NASSCOM®

PRE-BUDGET MEMORANDUM 2016-17

Transfer Pricing Issues

January 2016

Contents

EXECUTIVE SUMMARY

The Indian IT-BPM has demonstrated flexibility and resolve to adjust to turbulent economic conditions and experience double digit growth. Contribution of the IT sector to the Indian economy has been significant and today as $146 Billion Industry, is the largest private sector employer in the organized sector.

The emergence of a rapidly growing ecosystem for innovation driven entrepreneurs and start-ups is further paving way for growth and long term success in the future. With over 2,000 digitally focussed Start-ups and IT SMEs today, it is the second largest hub globally, after China.

The cross sectoral impact of the IT sector has never been so critical for India's growth and development agenda. The Government recognises its potential, and the Technology sector is undoubtedly a key pillar in various flagship initiatives like Digital India, Make in India, Skill India as well as Start-up India.

Ease of business is the most critical enabler in an entrepreneurship ecosystem.

The focus of our budget recommendations is therefore on legislative changes and clarifications to ensure ease of business and growth of Industry. Further, there are specific proposals for start-ups for consideration, along with a proposed definition of start-ups.

The IT sector has witnessed maximum impact of Transfer Pricing adjustments over last 10 years arising out of disputes around selection of comparable companies during assessment and unrealistic adjustments made to the margins. Redefining safe harbour margins, which have so far remained ineffective, should be undertaken on a priority to encourage uptake by Industry and will help Small and medium size companies in easing regulatory compliance.

Several important legislative changes announced in the previous year's budgets are awaited. CBDT guidelines on Foreign Tax credit, reporting norms, Transfer Pricing rules, Rules on the Place of effective Management are some of them. These are critical legislative changes a delay in which is causing uncertainty and inconvenience. There is an urgent need to expedite notification of these changes.

The GST Bill is of tremendous significance for the industry at large and the Indian IT sector in particular.

The IT sector is characterized by fast changing technologies leading to new business models, service delivery methods and platforms. These have far reaching implications not only on business operations, but also the policy and resulting business environment. It is therefore critical that India keeps pace with the dynamic nature of the technology, businesses and governance. We urge the Government to consider adopting collaborative approach with the Industry as policies and rules need to be tweaked and modified, framed anew and revisited for its relevance.

Details of NASSCOM recommendations pertaining to Transfer pricing for the IT/ITeS sector are enclosed in the Pre-Budget Memorandum 2016-17.

SUMMARY - TRANSFER PRICING		
S. No	**Issues and Recommendations**	**Justification**
1.	**Changes proposed in rules for computation of Arm's Length Price**	
2.	**Absence of Article 9(2) in DTAAs restricting bilateral APAs and MAP** Indian tax authority disallow entering of bilateral APA's and MAP in case an Indian entity has an associated enterprise in countries wherein India does not have Article 9(2) in its DTAAs. **Recommendation** Need for deliberation and industry consultation. Government should advise companies on how to address the challenges arising due to absence of certain provisions in the tax treaties	Issues in claiming benefits of DTAA
3.	**Concerns on APA Roll Back Provisions In Cases Of DTAAs Comprising Article 9 (2)** APA rollback rules disallow the use of rollback provisions when it has the effect of reducing the total income or increasing the loss, as the case may be, of the applicant as declared in the return of income of the said year. **Recommend** that suitable modifications be made to allow rollback provisions in such cases.	Not justified in the case of bilateral APA applications wherein the treaty itself provides for corresponding deduction in the other contracting state for avoidance of double taxation, i.e., Article 9(2).
4.	**Risk based assessment audits** Currently a transaction value threshold is being adopted by the Revenue for case selection; this should be replaced by a risk based assessment approach which may be set out through instructions/circulars on an annual basis. Further, Transfer Pricing provisions should not be invoked against tax payers who are entitled to tax holidays (section 10A/10AA reliefs) in India.	Defeating the intent to prevent shifting out profits by manipulating prices charged or paid in international transactions, thereby eroding the country's tax base.
5.	**Safe Harbour Rules not effective for the sector – Need for rationalising the margins** Safe harbour notifications have had limited uptake. **Recommend** that safe harbour notification needs to be re-examined for margins to be rationalized	Limited adoption and not reflecting business realities
6.	**Continued aggressive assessments** Indian IT Industry has been facing several unwarranted assessments on account of transfer pricing adjustments.	Need to rationalise the assessment procedures.
7.	**Ambiguities in Domestic Transfer Pricing** Ambiguity in the current provision **Recommend** clarifications issued e g. TP provisions to apply to revenue expense only; Definition of "close connection"; In addition domestic transfer	If not clarified, likely to create hardships for small scale businesses and additional compliance burden for companies

	pricing provisions should apply only in cases of income escaping tax and not in case tax neutral transactions	
8. (8.1-8.5)	**Guidelines for certainty and consistency** Currently, there is substantial ambiguity in case of Headquarter and regional Headquarter cost allocations being rendered by the overseas affiliate to the Indian entity. **Recommend** issue of guidance related to Intercompany loans, Guarantee / Letter of comfort / Undertaking, Headquarter and regional Headquarter cost allocations, Adjustments for differences in functions and risks and restructuring.	In case of comparability adjustments there is a lot of ambiguity with regard to methodology, application, quantification etc.
9.	**TP Documentation threshold** No documentation requirements on threshold limit upto INR 10 million **Recommend** increase of threshold limit for the sector	Upward revision in monetary limit required as software transaction values have increased, requiring almost all companies to maintain onerous documentation
10.	**Change in Dispute Resolution Panel** Structural changes required for more effective DRP **Recommend** DRP to be constituted as an 'independent' judicial board with panellists from economic legal and accounting background and tax department;	DRP has been limited in its ability to resolve disputes in the past and there have been prolonged litigations.
11.	**Levy of penalty on single transaction to be rationalized** Multiple provisions for levy on penalty on a single transaction **Recommend** that a single penalty be levied on non-compliance of a provision to avoid duplication of penalty.	• Section 271AA: Failure to keep and maintain information, documents; • Section 271 BA: Penalty to furnish report from accountant; • Section 271 G: Penalty for failure to furnish information u/s 92D

TRANSFER PRICING ISSUES

1. CHANGES PROPOSED IN THE RULES FOR COMPUTATION OF ARM'S LENGTH PRICE

The release of draft rules for computation of arm's length price in the month of July this year has been in response to a long deliberation with Industry on how TP issues can be addressed. However, the current rules notified continue to have significant deviation from global norms and the statistical concepts associated with them..

Based on our analysis, we are afraid that the prescribed percentile range of 35th to 65th, mandating minimum number of comparables to qualify for use of range and multiple year data will not have significant impact on the current situation and disputes, uncertainties may continue as before.

Following are some of the issues which we foresee and suggestions thereof:

1.1 Applicability of "range" and multiple year data on selected methods

The rules restricts applicability of "range" and multiple year data to Transactional Net Margin Method ("TNMM"), Resale Price Method ("RPM") and Cost Plus Method ("CPM") used to determine the arm's length price ("ALP") of the transaction.

Recommendation

Internationally there is no restriction on the method to be applied for using range and multiple year data for determining ALP. Hence, the "range" concept and multiple year data should be used for all the methods which could be applied for determination of ALP and not just restricted to the methods prescribed in the rules.

1.2 Number of comparables for applicability of "range" concept

The rules prescribe a minimum of 6 comparable companies, based on the similarity of their functions, assets and risks (FAR) with the tested party for the adoption of "range" concept. Identifying 6 comparables for all transactions may be difficult due to constraints such as data availability for 2 out of 3 years, business comparability, quantitative comparability, etc. Consequently, most taxpayers may not be able to adopt the range concept.

Further, if during the audit stage the number of final comparables fall below the mandated 6, due to rejection of certain comparable companies, the method of determining ALP will change from "Range" concept to Arithmetic mean which will add to complexities and increased litigation.

It is also important to note that the internationally accepted OECD Guidelines do not outline a minimum number of comparable entities to be considered for calculation of range

Recommendation

1. The rules should not specify any minimum number of comparable entities as a prerequisite for the use of “range” concept.

   OR

   We recommend a reduction in minimum requirement of comparable companies for application of the range concept from 6 comparable transactions to 4 comparable transactions**.** It may also be clarified that in case of a transaction with less than 4 comparables, the arithmetic mean concept shall continue to apply.

2. Guidance may be provided regarding the selection of appropriate comparables considering the various constrains thereby allowing flexibility to the taxpayers in preparing reliable set for comparable companies.

1.3 “Range” between 35 to 65 percentile instead of inter-quartile range

The rules provides a range between 35 to 65 percentile of the data set. The use of range between 35th to 65th percentiles of the data set may not provide relative reliability on comparable price. The range of 35th to 65th percentile is narrow than interquartile range 25th to 75th percentile, restricting the set of finally selected comparables will eventually fall within the range.

Further, use of inter-quartile range (25th to 75th percentile) is amongst the globally accepted best practice and also closer to economic realities wherein prices, and or margins, are compared to those within a range and not at to a particular point. Some of the countries following interquartile range are USA, United Kingdom, Germany, China, Singapore, Australia, Malaysia, Netherlands, Argentina, Columbia, Denmark, France, Italy, Korea, Israel, Portugal, Spain, Uruguay, Venezuela, South Africa, Thailand, Sweden.

Recommendation

It is recommended that the rules be modified to provide that the interquartile range from the 25^{th} to 75^{th} percentile would be used to test the arm’s length nature of the transaction.

1.4 Use of multiple year data

Rule 10B(4) as notified provides that the the data to be used in analyzing the comparability of an uncontrolled transactions with an international transaction or a specified domestic transaction will be:

(i) the data relating to the current year ; or

(ii) the data relating to the financial year immediately preceding the current year, if the data relating to the current year is not available at the time of furnishing the return of income by the assessee , for the assessment year relevant to the current year

- Further data of the current year, shall be used during the transfer pricing audit if it becomes available at the time of assessment.

- The above para prescribes the use of "Multiple year data" concept in case of only three methods viz. the Transactional Net Margin Method, Resale Price Method, or Cost Plus Method

Issues

- Requirement of use of the financial data of comparable companies which is not available in the public domain on or before the specified date, but which becomes available subsequently by the time of assessment, will not be in line with the contemporaneous documentation requirement under the Indian TP provisions.

- There is no clarity whether at the time of assessment, the data of the current year can be used by both the taxpayer and the department.

- The notifications provide for use of data of current year or the data relating to the financial year immediately preceding the current year. However in the illustration provided to the notification, data of current year and immediately preceding two financial years is used. Hence there is an ambiguity.

- Also use of data of current year and 2 preceding years is not in line with the global best practices which allow three years data to be used excluding current year's data.

- In cases of overseas tested party, which follow rules for data as per their respective jurisdictions (eg. previous three years data), it will be an issue to get and accordingly, use the current year data , which would not be available

Recommendation

- Taxpayer should be allowed to use data of prior three years (not including current year), which is available in the database at the time of preparation of TP documentation. Also it should be extended to CUP, PSM and Other method as well.
- The data of current year can be used only if it is available at the time of preparation of TP documentation and not subsequently at the time of assessment.
- The provision that use of data of the current year can be used during the transfer pricing assessment if it becomes available should be done away with as by that time pricing and commercial arrangements would have already been set keeping in mind the data available.
- The benefit of multiple year data should also be made available to past years whose assessment proceedings have not yet been completed i.e for FYE 2012, FYE 2013 and FYE 2014.

2. ABSENCE OF ARTICLE 9(2) IN DTAAS RESTRICTING BILATERAL APAS AND MAP

Issue

India does not have Article 9(2) in its DTAAs with certain major trading partners including Belgium, Germany, France, Singapore and the Republic of Korea. In the absence of Article 9(2),

The Competent Authority of India has so far followed the practice of not admitting cases of economic double taxation under its MAP and as per the guidance note, the tax administration would apply similar position to the APA program.

Pursuant to the same, Indian tax authority disallow negotiation of bilateral APA's in case an Indian entity having an associated enterprise in such countries. Mutual agreement procedures (MAP) negotiations are also disallowed in such countries.

Further, the OECD commentary provides even if a bilateral tax treaty does not contain the provisions of corresponding adjustment in TP matters, in the form of Article 9(2), the two sovereign States can still mitigate double taxation arising out of TP adjustments by allowing corresponding adjustments, through invoking Article 25(3). In this regard too, India, (which has the status of an observer nation to the OECD MC of 2010), has reservations with the mechanism of granting corresponding adjustment in TP matters through invoking Article 25(3).

Indian views are driven from the understanding that OECD Model Tax Conventions do not represent internationally agreed guidance and have suggested that an Inter-Governmental Commission with a balanced representation from the Governments of developing and developed countries should be construed to take decisions with regard to these provisions.

Recommendation

There is a need for deliberation and industry consultation in this regard and Government should advise companies on how to address the challenges arising due to absence of certain provisions in the tax treaties. This would also ensure a continuing trade relation with important trade partners of India, namely Singapore, Germany, France, and the Republic of Korea.

3. CONCERNS ON APA ROLL BACK PROVISIONS IN CASES OF DTAAs COMPRISING ARTICLE 9 (2)

Rule 10 MA(3) of the APA rollback rules provides as follows: "Notwithstanding anything contained in sub-rule (2), rollback provisions shall not be provided in respect of international transaction for a rollback year, if – ….(ii) the application of rollback provisions has the effect of reducing the total income or increasing the loss, as the case may be, of the applicant as declared in the return of income of the said year.

The above position of rollback is not justified in the case of bilateral APA applications wherein the treaty itself provides for corresponding deduction in the other contracting state for avoidance of double taxation, i.e., Article 9(2).

Recommendation

We recommend that suitable modifications be made in the rules, to allow rollback provisions which has the effect of reducing the total income or increasing the loss of the applicant for the relevant year.

4. RISK BASED ASSESSMENT AUDITS

In relation to transfer pricing audits, presently a transaction value threshold is being adopted by the Revenue for case selection; this should be replaced by an objective risk based assessment approach which may be set out through instructions/circulars on an annual basis. Although the recent Instruction No. 8/2015 issued on October 16th, 2015 sets out that the Assessing Officer should apply more discretion in referring cases for scrutiny by the Transfer Pricing Officer, it will be helpful if some criteria or parameters are laid out based on which a referral could be made.

A transaction value based audit approach is not always an indicator of the need for scrutiny for such transactions and should be supplemented with some qualitative criteria for case selection.

Further, it is observed that despite the well-articulated clarity in the rationale behind the Transfer Pricing provisions, the assessing officers are arbitrarily and/or mechanically invoking the transfer pricing provisions even in cases where the assessees are eligible for tax relief's u/s 10A/10AA or have related party transactions with well-regulated tax jurisdictions. In relation to the same we suggest that Transfer Pricing provisions shall not be invoked against tax payers who are entitled to tax holidays (section 10A/10AA reliefs) in India.

5. SAFE HARBOUR RULES NOT EFFECTIVE FOR THE SECTOR – NEED FOR RATIONALISING THE MARGINS

Issue

Currently, the margins notified under the safe harbour vary from 20 to 30 percent depending on the characterization of the entity. Redefining safe harbour margins, which have so far remained ineffective, should be undertaken on a priority to encourage uptake by Industry and will help Small and medium size companies in easing regulatory compliance.

The margins are high and not reflective of the business realities. Hence, very few companies in the IT sector have opted for the safe harbours.

We believe that the current safe harbour margin have been determined on the basis of the margins determined by the Revenue authorities in transfer pricing audits. And that tax payers' propositions and rationalization of margins by higher appellate authorities (through elimination of outliers and functionally different companies) have not been considered in arriving at the safe harbour. Therefore the current safe harbour do not reflect the arms' length price. (ref table)

Assessment Year	Mark-up arrived by IT companies	Mark-up arrived by ITeS companies
2007-08	10 to 15 %	10 to 15 %
2008-09	13 to 18 %	13 to 18 %
2009-10	13 to 18 %	13 to 18 %
2010-11	5 to 20 %	6 to 18%

2011-12	5 to 20 %	6 to 18%

Safe Harbors potentially offer significant compliance relief to small and medium companies. While larger companies would typically choose advance price agreements (APA), safe harbors are the only recourse for smaller companies. Unfortunately the current safe harbor margins are high and unrealistic, depriving small and medium sized companies of regulatory ease.

Recommendation

It is recommended that more practical and feasible margins, that are reflective of the ALP be notified under the safe harbour rules, especially after taking into account the rationalization of margins by the higher appellant authority.

6. CONTINUED AGGRESSIVE ASSESSMENTS

The Indian IT Industry has been facing several unwarranted assessments on account of transfer pricing adjustments. While the APA program has taken off, and companies are considering adoption, the Safe harbour notifications have had limited uptake. Therefore most companies have had to resort to TP assessments. Some of the continuing dispute areas are as follows:

- Criteria for Identifying comparables and filters adopted

Tax authorities continue to pose problems by adopting different criteria of selecting comparables for benchmarking. Functional, assets, risk profile and the prevailing business conditions are not being considered appropriately for e.g. the marketing set employed by the tax authorities seemed to revert more towards commission agents, insurance and broking sets as was utilized 2 years ago in spite of the tribunal having rejected commission companies while identifying comparable companies.

Further, filters adopted by the authorities across jurisdictions are ignoring business conditions. For e.g., companies earning supernormal profits (margins 50% to 80%) and industry giants are used as comparables. Companies with declining sales for the last 3 years are being rejected as comparables despite taxpayers excluding companies with continuous losses in last 3 years in their comparator set.

- Recent rulings / DRP decisions overlooked

Recent rulings and judgments passed in favour of the taxpayers overlooked e.g. Adjustments made on outstanding inter-company receivables despite ITAT judgments supporting the fact that no such adjustments are warranted. Imposition of cap on working capital, continued use of very high turnover companies in marketing sets where tribunal orders are not being regarded.

7. AMBIGUITIES IN DOMESTIC TRANSFER PRICING

Issue

The Finance Act 2015 increased the threshold for applicability of Domestic Transfer Pricing from INR 5 crores to INR 20 crores. However ambiguity around some provisions like directors' remuneration and associated comparables continues and we urge clarifications maybe issues at the earliest.

- The term "specified domestic transaction" includes any expenditure in respect of which payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A of the Act. Such expenditure could possibly include capital expenditure made to such a related person. It should therefore be clarified that these provisions pertain to revenue expenditure only.
- Domestic transfer pricing provisions should apply only in transactions involving income escaping tax and not in case tax neutral transactions i.e. where there is a transaction between two entities both of which are tax paying, such a transaction will be tax neutral since a deduction in the hands of one entity will automatically be taxed in the hands of the other entity. Hence in such a case, domestic transfer pricing provisions should not apply and there should be a specific exemption introduced in the law to this effect.
- This amendment also covers a scenario wherein the payment of remuneration by the company to its director or relative of such directors is also required to be at arm's length. The same casts an onerous responsibility on the company vis - à- vis justification of the arm's length nature of such payments.
- Further, there is ambiguity in relation to the definition of the term 'closely connected persons' as described in section 80IA (10) of the Act, a suitable clarification should be provided in this regards.

Recommendation

(i) Necessary guidance for benchmarking directors' remuneration should be provided, as by the nature itself these could be very peculiar transactions depending on the extent of ownership, technical ability, seniority etc.

(ii) The amendment relating to domestic transfer pricing provisions applicable to all those companies considered as related parties under section 40A(2)(b) of the Act seeks to cover a situation wherein there could not be any loss to the exchequer. The same is not in line with the suggestion provided by the Supreme Court in case of Glaxo SmithKline. The Supreme Court had provided the situation wherein transfer pricing should be applicable in case of transactions between a profit making and a loss unit / company. The other scenario which was envisaged by the Supreme Court was transactions between units / assesses having different tax rates. Other than the scenarios contemplated above, a corresponding adjustment should be allowed and hence provided for on the statue.

(iii) It should be suitably clarified that the transfer pricing provisions would only apply to revenue expenditure referred to in section 40A(2)(a) of the Act, and not to all payments made to persons specified in section 40A(2)(b) of the Act.

(iv) The words “close connection” appearing in section 80-IA(10) of the Act needs to be clarified to avoid ambiguity in the application of provisions of section 92BA of the Act.

(v) Further, clarity should be provided with regard to inter-unit allocation of costs between eligible and non-eligible units i.e. whether corporate cost allocations from a non-tax holiday unit of a company to a tax holiday unit of the same company would get covered within the provisions of Section 80-IA(8) and consequently need to be reported as a specified domestic transaction.

(vi) The Advance Pricing Agreement (APA) provisions are being made applicable to only international transactions. The same should also be made applicable to domestic transactions covered by Transfer Pricing regulations.

8. GUIDELINES FOR CERTAINTY AND CONSISTENCY

Issue

Currently, there is substantial ambiguity in case of Headquarter and regional Headquarter cost allocations being rendered by the overseas affiliate to the Indian entity. Further, in case of comparability adjustments there is a lot of ambiguity with regard to methodology, application, quantification etc.

This can be substantially reduced if the Board issues appropriate guidelines giving due consideration for the factors involved.

Recommendation

Guidelines can be issued by the Board giving due consideration for the following factors:

8.1 Inter-company Loans

i. Intention for advancing of interest free loans, especially in case of ‘quasi-equity’. A loan which is ‘quasi-equity’ should be regarded as equity and there should not be requirement for charging interest on such loans.

ii. Role of lender of loan especially when loans are rendered under parental role / shareholder’s activity. If the loans are provided out of surpluses of the Indian parent and they are supporting the parental role / shareholder’s activity, there should not be requirement for charging interest on such loans.

iii. Commercial reasons and inherent business benefits in terms of enhanced business

iv. Global practices for benchmarking interest rates to be charged, if any, by considering comparable interest rates prevailing in the borrower’s country (e.g. LIBOR for loans given from India to European AEs)

8.2 Guarantee / Letter of comfort / Undertaking

i. Business rationale in terms of future benefit received by the company providing guarantee

ii. The association of the parent company for securing contracts as a group should not be construed as resulting in international transactions between the Indian Company and the overseas subsidiary;

iii. Arm’s length price, if computed, should be on the basis that benefits to be secured are reduced from the price of such assurances in comparable uncontrolled transactions.

8.3 Headquarter and regional Headquarter cost allocations:

i. Absence of industry benchmarks in public domain to test management payouts.

ii. Guidance on specific documentation to be maintained elaborating costs incurred and the benefits received.

8.4 Adjustments for differences in functions and risks

i. Clear guidelines on carrying out economic and risk adjustments with proper methodology.

ii. Revenue authorities to give due consideration to business strategies and commercial realities such as market entry strategies, market penetration, and non-recovery of initial set-up costs, unfavourable economic conditions and other legitimate business peculiarities while determining the arm's length pricing

8.5 Restructuring

A comprehensive guidance or definition on what types transactions will be covered under restructuring or reorganizing (such as conversions and transfers that have cross-border impact) and the detailed reporting and benchmarking requirement be specifically laid down.

Section 92B considers a transaction of business restructuring or reorganization as an international transaction. However, there is no definition of restructuring or reorganization in the Act. Accordingly, there exist an ambiguity as to what transactions gest covered under business restructuring or reorganization. In addition, there is no clarity as to whether a transaction of business restructuring or reorganization would need to be reported if the act of business restructuring results in the enterprises becoming an AE.

9. TP DOCUMENTATION THRESHOLD

Issue

For aggregate value of transactions exceeding INR 10 million, TP documentation is required.

This monetary threshold prescribed for TP documentation has not been changed since the introduction of TP Regulations in the Income-tax Act, 1961. Further, given the ever increasing quantum of cross-border transactions, the prescribed limit seems to be on the lower side especially in case of software companies as software transaction values have increased manifold, requiring almost all companies in this sector to maintain onerous documentation.

Recommendation

Upward revision in monetary limit is required as software transaction values have increased, requiring almost all companies to maintain onerous documentation.

10. CHANGES IN DISPUTE RESOLUTION PANEL

Section 144C was introduced w.e.f. 1-4-2009 and deals with reference to DRP as a pre-assessment statutory requirement. With Section 144C providing that the DRP shall be constituted by the Board as a collegium three Commissioners of Income-tax, a statutory framework is provided for senior officials to take objective decisions. Section 253 is amended w.e.f. 1-7-2012 to provide that the directions issued by the DRP u/s 144C(5) is appealable before the ITAT. The over-arching objective of making a referring the draft assessment order to the DRP is to resolve the disputes and arrive at finality.

Issue

a) Though the right of appeal to the ITAT is provided for objections filed on or after 1st July 2012, the DRP is still not serving its central purpose i.e. dispute resolution. The DRP directions for objections filed after July 1, 2012 also tend to follow the earlier DRP directions, which were issued when there was no right of appeal.

b) The CIT/DIT have been discharging their duties/ functions of DRP in addition to their regular duties, and are accordingly constrained. Thus, the important task of resolving disputes of assessees receives only a divided attention and impairs independence.

Recommendation

- DRP should constituted as an 'independent' judicial board, much like the Approving Panel for Advance Pricing Agreements. Rather than comprising of only revenue officials who are duty-bound to meet revenue collection targets, the DRP should have panellists from economic, legal or accounting background and with knowledge of income tax matters.
- In order to avoid cases of actual or perceived bias and to ensure objectivity in the dealing of cases, specific provisions may be inserted to restrain a jurisdictional Commissioner/ Director from being appointed as a member of the DRP hearing cases falling within his/ her jurisdiction. This view was also endorsed by the recent judgments[1].

11. LEVY OF PENALTY ON SINGLE TRANSACTION TO BE RATIONALIZED

Issue

Currently, there are multiple provisions for levy on penalty on a single transaction. Accordingly, in the Act, there are penalties for the following:

- Section 271AA: Failure to keep and maintain information and documents;
- Section 271 BA: Penalty to furnish report from accountant; and
- Section 271 G: Penalty for failure to furnish information or document under section 92D.
- The same results in multiple penalty being levied for the same default or non--compliance.

Recommendation

Penalty provisions are implemented with the intention to get the tax payer to adhere to the provisions of the Act rather than cause considerable hardship. Accordingly, it is recommended that a single penalty be levied on non-compliance of a provision to avoid duplication of penalty. For e.g., Section 271AA imposes 2 percent penalty on transaction value in the event of failure to keep and maintain information and documents under section 92D. Section 271G again imposes 2 percent penalty on failure to furnish the information or documents maintained under section 92D. In the event that a tax payer has not maintained

[1] *Hyundai Heavy Industries [2011-T11-28-HC-UKHAND-INTL]*
Huntsman International (India) Limited 23 taxman.com 52 (Mum)
Lionbridge Technologies Private Limited [2012] 51 SOT 40 (Mum)

the documents, such taxpayer should be penalized only under section 271AA and not under both section 271 AA and section 271 G.

Further, penalty should not be imposed for non-reporting of transactions which gets covered under the purview of international transaction by virtue of retrospective amendments, due to impossibility of performance.