



Advance Pricing Agreement Frequently Asked Questions



The concept of Advance Pricing Agreement (APA) has been introduced in India. The Central Board of Direct Taxes has recently notified advance pricing agreements scheme. Given the numerous transfer pricing cases in dispute, introduction of APAs is expected to considerably alleviate the uncertainty regarding arm's length pricing of international transactions.

Advance Pricing Agreement (APA) provisions were introduced in the Income-tax Act, 1961 (Act) w.e.f. 1 July 2012. The rules in respect of the APA scheme have been notified by the Central Board of Direct Taxes (CBDT) by way of insertion of Rule 10F to Rule 10T and Rule 44GA in the Income-tax Rules, 1962 (Rules).

The various aspects of rules/ guidelines governing APA and certain operational matters relating to APA are analysed below:

APA

1. What is an Advance Pricing Agreement (APA)?

An APA is an agreement between a tax payer and tax authority determining the transfer pricing methodology for pricing the tax payer's international transactions for future years. The methodology is to be applied for a certain period of time based on the fulfillment of certain terms and conditions (called critical assumptions).

2. What are the different types of APAs?

An APA can be unilateral, bilateral, or multilateral.

- **Unilateral APA:** an APA that involves only the tax payer and

the tax authority of the country where the tax payer is located.

- **Bilateral APA (BAPA):** an APA that involves the tax payer, associated enterprise (AE) of the tax payer in the foreign country, tax authority of the country where the tax payer is located, and the foreign tax authority.
- **Multilateral APA (MAPA):** an APA that involves the tax payer, two or more AEs of the tax payer in different foreign countries, tax authority of the country where the tax payer is located, and the tax authorities of AEs.

3. How are APAs different from Mutual Agreement Procedure (MAP)?

MAP is a mechanism laid down in tax treaties to ensure that taxation is in accordance with the tax treaty. This can also be invoked when a tax payer suffers or is likely to suffer an adverse action during transfer pricing audit to avoid economic double taxation. On the other hand, APA can be entered into for prospective years. Tax payers with litigation history may opt to file MAP in respect of pending disputes and also opt for APA for the same

transactions for the future years as an effective dispute resolution/avoidance strategy.

Benefits & scope of APA

4. What are the key benefits of APA?

An APA provides the following benefits-

- Certainty with respect to tax outcome of the tax payer's international transactions, by agreeing in advance the arm's length pricing or pricing methodology (ies) to be applied to the tax payer's international transactions covered by the APA;
- Removal of an audit threat (minimize rigours of audit), and deliverance of a particular tax outcome based on the terms of the agreement;
- Substantial reduction of compliance costs over the term of the APA; and
- For tax authorities, an APA reduces cost of administration and also frees scarce resources.

Consequently, APAs provide a win-win situation for all the stakeholders involved.

5. What will be the scope of an APA?

An agreement, among other things,

would include :

- International transactions covered;
- Agreed transfer pricing policy;
- Determination of arm's length price including the transfer pricing methodology to be applied;
- Definition of any relevant term; and
- Critical assumptions and the conditions, if any, other than that provided in the Act or the Rules.

6. What are critical assumptions?

An APA will define in advance the critical assumptions, including those not within the control of the enterprise or the tax authorities. Such assumptions can be any fact about the enterprise, an affiliate, a third party, an industry or general economic conditions.

Examples of some of the assumptions can be as below:

- assumptions about the relevant domestic tax law and treaty provisions and government regulations;
- assumptions about economic conditions;
- assumptions about the nature of the functions and risks of the enterprises involved in the transactions;

- assumptions about the enterprises that operate in each jurisdiction and the form in which they will do so etc.

7. Will the APA process allow more leeway to negotiate arm's length price?

Yes. Under the provisions of the Act and the scheme, the APA can determine the Arm's length price by application of any of the prescribed methods or any other method with such adjustments or variation as may be necessary or expedient to do.

Eligible tax payer & permissible transactions

8. Who is eligible to file for an APA?

Any tax payer who has undertaken an international transaction or is contemplating to undertake an international transaction is eligible to file for an APA.

9. What are the transactions that can be covered in an APA?

Any type of international transaction can be covered in an APA.

10. Can tax payers opt to cover some of the several international transactions in an APA?

Yes, the taxpayers have the option covering all or some of the international transactions in an APA

11. Do the APA rules prescribe any criteria for accepting an APA?

There are no monetary limits or other prescribed criteria for a tax payer to be eligible for applying for an APA.

Pre-filing Consultation

12. What is pre-filing consultation?

The APA Rules provide for a preliminary consultation before formally lodging an APA application. In such consultation, the tax payer and the APA team will discuss and clarify the scope of the APA, the transfer pricing issues involved and whether an APA can be executed or not.

The pre-filing consultation is mandatory, and specified information has to be filed as part of the pre-filing application. However, the discussion during the pre-filing meeting is not binding on either the tax payer or the tax authorities.

13. Can tax authorities reject any APA application based on the outcome of the pre-filing discussions?

The pre-filing consultation would not bind the CBDT or the tax payer to either initiate the APA process or to enter into an APA. However, it may be possible that in a pre-filing

meeting the authorities may indicate their reluctance to accept the proposed methodology which could influence the negotiation process. It is expected that that understanding reached at this stage will be communicated in writing.

14. How can the anonymity be maintained in the pre-filing stage?

Tax payers have the option of entering into the pre-filing consultation process on a no-name basis. However, considering the extent of detailed information to be furnished, one needs to evaluate whether and to what extent anonymity can be maintained.

Application for APA

15. What are the procedures for filing of an APA application for unilateral, bilateral, and multilateral APAs?

An application for a unilateral agreement should be made to the Director General of Income Tax (international taxation) (DG-IT).

For BAPA/MAPA, application should be made to the Competent Authority (CA) in India. The CA will send the application to DG-IT who in turn will send it to respective APA teams.

In the case of BAPA/MAPA, negotiations between the CAs of India and other country (ies) shall be carried out in accordance with the provisions of the tax treaties. Further, the process in India will be initiated, only after filing the application with the CAs in the AEs' jurisdiction and evidence to that effect is provided to the Indian CA.

16. What are the prescribed fees for the APA applications?

An APA application is required to be accompanied with the filing fees as below:

International transactions Value (in approx. USD)	APA filing fee (in approx. USD)
Value <= 20 million	20,000
Value > 20 million <= 40 million	30,000
Value > 40 million	40,000

(1 USD = 50 INR)

The fees shall be computed with reference to the total value of international transactions in respect of which an APA is proposed. Accordingly, the fees shall be based on transaction value of the full period of the proposed APA.

17. How is the additional fee computed?

In case of any proposal for amendment to an APA application filed that involves inclusion of additional transactions, additional (incremental) fee is payable based on the increase in the total value of the international transactions as compared to the total value of the transactions originally proposed in the APA.

18. Can a tax payer amend the APA application once filed?

Yes. An applicant can request in writing for an amendment to an application, at any stage, before the finalization of the terms of the agreement.

19. When can the application be withdrawn and what are the procedures for the same? How would this work in the case of BAPA / MAPA?

If any defect is noticed in the application filed by the applicant following a successful pre-filing consultation and if the application is withdrawn at this stage, then the fee paid by the applicant shall be refunded.

Further, the tax payer may withdraw an application at any time before its finalization, by filing a request in a prescribed Form. However, in case of such withdrawal, the tax payer would not be eligible for receiving a refund of filing fee. The procedure is no different for BAPA/MAPA.

20. Should a separate application be made for transactions with each Associated Enterprise (AE) separately?

It is understood that a single application providing full details of all the AEs and the international transactions with them would suffice and separate applications need not be required.

In case of where AEs are located in different jurisdictions, the tax payers have the option of seeking bilateral or multilateral APA. In the case of bilateral and multilateral applications, negotiations between the CAs of India and other country(ies) shall be carried out in accordance with the provisions of the tax treaties, and the APA process in India will be initiated only after filing the application with the CAs in the AEs' jurisdiction and an evidence to that effect is provided to the Indian CA.

21. Can a tax payer file one consolidated application covering all the transactions?

A single APA application can be sufficient for covering multiple types of transactions involving multiple AEs and no separate applications are required.

22. Can the past years' litigation be considered in an APA Application?

Any person who has undertaken an international transaction, or is contemplating to undertake an international transaction is eligible to file for an APA. The APA provisions are prospective in nature and there is no option for rollback.

However, it is possible to enter into an APA in case of the transactions that are under litigation. In case of such transactions, APA can be entered into only prospectively and an application has to be filed before the beginning of the financial year for which the said transactions are intended to be covered. However, past years litigation cannot be considered for APA.

Negotiation process

23. What would be the composition of the APA team?

The APA team consists of income-tax

authorities as constituted by the CBDT including experts in economics, statistics, law or any other field as may be nominated by the DG-IT.

24. Is the APA team equipped with adequate staff / resources to meet the demand for APAs?

At various fora, the tax authorities have reiterated that the APA team is adequately staffed, trained and the number of staff would be increased, if required.

25. Who can appear before the APA team to carry out the negotiations?

Tax payers or their authorized representative can carry out the negotiations.

26. How is the APA process different from the regular transfer pricing assessment?

The APA process is legally binding on both the parties for a period of five consecutive years or less as agreed between the tax payer and the CBDT. The regular transfer pricing audit is carried on a year on year basis. APA provides certainty and reduces litigation.

Transparency and open minded approach during negotiation, both by tax authorities and tax payer is the key for a successful APA. No negotiation process is involved in the regular transfer pricing assessment.

27. Is there a time frame for the negotiation and conclusion of APA?

No time frame has been specified in the Rules. However, the tax authorities have indicated that they will endeavor to enter into unilateral APAs within one year and BAPA / MAPA within two to three years.

28. Will APA application & materials be shared with the Indian revenue authorities?

Currently the APA rules do not have any explicit provision with regard to sharing of the information furnished in the course of APA negotiations with the transfer pricing officers or in the event of withdrawal of APA application or cancelation of an APA.

29. Will the finalized APAs be available in the public domain?

The APAs executed are tax payer specific. Hence, these will not be available in the public domain.

Compliance Obligation

30. What are the compliance requirements during the negotiation of APA?

Rules provide that filing of an application for APA will not prevent the operation of other Transfer Pricing Provisions of the Act, Therefore, based on the current provision, tax payer may have to comply with all the provisions including maintenance of transfer pricing documentation and filing of Form 3CEB.

31. Will the tax authorities carry out regular audits during the negotiation of APA?

As mentioned above, tax payer will have to comply with all the provisions including maintenance of transfer pricing documentation and filing of Form 3CEB. Tax authorities will continue with the audit as per the provisions of the Act even while the APA is under negotiation.

On conclusion of APA, tax payer has to revise its return of income for the past years, covered under APA, within three months from the conclusion of APA. Tax authorities will complete/amend the audit of revised returns in accordance with the terms of the APA

32. How will the transfer pricing audit provisions apply to transactions covered under an APA, post conclusion of APA?

The covered transactions under the agreement will not be subjected to regular audit by the Transfer Pricing Officer (TPO). An Annual Compliance Report is required to be filed which will be audited by the jurisdictional TPO.

Non-compliance of the terms of the APA, including the critical assumptions, may lead to the cancellation of the APA.

In the cases, where international transactions are not covered under an APA, the regular audits will be carried out in respect of such transactions

Validity & Renewal of APA

33. What is the validity period for an APA once executed?

Validity period for an APA is five consecutive years or less as agreed between the taxpayer and the CBDT.

34. What are the procedures for the cancellation of the APA?

The CBDT has the powers to cancel an APA if the results of the

compliance audit indicate that:

- the applicant has failed to comply with the terms of the agreement,
- there is a failure to file the annual compliance report within the stipulated timeline,
- there are material errors in the annual compliance report filed by the applicant, or
- if the applicant is in disagreement with the proposed revision in the APA.

If an agreement is cancelled based on the discovery of fraud or misrepresentation of facts on the part of the applicant the same shall be deemed cancelled ab-initio and audit will take place accordingly.

35. What are the procedures of the renewal of APA?

In case of renewal of an agreement, all the procedures other than the pre-filing procedures will be followed by the applicant treating the application at par with a new applicant. It is expected that where the circumstances do not change materially getting a renewal of an APA would be a lot easier than getting an APA for the first time. Renewed APA can be on new terms depending on the facts of the case.

36. Does the APA rules provide for roll back provision?

The APA rules do not contain any roll back provisions. APA application is to be filed before the first day of the financial year (e.g. before 1 April 2013 for financial year 2013-14) in respect of continuing transactions. Whereas, for transactions proposed to be undertaken for the first time, such application is required to be filed prior to undertaking of the said transaction, and can be effective even from the middle of the financial year. The timelines are for the main filing. Accordingly, pre-filing application has to be submitted much before the said timelines. It is expected that going forward the terms of the APA may be applied to past years as in the practice in other countries.

Decision Matrix for APA

37. What are the key points to consider while deciding whether to go for an APA or not?

The following key points should be considered by a tax payer while taking this decision:

- ongoing and expensive audit history;
- nature of transactions being complex;
- facts are expected to remain stable over a period of next few years;
- New transactions, proposed to be entered, which may give rise to litigation; and
- Transactions entailing business restructuring, intangibles, financial transactions etc.

In the aforementioned cases, APA may be preferred to achieve certainty in pricing of transactions.

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