

SUSTAINABILITY CHALLENGES FACED BY SMES FROM TRANSFER PRICING LAWS

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Abstract

Entrepreneurial zeal is a backbone of any emerging economy. Most of the geographies of the world have gone at lengths to preserve and promote their respective industries, for the overall economic development. The SME sector is one such crucial aspect, which the world economies are interested in. India, in particular, looks at SMEs as an important way for building and strengthening the nation (Ministry of Micro, Small and Medium Enterprises, 2019). Everyone acknowledges and dreams of minting the strides in technological and industrial advancements that the SME sector brings up (Mcintyre, 1994).

In order to conduct and flourish their businesses, the SMEs have to accept, embrace and sometimes overcome the administrative and legal framework of a country. One such vital aspect which requires an iron clad planning from these entities is the taxation regime. Although small and/or medium in nature (as their names suggest) e-commerce specifically, and exuberant conveyance facilities generally, have allowed SMEs to dream big (Rawlings, 2017; Drahos, 2017). This brings up a possibility of cross border transactions, thus triggering the Transfer Pricing provisions, of the respective countries.

The Transfer Pricing provisions have been enacted to allow a particular country to earn its dues rightfully, as well as to not burden an entity to pay taxes twice (with a cascading effect). This being said, the strength of these laws is still an open-ended predicament, since, a rift between these laws is witnessed by many in the developed West and the developing & least developed East (Medium, 2019). Such a rift creates a conundrum about whether indeed it is possible for SMEs to sustain in the globalized world markets, let alone to grow into prosperity (EY, 2019).

This paper highlights the transfer pricing related legal challenges that the SMEs face and, deals with the possibility for SMEs to co-exist with them, leading to sustenance

Key words: Transfer Pricing, International Taxation, Small and Medium Enterprise, Sustainability.

Introduction

Entrepreneurial zeal is a backbone of any emerging economy. Most of the geographies of the world have gone at lengths to preserve and promote their respective industries, for the overall economic development. The Small and Medium Enterprise (SME) sector is one such crucial aspect, which the world economies are interested in. India, in particular, looks at SMEs as an important way for building and strengthening the nation (Ministry of Micro, Small and Medium Enterprises, 2019). Everyone acknowledges and dreams of minting the strides in technological and industrial advancements that the SME sector brings up (Mcintyre, 1994). Although at a nascent stage for SMEs, Initial Public Offerings (IPO) have been seen as a global pathway to go public (Beerannavar, 2015).

The developed economies and the sizes of the entities in such economies is unlike how it used to be or is dissimilar to how it is in a developing or a least developed economy (Vengedasalam, 2014). Especially, if the least developed economies are concerned, most of the workers, estimated to be around two thirds of the workers, are employed in micro enterprises. Such enterprises usually have less than five employees (Vengedasalam, 2014). Amongst others, the employment quota is diverted to the larger enterprises, mostly having more than 100 employees (Taussig, 2007). An economy boasting of such large enterprises have a very little or no occupancy for such very small enterprises to survive and thrive (Vengedasalam, 2014). A

comparative analysis with the total workforce will suggest that the presence of such SMEs in the economies giving a platform for large enterprises to thrive is around 10 percent. If the comparability is taken to the developed countries, almost two thirds of the population there works for the large enterprises (Snower, 2020). The remainder population work for medium sized or small enterprises leaving very few to be working for a very small enterprise. The economic activity and the circulation of currency in the economy mostly happen through these large enterprises. This data might suggest that the only way for an economy to thrive is to have fully functional large enterprises. However, such a conclusion is far away from the truth. In reality, what these statistics are concealing is the role that a SME can play to boost any economy, irrespective of its size (Taussig, 2007). A reality check would be that if the advent of technologies is seen, statistically, most of it has come from garages and rented cubicle apartments, ultimately pointing their fingers at SMEs (Taussig, 2007). The source for finance has been a fundamental aspect behind driving an enterprise. A large enterprise tends to get its finances from any particular place possible, however, when a SME is considered, approaching for finance seems a bit difficult (Indian Institute of Banking & Finance, 2017). It has to be acknowledged that arranging finance through keeping something as collateral and also through a sizable government support is possible when a large enterprise is playing the cards but the same is nearly impossible for a SME (Indian Institute of Banking & Finance, 2017).

Many analysts across the world, probably with a belief and a motivation that the SME sector should survive, have successfully managed to establish a link between the growth of the gross domestic product (GDP) and sustainability in employment, with that of a thriving SME sector (Indian Institute of Banking & Finance, 2017). This in-turn also suggests that if a government policy is inclining towards a favorable policy making decisions, towards SMEs, it will end up having an overall positive impact on the economy at large (Gabriela, 2016; Sudhakar, 2018).

No promoter wants his entity to remain as a SME for its entire life (Gabriela, 2016). The aim most often is to convert a SME into a large organization or another expectation is that the SME will be sold over to someone to make huge profits. There are many steps that one has to undertake to bring this vision into fruition. However, there are many challenges that a SME will face (Tax Guru, 2019), some of them being that of capital influx, uncertainty of Government Policies, adaptability to business environment in a territory, cultural adaptability, leadership and strategy. Though there are several challenges the authors would like to limit the discussion and analysis to the impact of transfer pricing regulations on SME. The authors further suggest a way forward for sustainability for SMEs on who such transfer pricing regulations would become applicable.

Transfer Pricing

The government policies may tend to have a very negative impact on any business (ACCA Global, 2020). A large enterprise though, having some funds in its reserves, can survive any such adverse policy but for a SME, it gets intricate as they may not have as much of a muscle, as a large entity, to tackle any such policies.

The post-world war era has seen a total shift in the outlook of the countries of the world. A few global conflicts aside, the approach of these countries has changed extravagantly (Indian Institute of Banking & Finance, 2017). Now, in order to survive and thrive, a country has to maintain a certain degree of harmony throughout the world. This harmony mostly is linked with the trade relations that any particular country has with all the other countries. The more it makes oneself investor friendly, the more it would take strides in its overall development (Transfer Pricing Services, 2020). This, as if, has given a new lease to life for many SMEs as now; they can focus directly on a customer on a global level, and not just any local one. The transactions that these entities enter into are in multitudes. Since income gets earned from multiple fronts, if the cardinals of taxation laws are to be considered, an entity would be liable to pay taxes everywhere (Indian Institute of Banking & Finance, 2017). This will be a huge discouragement for anyone willing to conduct a business and thus the companies tend to enter into Avoidance of Double Taxation Agreements (ADT) (Indian Institute of Banking & Finance, 2017). There is also a possibility where any entity, let alone a large or a SME, may incorporate multiple entities the world over to take benefit of their domestic taxation regimes. To avoid this, the transfer pricing rules are in place (Uyar, 2014).

Transfer Pricing, the Concept

Purely from the view-point of the taxation and accounting concepts, transfer pricing is a method which is comprised of all rules and methods which are used for pricing of the transactions between and within the entities which are having a common ownership or control. This usually includes all the entities which are a part of a particular group of companies/entities. The fact that the transactions are happening across the border brings in two or more revenue laws in picture (Indian Institute of Banking & Finance, 2017). It always has to be realized that all these laws may not be in sync, i.e. the framers of two different geographies might have an intrinsically different view of looking towards the world (Transfer Pricing Asia, 2019). This countenance, of having a different approach, might seem very nominal, is actually the root cause of majority of the conflicts between the laws in the world. It is true that most of the countries of the world are bound by treaties and agreements like General Agreement of Tariff & Trade (GATT) or General Agreement of Trade in Services (GATS) but paramount importance is still given to the domestic laws when a contention arises between an international law and a domestic law (Sangal, 1979). This potential of entering into a transaction anywhere in the world, within a controlled group, or as they are termed, cross-border controlled transactions, allows an entity to curve the taxable income in its favor (Sangal, 1979). The revenue and tax authorities of many countries are against such practices as they may lead to depriving a country from losing potential revenue through taxes (McDaniel, 2018). Hence, the rationale behind these laws is the safeguarding of that revenue which a country deserves and utilizing that revenue ahead for betterment of nation (TP Week, 2019).

How Transfer Pricing works?

Suppose an entity, Major Technologies Inc. (Parent), is a parent company situated in the United States of America (USA) of a globally established group called Major Group. This company has its main business of manufacturing of laptops. It has a subsidiary in the Bahamas called Major Ltd (Subsidiary I) and another in Mexico called Major de Mexico Inc (Subsidiary II). Both the entities are in the business of manufacturing touch pads.

Now, Parent is in a need of one thousand five hundred touch pads for its laptops. It is aware that the tax rates in USA are cyclopean as compared to Bahamas and Mexico. The tax rate in Bahamas is NIL for Subsidiary I.

Hence, a Parent purchase touch pads from Subsidiary I and Subsidiary II and pays the invoice amount accordingly. The invoice price was 100\$ more than what is usually charged for touchpads.

The Parent chose this strategy because, since the tax rates are higher in USA, it made expenditure there. Expending funds results into a reduction of turnover, in turn the reduction of profit, since, on a basic level, Parent is giving away a part of its earnings. Since the funds are given out, the profit of Parent goes down resulting into a lower amount of profit, or even loss. Since tax is levied on the profits (earning) of a Company, and since Parent might have had losses, let alone a lesser profit, tax may not even get levied on Parent, let alone a levy of a lower amount.

Adjacently, Subsidiary I and Subsidiary II have generated revenue since they managed to sell their goods. The bottom line here is that the tax rates are low in Mexico and are NIL in Bahamas. This suggests that no matter what these entities end up making, they are not in any obligation to partake anything with the local government. Focusing upon the fact that the goods were sold at a higher price than normal, inflates their profits but, there is no governmental revenue to be collected on such profits, since the taxes are either low or are NIL.

This overall deed clearly portrays an intention to deceive the revenue authorities of USA.

Transfer Pricing (Vengedasalam, 2014; McDaniel, 2018, MNE Tax; 2019), or Arm's Length Pricing is an ideal solution to this. The revenue authorities do not cater to the price at which the goods have been sold by Subsidiary I and Subsidiary II to Parent, but they compare it with an uncontrolled transaction (transaction entered at an Arm's Length). It means, in this case, the authorities will compare the prices of the touch pads with all the other entities dealing with a similar business and construct an arm's length price (ALP). This ALP then is

charged to the transaction entered into between Parent and Subsidiary I & Subsidiary II thus fetching out the correct taxable amount.

Hence, Parent, who, let's say, earlier, had shown a loss of \$100,000 by applying the transaction cost of \$150,000 now has a profit of \$35,000 since the ALP of the touch pads was \$10 and not \$100, as charged earlier. Hence, Parent had no need to shell out the extra \$90, which it had paid to Subsidiary I and Subsidiary II.

Now, the revenue authorities of USA are in a position to levy an appropriate tax on \$35,000 which is the profit that Parent had made in the year.

Table 1: Illustration of methods of calculation by Parent & Tax Authorities

Calculation made by Parent	
Particulars	Amount (USD)
Revenue from operations	50,000
Less: Purchase of goods (1500 x \$100)	150,000
Profit/(Loss) before interest and taxes	(100,000)

Calculation made by Tax authorities	
Particulars	Amount (USD)
Revenue from operations	50,000
Less: Purchase of goods (1500 x \$10)	15,000
Profit/(Loss) before interest and taxes	35,000

Impact of Transfer Pricing Laws

Majority of the governments, the world over, have adopted the transfer pricing rules (Vengedasalam, 2014; MNE Tax, 2019). Most of these are a combination of the Arm's Length Principle, and other laws (Vengedasalam, 2014; PWC, 2019). The rules of these countries function in such a manner wherein, an entity, be it a large entity or a SME, is allowed to set up its prices in whichever way they want (Tax Guru, 2019; Jhabakh, 2008). Once these prices are set and the transaction gets entered into, the tax authorities then have a free hand to adjust those prices (Taxmann, 2019). The term free hand is to be used through the provincial nature of it in a way that the entries can only be adjusted within the confines of the transfer pricing rules. Such adjustments are mainly based on the plebian that the transaction has been entered into on the basis of the Arm's Length, i.e. the price charged/the price at which the amount was paid, would have been the same one had this transaction have happened with an unrelated entity. It is of significance to note that an intention is not being recognized here. It means, whether the entity had an intention to either avoid or evade taxes has not been used as a litmus test to imbibe arm's length pricing. The rules take into consideration the situation in the market, the functions undertaken, the risks involved and the terms & conditions at which a sale has happened (Elgar, 2019). These parameters allow the comparability to be on the basis of related party transactions or the core profitability of the entity. Prices are generally adjusted by the entities by manipulating with the taxable income of all the parties which are involved, and which could be compared with, of a particular jurisdiction. The adjustment of and withholding of taxes is also one such parabola. Tax returns, once filed, trigger such adjustments (OECD, 2019). The assumption is that the return in itself is filed by planning out the extent up to which an amount can

be brought down, and then, once the return gets filed, the entire machinery of the group is molded in such a way so as to get the transactions outside of the ambit of taxation (Lin, 2017; Sangal, 1979).

Many countries and their rules also allow for multiple methods to be used for transfer pricing. The only measure of criteria here is if all the methods being used are appropriate, i.e. are widely recognized or the data which is used for utilizing these methods is a reliable one. The methods which are the most commonly used ones are Comparable Uncontrolled Prices Method (CUP), Cost-Plus Method (CPM), Profit Split Method (PSM), Resale Price Method (RPM) and some other methods based on the profitability of the assessee. The methods by which the goods are tested as against services also differ. There are also provisions related to the methods or mechanisms that are used for sharing of costs or for allocation of costs which are mobilized for the acquisition of assets. Most of the times, it has been observed that such coloring is purely done to avoid taxes. As such, the nature of the goods or services has no paramountcy (Indian Institute of Banking & Finance, 2017; McDaniel, 2018).

Some countries contend that an arm's length price may not be a price at a certain particular point of time, but a series of transactions which have taken place at different points of the chronological order (Robinson, 2000). Example, the inter-quartile range is a method which is used in the United States of America. It provides tools which will allow the authorities to measure whether, amongst the given range of prices, a mentioned particular price is indeed at an arm's length (International Fiscal Association, 2018). If the data, or the range provided has a large-scale deviation, it would itself suggest that the data or the range is not reliable. The authorities might then choose to increase the range of the period, which then can generate a multiplicity of data. Economic substance is another such yardstick for measurement (Whillian, 2009). The goods or services being considered in a particular transaction by an entity, wherein, their substance on the basis of their utility, and the price range being allocated to it by itself, if are creating a general rift, conceptually, the entire transaction will get sidelined (International Fiscal Association, 2018).

Challenges revolving around the transfer pricing rules

The Organization of Economic Cooperation & Development (OECD) and World Bank are the proponents of the Arm's Length Principle and have always recommended intragroup pricing methods (Analysis Foundation, 2018). Administrative methods and practices, treaties (unilateral & bilateral) are a few of the key methods through which the methods can be collated (Andersson, 2018). Out of the G20 countries, 19 have already adopted it. Most of the countries of the world follow the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereinafter called Guidelines)(Andersson, 2018). Howbeit, the rules that these countries adopt for themselves, on the domestic level, tend to have their own variations. It means that the culture and the socio-economic polity of a particular country play a big role in shaping these transfer pricing rules (Rawlings, 2017). Thereupon, the rules, although adopted, may differ on multifarious notches, against the Guidelines.

The membership of the OECD itself becomes a big cause for concern if looked at objectively. Following is the list of all the countries which are a part of OECD till date, these countries are bifurcated on the lines of the continents that these countries are a part of.

Table 2: OECD Member countries

Asia	Europe	North America	South America	Australia	Africa
Israel, Japan, South Korea	Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Lithuania,	Canada, Mexico, United States of	Chile	Australia, New Zealand	-----

	Luxembourg, Netherlands, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom.	America			
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From the table, the massive gap between representations is clearly visible. Amongst the member countries 27 are from Europe alone, 3 are from Asia, 3 are from North America, 2 are from Australia, only 1 is from South America and there is no representative from Africa. The key aspect to be noted here is that the OECD guidelines are followed the maximum the world over (Drahos, 2017). There are other manuals/rules available, one of which being United Nations Practical Manual on Transfer Pricing for Developing Countries (called ‘Manual’ hereinafter) (Medium, 2019). Yet, when it comes to more acceptability, the OECD Guidelines have a lot more of it than the UN Manual. The fact that the Guidelines are seen as a point of comparison, a yardstick against which the transfer pricing transactions are measured, the representation statistics explained above prove to be a burly game changer (EY, 2020).

Challenges faced by SMEs due to disorganized Transfer Pricing Regimes

In order to conduct and flourish their businesses, the SMEs have to accept, embrace and sometimes overcome the administrative and legal framework of a country (Tax Guru, 2019). One such vital aspect which requires an iron clad planning from these entities is the taxation regime. Although small and/or medium in nature (as their names suggest) e-commerce specifically, and exuberant conveyance facilities generally, have allowed SMEs to dream big (TP Week, 2019; Vengedasalam, 2014). This brings up a possibility of cross border transactions by SMEs, thus triggering the Transfer Pricing provisions, of the respective countries.

The Transfer Pricing provisions have been enacted to allow a particular country to earn its dues rightfully, as well as to not burden an entity to pay taxes twice (with a cascading effect). This being said, the strength of these laws is still an open-ended predicament, since, a rift between these laws is witnessed by many in the developed West and the developing & least developed East (MNE Tax, 2019). Such a rift creates a conundrum about whether indeed it is possible for SMEs to sustain in the globalized world markets, let alone to grow into prosperity (Tax Guru, 2019).

If the exact same challenges, that the SMEs face, which have been discussed above, are looked at purely from the purview of the disorganized transfer pricing regimes, the picture gets much more clearer as to why this is a challenge, and many a times, an uphill task, for SMEs to survive. This setting is for SMEs the world over, which would make one realize how it must be for the ones in the least developed countries, particularly the ones in Africa. Non-partisan point of view towards Africa, and one would see that even in BRICS, where the next concentration of economic prowess is foreseen, only has South Africa, the furthest country down south, as a member. This country too is facing its own issues with the current political turmoil.

Capital influx

As seen before, an influx of capital is a challenge which any entity, faces. Of course, the size of such an entity plays a big role in defining how and by how much will the magnitude of this challenge affects its future course. For SMEs, the onslaught is always mounting.

The investors will be having a thought process about how much and when to invest. There are quite a lot of factors which are studied before putting in the first tranche. The viability of the business, the durability and the acceptability of the product/service is, no doubt, an important factor, but certainly not the only one.

Most of the times, as it has been observed, the investors, including Venture Capitalists (VCs), have quite a lot of pitch-ins happening almost on a daily basis. To select the perfect one from it is not an easy task because, ultimately, even they want their buck to reap in the maximum. Such VCs always have one eye on all the externalities that would affect their prospective investment. It has been seen that VCs might make or break a deal, even when the pitch in was super impressive.

Transfer pricing regime can play a key role in shaping the Capital influx. Due diligence, is a critical angle before any capital is pooled in. This is conducted in many levels. Before even getting into the mettle of an entity, all the other factors are considered. If anywhere, it is found that the transfer pricing regime, of that particular geography, is going to affect the VCs funding, it will halt for other aspects. There are a few examples in which the funding had been pulled out from Africa and was shifted to South Asia, purely because of the rigidity in transfer pricing regimes, the product or service having no part to play in this.

Government Policies

Since the entire transfer pricing regime is based on the acceptability and reluctance of the Government, there is no doubt that transfer pricing via governments thought process plays a role in the survival of a SME. Even before implementation, the mere choice itself plays a key role.

It could be seen that many African countries have chosen to adopt the tax code based on the ALS. These countries, however, also have some special tax codes and regimes. These tax codes and regimes are usually allocated to a specific type of an industry. These industries include mining, oil, natural gas, and such industries linked with the exploitation of the natural resources of that particular country. The scrutiny of the transactions and places of business of the Multinational Corporations (MNCs) in the Africa has come under scrutiny because of the existing contracts which have been entered into by these MNCs with the geographical representatives of Africa. Many of such contracts under consideration are allowing these MNCs to exploit the natural resources of the African countries for which a very miniscule or no compensation is being provided to these countries. This has also opened up for a possibility that the resource rich nations of Africa, being South Africa and Ghana are about to impose a “super tax” on excess profits being made for mining. The parameters of this excessiveness would then have to be defined meticulously. Nigeria who, recently passed the Income Tax (Transfer Pricing Regulations) 2018 had gone ahead, as a prologue to passing of such legislation, that the MNCs which had set their bases in Nigeria had gone on to cause the country a loss of \$5 billion.

Although this works for Africa, if it has a tinge of authoritative point of view, the businesses will start pulling out of the continent, thus reducing the scope for progress. This will be a short term sigh of relief for the MNCs, the homegrown ones, but, the further this continues, this will put a set back on their growth aspirations as, they will not be able to expand globally.

Environmental Adaptability

The environmental adaptability will play a part once an SME starts flexing its muscles away from its home base. There, along with setting itself up, it needs to be extra cautious, especially about the revenue laws. It is always said that any revenue department has its eyes, totally focused upon an entity which has come from an offshore. This makes things even more complicated.

If the SME intends to transact with any local vendor of that newly penetrated shore, it needs to take care about not just the transactions between itself and the offshore vendor, but also whether there are any transactions, between that offshore vendor, and its own investor. These transactions are looked at from a perspective of, as if, they are a well-knit web, which needs a holistic view. This makes things tricky for this SME, as, it first needs to set shop, set base, and only then it can think about compliances. However, the fact that a holistic idea is required, they might have to take help of an offshore entity rendering such services. Usually, the consultation charges of these entities are quite high. Already established consultancy entities, although very reliable, end up costing a fortune, which again restricts the investment required for an actual business set up and prosperity.

Cultural Adaptability

This works as the elixir of life or as a poison pill, depending upon how an entity has shaped up, when being coupled with the transfer pricing provisions. By culture, the question, of course is about the entity's compliance culture. Now, there is a persuasive literature available to suggest why compliance with laws is a costly affair. There are many governments, around the world, who either charge an amount as a filing fee, for any returns which are to be filed with them, or have a procedure so complicated, that even if there isn't any filing fee involved, an entity has no choice but to hire an expert consultant, to drive them through. India is one such country. Although, there aren't any filing fees for making a submission of a periodic income tax return, there are other government organizations like Ministry of Corporate Affairs, Food and Safety Standards Authority of India, etc., who charge an extensive fee for making, not just event based compliances, but also for periodic compliances. For Ministry of Corporate Affairs, even if an entity, if registered as a Company, has no transaction in a particular year, still, it has to file its Balance Sheet and Profit & Loss Account, with it, for a prescribed filing fee.

it is of ascendant importance, that even at a budding stage of its lifecycle, it has to implement, a strong compliance-oriented policy. Transfer pricing, in itself, anyway, is heavy on compliances. Adding to this, the fact that the provisions tend to get tricky, and are extensively dependent on a geographic adaptability, the question remains as to how much of a discipline needs to be inculcated by an entity, in itself, for being compliant, and especially, when should it be rigid, and when flexible.

For large entities, it always is possible to restructure. Rather, there are many large entities that restructure themselves, as a policy, at periodic intervals. They also have in place, either the consultancy firms like EY, Deloitte, KPMG, and PWC (hereinafter referred to as the Big 4 Audit Firms) as their internal auditors or a tier II firm. It will be irrational to expect SMEs to afford such luxuries. Hence, if it decides to be zealously compliant, there are chances that it is divulging from its available capital, i.e., it is not utilizing it where it matters the most, for the enhancement of its product or service. The cost for this might be growth, or progress. Wherefore, it is acute to have a harmonized transfer pricing provisions, across all the geographies, to help such SMEs to prosper.

Leadership & Strategy

This again, plays a key role for transfer pricing provisions, to not be an issue. Usually, the SMEs involved in Science, Technology, Engineering, Mathematics (STEM) oriented products or services, have the technical people on the driver's seat. Such people are indeed visionary and have a high ambition for success. Their focus is always on STEM analysis, which might make them take a hasty decision, not considering the repercussions through the glasses of transfer pricing norms. It might happen that they choose to go for cheaper options, which are compliance costly, than the relatively expensive ones, but which are at arm's length. Along these lines, it is of sheer value to have a faultless judgment about how the transfer pricing provisions are going to affect even an average, stock related decision.

Case laws:

In *Compaq Computer Corporation v. Commissioner* (1999), a leading case from the United States of America, the issue was about whether the CUP method used by the Assessee, for its inter group transactions, was in accordance with the law, or should it have gone for some other method. The Court, after observing all the attributes, and after satisfying itself, had held that the choice of CUP, by the Assessee was in accordance with the law. The prime factor considered was whether the Assessee was successful in proving that the transaction was at Arm's Length, which had happened so. Hence, the Court had found nothing inaccurate in the Assessee's contention of going ahead with the CUP method.

As discussed extensively earlier, a sound knowledge of the transfer pricing laws is required to have a hassle-free compliance. Here, a SME would definitely have had to inculcate significant resources to get things right, to apply the perfect transfer pricing strategy.

In *DHL Corporation and Subsidiaries v. Commissioner* (1998), another case from the United States of America, the issue was about an ownership of a trademark and how arm's length pricing was coming in prominence. The memorandum of understanding between the parties had been altered 6 times, which was bringing in the contentions. The Court, after satisfying itself, had rejected the contentions of both DHL being the Assessee, and IRS. The ownership rights of Assessee were in itself questioned by the Court. Moreover, the Court had also gone ahead to impose a transfer pricing penalty on the Assessee, because of the questionable way in which the documentation was filed. The Assessee's contention that it was done by the Consultant, hence a third party, was struck down, since the consultant himself was appointed by the Assessee for doing its work. The Court had severely criticized the non-cooperative behavior of the Assessee and IRS. Right from the legal agreements, to conduct of the parties, was brought under the scanner.

This case is a conclusive proof as to how it is a cumbersome task upon SMEs to get their transfer pricing compliances absolutely spot on. This case had the Court, not only quashing the contention of the Assessee, but also penalizing it, for faulty documentation process. Here, the Assessee, being DHL, could afford to adhere to all these penalties, and still carry on its business the world over, it being a large entity. This is next to impossible for a SME. If it ends up committing any such blunders, it might prove to be a death sentence for itself. Accordingly, a SME has to plan out its transactions and calculate the ALP correctly; else, a transfer pricing compliance would end up becoming a priority for it, and not its own products or services. This might totally dampen the spirit of its promoters, if they realize that too much time, and resources, is being diverted not at their core objects, but at the ancillary activities.

In *San Remo Macaroni Co Pty Ltd V. CMR of Taxation* (1998), a leading case from Australia, the issue was about the revaluation of currencies. The Assessee had gained some significant benefit out of a revaluation of Swiss Francs. The stated revaluation had violated the terms of the transfer pricing agreement, which the Assessee had entered into. The Assessee had counter argued that the Commissioner himself had acted in bad faith and had manipulated the accounts. The Court, after satisfying itself from all angles had held that there indeed was a transfer pricing violation as, due to an unprecedented revaluation of currencies. Also, the Court had also observed that the actions of the Commissioner were as per the letter of the law, which had been bestowed upon him. They were neither malicious nor were outside the book.

Since the contention here was about the valuation of Swiss Francs, this case law directly impacts the sustainability of those SMEs which aimed at flexing themselves offshore. There are many SMEs, whose primary clientele itself is an offshore entity. A few cottage industries in India as well, for ex: the manufacturers of handicrafts, textiles, handmade toys, etc., have their underlying cynosure on the entities not situated in India.

For such SMEs, it is an inconceivable notion to accurately know how a valuation norm is to be used. Since, such entities are only capable of focusing on their core business; they tend to take the help of an outside entity. Many a times, the Government, *suo moto*, might launch schemes to assist these entities, with their businesses at the offshore. It is a prevalent practice to incorporate an entity there, which then acts as a face for all such SMEs. This situation ends up relating itself directly with the underlying case law. One cannot expect such SMEs to be actively involved in such background tasks. Hence, the entire compliance work might be performed by an outside consultant, thus again, making it to think twice before the allocation of costs. One might feel that the only downside to all this is the rising costs, however, one should also keep in mind the faltering goodwill, which might crop up after such orders are issued by the Courts. There is only a certain distance that one can travel under the garb of making an 'honest mistake'.

In *Rochester (UK) Limited and Another v Pickin* (1998), a leading case from the UK, the contention was about how it was incorrect for the Assessee to introduce and insert, a Swiss entity, in the chain of supply involving all the related entities, so that the Assessee would end up paying excessively. Such an excessive payment, will incur entries in the expenditures, thus resulting into a decrease in profit, or even loss. Since the taxes in UK were quite high, as compared to the other entities in the supply chain, this small adjustment resulted in the Assessee, paying a significantly less amount of tax. In this case however, the Court had ruled in the favour of the Assessee. The Court's view was that just because an entity has been entered in the supply chain, one cannot automatically assume that the transactions, thenceforth, will be done with an intention to deceive. The

transaction in question, between the Assessee and the Swiss entity, had been done at an Arm's Length. This was the only litmus test required for the Court for its ruling.

This is one of those cases which work as a sigh of relief, especially for the SMEs. The bottom line prevails that as long as the transactions which the Assessee in question, is entering into, are being done at an arm's length basis, the complexity of the transaction is just elementary information. One, especially any government regulatory authority, cannot assume and question it. It is usually seen that at the giant chain of transactions, most SMEs are roped in, by the large entities. Hence, as long as the SMEs are involved in any transaction which is at an arm's length, it should not be the SMEs' worry as to whom and how they will get entangled into a government-oriented enquiry. However, again, for this to work, a proper insight of the transfer pricing laws will be required. An eminent planning for this to fall properly into pieces is the key, for which, a dedicated source is a necessity.

In *Glaxo Group Ltd and others V. Inland Revenue Commissioners* (1996), another case from the UK, the issue was about a requirement of further assessments. The Assessee had already disclosed a price, by making adjustments as per all the rules, regulations and norms of transfer pricing. Yet, a question had arisen about its further assessment. Since the time limit for assessments had also been lapsed, the issue had been blown wide open. The revenue department was of the opinion that the transactions themselves had not been done on an arm's length basis. It is pertinent to note that this case had been appealed by the Assessee. The Court had upheld the previous decision here and had encouraged the commissioner to make the necessary adjustments for an increase in the assessment, at the hearing of the appeal.

The fact that it was appealed makes it critical for the sustenance of the SMEs. It should be noted that the mechanism, allowed for further assessments, and the ruling had not been held, purely on the previously submitted returns. This stance had been taken, and was upheld by the court of law, twice. The SME, hence, again, might enter into a position where, even its well thought out return, by applying the entire know how about the procedures, the consultation of an expert entity, will all seem meaningless, if it opens up for further scrutiny. This again proves to be a battle, keeping in mind the sizes of such SMEs.

In *SmithKline Beecham Animal Health Inc. v. Canada* (2002), a leading case from Canada, the Assessee had paid a certain amount to its non-resident affiliates. The question had arisen about its sanctity, i.e. about the fact that whether these amounts would have differed, had the arm's length principle would have been used. The Assessee had claimed that whatever returns that he had filed and the amount which he had disclosed was based in entirety on the transfer pricing laws. The documents sought were also on its basis. The documents being provided to either of the parties, was a contentious issue, since the parties were expecting for the documents to be provided as per the relevance of facts. The Court observed and had held that only the provision of documents was enough. It was no party's job to make sure that the documents have been arranged as per the requirement of the other.

This case may not be having a direct impact on the SMEs, but certainly, the interpretation surrounding around the provisions of documents is vital. The SMEs, most of the times themselves have a low-standard data maintenance awareness. This being a key aspect of the decisions of the courts, it needs a special attention from the SMEs. This is another aspect which will divest them from their future goals and ambitions.

Conclusion &Recommendations:

From the aforesaid discussion and context, it is clear how a SME has to fight different battles daily, if it indeed plans to survive and sustain its business. To establish this sustainability model, a sturdy legal compliance structure is a requirement. Transactions triggering the provisions of Transfer Pricing are a key aspect of a compliance structure and hence, for this, the following are a few recommendations which a SME can utilize to sustain itself in the market:

1. Foreign ventures are understandable; however, one should plan the channels of foreign investments appropriately. Establishing Special Purpose Vehicles (SPVs) could be avoided if not the need of the hour.

2. Hiring of an experienced, tax compliance expert as a consultant. Experience comes with a price; hence, allocating its funds in the business precisely, by budgeting this cost.

3. Inculcating a habit of being compliant with the laws, especially the taxation laws, from the very stage of the entity's establishment itself. This will allow the SMEs to safeguard itself in testing waters.

Safeguarding the interest of the SMEs is an important function of the governments of the world. Since, it is one way which allows commoners, average individuals, to dream big. Along with the Governmental support, the SMEs should also plan themselves judiciously so that it can not only survive and sustain but thrive in a market. If global dreams are to be fulfilled, the taxation angle can be a boon or a bane, depending upon how well one has understood the laws. Hence, a befitting transfer pricing compliances regime will help the SMEs gain an extensive eminence, among the market forces

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