Getting it right is the taxman’s biggest challenge

Given the way transfer pricing cases in India are rising—from R44,000 crore in FY12 to R70,000 crore in FY13, before falling to R60,000 crore in FY14—it is obvious the taxman rem ains unconvinced by how industry, both Indian and overseas, is reporting its revenues. As FE reported Monday, after asking
Microsoft to increase its taxable income for FY06-09 by R5,135 crore, the taxman has also questioned its income statement for FY10. While Microsoft has said its taxable income was 16.4% of its costs in India—the India centre is an offshore R&D one—the taxman’s view is Microsoft is hiding value; that the work being done in India is actually of value to Microsoft’s global clients and that, given this, the margins imputed to the India centre should be of the magnitude declared by IT majors such as Wipro and Infosys.

Figuring out where value lies is a tricky business and it is difficult to, a priori, argue the taxman is wrong in asking Microsoft and others to declare a higher value for their India operations. More so, given the fact that many of these MNCs have tax issues with their home countries—indeed tax authorities in most OECD countries are looking at finding ways to tax their companies. But given how most MNCs have a problem with the Indian taxman—India’s rank in the Doing Business ratings is 158th out of 189 countries—perhaps the taxman’s operations need to be rethought. A regular dialogue with OECD taxmen—or perhaps seconding Indian taxmen to OECD tax authorities—may be one way to deal with things. The last thing India wants to do, at this stage of development, is to frighten away investors due to what the BJP manifesto calls tax terrorism.