**Specified Domestic Transactions**

Transfer pricing regulations introduced in India in 2001, till very recently covered only cross border related party transactions. The Finance Act, 2012 however, has extended its scope to cover certain domestic transactions with related parties within India, defined as ‘Specified Domestic Transactions’.

This will principally have impact in two ways. To begin with, the pricing of the domestic transactions will need to comply with the arm’s length principle by application of one of the prescribed methods. In addition, there will be compliance and documentation obligations for such specified domestic transactions.

A synopsis of the regulations has been explained below.

**Regulation**

**1. How are Specified Domestic Transactions defined?**

The following transactions with the aggregate value exceeding INR 50 million (US$ 1 million) are covered.

• Expenditure for which payment is made or to be made to specified domestic related parties.

• Transfer of goods or services to/from eligible business (tax holiday undertaking) from/to

other business (non-tax holiday undertaking).

• Business transactions between eligible business (tax holiday unit) and other person(s) producing more than ordinary profits owing to close connection.

**2. Which tax payers covered under Specified Domestic Transactions?**

Any taxpayer incurring any expenditure with specified domestic related parties are required to comply with the regulations.

**3. How do you define a specified domestic related party?**

The domestic related party will inter alia include a director, a relative of the director, a person having substantial interest in the taxpayer (carrying not less than 20% of the voting power) and fellow related parties where a single person has substantial interest in two taxpayers.

**4. Which other tax payers are covered under Specified Domestic Transactions?**

• Taxpayers claiming tax holidays are covered e.g.

|  |  |
| --- | --- |
| Location based tax holiday | • Undertakings having a unit in a Special Economic Zone – Sec 10AA  • Undertakings located in industrial backward district (Jaisalmer in Rajasthan, Bhojpur in Bihar, etc) – Sec 80-IB  • Undertakings located in Himachal Pradesh,  Uttaranchal, or notified areas in North Eastern States (Assam, Tripura, etc) – Sec 80-IC  • Undertakings engaged in business of hotel/ convention centre in specified areas/ districts – Sec 80-ID |
| Sector based tax holiday | • Generation/ transmission or distribution of power or developing, operating, maintaining of infrastructure facilities, etc – Sec 80-IA  • Company/companies engaged  • Company/companies engaged in refining oil, undertakings engaged in developing and building housing projects, etc – Sec 80-IB |

**5. Which are the illustrative lists of Specified Domestic Transactions?**

Transactions between the specified persons and also between the inter unit transactions of taxpayers would be covered. e.g.normal operating transactions, remuneration to directors, allocation of costs, etc.

**6. Which is the effective date for application of the proposed regulation?**

It would be applicable to transactions entered into w.e.f. 1 April 2012.

**Compliance**

**7. What are the compliance requirements for taxpayers that have Specified Domestic Transactions?**

Taxpayers that have Specified Domestic Transactions would need to do the following:

• Maintain requisite information and documents as prescribed; and

• Obtain and furnish a prescribed report from an Accountant in Form 3CEB.

**8. What is the due date for filing the Accountant’s report and documentation?**

• The Accountant’s report needs to be submitted with the tax authorities by the due date of

filing annual return of income. At present, the due date is 30 November.

• Documentation is not required to be submitted along with the Accountant’s report, but is to be in place by the due date. It it does need to be submitted during the course of the audit/ assessment.

**Penal Consequences**

9. What is the penalty regime for non-compliance with the regulation?

A stringent penalty regime has been prescribed:

• Failure to maintain documents – 2% of the value of the transaction

• Failure to furnish documents – 2% of the value of the transaction

• Failure to report a transaction in Accountant’s report – 2% of the value of the transaction

• Maintaining or furnishing incorrect information or documents – 2% of the value of the transaction

• Adjustment for incorrect pricing – 100% to 300% of the additional tax payable

**Methods for determining Arm’s Length Price**

10. Are there prescribed methods to determine Arm’s Length Price?

The Arm’s Length Price has to be determined applying any of the prescribed methods

• Comparable Uncontrolled Price Method (CUP)

• Resale Price Method (RPM)

• Cost Plus Method (C+)

• Profit Split Method (PSM)

• Transactional Net Margin Method (TNMM)

• Or any other method as prescribed by the Central Board of Direct Taxes

**Economic Analysis – Comparables Search**

**11. How can the search for potential comparables be conducted?**

Apart from internal information and comparables, external comparables may be searched in public domain such as:

• Websites, industry magazines and public database

• Indian Databases such as Prowess and Capitaline

**Documentation**

**12. Is there any prescribed list of documentation to be maintained?**

The documentation would mainly include the following:

• Ownership structure and group profile

• Industry and business analysis

• Functions, Assets and Risks analysis (FAR analysis)

• Selection and application of most appropriate method

• Comparability analysis and

• Determination of Arm’s Length Price

**Assessment/Audit**

**13. What is the administrative set up for assessment of Specified Domestic Transactions?**

A separate cell consisting of transfer pricing officers will now perform the assessment of Specified Domestic Transactions instead of assessing officers.

**14. What is the statute of limitation for completion of assessment?**

The time limit for completion of audit is at present will be of 48 months from the end of the relevant tax year.

**Going Forward**

**15. How can one implement the regulations around Specified Domestic Transactions?**

It will be necessary to identify and map the transactions which will now be covered under the expanded scope of transfer pricing regulations. The taxpayers need to ensure that such identified transactions are analyzed so as to comply with the Arm’s Length Principle based on the application of the most appropriate method adequately supported by a robust economic analysis. It is advisable to organize for a timely compilation of relevant details and to ensure entering of such transactions at Arm’s Length Price.

**Source : Deloitte**