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CBDT clarifies place of effective management guidelines

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The Central Board of Direct Taxes (CBDT) issued a notification on 23 October to clarify the recent place of effective management (POEM) guidelines. The Finance Act 2015 had amended section 6(3) of the Indian Income Tax Act (ITA) to provide that a foreign company would be considered to be an Indian tax resident if its place of effective management is in India. This was made effective from financial year 2016-17 onwards. The CBDT released POEM guidelines in January 2017 laying down guiding principles to determine the place of effective management of foreign companies.

Stakeholders expressed concerns in cases of general and non-specific functions carried out by Indian regional headquarters of a multinational company. As per POEM guidelines, a foreign company would be presumed to have its POEM outside India if (1) its active place of business outside India; and (2) its board meetings are conducted outside India. However, the aforesaid presumption would not hold good if the board of directors (BOD) of foreign subsidiaries stand aside in favour of exercise of control by their Indian holding company/shareholders/any other person resident in India (standing aside), in which case the POEM would be considered to be in India. The POEM guidelines also clarified that mere following of the global policy of the group laid down by the parent entity (in the field of payroll functions, accounting, human resource functions, IT infrastructure and network platforms, supply chain functions, routine banking operational procedures) would not constitute BOD standing aside so long as the functions performed under the global policy was not specific to any entity or group of entities.

While POEM guidelines addressed a situation involving foreign subsidiaries following the global policy laid down by its Indian holding company, it did not address the situation of an MNC having Indian regional headquarters with Indian employees that follow the global policy laid down by the MNC in relation to its subsidiaries/other constituents of the group company.

The clarification provides that where Indian regional headquarters act for its subsidiaries/other constituents of the group company situated in its region of responsibility as per the global policy laid down by the MNC, it would not constitute a case of the BOD standing aside and, should not lead to establishment of POEM of such subsidiaries/other constituents in India. That said, the benefit shall apply only if (1) functions carried out the Indian regional headquarters are pay roll, accounting, human resources, IT infrastructure, network platforms, supply chain and routine banking functions; and (2) the functions performed are not specific to any entity or group of entities. The clarification also provides that the benefit is subject to general anti-avoidance rules under the ITA.

The business law digest is compiled by Nishith Desai Associates (NDA). NDA is a research-based international law firm with offices in Mumbai, New Delhi, Bengaluru, Singapore, Silicon Valley and Munich. It specializes in strategic legal, regulatory and tax advice coupled with industry expertise in an integrated manner.