

Decoding Place of Effective Management:

1. Place of Effective Management is an internationally acceptable test to determine whether a company incorporated in a foreign jurisdiction is a tax resident of another country. Place of effective management means a place where Key management, and commercial decisions that are necessary for the conduct of the business of an entity as a whole are in substance made.
2. The place of effective management in case of a company engaged in active business outside India shall be presumed to be outside India if the majority meetings of the board of directors of the company are held outside India.
3. It may be noted that an entity may have more than one place of management, but it can have only one place of effective management at any point of time. Since “residence” is to be determined for each year, POEM will also be required to be determined on year to year basis. The process of determination of POEM would be primarily based on the fact as to whether or not the company is engaged in active business outside India.
4. A set of guiding principles to determine POEM has been issued by CBDT vide Circular No. 06 of 2017 dated 24.01.2017. The intent is to target shell companies and companies which are created for retaining income outside India although real Control and management of affairs is located in India. Further, Circular No 8 of 2017 dated 23.02.2017 clarifies that section 6(3)(ii) shall not apply to companies having turnover or gross receipts of Rs.50 Crore or less in a financial year.

5. It is reiterated that the above principles for determining the POEM are for guidance only. No single principle will be decisive in itself. The above principles are not to be seen with reference to any particular moment in time rather activities performed over a period of time, during the previous year, need to be considered. In other words a “snapshot” approach is not to be adopted. Further, based on the facts and circumstances if it is determined that during the previous year the POEM is in India and also outside India then POEM shall be presumed to be in India if it has been mainly /predominantly in India.

6. It needs to be emphasized that the determination of POEM is to be based on all relevant facts related to the management and control of the company, and is not to be determined on the basis of isolated facts that by itself do not establish effective management, as illustrated by the following examples:

(i) The fact that a foreign company is completely owned by an Indian company will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.

(ii) The fact that there exists a Permanent Establishment of a foreign entity in India would itself not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.

(iii) The fact that one or some of the Directors of a foreign company reside in India will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.

(iv) The fact of, local management being situated in India in respect of activities carried out by a foreign company in India will not , by itself, be conclusive evidence that the conditions for establishing POEM have been satisfied.

(v) The existence in India of support functions that are preparatory and auxiliary in character will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.

7. As per the Circular No. 06, A company shall be said to be engaged in “active business outside India” if the passive income is not more than 50% of its total income; and

(i) less than 50% of its total assets are situated in India; and

(ii) less than 50% of total number of employees are situated in India or are resident in India; and

(iii) the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.

8. Passive income of a company shall be calculated as the sum of Income from the transactions, where both the purchase, and the sale of goods is from/ to its Associated Enterprises AND Income by way of royalty, dividend, capital gains, interest or rental income. However, interest income of banking companies and public financial institutions would not be regarded as passive income.

https://www.incometaxindia.gov.in/news/circular06_2017.pdf