

Chapter 2

Residential Status and Incidence of Tax

Introduction:

It is critical for the Income Tax Department to establish a taxable individual's or company's residence status. It is especially important during the tax filing season. In reality, this is one of the variables used to determine a person's taxability.

Residential Status for Income Tax

An individual's taxability in India is determined by his residential status under the income tax act in India for any given fiscal year. The phrase "residential status" was coined by India's income [tax](#) rules and should not be confused with an individual's citizenship in India.

An individual may be an Indian citizen but become a non-resident for a certain year. Similarly, a foreign citizen may become a resident of India for [income tax](#) purposes in a given year.

It is also worth noting that the residential status as per income tax differs to sorts of people, such as an individual, a corporation, a company, and so on, decided differently.

Residential Status of an Individual.

On the basis of residence, the assessee are divided into three categories. As per the provisions of the Income Tax Act, an individual and a Hindu undivided family can either be –

- 1) Resident and Ordinarily Resident; or
- 2) Resident but not Ordinarily Resident; or
- 3) Non-Resident

How to determine residential status?

For the purpose of income tax in India, the income tax laws in India classifies taxable persons as:

1. A resident
2. A resident not ordinarily resident (RNOR)
3. A non-resident (NR)

The taxability differs for each of the above categories of taxpayers. Before we get into taxability, let us first understand how a taxpayer becomes a resident, an RNOR or an NR.

Resident

A taxpayer would qualify as a resident of India if he satisfies one of the following 2 conditions:

1. Stay in India for a year is 182 days or more or

2. Stay in India for the immediately 4 preceding years is 365 days or more and 60 days or more in the relevant financial year

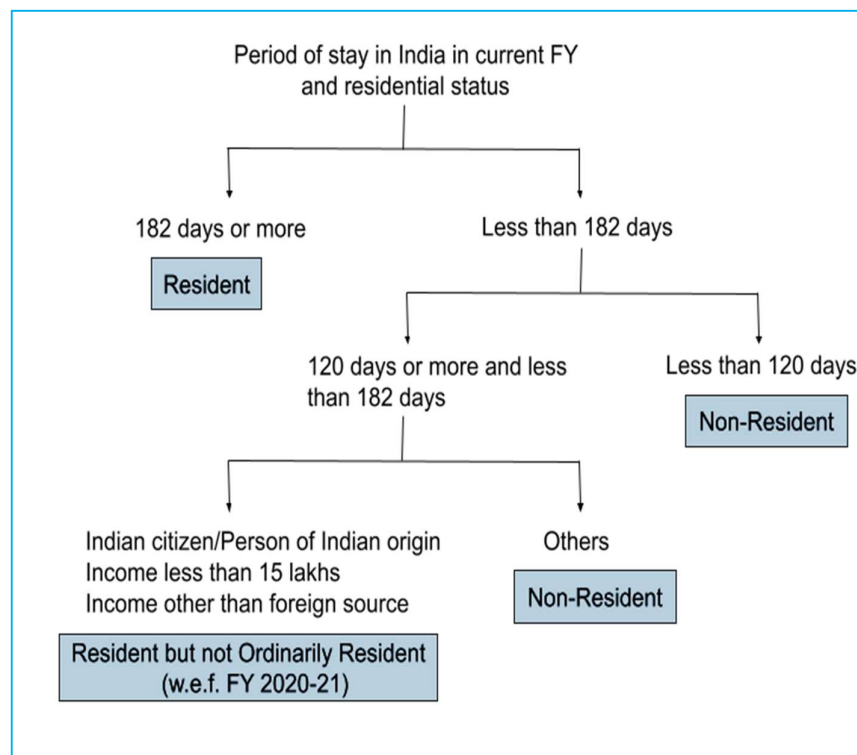
Exceptions to Residential Status

In the event an individual who is a citizen of India or person of Indian origin leaves India for employment during an FY, he will qualify as a resident of India only if he stays in India for 182 days or more. Such individuals are allowed a longer time greater than 60 days and less than 182 days to stay in India.

However, from the financial year 2020-21, the period is reduced to 120 days or more for such an individual whose total income (other than foreign sources) exceeds Rs 15 lakh.

In another significant amendment from FY 2020-21, an individual who is a citizen of India who is not liable to tax in any other country will be deemed to be a resident in India. The condition for deemed residential status applies only if the total income (other than foreign sources) exceeds Rs 15 lakh and nil tax liability in other countries or territories by reason of his domicile or residence or any other criteria of similar nature.

The amendment can be further simplified as below-



Resident Not Ordinarily Resident

If an individual qualifies as a resident, the next step is to determine if he/she is a Resident ordinarily resident (ROR) or an RNOR. He will be a ROR if he meets both of the following conditions:

1. Has been a resident of India in at least 2 out of 10 years immediately previous years and
2. Has stayed in India for at least 730 days in 7 immediately preceding years

Therefore, if any individual fails to satisfy even one of the above conditions, he would be an RNOR.

From FY 2020-21, a citizen of India or a person of Indian origin who leaves India for employment outside India during the year will be a resident and ordinarily resident if he stays in India for an aggregate period of 182 days or more. However, this condition will apply only if his total income (other than foreign sources) exceeds Rs 15 lakh. Also, a citizen of India who is deemed to be a resident in India (w.e.f FY 2020-21) will be a resident and ordinarily resident in India.

NOTE: Income from foreign sources means income which accrues or arises outside India (except income derived from a business controlled in India or profession set up in India).

Non-resident

An individual satisfying neither of the conditions stated in (a) or (b) above would be an NR for the year.

Taxability

Resident: A resident will be charged to tax in India on his global income i.e. income earned in India as well as income earned outside India.

NR and RNOR: Their tax liability in India is restricted to the income they earn in India. They need not pay any tax in India on their foreign income. Also note that in a case of double taxation of income where the same income is getting taxed in India as well as abroad, one may resort to the Double Taxation Avoidance Agreement (DTAA) that India would have entered into with the other country in order to eliminate the possibility of paying taxes twice.

1) Resident and Ordinarily Resident: -

An individual is said to be resident in India in any previous year if he satisfies any one of the basic conditions and both the additional conditions.

Basic Conditions: -

- a) He is in India in the relevant previous year for a period of 182 days or more, or
- b) He is in India for at least 60 days or more during the relevant previous year and he has been in India for at least 365 days or more during the four years immediately preceding the previous year.

Exceptions to the above rules of 60 days stay in India: -

- i) An individual who is a citizen of India and leaves India in any previous year for the purpose of employment or as a member of the crew of an Indian ship must have stayed in India for at least 182 days during the previous year instead of 60 days;
- ii) If any citizen of India or a foreign national of Indian origin, who is living outside India, comes on a visit to India in the previous year, he must have stayed in India for at least 182 days during the previous year instead of 60 days.

Notes:

1. A person is deemed to be of 'Indian origin' if he, or either of his parents or any of his grandparents, was born in undivided India. It may be noted that grandparents include both maternal and paternal grandparents.
2. It is not at all necessary that he should stay at a stretch for 182 days. His total stay for at least 182 days may be with gaps.
3. For calculating number of days stay in India, days of entry and exit should be included in the period of stay in India.

Additional Conditions:

A person has to satisfy both the following additional conditions besides satisfying any one of the above mentioned basic conditions in order to become 'Resident and Ordinarily Resident'.

- i) He has been resident in India in at least 2 out of 10 previous years immediately preceding the relevant previous year.
- ii) He has been in India for at least 730 days in all during the seven previous years preceding the relevant previous year.

Note: The day on which he enters in India as well as the day on which he leaves India shall be taken into account as the stay of the individual in India

2. Resident but not Ordinarily Resident:

If an individual satisfies any one of the above basic conditions but does not satisfy the two additional conditions, he is said to be 'Not Ordinarily Resident'.

3. Non-Resident:

If an individual satisfies none of the basic conditions, he is said to be 'Non-Resident'

Residential Status of Firm

A partnership firm is said to be resident in India if –

- a) **Resident:** The control and management of their affairs are wholly or partly situated within India during the relevant previous year.
- b) **Non-resident in India:** If the control and management of their affairs are situated wholly outside India. A firm cannot be ordinarily or not ordinarily resident. The residential status of the partners is not relevant in determining the status of the firm.

Residential Status of Company

- a) **Resident:** A company is said to be a resident in India in any previous year, if -
 - i) It is an Indian company; or
 - ii) Its place of effective management, in that year, is in India.

An Indian company is always resident in India. A foreign company is resident in India only if during the previous year, place of effective management is situated wholly in India.

- b) **Non-resident:** A foreign company is treated as non-resident if during the previous year, place of effective management is either wholly or partly situated out of India.

A company can never be ordinarily or not ordinarily resident in India. In case of a foreign company even the slightest place of effective management is exercised from outside India, it would be treated as a non-resident.

Incidence of Tax

Tax is levied on total income of a person. The total income is based on the residential status of assessee. Section 5 provides the scope of total income, which varies on the basis of status.

Relationship between Residential Status and Incidence of Tax

In order to understand the relation between residential status and tax liability, one must understand the meaning of Indian income and foreign income.

Indian Income and Foreign Income

Indian Income: Any of the following three is an Indian Income -

- i) If income is received in India during the previous year and at the same time it accrues. India during the previous year.
- ii) If income is received in India during the previous year but arises outside India during previous year.
- iii) If income is received outside India during the previous year but it arises or deemed to in India during the previous year.

Foreign Income: Any of the following two conditions are satisfied then such income is foreign income

Income. i) Income is not received in India. ii) Income does not arise or does not deemed to arise in India.

*** II = Indian Income, CI = Controlled Income, EI=Exempted Income,

FI = Foreign Income and NI= Nature of Income

Deemed Income: Income which is considered to be available for use by an individual regardless of actual receipt.

Deemed Incomes Under The Income Tax Act

This article discussed deemed income under sections 68, 69, 69A, 69B, 69C and 69D. This includes Tax Treatment of [Cash](#) Credit, Unexplained investments, Unexplained money, Amount of investments not fully disclosed in books of account, Unexplained expenditure and Amount borrowed or repaid on hundi in cash.

(i) Cash Credits [Section 68]

Where any sum is found credited in the books of an assessee maintained for any previous year and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year. Such cash credits may be assessed either as [business](#) profits or an income from other sources. In the case of the business community, it is usually considered as business profit. It will be taxed in the year in which such cash credits are detected.

If the assessee fails to submit any satisfactory explanation or the A.O. is unsatisfied with the explanation, the income is treated as the assessee's income from undisclosed sources.

(ii) Unexplained Investments [Section 69]

In the financial year immediately preceding the assessment year, the assessee has made investments that are not recorded in the books of accounts, and the assessee fails to furnish any. Satisfactory explanation as from where this money came or if the Assessing Officer is not satisfied with the explanation the assessee has furnished the value of such unexplained investment may be deemed to be the assessee's income of such financial year.

(iii) Unexplained Money etc. [Section 69A]

In any financial year, the assessee is found to be the owner of any money, bullion. Any jewellery or other valuable articles and all these valuable articles, money, bullion, jewellery etc. are not recorded in the books of accounts of the assessee, the assessee either does not furnish any explanation as to how he acquired these things or his explanation if furnished, is not up to the satisfaction of the Assessing Officer, the money. The value of the bullion, jewellery, or other valuable articles may be deemed the assessee's income for such financial year.

(iv) Account of Investment, etc., not fully disclosed in Books of Accounts [Sec. 69B]

In case the assessee acquired certain investments, jewellery, valuable article etc. and the actual money spent on these items is more than what is shown or recorded in his books of accounts and the assessee either does not furnish any explanation for this or with his explanation the Assessing Officer is not satisfied, the excess amount under section 69B may be deemed to the income of the assessee for such financial year.

(v) Unexplained Expenditure [Section 69C]

Where in any financial year an assessee has incurred any expenditure, and he does not explain the source of such expenditure or part thereof or the explanation offered by him is not satisfactory according to the opinion of A.O., the amount covered by such expenditure or part thereof, as the case may be, is deemed to be the income of the assessee for such financial year. The amount of unexplained expenditure deemed as income of the assessee shall not be allowed to be deducted under any head of income.

(vi) Payment of Hundi Money in Cash [Section 69D]

Any amount borrowed on 'hundi' or 'repaid on hundi' otherwise than in account payee cheque drawn upon a bank shall be deemed the income of the person borrowing or repaying the amount for the previous year in which such amount

was borrowed or repaid. If the amount borrowed is taxed as deemed income under the provisions of 69D, it will not be taxed again when the amount is repaid. The amount repaid shall include the amount of interest also.

Tax rate on deemed incomes covered u/s 68, 69, 69A, 69B, 69C and 69D [Section 115BBE]

W.e.f. A.Y. 2017-18, Deemed incomes covered under sections 68, 69, 69A, 69B, 69C, and 69D shall be charged to tax at a flat rate of 60%. This section has been inserted to restrict the benefit of basic exemption regarding such incomes being claimed by assessee liable to pay tax as per slab system (i.e., [individuals](#), [HUF](#), etc.) Further, while calculating the above incomes, no deduction for any expenditure or allowance shall be allowed to the assessee. The Finance Act 2016 has provided that no set-off of any loss shall be allowable for income under sections 68, 69, 69A, 69B, 69C or section 69D.

1. MEANING OF INCOME RECEIVED OR DEEMED TO BE RECEIVED.

- All assesseees are liable to tax in respect of the income received or deemed to be received by them in India during the previous year **irrespective of -**
 - (i) **their residential status, and**
 - (ii) **the place of its accrual.**
- Income is to be included in the total income of the assessee immediately on its actual or deemed receipt.
- The receipt of income refers to only the first occasion when the recipient gets the money under his control.
- **Therefore, when once an amount is received as income, remittance or transmission of that amount from one place or person to another does not constitute receipt of income in the hands of the subsequent recipient or at the place of subsequent receipt.**

Chart Showing the Incidence of Tax for Different Types of Status

Different Kinds of Incomes	Nature of Income	Different Types of Status		
		Ordinarily Resident (R & OR)	Not Ordinarily Resident (R but NOR)	Non-Resident (NR)
1	Income earned or deemed to be earned in India but received outside India.	II	Taxable	Taxable
2	Income earned or deemed to be earned outside India but received in India	II	Taxable	Taxable
3	Income earned and received in India or Income deemed to be earned and received in India.	II	Taxable	Taxable
4	Income earned or deemed to be earned and received both outside India.	FI	Taxable	Not Taxable
5	Income earned and received outside India from a business controlled or profession setup in India income may or may not be remitted to India.	CI	Taxable	Not Taxable
6	Income earned and received outside India from a business controlled or profession set up outside India.	FI	Taxable	Not Taxable
7	Past untaxed foreign income brought onto India during the relevant previous year. Note: Gift is not an income, if it is less than 50,000. (If gift is received by an individual from a relative or at the time of marriage or by will, it is tax free).	EI	Not Taxable	Not Taxable
8	Gift from a friend exceeding 50,000 received in India is an income. Therefore taxable.	II	Taxable	Taxable
9	Dividend from an Indian company.	II	Taxable	Taxable
10	Dividend from co-operative societies.	II	Taxable	Taxable

11	Dividend from foreign company received in India	II	Taxable	Taxable	Taxable
12	Share of profit from HUF	EI	Not Taxable	Not Taxable	Not Taxable