

Tax - Residents Rule in India



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Residential Status under Income Tax Act, 1961

Author: Neha Mishra

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INTRODUCTION

Definitions of residence for tax purposes vary considerably from state to state. For individuals, physical presence in a state is an important factor. Some states also determine residency of an individual by reference to a variety of other factors, such as the ownership of a home or availability of accommodation, family, and financial interests. For companies, some states determine the residence of a corporation based on its place of incorporation. Other states determine the residence of a corporation by reference to its place of management. Some states use both a place-of-incorporation test and a place-of-management test. Domicile is, in common law jurisdictions, a different legal concept to residence. Residence as defined in double taxation treaties is different from residence as defined for domestic tax purposes.

Residential Status

Section 6¹ lays down the tests of territorial correlation amounting for residence for all taxable entities. Two different tests are provided for individuals, two for companies, and one for Hindu undivided families, firms, associations of persons and other assessable units. The tests are mock – staying for a day more or less may make a difference- but they make for exactitude and accuracy, and they were held legitimate and inter vires under the 1922 Act².

Residential status: Three types of residential status are envisaged for an assessee under the Act. He may be-

- Resident (also known as resident and ordinarily resident)
- Non- Resident or not resident.

¹See Section 6, Income Tax Act, 1961.

²Kanga, Palkhivala and Vyas, The Law and Practice of Income Tax, Lexis Nexis Buttersworths, I Vol, IX, Ed.,2004, p-348.

- Resident but not ordinarily resident (a category of residential status) only valid for individuals and Hindu undivided families³.

DETERMINATION OF RESEDENTIAL STATUS OF AN INDIVIDUAL

In order to determine whether an Individual is a ‘Resident’ or a ‘Non-Resident Indian’, his residential status is required to be determined under Section 6 of the Income–Tax Act (hereinafter referred to as the ‘ACT’), 1961. There are two alternative technical tests (or conditions) of residence for individual taxpayers. Each of the two tests relate to the physical presence of the taxpayer in India in the course of the “previous year” which would be the twelve months from April 1 to March 31.

As per section 6 of the Act, an individual is said to be non-resident in India if he is not a resident in India and an individual is deemed to be resident in India in any previous year if he satisfies any of the two conditions mentioned under section 6 pf the Act.

An individual is said to be ‘**Resident**’ in India in any previous year if: -

CONDITION NO. 1 - he is in India in that year for an aggregate period of **182** days or more;

OR

CONDITION NO. 2 – he is in India for a period of **60 days** or more during the previous year and **365 days** or more during 4 years immediately preceding the previous year.

The above provisions are applicable to all individuals irrespective of their nationality. If any of the above conditions are satisfied an individual is ‘Resident’ (Ordinary Resident) in India. However, If none of the above two prescribed conditions are satisfied, he is ‘**Non – Resident**’

EXCEPTIONS TO THE ABOVE RULE

³Supra note 1.

As a special concession for Indian citizens and foreign citizens of Indian origin, the provisions of condition no. 2 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 in following two cases:

- (1) where an Indian citizen 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; and
- (2) where an Indian citizen or a foreign citizen of Indian origin (NRI), who is outside India, comes on a visit to India during the previous year.

A person shall be deemed to be of Indian origin if he, or either of his parents or any of his grand-parents, was born in undivided India.

- In the above context, an individual visiting India several times during the relevant "previous year" should note that judicial authorities in India have held that both the days of entry and exit are counted while calculating the number of days stay in India, irrespective of however short the time spent in India on those two days may be.
- During computation of period of stay for determining residential status, it is not necessary that the stay should be continuous. And the stay can be anywhere in India, not at only one place.

NON- ORDINARY RESIDENT

As per section 6(6) of the Act, an individual, who is defined as Resident in a given financial year is said to be "not ordinarily resident" in any previous year if:

- he has been a non-resident in India **9 out of the 10** preceding previous years OR he has during the **7 preceding previous years** been in India for a period of, or periods amounting in all to, **729 days or less**.
- a Hindu undivided family whose manager has not been non-resident in India in **9 out of the 10** previous years preceding that year, OR has not during **the 7 preceding previous years** been in India for a period of, or periods amounting in all to, **729 days or less**.

Till 31st March 2003, 'Not Ordinarily Resident' was defined as a person who has not been resident in India in 9 out of 10 preceding previous⁴ years or he has not during the 7 preceding previous years been in India for a period of, or periods amounting in all to, 730 days or more.

DETERMINATION OF RESIDENTIAL STATUS OF HINDU UNDIVIDED FAMILY, FIRM, ASSOCIATIONS OF PERSON, COMPANY AND OTHER PERSONS.

As per Section 6 of the Income-tax Act, 1961:

- A Hindu undivided family, firm or other association of persons is said to be resident in India in any previous year in every case except where during that year the control and management of its affairs is situated wholly outside India.
- A company is said to be resident in India in any previous year, if
 - (a) It is an Indian company; OR
 - (b) During that year, the control and management of its affairs is situated wholly in India
- Every other person is said to be resident in India in any previous year in every case, except where during that year the control and management of his affairs is situated wholly outside India.

If a person is resident in India in a previous year relevant to an assessment year in respect of any source of income, he shall be deemed to be resident⁵ in India in the previous year relevant to the assessment year in respect of each of his other sources of income.

An analysis of the all provisions of section 6 of Income - Tax Act, 1961 would thus indicate that:

1. To become a non-resident for income- tax purposes, an Indian citizen leaving India for the first time to take up employment abroad should be out of the country latest by 28th September and should

⁴Girish Ahuja and Ravi Gupta. Concise Commentary on Income Tax, Bharat Law House Pvt. Ltd., 6th Ed., 78(2005).

⁵kanga, Palkhivala and Vyas, The Law and Practice of Income Tax, Lexis Nexis Buttersworths, I, 9th Ed., 354-357(2004).

not return to India before 1st April of the next year. However, in case of a person leaving India for taking up a business or profession, the criteria of 60 days will apply, as defined earlier.

2. An NRI individual, whose total stay in India in 4 preceding years exceeds 364 days, will not lose his non-resident status in the following year(s) if his total stay in India in that year (from April 1 to March 31) does not exceed-

(a) 181 days, if he is on a “visit” to India; or

(b) 59 days, if he comes to India on “transfer of residence”.

An NRI who has returned to India for settlement, whose total stay in India for 4 preceding years does not exceed 364 days will not lose his non-resident status in the following year(s) if his total stay in India in such year(s) (from April 1 to March 31) does not exceed 181 days.

3. A new-comer to India would be treated as “Not Ordinary Resident” for the first two years of his stay in India or if treated as Non-Resident in the year of arrival then for the second and third year of his stay in India. An individual (whether Indian or foreign citizen) who has left India and remains non-resident for at least nine years preceding his return to India or whose stay in 7 years preceding the year of return has not exceeded 729 days would, upon his return, be treated as “non-resident” or “not ordinarily resident” depending upon the number of days stay in India in the year of return. The status of “not ordinarily resident” will remain effective for 2 years including or following the year of return as the case may be.

IMPORTANT POINTS FOR CONSIDERATION

1. Residential status is always determined for the Previous Year because the assessee has to determine the total income of the Previous Year only. In other words, as the tax is on the income of a particular Previous Year, the enquiry and determination of the residence qualification must confine to the facts obtaining in that Previous Year.
2. If a person is resident in India in a Previous Year in respect of any source of income, he shall be deemed to be resident in India in the Previous Year relevant to the Assessment Year in respect of each of his other sources of Income. [Section 6(5)]
3. Relevant Previous Year means, the Previous Year for which residential status is to be determined
4. It is not necessary that the stay should be for a continuous period.
5. It is not necessary that the stay should be at one place in India.

6. Presence in territorial waters in India would also be regarded as stay in India.
7. A person is said to be of Indian Origin if he or either of his parents or any of his grandparents was born in undivided India [Section 115C].
8. Official tours abroad in connection with employment in India shall not be regarded as employment outside India.
9. A person may be resident of more than one country for any Previous Year.

Relevant Points for NRIs

Previous Year is period of 12 months from 1st April to 31st March. Number of days stay in India is to be counted during this period.

1. Both the Day of Arrival into India and the Day of Departure from India are counted as the days of stay in India (i.e. 2 days stay in India).
2. Dates stamped on Passport are normally considered as proof of dates of departure from and arrival in India.
3. It is advisable to keep several photocopies of the relevant passport pages for present and future use.
4. Ensure that date stamped on the passport is legible.
5. Keep track of no. of days in India from year to year and check the same before making the next trip to India. It is advisable to maintain a chart for the number of days stay in the current and in the preceding seven (7) previous years.
6. In the 1st year of leaving India for employment outside India, ensure that you leave before 29th September. Otherwise total income of the financial year (including the foreign income) will be taxable in India if it exceeds the basic exemption limit.
7. During the last year of stay abroad, on transfer of residence to India, ensure to come back on or after Feb 1st (or Feb 2nd in case of a leap year). Since arrival before this date will result in stay in India exceeding 59 days. However, a person whose stay in India in preceding four (4) previous years does not exceed 365 days, he may return after September 30th of the relevant year without loss of non-resident status.

SOURCES OF INCOME	R & OR	R & NOR	NR
Indian Income Income received or deemed to be received in India during the current financial year.	Taxable in India	Taxable in India	Taxable in India
Income accruing or arising or deemed to accrue or arise in India during the current financial year.	Taxable in India	Taxable in India	Taxable in India
Income accruing or arising or deemed to accrue or arise out side India, but first receipt is in India during the current financial year	Taxable in India	Taxable in India	Taxable in India
Foreign Income Income accruing or arising or deemed to accrue or arise outside India and received outside India, during the current financial year.	Taxable in India	Taxable in India	Not Taxable in India
Income accruing or arising or outside India from a Business/ profession controlled in/from India during the current financial year.	Taxable in India	Taxable in India	Not Taxable in India
Income accruing or arising out side India from any source other than Business Profession controlled from India	Taxable in India	Taxable in India	Not Taxable in India.

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EMAIL AT: contact@astrealegal.com

QUICK CONTACT: +91 9822720483, +91 020 – 65108782

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