

# Tax Hotline

January 13, 2005

## AAR DENIES RULING ON A TRANSFER PRICING APPLICATION

Recently, the Indian Advance Ruling Authority ("**AAR**") had an opportunity to adjudicate upon transfer pricing questions raised for the first time in an advance ruling application by Instrumentarium Corporation ("**the Applicant**"), a Finnish resident. The AAR stated that adjudication on the issue raised by the Applicant was outside its scope and that the Applicant would be required to adhere to the Indian transfer pricing regulations.

The Applicant had given interest-free loan to its wholly owned subsidiary ("**Datex**") in India and raised, inter alia, the question before the AAR that applying arm's length price to this transaction would be detrimental to the Indian revenue base and hence this transaction should be outside the purview of the Indian transfer pricing regulations .

The Applicant contended that the fact that the loan was an interest free loan would work out to the benefit of the Indian Tax Authorities since under the India-Finland Double Taxation Treaty ("**Treaty**") any interest income of the Applicant would be taxed at a concessional rate, while under the Income Tax Act, 1961 ("**ITA**") the income of Datex would be taxed at the rate of 35%. This argument sprung from the fact that the interest free loan would enhance the profits of Datex and would thus increase the taxes collected in India on the transaction. The Applicant relied on Section 92(3) of the ITA which states that the transfer pricing provisions would not apply if the transaction carried out between two parties would lead to the erosion of the taxable revenue in India, if carried out at an arm's length. The Applicant also relied on the non-discrimination provisions under the Treaty and stated that as transfer pricing provisions did not apply to transactions between two Indian residents, applying them to the Applicant would be discriminatory.

The AAR held that the question raised did not relate to tax liability of the Applicant arising out of this transaction but related to consequences of implementation of transfer pricing provisions on the Indian exchequer. Therefore, the AAR was not bound to rule on the same. The AAR further held that even if the impact of applying arm's length price between two parties was detrimental to the tax revenue, it was for the income tax authorities to determine the same and thus allow the parties to the transaction not to carry out the same at an arm's length price and not the AAR.

The AAR also dismissed the non-discrimination contention raised by the Applicant and stated that non-discrimination provisions can only be invoked by the nationals (i.e. individuals) of the contracting states and not by a company. The AAR held that in any case, it was not open to either the Applicant or the AAR to determine the issue of the applicability of the transfer pricing provisions under ITA and the same would have to be determined by the income tax authorities at the time of assessment of Datex. The AAR took the view that determination of arm's length price involves determination of fair market rate of interest and that the same is outside its purview. Accordingly, the AAR stated that it cannot give a ruling on this issue. However, it ruled that the Applicant would be required to adhere to the transfer pricing regulations under the ITA.

It must also be borne in mind that an advance ruling is binding only on the parties to the ruling. As regards third parties, such a ruling would have only a persuasive value. This decision does not throw sufficient light on the ability of foreign companies to seek advance ruling on the applicability of transfer pricing provisions in India.

*Source:* Judgement of AAR in the matter of INSTRUMENTARIUM CORPORATION (A.A.R. No. 609 of 2003)

## DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

## Research Papers

### Medical Device Industry in India

April 28, 2025

### Clinical Trials and Biomedical Research in India

April 22, 2025

### Structuring Platform Investments in India For Foreign Investors

March 31, 2025

## Research Articles

### 2025 Watchlist: Life Sciences Sector India

April 04, 2025

### Re-Evaluating Press Note 3 Of 2020: Should India's Land Borders Still Define Foreign Investment Boundaries?

February 04, 2025

### INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

## Audio

### CCI's Deal Value Test

February 22, 2025

### Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

### Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

## NDA Connect

Connect with us at events, conferences and seminars.

## NDA Hotline

Click here to view Hotline archives.

## Video

Vyapak Desai speaking on the danger of deepfakes | Legally Speaking with Tarun Nangia | NewsX

April 01, 2025

**Vaibhav Parikh, Partner, Nishith  
Desai Associate on Tech, M&A, and  
Ease of Doing Business**

March 19, 2025

**SIAC 2025 Rules: Key changes &  
Implications**

February 18, 2025