ARM'S LENGTH IN AN AGE OF BASE EROSION: A CRITICAL STUDY OF THE OECD TRANSFER PRICING GUIDELINES AND THEIR APPLICATION IN INDIA

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ABSTRACT

Multinational enterprises (MNEs) increasingly organise their businesses through networks of associated companies located in different countries. Goods, services, intellectual property, finance, data and business risks move within these groups, but the prices assigned to those movements determine how much profit is reported and taxed in each jurisdiction. Transfer pricing is therefore not merely an accounting exercise. It is a central question of fiscal sovereignty, distributive fairness and economic development. When related parties set prices that do not reflect the economic substance of their dealings, profits may be shifted away from the countries where people, markets, infrastructure and productive activity generate value. This process contributes to base erosion and profit shifting (BEPS).

This article critically examines the arm's length principle (ALP), the international standard developed through the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. It explains the legal and economic foundations of transfer pricing, the five comparability factors, functional analysis, accurate delineation of transactions, the most appropriate method rule, and the treatment of intangibles, intra-group services, financial transactions, business restructurings and hard-to-value intangibles. It then analyses the OECD/G20 BEPS project, particularly Actions 4, 8-10 and 13, and the later developments concerning Amount B and the Two-Pillar Solution.

The Indian position is examined through the transfer pricing framework first introduced by the Finance Act, 2001 under Sections 92 to 92F of the Income-tax Act, 1961, and the corresponding provisions of the Income-tax Act, 2025, which came into force on 1 April 2026. The article considers the statutory rules, documentation and reporting duties, the role of the Transfer Pricing Officer, safe harbour rules, advance pricing agreements, secondary adjustments, thin-capitalisation restrictions and dispute resolution. Landmark Indian decisions are analysed to show how courts have addressed the limits of tax administration, the need for evidence-based benchmarking, intra-group services, marketing intangibles and capital transactions.

The central argument is that the arm's length principle remains indispensable but is not a complete answer to modern profit shifting. Its effectiveness depends on reliable comparables, transparent group documentation, the substance of functions and risks, institutional capacity and effective dispute resolution. India must protect its tax base without turning legitimate cross-border commerce into a source of unpredictable litigation. A balanced approach should combine rigorous enforcement with certainty, proportionality, digital capacity and international cooperation.

Keywords: Transfer Pricing; Arm's Length Principle; Base Erosion and Profit Shifting; OECD Guidelines; Multinational Enterprises; Comparability Analysis; Income-tax Act, 2025; Advance Pricing Agreement; Economic Development.

1. Introduction

Imagine an Indian company that manufactures medicines, employs thousands of workers, conducts clinical and regulatory work, and sells products to Indian hospitals. It is part of a multinational group. The Indian company pays a substantial royalty to a related company in a low-tax jurisdiction for the right to use the group's brand and patents. It also pays interest on an intragroup loan, management fees for regional support, and a distribution margin to an overseas affiliate. Each payment may be commercially genuine. But if the royalty is excessive, the loan is structured mainly to generate deductible interest, or the management fee relates to services never actually received, the Indian company's taxable profit may be artificially reduced.

This example captures the central problem of transfer pricing. A multinational group is legally divided into separate companies, but economically it may operate as one integrated enterprise. Independent companies negotiate prices with one another in their own interests. Associated enterprises, by contrast, may coordinate their decisions and allocate income and expenses in a manner that affects the group's overall tax burden. The law therefore asks a counterfactual question: what price would independent enterprises have agreed upon in comparable circumstances?

The arm's length principle is the internationally accepted response. It requires the conditions of transactions between associated enterprises to be consistent with those that would have operated between independent enterprises in comparable circumstances. The OECD Transfer Pricing Guidelines provide a detailed framework for applying this principle. Their purpose is

dual: to protect the tax base by preventing artificial profit shifting and to reduce economic double taxation by providing a common analytical language for taxpayers and tax administrations.

The issue has become more complex in an economy in which value is generated not only through factories and physical assets, but also through software, algorithms, brands, data, research, platforms, networks and access to consumers. A group may legally own an intangible in one jurisdiction while the economically significant development, enhancement, maintenance, protection and exploitation functions are performed elsewhere. A company may provide funding but lack the people and decision-making capacity to control the risks for which it claims a return. Transfer pricing rules must distinguish legal form from economic reality without allowing tax authorities to replace commercial judgment with hindsight.

India is an important jurisdiction in this debate. It is both a major market for multinational enterprises and a provider of services, technology, manufacturing and skilled labour. The allocation of profits between Indian entities and overseas associated enterprises affects corporate tax revenue, investment decisions, employment and the fairness of the tax system. India introduced detailed transfer pricing provisions in 2001 and has since developed a specialised administrative and judicial framework. The transition to the Income-tax Act, 2025, effective from 1 April 2026, makes it necessary to discuss the present law using the new section numbering while explaining the earlier framework for historical cases.

This research proceeds from the proposition that transfer pricing is not simply about finding

the ‘correct’ price. It is about identifying the real transaction, understanding who performs economically important functions, who uses assets, who controls risks, and how the resulting profit should be allocated. The article evaluates whether the OECD framework and its Indian implementation achieve that goal in an era of increasingly sophisticated base erosion.

1.1 Objectives of the Study

- To explain the meaning, objectives and economic significance of transfer pricing and the arm’s length principle.
- To examine the structure, methods and major substantive chapters of the OECD Transfer Pricing Guidelines.

- To analyse how transfer pricing practices can facilitate base erosion and profit shifting.
- To trace India's transfer pricing regime from the 1961 Act to the Income-tax Act, 2025 and the Income-tax Rules, 2026.
- To study leading Indian judicial decisions and their contribution to the interpretation of transfer pricing law.
- To critically evaluate the strengths, limitations and developmental consequences of the arm's length principle.
- To suggest reforms that balance protection of India's tax base with certainty, investment and fair dispute resolution.

1.2 Research Questions

- How does the arm's length principle seek to allocate profits between associated enterprises?
- To what extent do the OECD Guidelines address modern BEPS strategies involving intangibles, services, finance and digital business models?
- How effectively has India incorporated international transfer pricing standards into its domestic tax law?
- Do Indian courts adequately balance revenue protection with commercial reality and taxpayer certainty?
- Can the arm's length principle alone address profit allocation challenges in a digital and highly integrated global economy?

1.3 Research Methodology and Scope

The study adopts a doctrinal and analytical methodology. It relies on primary legal materials, including the OECD Transfer Pricing Guidelines, OECD/G20 BEPS reports, the Income-tax Act, 2025, the Income-tax Rules, 2026, the earlier Income-tax Act, 1961, and reported

Indian judicial decisions. It also uses official materials published by the OECD and the Income

Tax Department. The focus is on the legal and policy framework governing cross-border associated-enterprise transactions in India. The article is not a transaction-specific tax opinion; individual transfer pricing outcomes depend on the facts, contractual arrangements, accounting records and applicable rules for the relevant tax year.

A temporal distinction is essential. Transactions and assessments relating to periods governed by the 1961 Act must be analysed under that enactment and the rules applicable to those periods. From 1 April 2026, the Income-tax Act, 2025 and Income-tax Rules, 2026 provide the current framework. The corresponding provisions are identified below; the new numbering should not be retrospectively applied to earlier assessment years.

2. Definitions and Legal Framework

2.1 Meaning of Transfer Pricing

Transfer pricing refers to the ***price or other conditions*** attached to transactions between ***related or associated enterprises***. These transactions may include the sale of goods, licensing of intellectual property, provision of services, loans, guarantees, cost-sharing arrangements, business restructurings and transfers of business assets. Transfer pricing itself is not illegal. Every multinational group must determine prices for internal transactions. The legal concern arises when the conditions of controlled transactions depart from the conditions that independent enterprises would have agreed in comparable circumstances, resulting in an inappropriate allocation of taxable profits.

2.2 Meaning of the Arm's Length Principle

The arm's length principle requires ***associated enterprises*** to price their transactions as if they were ***independent parties*** dealing with one another under comparable conditions. In simple terms, a parent company should not be able to charge its Indian subsidiary an inflated royalty or interest rate merely because both companies belong to the same group. The comparison is not necessarily with a single market quotation. It requires a careful examination of the transaction, the parties' functions, assets and risks, contractual terms, market conditions and business strategies.

The principle is reflected in **Article 9 of the OECD Model Tax Convention**, which addresses profits that would have accrued to an enterprise but for conditions made or imposed between

associated enterprises that differ from those between independent enterprises. Article 9 also supports corresponding adjustments in appropriate cases to relieve economic double taxation. The OECD Guidelines explain how the principle is to be applied in practice.[1]

2.3 Associated Enterprises

Associated enterprises are entities connected through participation in ***management, control or capital,*** including specified forms of direct or indirect control and economic dependence. The relationship matters because the parties may not have the same independent bargaining incentives as unrelated businesses. Under the **Income-tax Act, 2025, Section 162** defines associated enterprises for the transfer pricing chapter. Its predecessor was Section 92A of the 1961 Act. The detailed statutory tests must be read with the relevant provisions and rules rather than assuming that every commercial relationship automatically creates an associated-enterprise relationship.[2]

2.4 International Transaction and Specified Domestic Transaction

Section 163 of the Income-tax Act, 2025 defines an ***international transaction*** between two or more associated enterprises, one of which is necessarily a non-resident. The statutory concept covers, among other things, purchases, sales, leases and use of tangible or intangible property, provision of services, lending or borrowing, guarantees, cost-sharing and other transactions having a bearing on profits, income, losses or assets. Certain transactions with third parties may also be treated as international transactions where the statutory conditions for a ***deemed international transaction*** are satisfied.[3]

Section 164 deals with ***specified domestic transactions (SDTs).*** Domestic transfer pricing rules were introduced to address specified categories of related-party domestic dealings, particularly where profit allocation could affect tax incentives, deductions or the tax base. The scope and monetary threshold must be checked against the current statutory text and rules for the relevant tax year. A domestic transaction is not automatically covered merely because the parties are related.[4]

[1] OECD Model Tax Convention on Income and on Capital art. 9 (18 November 2025), Models IBFD
[2] Income-tax Act, § 162 (2025)
[3] Income-tax Act, 2025, § 163 (India).
[4] Income-tax Act, 2025, § 164 (India).

2.5 Base Erosion and Profit Shifting (BEPS)

Base erosion occurs when a country's taxable profits are reduced through deductible payments, artificial losses, exemptions or other arrangements that shift the tax base away from the jurisdiction where the economic activity occurs. **Profit shifting** describes the movement of reported profits to jurisdictions with lower or no taxation, often where the group has limited economic substance. Common mechanisms include excessive interest deductions, inflated royalties, management charges unsupported by actual services, strategic allocation of intellectual property, and contractual allocation of risks to entities that do not control those risks.

BEPS is not synonymous with every instance of tax planning or every transaction with a low-tax jurisdiction. A genuine commercial transaction may lawfully produce a tax consequence. The concern is artificial arrangements that exploit mismatches, gaps or weaknesses in domestic and international tax rules. The OECD estimates that BEPS causes significant annual revenue losses globally and treats it as a threat to the fairness and integrity of tax systems.

2.6 Transfer Pricing: A Simple Illustration

Assume an Indian subsidiary manufactures a product and sells it to its overseas parent for ₹100 per unit. The parent then sells the product to an independent customer for ₹180. If the Indian company's manufacturing costs are ₹70, it reports a profit of ₹30. If the same goods, under comparable conditions, would have been sold by an independent manufacturer to an independent distributor for ₹140, the ₹100 transfer price may leave an unusually large share of the group's profit outside India. A transfer pricing analysis would examine product characteristics, functions, assets, risks, contractual terms and market conditions before deciding whether an adjustment is justified. The example is illustrative only: the arm's length price cannot be determined from the resale price alone.

2.7 Why Transfer Pricing Matters to Economic Development

Corporate income tax is a source of public revenue used to finance infrastructure, education, healthcare, transport, public administration and social protection. If profits generated through activity in India are shifted elsewhere, the State may lose revenue needed for development. At the same time, uncertain or arbitrary transfer pricing adjustments can increase compliance

costs, discourage investment and create the risk of double taxation. A sound regime must therefore pursue two connected goals: protect the legitimate tax base and provide predictable rules for genuine investment and trade.

3. The OECD Transfer Pricing Guidelines

3.1 Background and Evolution

The OECD developed its transfer pricing work in response to the growth of multinational enterprises and the difficulty of allocating their profits among countries. The OECD Transfer Pricing Guidelines were first approved in 1995 and have since been revised to respond to changes in business structures, international tax policy and BEPS risks. The 2022 edition consolidates important guidance on transactional profit methods, hard-to-value intangibles and financial transactions. On 19 February 2024, the Guidelines were updated to incorporate Amount B guidance for qualifying baseline marketing and distribution activities.

The Guidelines are not a global tax statute and do not automatically override domestic law. They are an ***internationally influential interpretative framework***. Their legal effect in a particular country depends on domestic legislation, tax treaties, administrative practice and the manner in which courts use them. In India, the statutory provisions and rules are ***binding***; OECD materials may assist in interpreting concepts and methods where relevant, but they cannot displace the enacted Indian law.

3.2 The Arm's Length Principle as the International Consensus

The OECD Guidelines treat the arm's length principle as the preferred standard for evaluating cross-border transactions between associated enterprises. The principle seeks to place associated enterprises and independent enterprises on a comparable footing for tax purposes. It is intended to reduce the risk that ***group membership*** will be used to allocate profits in a way that unrelated parties would not accept. It also seeks to limit ***double taxation*** by encouraging tax administrations to apply a common analytical framework.

3.3 Accurate Delineation of the Actual Transaction

Accurate delineation is the starting point of a reliable transfer pricing analysis. The tax authority and taxpayer must identify what the parties actually did, not merely what the contract

calls the arrangement. Written agreements are relevant, but actual conduct, decision-making, functions performed, assets used, risks controlled and the parties' financial capacity must also be examined. If the contract allocates a major commercial risk to an affiliate that has no personnel or capacity to control it, the contractual allocation may not determine the appropriate profit allocation.

The OECD analysis first identifies the commercial or financial relations between the associated enterprises and the economically relevant circumstances. It then compares the accurately delineated controlled transaction with comparable uncontrolled transactions. The two stages are related but distinct: a benchmarking exercise cannot cure a failure to identify the real transaction.

3.4 The Five Comparability Factors

1. **Characteristics of property or services**: nature, quality, reliability, volume, specification, contractual rights and the features of the goods or services transferred.

2. **Functional analysis**: functions performed, assets employed and risks assumed by each party, including the people who make important decisions and control economically significant risks.

3. **Contractual terms**: express and implied terms allocating responsibilities, risks, benefits, pricing, warranties, payment terms and ownership rights.

4. **Economic circumstances**: geographical market, market size, competition, level of the market, purchasing power, regulation, location-specific advantages and the economic conditions prevailing at the relevant time.

5. **Business strategies**: market penetration, product launch, research and development, restructuring, brand-building, market-share strategies and other commercial plans that may affect pricing.

A comparison is reliable only to the extent that differences do not materially affect the price or profit indicator, or can be adjusted with reasonable accuracy. The OECD does not require identical transactions. It requires sufficiently comparable transactions and transparent adjustments.

3.5 Functional, Asset and Risk (FAR) Analysis

FAR analysis is the practical heart of transfer pricing. It asks what each entity actually does, what assets it uses and what risks it genuinely assumes. **Functions** may include manufacturing, procurement, research, marketing, distribution, software development, treasury and management. **Assets** may be tangible, such as factories and machinery, or intangible, such as patents, trademarks, software and customer relationships. **Risks** may include market risk, product liability, inventory risk, credit risk, foreign exchange risk, research and development risk and financial risk.

A party should not receive a large return merely because a contract assigns it a risk. The analysis examines whether the party has the capability and actual authority to make decisions about accepting, managing and mitigating the risk, and whether it has the financial capacity to bear the consequences. This prevents a group from allocating residual profits to a passive shell company that merely provides capital or holds legal title.

3.6 The Most Appropriate Method Rule

The OECD Guidelines do not prescribe one method for every transaction. The method that produces the ***most reliable arm's length result*** must be selected after considering the nature of the transaction, the availability and reliability of data, the degree of comparability and the strengths and weaknesses of the available methods. The **traditional transaction methods** are generally preferred where they can be applied with equal reliability. **Transactional profit methods** may be appropriate where direct price comparisons are unavailable or unreliable.

3.7 The Five Principal Transfer Pricing Methods

Comparable Uncontrolled Price (CUP) Method: Compares the price charged in a controlled transaction with the price charged in a comparable transaction between independent parties. It is particularly useful where products or services are sufficiently comparable and reliable market data exists. Example: comparing the price of a commodity sold by an Indian subsidiary to its parent with the price at which it sells the same commodity to an independent buyer.

Resale Price Method (RPM): Begins with the price at which a product purchased from an associated enterprise is resold to an independent customer, then subtracts an appropriate gross resale margin and relevant costs. It is often useful for distribution activities where the reseller

does not add substantial value or own unique intangibles.

Cost Plus Method (CPM): Starts with the supplier's relevant costs and adds an appropriate gross mark-up for the functions performed and risks assumed. It may be suitable for contract manufacturing, routine services and certain intra-group supply arrangements, provided cost bases and comparable mark-ups are reliable.

Profit Split Method (PSM): Identifies the combined profit arising from closely integrated transactions and splits it between associated enterprises on an economically valid basis reflecting their relative contributions. It may be appropriate where both parties make unique and valuable contributions or operations are highly integrated and cannot be reliably evaluated separately.

Transactional Net Margin Method (TNMM): Examines the net profit margin earned by a party from a controlled transaction relative to an appropriate base, such as sales, costs or assets, and compares it with the margin earned in comparable uncontrolled circumstances. It is widely used in practice because net margins may be less affected than gross margins by certain productlevel differences, although comparability and segmentation remain essential.

The OECD Guidelines also recognise other methods where they provide a more reliable measure of an arm's length outcome and are consistent with the principle. The method should not be chosen merely because it produces a preferred tax result.

3.8 Comparability Adjustments and the Arm's Length Range

Differences between the controlled and uncontrolled transactions may require adjustments. Examples include differences in working capital, accounting treatment, product mix, credit terms, geographical markets, capacity utilisation and functions performed. Adjustments must be supported by evidence and should improve comparability rather than mechanically manufacture a desired result.

Transfer pricing is not an exact science. A benchmarking analysis may produce a range of outcomes rather than a single price. The OECD Guidelines recognise that a range may be appropriate where several comparables have a similar degree of reliability. Less comparable observations should be excluded where possible; statistical tools such as the interquartile range may be used where residual comparability defects remain. The Indian rules also provide for an

arm's length range in prescribed circumstances.

3.9 Special Issues Under the OECD Guidelines

3.9.1 Intangibles and DEMPE Functions

Intangibles include patents, trademarks, software, know-how, brands, customer relationships, licences and other valuable non-physical business rights. They are especially vulnerable to profit shifting because legal ownership can be located in a jurisdiction different from the place where the intangible is developed or commercially exploited. The OECD uses the DEMPE framework: **Development, Enhancement, Maintenance, Protection and Exploitation.** The analysis identifies which group entities perform and control these functions, use relevant assets and assume the associated risks. Legal ownership alone does not automatically entitle an entity to all income generated by an intangible.

3.9.2 Intra-Group Services

A multinational group may centralise legal, accounting, human resources, information technology, procurement, strategy or technical support services. The key questions are whether the service was actually rendered, whether the recipient obtained or reasonably expected a benefit, whether an independent enterprise would have paid for it or performed it internally, and whether the allocation key and mark-up are appropriate. Shareholder activities, duplicate services and incidental group benefits ordinarily require careful scrutiny. A tax authority should not reject a genuine service merely because the taxpayer cannot demonstrate an immediate increase in profit; the relevant question is whether the activity provided economic or commercial value.

3.9.3 Financial Transactions

Intra-group financial transactions include loans, guarantees, cash pooling, hedging, treasury functions and captive insurance. The analysis considers the borrower's creditworthiness, realistic alternatives, currency, maturity, security, covenants, purpose of the funding, implicit group support and the lender's actual functions. A purported loan may, on its actual terms and circumstances, have characteristics of equity. A guarantee fee should not be charged automatically where the borrower benefits only from implicit group support rather than a distinct service.

3.9.4 Business Restructurings

Business restructuring may involve shifting manufacturing, distribution, research, intellectual property or risks from one group entity to another. The analysis asks whether something of value has been transferred, whether the transferor surrendered rights or profit potential, whether an independent enterprise would require compensation, and whether the postrestructuring allocation of profits reflects actual functions and risks. A mere change in legal structure does not automatically create taxable compensation, but a transfer of valuable rights or business opportunities may do so.

3.9.5 Cost Contribution Arrangements

A cost contribution arrangement is a contractual arrangement under which associated enterprises share contributions and risks relating to the joint development, production or

acquisition of assets, services or rights. Contributions should reflect the parties' reasonably anticipated benefits. If contributions do not correspond to expected benefits, balancing payments may be required. The arrangement must have genuine economic substance and be supported by appropriate documentation.

3.9.6 Hard-to-Value Intangibles

Hard-to-value intangibles are intangibles for which, at the time of transfer, reliable comparables are unavailable and projected cash flows or assumptions are highly uncertain. The OECD provides an approach allowing tax administrations, in specified circumstances, to use ex post outcomes as evidence of the reasonableness of ex ante pricing assumptions. This is not an unrestricted power to use hindsight: it is subject to defined exceptions and requires consideration of the information reasonably available when the transaction was entered into.

3.9.7 Commodity Transactions

Commodity transfer pricing raises issues concerning quoted prices, pricing dates, quality, delivery terms, transport, insurance and market differentials. The OECD guidance recognises the importance of reliable quoted prices and the need to identify the actual pricing arrangements. Taxpayers should retain contemporaneous evidence of the pricing date and the commercial factors affecting the transaction.

3.10 Transfer Pricing Documentation Under BEPS Action 13

BEPS Action 13 introduced a ***three-tier documentation structure***: the master file, local file and country-by-country (CbC) report. The **master file** provides a high-level picture of the MNE group, including its organisational structure, business activities, intangibles, intercompany financial activities and global financial and tax position. The **local file** focuses on material transactions involving the local entity, including financial information, comparability analysis and the selection and application of the transfer pricing method. The **CbC report** gives tax administrations a jurisdiction-by-jurisdiction overview of revenue, profit, taxes paid and certain indicators of economic activity.

The three documents serve different purposes. The master file gives context; the local file supports the local transfer pricing position; and the CbC report is principally a high-level risk assessment tool, not a substitute for a transaction-level transfer pricing analysis. Confidentiality, appropriate use and consistency of information are essential.

3.11 OECD/G20 BEPS Actions Relevant to Transfer Pricing

Action 4 – Limiting Base Erosion Involving Interest Deductions: Targets excessive interest deductions and other financial payments that erode the tax base. The OECD recommended an earnings-stripping approach, commonly based on a fixed ratio of net interest to EBITDA, with optional group-ratio rules.[5]

Actions 8-10 – Aligning Transfer Pricing Outcomes with Value Creation: Revised the guidance on intangibles, contractual risk allocation, capital-rich entities and other high-risk areas so that profits follow actual economic contributions rather than paper contracts alone.[6]

Action 13 – Transfer Pricing Documentation and CbC Reporting: Established the master file, local file and CbC report to improve transparency and help tax administrations identify

[5] Org. for Econ. Coop. & Dev. [OECD], *Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 – 2015 Final Report: OECD/G20 Base Erosion and Profit Shifting Project* (2015) [hereinafter *OECD Action 4 Final Report*], https://doi.org/10.1787/9789264241176-en.
[6] Org. for Econ. Coop. & Dev. [OECD], *Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 – 2015 Final Reports: OECD/G20 Base Erosion and Profit Shifting Project* (2015) [hereinafter *OECD Actions 8-10 Final Reports*], https://doi.org/10.1787/9789264241244-en.

and assess BEPS risks.[7]

Action 14 – Making Dispute Resolution Mechanisms More Effective: Seeks to improve the effectiveness and timeliness of mutual agreement procedures under tax treaties, helping taxpayers resolve cases of double taxation.[8]

Action 1 – Tax Challenges Arising from Digitalisation: Addresses the difficulties created by highly digitalised and global business models, where value and market participation may not be reflected adequately by traditional physical-presence concepts.[9]

3.12 Two-Pillar Solution and Amount B

The OECD/G20 Two-Pillar Solution responds to tax challenges arising from ***digitalisation and globalisation***. **Pillar One** includes **Amount A**, a proposed reallocation of a portion of residual profits of the largest and most profitable MNE groups to market jurisdictions, subject to the agreed scope and conditions. **Amount B** is different: it provides a simplified and streamlined approach to applying the arm's length principle to qualifying baseline marketing and distribution activities. It is designed to reduce recurring disputes and compliance burdens, with particular attention to jurisdictions with limited administrative capacity.

Amount B is not a universal fixed margin for every distributor. It applies only where the transaction meets the defined scope and scoping criteria. The analysis still begins with accurate delineation and the functions performed, assets used and risks assumed. Transactions involving unique and valuable intangibles, certain commodities or non-distribution activities may fall outside the simplified approach. The OECD published a consolidated Amount B report in February 2025, incorporating guidance released through December 2024.

Pillar Two establishes a ***global minimum tax framework*** for in-scope multinational groups, generally using a 15 per cent minimum effective tax rate. It is important not to confuse Pillar

[7] Org. for Econ. Coop. & Dev. [OECD], *Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 – 2015 Final Report: OECD/G20 Base Erosion and Profit Shifting Project* (2015) [hereinafter *OECD Action 13 Final Report*], doi.org.
[8] Org. for Econ. Coop. & Dev. [OECD], *Making Dispute Resolution Mechanisms More Effective, Action 14 – 2015 Final Report: OECD/G20 Base Erosion and Profit Shifting Project* (2015) [hereinafter *OECD Action 14 Final Report*], doi.org.
[9] Org. for Econ. Coop. & Dev. [OECD], *Addressing the Tax Challenges of the Digital Economy, Action 1 – 2015 Final Report: OECD/G20 Base Erosion and Profit Shifting Project* (2015) [hereinafter *OECD Action 1 Final Report*], doi.org.

Two with transfer pricing. Transfer pricing allocates profits between associated enterprises under the arm's length principle; Pillar Two imposes a minimum-tax architecture that can reduce the tax advantage of shifting profits to very low-tax jurisdictions. The two frameworks may interact but perform different functions.

4. Indian Transfer Pricing Framework

4.1 Historical Development in India

India introduced specific transfer pricing provisions through the **Finance Act, 2001,** following concerns that multinational groups could manipulate prices in transactions between associated enterprises and shift profits outside India. The provisions were broadly based on the OECD approach and became applicable from the assessment year 2002–03. **Chapter X** of the **Income-tax Act, 1961** contained **Sections 92 to 92F**, supported by **Rules 10A to 10E** and related rules in the **Income-tax Rules, 1962.** The regime was subsequently expanded to cover specified domestic transactions and strengthened through documentation, reporting, safe harbour and advance pricing agreement mechanisms.

The **Income-tax Act, 2025** came into force on 1 April 2026. Its **Chapter X** continues the special provisions relating to avoidance of tax, including transfer pricing, but uses a new section numbering structure. The change is not merely academic: students and practitioners must cite the correct statute for the tax year under consideration.

4.2 Current Statutory Framework: Income-tax Act, 2025

The following table identifies the principal current provisions and their broad predecessors under the 1961 Act. It is a navigational comparison, not a substitute for checking the full statutory text, amendments and applicable rules.

Subject	**Income-tax Act, 2025**	**Earlier Income-tax Act, 1961**
Computation having regard to ALP	Section 161	Section 92
Associated enterprises	Section 162	Section 92A
International transaction	Section 163	Section 92B

Specified domestic transaction	Section 164	Section 92BA
Determination of ALP/ methods	Section 165	Section 92C
Reference to Transfer Pricing Officer	Section 166	Section 92CA
Safe harbour rules	Section 167	Section 92CB
Advance Pricing Agreement	Section 168	Section 92CC
Effect to APA	Section 169	Section 92CD
Secondary adjustment	Section 170	Section 92CE
Documentation and information	Section 171	Section 92D
Accountant's report	Section 172	Section 92E
Definitions for transfer pricing chapter	Section 173	Section 92F

Section 161 is the principal charging/computational rule for transfer pricing purposes:

Income, expenditure, interest and relevant cost allocations arising from international and specified domestic transactions are to be determined having regard to the arm's length price.[10] **Section 165** prescribes the recognised methods and the most appropriate method approach.[11] **Section 166** governs the reference to and determination by the Transfer Pricing Officer.[12] **Sections 171 and 172** address documentation and the accountant's report.[13] **Sections 167 to 170** deal with safe harbour rules, APAs, the effect of APAs and secondary adjustments.[14]

4.3 Determination of Arm's Length Price in India

Section 165 of the 2025 Act recognises the comparable uncontrolled price method, resale price

[10] § 161, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 161*].
[11] § 165, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 165*].
[12] § 166, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 166*].
[13] §§ 171–172, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, §§ 171–172*].
[14] §§ 167–170, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, §§ 167–170*].

method, cost plus method, profit split method, transactional net margin method and such other method as may be prescribed. The most appropriate method must be selected in light of the nature of the transaction, the class of transaction or associated enterprise, functions performed and other relevant factors. The statutory text also addresses the determination of the ALP where one or more prices result and the permitted tolerance notified by the Central Government.[15]

The **Income-tax Rules, 2026** provide the detailed machinery for applying the methods. **Rules 77 to 80** address definitions, other methods, determination of ALP and selection of the most appropriate method; **Rule 81** addresses determination where more than one price results; **Rule 82** provides for an option to determine ALP for similar transactions over multiple years in a single proceeding. The precise rule applicable must be checked against the transaction and tax year.[16]

4.4 Transfer Pricing Officer and Assessment Procedure

Under **Section 166**, where an assessee has entered into an international transaction or specified domestic transaction and the **Assessing Officer** considers it necessary or expedient, the matter may be referred to the **Transfer Pricing Officer** with the prior approval of the **Principal Commissioner or Commissioner.** The TPO examines the transaction, calls for evidence, considers the taxpayer's submissions and determines the ALP by a written order. The Assessing Officer then computes total income in conformity with the TPO's determination, subject to the statutory framework and available appellate remedies.

The TPO's role is not to decide whether the taxpayer's business decision was commercially wise. The task is to determine whether the conditions of the controlled transaction are consistent with the arm's length principle. A proper order should identify the transaction, explain the method selected, address the taxpayer's evidence, justify the comparables and adjustments, and give reasons for rejecting competing analyses.[17]

4.5 Documentation and Accountant's Report

Section 171 requires persons entering into international or specified domestic transactions, and constituent entities of international groups, to maintain prescribed information and documents.

[15] § 165, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 165*].
[16] R. 77–82, Income-tax Rules, 2026 (India) [hereinafter *Income-tax Rules, R. 77–82*].
[17] § 166, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 166*].

The documentation should enable the taxpayer to demonstrate the nature of the transaction, associated-enterprise relationship, contractual terms, functional analysis, method selected, comparables, adjustments, assumptions and actual computation.[18] **Section 172** requires a person who has entered into an international or specified domestic transaction during a tax year to obtain and furnish an accountant's report in the prescribed form and manner.[19]

The documentation obligation is not satisfied by merely producing an agreement or a spreadsheet. It should be contemporaneous, consistent with actual conduct and capable of being reconciled with the books of account, tax return and group documentation. For multinational groups, master file and CbC reporting obligations also arise where the statutory thresholds and conditions are met.

4.6 Safe Harbour Rules

A safe harbour is a prescribed circumstance in which tax authorities accept a declared transfer price or income if the taxpayer and transaction satisfy the eligibility conditions. Safe harbours simplify compliance and can reduce disputes for routine or lower-risk transactions. Their advantage is predictability; their limitation is that prescribed margins may not reflect the economics of every business. **Section 167 of the 2025 Act** empowers the Board to make safe harbour rules. The Income-tax Rules, 2026 contain the corresponding procedures and eligible transaction categories.[20]

4.7 Advance Pricing Agreements (APAs)

An Advance Pricing Agreement is an agreement between the taxpayer and the tax administration that determines the arm's length price or the manner of determining it for specified international transactions over an agreed period. It may be unilateral, bilateral or multilateral, depending on the parties and jurisdictions involved. APAs can provide certainty, reduce recurring disputes and avoid double taxation where competent authorities agree on a common approach. Under the **2025 Act, Section 168** provides for APAs and **Section 169** deals with giving effect to them.[21]

[18] § 171, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 171*].
[19] § 172, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 172*].
[20] § 167, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 167*].
[21] §§ 168–169, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, §§ 168–169*].

4.8 Secondary Adjustments

A **primary adjustment** increases or decreases the taxable income of an Indian taxpayer to reflect an arm's length price. A **secondary adjustment** addresses the excess money that remains with the associated enterprise as a consequence of the primary adjustment. It may require repatriation of the excess amount or, where statutory conditions apply, treatment of the amount as an advance and computation of interest. **Section 170 of the 2025 Act** continues the secondary adjustment framework. Its application depends on the statutory monetary threshold, the type of primary adjustment and the prescribed time for repatriation.[22]

4.9 Thin Capitalisation and Interest Deduction

Thin capitalisation occurs where a company is financed with a disproportionately high level of debt, particularly related-party debt, allowing substantial interest deductions to reduce taxable profits. **BEPS Action 4** recommends measures to limit excessive interest deductions. India introduced a limitation under **Section 94B of the 1961 Act**, generally restricting the deduction of specified interest paid or payable to associated enterprises to 30 per cent of EBITDA or the interest paid or payable to associated enterprises, whichever is lower, subject to the statutory scope and exceptions. The corresponding provision under the 2025 Act must be cited by its current numbering for periods governed by that Act. This provision complements transfer pricing rules:

the interest rate may be arm's length, yet the deduction may still be restricted under an earningsstripping rule.[23]

4.10 Specified Domestic Transactions

Specified domestic transaction rules address selected domestic related-party arrangements where profit allocation can affect tax incentives or deductions. They are not identical to the international transfer pricing regime because both parties may be residents. The statutory definition, categories and threshold have changed over time; therefore, the precise applicable provision and threshold must be checked for the relevant tax year. The purpose is to prevent domestic profit shifting that distorts the tax base or the use of tax benefits.

[22] § 170, Income-tax Act, 2025, 30 Acts of Parliament, 2025 (India) [hereinafter *Income-tax Act, § 170*].
[23] § 94B, Income-tax Act, 1961 (India) [hereinafter *Income-tax Act, § 94B*].

4.11 Penalties and Compliance Consequences

Failure to maintain prescribed documentation, furnish the accountant's report, report international transactions correctly or provide information during proceedings may attract penalties under the applicable provisions. Penalties are intended to encourage disclosure and reliable records, but they must be applied according to the statutory requirements and procedural safeguards. Taxpayers should distinguish a genuine pricing disagreement from a failure to comply with reporting and documentation duties.

4.12 Dispute Resolution and Mutual Agreement Procedure

Transfer pricing adjustments can lead to economic double taxation where one country increases the taxable profits of an associated enterprise but the other country does not make a corresponding adjustment. Domestic appeals, the Dispute Resolution Panel mechanism where applicable, and the mutual agreement procedure (MAP) under an applicable tax treaty are important safeguards. MAP allows competent authorities to consult and seek a resolution consistent with the treaty. APAs can prevent disputes before they arise, while MAP addresses disputes after a tax adjustment has occurred.

5. Landmark Indian Case Laws

Indian courts and tribunals have shaped transfer pricing law by clarifying the role of OECD principles, the limits of tax administration, the treatment of intra-group services, the selection of comparables and the allocation of marketing-related returns. The following decisions are particularly relevant. Historical cases decided under the 1961 Act remain important for interpreting similar concepts, but their statutory references should be translated carefully when applying the 2025 Act.

DIT v. Morgan Stanley & Co. Inc., (2007) 7 SCC 1 (Supreme Court)

Facts: Morgan Stanley, a US-based multinational, provided certain services through an Indian affiliate. The dispute concerned the attribution of profits to a permanent establishment in

India and whether the Indian affiliate's remuneration at arm's length adequately compensated the relevant Indian functions.

Decision and relevance: The Supreme Court explained the significance of transfer pricing analysis in determining whether further profits should be attributed to an Indian permanent establishment. Where the associated Indian enterprise is remunerated at arm's length for the functions performed, that may, depending on the facts and functions, exhaust the attribution of profits to the PE. The case is important for understanding the relationship between transfer pricing and permanent establishment profit attribution.[24]

Aztec Software and Technology Services Ltd. v. ACIT, (2007) 107 ITD 141 (Bang.) (Special Bench, ITAT)

Facts: The taxpayer, an Indian software company, entered into transactions with associated enterprises for onsite software services and marketing support. The TPO questioned the comparables, the method and the allocation of profits between the Indian and overseas entities.

Decision and relevance: The Special Bench discussed the legal framework for invoking transfer pricing provisions and the need for a reasoned analysis of comparability, functions, assets and risks. It emphasised that the method and comparables must be evaluated in light of the actual transaction. The decision is an early and influential exposition of India's transfer pricing regime.[25]

CIT v. EKL Appliances Ltd., (2012) 345 ITR 241 (Delhi)

Facts: The taxpayer paid brand fees/royalty to its associated enterprise. The TPO questioned the commercial justification for the payment and sought to determine the ALP by effectively questioning whether the taxpayer needed the benefit.

Decision and relevance: The Delhi High Court held that the TPO cannot determine ALP by substituting his own judgment for the taxpayer's commercial decision or by deciding that the taxpayer should not have entered into the transaction. The inquiry is whether the price is at arm's length. The case is central to the distinction between transfer pricing and a general test of commercial expediency.[26]

[24] AIRONLINE 2007 SC 338
[25] [2007]107ITD141(BANG), [2007]294ITR32(BANG)
[26] (2012) 345 ITR 241 (Del), (2012) 250 CTR 362 (Del), (2012) 209 Taxman 451 (Del), (2012) 71 DTR 257 (Del), TS-206-HC-2012 (DEL), ITA Nos. 1068 & 1070 of 2011

Cushman and Wakefield (India) Pvt. Ltd. v. ACIT, (2014) 367 ITR 730 (Delhi)

Facts: The dispute concerned payments by an Indian entity to its associated enterprise for management and support services. The TPO examined whether the services had been rendered and whether the charges were justified.

Decision and relevance: The Delhi High Court distinguished the question whether a service was actually rendered and whether the expenditure is allowable from the transfer pricing question of determining its arm's length price. The decision highlights the importance of evidence of actual services, benefits and the correct statutory function of the TPO.[27]

Vodafone India Services Pvt. Ltd. v. Union of India, (2014) 368 ITR 1 (Bom.)

Facts: Vodafone India issued shares to its overseas holding company at a premium. The TPO valued the shares at a higher amount and treated the difference as an international transfer pricing adjustment, including a notional loan and interest component.

Decision and relevance: The Bombay High Court held, on the facts and statutory language then applicable, that the share issue was a capital-account transaction and the alleged shortfall did not constitute income capable of being adjusted under the transfer pricing provisions. The Union Government accepted the decision and did not appeal. The case is important on the limits of the transfer pricing chapter and the distinction between capital receipts and taxable income.[28]

Shell India Markets Pvt. Ltd. v. ACIT, (2014) 369 ITR 516 (Bom.)

Facts: The case involved the issue of shares by an Indian subsidiary to its foreign parent and a transfer pricing adjustment based on the alleged undervaluation of those shares.

Decision and relevance: The Bombay High Court followed the reasoning in Vodafone India Services and rejected the attempt to treat the alleged share-price shortfall as taxable income under the transfer pricing provisions as they then stood. It is significant for the treatment of capital transactions and the limits of the ALP machinery.[29]

[27] (2014) 367 ITR 730 (Del), (2014) 225 Taxman 8 (Del), (2014) 269 CTR 16 (Del), (2014) 105 DTR 257 (Del)
[28] (2014) 368 ITR 1 (Bom), 50 taxmann.com 300 (Bombay), 228 Taxman 25 (Bombay), (2014) 271 CTR (Bom) 488, (2014) 110 DTR (Bom) 1, MANU/MH/1825/2014
[29] (2014) 369 ITR 516 (Bom.), 51 taxmann.com 519 (Bombay), 228 Taxman 99 (Bombay), 273 CTR 161 (Bombay).

Sony Ericsson Mobile Communications India Pvt. Ltd. v. CIT, (2015) 374 ITR 118 (Delhi)

Facts: The dispute involved Indian distributors of mobile phones and related products, payments for advertising, marketing and promotion (AMP), and the question whether such expenditure created or enhanced marketing intangibles for the foreign associated enterprise.

Decision and relevance: The Delhi High Court examined the transfer pricing treatment of AMP expenditure, the use of bundled transactions, and the application of TNMM and other methods. The judgment cautioned against treating every high level of advertising expenditure as a separate international transaction without proper analysis. It remains important in disputes involving marketing intangibles and local market contributions.[30]

Maruti Suzuki India Ltd. v. CIT, (2016) 381 ITR 117 (Delhi)

Facts: The dispute concerned AMP expenditure by an Indian automobile manufacturer and whether the expenditure resulted in an international transaction with its foreign associated enterprise for brand promotion.

Decision and relevance: The Delhi High Court held that the existence of an international transaction cannot simply be presumed from the fact that an Indian company incurs substantial AMP expenditure. The Revenue must establish the relevant arrangement or understanding and apply the correct legal test. The case protects taxpayers from automatic adjustments based solely on expenditure levels.[31]

Pr. CIT v. Softbrands India (P.) Ltd., (2018) 406 ITR 513 (Karn.)

Facts: The Revenue challenged ITAT decisions in transfer pricing matters, seeking High Court intervention in disputes involving comparables and benchmarking.

Decision and relevance: The Karnataka High Court reiterated the limited scope of a substantial question of law in transfer pricing appeals. Pure questions of fact and the selection of comparables generally do not warrant interference unless the findings are perverse or raise a legal issue. The decision reinforces the importance of reasoned fact-finding by the TPO and

[30] (2015) 374 ITR 118 (Delhi), [2015] 231 Taxman 113 (Delhi) [2015] 55 taxmann.com 240 (Delhi) [2015] 276 CTR 97 (Delhi).
[31] (2016) 381 ITR 117 (Delhi), 64 taxmann.com 150 (Delhi), 237 Taxman 256 (Delhi), 282 CTR 1 (Delhi).

ITAT.[32]

CIT v. Glaxo SmithKline Asia (P.) Ltd., (2010) 195 Taxman 35 (SC)

Facts: The dispute concerned related-party domestic transactions and the possibility of shifting profits through transactions between associated entities, including the adequacy of the existing domestic tax framework.

Decision and relevance: The Supreme Court highlighted the need for an appropriate legislative framework to deal with domestic transfer pricing and related-party pricing concerns. The decision is relevant to the policy background for the later introduction and development of specified domestic transaction provisions.[33]

6. Critical Analysis: Arm's Length in an Age of Base Erosion

6.1 Strengths of the Arm's Length Principle

The ALP offers a common international language for allocating profits among associated enterprises. It respects the separate legal personality of group companies and recognises that each entity may perform different functions and bear different risks. It can accommodate a wide range of transactions and business models, and it provides a basis for corresponding adjustments and treaty-based dispute resolution. Its flexibility is a strength because it avoids a rigid formula that would treat a routine distributor, a research-intensive company and a unique technology owner as economically identical.

6.2 The Comparability Problem

The principle depends heavily on comparable uncontrolled transactions. In many developing economies, public financial data is limited, industry classifications are broad, and independent companies may not perform functions sufficiently similar to those of multinational subsidiaries. Tax administrations may rely on foreign comparables that operate in different markets, face different risks or enjoy different levels of purchasing power. A benchmark that appears statistically precise may therefore be economically weak. The result can be an

[32] (2018) 406 ITR 513 (Karn.), 94 taxmann.com 426 (Karnataka), 303 CTR 695 (Karn), 168 DTR 185 (Karn).
[33] (2010) 195 Taxman 35 (SC), (2010) 236 CTR 113 (SC), 328 ITR 11 (SC), 164 DTR 256 (SC).

adjustment based on data that does not accurately reflect Indian market conditions.

6.3 The Problem of Integrated Multinational Groups

The separate-entity approach assumes that group entities can be evaluated as if they were independent enterprises. Yet multinational groups create synergies through shared technology, centralised procurement, global brands, integrated supply chains and coordinated risk management. Some of these benefits cannot easily be isolated or priced by looking at each entity separately. The profit split method may be more suitable in some highly integrated cases, but it can be difficult to apply because the combined profit and contribution keys are often contested.

6.4 Intangibles and the Separation of Legal Ownership from Value Creation

The allocation of returns from intellectual property is one of the most difficult BEPS problems. A group may register a patent or brand in a low-tax jurisdiction while research, engineering, marketing and commercial exploitation occur in countries with higher taxes. The DEMPE framework improves the analysis by focusing on actual contributions. However, measuring the value of each contribution remains difficult, especially where innovation is uncertain, data is proprietary and the intangible's future success is not known at the time of transfer.

6.5 Intra-Group Services and the Benefit Test

Management fees, technical support charges and shared-service allocations are recurring sources of controversy. Tax authorities are justified in asking whether a service was actually provided and whether the recipient obtained a benefit. But the benefit test should not become an overly narrow requirement that every service must generate immediate revenue. Some services protect the business, reduce risk, satisfy regulatory requirements or improve long-term capacity. The proper inquiry should be evidence-based and should distinguish real services from shareholder activities, duplicative services and unsupported allocations.

6.6 Digitalisation and the Limits of Physical Presence

Digital businesses may derive substantial value from users, data, network effects and access to markets without maintaining the traditional physical footprint. The arm's length principle can address many related-party transactions within digital groups, but it does not by itself resolve

the broader question of how taxing rights should be allocated where market participation is not matched by a conventional permanent establishment. This is why the OECD's digitalisation work and Pillar One discussions sit alongside, rather than simply inside, traditional transfer pricing rules.

6.7 India's Administrative and Litigation Challenges

India has a developed transfer pricing administration, including specialised TPOs, documentation obligations, safe harbours, APAs and dispute resolution mechanisms. Nevertheless, recurring litigation can arise from the selection of comparables, working-capital adjustments, risk adjustments, AMP expenditure, intra-group services, management fees, royalties, corporate guarantees, loans and the treatment of business restructurings. Multiple rounds of assessment and appeals increase costs for both taxpayers and the State. Inconsistent approaches across years or officers may weaken certainty.

6.8 The Risk of Double Taxation

A transfer pricing adjustment in India may not be matched by a corresponding reduction in the other jurisdiction. The same group profit may then be taxed twice. Treaty Article 9 and the mutual agreement procedure are important tools, but MAP can be lengthy and outcomes are not always guaranteed. Bilateral and multilateral APAs, timely competent-authority engagement and better treaty coordination can reduce this risk.

6.9 Transfer Pricing and Economic Development

For India, transfer pricing enforcement has a developmental dimension. A fair allocation of profits can strengthen revenue collection and public investment. It can also protect domestic businesses that do not have access to complex cross-border tax structures. However, enforcement must be proportionate. If legitimate payments for technology, finance, research or services are routinely challenged without adequate evidence, the cost of doing business rises and investment decisions may be distorted. The objective should not be to maximise adjustments, but to secure the tax base that properly belongs to India under the law.

6.10 Is the Arm's Length Principle Sufficient?

The ALP remains the central standard for transfer pricing, but it is not a complete solution to

every form of BEPS. It is transaction-specific, data-intensive and dependent on a hypothetical comparison. It can be difficult to apply to highly integrated groups and unique intangibles. Global minimum tax rules, interest limitation rules, controlled foreign company rules, withholding taxes, anti-abuse provisions, treaty measures and transparency obligations are therefore complementary tools. A balanced international tax system needs a combination of these mechanisms rather than reliance on one principle alone.

7. Suggestions and Recommendations

a. Strengthen the quality of Indian comparables. Develop reliable, sector-specific databases and improve access to audited financial information so that benchmarking reflects Indian market conditions rather than mechanically relying on foreign comparables.

b. Require reasoned and transaction-specific TPO orders. Each adjustment should identify the accurately delineated transaction, explain the chosen method, justify the tested party and comparables, and address the taxpayer's material objections.

c. Apply DEMPE analysis consistently. In cases involving intellectual property, the allocation of returns should reflect actual development, enhancement, maintenance, protection and exploitation functions, including control of risks and financial capacity.

d. Adopt a proportionate approach to intra-group services. Require evidence of actual services, recipient benefit and a rational allocation key, while avoiding the assumption that the absence of immediate revenue proves that no service was received.

e. Expand bilateral and multilateral APAs where appropriate. These agreements can prevent recurring disputes and reduce the risk of double taxation, particularly in sectors with repeated and predictable related-party transactions.

f. Improve the efficiency of MAP. Competent authorities should establish clear timelines, better case-management systems and transparent communication so that treaty disputes are resolved without excessive delay.

g. Use Amount B carefully. India should evaluate the simplified approach for qualifying baseline distributors, taking account of market conditions, administrative capacity and the interests of developing and market jurisdictions.

h. Integrate digital data and risk analytics. Tax authorities should use CbC reports and other lawful information for risk assessment, while ensuring that CbC data is not treated as conclusive proof of an arm's length price.

i. Provide certainty during the transition to the 2025 Act. The tax administration should publish clear guidance, cross-reference tables and practical examples explaining the transition from Sections 92–92F to Sections 161–173 and the corresponding 2026 Rules.

j. Ensure proportionality in penalties. Penalties should distinguish deliberate concealment from genuine interpretative disagreement, while maintaining meaningful consequences for noncompliance and inaccurate reporting.

k. Strengthen specialist capacity. Continuous training in valuation, economics, financial modelling, digital business models, intangible assets and international tax treaties is necessary for both tax officials and adjudicating bodies.

l. Improve taxpayer education and compliance support. Clear guidance, advance consultations and accessible examples can encourage voluntary compliance and reduce avoidable litigation.

m. Coordinate transfer pricing with other anti-BEPS measures. ALP enforcement should be read alongside thin-capitalisation limits, treaty anti-abuse rules, CFC measures where applicable, withholding tax rules and the global minimum tax framework.

n. Publish anonymised guidance on recurring issues. Reasoned summaries of common disputes involving royalties, guarantees, shared services, marketing intangibles and benchmarking would promote consistency without prejudging individual cases.

8. Conclusion

Transfer pricing sits at the intersection of international commerce and national fiscal sovereignty. In a multinational enterprise, a large part of economic activity takes place through transactions between companies that are legally separate but commercially connected. The prices attached to these transactions influence where profits are reported and where tax is paid. When those prices are manipulated, the result may be base erosion, unfair competition and a loss of public revenue. When transfer pricing rules are applied without sufficient regard to

commercial reality, however, they may produce double taxation, uncertainty and unnecessary barriers to investment.

The OECD Transfer Pricing Guidelines provide a sophisticated framework for applying the arm's length principle. Their emphasis on accurate delineation, comparability, functional analysis, control of risk and value creation has improved the international response to artificial profit shifting. The BEPS project, especially Actions 4, 8-10 and 13, has strengthened the rules on interest deductions, intangibles, risk allocation and transparency. Amount B offers a practical simplification for certain baseline distribution activities, while the Two-Pillar Solution addresses wider questions raised by digitalisation and globalisation.

India has developed a comprehensive transfer pricing regime since 2001. Its judicial decisions have helped define the proper limits of the TPO's role, the need for evidence of services, the treatment of marketing expenditure and the distinction between capital transactions and taxable income. The Income-tax Act, 2025 and the Income-tax Rules, 2026 now provide the current statutory framework from 1 April 2026, while the earlier law remains relevant to periods governed by it.

The principal weakness is not the absence of legal rules but the difficulty of applying them consistently to complex business realities. Reliable comparables may be scarce, intangibles are difficult to value, integrated groups do not always fit a separate-entity model, and disputes can remain unresolved for years. The way forward is therefore not simply stricter enforcement. It is better evidence, stronger institutional capacity, predictable procedures, proportionate penalties and effective international dispute resolution.

Ultimately, the arm's length principle must ensure that profits follow genuine economic contributions without penalising legitimate business arrangements. For India, the objective is a transfer pricing system that protects the tax base, encourages responsible investment, supports fair competition and generates the public revenue necessary for sustainable economic development. The true measure of success is not the number or value of adjustments made by tax authorities, but whether the system allocates taxable profits fairly, consistently and with legal certainty.