

Gurugram Branch of ICAI



GCCs - Transfer Pricing & Cross Border Tax Advisory Opportunities

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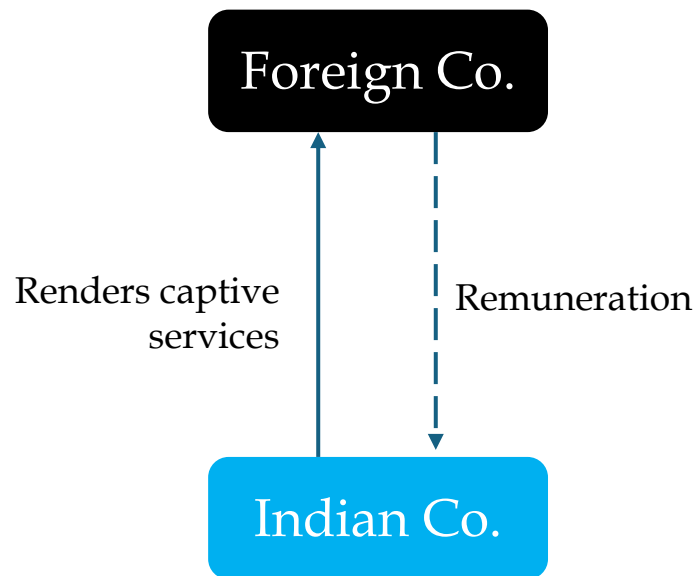
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Meaning of Global Outsourcing

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What is Global Outsourcing?

Global outsourcing refers to delegation of business processes or services by a company in one country to an entity/service provider located in another country.



Key Features

- Cross-border arrangement
- Service-oriented model
- Inter-company transactions
- Cost plus remuneration model common
- Transfer pricing implications arise
- Funding can be structured in tax efficient manner

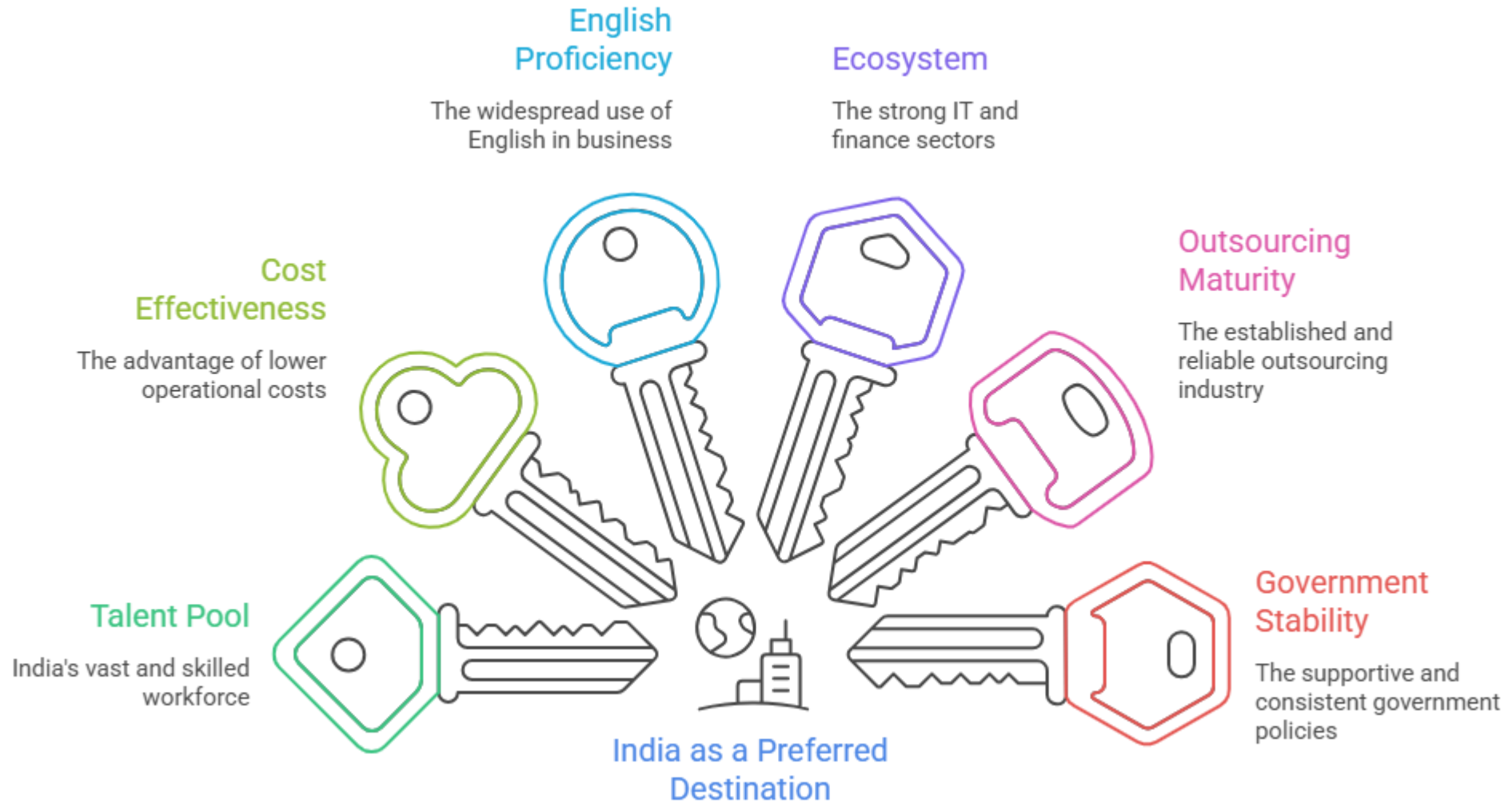
Common Structures

- Third-party outsourcing
- Captive service centres
- Global Capability Centres (GCCs)
- Hybrid models

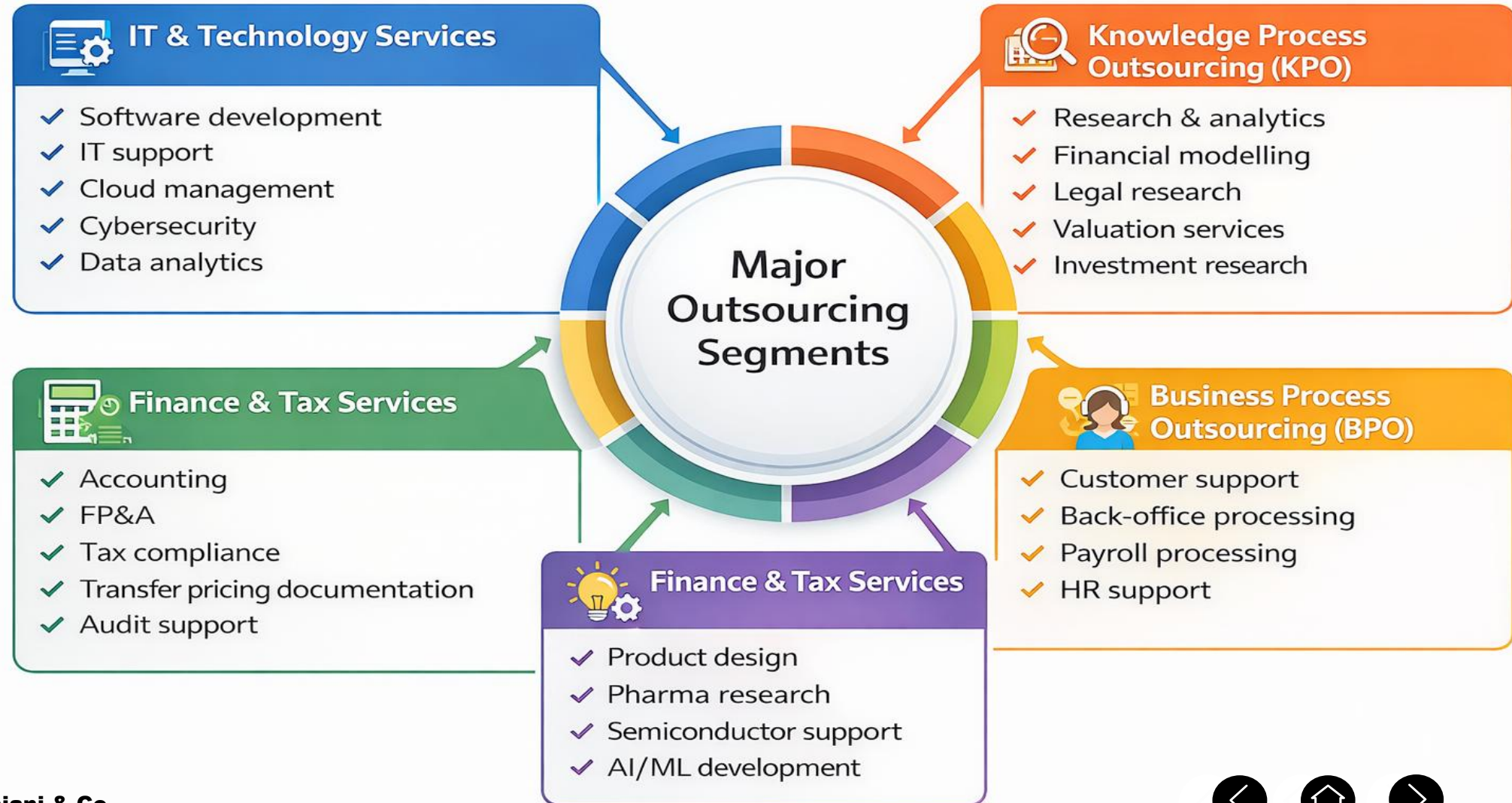


Globalisation & Rise of Outsourcing

Why Companies Outsource Globally?



Major Outsourcing Segments



Common Operating Structures

Operating Structures



Third-Party Vendor Model

Independent service provider with contractual arrangement and less TP exposure.



Captive Service Provider Model

Indian subsidiary provides services exclusively to AE with cost-plus remuneration.



Global Capability Centres (GCCs)

Strategic centres of MNCs performing high-end functions.



Build-Operate-Transfer (BOT) Model

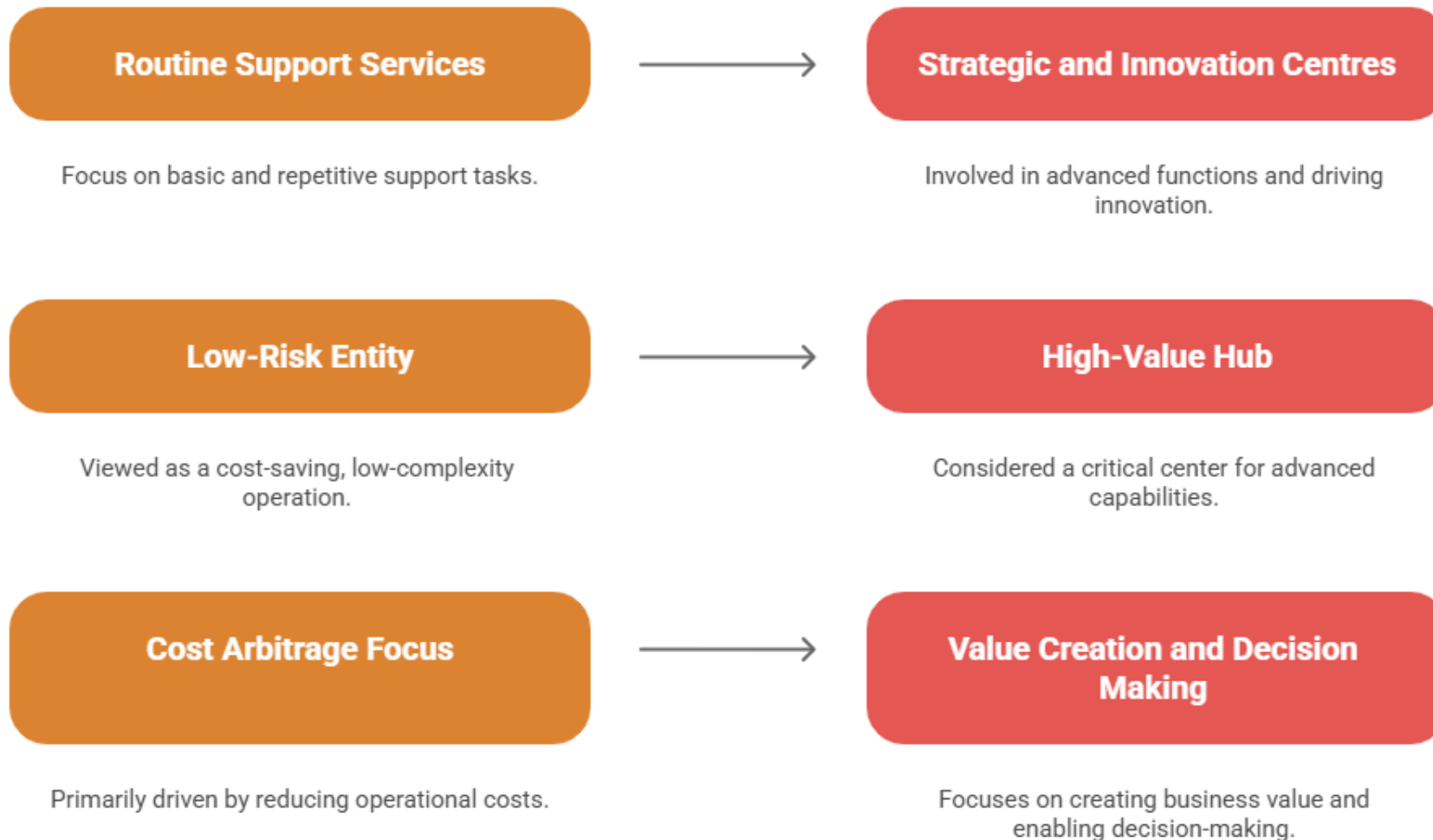
Third party establishes operations and eventually transfers to MNC.



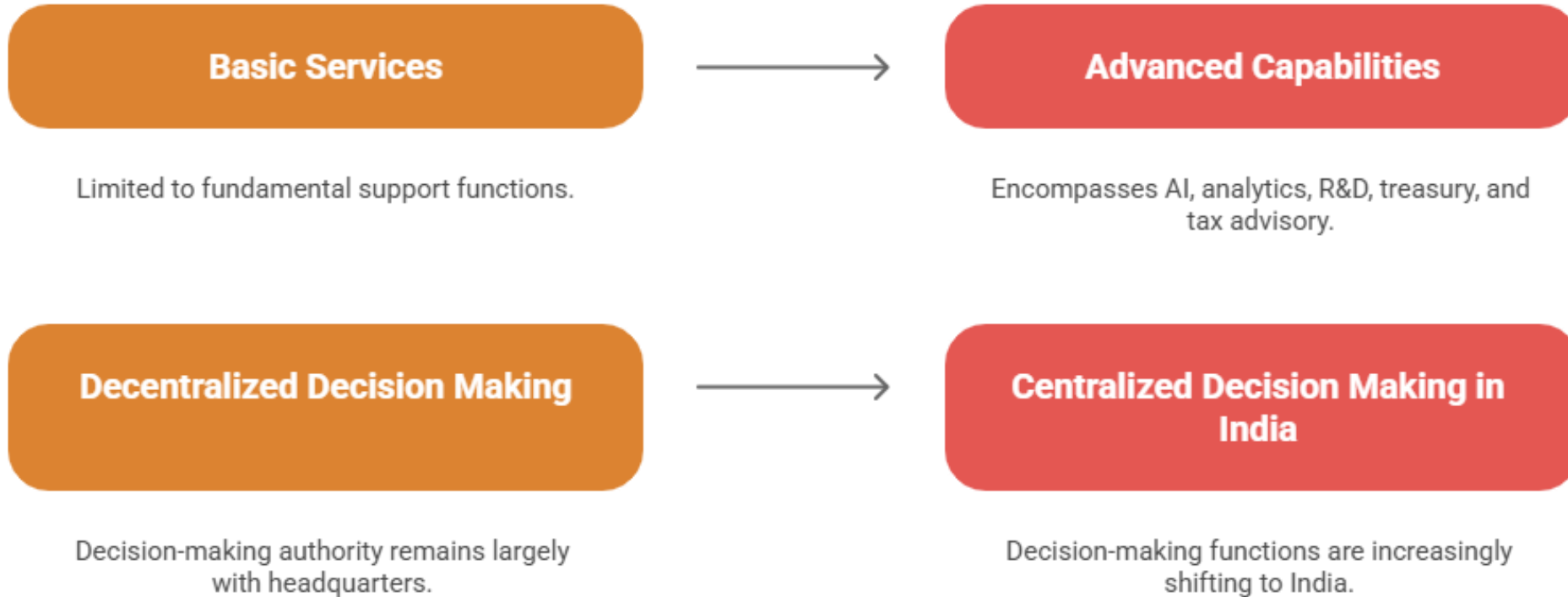
Evolution of GCCs in India



India's GCC Story



India's GCC Story



India's GCC Story

Key Sectors



Technology

GCCs provide software development, cloud services, cybersecurity, AI/ML solutions, and IT support for global technology companies.



Banking & Financial Services

GCCs support financial institutions through risk management, compliance, analytics, investment research, and digital banking operations.



Healthcare

GCCs deliver healthcare analytics, medical billing, clinical data management, telemedicine support, and R&D assistance.



Manufacturing

GCCs assist manufacturers with supply chain management, product design, engineering services, procurement, and process automation.



E-commerce

GCCs manage customer support, digital marketing, data analytics, logistics coordination, and platform technology operations for online businesses.





Transfer Pricing Relevance in Outsourcing

Why TP Becomes Critical?

TP Trigger

GCCs are captive service providers. Thus, revenue from, and cost incurred towards Associated Enterprise(s) is subject to Transfer Pricing regulations.

Common International Transactions

- Provision of IT/ITES services
- Shared services
- Management support services
- Cost allocations
- Royalty and IP usage
- Inter-company reimbursements
- ESOPs

Tax Authority Focus Areas

- Correct characterization
- Correct cost base
- Functional profile
- Profit attribution
- Low margins/ excessive losses
- Substance vs. Form (basis the contractual terms)

Core TP Objective

To ensure transactions are conducted at Arm's Length Price (ALP).



FAR Analysis in Outsourcing Structures

FAR = Functions, Assets, Risks

Functions Performed

- Routine processing
- Technical development
- Decision-making authority
- Customer interaction

Assets Employed

- Human capital
- Technology platforms
- IP ownership
- Infrastructure

Risks Assumed

- Market risk
- Credit risk
- Foreign exchange risk
- Capacity utilisation risk
- Operational risk

Importance

FAR analysis determines:

- Characterisation of the entity (routine captive centre vs. entrepreneurial/value-creating entity)
- Selection of the appropriate transfer pricing method
- Determination of arm's length profitability
- Identification of DEMPE functions and intangible value creation
- Assessment of economic substance over contractual arrangements
- Allocation of profits in line with OECD BEPS principles
- Defence during TP audits, APA proceedings, and litigation

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Arm's Length Principle

Arm's Length Principle (ALP)

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ALP means related-party transactions should be priced as if they were undertaken between unrelated parties under similar circumstances.

OECD Principle

Associated enterprises should earn profits consistent with functions performed, assets used and risks assumed.

Objective of ALP

- Prevent profit shifting
- Ensure fair taxation
- Maintain global tax transparency

Typical Example

Indian captive centre receives: Cost + 12% markup

Question: Is 12% arm's length?



TP Methods used for ALP Determination

Methods under Transfer Pricing Regulations

Traditional Transaction Methods

1. Comparable Uncontrolled Price (CUP)
2. Resale Price Method (RPM)
3. Cost Plus Method (CPM)

Transactional Profit Methods

4. Profit Split Method (PSM)
5. Transactional Net Margin Method (TNMM)

Most Commonly used method(s) by Captive Service Providers

- TNMM - Profit Split method - Where both entities contribute significant intangibles or DEMPE functions

Transactional Net Margin Method - TNMM (Most Common Method)

Concept

- Compare net profit margin earned by tested party with comparable companies.
- Profit Level Indicator (PLI) is usually - Operating Profit / Operating Cost (OP/OC)

Why TNMM Dominates?

- Easier availability of comparables
- Suitable for service entities
- Less affected by transactional differences

Common in India

ITES / BPO / KPO / R&D captive entities



TP Challenges in GCC Models

Major Litigation Areas

Characterisation Disputes

- Routine ITES vs. High-end KPO/Software Development.

Comparable Selection Issues

- Giant companies included
- Functional dissimilarity
- Extraordinary events

Location Savings Debate

Whether Indian cost advantage should increase profits?

DEMPE Concept

Development, Enhancement, Maintenance, Protection and Exploitation of IP.

Major Litigation Areas

DEMPE – Meaning and Impact on Transfer Pricing

DEMPE refers to functions relating to intangibles:

- D – Development
- E – Enhancement
- M – Maintenance
- P – Protection
- E – Exploitation

Introduced under OECD BEPS Actions 8–10, DEMPE focuses on identifying:

- who actually performs key intangible-related functions,
- who controls risks, and
- who creates economic value.

Impact on Transfer Pricing Analysis

DEMPE significantly changed TP analysis by shifting focus from:

- mere legal ownership of IP
to
- actual value-creating activities and substance.

Major Litigation Areas

Key implications:

- Mere funding or legal ownership of IP is not sufficient to claim residual profits.
- Entities performing significant DEMPE functions should receive appropriate returns.
- Captive R&D and GCC structures face greater scrutiny.
- Routine cost-plus models may be challenged where Indian entities contribute to valuable intangibles.
- Functional analysis now heavily examines:
 - ✓ people functions,
 - ✓ decision-making,
 - ✓ control over risk,
 - ✓ and economic substance.

DEMPE has therefore become a central concept in modern transfer pricing and intangible profit allocation.



TP Optimisation Strategies

How Can Structures Be Optimised?

Functional Alignment

Ensure actual conduct matches agreements.

Robust Documentation

- Inter-company agreements
- Invoices
- Benefit analysis
- FAR documentation

Appropriate Characterisation

Avoid mismatch between functions and remuneration.

Advance Pricing Agreements (APA)

- Reduce litigation
- Improve certainty
- Long-term TP stability

Safe Harbour Rules

- Lower compliance burden for eligible taxpayers.
- IT enabled services, knowledge process outsourcing services and contract R&D services relating to software development, to be clubbed together under IT Services
- **Common safe harbour margin of 15.5 percent applicable to all**
- This Safe Harbour margin is **not applicable** to Engineering and Design / Product R&D GCCs

Operational Optimisation

- Centralisation of support services
- Shared service models
- Technology-driven efficiencies



BEPS & Global TP Developments

Emerging Global Tax Landscape

OECD BEPS Framework

Focus on:

- Substance over form
- Profit allocation
- Anti-profit shifting

Pillar One & Pillar Two

Global minimum tax regime.

Impact on Outsourcing

- Increased transparency
- Greater reporting requirements
- Substance-based taxation

Increased Importance of GCCs

India becoming strategic value-creation hub.



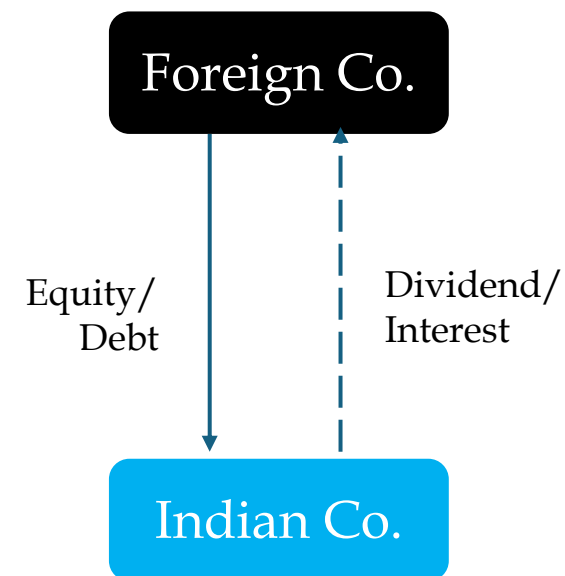
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Funding structuring

Funding structuring

Funding of GCCs

- Significant capital investment may be required for establishing high-end GCCs, particularly in technology, R&D, engineering, and digital transformation sectors.
- Funding for GCC set-up can generally be structured through:
 - ✓ Equity contribution
 - ✓ Debt funding, including External Commercial Borrowings (ECBs)
- Debt funding may provide a tax-efficient mechanism for financing initial infrastructure and operational set-up costs.
- In many captive service models, interest expense generally does not form part of the operating cost base for computing transfer pricing margins under TNMM.
- Accordingly, debt funding may help optimize post-tax returns without directly impacting operating profitability benchmarks.
- However, **limitation on deductibility of interest** under thin capitalization provisions needs to be considered while computing taxable income (Section 94B – Old Act / Section 177 – New Act)



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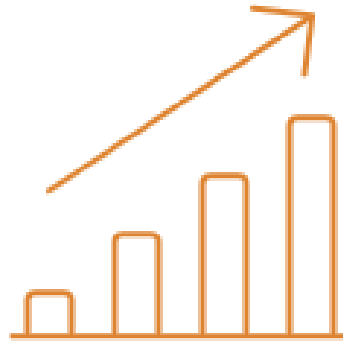
Opportunities for Chartered Accountants

Professional Opportunities



Advisory Areas

TP documentation, Benchmarking studies, APA support, Litigation representation, Cross-border structuring, GCC advisory.



Growing Demand Areas

TP automation, International taxation, Global mobility, Digital taxation, ESG reporting.



Why This Field is Attractive?

High growth area, Global exposure, Strategic consulting opportunities.

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