



Union Budget 2025-26

Transfer Pricing Perspective

February 2025

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Background

The Finance Minister presented the Union Budget for 2025-26 on 01 February 2025. To power the growth of the economy, the budget laid four engines viz., Agriculture, MSME, Investment & exports, fueled by reforms. The budget speech featured a major transfer pricing update on introduction of Transfer pricing audit / assessment of arm's length price for multi-year period.

The alert covers the detailed Transfer Pricing related proposals in the Finance Bill, 2025.

Transfer Pricing Updates

A. Rationalisation of TP audit: Introduction of multi year arm's length price determination

Currently, transfer pricing assessment / audit is undertaken by the Transfer Pricing Officer (TPO) (u/s 92CA of the Income-tax Act, 1961) on the reference from Assessing Officer (AO). The tax department has observed that in several transfer pricing assessments, the nature of international transactions or specified transactions are similar for various years, with the same associated enterprises ('AE'), quantum of transactions etc. For these very similar international transactions / specified domestic transactions, the same arm's length price determination takes place during each of the assessments.

To ease the burden of taxpayers and tax authorities, the TP audit is intended to be rationalized through the introduction of multi-year arm's length price ('ALP') determination. Taxpayers will be given an option to elect for the TPO to determine the ALP for multi-year period i.e., applying ALP for year under consideration for the two consecutive years. The following amendments are considered for implementation of multi-year period TP assessment:

1. Taxpayer would be required to exercise the option for multi-year period TP assessment before the TPO.
2. Within one-month period, TPO to pass an order to determine if exercise of the option is valid, as per the prescribed conditions.
3. Where the exercise of the option is deemed valid by the TPO:

- i. ALP determined for the said year will be applicable for next two consecutive years as well.
 - ii. TPO shall pass the order for the two following consecutive years for the similar transactions
4. AO shall recompute the income for the taxpayer through amending the Assessment Order in conformity with the TP order passed by the TPO or after taking into account the directions by Dispute resolution panel ('DRP'), as the case may be.
5. For the consecutive years, re-computation timeline is within 3 months from the end of the month in which assessment for the year under consideration is completed.
6. Where the Assessment Order / intimation as per 143(1) is not made within the above 3-month period, for the two consecutive years, the re-computation will have to be undertaken within a period of three months from the end of the month in which such Assessment order / intimation is made for the respective year.
7. After the TPO passes the order for said two consecutive years, no reference for determination of arm's length price shall be made for the said transactions.

The following existing provisions will be applicable where taxpayer opts for multi-year period:

- Where the TPO enhances the income in the TP order, deduction u/s 10A or 10AA or 10B or under Chapter VI-A will be disallowed.
- The TP order of the taxpayer has resulted in a decrease in the income for AEs, and the said income of AE shall not be recomputed.

CBDT is conferred with powers to make guidelines in connection with the above multi-year period TP assessment, subject to approval of Central Government.

Chapter XIV-B of the Income-tax Act, 1961 covers the procedural aspects w.r.t. search proceedings and assessment, which covers the concept of block-assessment for 6 years. The proposed amendment provides that the aforementioned multi-year TP assessment would not apply to the proceedings under chapter XIV-B of the Income-tax Act.

This above amendment would be applicable for financial years commencing FY 2025-26 (AY 2026-27).

B. Expansion of 'Safe harbour rules'

Safe harbor rules ('SHR') are the provisions in Indian transfer pricing regulations that allow the taxpayers to adopt simplified methods for determining the ALP for the international transactions undertaken by the taxpayer with its AEs.

In the Budget speech, it was proposed that the SHR will be expanded with an intention:

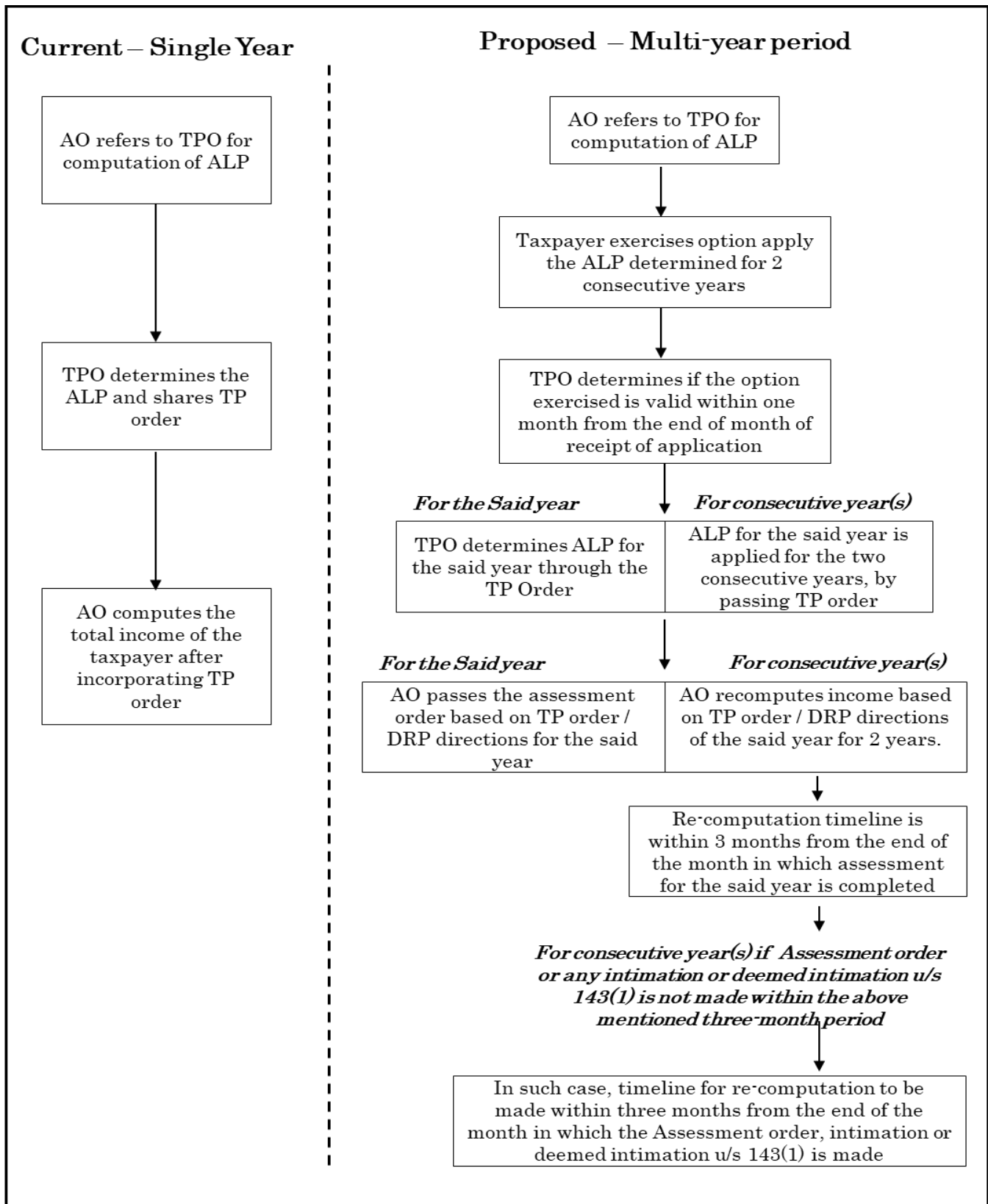
- To provide greater tax certainty in relation to the international transactions; and
- To minimise protracted tax litigation

The notification from the CBDT on the revised SHR is awaited.

C. Faceless scheme

The last date for notifying faceless schemes by the Central Government (i.e., 31 March 2025) for TP assessment proceedings before the TPO, DRP and Income-tax Appellate Tribunal is proposed to be omitted.

The pictorial summary of determination of arm's length price for 'multi-year' period is provided below:



Our views

With regard to multi-year ALP determination, at this juncture the finance bill provides only a broader framework and there exists ambiguity on the procedural mechanics. Hence we may expect some clarity from the CBDT in the rules. Some areas which require more clarification are:

- The Budget speech mentions determination of ALP for “block period” of three years, the concept of which is prevalent in some of the developed countries including TP regulations of USA and Singapore¹. However, the concept discussed in the developed countries is akin to ‘term test’, where the determination of the arm’s length price is done in a consolidated manner for the said 3 years, rather than testing the arm’s length price for each year individually. In certain cyclical phases, the business might earn profits in excess of normal profits for two years and lesser than arm’s length profit for one year. During regular TP audit, adjustment would be done for year of loss, and the excess profits of the other years cannot be considered / adjusted. However, when the three year is considered in aggregate / in toto, the profits earned for all the three years would be considered to be at arm’s length.

Though the budget speech intended to align with global best practices of “block period” for ALP determination for 3 year period, the current proposal provides for leveraging the arm’s length price of one year for the following two years, where the facts and circumstances are similar for the next two years. The benefit of the proposal is limited to reduction of assessment proceedings before the TPO for the next two years, and does not provide complete / wholistic benefit of conducting of TP audit for three years – through considering it as one time period. Though the detailed rules for implementation of the multi-year assessment is awaited, the current proposal in the budget is not in alignment with global practices of “term testing” approach.

- The sections and rules relating to maintenance of contemporaneous documentation i.e., Section 92D and Rule 10D have not been amended to provide that documentation need not be maintained for the subsequent two years. Therefore, current annual compliances will apply for the subsequent two years as well.
- The amendment to Section 92CA emphasises on arm’s length price determination of “similar transactions” (i.e., international transactions undertaken by the Assessee in the previous year and two consecutive years following the previous year), whereas there is no specific mention about the international transactions for which the taxpayer has not opted for the multi-year ALP assessment. For instance, when the taxpayer has multiple international transactions and has not opted for all of them under the multi-year assessment procedure, whether separate reference will be made by the AO for ALP determination of those transactions or will it escape the TP assessment process?
- The due date / deadline for filing the form for opting the multi-year ALP determination by the taxpayer is not specified. It is expected that the form and time period will be notified by the CBDT in this regard

¹ https://www.irs.gov/pub/irs-apa/apa_study_guide.pdf (page 41 to 45)

https://www.iras.gov.sg/media/docs/default-source/e-tax/etaxguide_cit_transfer-pricing-guidelines_7th.pdf?sfvrsn=26bfb1a6_18 (para 5.117)

- While the bill specifies the timeline for the TPO to analyse and declare the validity of the option exercised by the taxpayer (i.e., within one month from the end of the month in which such option is exercised by the taxpayer), the timeline for determination of the ALP for the three year is not prescribed. Hence it is not clear if the ALP determination for the consecutive two years would also need to be completed within the timeline for completion of TP assessment of the relevant previous year itself.
- Whether the taxpayer will be provided sufficient opportunity to position itself better considering the determination of ALP by the TPO for the previous year will have an impact not only on that specific year but also on subsequent two years

Nevertheless, considering instances of repetitive annual audits that results in the prolonged disputes, the multi-year ALP determination is a welcome move as this is expected to reduce the administrative and compliance burden for taxpayers and revenue. However, taxpayers would reap complete benefit / avail holistic relief where the concept of 'block period' or 'term testing' is implemented, similar to countries where TP practice is more developed / matured.

Having said that, before exercising this option one needs to pay attention to certain critical aspects such as nature of its business, probable international transactions to be entered into with its AE in the near future, the magnitude of information which might be called for, etc.,

About us



VSTN Consultancy Private Ltd is a boutique Transfer pricing firm with extensive expertise in the field of international taxation and transfer pricing. VSTN Consultancy has been awarded by International Tax Review (ITR) as Best Newcomer in Asia Pacific – 2024 and is recognised as one of the finest performing transfer pricing firms.

Our offering spans the end-to-end Transfer Pricing value chain, including design of intercompany policy and drafting of Interco agreement, ensuring effective implementation of the Transfer Pricing policy, year-end documentation and certification, Global Documentation, BEPS related compliances (including advisory, Masterfile, Country by Country report), safe harbour filing, audit defense before all forums and dispute prevention mechanisms such as Advance Pricing agreement.

We are structured as an inverse pyramid where leadership get involved in all client matters, enabling clients to receive the highest quality of service.

Being a specialized firm, we offer advice that is independent of an audit practice, and deliver it with an uncompromising integrity.

Our expert team bring in cumulative experience of over six decades in the transfer pricing space with Big4s spanning clients, industries and have cutting edge knowledge and capabilities in handling complex TP engagements.

