



CBDT issues a final notification on special transitional provisions for a foreign company said to be resident in India on account of POEM

The Finance Act, 2015 amended the provisions dealing with the residential status of a company under Section 6(3) of the Income-tax Act, 1961 (the Act). It provides that a company would be resident in India in any previous year if it is an Indian company or its Place of Effective Management (POEM) in that year is in India. In the context of the implementation of POEM based residence rule, certain issues relating to the applicability of current provisions of the Act to a company which is incorporated outside India and has not earlier been assessed to tax in India have arisen. In particular, the issues are related to applicability of specific provisions of the Act like advance tax payment, Tax Deduction at Source (TDS) provisions, computation of total income, set off of losses and manner of application of transfer pricing provisions. In order to provide clarity in respect of the implementation of POEM based rule of residence and also to address concerns of the stakeholders, provisions of Section 115JH of the Act have been introduced with effect from Assessment Year 2017-18.

Section 115JH of the Act, inter alia, provides that the central government may notify exception, modification and adaptation subject to which, provisions of the Act relating to computation of total income, treatment of unabsorbed depreciation, set off or carry forward and set off of losses, collection and recovery and special provisions relating to avoidance of tax shall apply.

In 2017, the Central Board of Direct Taxes (CBDT) issued draft notification¹ providing such exception, modification and adaptation for application of provisions of the Act. Recently, CBDT has issued final notification² dealing with special transitional provisions for a foreign company said to be a resident in India on account of POEM. The notification deemed to come into force from 1 April 2017.

A comparison of the draft and final notification and the key differences between them are as follows:

Clause no. in final notification	Draft Notification	Final Notification
A	Exceptions, modifications and adaptations	
	<i>WDV of the depreciable asset</i>	
(i)(a)	If the foreign company is assessed to tax in the foreign jurisdiction ³ , the Written Down Value (WDV) of the depreciable asset as per the tax record in the foreign country on the 1st day of the previous year shall be adopted as the opening WDV for the relevant previous year.	Principally same
(i)(b)	—	In a case not covered by (i)(a) above, the WDV shall be calculated in the manner, as though the asset was installed, utilised and the depreciation was actually allowed as per the provisions of the foreign laws and the

¹ Draft Notification, dated 15 June 2017

² CBDT Notification No. 29/2018, dated 22 June 2018

³ The term 'foreign jurisdiction' is defined to mean the place of incorporation of the foreign company.

		WDV so arrived at as on the 1st day of the previous year, shall be adopted to be the opening WDV for the said previous year.
(ii)	If the foreign company is not assessed to tax in the jurisdiction where it is based, then WDV of the depreciable asset as appearing in the books maintained in accordance with the laws of that foreign jurisdiction shall be adopted.	Additionally, it has been stated that the WDV of the depreciable asset as appearing in the books of account as on the 1st day of the previous year shall be adopted as the opening WDV.
	<i>Brought forward losses and unabsorbed depreciation</i>	
(iii) to (vi)	<p>If the foreign company is assessed to tax in the foreign jurisdiction, its brought forward loss or unabsorbed depreciation as per the tax record shall be determined year wise on the 1st day of the previous year in which it is said to be resident in India. They shall be deemed as losses or unabsorbed depreciation brought forward on the 1st day and shall be allowed to be set off and carried forward in accordance with the provisions of the Act.</p> <p>Where the foreign company is not assessed to tax in the foreign jurisdiction, its brought forward loss or unabsorbed depreciation as per the books prepared in accordance with the foreign laws shall be determined year wise on the 1st day of the previous year in which it is said to be resident in India. They shall be deemed as losses or unabsorbed depreciation brought forward on the 1st day and shall be allowed to be set off and carried forward in accordance with the provisions of the Act.</p>	<p>The words 'brought forward loss and unabsorbed depreciation' are used instead of 'brought forward loss or unabsorbed depreciation.'</p> <p>The final notification clarifies that the brought forward loss and unabsorbed depreciation of the foreign company shall be deemed as loss and unabsorbed depreciation brought forward as on the 1st day of the said previous year and it shall be allowed to be set off and carried forward in accordance with the provisions of the Act for the remaining period calculated from the year in which they occurred for the first time taking that year as the first year.</p> <p>Further, the losses and unabsorbed depreciation of the foreign company shall be allowed to be set-off only against such income of the foreign company which has become chargeable to tax in India on account of it becoming as Indian resident.</p> <p>Additionally it has been stated that in the cases where the brought forward loss and unabsorbed depreciation originally adopted in India are revised or modified in the foreign jurisdiction due to any action of the tax authority, the amount of the loss and unabsorbed depreciation shall be revised or modified for the purposes of set off and carry forward.</p>
vii	In case where the accounting year does not end on 31 March, the foreign company shall be required to prepare Profit & Loss Account and Balance Sheet for the period starting from the date on which the accounting year immediately following said accounting year begins, to 31 March of the year immediately preceding the period beginning with 1 April and ending on 31 March during which the foreign company has turned resident. The foreign company shall also be required to prepare Profit & Loss Account and Balance Sheet for succeeding periods of twelve months, beginning from 1 April and ending on 31 March, till the year the said foreign company remains resident in India on account of its POEM.	No change
viii	For the purpose of carry forward of loss, in case where the accounting year does not end on 31 March and the period starting from the date on which the immediately following year begins on 31 March of the	This clause has been extended to 'unabsorbed depreciation' also

	<p>year, immediately preceding the period beginning with 1 April and ending on 31 March during which the foreign company has turned resident, is –</p> <ul style="list-style-type: none"> ➤ Less than six months, it shall be included in that accounting year ➤ Equal to or more than six months, that period shall be treated as a separate accounting year. <p>Thus, if the accounting year of the foreign company is the calendar year, the accounting year immediately preceding the accounting year in which the foreign company is held to be resident in India on the basis of its POEM, shall be increased by three months⁴ and if the accounting year of the foreign company is from 1 July to 30 June, the accounting year immediately preceding the accounting year in which the foreign company is held to be resident in India on the basis of its POEM, shall be of nine months from 1 July to 31 March.</p>	
ix	—	In cases covered in point no. (viii), loss and unabsorbed depreciation as per tax record or books of account of the foreign company shall be allocated on a proportionate basis.
x	Where more than one TDS related provisions of Chapter XVII-B of the Act apply to the foreign company as a resident as well as the foreign company, the provisions applicable to the foreign company shall apply.	The term 'alone' is inserted to provide that the TDS related provisions applicable to the foreign company alone shall apply.
xi	—	Compliance to the TDS related provisions of Chapter XVII-B of the Act as are applicable to the foreign company prior to its becoming Indian resident shall be considered sufficient compliance.
xii	The provisions of Section 195(2) ⁵ of the Act shall apply in such manner so as to include payment to the foreign company.	No change
xiii	Once the foreign company is held to be resident in India on account of its POEM in India, it shall be entitled to relief or deduction of taxes paid under the provisions of Section 90 or Section 91 of the Act.	No change
xiv	—	In case where income on which foreign tax has been paid or deducted, is offered to tax in more than one year, Foreign Tax Credit (FTC) shall be allowed across those years in the same proportion in which the income is offered to tax or assessed to tax in India in respect of the income to which it relates and shall be in accordance with the provisions of Rule 128 of the Income-tax Rules, 1962 (the Rules).

⁴ i.e., 1 January to 31 March

⁵ Section 195(2) – Where person responsible for paying any sum chargeable under the Act to a non-resident considers that the whole of such sum would not be income chargeable in the case of the recipient, he may make an application to the AO to determine, the appropriate proportion of such sum so chargeable and upon determination, tax shall be deducted under Section 195(1) of the Act only on that proportion of the sum which is so chargeable

xiv Explanation (ii)	The rate of exchange for conversion into rupees of value expressed in foreign currency, wherever applicable, shall be in accordance with the provision of Rule 115 of the Income-tax Rules, 1962.	No change
B	—	The exceptions, modifications and adaptations referred above shall not apply in respect of such income of the foreign company becoming Indian resident on account of its POEM in India which would have been chargeable to tax in India, even if the foreign company had not become Indian resident.
C	—	In a case where the foreign company is said to be resident in India during a previous year, immediately succeeding a previous year during which it is said to be resident in India; the exceptions, modifications and adaptations referred above shall apply to the said previous year subject to the condition that the WDV, the brought forward loss and the unabsorbed depreciation to be adopted on the 1st day of the previous year shall be those which have been arrived at on the last day of the preceding previous year in accordance with the provisions of this notification.
D	The above exceptions, modifications and adaptations shall be applicable where a foreign company is said to be resident in India in any previous year on account of its POEM being in India and such foreign company has not been resident in India in any of the previous years preceding the said previous year for the purposes of taxation of said foreign company only and all transactions of the said foreign company with other person or entity under the Act shall not be altered only on the ground that the said foreign company has turned resident on account of its POEM being in India.	Principally same
E	Subject to the above, the foreign company shall continue to be treated as a foreign company even if it is said to be resident in India on account of its POEM being in India and all the provisions of the Act shall apply accordingly. Consequently the provisions specifically applicable to: <ul style="list-style-type: none"> • A foreign company shall continue to apply to it; and • Non-resident persons shall not apply to it and the provisions specifically applicable to a resident shall apply to it. 	No change
F	The rate of tax in case of a foreign company shall remain the same, i.e., the rate of income-tax applicable to the foreign company; even though residency status of the foreign company changes from non-resident to a resident on the basis of POEM.	Additionally, it has been stated that in case of conflict between the provision applicable to the foreign company as a resident and the provision applicable to it as a foreign company, the latter shall generally prevail.

Our comments

CBDT has issued the much awaited final notification on transitional provisions for a foreign company said to be resident in India on account of POEM. The final notification provides certain additional provisions viz. deemed computation of WDV considering the depreciation, restriction on the period for allowability of the brought forward loss and unabsorbed depreciation, allowability of such loss and depreciation on a proportionate basis where accounting period followed by the foreign company is different, etc.

Relief is given to foreign companies by providing that the compliance of TDS provisions prior to becoming Indian resident shall be considered as sufficient compliance. In addition to the allowability of FTC, it is provided that the FTC will be allowed on proportionate basis depending upon years over which income is offered to tax or assessed to tax in India.

The exceptions, modifications and adaptations shall not apply in respect of such income of the foreign company becoming Indian resident on account of its POEM in India which would have been chargeable to tax in India, even if the foreign company had not become Indian resident.

The draft notification as well as the final notification state that the tax rate applicable to a foreign company will remain same under the POEM situation. It has been clarified that in case of conflict between the provisions applicable to a foreign company as a resident and the provisions applicable to it as a foreign company, the latter shall generally prevail.

The notification does not deal with some specific issues like applicability of Indian transfer pricing provisions, advance tax provisions, advance ruling provisions, etc. to the foreign companies becoming resident on account of POEM.

The foreign companies would require to evaluate the impact of the final notification depending upon the facts of each case.

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