



Tax alert: Safe Harbour rules amended to streamline intra group financing arrangements with global standards

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Unveiling India's latest Safe Harbour amendments: Revised intra-group loan rules and new interest rate benchmarks.

In a nutshell



Revised intra group Loan Definitions:

The definition of "intra-group loan" now includes loans to any non-resident associated enterprise, with the exclusion of loans by financial companies.



Interest Rate Reform:

Shift from LIBOR to specific reference rates for determining interest rates on foreign currency intra-group loans, with a dual basis point structure based on aggregate loan amounts.



Credit Rating Clarification:

Credit ratings for determining interest rates must now come from SEBI registered and RBI accredited agencies, with the lowest rating applied when multiple are available.



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The Central Board of Direct Taxes (CBDT) has introduced pivotal amendments to the Safe Harbour provisions under the Income Tax Rules, 1962, through Notification No. 104/2023/F. No. 370142/26/2023-TPL, issued on December 19, 2023. These amendments will come into effect from April 1, 2024, applicable for assessment year 2024-25, and pertaining to the ongoing financial year 2023-24.

Key highlights of the amendments include:

1. Revised Definitions in Rule 10TA:

- 1.1 The definition of "intra-group loan" has been revised. Earlier, an "intra-group loan" was defined as loans advanced to wholly owned subsidiaries being non-residents and sourced in Indian rupees.

The new definition now encompasses loans advanced to any non-resident associated enterprise, excluding those by financial companies or enterprises engaged in normal lending or borrowing operations. Further, the condition of loan being sourced in Indian rupees is done away with.

- 1.2 Independently, the definition of operating incomes and operating expenses has been slightly modified. Earlier, any 'income' or 'loss' on transfer of assets or investments was considered as a non-operating item. However, the said definition has been modified to provide that income or loss on transfer of those assets or investments whose depreciation is included in the operating expenses, shall be considered as operating in nature. This would mean that where a capital asset on which depreciation is reckoned, is disposed of such gain or loss on disposal would also be includible in the operating income or operating cost base.

2. Revamped Rule 10TD: Intra-group Loan Advancements Redefined:

- 2.1 Intra-group Loans in Indian Rupees: Updated approach:

In the previous ruleset, the interest rate for loans in Indian Rupees was linked to the one-year SBI lending rate plus a basis points adjustment based on the "CRISIL" credit rating of the associated enterprise. With the subject notification, the word "CRISIL" has been omitted from the said clause which means that the credit rating shall mandatorily not be from CRISIL only.

- 2.2 Intra-group Loans in Foreign Currencies: New Determination Method:

2.2.1 **Basis of determining the base interest rate shifted from the LIBOR to specific reference rates:** An updated ruleset for advancing of intra-group loans in foreign currencies has been brought. The interest rate for intra-group loans denominated in foreign currency was earlier based on the six-month London Inter-Bank Offer Rate (LIBOR) of the relevant foreign currency as of September 30 of the financial year. The new rule provides that interest rate for such loans will now be based on the reference rate of the relevant foreign currency as on September 30 of the financial year.

2.2.2 **Basis Points Adjustment:** The new framework introduces a dual structure based on the loan amount, i.e., for aggregate loans up to an equivalent of INR 250 crores, the additional basis points over reference rates range from 150 basis points for high credit ratings to 400 basis points for lower or unavailable ratings. For loans exceeding this threshold, the basis points over the reference rate increase, going up to 600 basis points, addressing the higher risk associated with larger aggregate loan amounts. This bifurcation acknowledges the varying degrees of risk in lending activities, offering a more tailored and risk-sensitive approach. Overall, these amendments not only align with international financial norms but also introduce a form of risk assessment into the realm of transfer pricing, potentially reducing disputes and enhancing compliance transparency for multinational enterprises operating in India.

3. Defining Reference Rates and Credit Ratings:

- (i) *Reference rates:* The notification provides clear definitions of "reference rate" and "credit rating" for the purposes of the amended rules. Reference rates for various major currencies like US Dollar, Euro, UK Pound Sterling, Japanese Yen, Australian Dollar, and Singapore Dollar have been detailed. For instance, the

reference rate for the US Dollar is defined as the 6-month Term Secured Overnight Financing rate (SOFR) administered by Chicago Mercantile Exchange (CME), increased by 45 basis points, the reference rate for the Euro is the 6 month Euro Inter Bank Offered Rate (EURIBOR), currently administered by European Money Markets Institute, and the reference rate for the Australian Dollar is the 6 month Bank Bill Swap Rate (BBSW) administered by the Australian Securities Exchange.

- (ii) *Credit ratings:* Further, the credit rating is defined as the rating assigned by a SEBI-registered and RBI accredited credit rating agency, applicable for the relevant financial year. This requirement ensures that the credit ratings used for determining transfer prices for intercompany financing are reliable and recognized by the key financial regulatory authorities in India. If an associated enterprise has only one credit rating from a registered and accredited agency, such rating is used for determining the interest rate; however, when multiple credit ratings exist, the lowest of those ratings is applied to assess its creditworthiness.

Conclusion:

These amendments reflect the Indian government's ongoing efforts to streamline and clarify tax regulations, ensuring a more transparent and efficient tax environment in India. They also mark a significant stride towards aligning the country's tax regulations with global financing standards. While these changes are in respect of safe harbour election, they are expected to simplify compliance, reduce transfer pricing disputes, and enhance certainty for multinational corporations operating in India and also, more broadly speaking, serve as a harbinger for documentation and audit practices in the transfer pricing context.

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