

## Options Realistically Available in Arm's Length Analysis: An Indian Perspective

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### Introduction: The Untapped Core of Arm's Length Behaviour

In transfer pricing, the idea of Options Realistically Available (ORA) is one of the most important yet least discussed aspects of the arm's length principle. The OECD Transfer Pricing Guidelines (2022) describe it in paragraph 1.38, noting that independent enterprises ***"will only enter into a transaction if they see no alternative that offers a clearly more attractive opportunity."*** In simple terms, before entering into any deal, unrelated parties weigh their options and choose the one that makes the most business sense.

The ORA test asks a practical and powerful question: given all the choices available, was the transaction between related parties the most reasonable one an independent business would have chosen? ORA does not replace the arm's length price; rather, it strengthens it. It connects pricing to real business decision-making, helping us understand not only *how much* a transaction should be priced, but also *why* it makes sense commercially. In this way, ORA turns transfer pricing from a mere numerical comparison into a test of sound business judgment and economic logic.

For India, this idea can be both timely and valuable. Over the past two decades, Indian transfer pricing practice has grown in depth and sophistication, keeping pace with global standards. As India increasingly focuses on aligning profits with value creation, the ORA framework offers an additional perspective—it allows us to see transactions not only through numbers and margins but also through the lens of business reasoning and realistic alternatives. This makes transfer pricing analysis more complete and forward-looking.

This article explores how the ORA concept fits within the Indian transfer pricing landscape. It explains its meaning and origin, how it operates in practice under the OECD framework, and how it can be applied to real cases in India. It also highlights situations where considering ORA could improve both taxpayer analysis and administrative decision-making, bringing greater economic clarity and balance to the arm's length principle.

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### Evolution and Theoretical Foundation of ORA in OECD Thought

The ORA doctrine is not an isolated innovation but rather the culmination of the OECD's long-standing endeavor to align transfer pricing outcomes with **value creation and commercial reality**. Since the early League of Nations reports in the 1930s, transfer pricing discourse has oscillated between two poles — legal form and economic substance. The BEPS Actions 8-10 reforms marked a decisive turn toward the latter by embedding

economic rationality as the touchstone for delineating controlled transactions.

Paragraphs 1.38 to 1.40 of the OECD Guidelines articulate the essence of ORA: before accepting the terms of a transaction, independent enterprises assess all realistic alternatives open to them. They proceed only if the transaction, as structured, does not make them worse off than the next-best available option. The same principle reappears in paragraph 1.122, which authorizes tax administrations to disregard or recharacterize a transaction if, viewed in its totality, it diverges from what commercially rational parties would have undertaken. For intangibles, the OECD Guidelines requires consideration of both parties' realistically available options when determining whether a license, sale, or cost-sharing arrangement reflects arm's length behaviour. Similarly, the 2020 OECD Guidance on Financial Transactions extends the principle to group financing, emphasizing that both borrower and lender should evaluate alternative financing options and opportunity costs before agreeing on intra-group terms.

Through these provisions, the OECD embeds ORA not as a mere adjunct to pricing, but as a **conceptual precondition** for establishing that the transaction itself is arm's length. It recognizes that no amount of comparability analysis can salvage a transaction that independent enterprises, facing real market constraints, would never have undertaken in the first place. This insight shifts the analytical focus from "What is the right price?" to "Was the decision itself rational?"—a shift that resonates deeply with the logic of managerial economics and corporate finance.

The term 'realistically available' embodies two distinct dimensions. First, **legal availability** requires that an option must not violate applicable laws, regulations, or binding contractual obligations. For instance, regulatory restrictions in banking or pharmaceuticals may render certain restructuring alternatives legally unavailable. Second, **practical realism** demands that alternatives align with the entity's current functional capabilities, asset base, and strategic positioning. An option requiring an Indian textile manufacturer to pivot into aerospace manufacturing, while legally permissible, fails the realism test. Similarly, contractual constraints—such as non-compete clauses or exclusivity arrangements—can render otherwise attractive third-party alternatives unavailable during the restriction period. The 'realistic' qualifier thus serves as a necessary boundary condition, preventing the list of alternatives from expanding infinitely into theoretical possibilities disconnected from commercial reality.

The ORA test requires not merely that an alternative be marginally superior, but that it be **'clearly more attractive'** than the controlled transaction.

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## The Indian Context: Strengthening the Arm's Length Story

In India, transfer pricing has developed into a highly structured and methodical system over the past two decades. The rules under Section 92C of the Income-tax Act, 1961, along with Rules 10B and 10C, provide detailed guidance on how to determine the arm's length price for international transactions. This framework has given Indian taxpayers and authorities a clear process for benchmarking prices and margins, ensuring consistency and predictability.

As transfer pricing practice continues to evolve, there is growing interest in understanding not only the *price* of a transaction but also the *business reasoning* behind it. The concept of ORA offers a way to enrich this analysis. By exploring whether the terms of a transaction make sound business sense when compared with the realistic alternatives available to the

parties, ORA helps bring commercial understanding into the pricing discussion. This perspective complements the existing focus on comparables and margins, making the overall assessment more complete.

Courts in India have often emphasized that tax authorities should respect the principle of commercial expediency, recognizing that businesses make decisions based on commercial and strategic considerations. This philosophy aligns closely with the ORA concept, which does not question business judgment but seeks to understand whether, at arm's length, a similar decision would have been made by independent enterprises.

Internationally, several jurisdictions have already begun applying this type of reasoning. For instance, courts in Australia and the United Kingdom have used the idea of “realistic alternatives” to evaluate whether intra-group financial arrangements reflect what unrelated parties would have done under comparable conditions. These examples illustrate how ORA can serve as a helpful lens to better interpret business realities in transfer pricing without altering existing legal standards.

In the Indian context, adopting ORA thinking would simply mean adding a broader layer of commercial perspective to an already strong framework. It encourages both taxpayers and authorities to consider transactions not just in terms of outcomes, but also in terms of choices—why a particular arrangement made business sense at the time. Such integration strengthens the overall alignment between economic behavior and the arm's length principle, ensuring that transfer pricing analysis remains grounded in both fairness and business logic.

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## Dissecting the ORA Test: From Decision Logic to Economic Proof

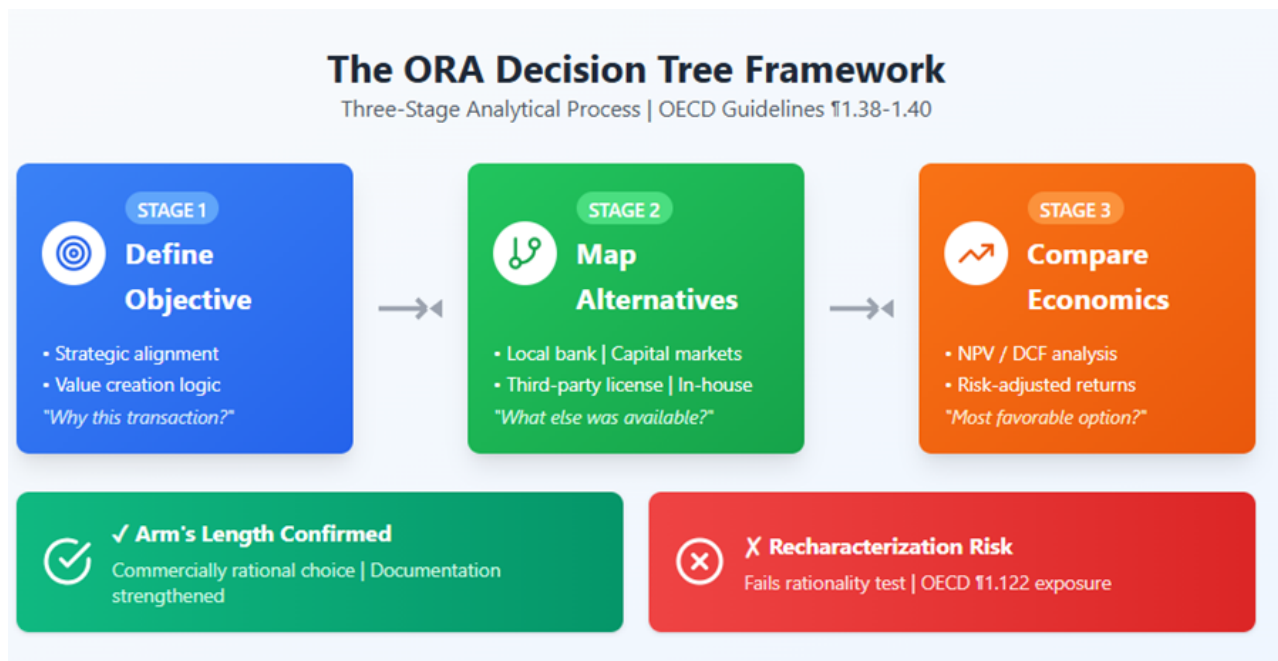
At its core, the ORA framework unfolds in three interdependent stages. First, it demands identification of the **commercial objectives** pursued by each party in the controlled transaction. Every intra-group arrangement—be it a financing structure, a licensing agreement, or a business restructuring—must serve a definable strategic or operational purpose. The inquiry here is not whether the transaction yields immediate profit, but whether it is consistent with the entity's broader value-creation logic. For instance, an Indian subsidiary paying royalties might justify this as a means of accessing global brand equity and technology, while the foreign parent may view it as monetization of intellectual capital. ORA requires the taxpayer to articulate this purpose clearly.

The second stage involves **mapping the set of realistic alternatives** that were available to each party at the time of entering into the transaction. These alternatives must be feasible, not hypothetical. In a financing scenario, alternatives could include borrowing from local banks, accessing capital markets, or adjusting dividend policies. In an intangible transfer, options might range from developing local know-how to outsourcing production. What matters is whether these alternatives were *practicably available* given the entity's capabilities, regulatory constraints, and market environment. This step guards against both taxpayer rationalization and administrative hindsight.

Finally, the third stage entails a **comparative economic evaluation** of these alternatives. This is the analytical heart of ORA. Using discounted cash-flow techniques, opportunity cost analysis, or risk-adjusted return modelling, one must determine whether the controlled transaction offered an outcome that was at least as favorable as the next-best option. If not, the transaction fails the test of commercial rationality. Importantly, this analysis is inherently *ex ante*: it examines the expectations and constraints at the time of decision-making, not the *ex post* results that hindsight may reveal.

Together, these three stages transform ORA from a theoretical notion into a practical analytical tool capable of harmonizing tax, finance, and strategy perspectives.

Imagine an Indian technology subsidiary paying royalties for the use of global software platforms. ORA would ask whether the company had other realistic options—such as developing local software, licensing from third parties, or using open-source alternatives. If the in-house development cost and timeline were much higher, or the third-party technology lacked scale and security, continuing with the group license becomes a commercially rational choice. This type of reasoning not only supports the pricing of the royalty but also clearly demonstrates *why* the chosen transaction aligns with business and market realities.



## ORA vs. Benefit Test: A Critical Distinction

While both ORA and the Indian "benefit test" examine commercial rationality, they operate at fundamentally different analytical levels. The **benefit test**—a retrospective, question: "Did the Indian entity receive commensurate value for the payment made?" It focuses on whether services were actually rendered or intangibles actually used, often leading to *ex-post* disallowance of payments where demonstrable benefit cannot be proven. In contrast, **ORA operates ex-ante**, examining whether the *decision to enter the transaction* was commercially rational given the alternatives realistically available at that time. For example, the benefit test might disallow royalty payments if technology transfer is unproven, whereas ORA would ask: "Could the entity have developed the technology internally, licensed from third parties, or operated without it—and if so, why was the intra-group arrangement the most rational choice?" Thus, ORA complements rather than replaces the benefit test: the former validates the **structural logic** of the transaction, while the latter validates the **quantum and delivery** of value.

## Understanding Indian Jurisprudence Through the ORA Perspective

Indian transfer pricing jurisprudence provides several examples where the underlying themes resonate closely with the spirit of ORA, even if the term itself was not explicitly used in the decisions. These cases reflect the courts' and tribunals' growing emphasis on

understanding the *business logic* and *economic context* of related-party dealings—principles that align well with the ORA framework.

In *Maruti Suzuki India Ltd v. CIT (2010)*, the Delhi High Court examined the issue of marketing intangibles and royalty payments made to the foreign parent, Suzuki Japan. The discussion revolved around whether the Indian entity's marketing expenditure and royalty created value locally or primarily benefited the parent's global brand. When seen through an ORA lens, it is important to evaluate whether such arrangements represent the most effective business choice available to the parties.

The principle of commercial expediency articulated in *EKL Appliances Ltd (2012)* also echoes the foundation of ORA. The Delhi High Court observed that tax authorities should not second-guess a taxpayer's business judgment, provided the transaction is commercially reasonable. The ORA approach supports this idea by providing an objective method to explain that a transaction was indeed rational when compared with feasible alternatives. It reinforces, rather than replaces, the concept of commercial prudence recognized by the Court.

Similarly, the decision in *Li & Fung India Pvt. Ltd (2014)* highlights how ORA thinking can help clarify functional realities. The Court recognized that the Indian entity operated as a low-risk sourcing service provider rather than an entrepreneurial trader. By viewing this structure through an ORA framework, one can better understand that the Indian subsidiary's limited-risk profile and lack of capital made its chosen model the most practical and economically sensible arrangement. In this way, ORA serves as a supportive analytical tool that validates the economic soundness of the taxpayer's role and remuneration.

Other cases, such as *Bharti Airtel Ltd (2014)* concerning management services and *Aditya Birla Minacs Worldwide Ltd (2019)* involving intra-group loans, also reflect themes consistent with the ORA approach. These matters emphasize the need to consider whether the terms of related-party arrangements—such as service fees or financing rates—align with what would be reasonable when compared with realistic market alternatives. Incorporating ORA-type analysis into such discussions provides a clearer economic narrative, allowing both taxpayers and authorities to understand the commercial choices behind the transactions.

Overall, Indian judicial reasoning already embodies many of the values that ORA seeks to promote—commercial logic, transparency, and a focus on economic reality. Applying ORA more explicitly would not alter this foundation but would further enrich it, offering a structured way to demonstrate that controlled transactions reflect the same decision-making discipline expected between independent enterprises.

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## **ORA and Business Restructurings: The Question of Surrendered Options**

The ORA principle becomes particularly consequential in business restructurings, which often involve a transfer of potential upside or strategic autonomy from a local entity to a foreign principal. The OECD's Chapter IX emphasizes that in determining whether the restructured arrangement is arm's length, one must assess whether the restructured entity had "realistically available options" other than accepting the new terms.

Consider an Indian manufacturer converted into a limited-risk contract manufacturer for its Singapore parent. ORA would require examining whether, at the time of conversion, the Indian entity could have continued as an independent producer, supplied third-party

customers, or negotiated compensation for relinquishing its market rights. If no independent enterprise would surrender control without adequate consideration, the restructuring lacks commercial rationality.

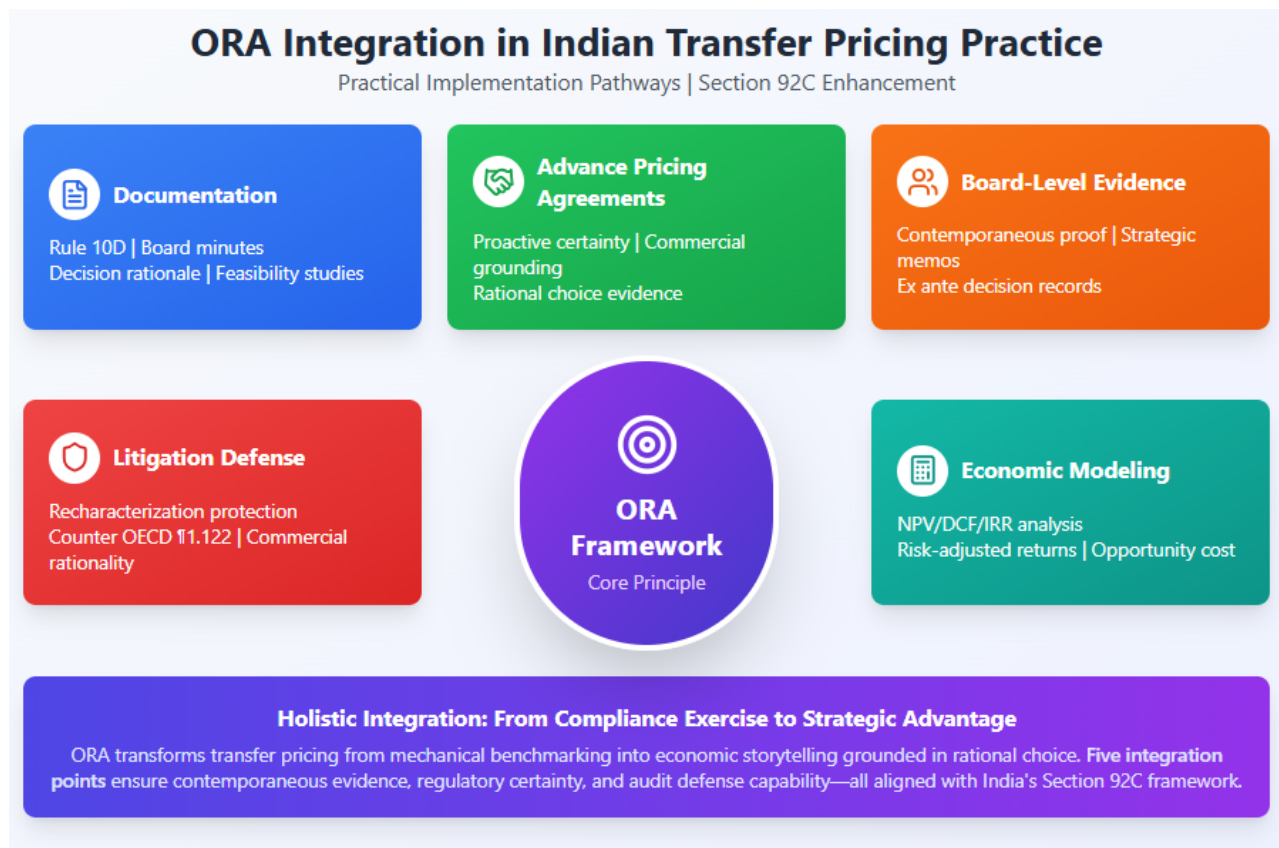


## Integrating ORA Into Indian Transfer Pricing Documentation

To operationalize ORA within Indian compliance practice, taxpayers must embed the reasoning directly into their **local files**. Rule 10D(1) already requires a description of the functions, assets, and risks; this can be expanded to include a narrative on decision rationale and alternative evaluations. Board minutes, feasibility studies, and inter-company memos can serve as contemporaneous evidence demonstrating that the controlled transaction represented the most rational choice available.

In **Advance Pricing Agreements (APAs)**, the inclusion of ORA analyses can enhance credibility by demonstrating that the chosen structure was commercially grounded. For instance, in an APA concerning a contract R&D centre, taxpayers can show that continuing as a full-risk entrepreneur would have entailed capital exposures inconsistent with group strategy, making the limited-risk model the most rational option.

In litigation, ORA evidence can protect taxpayers against recharacterization. If the taxpayer can show that the transaction mirrored the rational choice an independent enterprise would have made, this can greatly add to the comparability analysis.



## Quantifying ORA: From Narrative to Numbers

While ORA begins as a qualitative reasoning exercise, it gains persuasive force when supported by quantitative analysis. Modern corporate finance tools—e.g. net present value modelling—can be adapted to demonstrate that the selected controlled transaction maximized expected utility relative to feasible alternatives.

For example, in assessing whether an Indian entity should license technology or acquire it outright, analysts can compare the NPV of expected cash flows under each scenario, incorporating risk premiums and control benefits. Similarly, in financing arrangements, comparing the internal rate of return from intra-group debt with the opportunity cost of local bank borrowing provides an empirical basis for ORA. Such quantification translates the abstract notion of “realistic options” into demonstrable economic evidence, making it a potent defense in audit or litigation.

## International Parallels and Emerging Consensus

Globally, tax administrations are converging toward the ORA framework. The Australian Tax Office's approach post-*Chevron*, the German Ministry of Finance's 2021 Administrative

Principles for Financial Transactions, and the U.S. Treasury Regulations all require consideration of alternatives realistically available. The common thread across these jurisdictions is a focus on **economic substance expressed through choice**. India, being an active member of the OECD Inclusive Framework, cannot remain an outlier. Aligning with ORA would not only enhance coherence with global standards but also lend intellectual discipline to the domestic audit process, which often veers into subjective assertions of “benefit” or “intent.”

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## Challenges, Safeguards, and the Path Forward

Integrating ORA into Indian transfer pricing is not without practical difficulties. The most immediate challenge lies in the evidentiary burden as it requires contemporaneous documentation explaining why a particular structure was chosen. Without such evidence, ORA could become a tool of hindsight for tax authorities. This risk can be mitigated by requiring that ORA analyses be prepared *ex ante* and included in inter-company documentation at the time of the transaction.

A second challenge is **judicial perception**. It must be emphasized that ORA is not an invitation to question the wisdom of business decisions; rather, it is a framework for assessing whether those decisions are economically rational in an arm’s length setting. When properly understood, ORA complements, rather than contradicts.

Finally, policymakers should ensure that ORA is applied symmetrically. It should not become a one-sided tool for the revenue authorities to recharacterize taxpayer transactions. Instead, it should operate as a neutral principle — capable of both challenging and defending structures based on their commercial rationality.

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## Policy Imperative: Embedding ORA in Indian Regulations

Given India’s increasing alignment with OECD standards, codifying ORA would be a logical next step. The Central Board of Direct Taxes (CBDT) could issue a circular clarifying that arm’s length behavior encompasses the evaluation of realistically available alternatives. Alternatively, Rule 10B(2) could be amended to include “economic alternatives available to the parties” as an explicit comparability factor. Such policy articulation would provide much-needed clarity to taxpayers and tax officers alike, anchoring transfer pricing analysis in economic logic.

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## Conclusion: From Price Comparison to Choice Rationalization

The doctrine of **Options Realistically Available** represents the next evolutionary step in India’s transfer pricing discourse. It extends the arm’s length principle beyond price determination to encompass decision-making behavior itself. In a global environment increasingly focused on value creation and economic substance, India’s continued reliance on mechanical benchmarking risks conceptual stagnation. ORA offers a path forward — one that integrates economics, law, and business judgment into a coherent analytical framework.

By systematically asking whether a taxpayer had better options and why those options were not chosen, ORA converts transfer pricing from an exercise in mechanical comparison into a discipline of **economic storytelling grounded in rational choice**. It encourages transparency in business reasoning, deters artificial structuring, and provides courts with a principled basis to distinguish genuine commercial conduct from tax-motivated design.

If India embraces ORA, it will not merely align itself with OECD orthodoxy; it will enrich the global conversation by grounding transfer pricing in the lived realities of emerging-market enterprise behavior — a contribution both pragmatic and intellectually transformative.

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