Demystifying TP Compliances for Non-Residents in India

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The clock is ticking, and Indian Transfer Pricing (“TP”) Compliances for the financial year 2022-23 are just around the corner, with due dates in Oct/Nov '23.

Ensuring compliance with Indian transfer pricing regulations isn't just a box to tick; it's a strategic imperative. Non-compliance can result in serious repercussions with tax authorities. While many multinationals are abreast and carefully track the TP compliances of resident entities, there has been confusion or oversight regarding TP compliances applicable to a non-resident entity especially the associated enterprises (“AEs”) of Indian entities.

In this article, we have highlighted the applicability of Indian TP compliances for Non-Residents (“NR”) in India.

A. Applicability of TP provisions to NRs

Section 92(1) of the Income Tax Act, 1961 (“IT Act”) (the primary section for the applicability of TP) provides that income arising from international transactions has to be at arm's length price (“ALP"). Accordingly, Indian TP provisions would apply to NRs only when they enter into international transactions that give rise to taxable income in India.

If an NR has taxable income in India as per the provisions of the ITA from its AEs in the nature of services income, royalty/license fees, interest, sale/transfer of shares (capital gains), guarantee commission, etc., the NR has to comply with TP regulations in India.

ALP analysis from the standpoint of Indian resident AEs alone is not sufficient, as the TP regulations require even the NR AEs to substantiate the ALP for taxable international transactions.

B. TP compliances applicable to NRs in India

The following are the applicable TP compliances from an NR's standpoint, along with penalties for non-compliance:

TP Compliances for NR	Threshold for applicability	Due date	Penalty for non-compliance
Accountant's Report **(Form No. 3CEB)**	If International Transactions (irrespective of threshold) are undertaken with foreign Associated Enterprises (AEs) *[Sec 92E (Form No. 3CEB) is applicable for all taxpayers including NR]*	31st October	INR 1,00,000 *[Sec 271BA is applicable to all taxpayers including NR]*
Transfer Pricing Study Report	If aggregate value of International Transactions > INR 1 Crore *[Sec 92D & Rule 10D (TP Study) is applicable to NR having international transactions that gives rise to taxable income in India]*	31st October	2% of value of international transactions *[Sec 271AA(1) is applicable to all taxpayers including NR]*
Master File (Form No. 3CEAA)	**Part A** is applicable if International Transactions are undertaken during the financial year (Part A is applicable to all MNEs irrespective of threshold) **Part B** is applicable if below twin conditions are satisfied: • Consolidated Group Revenue exceeds INR 500 Crores and • Aggregate value of all International Transactions exceeds INR 50 crores or the Intangible Property related International Transactions exceeds INR 10 Crores *[Sec 92D & Rule 10D (Form No. 3CEAA) is applicable for all taxpayers including NR*	30th November	INR 5,00,000 *[Sec 271AA(2) is applicable to all taxpayers including NR]*

C. Stand that could be adopted for NR TP compliances:

There have been a number of rulings from tribunals, high courts, and the Authority for Advance Ruling (AAR) regarding the applicability of TP regulations, flipside compliances, penalties, and ALP adjustments

in the case of NRs. Based on the precedents and the relevant Tax and TP provisions, the following is the stance that could be adopted for NR TP compliances in India:

Filing of Form No. 3CEB, maintenance of TP Study Report and Corporate Tax Return by NR

Income earned by NR	**Form 3CEB & TP Report compliance requirement**	**Corporate Tax Return Requirement ("ROI")**
Taxable as per Income Tax Act & DTAA	To be reported in Form 3CEB & TP Study Report to be maintained (if value > INR 1 Crore)	Applicable unless TDS is deducted at rates given in Section 115A and there is no other income chargeable apart from incomes specified in Section 115A.
Taxable as per Income Tax Act but exempt as per DTAA	To be reported in Form 3CEB & TP Study Report to be maintained (if value > INR 1 Crore)	Applicable where DTAA benefit is opted by NR.
Not taxable as per Income Tax Act	Not to be reported *(Can be disclosed in Form No. 3CEB out of abundant caution if there are any other taxable international transactions)*	Not applicable
Other transactions of NR not impacting the taxable income	Not to be reported *(Can be disclosed in Form No. 3CEB out of abundant caution if there are any other taxable international transactions)*	Not applicable

D. TP compliances applicable even in case of ITR exemption

Section 115A provides an exemption to NRs from filing a Return of Income (ROI) when their total income consists of interest, dividends, FTS (Fees for Technical Services), and royalties, provided that tax has been deducted as per the rates provided therein. Further, to claim such exemption, there should not be any other income arising to NR that is assessable under the IT Act.

However, there is no corresponding exemption in Sections 92E and 92D, and it would be advisable for NRs to comply with TP regulations to avoid harsh penalties under Sections 271BA and 271AA of the IT Act.

E. Filing of Master File (Form No. 3CEAA) by NR

The Central Board of Direct Taxes ("CBDT"), vide Notification No. 31/2021 dated April 5, 2021, amended Rule 10DA(4). As a result, if there are more than one resident as well as non-resident constituent entities, Form No. 3CEAA can be filed by any one designated constituent entity on behalf of all constituent entities. Accordingly, this redundant compliance burden on NRs is eased by the government.

F. Mitigating the risk of potential litigation

Under the Indian domestic TP litigation mechanism, the Assessing Officer ("AO") has to refer the scrutiny of international/specified domestic transactions to a designated Transfer Pricing Officer ("TPO"). The CBDT has issued Instruction No. 03/2016 to the revenue authorities with guidance on the risk parameters to be considered in order to make a reference to the TPOs. According to the guidance:

- Cases to be selected for scrutiny should be based on "TP risk parameters" either under the

Computer Aided Scrutiny Selection (CASS) or under the Compulsory Manual Selection Process. CBDT's instruction in this regard does not specify what exactly the TP risk parameters are, but they may be available to the revenue authorities internally.
- Cases selected for corporate tax scrutiny can also be chosen for TP scrutiny based on the following Non-TP risk parameters:

- Non-filing of Form No. 3CEB or non-reporting of transactions in Form No. 3CEB.
- TP adjustments of INR 10 Cr or more in earlier years, where such adjustments are upheld by judicial authorities or are pending in an appeal.
- Search, seizure, or survey operations have findings relating to TP matters in India.

Accordingly, considering that there are TP and Non-TP risk parameters that could trigger potential scrutiny and penalties for non-filing of Form No. 3CEB in India, it is imperative for NRs to evaluate the applicability of TP compliances and ensure compliance in India.

G. Emphasis on Two-Sided Transfer Pricing Analysis

To satisfy the Arm's Length Pricing ("ALP") test by both the parties involved in the transaction, a two-sided holistic TP analysis is required to ensure that both the Indian AE and NR AE are meeting the ALP test. This analysis ensures that the transfer price is set within the arm's length range that is acceptable for both the jurisdictions/parties involved. Although complex and time-consuming, this process is crucial to avoid double taxation or tax disputes. In a landmark ruling of Instrumentarium Corporation Limited [I.T.A. Nos. 1548 and 1549/Kol/2009], the Kolkata Tribunal held that a two-sided TP analysis is required to determine the arm's length price in both the jurisdictions involved in the transaction. The case emphasized that the transfer price must be set within the arm's length range to avoid double taxation or tax disputes.

H. Check points for NR TP compliances

- Where it is concluded that TP compliances are applicable, the primary requirement would be to obtaining a Permanent Account Number (PAN) in India as all the filings are electronic. Obtaining PAN for NRs (i.e., by applying in Form 49AA) is a time taking procedure where documents of NR like certificate of incorporation etc., are required to be apostilled or attested by Indian consulate/embassy in the foreign country. Thus, the same should be triggered at the earliest to comply with the impending due dates.

- Additionally, it would be advisable to authorize any person holding Digital Signature (DSC) in India by initiating a Power of Attorney (PoA) as TP filings in electronic forms would also require digital signing. Obtaining of DSC by NR individuals (acting as signatories for NR outside India) may also be opted depending upon the convenience.

- Since NR may not statutorily required to maintain books of accounts in India under any law, reliance should be placed on Form No. 26AS, invoices, agreements etc. Reliance can also be placed on documents, information and accounts maintained by the Indian AE with whom the NR AE has entered into international transaction.

- Transfer Price should fall within the arm's length range to the meet the arm's length requirements from both Indian AE and NR AE (flipside) standpoints.

- Value of international transactions reported in Form No. 3CEB should match with the Form No. 26AS and the Income Tax Return to avoid any scrutiny notices due to mismatches.

- Report all taxable international transactions and also other international transactions (wherever required) out of abundant caution to avoid penalties for failure to report qualifying international transactions.

I. Judicial Rulings in the context of NR TP Compliances:

Case law reference	Important observations

Filing of Form No.3CEB by Non-residents	
Venenburg Group B.V. [TS-10-AAR-2007]	**Case Summary:** The Authority for Advance Ruling (AAR) held that the applicant was ***not taxable*** in respect of capital gains on sale of shares held in its Indian subsidiary ***under the provisions of India Netherland Tax treaty*****.** AAR held that since the provisions of the tax treaty were more beneficial to the assessee than provisions of the Act, the same were applicable to the assessee. **Conclusion:** The AAR further held that it was ***not necessary for the applicant to file tax return*** in India in the absence of tax liability in India and ***transfer pricing provisions under section 92 to 92F were not attracted*** in respect of the aforesaid transactions.
Praxair Pacific Ltd. [TS-5020-AAR-2010-O]	**Case Summary:** The assessee, a tax resident of Mauritius, proposed to transfer its holding in Indian company to its wholly owned Indian subsidiary. The AAR held that the transaction could not be regarded as 'transfer' in view of provision of section 47(iv). Further, the AAR also held that the transaction was***not subject to capital gain tax in view of provisions of India Mauritius tax treaty***. The AAR further held that provisions of section 115JB (MAT provisions) were not applicable to foreign company. **Conclusion:** The AAR also held that ***transfer pricing provisions were not applicable*** as income was not taxable in India.
Dow Agro Sciences Agricultural Products Ltd. [TS-5000-AAR-2016-O]	**Case Summary:** The applicant, a company, incorporated and registered in Mauritius, contends that its investment in Dow Agrosciences India (DAS India) is a capital asset. The Revenue argues about the existence of a Permanent Establishment (PE) in India, but the applicant has provided documents supporting no PE. The applicant reiterates that ***profits from the sale of equity shares of DAS India won't be taxable in India due to the DTAA*** between India and Mauritius. **Conclusion:** ***Transfer pricing provisions (Sections 92 to 95) are not***

	applicable if the transaction is not taxable in India. Since the proposed share transfer does not attract tax in India under the tax treaty's Article 13, these provisions do not apply.
Goodyear Tire and Rubber Co. [TS-178-AAR-2011]	**Case Summary:** In the facts of the given case, Goodyear Tire and Rubber Company USA, proposed to transfer its 74% shareholding in Goodyear India Limited (listed on BSE) to its Singapore based subsidiary as ' Gift' and at NIL value . Goodyear USA argued that since the ***full value of consideration received or accruing as a result of the transfer of shares was NIL, the mechanism to charge the capital gains to tax fails.*** The AAR upheld Goodyear's contention and ruled that 'It is settled law that Section 45 must be read with Section 48 and if the computation provision cannot be given effect to for any reason, the charge under Section 45 fails. **Conclusion:** The AAR further held that ***transfer pricing provisions under section 92 to 92F were not applicable to the facts of the case as the transaction was not taxable under Indian tax laws.***
Vodafone India Services Pvt. Ltd. v. Union of India [TS-5904-HC-2014(Bombay)-O]	The Bombay High Court concluded that if ***'income' is chargeable to tax under the normal provisions Of the Act, then alone Chapter X/transfer pricing provisions of the Act could be invoked*.** The Government of India vide Instruction No. 2/ 2015 dated 29.1.2015 has accepted the decision of the Bombay High Court in the case Of Vodafone Services Pvt. Ltd. According to the said instruction, the premium arising on issue of shares is a capital account transaction and does not give rise to income and hence not liable to transfer pricing adjustment.
Castleton Investment Limited.[TS-607-AAR-2012-TP]	**Case Summary:** The AAR held that transfer pricing provisions (Sections 92 to 92F) are applicable even if the income, such as capital gains, is exempt from taxation. In the case of Castleton Investment Limited, a Mauritius-based company, which held shares in an Indian listed company, the AAR determined that the provisions are considered machinery provisions. As such, capital gains cannot be determined without applying these sections. Whether the gain is ultimately taxable in India or not, the transfer pricing provisions would still apply if the transaction falls within their ambit. **Conclusion:** The ***applicability of Section 92 does not depend on***

	chargeability under the Act. Thus, the AAR ruled that transfer pricing provisions would be applicable in this case of transferring investment to an associated enterprise in Singapore.
Armstrong World Industries Mauritius Multiconsult Ltd. [TS-628-AAR-2012]	**Case Summary:** Armstrong World Industries Mauritius Multiconsult Ltd., a fully-owned subsidiary of Armstrong World Industries Ltd., UK (Armstrong UK) and a tax resident of Mauritius, intends to repurchase a portion of its shares from the applicant (holding 99.97% of shares) while the remaining shares (0.03%) are held by Armstrong UK. ***This proposed buyback is not liable to capital gains tax in India by virtue of the India-Mauritius*** **Conclusion:** Thus, the AAR held that ***transfer pricing provisions would be applicable*** in the said case, taxpayer would be liable to comply with the Transfer Pricing provisions irrespective of whether the taxpayer earns any taxable income in India or not.
BNT Global Pvt. Ltd. v. ITO [TS-319-ITAT-2017(Mum)-TP]	**Case Summary:** The taxpayer has not filed the audit report in Form 3CEB for its international transaction involving the receipt of foreign remittance from its Non-Resident Indian (NRI) Director, who was also a beneficial shareholder, in exchange for share capital and share premium within the company. **Conclusion:** The ***ITAT upheld the penalty under Section 271BA for the failure as the share issuance transaction fell within the ambit of Section 92E***, requiring the filing of Form No. 3CEB. The reliance on the Vodafone India Services Pvt. Ltd. case was rejected, as it dealt with different facts and penalties.
Convergys Customer Management Group Inc. [TS-690-ITAT-2020(DEL)-TP]	**Case Summary:** Taxpayer only submitted Form 3CEB during the scrutiny and has not filed TP Study. Further, taxpayer did not disclose certain international transactions (of reimbursements, interest payments, FTS) on the premise that they are not subject to tax in India in accordance with the Treaty provisions. A categorical finding was given by the ITAT that every person has to maintain its own documents which taxpayer failed to and instead relied on its Indian subsidiary's TP study. **Conclusion:**

	The ***ITAT upheld that Form 3CEB submission is not equivalent to TP-documentation compliance u/s 92D*** while dismissing the Miscellaneous Application upholding levy of penalty u/s 271AA for non-maintenance of documents u/s 92D.
"Without prejudice" explained	
Commissioner of Wealth-tax v. Apar Ltd. [TS-5255-HC-2002(Bombay)-O]	The term "without prejudice" was used to indicate to the Assessing Officer that filing a return and paying taxes should not impact the rights of the taxpayer. The taxpayer reserves the option to claim settlement as if the return was not filed under the Act. ***By filing the return "without prejudice," the taxpayer denies liability to be assessed under the Act and implies the possibility of future rectification in accordance with the law.*** However, when any compliance is undertaken "without prejudice," it must be clearly disclosed, along with relevant facts and justifications, in the documentation maintained by the non-resident and in Form No. 3CEB issued by the accountant.
On maintenance of separate transfer pricing documentation by non-residents	
DCIT v. Convergys Customer Management Group Inc. [TS-543-ITAT-2020(DEL)-TP]	**Case Summary:** The ITAT imposed a penalty on Convergys Customer Management Group Inc., a US-based non-resident company, for ***not maintaining TP documents*** under Section 271AA of the Income Tax Act. The case involved its ***Indian subsidiary, Convergys India Services Pvt. Ltd., providing call center/back office support services.*** The Assessing Officer found a fixed place PE and Service PE in India with attributable profits, resulting in disallowances and penalties for not maintaining TP documents. **Conclusion:** In conclusion, the ***ITAT upheld the penalty imposed under Section 271AA*** of the Income Tax Act, stating that the CIT(A) was wrong in deleting the penalty.
On TP adjustment in hands of NR	
Instrumentation Corporation Ltd., Finland v. ADIT [I.T.A. Nos. 1548 and 1549/Kol/2009]	**Case Summary:** Instrumentarium Corporation, a Finnish company (F Co.), provided an interest-free loan to its Indian subsidiary, Datex Ohmeda India Pvt. Ltd. (I Co.). The case revolved around whether the loan was at arm's length and ***whether it eroded India's tax base***. **Conclusion:** The Assessing Officer argued that the transaction was not at

	arm's length, resulting in an adjustment to the interest income of F Co. The company contended that applying transfer pricing provisions in this situation would lead to a reduction in the Indian tax base and increased losses for I Co., which could be carried forward and set off in subsequent years. The Income Tax Appellate Tribunal (ITAT) held that Section 92(3) of the Income Tax Act required assessing the impact on profits or losses for the year under consideration and for the taxpayer in question, rather than considering the impact on taxes in subsequent years. Thus, if the transaction was accepted without an arm's length pricing adjustment, ***it would result in tax base erosion to the extent of the taxability of interest in the hands of F Co.*** The ITAT also ***rejected*** the argument that a ***corresponding deduction*** should be given to I Co.

J. Conclusion

To successfully navigate the complex TP landscape in India, here's what both residents and NRs should do:

- **Ensure Compliance:** It's crucial for multinationals to diligently ensure compliance in India with applicable transfer pricing regulations for both resident and non-resident entities in India (i.e., filing all the relevant forms in India related to three-tiered documentation). Non-compliance could be viewed negatively by tax authorities.
- **360-Degree Analysis:** It's pertinent to ensure that the information disclosed in Form No. 3CEB, the local file, master file, and country-by-country report provides a comprehensive view and supports the transfer pricing and other tax positions of the multinational group. Applicability and filing of corporate tax returns should also be perused diligently.
- **Robust Documentation:** Remember, it's not limited to filings alone. TP and tax filings should be backed up by the maintenance of robust supporting documentation to substantiate the TP positions and analysis in case of future audits/scrutiny by tax authorities.

In a nutshell, robust transfer pricing documentation and adherence to guidelines should be your top priority if you're a multinational operating in India.

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