Revision in tax pacts to push advance pricing agreements

Move aimed at reducing transfer pricing disputes with multinational firms

India will renegotiate its tax treaties with Germany, France, Singapore, Italy and South Korea to pave the way for bilateral advance pricing agreements (APAs) with these countries. If renegotiation takes long, it might also consider unilaterally changing its position in the treaties to allow multinationals sign APAs in India and avoid conflicts with tax authorities over their share of taxes.

“There are two options: You negotiate tax treaties, but that is time-consuming. The second is: The government unilaterally changes its position, but not everybody in the tax department is on board for that. We are working on both,” said a finance ministry official, who did not wish to be identified.

APA is an agreement between a taxpayer and the tax authority over the methodology to be used for computing the arm’s length price of transactions among group companies. India has already signed five unilateral APAs, but it is yet to sign its first bilateral pact involving the country where the MNC is based.

The Double Taxation Avoidance Agreements (DTAAs) with Germany, France, Singapore, Italy and South Korea don’t provide for a bilateral APA. Some companies from these countries such as Samsung, LG, and Siemens are learnt to have shown interest in bilateral APAs but are not eligible currently, and as a result most applications have come from Japan and the UK. First bilateral APA might be signed with Japan soon.

“Paragraph 2 in Article 9 of tax treaties allows one country to give some compensatory or corresponding adjustments if there is double taxation. In the absence of Article 9(2) in treaty with a country, we cannot accept bilateral APA application from its taxpayers because when there is double taxation and provision for compensatory adjustment is not there how to resolve it,” said another official.

Tax experts said most countries had unilaterally changed this position in their treaties to accept bilateral APAs and India could also review its position in order to find a quick resolution.

“India has taken a position that if a tax treaty with any country does not have the provision for corresponding adjustment then India won't enter into APA. We have written to the Central Board of Direct Taxes to revisit this stand,” said SP Singh, senior director, Deloitte.

With a bilateral APA, taxpayers face the risk of double taxation. Indian tax authority taxes only the Indian entity and the foreign jurisdiction taxes the parent. While DTAA says the same income would not be taxed twice, the arm's length price can be interpreted differently by tax authorities of two countries.

“Taxpayers are saying that India can unilaterally change its position in DTAAs. There are enough grounds for India to do that. Countries like Germany are keen on bilateral APAs,” said Vijay Iyer, Partner, EY.

The bilateral APAs are likely to be signed in areas such as information technology, consumer electronics, telecom and manufacturing. The general trading companies of Japan called Sogo Shosha are keen on finalising the agreements early so that their companies investing in India have tax certainty.

“We have started treaty negotiation but that may take a lot of time because you can have maximum two to three meetings in a year. So we are also trying to change India’s position. India says there should be 9(2) for bilateral APA, others say 9(1) is sufficient,” added the first official.

There is a rush to apply for APAs also because in Budget 2014-15, Finance Minister Arun Jaitley had allowed rollback of APA provisions to past years and introduce range concept to determine arm's length price to reduce transfer pricing disputes.

Officials said the CBDT was in the process of framing the rules and these might be notified next month. The rollback is only for applying the agreed methodology to previous years and not the price.

(Business Standard)