

Residential Status under the Income Act, 1961 in light of Finance Act, 2020
written by Gaurav Purohit | June 6, 2020



In India, the residential status of a person plays a vital role in determining the taxability of income of any person. The Income Tax Act, 1961 follows the residence-based taxation system wherein the income is taxed on the basis of the residential status of the taxpayer. Contrary to the popular notion that taking up of foreign nationality will attract tax benefits, the Citizenship of any individual has very limited relevance as far as Indian taxation is concerned. Even Double Taxation Avoidance Agreements ("DTAA") entered into by India follows the principle of residential status and has nothing to do with citizenship.

Affect of Finance Act on Residential Status and Tax Burden

Section 6 of the Income Tax Act, 1961[1] divides the assesses into four categories i.e. Individual, Hindu Undivided Family, Company and other persons. Further, the individual assesses on the basis of his residential status is divided into two categories i.e. Resident and Non-Resident and Resident is further subdivided into Ordinary Resident and Non-Ordinary Resident. This article discusses the tax liability of an Individual Resident and Resident but Not Ordinary Resident ("RNOR/NOR") in light of Finance Act, 2020.

WHO IS A RESIDENT?

As per the Section 6(1) of the Income Tax Act, 1961[2] an individual is considered to be a Resident if one of the two conditions is fulfilled:

1. If an individual, during the relevant year, stays in India for 182 days or more, or
2. If an individual who stays in India for 365 days or more during the preceding four years and his period of stay during the relevant year is 60 days or more.

Further, the explanation to Section 6(1) provides relaxation with respect to the number of days mentioned in Section 6(1)(b), whereby in place of 60 days, 182 days shall be substituted. This means that even though the person may have stayed for a period exceeding 365 days during preceding 4 years but only if the said individual has stayed for 182 days or more during the relevant Financial Year ("F.Y.") then only he will be considered as Resident in India for tax purpose.

This provision provides relaxation to an Indian citizen or a Person of Indian Origin ("PIO") allowing him to stay in India for longer duration without becoming resident of India under Indian Tax Laws. The same principle applies for an Indian Citizen who leaves India as a member of the crew of an Indian ship.

AMENDMENT WITH RESPECT TO RESIDENT

The Finance Act, 2020 has introduced some amendments to the Income Tax Act, 1961 with respect to the tax liability of Indian Citizens and PIOs. As mentioned above the relaxation is provided to an Indian citizen or a PIO by

providing an extended period of 182 days instead of 60 days. However, many Indian Citizens and PIOs have exploited such relaxation to avoid their tax liabilities. Individuals, who carry out their considerable business activities from India, manage their period of stay in India in such a manner that they always remain a non-resident and escape their tax liability and avoid the payment of tax across the globe.

Thus, to cover up such loophole the Government of India has introduced an amendment through the Finance Act, 2020. As per the Amendment[3], an Indian Citizen will be deemed to be a Resident of India if he is not liable for tax in any other country on account of residency or domicile in any country, provided that his total income, excluding the income from foreign sources, exceeds Rs. 15 lakhs in the relevant FY. In other words, those Indian citizens whose total Income is more than Rs. 15 lakhs excluding the income from foreign sources and has no domicile or residence in any other country, will be "deemed to be resident of India".

Further, the Amendment provides that the individual deemed resident would qualify to be NOR in India for such FY. Thus "deemed resident" may not have immediate tax implication due to being considered as NOR if he visits India for less than 182 days but he will lose the benefit of NOR if his stay in India is for 182 days or more as the condition of being a Non-Resident for 9 years out of the preceding 10 years may not be fulfilled.

Further, the period of 182 days specified in the Explanation to Section 6(1) of the Income Tax Act, 1961 for Indian citizen and PIO with total income other than income from foreign sources more than Rs. 15 lakhs, has been reduced to 120 days. In other words, the amendment has reduced the time, Indian Citizens or PIOs need to spend in India to qualify as an Indian tax resident, from 182 days to 120 days in the relevant FY.

NOT ORDINARY RESIDENT

As per Section 6(6)(a) of Income Tax Act, 1961 an individual is a NOR if an individual who has been a non-resident in India in 9 out of 10 previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of 729 days or less. A similar rule applies for the Hindu Undivided Family as well.

It was observed in the case of *Jayram Rajgopal Poduval vs Assistant Commissioner Of Income Tax*[4] that the essence of Section 6(6) is that where the individual is resident in the previous year, but was not resident in India in 9 out of 10 previous years preceding that year or was not in India for a total period of 729 days or more in seven years preceding that year, then his residential status will become Resident but Not Ordinary Resident (RNOR).

Thus, in order to acquire the status of RNOR, it is a sine qua non that on one hand, the individual should not be non-resident in that year and on the other hand he should firstly be resident in that year and should fulfil either of the conditions of Section 6(6). Thus, he should meet either of the conditions of Section 6(1), i.e., be in India for 182 days or more in the previous year and thereafter either of the conditions enshrined in Section 6(6) be fulfilled, say, he should not be the resident in India in 9 out of 10 previous years preceding that year.

AMENDMENT WITH RESPECT TO NOT ORDINARY RESIDENT

The definition of NOR is extended vide Finance Act 2020. As per the Amendment[5] Indian Citizen or PIO who has an income exceeding Rs. 15 lakhs

from sources in India and from a business controlled from India or profession set up in India and the total stay in India during the year is 120 days or more but less than 182 days then such individuals would be considered as NORs.

The ordinary resident is taxed on income earned in India as well as outside India. However, NORs are taxed only to the extent of income earned in India, and with respect to income earned outside India; NORs are not liable for taxation under the Indian Income Tax laws.[6] Thus, the foreign income of such deemed residents would not be taxable in India, unless such income is derived from a business or profession controlled from India. With the passage of this necessary amendment, which excludes the taxability of foreign income of such deemed residents; the question related to taxation of global income in India has been settled.

CONCLUSION

The objective of the Amendment is to catch hold of those individuals (typically high net worth individuals), who are Indian citizens and have been arranging their affairs in such a manner so as to avoid paying taxes in any country. The Amendment will discourage tax abuse and will help in increasing the revenue for the Government of India. This amendment has also brought a revolutionary change in the tax laws of India. Hitherto the status of residency in India used to be decided on the basis of longevity of his stay in India, but by the introduction of the “deemed residency” the traditional rule of residency has been done away with.

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- Finance Act on Residential Status - NOR
 - [1] <https://indiankanoon.org/doc/191105/>
 - [2] Supra
 - [3] Inserted Section 6(1A) to Income Tax Act, 1961 by Finance Act, 2020
 - [4] Income Tax Appellate Tribunal – Mumbai decided on 18th January, 2008
 - [5] <https://www.indiabudget.gov.in/doc/memo.pdf>
 - [6] https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/822/PressRelease_CBDT_issues_clarification_on_the_new_provision_pertaining_to_residence_in_India_03022020.pdf
 - [1] <https://indiankanoon.org/doc/191105/>
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 - [4] Income Tax Appellate Tribunal – Mumbai decided on 18th January, 2008
 - [5] <https://www.indiabudget.gov.in/doc/memo.pdf>
 - [6] https://www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/822/PressRelease_CBDT_issues_clarification_on_the_new_provision_pertaining_to_residence_in_India_03022020.pdf

Contributed By - Gaurav Purohit

Designation - Associate

King Stubb & Kasiva,

Advocates & Attorneys

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Tel: [+91 11 41032969](tel:+911141032969) | Email: info@ksandk.com