
Tax Planning Avenues for NRIs / Returning NRIs / Outgoing NRIs

As a Non resident Indian, you are always skeptical about the tax laws in India and its administration. Over the years, the laws in India have been relaxed and simplified. The administration has also improved by being more friendly towards Non residents.

In following lines, I have tried to narrate our experience with important areas where a NRI needs to plan his affairs with Indian Taxation laws.

a) Residential Status :

As per Indian income tax Act, all individuals are categorized in three residential types: 1) Ordinary Resident 2) Resident but not ordinary Resident (RNOR) & 3) Non resident (NR). Taxation in India largely depends on residential status & nature of income. The number of days spent in India by a person decides the residential status.

It is important for NRIs to mention their residential status as “NRI” in all forms / applications etc. These could be for application of PAN , purchase of Mutual Funds etc. Any error here can have tax / legal implications. There are specific exemptions / deductions available for each category of residents and by mentioning incorrect residential status, one can miss out on the same.

In case of a resident Indian leaving India for employment / business outside India, his date of departure from India can be crucial in determining his residential status and taxability of income for that year. He therefore needs to plan the same carefully.

Case study -

For example, if Mr X leaves India on 1 st of April and carried out business overseas and earned a profit of USD 2 Mln. As he departed India on 1st April, it is likely that he would be treated as a Non Resident for that year and will not be taxed on this income of 2 Mln. Now consider a situation where Mr X departed on 15th October of the same year. In this situation, it is likely that he would be treated as a resident in India for that year and can be taxed on this income of 2 Mln in that year.

Similarly in case of a Resident but Not ordinarily resident (RNOR), income earned or received in India is taxable. Their other global income is not taxable in India. As I mentioned earlier, as the residential status is based on the number of days stay in India,

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if planned well ~ one can retain RNOR status for 3 years ended after his return to India (subject to fulfillment of conditions). This would ensure that his global income is not taxed in India for maximum permitted time limit.

b) Avoidance of Double Taxation in two different countries :

Income earned / received in India is taxable in India even in case of NRIs. In order to make sure that the NRIs do not end up paying tax on the same income in their residing country, Government of India has signed Double Tax avoidance agreement (DTAA) with more than 30 countries. Provisions of many of these DTAA throws up avenues for better planning of minimization of tax incidence for NRIs.

c) Tax saving in respect of Investments in specified Schemes / instruments :

NRIs having taxable income in India can invest in specifies instruments / schemes (like PPF, Life insurance premium, Nation saving certificates, Government recognized mutual funds etc) upto Rs.1 lac and use provisions of Income Tax Act for saving tax .

Also, for those NRIs that have realized profit on sale of property or other specified capital asset, they can invest the gain in specified financial instruments / another residential property (subject to conditions) and attain a Zero Tax position.

It is pertinent to note that following incomes are taxfree for NRIs –

- a) Interest on deposit in NRE account
- b) Interest on deposit in FCNR account /deposit.

d) No tax on Profit on sale of shares / Mutual Fund Units :

NRIs need to note that in case they have invested in shares of an Indian company through recognized stock exchanges in India and have sold these shares after holding them for more than one year, the gain on the same is tax free.

Also in case of sale of Mutual Funds units, there is no tax payable if the units are held for more than one year (*subject to conditions*).

e) Selection of Entity / structure for doing business in India :

For NRIs and returning NRIs, it is important that they select an appropriate structure in India for their ventures / employment contracts –

Indian Income Tax offers different tax treatment to different entities like Sole proprietary concern / Partnership firms / Corporate entity. NRIs need to choose an appropriate structure to suit their requirements and reduce the tax incidence.

For those working under contracts, they need to understand that in case they function under the employment contract, they are taxed as “salaries” and no deduction is available to them. However, if they were to choose to work under the “consultancy contracts”, they are eligible to claim further deductions towards expenses incurred while computing their taxable income under Indian Taxation laws.

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