Tax department gets a Rs.10,000 cr windfall from pact with MNCs

Gireesh Chandra Prasad: Updated: 27 Jan 2020, 12:05 AM IST

- **The gain is from a pact that lets MNCs negotiate how their profit margins for India are calculated for five years**
- **While the advance pricing agreement scheme offers tax certainty only within India, a bilateral or multilateral APA would offer relief to the company from double taxation as well**

New Delhi: The income tax department has made a windfall gain of ₹10,000 crore from a scheme meant to avoid tax disputes, with multinational companies operating in India, a development that could give impetus to new schemes that will reduce litigation while adding to the government coffers.

The gain is from the advance pricing agreement (APA) programme that allows MNCs to negotiate how profit margins for India operations are to be calculated for tax purposes for five years in return for avoiding rigorous scrutiny of transaction details. Introduced in 2012, the scheme was tweaked in 2015 to allow such negotiated profit margins applicable for the past four years as well, allowing companies tax certainty for a total of nine years. Extending the agreed profit margin for past years has led to many MNCs revising their past year profit margins upwards, a government official said on condition of anonymity. Questioning the price at which MNCs transact with their units in India, called transfer price, has been an area of intense tax disputes at the beginning of this decade, which forced the government to roll out the APA scheme. Companies such as International Business Machines Corp. and Microsoft Corp. had in the past faced transfer pricing disputes in India.

“In the retroactive APAs, when companies agree for, say, 16% profit margin, and revise past years’ profit margin to 16% from a previously disclosed 14% to secure certainty in taxation, the department has benefited. So far, the estimate is that the department has benefited by more than ₹10,000 crore, with about 320 APAs having been signed till 2019," said the official cited earlier. Close to 60 more APAs have been cleared by the Central Board of Direct Taxes (CBDT) and are waiting to be signed, said the official.

The price at which MNCs transact with their associated enterprises across the border is of key interest to the tax department as any profits that are not taxed here would erode the country’s tax base. Tax officials verify that the cross-border transactions are on an arm’s length basis by comparing them with the industry benchmark or margins in similar transactions between unrelated parties. India’s services sector, especially the information technology industry, had in the past borne the brunt of taxmen upwardly revising the profits reported here, known as transfer pricing adjustments.

The success of the APA scheme is likely to give impetus to others that could reduce the cost of tax collection and at the same time, offer tax certainty to businesses. A seven-member task force, led by former CBDT member Akhilesh Ranjan, had suggested to the government in its report last year that the concept of mediation could be introduced in law to resolve tax disputes.

The finance ministry has not made the report public yet, but is widely expected to rely on the ideas suggested by it in shaping tax proposals in the union budget for FY21.

“Barring a few extreme cases, industry has generally been happy about the outcome of the APA programme. This could encourage the government to come up with more schemes meant to reduce litigation," said Amit Maheshwari, partner at Ashok Maheshwary and Associates Llp.

Although the APA scheme has been a success, making the tax authorities in other countries, where the MNC has units, Parties to such deals has not seen a similar degree of success.

While the APA scheme offers tax certainty only within India, a bilateral or multilateral APA would offer relief to the company from double taxation as well.