



CITIZENSHIP BASED TAXATION IN INDIA

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Tax incidence on a taxpayer in India depends upon his residential status. Whether an income earned by an individual, in or outside India, is taxable in India depends on the residential status of the individual rather than on his citizenship. People are often under the wrong impression that taking up foreign citizenship helps obtain tax benefits. The Income Tax Act, 1961 (Act) does not provide tax benefits on the basis of a person's citizenship.

In the Finance Act 2020, an important amendment to the Income Tax Act 1961 is made to levy tax on Individuals based on the Citizenship rather than on the residential status. Under the existing provisions of Income Tax Act 1961, Section 6 lays down the conditions for determining the residential status of Individual and accordingly, the individual is classified as Resident, Resident and Not Ordinarily Resident and Non Resident depending up his presence in India during the previous year and the income is charged to tax in accordance with the provisions of section 9.

Now the focus is on increasing the tax base so as to enable levy tax on source of income rather than the residential status. The source of income is place of accrual.

Present amendment is sought to increase the tax base thereby resulting in increased tax revenue to the government in the category of individual by focusing the citizenship or nationality.

Indians are migrating outside India for employment and business. The trend is increasing in the country resulting in not only brain drain but also resulting in loss of tax revenue to the country as the tax revenue is diverted to other countries.

High Net Worth Individuals (HNI) are planning their affairs in such a way that they are not liable to be taxed in any country or territory. Under the existing provisions of residential status, it is possible to avoid taxes.

The amendment speaks as

“The issue of stateless persons has been bothering the tax world for quite some time. It is entirely possible for an individual to arrange his affairs in such a fashion that he is not liable to tax in any country or jurisdiction during a year. This arrangement is typically employed by high net worth individuals (HNI) to avoid paying taxes to any country/jurisdiction on income they earn. Tax laws should not encourage a situation where a person is not liable to tax in any country. The current rules governing tax residence make it possible for HNIs and other individuals, who may be Indian citizen to not to be liable for tax anywhere in the world”

The second proviso of Sec. 6 (1)(b) is amended by The Finance Act, 2020, w.e.f., Assessment Year 2021-22 to provide that the period of 60 days shall be substituted with 120 days

The Finance Act, 2020 has introduced new section 6(1A) to the Income-tax Act, 1961. The 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 lakhs during the previous year. For this provision, income from foreign sources means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India).

From the Assessment Year 2021-22, an Indian Citizen earning total income in excess of Rs. 15 lakhs (other than from foreign sources) shall be deemed to be resident in India if he is not liable to pay tax in other country.

Most of the countries in the world levy personal tax based on the residential status. There are some countries which levy tax based on citizenship of the individual. The countries levy tax on foreign income of their non-residents. One of the country adopting the citizenship based taxation is United States.

This proposal has created confusion among Indian expatriates working in other countries.

Introducing citizenship-based taxation in India is in line with India's intent to increase its tax base and to increase the tax revenue. This makes an individual to plan the physical stay in India v/s overseas.

In view of this, Indian citizens who qualify as deemed residents and who have foreign income from business need to determine business income and declare and chargeable to tax in India, if the specified conditions are met.

We have already have Double Taxation Avoidance Agreements with around 85 countries. Tax Payers allowed to claim the relief either as per Section 90 or Section 91. But with the new amendment, there are chances of taxing the income in both the countries. As per the amendment the foreign income is taxed *if he is not liable to pay tax*. Since the method of personal taxation varies across the world, the amendment may create confusion.

It is imperative that the country is required to increase the tax base in respect of personal taxation. The tax authorities will have to continuously required to function in order to get the information from various countries.

Already the Government has introduced two tax regimes – old and new from the Assessment Year 2021-22 which has created ambiguity among the tax payers. Adding, the new provision, i.e., citizenship based taxation will create further confusion for the NRIs.

The move towards taxing the income on citizenship rather than on source of will make the non-residents to reduce their relationship with the country and may resort to permanently renounce the citizenship of the country.

India with a population of 130 crores, only around 6 crores file tax returns and around 1.5% to 2.00 % pay income tax.

The number of individual tax payers who have disclosed income above Rs 5 crore in the whole of the country is only around 8,600 during the previous assessment year.

Around 2200 professionals disclosed annual income of more than Rs.1 crores excluding other incomes like rental, interest, capital gains among others in the returns filed in the ongoing fiscal.

The above indicates that there is a need to increase the tax payers by increasing the tax base. The tendency is higher among the individuals to evade tax among the individuals other than salaried people. In the US, a single person starts paying income tax at an income level of about \$12,000 (approx. Rs 8.6 lakh), which closely parallels the level of the poverty line for an individual.

USA is the only country taxing its worldwide nonresident citizens. Under the Double Taxation Treaties they may get credit for the tax paid. But they are required to file the income tax returns.

It is high time to think about the progressive taxation, i.e., increase the tax base and reduce the tax rates and also the income increases, the rate also increases. In a country like India, this is the alternative to increase the tax revenue.

In the FY 2019-20, the personal tax revenue to Government was Rs. 5.55 lakh crores constituting around 26.30% of the total tax revenue. There is need for enhancing this figure in view of the population in the country. But taxing Non Residents based on Citizenship is not a solution.

Most of the countries has the tax limit below the average of the people. But in India the tax limit is much higher than the average income.

According to CBDT, there is an improvement in the tax base. The introduction of Citizenship Based Taxation in the country, may result in reversal of the trend of increasing the tax base in personal taxation segment.

There are instances, where, some countries after introducing the citizenship based taxation has withdrawn. For example Phillipines.

Instead, Government may require to resort to other provisions of the tax law to bring the tax evaders into the tax net. Even there is increase in personal taxation to the extent of 1%, it will result in substantial amount of tax revenue.