The Budget's impact on NRIs—what you need to know

Relaxation in double taxation of retirement funds to setting up of one-person company, the Budget 2021 has something for NRIs as well.

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Representative image (PC- MoneyControl.Com)

The **Budget 2021** has received an overwhelmingly positive response from almost everyone—the stock market, corporates, small and medium businesses, investors, both domestic and foreign, as well as the common man.

The cornerstone of the Budget is the emphasis on growth through huge capital spending (funded largely through borrowings), especially in infrastructure.

Another major reason for the wide acceptability of the Budget has been the stability in the tax regime (no major change in the tax rates) coupled with the initiatives to ease tax compliance and reduce harassment.

While the Budget has been by and large tax-neutral, it has made some changes that will have an impact on non-resident Indians (NRIs). Let us look at some of these measures:

Relief for returning NRIs

One of the major hardships faced by returning NRIs has been the possibility of **double taxation of their retirement funds** overseas. Many NRIs have been maintaining funds overseas in their retirement account even after they come back to India. The income earned from such funds is taxed in India on an accrual basis (usually every year), whereas it may be taxed overseas on a receipt basis when actually received).

For Instance, NRIs working in the US contribute funds to 401 Kaccount (a retirement fund like Employees Provident Fund in India) from their salary. The income in this account accrues on ongoing basis but is taxed in the US at the time of withdrawal or maturity.

When they return to India and continue to maintain such retirement account overseas, they are taxed in India on accrual basis. At the same time, they are liable to be taxed in US at the time of withdrawal. This creates a mismatch in the tax liability, especially since India has Double Taxation Avoidance Agreements (DTAA) with many countries whereby tax credit is available in one country for the tax paid in another country.

The government has taken cognisance of this problem and decided to frame rules to alleviate their hardship in this regard. Given the highly technical and complicated nature of this problem, it remains to be seen how effective these rules will be and how many people will benefit from the same.

NRIs can form one-person company

With a view to encourage entrepreneurship in general and make it easy from NRIs to set up business in India the government has made changes in the Companies Act to also allow **NRIs to set up a one-person companies** (OPCs).

An OPC is a corporation with only a single member (unlike a minimum of two members for a conventional corporation). The main advantage of OPC is segregation of personal liability from corporate liability, which means that the individual promoters' personal assets are protected against any dues of the OPC.

Another advantage of an OPC is less stringent compliance requirement compared to a company or LLP. Now, with the change in the Budget, not only are NRIs allowed to form OPC but the residency rules have also been relaxed. They now need to spend only 120 days in India instead of 182 to qualify as NRIs for the incorporation of OPC.

Apart from this, to move more businesses into the formal sector by easing compliance requirement, the government has increased the threshold for businesses to qualify as OPC. The paid-up capital limit has been increased from Rs 50 lakhs to Rs 2 crore and the turnover from Rs 2 crore to Rs 20 crore.

Defining 'liable to tax'

Another change for NRIs is the definition of "liable to tax" in the Income Tax Act.

Countries usually tax their residents based on the residence (the number of days they spend in the country) or domicile status. Many high net worth individuals (HNIs) have been planning their stay in countries in such a manner that they are not liable to tax in any country.

For Instance, an Indian citizen who is based in UAE and spends less than 120 days (182 days till last year) in India is liable to tax in India only on income from Indian source (let's say from property or investments in India) and not on the income arising outside India (let's say business or assets in UAE). Since there is no personal taxation in UAE, such individuals will not have to pay any tax on such income arising in Dubai.

Intending to bring such NRIs into the tax net, the government in 2020 introduced the concept of "deemed resident". This new provision provides that an Indian citizen shall be deemed to be resident in India (if his total income, other than income from foreign sources exceeds Rs 15 lakh) when they are not liable to tax in any country or jurisdiction by reason of their domicile or residence or a similar criteria. A deemed resident, thus, is taxed in India on their Indian as well as global Income.

However, due to ambiguity in the wording of the law, this new provision could not be effectively implemented. This year, the government has decided to tighten this provision by clearly defining the term "liable to tax", thereby plugging the loophole.

An offshoot of this provision has been that many NRIs are now looking at taking citizenship of other countries so that they are not hit by this provision.

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