



Draft scheme for computation of ALP

The Finance Minister in his Budget speech during the introduction of Finance Bill, 2014 had announced that range concept for computing Arm's Length Price (ALP) would be introduced in the Transfer Pricing law in India. It was also announced that use of multiple year data would be permitted for undertaking comparability analysis.

Accordingly the CBDT on 21st May, 2015 has come out with a draft scheme of the proposed rules for computation of ALP on an international transaction or Specified Domestic Transaction on or after 1st April, 2014 and has invited comments and suggestions of stakeholders and general public on the said scheme by 31st May, 2015.

Following is a brief of the draft scheme:

A. Adoption of the range concept:

- i. The Range concept shall be used only in case the method used for determination of ALP is Transactional Net Margin Method (TNMM), Resale Price Method (RPM) or Cost plus Method (CPM).

However the range concept could also be extended to other methods like Residuary Profit Split Method which not prescribe in the draft scheme.

- ii. Selection of minimum 9 comparable companies for being eligible to use the range concept could be a challenge and looks irrational because in certain cases, one may get a number of comparables whereas in other cases, the taxpayer might get only a handful of comparable companies which could be only 2 or 3.

iii. The scheme proposes to use a range between 40th to 60th percentiles. Internationally inter-quartile range of 25th to 75th percentile is accepted and hence the range proposed provides a narrow arm's length range.

Further the scheme does not provide the mechanism for computing the 40 percentile to 60 percentile. There could be different ways of arriving at the percentile. Adoption of different methods might lead to further litigation.

B. Use of Multiple Year Data:

- i. The multiple year data would be used only in case determination of ALP is by TNMM, RPM or CPM;
- ii. Option of using 2 out of 3 years data has been given if the current year data is not available in the database or a comparable fails to clear a quantitative filter or if the comparable is a newly set-up comparable company. However if the current year data is available and the earlier years then that comparable has to be excluded.

It is a welcome step by the Govt. of India to introduce the above concepts in the law of Indian Transfer Pricing Regulations; however it would be appreciated if the ambiguities contained in the proposed scheme be looked upon and appropriate guidance issued to provide a much needed roadmap in the transfer pricing law in India.

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