

Residential Status of An Individual, Post Budget 2020

Determination of the residential status in India as per the Income-tax Act, 1961 is the first and foremost pursuit to compute any person's taxable income in India. In other words, every person – citizen or non-citizen, corporate or non-corporate – who may be liable to pay Income-tax in India needs to determine the residential status as per the provisions of the Act. It is the residential status of any person that determines, the incomes on which the person would be liable to pay tax in India and at specified rates, the applicability of various provisions of Direct Tax Avoidance Agreements (DTAAs), the availment of Foreign Tax Credits (FTCs), the extent of declarations and forms required to be submitted to the Income Tax Department, etc. Read on....



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The Income-tax Act, 1961 (hereinafter referred to as “the Act”) provides for three categories of residential status in India – Resident, Not Ordinarily Resident and Non-Resident..

1. Definition

Section 2(42) defines “resident” as - “resident” means a person who is resident in India within the meaning of Section 6” and Section 2(30) defines “non-resident” as - “non-resident” means a person who is not a “resident”.....

Therefore, the term “Not Ordinarily Resident” has not been explicitly defined in the Act but can be derived from the definitions of other two terms. Basically, *not ordinarily resident*

status is a transition phase when a person gets transferred from the status of “non-resident” to the status of “resident”. This has been provided under the Act so that the ambit of tax in India does not get increased all of a sudden for a non-resident.

2. Criteria (refer summarised chart also)

Section 6 of the Act lays different principles to determine the residential status for different categories of persons – individuals, Hindu Undivided Family, firm, or other association, company, and every other person. Here, we shall discuss provisions relating only to the determination of individual's residential status.





Not ordinarily resident status is a transition phase when a person gets transferred from the status of “non-resident” to the status of “resident”.

• Criteria under the Act to treat an individual as “resident” in India

An individual – citizen or non-citizen - is said to be resident in India, for the year, if he:

- is in India in that year for a period or periods amounting in all to 182 days or more; or
- having within the four years preceding the year under consideration been in India for a period or periods amounting in all to 365 days or more *and* is in India for a period or periods amounting in all to 60 days* or more in the year under consideration; or
- being a citizen of India, having total income, other than the income from foreign sources[#], exceeding ₹ 15 lakhs during the year and is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.

* Exceptions to the criterion of 60 days

- The criterion of 60 days shall be raised to 182 days in following cases:
 - in case of a person being a citizen of India, who leaves India as a member of the crew of an Indian ship, or for the purposes of employment outside India, and
 - in case of a person being

a citizen of India or a person of Indian origin who, being outside India, comes on a visit to India.

- The criterion of 60 days shall be raised to 120 days in case of the citizen or person of Indian origin having total income, other than the income from foreign sources, exceeding ₹15 lakhs during the year.

Income from foreign sources

Income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India i.e. this shall be included in calculating the threshold).

• Criteria under the Act to treat an individual as “non-resident” in India

An individual who does not meet any of the conditions laid for a “resident” shall be treated to be a “non-resident” for the purposes of the Act.

• Criteria under the Act to treat an individual as “not ordinarily resident” in India

An individual is said to be “not ordinarily resident” in India if he:

- has been a **non-resident** in India in **nine out of the ten years** preceding the year under consideration; or
- has during the **7 years** preceding the year under consideration **been in India** for a period of, or periods amounting in all to, **729 days or less**; or
- is a person referred to in point (c) of “resident” criteria or point (B) of “Exceptions to the criterion of 60 days” of “resident” criteria above.

3. Incomes taxable in India

As per Section 5 of the Act, following are the incomes which shall be taxable in India depending on the residential status of an individual:

S. No.	Nature of income/ Residential Status	Received or is deemed to be received in India	Accrues or Arises or is deemed to accrue or arise to him in India	Accrues or Arises to him outside India
1	Resident	✓	✓	✓
2	Not ordinary resident	✓	✓	✗ [^]
3	Non-resident	✓	✓	✗

[^] included if it is derived from a business controlled in or a profession set up in India.

Analysis

Assessee’s perspective

- Marginal relief for this amendment has been given by the Memorandum to Finance Bill, 2020. It states that there are cases in which individuals who are actually carrying out substantial economic activities from India manage their period of stay in India, so as to remain a non-resident in perpetuity and therefore not required to declare their global

income in India.

It is entirely possible for an individual to arrange his affairs in such a manner that he is not liable to tax in any country during a year. This arrangement is majorly employed by high net worth individuals (HNWI) to avoid paying taxes to any country. The current rules governing tax residence makes it possible for HNWIs and other individuals, who may

be Indian citizen to not to be liable for tax anywhere in the world. Such a circumstance is certainly not desirable; particularly in the light of current development in the global tax environment where avenues for double non-taxation are being systematically closed.

2. Before the amendment by the Finance Act, 2020, an individual who is an Indian citizen or a person of Indian origin was virtually under the ambit of only 182 days criterion, i.e., if such individual lives outside India and comes to India only for the purpose of visit, then he could have stayed in India for any period less than 182 days and he would still be classified as non-resident and therefore, any of his income which accrues or arises outside India would remain outside the ambit of tax in India.
3. Now, after the amendment by the Finance Act, 2020, above criterion shall stand restricted only to such Indian

citizens or persons of Indian origin who live outside India and come to India only for the purpose of visit and have income upto ₹15 lakhs from sources other than foreign sources.

4. For Indian citizens and persons of Indian origin whose income from sources other than foreign sources exceeds ₹ 15 lakhs, following shall be the criteria:

S.N.	Individual is	Category
1	Indian citizen not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.	Not ordinary resident
2	(i) Indian citizen other than above i.e. he is liable to pay tax in any other country or he is not liable to pay tax in any other country because of reason other than his domicile or residence or any other criteria of similar nature, or (ii) Person of Indian origin who has been in India for less than 120 days	Non-resident
3	(i) Indian citizen as referred to in S.N. 2, or (ii) Person of Indian origin who has been in India for 120 days or more but less than 182 days in this year and has been in India for 365 days or more in 4 preceding years	Not ordinary resident
4	(i) Indian citizen as referred to in S.N. 2, or (ii) Person of Indian origin who has been in India for 120 days or more but less than 182 days in this year and has been in India for less than 365 days in 4 preceding years	Non-resident



The current rules governing tax residence makes it possible for HNWI and other individuals, who may be Indian citizen to not to be liable for tax anywhere in the world. Such a circumstance is certainly not desirable; particularly in the light of current development in the global tax environment where avenues for double non-taxation are being systematically closed.

It is needless to mention here that if any individual is in India for 182 days or more, he shall automatically be treated as resident subject to other two conditions, fulfilling which he shall be classified as not ordinary resident.

5. In accordance with above analysis, it can be concluded, for persons mentioned in table above, that:
 - (i) because of the amendment made through the Finance Act, 2020 the residential status can be raised only to the level of not ordinary resident and not to the level of resident.
 - (ii) the ambit of taxation in India will get increased **only to** income derived from a business controlled

in or a profession set up in India.

- (iii) the disclosure requirements under Schedule FA – for foreign assets and Schedule AL – for assets and liabilities (except for Indian assets) shall not apply, as instructions to file Income Tax Returns explicitly exempt / reduce the ambit of disclosure for not ordinary residents.
- (iv) the amended Act distinguishes between the Indian citizens who are not liable to tax anywhere in the world **because of their residential status** and those who are not liable to tax anywhere in the world **because of any**

other criteria.

- (v) citizens of India, who come under the ambit of this amendment will need to decide the reason because of which they are not liable to tax in any other country and upon such determination, the criteria for determining their residential status in India can be ascertained.

Government's perspective

India is the largest recipient of personal remittances in the world. India's personal remittances receipts in 2019, in accordance with the World Bank's data, stand over US \$83 billion. As per data from various other sources, including that from RBI, majority portion of this remittance is received from the Gulf Cooperation Council (GCC) countries (United Arab Emirates (UAE), Saudi Arabia, Qatar, Kuwait, Oman).

Majority portion of these remittances is for the purpose of Family maintenance, followed by Deposits in banks, Others, and Investments (land property / equity shares).

There is a common perspective that after the amendment in residential status by Finance Act, 2020, India may lose a portion of personal remittances sent by number of Indian citizens or persons of Indian origin working abroad. This argument is made on the ground that majority of GCC countries including UAE, Qatar, Kuwait and Oman do not levy any tax on individual's income because of which all Indian citizens or persons of Indian origin working in such countries will now come under the ambit of Indian Income-tax law and will have to pay taxes on their global income.

However, in accordance with analysis done above, it is clear that there is no provision inserted under the Act which makes Indian citizen or person

of Indian origin residing and earning abroad as 'resident' for the purpose of levying tax on their foreign incomes in India. Residential status of Indian citizens having income exceeding ₹ 15 lakhs in India including income derived from a business controlled in or a profession set up in India, can only be raised to 'not ordinary resident' in India for the purpose of Indian Income-tax law and therefore, *income which accrue or arise to such citizens outside India except income derived from a business controlled in or a profession set up in India shall not be taxable in India.* Further, disclosure requirements for such citizens and persons of Indian origin shall be limited. *However, there will now be a reduction in number of days for which such citizens or persons of Indian origin can stay in India.*

Therefore, there is no reason because of which there may be a reduction in above remittances. However, business investments by such citizens and persons of Indian origin may see a slump because of increased taxability ambit on business incomes of such citizens and persons of Indian origin.

Issue in the drafting of amendment

Clause (1) of Section 6 of the Act states the criteria of 182 days and 365 days for any individual to be classified as resident.

For making amendment in the Act, the Finance Act has inserted clause (1A) after clause (1) in Section 6.

Clause (1A) reads as under:

"Notwithstanding anything contained in clause (1), an individual, being a citizen of India, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year shall be deemed to be resident in India in that previous year, if he is not liable to tax in any other country or territory by reason of his domicile or residence or any



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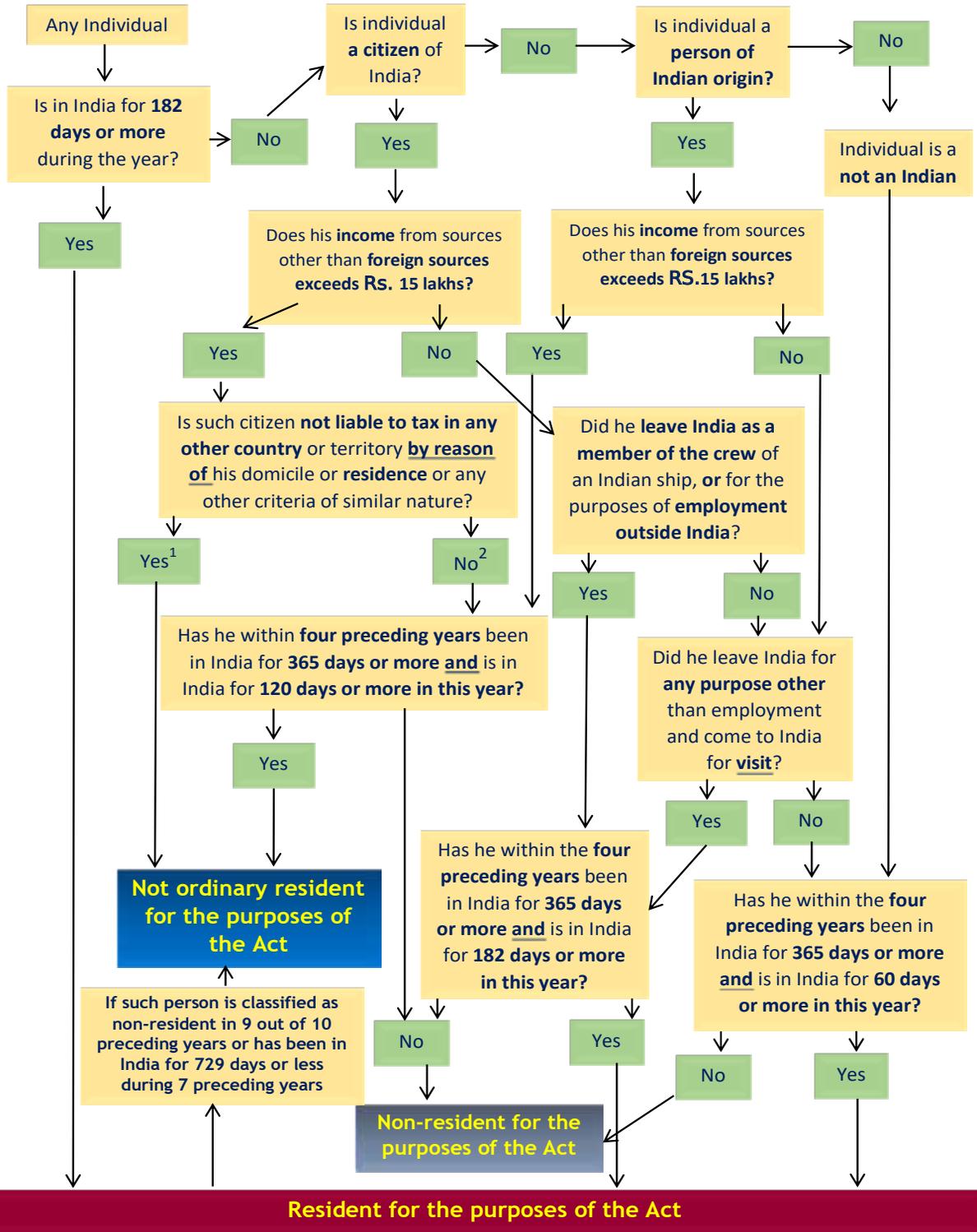
other criteria of similar nature,"

Now, clause (1A) clearly overrules clause (1). All the conditions, viz. individual shall be an Indian citizen, Indian sources income exceeds ₹ 15 lakhs and he shall not be liable to tax in any other country by reason of his domicile or residence, can virtually be satisfied by any Indian citizen i.e. even by those who permanently reside in India.

Further, newly inserted sub-clause (d) in clause (6) of Section 6 makes above persons as 'not ordinary resident' and therefore by virtue of clause (1A) read with clause (6) of Section 6 of the Act, any Indian citizen can be classified as 'not ordinary resident' and thereafter he is not required to pay tax on global income in India. Furthermore, the disclosure requirements will also get reduced.

The above interpretation can never be the intent of the amendment, therefore, clarification in this regard is awaited.

Summarised chart for the determination of residential status of an individual under the Act



1. i.e. he is not liable to pay tax in that country because of the above reason.

2. i.e. he is liable to pay tax in that country or not liable to pay tax in that country because of reason other than that mentioned above.

