

India Aims to Make Peace With Multinationals Through Tax Deals

BNA Snapshot

- More companies approach Indian tax authorities on intercompany pricing pacts
- India launched its Advance Pricing Agreement program in 2012

By Benjamin Parkin

Foreign companies eager to do business in India are flocking to sign up to a tax program designed to avoid the notoriously long and costly transfer pricing lawsuits that have tied up other multinationals. But the optional program is burdened by growing backlogs and wait times. Companies applying to negotiate pacts to lock in their tax rates for moving money out of their Indian operations—known as advance pricing agreements (APAs)—rose 66 percent to 168 applications in the 2017-18 year, according to a report from India's tax department. The number of applications for bilateral deals, which involved tax authorities in the U.S. and elsewhere, more than doubled.

The average time taken to complete a unilateral APA involving the Indian tax authorities, however, rose to average a little over three years—at 39 months. The time taken for bilateral deals rose to nearly four years.

Countries' transfer pricing rules typically require a multinational company to treat the sales of goods and services between subsidiaries as if they were independent businesses, to ensure that those transactions occur at market rates. APAs set in stone a company's intercompany pricing for future years providing tax certainty.

Countries are clamping down on how multinational companies price their intercompany sales because many tax authorities consider the prices charged often amount to a form of tax avoidance, as businesses can siphon off profits into lower tax countries by moving money between their international units.

The principles of transfer pricing are used when individual units of a larger multi-entity company are treated as being separately run.

Avoiding Expensive Disputes

Practitioners told Bloomberg Tax the six-year-old APA program has helped attract more companies to India and increased confidence that they can avoid becoming trapped in expensive cases.

WNS Holdings Ltd., a business process management company, negotiated a five-year APA with India authorities from 2013. The company said this year it applied to renew the pact for another five years from April 2018.

"There's a lot of backing for the APA program," said Meyyappan Nagappan, leader of the international tax team at Nishith Desai Associates in Mumbai. APAs "will go a long way to provide certainty, expansion and bring more money and trade to India."

Indian tax officials have tried to shed a reputation for an adversarial approach toward multinationals, fostered by a series of high-profile disputes with the likes of Vodafone Group Plc and Nokia Corp.

And multinationals like Microsoft Corp., LG Electronics Inc. and Canon Inc. had previously been embroiled in transfer pricing disputes with India over their practices.

Tax Certainty

India launched its APA program in 2012, a little over a decade after introducing laws to deal with transfer pricing.

India's APA program gives businesses an opportunity to agree on its transfer pricing practices with tax officials for up to five years into the future and four years retroactively, helping to pre-empt disputes.

The number of total applications for APAs swelled from 146 in the first year to 985 in 2017-18, according to government figures. A total of 219 of those had been completed, according to the government, although the companies are rarely revealed.

"The APA Programme exemplifies the Government's commitment to establish and nurture a non-adversarial approach to taxation," Shabri Bhattasali, a member of India's tax department, wrote in a report.

Back-Office Services

Nearly 70 percent of APAs completed in 2017-18 came from the service sector, the government said, with the largest share of those in IT, followed by banking and finance. Practitioners said the importance of those sectors in attracting foreign investment to India makes APAs a particularly useful tool.

Interest in bilateral deals, which bring in tax authorities like the U.S. Internal Revenue Service, is particularly high, practitioners said, given the added certainty those agreements provide. A third of bilateral applications involve the U.S, where many companies are looking to expand into India. Indian IT company Infosys Ltd., meanwhile, went the other way, saying earlier this year it signed an APA with U.S. authorities.

Indian authorities have lauded APA's success in increasing the ease of doing businesses in the country. Foreign companies had previously faced waves of litigation, practitioners said, as tax authorities scrutinized and penalized their practices. Practitioners said some companies floated moving back-office operations to countries like the Philippines because of costly disputes with the Indian tax authorities.

"Several multinationals were apprehensive," said Anuj Khorana, a partner at EY. The APA program "has brought back the confidence."

An Overwhelmed System?

Some practitioners working on APAs, however, said the system is becoming overwhelmed. The number of APAs signed fell 24 percent, to 67 in 2017-18, according to government figures. They attribute that to the increasing time taken to finish a deal and the growing list of applicants. The delays can add to costs as companies contract lawyers and others, as well as prompt them to ease off investment and expansion in India while their tax situation remains uncertain.

The time taken to complete a pact "doesn't give the confidence that the APA is moving with the efficiency and smoothness that it ought to be," said Mukesh Butani, a partner at BMR Legal. He said he had "mixed sentiments" about the program.

Four commissioners and their teams handle India's APAs, which practitioners said leaves a small number of people trying to work through the nearly 700 pending applications.

Butani and other practitioners said Indian authorities remain overly adversarial in their approach, demanding high tax payments that companies are loathe to accept. That in turn slows down the program further, they said. With the early APAs up for renewal, practitioners said bolstering manpower and streamlining the program is crucial.

"The success of this program depends on having good manpower," said Nitin Narang, transfer pricing partner at Nangia Advisors LLP. "All of this would take a lot of coordination from the top."

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