

# Govt clears pending MNC tax issue

The Income Tax (I-T) Department on Thursday resolved the long-pending issue regarding taxing the foreign companies' development centres in India.

The I-T department issued a clarification, based on the Rangachary committee report, saying such development centres will be considered as contract R&D service providers if the parent performs economically significant functions in the research and product development cycle. Further, the parent will have to provide funds, capital and other significant assets, including intangibles.

Also, the development centre will be treated as a contract R&D service provider if it is under the direct supervision of the parent and does not have any significant realised risks. Such recognised contract R&D centres in India would be liable to lower tax. Those not in this category would be treated as units coming out with new products, solutions or software and, hence, liable to pay higher tax.

The Rangachary committee was set up by the Prime Minister's Office to resolve this issue, since India is seen as an attractive location for such centres. The issue has been a long-pending one between the tax authorities and companies, particularly in the segments of information technology and pharmaceuticals.

If the parent is situated in a low-tax or no-tax country, such development centres would not be treated as contract R&D centres. Besides, the development centre in India will not have any ownership right on the research done, if it is to be treated as a contract service provider.

Deloitte Haskins & Sells' partner, Neeru Ahuja, told *Business Standard* if the development centre is considered as one coming out with new products, solutions, etc, the parent company will have to give it royalty and technology fee; the tax on the centre would be much more than on a simple R&D contract service provider.

The I-T department also issued another circular to clarify where the profit-split method would be used in the case of R&D activities located in India. This, it has said, would be applied in international transactions involving unique intangibles or in case where these transactions are so inter-related that these cannot be evaluated separately.

In a profit-split method, the profits of associated enterprises are taken together and the profit of each unit is then arrived at. In this case, the tax would be higher than the usual cost-plus basis in transfer pricing.

(Business Standard)