

**F No. 500/139/2012**  
**Government of India**  
**Ministry of Finance**  
**Department of Revenue**  
**Central Board of Direct Taxes**  
**(Foreign Tax and Tax Research-I Division)**

New Delhi, the 26<sup>th</sup> day of March, 2013

**Circular No. 03 /2013**

**Subject: Circular on conditions relevant to identify development centres engaged in contract R&D services with insignificant risk**

It has been brought to the notice of CBDT that there is divergence of views amongst the field officers and taxpayers regarding the functional profile of development centres engaged in contract R&D services for the purposes of transfer pricing audit. Moreover, while at times taxpayers have been insisting that they are contract R&D service providers with insignificant risk, the TPOs are treating them as full or significant risk-bearing entities and making transfer pricing adjustments accordingly. The issue has been examined in CBDT. It is hereby clarified that a development centre in India may be treated as a contract R&D service provider with insignificant risk if the following conditions are cumulatively complied with:

1. Foreign principal performs most of the economically significant functions involved in research or product development cycle whereas Indian development centre would largely be involved in economically insignificant functions;
2. The principal provides funds/ capital and other economically significant assets including intangibles for research or product development and Indian development centre would not use any other economically significant assets including intangibles in research or product development;
3. Indian development centre works under direct supervision of foreign principal who not only has capability to control or supervise but also actually controls or supervises research or product development through its strategic decisions to perform core functions as well as monitor activities on regular basis;
4. Indian development centre does not assume or has no economically significant realized risks. If a contract shows the principal to be controlling the risk but conduct shows that Indian development centre is doing so, then the contractual terms are not the final determinant of actual activities. In the case of foreign principal being located in a country/ territory widely perceived as a low or no tax jurisdiction, it will be

presumed that the foreign principal is not controlling the risk. However, the Indian development centre may rebut this presumption to the satisfaction of the revenue authorities; and

5. Indian development centre has no ownership right (legal or economic) on outcome of research which vests with foreign principal, and that it shall be evident from conduct of the parties.

The satisfaction of all the above mentioned conditions should be borne out by the conduct of the parties and not merely by the contractual terms.

The above may be brought to the notice of all concerned.

*Batsala Jha Yadav*  
26/3/13

(Batsala Jha Yadav)  
Director APA  
Central Board of Direct Taxes

Copy to:

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9. The Institute of Chartered Accountants of India, IP Estate, New Delhi

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