

Statement by CBDT on Safe Harbour Rules Under Section 92CB of the Act

In order to reduce the increasing number of transfer pricing audits and prolonged disputes, the Finance (No.2) Act, 2009 w.r.e.f 1.4.2009 inserted a new section 92CB to provide that determination of arm's length price under section 92C or Section 92CA shall be subject to safe harbour rules. Vide this amendment, the Government of India had empowered the CBDT to make Safe Harbour rules. "Safe harbour" was defined to mean circumstances in which the income-tax authorities shall accept the transfer price declared by the assessee.

Thereafter, the issuance of the Safe Harbour Rules was examined and discussed at various points of time, but no finality could be reached. Since a number of representations were received from different stakeholders to prescribe the safe harbour rules, the Prime Minister on July, 30, 2012 approved the constitution of a Committee to Review Taxation of Development Centres and the IT sector consisting of Shri N. Rangachary, Chairman of the Committee and three others (hereinafter called the Rangachary Committee) with broad terms of reference as under:

1. Engage in consultations with stakeholders and related government departments to finalize the approach to Taxation of Development Centres and suggest any circulars that need to be issued.
2. Engage in sector-wise consultations and finalize the safe harbour provisions announced in Budget 2010, sector-by-sector. The Committee will also suggest any necessary circulars that may need to be issued.
3. Examine issues relating to taxation of IT sector and suggest any clarifications that may be required

Subsequently, the Government of India vide OM dated 12th September, 2012 approved the considered suggestion of the Rangachary Committee that it may finalize the Safe Harbour Rules in the following sector/ activities:

- (i) IT Sector
- (ii) ITES Sector
- (iii) Contract R&D in the IT and Pharmaceutical Sector
- (iv) Financial transactions-Outbound loans
- (v) Financial Transactions-Corporate Guarantees
- (vi) Auto Ancillaries-Original Equipment Manufacturers

The Rangachary Committee consulted various stakeholders including sector related government departments, NASSCOM, CII, FICCI, ASSOCHAM, ICAI, etc. and submitted six reports on Taxation of Development Centres and IT Sector and other sectors as referred to in the OM dated 12th September, 2013.

On the basis of the recommendations of the Rangachary Committee in the first report on Taxation of Development Centres and IT Sector (which was posted on the website of the income tax department www.incometaxindia.gov.in on 30th June, 2013), CBDT has issued the following circulars:

- Circular No. 1/2013 dtd. 17th January, 2013 on issues relating to Export of Computer Software under sections 10A, 10AA and 10B of the Act.
- Circular No. 6/2013 dtd. 29th June, 2013 on Conditions Relevant to Identify Development Centres engaged in Contract R&D Services with Insignificant Risk.

The Government of India has considered the other five reports of the Rangachary Committee. The major recommendations of the Rangachary Committee have been accepted, with some modifications, and the following decisions have been taken by Government:

(1) Safe harbour for the sectors recommended by the Rangachary Committee shall be applicable for two assessment years beginning from 2013-14.

(2) Safe harbour for various sectors, subject to certain ceilings, shall be as under –

SNo (1)	International Transaction (2)	Circumstances (3)
1.	Provision of software development services other than contract R&D where the total value of international transaction does not exceed Rs 100 crore	The operating profit margin declared in relation to operating expense incurred is 20 per cent or more.
2.	Provision of information technology enabled services other than contract R&D where the total value of international transaction does not exceed Rs 100 crore	The operating profit margin declared in relation to operating expense is 20 per cent. or more.
3.	Provision of information technology enabled services being knowledge processes outsourcing services other than contract R&D where the total value of international transaction does not exceed Rs 100 crore	The operating profit margin declared in relation to operating expense is 30 per cent. or more.
4.	Advancing of intra-group loan to wholly owned subsidiary where the amount of loan does not exceed Rs 50 crore .	The Interest rate declared in relation to the international transaction, is equal to or greater than the base rate of State Bank of India (SBI) as on 30 th June of the relevant previous year plus 150 basis points.
5.	Advancing of intra-group loans to wholly owned subsidiary where the amount of loan exceeds Rs. 50 crore.	The Interest rate declared in relation to the international transaction is equal to or greater than the base rate of SBI as on 30 th June of the relevant previous year plus 300 basis points.

6.	Providing explicit corporate guarantee to wholly owned subsidiary where the amount guaranteed does not exceed Rs. 100 crore.	The commission or fee declared in relation to the international transaction is at the rate of 2 per cent or more per annum on the amount guaranteed.
7.	Provision of specified contract research and development services wholly or partly relating to software development.	The operating profit margin declared in relation to operating expense incurred is 30 per cent. or more.
8.	Provision of contract research and development services wholly or partly relating to generic pharmaceutical drugs.	The operating profit margin declared in relation to operating expense incurred is 29 per cent. or more.
9	Manufacture and export of core auto components	The operating profit margin declared in relation to operating expense is 12 per cent. or more.
10.	Manufacture and export of non-core auto components.	The operating profit margin declared in relation to operating expense is 8.5 per cent. or more.

(3) Safe harbour rules shall not be applicable in respect of an international transaction entered into with an associated enterprise located in any country or territory notified under section 94A of the Income-tax Act, 1961, or in a no tax or low tax country or territory.

(4) Safe harbour rules shall be applicable only where a taxpayer exercises his option to be governed by such rules in a specified form to be furnished before the due date of filing of return.

(5) Where the Transfer Pricing Officer is of the opinion that the option exercised by the assessee is valid, he shall intimate acceptance of transfer price declared by the assessee

to the assessing officer and the assessee within a period of six months from the end of the month in which reference under section 92CA is received from the assessing officer. Where he is of the opinion that the option exercised is not valid, he shall proceed to determine the arm's length price in respect of the international transactions entered into by the assessee in accordance with sections 92C and 92CA without having regard to the safe harbour margin or price as specified in the rules.

(6) A taxpayer opting for safe harbour rules shall not be allowed to invoke Mutual Agreement Procedure (MAP) provided under the relevant DTAs.

(7) Where the safe harbour rules are not applicable in the case of an assessee, engaged in providing contract research and development services with insignificant risks, the Transactional Net Margin Method (TNMM) shall be considered as the most appropriate method for the determination of arm's length price unless it is shown by the assessee that it is not feasible to apply this method in the facts and circumstances of the case.

The draft rules along with the Second to the Sixth report of the Rangachary Committee have been posted on the website of the Income-tax Department. All stakeholders are requested to provide their comments, if any, by 26th August, 2013 to the Director (FT&TR) at her email id batsala.yadav@nic.in