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Thrissur Management Association

(Affiliate to All India Management Association)

Topic :-Recent Amendments to Residential Status

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Need for Section 6

- Section 6 of the Act lays down technical tests for determining the residence of a ‘person’ in India.
  - As the total income of an assessee and incidence of tax vary depending on the residential status in India

- Section 5 provides for the scope of income depending on the residential status.

- Thus, the need for section 6 is to determine which income to include, which depends on his residency status.

- Around the world, residency of an Individual is categorised as Resident and Non-resident. India has a special status known as Resident but not ordinarily resident (‘RNOR’). The legislature intends not to suddenly tax foreign income of an individual who becomes a resident merely because of excess number of days of stay in India.

Need for Section 6

- For an individual, the test depends on number of days of stay in India. The Act of 1922 had other criteria that if Indian income is more than foreign income, then also one is deemed resident of India. The Privy Council had examined this particular provision and it was held that it is a constitutional criteria, not an arbitrary criteria.

S. 4A of the Indian Income-tax Act, 1922	• S. 4A provided for the technical tests for the determination of the residence of a person in the taxable territories of the then British Empire

Wallace v CIT[1]	• The Privy Council held the tests in S. 4A to be constitutionally valid
	  • Despite the fact that they extend the provisions of the Act beyond the territories of India and
	  • That the tests artificially determine residence in India for the incidence of tax

S. 4A whether a precursor to S. 6 of 1961 Act?	• The tests laid down in S. 4A akin to S. 6 are artificial • These tests are accepted as they provide for **certainty** and **precision**

1. [1948] 16 ITR 240 (PC)

Section 5 - Scope of Total Income

Resident

a) Received or Deemed to Received In India
b) Accrues or arises or Deemed to accrue or Arise in India
c) Accrues or Arises Outside India

i.e. global income is taxable in India

RNOR

a) Received or Deemed to Received In India
b) Accrues or arises or Deemed to accrue or Arise in India
c) **Accrues or Arises Outside India but derived from Business Controlled or Profession Set up in India**

Not defined?

Non - Resident

a) Received or Deemed to Received In India
b) Accrues or arises or Deemed to accrue or Arise in India

Same as per definition of **Income from Foreign Source** – Section 6

Section 2(*30*) - "**non-resident**" means a person who is not a "resident", and for the purposes of sections 92, 93 and 168, includes a person who is not ordinarily resident within the meaning of clause (*6*) of section 6

BACKGROUND- Points to be noted while applying section 6

- Tests under Section 6 is applicable to the financial year (i.e. 1st April to 31st March) (known as previous year) for calculating the income

- The question of residence must be determined with reference to each year

- Finding of residence during one year would not warrant the assumption that assessee is also resident for the next year – Wallace vs. CIT (supra)

- The day of arrival should be ignored while calculating number of days, as held in the case of Manoj Kumar Reddy Nare (Bang. ITAT), followed by Fausta C. Cordeiro (Mumbai ITAT).
  - A word of caution: tax officials tend to count both the day of arrival and day of departure as 'days in India', irrespective of whether it is a full day or a few hours.

- Aggregation of stay in India from 1st April to 31st March

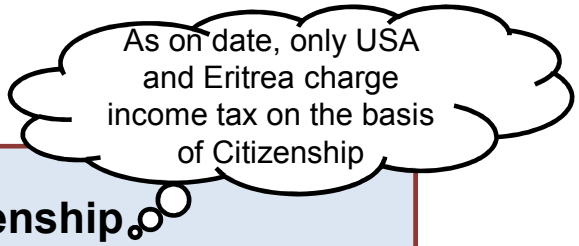
- Residency under Income-tax Act has no correlation with residency under other Acts such as FEMA

BACKGROUND- Points to be noted while applying section 6

- Residential status of assessee is solely on the basis of number of days present in India and other facts like 'economic presence' and 'legal presence' are irrelevant – ADIT v Sudhir Choudhrie (Delhi Tribunal)

- On loss of passport, secondary evidences such as notarized copy of passport, etc., were to be relied – ACIT v Sudhir Sareen (ITAT Delhi)

Difference between residence and citizenship



Residence

- Tax in India is levied on the basis of residence in India
- Residence is determined on the basis of section 6

Citizenship

- Tax in India may be levied on any individual irrespective of his citizenship
- Citizenship is determined basis the criterion stated in the Indian Citizenship Act, 1955

- Prior to Finance Act, 2020 amendments, the Act provided relaxation in criteria for determining residence of an Indian citizen or a Person of Indian Origin ('PIO')
- However, Finance Act, 2020 provides for a situation when a 'citizen of India' is deemed to be a resident for determining the incidence of tax

Importance of Section 6 with reference to DTAA

- A DTAA is applicable only to the persons who are residents of a contracting state (Article 1)
  - *Therefore, residence has to be determined for the purpose of application of a DTAA*

- A person has to be resident of a contracting state for claiming benefit under DTAA
  - *No treaty benefit can be claimed by a person if it is not a resident of either of the contracting state*

- If an individual due to different tax laws is a resident of both the contracting states then tie breaker test is to be applied (Article 4(2))

- If a person is resident of a particular country under DTAA, then India will take a view that he is non-resident in India – in such a situation whether Explanation 1A will apply?

A Resident but not ordinarily resident (RNOR) is a resident as per domestic law

Amendments in Section 6- Modification of residency provisions

Existing Rule till FY 2020-21

Before Amendment –

Resident in India if :-

a. Stays in India in previous year >= 182 days; (or)

b. Stays in India in previous year >= 60 days & Stays in India in the 4 years preceding to the previous year for >= 365 days

In the clause (b) above, 60 days to be replaced with 182 days in case of the following:

Citizens of India:

- Leaves India in any previous year as a member of the crew of an Indian ship
- Leaves for the purposes of employment outside India
- POI and Citizen of India who being outside India comes to visit India

Modification of residency provisions – 120 days to substitute 182 day

Proposed Amendment – Finance Bill 2020

Resident in India if :-
a. Stays in India in previous year >= 182 days; (or)
b. Stays in India in previous year >= 60 days & Stays in India in the 4 years preceding to the previous year for >= 365 days

In the clause (b) above, 60 days to be replaced with 182 days in case of the following:
Citizens of India:
- Leaves India in any previous year as a member of the crew of an Indian ship
- Leaves for the purposes of employment outside India

In the clause (b) above, 60 days to be replaced with 120 days in case of the following:
Citizens of India and POI $(Person\ of\ Indian\ Origin)$ being outside India, comes on a visit to India in any previous year

Not finalised. For final provision refer next slide

Modification of residency provisions – 120 days to substitute 182 day

Final Amendment – Finance Act 2020

Amended Sec 6(1)

Resident in India if :-

a. Stays in India in previous year >= 182 days; (or)

b. Stays in India in previous year >= 60 days & Stays in India in the 4 years preceding to the previous year for >= 365 days

In the clause (b) above, 60 days to be replaced with 182 days in case of the following:

Citizens of India:

- Leaves India in any previous year as a member of the crew of an Indian ship
- Leaves for the purposes of employment outside India

In the clause (b) above, 60 days to be replaced with 120 days in case of individuals where total income, other than income from foreign source, is more than INR 15 Lacs and in any other case182 days of the following:

Citizens of India and POI being outside India, comes on a visit to India in any previous year

For this provision, income from foreign sources means – Income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India.

Existing Rule till FY 2020-21
Deemed Residency for Stateless Person

Existing Provisions –

The Residency Provisions as per Income Tax Act may sometime results into a **Indian citizen** to be non-resident for all countries and resident for none. Thus, the issue of **stateless persons** has been bothering the tax world for quite some time.

Modification of residency provisions – Deemed Residency for Stateless Person

Proposed Amendment – Finance Bill 2020

Additionally, after the clause (1) of section 6, the following clause (1A) was proposed:

(1A) Notwithstanding anything contained in clause (1), an individual, being a citizen of India, shall be deemed to be resident in India in any previous year, if he 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.

- Proposal aimed to tax worldwide income of stateless person - **Immediate clarification by CBDT dt. 02/02/2020 -** to give benefit to bonafide persons working in abroad

Modification of residency provisions – Deemed Residency for Stateless Person

Sec 6(1A)

Final Amendment – Finance Act 2020

Additionally, after the clause (1) of section 6, the following clause (1A) was added:

(1A) 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 other criteria of similar nature <<Deemed to be a resident in India>>

Modification of residency provisions – Resident but Not Ordinarily Resident (RNOR)

Proposed Amendment – Finance Bill 2020

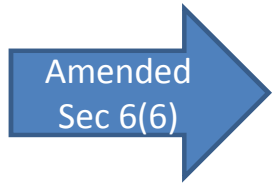
Once an **individual** qualifies as a resident in India, the second test is for **identifying RNOR status** of that individual which proposed as under:

~~a. Non-resident in 9 out of 10 preceding previous years; (or)~~

b. Stayed in India in the 7 years preceding to the previous year for <= 729 days

Similar is the case with **HUF** where the above test is to be applied with the **manager of the HUF i.e. Karta**

Modification of residency provisions – Resident but Not Ordinarily Resident (RNOR)



Final Amendment – Finance Act 2020

Once an **individual** qualifies as a resident in India, the second test is for **identifying RNOR status** of that individual which was is amended as under:

a. Non-resident in 9 out of 10 preceding previous years; (or)
b. Stayed in India in the 7 years preceding to the previous year for <= 729 days; (or)
c. Stayed in India in the previous year >=120 days but <182 days and total income, other than foreign sourced income >15 Lacs; or
d. Individual falling under (1A) as **deemed** to be resident in India (Stateless Person)

Similar is the case with **HUF** where the above test under (a) or (b) is to be applied with the **manager of the HUF i.e. Karta.**

Set aside the new proposal of Finance Bill 2020. It restored earlier two conditions and added further two situations

Amended residency rule for Indian Citizens/PIOs (FY 2020-21 onwards)

Residency/extended residency rule	Pre-amendment	Post-amendment
Indian citizen/PIO coming on a visit to India	• Is in India ≥ 182 days in relevant FY or, • Has been in India for ≥ 365 days within 4 preceding FYs and is in India for ≥ 182 (instead of 60) days in relevant FY	• NR if < 120 days in India under second condition • NR ≥ 120 days but < 182 days & 'total income' other than foreign source income ≤ INR 15 Lakh • NOR if ≥ 120 days but < 182 days & 'total income' other than foreign source income > INR 15 lakh ('**120 day rule**')
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	No deemed residency rule	• NOR if 'total income' other than foreign source income > INR 15 lakh ('**deemed residency rule**')

Adverse Impact of NOR status

- Increase in scope of income – income from business controlled or profession set-up in India.
- Concessional tax rates under Chapter XIIA and certain other exemptions available only to and NR not to NOR
- Concessional tax rates under DTAA would not be available where India is a source country and individual tie-breaks to India
- Presumption that control of firm, HUF, company, etc., is in India
  - Erin Estate v CIT 34 ITR 1 - SC
- Overall reduction in number of years of NOR status for Returning NRIs
- Clearly within tax compliance framework including TDS obligations, tax return filing, etc.
- Seafarers would be adversely affected as their incomes would not enjoy specific reliefs provided by the CBDT
- Loss of indirect transfer exemption on sale of units of FPIs and under Explanation 7

Beneficial Impact of NOR status

- Slab rates available for senior citizens, etc., would be available to NORs.
- TDS deduction not as per Section 195 lowering rates in most cases
- Eligible to claim Foreign Tax Credit for doubly taxed incomes
- Availing concessional tax rates under DTAA where India is a source country and individual tie-breaks to foreign jurisdiction
- Relaxation on reporting requirements (may not be required to file detailed ITR 2 as per extant provisions)
- Access to India DTAA network in respect of foreign sourced incomes

Neutral Impact of NOR status

- No obligation to report Foreign Assets
- NOR to be treated as NR for determining AE relationship, and for the purposes of Section 93
- No major changes under FEMA residential status due to change in tax residential status

BMA Impact - NOR status

- As per the BMA, an NR or an RNOR would only be an assessee in the event the BMA proceedings are in respect of undisclosed foreign income or undisclosed foreign asset of such person which relates to a period when the NR/RNOR was a ROR
- Since RNOR/NR is not required to file Schedule FA nor disclose any foreign income, there is no question of BMA applying in respect of the period where the person was and remains NR/RNOR.
- Accordingly, if a person become RNOR, he would not be required to disclose his foreign assets or income, nor would the applicability of the BMA be different for him as compared to if he were to be NR instead.

Impact of NOR status under treaty provisions

- Relevance of treaty benefit
  - If India is resident country, availing foreign tax credits for incomes arising outside India in India-controlled business/profession
- Individuals being tax residents of countries which levy personal taxes like UK, USA, etc
  - Dual residency and tie breaker tests may come into operation
    - If individual is resident of other country, deemed residency rule unlikely to apply
- Individuals being residents in countries which do not levy personal taxes (Middle East countries)
  - More relevant for deemed residency rule in view of controversy on being 'liable to tax' in other country and application of tie breaker test
  - UAE/ Kuwait treaty residency is based on days of physical presence

Impact under India-UAE Treaty

(1) For the purposes of this Agreement the term '**resident of a Contracting State**' means:

in the case of India: any person who, under the laws of India, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature. This term, however, does not include any person who is liable to tax in India in respect only of income from sources in India; and

in the case of the United Arab Emirates: an individual who is present in the UAE for a period or periods totalling in the aggregate at **least 183 days in the calendar year concerned**, and a company which is incorporated in the UAE and which is managed and controlled wholly in UAE.

Impact under India-UAE Treaty

UNITED ARAB EMIRATES
MINISTRY OF FINANCE

الإمارات العربية المتحدة
وزارة المالية

Tax Domicile Certificate for Individuals

Submission Date: 02 October 2018 Application Number: TAX/[redacted]/2018

Name: [redacted]

Nationality: [redacted]

Passport Number: N0[redacted]9

Visa Number: 6[redacted]25

Pursuant to the Agreement for the Avoidance of Double Taxation signed between the Government of the United Arab Emirates and the Government of **Republic of** [redacted] on [redacted] **2008**, the UAE Ministry of Finance certifies that [redacted] is resident of the United Arab Emirates.

This certificate is valid from **01 April 2018** to **31 March 2019**.

This certificate has been issued by the Ministry of Finance on 14 October 2018 [redacted] according to UAE local time.

Please verify the certificate using the following link:
https://eservices.mof.gov.ae/VatTax/Home/Validate

Tampering with or falsifying this certificate will result in legal action and penalties in accordance with the laws of the United Arab Emirates.

[redacted]

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www.mof.gov.ae

UAE issues **Tax Domicile Certificate**. What if, a person does not stays in UAE for more than 183 days but has this tax domicile certificate.

Can it be said that he is a resident in UAE as per domicile and therefore, deemed residency provision will not apply?

Issues and Concerns

1. Drafting Issues

- Clause 1A begins with a non-obstante clause which overrides clause 1. However, the wordings do not bring out clearly that Clause 1A is to override clause 1 only when an Indian citizen does not qualify as resident under clause 1

- leads to an interpretation where someone who is residing in India for 182 days or more during a particular previous year simply assumes that because he is not liable to tax in any other country by reason of domicile or residence, and he meets the income threshold criteria, he would be considered a resident not under clause 1, but under clause 1A, since clause 1A would override clause 1

- Consequently, he automatically becomes a RNOR through operation of clause 6(d) and the conditions of clause 6(a) would not be relevant, even if he were to become ordinarily resident under such conditions.

- Clause 1A make clause 1 redundant/otiose, therefore to this extent it would be appropriate that the scope of new provision is rationalized so that harmonious interpretation can be made.

2. Total income – a circular reference

- One of the criteria for application of new provisions is that the total income, other than income from foreign sources, should exceed INR 15 lakh. Therefore, one should be able to determine the total income in order to decide whether an individual could be deemed to be a resident as per new provisions.

- Section 2(45) defines “total income” to mean the total amount of income referred to in section 5, computed in the manner laid down in the Act. Section 5(2) deals with scope of total income of non-resident. Therefore, section 5 pre-supposes that the residential status of the person [whose total income has to be determined] is known

- Unless the residential status is known, one cannot determine the scope of total income under section 5, and unless total income is known, one cannot apply the amended provisions of residency under section 6.

3. Phrase-'*not liable to tax*'

One view: Liability to tax includes potential liability to tax

- The expression "liable to tax" is different from the "payment of tax" as held in Union of India v. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC). Thus, a mere non liability to tax should not enable invocation of section 6(1A)

- Such non liability should be linked to residence or domicile or any other criteria of similar nature. If the non-liability is not linked to any of these criteria, section 6(1A) cannot be invoked

- In the case of an Indian Citizen who is a non-resident in India and operates in UAE, he may earn income in UAE which would most likely be exempt in UAE. His non taxation in UAE arises because of the absence of taxation in the UAE, not because he is non-resident in UAE – therefore, he should not be covered under section 6(1A) and thus not be considered a deemed resident in India

Continued…..

3. Phrase-'*not liable to tax*'

- The principle that it is the sovereign right of each country to tax a particular income and it is each country's right whether it wants to tax a particular income or not, or even tax income at all. As long as they have right to levy tax, that is sufficient.

- Further, an individual can claim that he has a tax residency certificate from the UAE government and hence, if in future, UAE government imposes income-tax, he will be liable to tax in UAE, i.e. he has a potential tax exposure and hence should be considered liable to tax in UAE

3. Phrase-'*not liable to tax*'

Another view: Liability to tax does not include potential liability to tax

- Liability to tax under the amended provisions includes potential liability to tax, **negating the Supreme Court's decision in Azadi Bachao (supra)**.

- Income-tax law in India is applicable qua a previous year and all the circumstances present during a previous year determine the assessee's liability to tax. Thus, for FY 2020-21, a person would be liable to tax in Dubai only if – (i) Dubai makes a law levying Income-tax on him and (ii) he actually becomes liable to pay such a tax for FY 2020-21. A potential tax liability has no place under Indian Income-tax law.

- Central Board of Direct Taxes (CBDT) vide a **Press Release dated February 2, 2020** clarified that the new provision does not intend to include within the ambit of tax, those Indian citizens who were bonafide workers in other countries, including the Middle East

- Further, it was also clarified that in case of an Indian citizen who becomes a deemed resident of India under this proposed provision, income earned outside India shall not be taxed in India unless it is derived from an Indian business or profession. While clarification has been issued, it does not address the question of potential liability to tax that affects the Indian non-residents living abroad. Much clarification is required on this issue.

3. Phrase-'*not liable to tax*'

Provision has been subject matter of litigation in India for UAE residents with decisions going to and fro

- M.A. Rafik – Advance Ruling – December 1994 (213 ITR 317)
- Cyril Pereira – Advance Ruling – May 1999 (239 ITR 650)
- Emirates Fertilizer Trading – Advance Ruling - October 2004 (272 ITR 84)
- Abdul Razak A. Meman – Advance Ruling - May 2005 (276 ITR 306)
- Green Emirates Shipping and Travels – Mumbai Tribunal – November 2005 (286 ITR 60)
- Meera Bhatia v. ITO [2010] – Mumbai Tribunal - 1 taxmann.com 52 (M UM . - ITAT) – Oct 2010

4. DTAA Article 4(1)

- Treaties where Article 4(1) of the DTAAs entered by India state that a person is resident in that country if he is liable to tax therein by reason of his domicile, residence, place of registration, place of management or any other similar criterion.

- This definition does not include deemed residency of a person, and thus even though his India sourced income is chargeable to tax in India, DTAA benefit would not be available.

THANK YOU

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Amended Section 6(1)-Reproduced

***6**. For the purposes of this Act,—*
(1) An individual is said to be resident in India in any previous year, if he—

(a) is in India in that year for a period or periods amounting in all to one hundred and eighty-two days or more ; or

(b) [***]

(c) having within the four years preceding that year been in India for a period or periods amounting in all to three hundred and sixty-five days or more, is in India for a period or periods amounting in all to sixty days or more in that year.

Explanation 1.—In the case of an individual,—

(a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act, 1958 (44 of 1958), or for the purposes of employment outside India, the provisions of sub-clause (c) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted ;

Continued…..

Amended Section 6(1)-Reproduced

(b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to clause (e) of section 115C, who, being outside India, comes on a visit to India in any previous year, the provisions of sub-clause (c) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted [and in case of the citizen or person of Indian origin having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year, for the words "sixty days" occurring therein, the words "one hundred and twenty days" had been substituted].

Explanation 2.—For the purposes of this clause, in the case of an individual, being a citizen of India and a member of the crew of a foreign bound ship leaving India, the period or periods of stay in India shall, in respect of such voyage, be determined in the manner and subject to such conditions as may be prescribed.

New Section 6(1A)-Reproduced

(1A) 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 other criteria of similar nature.

Amended Section 6(6)-Reproduced

(6) A person is said to be "not ordinarily resident" in India in any previous year if such person is—

(a) an individual who has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less; or

(b) a Hindu undivided family whose manager has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less 7[; or

(c) a citizen of India, or a person of Indian origin, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year, as referred to in clause (b) of Explanation 1 to clause (1), who has been in India for a period or periods amounting in all to one hundred and twenty days or more but less than one hundred and eighty-two days; or

Continued…..

Amended Section 6(6)-Reproduced

(d) a citizen of India who is deemed to be resident in India under clause (1A).

Explanation.—For the purposes of this section, the expression "income from foreign sources" means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India)].