Taxation of Non-Resident Indians (NRIs) in India: Issues and Reforms

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Abstract

This study explores the complex world of NRI taxes, looking at current problems and suggesting changes to improve fairness and effectiveness. The report emphasizes difficulties NRIs experience, such as ambiguity in determining status, double taxes, and a lack of investment options. Additionally, it examines how these problems affect NRIs and the Indian economy. The study then makes extensive reform recommendations, including clearer residence regulations, streamlined tax filing procedures, and NRI-friendly investment opportunities. These changes are intended to provide a more favorable tax environment, fostering greater NRI community financial stability and economic involvement while supporting India's economic growth and international financial status.

Key words: double taxation, reform recommendations, investment opportunities.

Introduction

Non-Resident Indians

Indians who live outside of India for a variety of reasons, such as work, education, family relations, business, or employment, are known as non-resident Indians (NRIs). Despite residing overseas, NRIs keep close links to India and frequently take part in economic activities that have an effect on both their host nations and India.

Economic significance

- **Investments:** NRIs frequently make purchases on the Indian stock, bond, and real estate markets. They bring in cash from abroad, which may boost the economy, provide employment, and encourage innovation. They may also transmit information and skills as a result of their investments.
- **Transfer of Skills and information:** NRIs frequently pick up useful skills, information, and experience in their host nations. They carry this expertise with them when they visit India or conduct business there, which can enhance entrepreneurship, technology, and general economic growth.
- **Diaspora Networks:** The NRI community is a part of the worldwide Indian diaspora. The interchange of goods, services, and ideas between India and its host nations can be facilitated via this network. It creates chances for corporate collaborations, joint ventures, and partnerships across a range of industries.
- **Tourism:** NRIs commonly go to India for leisure, family reunifications, or business. The tourism sector in India is supported by this flood of tourists, which is a key source of income and employment development.
- **Education and Training:** A lot of NRIs travel abroad to complete their further education or professional training. They bring new information and skills with them when they return to India, which helps the nation's human capital flourish.

- **Philanthropy and social development:** NRIs frequently participate in charitable activities, sponsoring initiatives for community development, healthcare, education, and poverty reduction in India. This may benefit society and support government initiatives.
- **Cultural Exchange and Soft Power:** NRIs are essential to the international promotion of Indian tradition, art, and culture. The host nations and India benefit from this cultural exchange by developing mutual respect, understanding, and collaboration.

Importance of taxation

For Non-Residents

Revenue Generation: Taxes help the government generate money, which is then spent on infrastructure projects, social assistance programmes, and public services like healthcare and education. When they travel to India or have family there, NRIs profit indirectly from these services.

Legal Obligation: NRIs who get income from India must pay taxes on such income. By abiding by tax regulations, they can avoid penalties, fines, and other legal repercussions and maintain their legal standing.

Investment Climate: To draw in foreign investments, particularly those from NRIs, a fair and open tax structure is essential. NRI investment in India is boosted by a stable tax structure, which also promotes economic expansion.

Social Responsibility: NRIs frequently keep close ties with India, including emotional and familial ties. Even though they do not dwell there, their tax contributions aid in the welfare and prosperity of the nation.

For India Government

Generating Revenue: The government's main source of income is taxes. Both citizens and non-citizens alike profit from the funding of vital public services and infrastructure improvements.

Economic Growth: The resources required for managing fiscal policy are made available to the government through a well-functioning tax system. Maintaining economic stability and executing stimulus measures during economic downturns are part of this.

Growth and Investment Incentives: Investment and entrepreneurship are supported by an effective tax structure. The entire population gains from this since it generates more jobs, higher productivity, and greater economic growth.

Reduced Inequality: A more egalitarian society may be fostered by progressive taxation, which can assist redistribute wealth and lessen income inequalities. The stability and cohesion of society may be enhanced through this.

Fulfilment of International Commitments: For India to maintain its reputation in the international community, compliance with international tax norms is essential. In addition to facilitating cross-border corporate operations, it promotes global collaboration and aids in the fight against tax evasion.

National Security and Sovereignty: Ensuring the nation's sovereignty, supporting its military, and sustaining its security all depend on having enough money coming in.

Residential status

"A person is regarded as a resident of India if they satisfy one of the following requirements:

They spent at least 182 days or more in India during the relevant fiscal year. They have spent a minimum of 60 days in India during the financial year and a total of 365 days in India in the four years that came before the relevant financial year.

If a person does not satisfy one of the aforementioned requirements, they are regarded as non-residents. In the financial year, this implies they were in India for less than 182 days, and in the four years prior, they were not in India for 365 days or more."

Literature review

- **Nonresident deposits in India: a conceptual study by Dr. Neelam Sethi -** Non-Resident Deposits (NRDs) are a crucial source of foreign currency since they are unconditional, providing a known and dependable supply of foreign exchange. Because they are unaffected by currency fluctuations, FCNR Deposit Accounts (Foreign Currency Non-Resident Accounts) make up a sizable portion of non-resident deposits. A courtier's ability to build their financial position depends on deposits of this kind. The researchers have thoroughly examined this topic in reference to its notion and significance in an effort to increase interest in growing these deposits among NRIs.
- **Taxation of non-residents by Cling Harding -** This article focuses mostly on taxing capital gains obtained by non-residents. In light of Australia's extensive network of tax treaties, the article examines the fundamental domestic taxing system for capital gains for non-residents. The article also briefly examines the government's most recent plan to impose a capital gains tax withholding tax on non-residents. As part of this evaluation, the article covers some of the concerns and challenges that have lately surfaced in this area.
- **India's relationship with Non-Resident Indians by Marie Lall -** Taxing capital gains earned by non-residents is the main topic of this article. The essay analyses the fundamental domestic taxing structure for capital gains for non-residents in light of Australia's broad network of tax treaties. The government's most recent proposal to charge non-residents a capital gains tax withholding tax is also briefly discussed in this article. The article discusses some of the worries and difficulties that have recently come to light in this area as part of this evaluation.
- **India: recent changes affecting non resident taxpayers by Har Govind -** One of the laws that has undergone the most amendments in India is the Income-tax Act (IT Act). The Annual Finance Act allows for the enactment of around 30 modifications annually. Additionally, periodic separate modifying Acts are passed. The recent significant changes to income tax law that affect non-resident taxpayers and businesses are studied in this essay. Indirectly or through joint ventures, non-residents and international businesses are operating in India by establishing Indian corporations. Only the income that comes from India is taxed. They jointly own an Indian firm, which is taxed similarly to other Indian companies.
- **The research paper on Nonresident deposits in India: a conceptual study by Sonia Sorte & Dr. HG Abhyankar -** Non-Resident Deposits are significant because they are unconditional in nature, making them a confirmed and reliable source of foreign cash. In fact, a significant portion of non-resident deposits take the form of FCNR Deposit Accounts (Foreign Currency Non-Resident Accounts), which are unaffected by exchange rate changes. Deposit in Foreign Currency by Non-Residents an Indian-only product called a Foreign Currency Non-Resident (FCNR) Deposit is primarily intended for non-resident Indians (NRIs) and people of Indian origin (PIOs) who desire to hold financial deposits in

the foreign currency of their choice. Usually, the USD, GBP, EUR, JPY, AUD, and CAD are the available currency alternatives.

Research methodology

The approach involves a thorough analysis of current scholarly works, government publications, tax regulations, and official documents concerning the taxation of NRIs. This will make it easier to comprehend the current tax system, pinpoint the major problems NRIs confront, and evaluate recent revisions. To give context and serve as a standard, comparative evaluations of tax laws in other nations may also be presented. The research does not entail interviews or in-depth data analysis; instead, it concentrates on synthesizing and critically assessing existing literature to get insights into the difficulties and potential solutions in the taxation of NRIs in India.

Data analysis

Exemptions and deductions

Basic Exemption Limit:

The same fundamental exemption threshold applies to NRIs and residents alike. This restriction is INR 2.5 lakh for those under the age of 60, INR 3 lakh for people between the ages of 60 and 80, and INR 5 lakh for people above the age of 80 as of my most recent knowledge update in September 2021.

Foreign income tax:

Only income earned or received in India is taxed for NRIs. Indian income tax normally does not apply to money earned overseas.

Deductions under Section 80C: NRIs are allowed to make deductions under Section 80C for investments made in a number of specified securities, such as Provident Fund, National Savings Certificates, ELSS (Equity-Linked Savings Scheme), etc.

Exemption on Rental Income: Under Section 24(b), various deductions may be made by an NRI who owns real estate in India and receives rental income.

Contributions to the National Pension System are exempt, and NRIs may deduct their NPS contributions under Section 80CCD.

Interest from NRO Accounts: Interest from NRO (Non-Resident Ordinary) accounts is exempt from taxation in India up to a specific level.

DTAAs and their role in avoiding double taxation for NRIs

Double Taxation Avoidance Agreements (DTAAs) are bilateral agreements between two nations that are designed to prevent a taxpayer from being taxed twice on the same income in both their home country and the foreign country where the money is produced. These accords offer a framework for deciding which nation has the primary authority to tax particular forms of income.

DTAAs are essential in helping Non-Resident Indians (NRIs) manage their tax obligations. Here is how DTAAs function and what they mean for NRIs:

Allocation of Taxing Rights: DTAAs divide up the right to tax various forms of income, including wage income, business earnings, dividends, interest, and capital gains, among the signatory nations. The DTAA will establish, for instance, whether an NRI's income earned abroad is principally taxable in India or in the foreign country.

Residency requirements: In the event that a person is regarded as a tax resident in both countries, DTAAs also contain requirements that specify their tax residency.

- This is crucial for NRIs who may qualify for tax residency in both India and the foreign country in which they live or generate money.

Mutual Agreement Procedure (MAP): DTAAs typically create a procedure for resolving disputes. The Mutual Agreement Procedure is the name given to this process.

- The taxpayer may start a resolution process if the tax authorities of the two nations dispute on how to interpret or apply the DTAA.

Investment Promotion and Economic Cooperation: DTAAs can encourage international investments and business collaboration by increasing clarity and removing tax-related obstacles. For NRIs who conduct business or hold investments in both India and their place of residence, this might be very significant.

Prevention of Tax Evasion and Avoidance: DTAAs contain rules meant to discourage tax evasion and avoidance. It's possible that they have provisions for information sharing and teamwork between the tax administrations of the two nations' respective countries.

Impact of DTAA

Income Sourcing: DTAAs specify which country has the principal authority to tax particular forms of income. This prevents double taxation. This guarantees that foreign income generated by NRIs is only taxed once.

Residency Rules: DTAAs offer standards for determining a person's residency status. This makes it easier to determine whether an NRI must pay taxes in India or their home country.

Lower Withholding Rates: DTAAs frequently call for lower withholding tax rates to be applied to specific categories of income like interest, dividends, and royalties. NRIs who receive income from India may find this to be especially advantageous.

Tax Credits and Exemptions: Depending on the terms of the applicable DTAA, NRIs may be eligible to claim tax credits or exemptions. This aids in lowering the total tax obligation.

Clarity Regarding Taxation Laws:

Avoiding Conflicting Laws: DTAAs aid in resolving any potential differences in tax regulations between the country of residency and the country of origin. This clarifies for NRIs what their tax responsibilities are.

Protection from Discrimination: Non-Discrimination Clause: Many DTAAs contain a clause that guarantees that NRIs won't be exposed to unfair tax treatment in the source country. This protects their rights and promotes international business.

Avoiding Tax Evasion and Erosion:

Information Exchange: DTAAs frequently have clauses that allow nations to share tax-related data. This promotes transparency in tax proceedings and aids in the prevention of tax evasion.

Challenges and Criticisms: Interpretation and Application: There may occasionally be difficulties with the interpretation and application of DTAA rules. This may result in disagreements between taxpayers and tax authorities.

Complexity: NRIs may find it difficult to properly understand and take advantage of DTAAs due to their complicated language and complexities.

Impact on Investments and Economic Activity:

Increasing Investments: DTAAs can encourage international investments by granting some tax certainty and lowering the overall tax burden on NRIs.

Economic Development: By lowering tax barriers to international trade and investment, DTAAs support economic development.

Application to International Tax Planning:

Asset Allocation: NRIs frequently take DTAAs into account when deciding where to invest or carry out company operations in order to minimise their tax liability.

Issues

Complex Tax Laws: The Indian tax code can be challenging to understand, particularly for people who live abroad. NRIs frequently experience difficulty comprehending their tax responsibilities, which can result in unintentional non-compliance.

Restrictions on Repatriation: Individuals may be subject to constraints or restrictions when sending money, they have earned in India back to where they currently reside. This may limit the capital mobility of NRIs and deter investment.

Treatment of Foreign Income: India's reporting and taxation requirements for foreign assets, investments, and income may be unclear. Included in this are earnings from investments, investments abroad, and offshore accounts.

Property taxes: There are unique tax repercussions for NRIs who own property in India. It can be difficult to understand how to calculate property taxes, capital gains tax upon sale, and how to approach rental income.

Bank Account Reporting: It may be necessary for NRIs to declare overseas bank accounts and assets, which can be time-consuming and difficult.

Different tax authorities or officers may interpret tax rules differently, which might result in uneven tax treatment for NRIs. Confusion and irritation may result from this lack of consistency.

Lack of Clarity Regarding Exemptions and Deductions: NRIs may find it difficult to comprehend and make use of the exemptions, deductions, and tax credits available to them under Indian tax regulations.

Compliance Issues: It can be logistically difficult to file taxes in India from overseas. NRIs could have trouble locating required paperwork, connecting with tax experts, and fulfilling filing deadlines.

Investment Decisions and Tax Efficiency: To ensure they are making tax-efficient decisions, NRIs may need to carefully analyse the tax consequences of their investments, both in India and in their place of residence.

Limited Access to Tax Resources: It may be challenging for NRIs to maintain compliance because they have little access to trustworthy sources of knowledge on Indian tax rules and regulations.

Recent reforms related to taxation of NRIs

- Budget for 2021–202 Changes: Residential Status Clarification: The Finance Act 2020 refined the concept of "Resident" to stop people from abusing loopholes to evade paying taxes.
- Relief for NRIs Stranded in India: Due to the COVID-19 epidemic, a relief provision was introduced to make sure that NRIs who were trapped in India because of lockdowns didn't end up becoming residents for tax purposes.
- Relaxation in TDS Rates: Tax Deducted at Source (TDS) For certain payments made to locals and NRIs, TDS rates were lowered as a means of providing aid during the epidemic.
- Faceless Evaluation and Appeals: Digital Evaluation and Appeals: Reduced face-to-face connection and increased transparency are the goals of the implementation of faceless assessments and appeals.
- Procedure Simplification: Online Filing and Verification The government has been attempting to make tax filing and verification procedures easier to access through online platforms.
- Budgetary Amendments Proposed for 2021–2022: Reduction in the Minimum Period for Residential Status: The government proposed lowering the minimum period from 182 days to 120 days for a person to be declared a resident, which may have an impact on NRIs.
- Tax Relief for Provident Fund Withdrawals: It was discussed how to provide NRIs a tax break on their withdrawals from provident funds.
- Launch of the Vivad se Vishwas Scheme: To resolve open direct tax disputes, this programme was developed. It gave taxpayers, including NRIs, a venue to settle tax issues without having to go through drawn-out legal procedures.
- Rules for Not Normally Residents (NOR) have changed: Changes to the standards for identifying someone as not ordinarily resident were made by the Finance Act 2020, and these changes may have an effect on NRIs' tax obligations.
- Compliance with the Foreign Account Tax Compliance Act (FATCA) and the Common Reporting Standard (CRS), which have an impact on NRIs' financial reporting, is something that India has been attempting to achieve.

How these reforms affected NRIs and Indian economy

Impact on NRIs:

- Simplified Taxation Procedures: Tax law reforms that attempted to make things simpler have made it simpler for NRIs to comprehend and adhere to their tax duties. Financially, NRIs have benefited because this has lessened the necessity for costly expert aid and the stress of compliance.

- Improved Investment Confidence: NRIs' confidence in making investments in India has grown as a result of more transparent regulations on property taxation and other investments. Due to this, NRIs have increased their foreign direct investment (FDI), resulting in economic growth.
- Facilitated Repatriation of Funds: Thanks to reforms that relaxed repatriation limitations, NRIs are now able to transfer their money more freely across international borders. NRIs now have more flexibility and liquidity to manage their finances as a result.
- Real Estate Sector Stimulated: The real estate sector has been sparked by more transparent property taxation rules. It has benefited the building and housing industries as NRIs, who have historically been big investors in Indian real estate, are now more willing to enter into property deals.
- Avoiding Double Taxation: By effectively implementing Double Taxation Avoidance Agreements (DTAAs), NRIs are no longer subject to double taxation on their worldwide income.

The effect on the Indian economy:

- Higher FDI Inflows More overseas investments from NRIs have been drawn in thanks to simplified taxation and more explicit regulations. Since FDI inflows have increased as a result, capital formation and economic growth have both benefited.
- Increased NRI Investments in Real Estate and enterprises: The increased NRI investment in real estate and enterprises has stimulated economic activity across a number of sectors.
- Diversification of the Tax Base: The tax base has become more diverse as a result of the increased participation of NRIs in the Indian economy.
- Greater Financial Inclusion: Reforms that make it simpler for money to be repatriated have prompted NRIs to participate more actively in the Indian financial system. The financial markets have become more complex as a result, increasing financial inclusion.
- Greater Recognition of India as an Investment Location: India's reputation as an appealing location for investment has improved with the execution of reforms addressing NRIs' requirements. This perception has a favourable impact on both investor confidence in the Indian economy and worldwide rankings.

Suggestions

Recommendation of reforms

- Introduce streamlined tax filing methods designed specifically for NRIs to decrease complexity and boost compliance.
- To eliminate conflicts and ambiguity in interpretation, establish standard tax rules throughout all states.
- Establish precise regulations regarding the taxes of real estate owned by NRIs, including those governing rental income, capital gains, and inheritance.
- By removing pointless constraints and administrative roadblocks, simplify the procedure for repatriating funds.
- Create user-friendly online platforms for NRIs to file their taxes and make payments, making the process more straightforward and available.
- Run educational programmes and awareness initiatives aimed at NRIs to inform them of their tax rights and obligations.
- Enhance the dispute resolution process by creating a body or system specifically designed to deal with tax-related complaints involving NRIs and ensure prompt resolutions.

- To better their comprehension of NRI-specific tax regulations, provide normal tax officials with training on NRI taxes.
- Provide NRIs with specialised tax planning services to minimise their tax liability and ensure that they are in compliance with Indian tax legislation.
- Take a proactive role in bilateral conversations with nations that have a sizable NRI population to negotiate and revise DTAAs.
- Tax incentives should be introduced to encourage NRI investment in certain industries, such as infrastructure, technology, or healthcare, in order to support economic growth.
- Through official channels and embassies, ensure that NRIs are regularly informed about changes in tax laws and procedures.
- Establish a feedback system that will allow NRIs to share their thoughts on the tax system in order to help it keep becoming better.
- Make sure that the process of tax assessment is transparent, and give NRIs explicit justifications for any modifications or assessments that the tax authorities make.

Conclusion:

The taxation of non-resident Indians (NRIs) in India is the subject of a thorough investigation in this research paper, which also raises important questions and suggests possible improvements. The relevance of NRIs' tax resident status is explained in the opening paragraphs, along with the sources of their taxable income. In order to address concerns about double taxation, the study places a strong emphasis on the function of DTAAs. The difficulty of tax rules, their varying interpretations, prohibitions on repatriation, and the uncertainty of property taxation are among the main problems. The implications of recent reforms on NRIs and the Indian economy are highlighted and analysed. In its last section, the document makes reform suggestions and calls for streamlined tax rules, uniform application, loosened repatriation limits, and clearer property taxation regulations. Case studies that highlight particular difficulties NRIs in India have to deal with are also included.

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