

ADVANCED PRICING AGREEMENT (APA) ROLL BACK PROVISIONS

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The Advance Pricing Agreement provisions were introduced in 2012 through insertion of sections 92CC and 92CD in the Income-tax Act, 1961 by the Finance Act, 2012. Section 92CC of the Act empowers the CBDT to enter into an Advance Pricing Agreement (APA) with any person for determining the Arm's Length Price (ALP) or specifying the manner in which ALP is to be determined in relation to an international transaction to be entered into by such person.

In many countries the APA scheme provides for "roll back" mechanism for dealing with ALP issues relating to transactions entered into during the period prior to APA. Providing of such a mechanism in Indian legislation would lead to reduction in large scale litigations which are currently pending or may arise in future in respect of the transfer pricing matters. Thus, the Finance (No. 2) Act, 2014 amended the Act to provide for roll back mechanism in the APA scheme through sub-section (9A) inserted in section 92CC with effect from 1st October, 2014. Thereafter in March 2015, the CBDT announced Income-tax (Third Amendment) Rules, 2015 to prescribe the conditions, procedure and manner for such roll back mechanism, namely, Rules 10MA and 10RA, vide S.O. 758(E) dated 14th March, 2015. Subsequent to the notification of the rules, requests for clarification regarding certain issues have been received in the CBDT. The CBDT therefore issued FAQs vide Circular No. 10/2015 dated 10th June, 2015, clarifying certain issues.

The salient features of the rules and the clarifications thereon is as follows: -

I. Pre-filing consultation: The request for pre-filing consultation by the person who proposes to enter into an APA has been made optional.

II. Conditions for making an application for APA containing rollback provision:

The APA shall contain the roll back provisions subject to the following conditions:

- i. the international transaction for which the roll back provisions are intended to be applied should be the same as the international transaction to which the APA (other than the rollback provision) applies; The CBDT has clarified that "same" implies same nature of transaction, and undertaken with the same associated enterprise (AE). Also, the underlying FAR (functions, assets and risks) of the transaction should not be "materially" different i.e., the facts and circumstances should not change which could reasonably have resulted in an agreement with significantly different terms and conditions.
- ii. the return of income (ROI) for the relevant rollback year has been or is furnished by the applicant before the due date specified in Explanation 2 to 139(1); It has been clarified by the CBDT that the rollback provisions will be available even in case of revised ROI filed u/s 139(5) of the Act, but not in case of belated returns filed u/s 139(4).

- iii. the report in respect of the international transaction had been furnished in accordance with section 92E;
- iv. the applicability of rollback provision, in respect of an international transaction, has been requested by the applicant for all the rollback years in which the said international transaction has been undertaken by the applicant; An applicant has to choose all the 4 years for rollback, unless, the relevant international transaction did not exist in a rollback year; or the applicant fails the test of the rollback conditions contained in various provisions. In such cases, the Applicant can still apply for rollback for other rollback years.
- v. the applicant has made an application seeking rollback in Form 3CEDA in accordance with the prescribed rule.

III. Prohibition on including rollback provisions:

Rollback provisions shall not be provided in respect of an international transaction for a rollback year, if,-

- a. the determination of ALP of the said international transaction for the said year has been subject matter of an appeal before the Appellate Tribunal (AT) and the AT has passed an order disposing of such appeal at any time before signing of the agreement; However, if the matter has been set aside by the AT for fresh consideration by lower authorities with full discretion at their disposal, the benefit of rollback is still available, or
- b. the application of rollback provision has the effect of reducing the total income or increasing the loss, as the case may be, of the applicant as declared in the ROI of the said year.

IV. Manner of computing ALP:

Where rollback provision specifies the manner in which ALP shall be determined, then such manner ((including choice of Method, comparability analysis and Tested Party) shall be the same as has been determined for future years to which agreement applies, in respect of same international transaction.

V. How to apply for APA containing Rollback provision:

An applicant desirous of entering into an agreement with rollback provision is required to furnish along with the application, request in Form No. 3 CEDA and proof of payment of an additional fee of five lakh rupees.

VI. Applicability of rollback provision to existing agreements or agreements for which application is filed:

Applicant can apply for rollback provision even in those cases in which application for entering into agreement has been filed prior to 1st January, 2015 or where the agreement itself has been entered into before 1st January, 2015. In that case the applicant is required to request for rollback provision in Form No. 3CEDA along with proof of payment of requisite fee on or before 31st March, 2015 (extended to 30th June) or the date of entering into the agreement, whichever is earlier.

VII. Procedure for giving effect to rollback provision in APA:

- a. **Filing of modified return:** A modified return needs to be furnished within a period of 3 months from the end of the month in which the said APA was entered into. The time to file modified return for rollback years will start from the date of signing the revised APA incorporating the rollback provisions.

- b. **Withdrawal of pending appeal:** If any appeal filed by the applicant is pending before the CIT (A), Tribunal or the High Court for a rollback year, on the issue which is the subject matter of the rollback provision for that year, the applicant is required to withdraw the said appeal.
- c. **Cancellation of Agreement:** In case effect cannot be given to the rollback provision, for any rollback year on account of failure of assessee, the agreement shall be cancelled.

VIII. Others

- i. The applicant has an option to withdraw its roll back application even while maintaining the APA application for the future years. However, it is not possible to accept the rollback results without accepting the APA for the future years. It may also be noted that the fee specified in the prescribed rule shall not be refunded in case of withdrawal.
- ii. If rollback provisions are not given effect to in accordance with the prescribed rules, then the entire APA agreement would stand cancelled because the rollback provision has been introduced for the benefit of the applicant and is applicable at its option.
- iii. If a Mutually Agreement Procedure (MAP) has been already concluded for any of the international transactions in any of the rollback year under APA, rollback provisions would not be allowed for those international transactions for that year. However, if MAP request is pending for any of the rollback year under APA, upon the option exercised by the applicant, either MAP or application for roll back shall be proceeded with for such year.
- iv. The ALP for the rollback years would be agreed after full examination of all the facts, including validation of critical

assumptions. Hence, compliance audit for the rollback years would primarily be to check if the agreed price or methodology has been applied in the modified return.

- v. If there is a merger or demerger of a company, the person (company) who makes the APA application would only be entitled to enter into the agreement and be entitled for the rollback provisions. To illustrate, if A, B and C merge to form C and C is the APA applicant, then the agreement can only be entered into with C and only C would be eligible for the rollback provisions. A and B would not be eligible for the rollback provisions. To illustrate further, if A and B merge to form a new company C and C is the APA applicant, then nobody would be eligible for rollback provisions.

Thus, the IT (Third Amendment) Rules, 2015, allow retrospective application of APAs which will benefit the companies to avoid rigorous audits of cross-border transactions and the disputes arising from it. India has already signed five APAs with individual companies and one bilateral APA with a Japanese company and the tax authorities in Japan. These agreements are seen as instruments to ensure tax certainty for MNCs. These roll back provisions would help reduce significantly the number of cases that would go to the dispute resolution panel and subsequent litigation over the next few years.