

John Deere India Private Limited – ITAT – Pune

Outcome: In favour of taxpayer

Category: Adhoc transfer pricing adjustment

Taxpayer pays royalty to its AEs on all products (old and new products). The tax officer rejected payment of royalty on “old” products and proposed an adhoc adjustment, which further resulted in a double adjustment.

In the present case, reference was made to tax officer by assessing officer, to benchmark international transactions undertaken by taxpayer. Here, the law states that tax officer can make any separate adjustment in respect of international transaction. However, Tax Court opines that the tax officer is not empowered to propose an adhoc disallowance which is not as per provisions relating to transfer pricing.

Accordingly, Tax Court decides in taxpayer’s favour, holds that it is not the tax officer’s role to determine whether royalty payment was justified (on old products or not). Hence, Tax Court finds no merit in adhoc disallowance of royalty and removes the adjustment.

Herbalife International India Private Limited – ITAT – Bangalore

Outcome: Against taxpayer

Category: Payment of management fees

Tax Court rejects taxpayer’s views in respect of a tax adjustment made on management fees and royalty paid to its AE.

Taxpayer is engaged in the business of dealing in weight management, food & dietary supplements and personal care products. In the backdrop of present case, Tax Court opined that tax officer cannot perform its own arm’s length computation on the basis that there was no need for the taxpayer to incur the expenditure. However, it is the taxpayer’s responsibility to prove that actual services for which management fees were paid are rendered in substance or the technical knowhow on which royalty is paid, is actually used.

Accordingly, an arm’s length computation would be required only if there was an actual transfer of technical know-how which was used by taxpayer in

its manufacturing activity. Further, tax officer computed the arm’s length price at Nil value.

It is observed that taxpayer fails to conclusively prove that it received the administration services (management fees) & technical know-how for the manufacturing activity of the taxpayer. Further, Tax Court places reliance on the Indian Evidence Act where taxpayer fails to provide additional evidence. Therefore, holds the Nil arm’s length computation made by tax officer in respect of payment of management fees and royalty.

UEI Electronics Private Limited – ITAT – Bangalore

Outcome: Against taxpayer

Category: Risk adjustment

Tax Court rejects taxpayer’s claim of risk adjustment on account of differences between risk profile of taxpayer vis-à-vis the comparable companies.

Accordingly, taxpayer bears foreign exchange risk, manpower risk and general business risk. However, instead of showing that the comparable bore more risk, taxpayer did not compute the claim of risk adjustment. The taxpayer placed reliance on case decisions, in which another Tax Court had confirmed risk adjustment without giving an outcome as to how it was quantified. However, this precedent is rejected by present ruling Tax Court because the relied tribunal order was sub silentio (silent) on the outcome of risk adjustment and could not be relied upon.

Accordingly, Tax Court places reliance on Supreme Court ruling in BC Srinivas Shetty and holds that income cannot be subjected to tax if it cannot be quantified. Further, Tax Court rejects taxpayer’s claim as the taxpayer failed to quantify the risk adjustment with reasonable certainty & accuracy.

Luxottica India Eyewear Private Limited – ITAT – Delhi

Outcome: Against taxpayer

Category: AMP Intensity Adjustment

Tax Court rules in respect of AMP intensity adjustment applied by the tax officer.

Accordingly, taxpayer creates marketing intangibles in favour of its AE by carrying out AMP efforts in India. Considering the above activity as a function performed by taxpayer as a distributor, the tax officer did not treat AMP expense as a separate international transaction in the year under assessment. As opposed to earlier assessment years, where tax officer had treated AMP expense as a separate international transaction, the officer treated AMP as a function and made an AMP intensity adjustment to the profit margins of comparable companies.

This was mainly because, after an in-depth analysis of financials of each comparable company by tax officer, it was found that they were having low intensity of marketing functions, and a comparability adjustment was required to be made in the margins of such comparables. This was done by finding the excess of AMP expenditure incurred by taxpayer against selected comparables.

Tax Court holds that a distinction is required to be drawn between a 'function' and a 'transaction'. In taxpayer's case, tax officer treated AMP as a function which is accepted by the Tax Court. Therefore, upholds use of AMP intensity adjustment for a distributor (taxpayer) treating AMP as a 'function' instead of a 'transaction'.

In this backdrop, Tax Court further rejects taxpayer's proposition to carry out AMP intensity adjustment as a replacement to treating AMP expenses as a separate international transaction.

Recent News:

Trending in BEPS Implementation

OECD releases discussion draft for Implementation of Hard-to-Value Intangibles

A hard-to-value-intangible or HTVI are those intangibles for which at the time of transfer-

- No reliable comparison exists; and
- Projections / cash flows are highly uncertain, making it difficult to predict the ultimate success.

The OECD has come out with a discussion draft providing guidance on how to determine the pricing of transfers of HTVIs. The guidance aims to provide a north star to tax authorities for tackling the problem of inconsistencies / gaps in information i.e. what is available to the taxpayer and the same information which is not available with tax authorities. Following are the approaches to HTVI which would now be applied by tax authorities:

- Ex-post outcomes (actual outcomes) to be considered as presumptive (likely) evidence to test the appropriateness of ex-ante (forecast outcomes) arrangements.
- Ex-post outcomes should also account the probability of achieving actual income or cash flows during transfer (of HTVI) while valuing at the time of transaction.
- A revised value of an intangible transferred, that would result in an under-valuation or over-valuation, may be assessed to tax by considering contingent payments and price adjustment clauses, irrespective of payment methods of the taxpayer.
- Tax authorities should apply audit practices to ensure presumptive evidence is identified as early as possible.

Discussion draft is open to comments till 30th June, on the proposed guidance in the discussion draft, where interested parties can send their comments to TransferPricing@oecd.org The guidance document by OECD can be accessed [here](#).

OECD sets Jan 2019 deadline for first assessment of minimum standard - BEPS Action Plan 6 (prevention of treaty shopping)

OECD has released peer review document for assessing implementation of Action 6 minimum standard. *(To be analysed separately in our upcoming **Special Edition**).*