Representations for restoring 182 days rule for visiting Non-resident Indians (NRIs)/Persons of Indian origin (PIOs)

1. Executive Summary

1.1. Prior to amendment by Finance Act 2020, Explanation 1(b) to s.6(1) of the Income-tax Act 1961, provided for extended residency rule for Non-resident Indians (NRIs) and Persons of Indian origin (PIOs) who being outside India come on a visit to India. In terms of such extended residency rule, they were considered as 'non-resident' if their stay in India was below 182 days during the relevant tax year even if their stay in India in preceding four years was more than 365 days. This resulted in such taxpayers not being required to pay tax in India on their foreign sourced incomes.

1.2. Finance Act 2020 amended the above rule and introduced a graded extended residency rule as follows :-

(a) Regardless of quantum of India sourced income, visiting NRIs/PIOs will be treated as non-resident if their stay in India during relevant tax year is less than 120 days (instead of 182 days)

(b) If the quantum of India sourced income is less than Rs. 15 lakhs, such persons will continue to be treated as non-residents if their stay in India during relevant tax year is less than 182 days (as it existed prior to FA 2020 amendment)

(c) If the quantum of India sourced income is more than Rs. 15 lakhs, such persons will be treated as 'not ordinarily residents' as per newly inserted clause (c) of s.6(6)

1.3. The above change has resulted in adding more complexity to the extended residency rule for visiting NRIs and PIOs. Earlier, they simply had to keep a check on the period of stay in India below 182 days. Now, they also need to keep a tab on India sourced income of Rs. 15 lakhs as also stay in preceding four tax years. This creates various issues and confusion for taxpayers

1.4. After introducing such complexity, what the amendment has achieved is that for visiting NRIs and PIOs, if their India sourced income is more than Rs. 15 lakhs and stay exceeds 120 days, they will be liable to be taxed on India sourced incomes at rates applicable to residents (as distinguished from non-residents) i.e India sourced incomes get taxed at higher rates applicable to residents instead of lower rates applicable to non-residents

1.5. It is submitted that the above referred amendments need reconsideration and roll back for following brief reasons :-

(a) The amended rule does not meet the original objective of making people carrying out substantial economic activity from India but dodging residency in India by limiting their stay to 182 days, pay tax on their global incomes in India (as per Explanatory Memorandum to Finance Bill 2020)

(b) The incremental tax revenue which can be expected to be garnered is restricted to difference between normal slab rate and concessional rates applicable to non-residents

(c) The targeted individuals can simply avoid the higher taxes by limiting their stay in India to below 120 days instead of 182 days. Thus, the tax policy measure of reducing threshold from 182 days to 120 days does not meet the desired objective.

(d) On the other hand, the amended rule has a net negative revenue impact since NRIs/PIOs spending less time in India adversely impacts indirect and direct tax revenues from travel and hospitality sectors in India. Also, the lower threshold of 120 days' stay in India could lead to NRIs/ PIOs ceasing to create wealth/ additional investments in India to keep their Indian income below 15 lacs in any given year. This could result in lower investments and spending in India and thus, adversely affecting the economy

(e) Restoration of 182 days rule will encourage such NRIs/PIOs to spend more time in India with their family and friends, spend more money on travel and stay and have a net positive revenue impact due to externalities. It encourages more investment with India presenting better opportunities for investing in many sectors – more particularly, manufacturing and start ups.

(f) It will remove the complexity and become simple to understand & administer for both taxpayers and Tax Department

(g) Under the erstwhile 182 days regime, individuals could not have avoided taxes in India on active incomes like professional or technical fees from services rendered in India or business activities carried out in India – if they constituted 'substantial economic activities' as referred in Explanatory Memorandum to Finance Bill 2020. The domestic source rules and treaty provisions are wide enough to cover business incomes from physical presence in India from 120 days to 182 days. Thus, there is no perceived advantage of new 120 day rule.

1.6. In view of above reasons, it is submitted that erstwhile limit of 182 days for visiting NRIs/PIOs may be restored without any income quantum restrictions. It will allow NRIs/PIOs to spend more time in India which has positive impact on the Indian economy

Detailed representations

2. Position prior to amendment by Finance Act 2020 – 182 days rule

2.1. Prior to amendment by Finance Act 2020, Explanation 1(b) to s.6(1) provided for extended residency rule for Non-resident Indians (NRIs) and Persons of Indian origin (PIOs) who being outside India come on a visit to India. In terms of such extended residency rule, they were considered as 'non-resident' if their stay in India was below 182 days during the relevant tax year even if their stay in India in preceding four years was more than 365 days. This resulted in such taxpayers not being required to pay tax in India on their foreign sourced incomes. Even for India sourced incomes, they could avail treaty benefits as treaty residents of countries in which they are located.

2.2. The above threshold of 182 days was introduced from financial year 1994-95 onwards by increasing it from erstwhile limit of 150 days. Following is the rationale explained in CBDT Circular No. 684 dated 10 June 1994 :-

> *"Suggestions had been received to the effect that the aforesaid period of one hundred and fifty days should be increased to one hundred and eighty-two days.* ***This is because the non-resident Indians who have made investments in India, find it necessary to visit India frequently and stay here for the proper supervision and control of their investments****. The Finance Act, therefore, has amended clause (b) of the Explanation to section 6(1)(c) of the Income-tax Act, in order to extend the period of stay in India in the case of the aforesaid individuals from one hundred and fifty days to one hundred and eighty-two days, for being treated as resident in India, in*

the previous year in which they visit India. Thus, such non-resident Indians would not lose their 'non-resident' status if their stay in India, during their visits, is up to one hundred and eighty-one days in a previous year."

2.3. The earlier limit of 150 days was also an outcome of liberalisation in 1989 from earlier limit of 90 days in response to representations from NRIs that it was too short especially for those who had to supervise their investments in India.

2.4. Even as per Explanatory Memorandum to Finance Bill 2020, the intent of the above provision is explained as follows :-

> *"This provision provides relaxation to an Indian citizen or a person of Indian origin allowing them to visit India for longer duration without becoming resident of India."*

3. Original proposal of Finance Bill 2020 – Reduction of 182 days to 120 days

3.1. As per original proposal of Finance Bill 2020, it was proposed to reduce the number of days from 182 to 120 days such that visiting NRIs/PIOs would turn resident in India if their stay in preceding four years is 365 days or more and stay in India during relevant tax year is 120 days or more. The rationale explained for such proposal was as follows :-

> *"Instances have come to notice where period of 182 days specified in respect of an Indian citizen or person of Indian origin visiting India during the year, is being misused. 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 not be required to declare their global income in India"*

4. Substantial amendment at enactment stage of Finance Bill 2020 – Graded residency rule

4.1. However, at the enactment stage of Finance Bill 2020, the above proposal was changed and as per finally enacted provision, a graded extended residency rule was introduced as follows:-

(a) Regardless of quantum of India sourced income, visiting NRIs/PIOs will be treated as non-resident if their stay in India during relevant tax year is less than 120 days (instead of 182 days)

(b) If the quantum of India sourced income is less than Rs. 15 lakhs, such persons will continue to be treated as non-residents if their stay in India during relevant tax year is less than 182 days (as it existed prior to FA 2020 amendment)

(c) If the quantum of India sourced income is more than Rs. 15 lakhs, such persons will be treated as 'not ordinarily residents' as per newly inserted clause (c) of s.6(6)

5. Impact of graded extended residency rule

5.1. The above change has resulted in adding more complexity to the extended residency rule for visiting NRIs and PIOs. Earlier, they simply had to keep a check on the period of stay in India below 182 days. Now, they also need to keep a tab on India sourced income of Rs. 15 lakhs as also stay in preceding four tax years.

5.2. The period of stay in preceding four tax years could work either in favour or against the individual. That is, if an individual's stay during the preceding four tax years is less than 365 days, they would qualify as NR in India even if stay in current year exceeds 120 days but does not exceed 182 days. However, if the stay is for 365 days or more in the preceding four tax years, he/she could qualify as NOR in India as per the new 120 days rule for determining residency

5.3. The amendment brings a disparity in determination of residential status of the targeted individuals in the year they leave India (if for the purposes of employment outside India) i.e. Explanation 1(a) to Section 6(1) of the Income-tax Act, 1961 (IT Act) and in subsequent years when they, being outside India, come on a visit to India i.e Explanation 1(b) to Section 6(1) of the IT Act. In the year of leaving India, 182 days criterion is applied without income threshold of Rs. 15 lakhs. In the year of visit to India, 120 and 182 days criterion is applied based on income threshold of Rs. 15 lakhs. This creates confusion amongst the targeted individuals when determining their residential status in India in the first year of move and in subsequent years. Prior to the amendment, such determination was at par with each other.

5.4. The amendment creates a circular loop to the extent it requires determination of 'total income' first to determine residential status. This creates a typical 'chicken or egg' situation to find out what should be determined first – residential status or total income. There are certain exemptions and deductions available which are linked to an individual's residential status in India such as exemption under Section 10(4), Section 10(15)(ix) etc of the IT Act which become difficult to apply due to combined criterion of stay in India and India sourced income threshold.

5.5. After introducing such complexity, what the amendment has achieved is that for visiting NRIs and PIOs, if their India sourced income is more than Rs. 15 lakhs and stay exceeds 120 days, they will be liable to be taxed on India sourced incomes at rates applicable to residents (as distinguished from non-residents). For example, if they earn dividend from India, they will be liable to tax at slab rates instead of flat rate of 20%1 u/s. 115A.

5.6. Also, for claiming treaty benefits on such incomes, they will need to first qualify as residents of treaty countries as per domestic laws of such countries. Thereafter, being resident of both countries, they will need to tie break to treaty countries under residency tie breaker clause of treaties. But where treaty allocates taxing right to India without any cap, they will be liable to tax at rates applicable to residents. For instance, if treaty permits capital gains on unlisted shares to be taxed in India, they will be taxed on long term capital gains at normal rate of 20% (with indexation benefit) instead of 10% (without indexation benefit).

5.7. To sum up, the impact of amendment is that India sourced incomes get taxed at higher rates applicable to residents instead of lower rates applicable to non-residents.

6. Need for reconsideration and restoration of erstwhile 182 days rule

6.1. It is submitted that the above referred amendments need reconsideration and roll back for following reasons :-

(a) The original intent of making people carrying out substantial economic activity from India but dodging residency in India by limiting their stay to 182 days, pay tax on their global incomes in India (as per Explanatory Memorandum to Finance Bill 2020) does not match with the finally enacted provision. As per finally enacted law, even in a worst case scenario where individual spends more than 120 days and India sourced income is more than Rs. 15 lakhs, he/she is treated as NOR and not required to pay tax on global incomes in India.

(b) The amendment merely has effect of making such individuals pay tax on Indian incomes at rates applicable to residents. Hence, the incremental tax revenue which can be expected to be garnered is restricted to difference between normal slab rate and concessional rates applicable to non-residents.

[1] Plus applicable surcharge and cess

(c) The targeted individuals can simply avoid the higher taxes by limiting their stay in India to below 120 days instead of 182 days. In fact, with receding of Covid 19 pandemic and international travel becoming more easier, most NRIs/PIOs are likely to adopt this measure to avoid the higher taxes in India. Thus, the tax policy measure of reducing threshold from 182 days to 120 days does not meet the desired purpose making people carrying out substantial economic activity from India but dodging residency in India by limiting their stay to 182 days, pay tax on their global incomes in India.

(d) If NRIs/PIOs restrict their stay in India to less than 120 days, it will aggravate the negative impact on travel and hospitality sectors in India who are already adversely impacted by Covid 19. Thus, on a balance, India may not gain much tax revenues from NRIs/PIOs whereas it may stand to lose indirect and direct tax revenues from travel and hospitality sectors in India. In other words, the measure has a net negative revenue impact.

(e) There are a large number of Indians taking up overseas citizenship which could increase further. Also, the lower threshold of 120 days' stay in India could lead to NRIs/ PIOs ceasing to create wealth/ additional investments in India to keep their Indian income below 15 lacs in any given year. This could result in lower investments and spending in India and thus, adversely affecting the economy.

(f) On the other hand, restoration of erstwhile limit of 182 days without any income threshold will encourage such NRIs/PIOs to spend more time in India with their family and friends, spend more money on travel and stay and have a net positive revenue impact due to externalities. The original intent of allowing such NRIs/PIOs to spend more time in India to take care of their investments is more relevant today with India presenting better opportunities for investing in many sectors – more particularly, manufacturing and start ups.

(g) It will remove the complications caused by graded residency rule based on physical stay in India and quantum of India sourced income. The residency rule will become more simpler to understand and administer for both taxpayers and Tax Department.

(h) Under the erstwhile 182 days regime, individuals could not have avoided taxes in India on active incomes like professional or technical fees from services rendered in India or business activities carried out in India – if they constituted 'substantial economic activities' as referred in Explanatory Memorandum to Finance Bill 2020. The existing source rules of 'business connection' u/s. 9(1)(i) and fees for technical services u/s. 9(1)(vii) are wide enough to capture such incomes. As per Hon'ble Supreme Court ruling in the case of Formula One World Championship Ltd v. CIT [2017] 394 ITR 80 (SC), even a short presence of 2 to 3 days in India where non-resident has full authority to conduct business from a place in India constitutes a Permanent Establishment (PE) in India and gives right to India as a source country to tax such income.

Relief can be claimed only under treaty by virtue of absence of Permanent Establishment (PE) or fixed base in India and/or restrictive scope of fees for technical services in some treaties. Treaty relief continues to be available under new regime of 120 days subject to individual tie breaking residency to other country. The status does not change if such individuals restrict their stay in India to less than 120 days. Thus, there is no perceived advantage of new 120 day rule.

6.2. In view of above reasons, it is submitted that erstwhile limit of 182 days for visiting NRIs/PIOs may be restored without any income quantum restrictions. It will allow NRIs/PIOs to spend more time in India which has positive impact on the Indian economy.