and circumstances of each particular international transaction' and which provides 'the most reliable measure of an arm's length price'.³⁶ This provision is in line with the OECD guidelines and has to be interpreted based on the facts and circumstances of each case and will be dependent 'at finding the most reliable comparables,'³⁷ Rule 10C(2) of the rules lays down the factors³⁸ to be taken into account while finding the most appropriate method. These provisions shall be read in conjugation with section 92CB, which provides that the arm's length price shall be subject to the safe harbour rules. 'Safe harbour' has been defined as circumstances in which the income tax authorities shall accept the transfer price declared by the assessee.³⁹

Following are some of the prominent features of the Indian APA regime:

Types of APA

The three types of APA, which are generally permitted under the Indian law, are unilateral, bilateral and multilateral APAs. The

³⁶ Ministry of Finance, Circular No. 5, 30 Jul, 2013. available at http://www.incometaxindia.gov.in/archive/PressRelease_Circular_5_30_062013.pdf. (last visited: Mar. 01, 2014).

³⁷ See, The OECD Guidelines, ¶¶ 9.22-9.32.

³⁸ The factors to be taken into account for calculating the most appropriate method for calculation of Arm's Length Price for a *particular international transaction or specified domestic transaction* ("transaction") are-(a) the nature and class of the transaction; (b) the class or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises; (c) the availability, coverage and reliability of data necessary for application of the method; (d) degree of comparability between the transaction and the uncontrolled transaction and between the enterprises; (e) the extent to which reliable and accurate adjustments can be made to account for differences, if any, between transaction and the comparable uncontrolled transaction or between the enterprises; (f) the nature, extent and reliability of assumptions required to be made in application of a method.

³⁹ Income Tax Rules, 1962.

rules define unilateral agreement as neither an agreement between the board and the applicant which is neither a bilateral nor a multilateral agreement.⁴⁰ When the taxpayer enters into an APA with the revenue authorities of only one state, it is called a unilateral APA. These are generally considered problematic for reasons of disagreement of tax authority with the conclusion reached, the continuing uncertainty on the taxpayer, and non cooperation of foreign authorities with respect to adjustment of pricing. A bilateral APA comes into being when the applicant applies simultaneously to the revenue authority of two countries under the relevant treaty.⁴¹ Multilateral APA refers to an agreement between the board and the applicant, subsequent to, an agreement between the competent authority in India with the competent authorities in the other countries regarding the most appropriate transfer pricing method or the arm's length price.⁴²

Qualification for Application

No monetary qualification or cap has been prescribed under the Indian APA rules for a taxpayer in order to qualify to make an application for an APA. However, the need 'to determine the suitability of the international transaction for the agreement' is stated as a part of the pre filing consultation⁴³. Therefore, even though there is no express qualification, the intention appears to make the APA available to the taxpayers venturing into high yielding and complex transactions.

Pre-filing Consultation

For determining the viability of the APA, the assessee is required to make an application for pre-filing consultation before the Director General of Income Tax, before he makes a formal application for

⁴⁰ Income Tax Rules, Rule 10F(k).

⁴¹ Income Tax Department of India, *Advance Pricing Agreement Guidance with FAQs* (2013), at 2. available at www.itatonline.org/info/?dl_id=1215. (last visited Mar. 01, 2014).

⁴² *Id.* at 3.

⁴³ Income Tax Rules, Rule 10H(5)(iii).

APA.⁴⁴ The consultation and its outcome are not binding in nature.⁴⁵

A user fee has to be paid by the assessee at the time of making the application based on the likely value of transaction intended to be covered by the APA. For transactions amounting to not more than Rs. 100 crore, the user fee is Rs. 1 million. The user fee for transactions amounting to not more than Rs. 200 crore and more than Rs. 200 crore is 1.5 million and Rs. 2 million respectively.⁴⁶

Types of Transactions Covered

As far as the types of transactions are concerned, the Indian APA rules do not provide an exhaustive list of international transactions which can be covered under an APA. Hence, it is assumed that all the international intercompany transactions entered with associated enterprises can be brought under an APA. Further, APA is available for both continuing as well as proposed transactions. Moreover, it is not necessary that all the international transactions of a tax payer must be covered by the APA. The taxpayer is at the liberty to selectively choose the transaction for APA. However, it is expedient that the taxpayer fully discloses the related party transactions proposed to be undertaken before the APA team of the tax authorities. The APA scheme in India also covers certain domestic transactions (specified domestic transactions) if their aggregate exceeds Rs. 50 million in a financial year,⁴⁷ and they fulfill any of the other conditions laid down in Section 92BA. The APA is valid for a period not exceeding five consecutive previous years.⁴⁸

The APA is binding on both the taxpayer and the commissioner and the income tax authorities, unless there is a change in the law or facts having bearing on the agreement so entered.⁴⁹ The taxpayer

⁴⁴ Income Tax Rules, Rule 10H(1), (2).

⁴⁵ Income Tax Rules, Rule 10H(6)(a).

⁴⁶ I.T.A.T. F.A.Q.s at 8.

⁴⁷ Income Tax Act, § 92BA.

⁴⁸ Income Tax Rules, Rule 10M.

⁴⁹ Income Tax Rules, Rules 10M and 10Q.

may withdraw from the arrangement at any time before the terms of the APA are finalized.⁵⁰ However, the fee paid during the negotiations shall not be refunded.⁵¹ The assessee has to furnish an annual compliance report to the specified Director General for each year during the continuance of the APA.⁵² An APA can be cancelled on account of non compliance by the assessee with the terms of the agreement; or failure to file the annual compliance report in time; or if it contains material errors; or on a finding of fraud or misrepresentation of facts by the assessee.⁵³ A penalty is attracted under the Indian APA scheme at the rate of 2% of the value of international transaction, on the failure of the taxpayer to maintain prescribed documents or information or report any international transaction which is required to be reported. Such penalty shall also be imposed in case the assessee maintains or furnishes any incorrect information or documents.⁵⁴

APA in Other Countries: A Comparative View

The United States of America

The United States of America was the first country to adopt substantial penalties for transfer pricing and to bring in the requirement for companies to maintain detailed documentation of their transfer pricing system.⁵⁵ The IRS-US arrangement has been followed by many countries as a model for implementing the arm's length standards of transfer pricing in their regime by mandating for similar documents followed by penalty for non compliance.

Section 482 of the Internal Revenue Code and related regulations govern transfer pricing. Inter company transactions include those between US taxpayers and their controlled foreign corporations and between entities abroad and their foreign controlled

⁵⁰ Income Tax Rules, Rule 10J(1).

⁵¹ Income Tax Rules, Rule 10J(3).

⁵² Income Tax Rules, Rule 10O.

⁵³ Income Tax Rules, Rule 10R.

⁵⁴ I.T.A.T. F.A.Q.s at 19.

⁵⁵ Wagdy M. Abdallah, *Critical Concerns in Transfer Pricing and Practice* 201 (Greenwood Publishing Group, 2004).

corporations in the United States.⁵⁶ The Indian APA also governs similar transaction in respect of Indian companies. Further, the USA APA shares commonality with its Indian counterpart on a number of aspects, such as:

- i. APAs in the USA cover a period of 3-5 years, subject to renewal if the taxpayer and IRS agree upon that.⁵⁷
- ii. IRS also reserves the power to revoke or cancel an APA in certain cases, such as those involving fraud, misrepresentation etc.⁵⁸
- iii. User fee⁵⁹ for an APA request is \$50,000, but a small taxpayer APA is available for a lower user fee of \$22,500. The user fee to amend an APA request or to amend a completed APA is \$10,000. The user fee for an APA renewal request is \$35,000.
- iv. The IRS also follows the 'Best Method Rule' for determination of arm's length price, which is to be proposed by the assessee.⁶⁰

Further, the information related to an APA, is kept confidential.⁶¹ However, the secretary is to prepare an annual report, including some particular information regarding all APAs, without naming the taxpayers or disclosing their business related information.⁶² The Indian APA law, however, is uncertain on the point of confidentiality.

⁵⁶ United States General Accounting Office, *Report to the Senate on IRS's Advance Pricing Agreement Program* (2000), GAO/GGD-00-168, at 3.

⁵⁷ Internal Revenue Code, Section 4.07, § 482.

⁵⁸ Internal Revenue Code, Section 11.06, § 482.

⁵⁹ Internal Revenue Code, Section 12, § 482.

⁶⁰ Internal Revenue Code, Section § 1.482-1(c).

⁶¹ Internal Revenue Code, Section 13.01, § 482; *See*, 26 U.S. Code, §§ 6103, 6105, 894, and 7852(d).

⁶² Internal Revenue Code, Section 13.03, § 482; *See* § 521(b), Ticket to Work and Work Incentives Improvement Act, 1999, Pub. L. 106-170, 113 Stat. 1860, 1925.

One feature worth adopting from the USA system is the Compliance Assurance Process (CAP). CAP is structured to help conduct real time compliance reviews to determine the correct tax treatment of the tax return positions before a taxpayer files the tax returns. By creating a precedent, CAP not only helps maintain uniformity but also makes compliance easier and predictable.

China

China began using APAs on a trial basis in the late 1990s. In 1998, an APA was included as one of 'other reasonable methods of transfer pricing adjustments' in Article 28 of 'The Regulation on the Taxation of Transactions between Related Parties'.⁶³ In 2002, the APA program was formally introduced in Article 53 of 'The Implementation Rules of the Tax Collection and Administration Law of the People's Republic of China'⁶⁴, and APAs were elevated from an adjustment method to a program."⁶⁵ Bilateral APAs were introduced in China in 1998 by irregular circulars issued by the State Administration of Taxation (SAT), which were replaced with a much more detailed set of rules. The APA concept was first introduced in formal transfer pricing regulations.⁶⁶ The rules pertaining to APA have been revised in 2009 and are now contained in the Implementation Measures of Special Tax Adjustment.⁶⁷ China introduced multilateral APAs in 2004, in view of the fact that some companies may be part of a global group, and their APA with the Chinese authority may not be enforceable before the revenue authorities of the other countries.

A company situated outside China is associated to a Chinese company, if it has a direct or indirect ownership or control of a part or all of either the capital, business operations, supply of assets,

⁶³ Guo Shui Fa[1998] No. 59.

⁶⁴ Guo Wu Yuan Ling No. 362.

⁶⁵ State Administration of Taxation People's Republic of China, China Advance Pricing Arrangement: Annual Report 2011. *available at* <http://www.gov.cn/gzdt/att/att/site1/20121226/782bcb888c4d1244fca001.pdf>. (last visited Mar. 01, 2014).

⁶⁶ *Supra* note 633.

⁶⁷ Zhang, *supra* note 20 at 3.

purchase of products, or marketing of the Chinese company; or a share of the ownership or control, directly or indirectly, in common with the third party, of the Chinese company; or any other factor which leads to a mutually beneficial outcome.⁶⁸ Association on the basis of ownership, control, supply, marketing etc. is recognised by the Indian law also. Some other features of the Chinese APA law, which are similar to the Indian law are that the term of an APA may range from three years to five years starting from the year in which the formal application was filed, a minimum cap of RMB 40 million worth of annual related party transaction is required for entering into an APA, an option where the negotiating taxpayer can remain anonymous during the pre filing stage etc. SAT, like, India's 'most appropriate method' recognizes the 'relevant method' of pricing.⁶⁹ The documentation requirements⁷⁰ are also similar to the laws in India.

The Chinese law differs from the Indian legal framework in as much as the SAP does not charge any user fee for filing an APA request.⁷¹ Also, the APA could even be made retrospective, on the taxpayer's demand for the same.⁷² In India, such roll back provisions are not recognized. Further, incorrect/incomplete documentation is penalized⁷³, whereas in India such APA is only rejected.⁷⁴

One feature that India can borrow from China is their annual APA reports. Since 2009, SAT has been releasing annual reports containing rules, regulations, statistics, analysis, implementation procedure etc. This is a measure that is worthy of emulation as it

⁶⁸ Aaln Pasiy & Jian Li, *Transfer Pricing* 75(Brown Walker Press, 2012).

⁶⁹ *Transfer Pricing and Customs Valuation: Two Worlds to Tax as One* 221 (Anuschka Bakker & Belema Obuoforibo et. al. eds., IBFD, 2009).

⁷⁰ Articles 16-20 of Guoshuifa 2.

⁷¹ See, Guoshuifa 2.

⁷² *Id.*

⁷³ Guoshuifa 2 art. 106; Circular 114 (Guo Shui Fa [2009] No. 114), Implementation Measures for Special Tax Adjustments available at <http://www.eastwestassoc.com/docs/ChinaTransferPricingRegulations.pdf> (last visited Sept. 3, 2013).

⁷⁴ Income Tax Rules, Rule 10K(4).

not only creates certainty, but makes the APA process more transparent.

Australia

In the early 1990s, the Australian Taxation Office (ATO) responded to the inherent difficulties of determining an arm's length price, with the resulting legislative uncertainty, by adopting the mechanism of APA.⁷⁵ In 1995, the ATO formalized the procedures for obtaining a bilateral or unilateral arrangement by issuing Taxation Ruling TR 95/23.⁷⁶ In 2011 the ATO revised the policies and APA programmes and released the Practice Statement Law Administration 2011/1. A new and simpler APA was introduced for companies with a turnover of less than AU\$250m. This policy can be emulated by India which currently has the same threshold for all tax payers.

Like India, the ATO permits unilateral, bilateral and multilateral APAs.⁷⁷ It may run for three to five years, or more, in exceptional cases.⁷⁸ Once the APA comes into effect and the taxpayer has agreed to and complies with its terms, the ATO is administratively bound by the terms of the APA.⁷⁹ If the requirements prescribed by the APA are complied with and those assumptions are met, the Commissioner of Taxation is prevented from imposing any additional income tax on the covered international related party dealings than what is payable on the pricing worked out under the APA.⁸⁰ The ATO also allows for the 'most appropriate method' to

⁷⁵ The law governing Transfer Pricing is the Division 13 of Part III of Income Tax Assessment Act.

⁷⁶ Dr. Kerrie Sadiq, *The Taxing Effects of the Advance Pricing Arrangement Program: A Review of APAs and their Impact on Stakeholders*, JOURNAL OF AUSTRALIAN TAXATION, 104-132, 105.

⁷⁷ Australian Taxation Office, *ATO's Advance Pricing Arrangement Program*, PS/LA 2011/1, ¶¶ 10-12. available at <http://law.ato.gov.au/atolaw/view.htm?docid=psr/ps20111/nat/ato/00001>. (last visited Mar. 01, 2014).

⁷⁸ *Id.*, ¶128.

⁷⁹ *Id.*, ¶13.

⁸⁰ *Id.*

be used in an international transaction.⁸¹ All of this evidences that the Australian APA law is substantially similar to the Indian APA regime.

The ATO approach to the rollback of transfer pricing methodology to prior years of income or examination of prior years will depend on the circumstances of the taxpayer.⁸² The Australian law prescribes penalty rates where an APA is determined to avoid tax, with a penalty as high as 50% where 'the sole or dominant purpose' is tax avoidance.⁸³ Hence, the intention of the tax payer is taken into consideration and adequate exceptions are provided in cases of 'A Reasonably Arguable Position' (RAP).⁸⁴ Voluntary disclosures are rewarded and they result in the penalty being reduced.⁸⁵ This provision is lacking in the Indian legal framework.

Merits and Demerits of APA in India

The advantages of the APA regime in India are increased certainty and predictability, avoidance of controversy and penalty, avoidance of double taxation problem, enhanced party autonomy and reduction in record keeping costs. APA, specifically a bilateral one, is a *prima facie* guarantee against double taxation in an international dealing. It "provides a possible solution to situations where there is no realistic alternative way of both avoiding double

⁸¹ Australian Taxation Office, *ATO's Advance Pricing Arrangement Program*, PS/ LA 2011/1, ¶¶ Appendix 1. available at <http://law.ato.gov.au/atolaw/view.htm?docid=psr/ps20111/nat/ato/00001>. (last visited Mar. 01, 2014).

⁸² *Id.*, ¶179.

⁸³ *Id.*, ¶200.

⁸⁴ The taxpayer may have a RAP "if it would be concluded in the circumstances, having regard to relevant authorities, that what is argued for is about as likely to be correct as incorrect or is more likely to be correct than incorrect."; See, *supra* note 80.

⁸⁵ IRS Official Website, *Offshore Voluntary Disclosure Program Frequently Asked Questions*, 26 June, 2012. available at <http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers> (last visited Mar. 01, 2014).

taxation and ensuring that all profits are correctly determined and taxed at the appropriate time.”⁸⁶ Further, following the models of many countries, the APA provisions have retained the ‘most appropriate method’ of transfer pricing, thereby choosing a method which is transaction specific.

The APA arrangement also informs the taxpayer in advance as to the important records that are required to be kept to ascertain pricing or profits, relating to the international related party transactions covered under the APA, and hence reduces the unnecessary documentation. Additionally, the inclusion of experts from areas such as economics, statistics, law and others in the APA team helps bringing in a fresh perspective to the otherwise bureaucratic set up.

The APA will also prove to be beneficial for startup enterprises. The APA has been devised to evade actual or potential transfer pricing disputes in a designed and coordinated fashion, as opposed to the traditional adversarial process. Though, it cannot be said with actual conviction that APAs would either increase or reduce companies’ real time tax figures. It can be assumed that an APA will help in arriving at the same results a company would have achieved, after spending on potential litigation and costly audits, without the uncertainty and transaction costs. It enhances the predictability of the tax related aspects in a multinational related party transaction.

The APA in India comes with a catena of loopholes as well. Since APA will provide for a negotiated amount of tax to be paid by the taxpayer, the revenue loss will be huge. For instance, in the USA, the Senate investigators confirmed that the tax returns reveal that huge financial intermediaries are the beneficiaries of APAs covering transactions worth billions of dollars thereby causing a big financial loss.⁸⁷ Further, under a typical APA, the revenue authority would agree on not challenging the calculation of figures

⁸⁶ Sadiq, *supra* note 76 at 120.

⁸⁷ Lee A. Sheppard, *Draft Senate Finance APA Report Shows Incompetent IRS*, July 22, 2013, Tax Analyst. available at <http://www.taxanalysts.com/www/features.nsf/articles/ce8bee193fce2f8385257bb00065d111?opendocument>. (last visited Mar. 01, 2014)

relating to the structured transactions between a company and its foreign subsidiaries. This transaction is ideally to be done at an arm's length price. However, there being many methods of calculation, one method may yield a different arm's length price than the other. Since there is ample room for deviation during negotiations, the revenue department is vested with an arbitrary power to grant modification and vary the procedures at its discretion, giving rise to arbitrariness. Therefore, there is a possibility of the calculations becoming the single biggest factor in lowering a company's tax bill and boosting their after tax profits. The legal provisions also do not provide an opportunity to the tax payer to prefer an appeal. Probably, the only remedy is to file a writ with the High Court or the Supreme Court. While this might be seen as a solution to reduce frivolous appeals and unnecessary litigation, this could also have been converted into an opportunity to provide for a right to appeal before the Income Tax Appellate Tribunal.

In countries such as the United Kingdom, a specific time frame has been prescribed to conclude the APA deal. The Indian legal framework lacks any such time frame. This is coupled with the fact that analysing the critical details of the APA is time consuming due to which an APA in India is going to be a very long and tedious process. Since, APA is a new entrant into the Indian scenario it is very difficult to predict the quantum of time that may be required on an average for an APA to complete in the present context. Although, an APA is traditionally a time consuming process, but fixing a time limits, howsoever conservative, would have increased the predictability of the system and would have attracted more investors into the country. Further, the Indian rules lack any 'firewall provisions' to compile and safeguard the confidential data. Unlike other jurisdictions, which provide for confidentiality to the information provided by the taxpayer regardless of the outcome of the negotiation, the Indian law is silent on this aspect. Hence at this stage it cannot be confirmed that the information shared by the taxpayer would remain only with the revenue authorities.

Moreover, the present legal regime pertaining to APA makes no distinction between large multinational enterprises and small

companies and firms. It establishes the same thresholds irrespective of the value and scale of the transaction. This discourages those operating on a smaller scale to approach an APA as the cost of the process itself might be much more than that of the transaction. Special simplified APA procedures for small and medium size enterprises (SME) can address this problem.⁸⁸ A 2011 OECD survey of OECD member and observer countries found that a number of countries have adopted simplified measures for SMEs, small transactions and/or low value added services and that Canada, France, Germany, Netherlands and the United States have simplified APA procedures for SMEs.⁸⁹

Neither the legislative provisions nor the rules provide for a specific penalty in case of the breach of an APA by the taxpayer or in cases where there is a shortfall in the tax amount paid. This is problematic because in the absence of specific statutory provisions, increased reliance shall be on the decisions of the administrative and judicial authorities and this not only causes delays, but also leads to an uncertain position. Further it is uncertain as to whose burden it is to show that transfer pricing has not been arrived as per the APA.

Creating a Better Regime for APAs in India

The authors seek to put forth certain suggestive measures that can be used to ease the APA structure in India for both tax payers and administrative bodies.

Creating Safe Harbours

If framed properly and used cautiously, safe harbours can contribute to making APAs popular and ease the process for both taxpayers and administration. Recently, the OECD Council introduced the Revised Section E on safe harbours in Chapter IV of the OECD Guidelines. The section defines a safe harbour as “[...] a

⁸⁸ See, U.N. Manual, ¶ 9.6.2.13.

⁸⁹ OECD, *Multi-Country Analysis of Existing Transfer Pricing after Simplification Measures*, 10 June, 2011. available at <http://www.oecd.org/tax/transfer-pricing/48131481.pdf>. (last visited: Mar. 01, 2014).

provision that applies to a defined category of taxpayers or transactions and that relieves eligible taxpayers from certain obligations otherwise imposed by country's general transfer pricing rules."⁹⁰ The section also states that safe harbours are more appropriate in a situation where the transaction is of low risk and is preferably bilateral or multilateral. Safe harbours can take two forms, exclusion of certain classes of transactions from transfer pricing regulations; and stipulation of margins or thresholds for prescribed classes of transactions.⁹¹ In the United States, Section 482 of the Internal Revenue Code provides that the Internal Revenue Service may, in reviewing transactions between entities under common control, allocate income in such a manner so as to ensure an appropriate reflection of income between the entities.⁹²

In India, the safe harbour rules have been introduced by amending the Income Tax Rules after the recommendations of the Rangachary Committee.⁹³ Under Section 92CB of the Act, these rules have been introduced by adding Rule 10TA to Rule 10TG. A safe harbour has been defined to mean circumstances in which, the Indian revenue authorities shall accept the transfer pricing declared by the taxpayer.⁹⁴ The IT Rules specify sectors⁹⁵ and transactions⁹⁶ which are eligible for receiving a safe harbour. There are broadly four categories of eligible assessee and these are, those engaged in Information technology (IT)/ IT-enabled services sector, contract research and development and pharma sector, outbound loans and corporate guarantees and automobile original equipment manufacturing sector. These transactions have to meet the specific thresholds pertaining to operating profit margin, interest rates and

⁹⁰ The OECD Guidelines, ¶ 5.28.

⁹¹ OECD, *Draft Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, ¶ 4.96.

⁹² Yitzhak Hadari, "Resolution of International Transfer-Pricing Disputes, 30 Canadian Tax Journal 29 (1998).

⁹³ Committee to Review Taxation of Development Centres and the IT Sector headed by Shri N Rangachary.

⁹⁴ Income Tax Rules, Rule 10TD.

⁹⁵ Income Tax Rules, Rule 10TB.

⁹⁶ Income Tax Rules, Rule 10TC.

commission or fee.⁹⁷ An interesting feature is that all the transactions must qualify to be of 'an insignificant risk'⁹⁸. Such transactions are also no longer considered for mutual agreement procedure settlements.⁹⁹

The obvious advantage of using safe harbours is that they reduce compliance risks, costs, better allocation of resources etc. They reduce the administrative burden by allowing certain transactions to escape elongated audits and reviews. However, Section E points out that these provisions are not entirely safe and carry risks of taxable income being reported that is not consistent with the arm's length principle, and there might be a situation where the safe harbour and arm's length are inherently inconsistent allowing the taxpayer to choose the more favourable one and this might result in a loss of revenue. Further, it may make room for double taxation as an operating profit, for instance, arrived at one country to achieve safe harbour threshold may not be eligible for the same benefit in the other country and the swollen number shall be heavily taxed there.

These disadvantages can be cured by requiring the assessee to use a safe harbour a limited number of times in a year, or asking him to notify much in advance about the use of such harbours. If framed properly and used cautiously, safe harbours can contribute to making APAs popular and ease the process for both taxpayers and administration.

Using a Mutual Agreement Procedure

Mutual Agreement Procedure (MAP) is an additional method for dispute resolution available to the parties in the context of an APA arrangement. MAP is a common feature of Double Tax Avoidance Agreements (DTAA). This method of settlement is voluntary and operates only when both the parties agree to use it. Hence, it is a negotiated settlement. The OECD Model Convention under Article 25 mentions the process to be one where, "the competent authority shall endeavour, ... to arrive at a satisfactory solution, to resolve

⁹⁷ Income Tax Rules, Rule 10TD (2).

⁹⁸ Income Tax Rules, Rule 10TB (3).

⁹⁹ Income Tax Rules, Rule 10TG.

the case by mutual agreement with the competent authority of the other contracting state, with a view to the avoidance of taxation which is not in accordance with the convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the contracting states.”¹⁰⁰ An identical provision exists under Article 25 of the UN Model Convention¹⁰¹, however the MAP process here¹⁰² is much more detailed than the one specified in the OECD Model Convention.

In India, the provision for MAP is made under Rule 44H (4) of the Rules, which provide that; the assessing officer shall, within 90 days of receipt of the resolution by the Chief Commissioner or Director General of Income Tax, give effect to the resolution provided; the taxpayer gives his acceptance to the resolution arrived at under MAP; and withdraws the appeal filed under the domestic litigation provisions.

Providing for a MAP under an APA can solve the problem of a long drawn dispute, and taxpayers can also avoid getting dragged to alien jurisdictions. On the downside, MAPs under DTAAAs can by themselves be lengthy and complicated. An ideal MAP structure must be one that is consistent and one which does not deal with cases in an *ad hoc* manner.¹⁰³ To avoid double taxation it is best if that tax administrators implementing the MAP programme are able to make decisions independently of those implementing the audit programme.¹⁰⁴ When there exists an APA between two parties, in case of using a MAP, refunding the tax shall never arise and be a problem.¹⁰⁵

Providing for Dispute Settlement Methods Other than MAP

MAP, since it is a voluntary process shall fail if one of the parties disagrees to participate. The other methods available are

¹⁰⁰ OECD Model Convention art. 25(2).

¹⁰¹ U.N. Model Convention art. 25(2).

¹⁰² U.N. Model Convention art. 25(4); See U.N. Manual, ¶1.12.

¹⁰³ U.N. Manual, ¶ 9.6.1.

¹⁰⁴ U.N. Manual, ¶ 9.6.1.6.

¹⁰⁵ UN Manual, ¶ 9.6.2.3.

mediation, conciliation and arbitration. No authoritative and convincing statistics is available as of yet on the effectiveness of these measures. At the 2010 Annual Session of the UN Committee of Experts on International Cooperation in Tax Matters¹⁰⁶ most of the participants from the developing countries expressed potential interest in tax treaty arbitration procedures for the future but expressed reluctance to adopt arbitration at the particular point of time. The reasons may include lack of expertise and available resources with the developing nations to conduct and participate in arbitration proceedings. However, in the absence of any specific Indian provision on resolving disputes under an APA, these methods can be explored by the parties.

Making Documentation Easier

At every stage of the APA process, tax payer is required to present a variety of documents for compliance and this involves significant time and cost. The OECD has released a White Paper on Transfer Pricing Documentation¹⁰⁷ highlighting the problems posed by the increasingly complex and bulky documentation requirements of transfer pricing. The objective was to “develop a common template for country-by-country reporting to tax authorities by major multinational enterprises, taking account of concerns regarding non-cooperative jurisdictions” and to “make suggestions as to how transfer pricing documentation rules might be modified to make transfer pricing compliance simpler and more straightforward, while at the same time providing tax authorities with more focused and useful information for consideration in connection with transfer pricing risk assessment and transfer pricing audits.”¹⁰⁸

Chapter V of the OECD Guidelines is not an adequate guide anymore as the companies have in the past fifteen years at least, gone from producing ten documents to ten thousand as a part of

¹⁰⁶ Session held in Geneva from 18 to 22 October, 2010 *available at* <http://www.un.org/esa/ffd/tax/sixthsession/>. (last visited Mar. 11, 2014).

¹⁰⁷ OECD, *White paper on transfer pricing documentation*, 30 July 2013. *available at* <http://www.oecd.org/ctp/transfer-pricing/white-paper-transfer-pricing-documentation.pdf> (last visited Mar. 01, 2014).

¹⁰⁸ White paper, ¶1.

their transfer pricing requirements.¹⁰⁹ Practices also vary significantly from country to country. Some countries focus more on domestic transactions while forming these guidelines, making their documentation skewed. Most international efforts such as those by the European Union¹¹⁰ and the Pacific Association of Tax Administrators¹¹¹ have not resulted in a uniformly accepted model as their methods are largely inflexible and hence not widely used.¹¹²

The White Paper suggests a tiered approach to documentation with one master file containing the details pertaining to the structure of the enterprise, its operations, businesses and one local file containing details about the transaction at hand and whether arm's length principle is being met or not. This is similar to the European Union's Code of Conduct on Transfer Pricing Documentation for Associated Enterprises (EUTPD). A similar model can be emulated in India as well since the APA rules are in a very nascent stage and introducing this relatively easier model will help in making documentation much easier. A possible argument against the model suggested by the OECD is that the local conditions of developing countries are different and hence a different set of 'comparables' need to be maintained by the developing nations in both the tiers. This will not solve the problem of lack of uniformity.

Conclusion

APAs are going to play increasingly important roles due to rapid commercialization which results in the need for increase in revenue. The OECD has gone so far to term it as a 'safety valve' in

¹⁰⁹ See, The OECD Guidelines, ¶ 5.1; McWilliams, R., *GE Counsel Details Transfer Pricing Documentation Challenges*, Tax Management Transfer Pricing report, BNA (April, 2007).

¹¹⁰ (Resolution of the Council and of the representatives of the governments of the member states meeting within the Council on 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union) (2006/C 176/01).

¹¹¹ (The members include Australia, Canada, Japan and the United States).

¹¹² White Paper, ¶ 42.

the transfer pricing regime.¹¹³ The APA provisions in India are a welcome step towards modernizing the Indian tax regime and curbing the rates of tax litigation in the country. India is home to more than seventy percent of the total transfer pricing disputes that occur in the world¹¹⁴ and obviously most of these are pending in litigation circles. Now that the framework is in place, the next step should be to synchronize it with international guidelines and adapt beneficial provisions that exist in other jurisdictions.

¹¹³ OECD, *The Taxation of Global Trading of Financial Instruments* (1998), 29(112).

¹¹⁴ PWC , White Paper on Advance Pricing Agreement, 2011. available at http://www.pwc.in/en_IN/in/assets/pdfs/publications-2011/PwC_India_-_Mutual_Agreement_Procedure_Answering_Queries-130112.pdf (last visited Mar. 01, 2014).