WHY TRANSFER PRICING ?

	INDIA	BVI	USA
CHAIN OF TRANSACTIONS BETWEEN AE's	*A (Raw material provider) provides X quantity at Rs 100*	*S (Trader)* sales the same at Rs 950	*H (Manufacturer)* process it and sales to Third Party at Rs 1100
CHAIN OF TRANSACTIONS BETWEEN 3rd PARTIES	*A (Raw material provider)* provides X quantity at Rs 350	*B (Trader)* sales the same at Rs 550	*C (Manufacturer)* process it and sales to third party at Rs 1100

- It is clearly evident from the above transactions that A is providing the raw materials to its AE – S, at a lower price than what it charges to B, an unrelated independent party for the same item, and thereby, is conveniently able to manipulate it's reportable profits in India, where tax rates are high.
- Also S is selling the same item entirely to its AE – H, at a higher price than what an independent unrelated party is able to sells at, and thereby, able to shift the profits in the low tax jurisdictions. Furthermore, the taxable profit of H are also decreased, which results in AE – H paying very small taxes in the USA.
- This is the way in which MNE's are able to manipulate the prices at which goods and services are transferred and eventually evade taxes.

<u>CONCLUSION</u>: Transfer Pricing Regulations are aimed at countering the effect of shifting profits within an MNE using favourable transfer prices.

<u>References:</u>

H – Holding Company in USA (High Tax Rates)
S – Subsidiary Company of H in British Virgin Islands (BVI)
A – Subsidiary Company of H in India (High Tax Rates)
B – Third party Company
C – Third party Company
AE's – Associated Enterprises
MNE – Multinational Enterprise