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Newsflash: Income Tax – Regional Headquarter of Foreign Multinationals in India would not create POEM exposure where activities are of routine nature

Circular No.25 OF 2017, dated 23-10-2017



1.0 Background

- The new tax residency rule for foreign companies based on the concept of Place of Effective Management ('PoEM') has been effective since 1st April, 2017, i.e., Assessment Year 2017-18 onwards.
- The final guidelines for determining the PoEM was issued on 24 January 2017 vide Circular No. 06 of 2017. The guidelines essentially categorize foreign companies into two categories viz. Active Company and Passive Company.
- For Active Company, PoEM is presumed to be outside India if the majority meetings of the board of directors (BoD) of the company are held outside India. However, if on the basis of facts and circumstances, it is established that the BoD of the company are standing aside and not exercising their powers of management and such powers are being exercised by either the holding company or any other person (s) resident in India, then the PoEM shall be considered to be in India. For this purpose, it has been provided that merely because BoD follows general and objective principles of global policy of the group laid down by the parent entity which may be in the field of Pay roll functions, Accounting, Human resource (HR) functions, IT infrastructure and network platforms, Supply chain functions, Routine banking operational procedures, and not being specific to any entity or group of entities per se; would not constitute a case of BoD of companies standing aside.
- It has been further clarified that the PoEM guidelines shall not apply to companies having turnover or gross receipts of INR. 500 million or less in a financial year.
- Foreign Multinational Companies (MNCs) often establish regional headquarter structure to centralize administrative and management functions across that region. Such headquarter have premises, local staff and senior personnel responsible for the management of the business in that region.

2.0 Issue raised before the CBDT

In context of Foreign MNCs with regional headquarter structure in India, a query was raised as to whether PoEM may be triggered merely on the ground that certain employees having multi-country responsibility or oversight over the operations in other countries of the region are working from India, and consequently, their income from operations outside India may be taxed in India.

3.0 CBDT's Clarification

In this regard, it has been clarified that Regional Headquarter would not create PoEM exposure for subsidiaries / group companies in a region so long as it operates within the general and objective principles of global policy of the group laid down by the parent entity in the field of Pay roll functions, Accounting, HR functions, IT infrastructure and network platforms, Supply chain functions, Routine banking operational procedures, and not being specific to any entity or group of entities per se. In such case, it would, in itself, not constitute a case of BoD of companies standing aside.

Towards the end, the CBDT has specifically mentioned that the provisions of General Anti-Avoidance Rule (GAAR) may get triggered in such cases where the above clarification is found to be used for abusive/aggressive tax planning.

4.0 Our Comments

The above clarification is helpful in case of Foreign MNCs having regional Headquarter structure in India carrying out routine functions. However, it is worthwhile to note that where activities of regional headquarter involve setting policies and strategies for the subsidiaries in the region, it may be said that BoD of foreign subsidiaries are standing aside and thus create PoEM exposure in India.

Another aspect which has now been clarified through this Circular is that the interplay between GAAR and PoEM. The concept of PoEM is one of substance over form and in that sense it is a Special Anti-Avoidance Rule (SAAR), and therefore, normally GAAR should not be applied. However, as the concept of PoEM, including guidelines thereon may itself be subject to manipulation, GAAR can be invoked to deal with abusive/aggressive tax planning.

In the light of above, it would be advisable for Foreign MNCs to evaluate the existing activities of regional headquarters situated in India.



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