

# SPECIAL PROVISIONS RELATING TO CERTAIN INCOME OF NRIs

Some of the special tax concessions for NRIs/PIO investing in India were introduced in the Finance Act, 1983, which became effective on June 1, 1983. The tax provisions were further liberalized by subsequent Finance Acts and other amending laws.

## **Special Concessions**

Investment income from 'foreign exchange assets' comprising shares and debenture of and deposits with Indian companies and central government securities, subscribed to or purchased in convertible foreign exchange, is charged to income tax at a flat rate of 20%. No deductions are, however, allowed and tax is levied on gross income. The basic exemption, below which income is not taxed in India, is also not allowed.

Under these special concessions a reduced rate of 10% is applied to the long-term capital gains on transfer of any foreign exchange asset held by the NRI/PIO. In order to qualify for long-term capital gains, the minimum holding period for shares held in a company or any other security listed in a recognized Stock Exchange in India or units of Unit Trust of India or of a specified Mutual Fund is 12 months and for other assets it is 36 months. Long-term capital gains on foreign exchange assets are, however, exempted from tax if the net proceeds realized on transfer are re-invested, within six months of such transfer, in any specified securities and the new assets are retained for at least three years. The Finance Act, 2003 has withdrawn the taxing provision in respect of dividend received by the shareholders on shares held in Indian

companies. Accordingly, dividend received by the shareholders of Indian companies will be exempt from tax. The income received from units of Unit Trust of India and of specified mutual funds will also be exempt.

Finance Act 2004 has:

- (a) Granted tax exemption as regards long term capital gains arising from transfer of equity shares in a company and/or units of equity oriented schemes of Mutual Funds, which are subject to securities transaction tax; and
- (b) Fixed at 10% the tax on short-term capital gains arising from such shares and/or units.

The tax concessions in respect of investment income (and not long term capital gain) will continue to apply even after the NRI/PIO returns to India but such exemption would be available only in respect of foreign exchange assets other than shares in Indian companies and the exemption will continue until such time as the assets are transferred or converted into money. However, as dividend is exempt income from 1st April 2003, exclusion of shares from said provision is redundant.

In the circumstances where the income of NRI/PIO from such foreign exchange assets is below the taxable limit or the average level of tax is below 20%, he may elect not to be governed by the special tax concessions referred to above. He would then have to furnish a Return of Income in the normal course together with a declaration of such election and he would be entitled to claim a refund of the whole or a part of the tax

deducted at source, as may be appropriate. As mentioned above, short-term capital gains arising from transfer of equity shares and/or units of equity-oriented schemes of Mutual Funds, which are subject to securities transaction tax, are taxed at 10%. Other Short-term capital gain is taxable at normal slab rates as applicable to residents, and the return of income has to be filed by the NRI/ PIO making such gain. Capital gain from transfer of shares or debentures of Indian companies will be computed by converting the cost of acquisition, expenses incurred in connection with such transfer and the sale price of the capital asset into the same foreign currency as was initially used in

the purchase of these assets and the capital gain so computed in such foreign currency will be reconverted into Indian currency. This computation effectively gives the NRI/PIO the benefit of claiming exchange loss, if any, on all capital gains arising from sale of shares or debentures of Indian companies, whether these are long term or short term. It may be noted that the aforesaid benefit is available only if the investment is made from convertible foreign exchange. In respect of investment made from funds other than convertible foreign exchange, and if the asset is a long-term capital asset benefit of indexation can be availed. However, indexation is not available in respect of debentures.