TCS provisions on remittances under Liberalised Remittance Scheme

Impact of amendment in TCS provisions

Background

The tax collection at source (TCS) framework for Liberalised Remittance Scheme (LRS) was revamped effective 1 October 2023. There was *inter-alia* change in rates and thresholds for different categories of remittances. Now that the remittance data after the revision of these rates (effective from 1 October 2023) is available in public domain, this paper attempts to analyse the quantitative and qualitative impact of these changes seen so far and the trends going forward.

The journey

As per Section 206C(1G) of the Income Tax Act, 1961 (the Act), TCS is required to be levied on foreign remittances under the LRS. This provision was introduced vide Finance Act 2020 (with effect from 1 October 2020) to include foreign remittance 'outside India' through LRS and sale of overseas tour packages within its ambit.

The Finance Act, 2023, deleted the term 'out of India' (with effect from 1 July 2023). Hence, all remittances under LRS are now subject to TCS, whether transacted in India or outside India.

Details of TCS rates on remittances under LRS applicable up to 30 September 2023 and changes applicable from 1 October 2023 are provided below:

Type of remittance	TCS rate till 30 September 2023	TCS rates effective 1 October 2023
Education, where the source of funds is through a loan obtained from a specified financial institution	0.5% of the amount or the aggregate of the amounts in excess of INR 7 lakh.	0.5% of the amount or the aggregate of the amounts in excess of INR 7 lakh.
Education or medical treatment	5% of the amount or the aggregate of the amounts in excess of INR 7 lakh.	5% if aggregate remittance exceeds INR 7 lakhs.
LRS for other purposes	5% of the amount or the aggregate of the amounts in excess of INR 7 lakh.	Nil up to INR 7 lakh and 20% thereafter.
Overseas tour package	5% without any threshold limit.	5% up to INR 7 lakh and 20% thereafter.

Grant Thornton Bharat's point of view

Impact of revised rates of TCS on remittances w.e.f. 1 October 2023 on overall outflow under LRS

As per the Reserve Bank of India (RBI) reports, remittances abroad under the LRS during the financial year (FY) 2023-2024 were USD 31.73 billion, significantly higher than the remittances of USD 27.14 billion recorded for the financial year 2022-2023. However, between October 2023 and March 2024, LRS remittances decreased by 2.75%.

A deeper analysis of the major contributors under LRS remittances shows an interesting trend. Data for the period 1 October 2023 to 31 March 2024 vis-à-vis the same period last year shows that post 1 October 2023, there has been an increase in quantitative terms in remittances for foreign travel, overseas education, and medical expenses whereas remittances for deposits, purchase of immovable property, investment in equity/debt, gifts, donations, maintenance of close relatives, and others have witnessed a fall.

During FY 2022-23, the major contributors to forex outflow under LRS in (percentage terms) were:

50% Foreign travel

15% Maintenance of close relatives

13% Studies abroad

11% Gifts

This trend continued during the period 1 April 2023 to March 2024, and the major contributors to forex outflow were:

54% Foreign travel

15% Maintenance of close relatives

11% Studies abroad

11% Gifts

Impact of TCS on remittances made by Ultra High Net-worth Individuals (UHNIs)

In the past five years, around 30,000-35,000 UHNIs have migrated to countries such as the US, UK, UAE, Canada, Australia, Singapore, and Europe, and in 2022 alone, this number was 8,000.

The levy of TCS has enabled Revenue authorities to track remittances with tax returns filed by individuals leaving the country. Further, the regulatory requirement of repatriating unutilised or unspent funds held in an overseas account back to India within 180 days has created practical and operational difficulties for UHNIs. This climate of regulatory vigil may prompt UHNIs to look for avenues to park the funds in small to mid-term investment avenues until adequate funds are accumulated before the same can be deployed for the ultimate intended purpose.

Impact on certain high-value remittances made by residents

1. Investment in real estate outside India

In recent times, UHNIs have been diversifying their investment portfolio beyond Indian shores by investing in international real estate. The investment in real estate is generally with the intent of either having a second home, home for children studying abroad or even as a pure investment.

Remittances for the purchase of immovable property have declined by 16% during the period October 2023 to March 2024.

The current LRS framework permits family members to combine their LRS limits for buying real estate. However, the limit may still not be sufficient to cover the proposed investment. Therefore, a resident Indian may be constrained to send the required amount in multiple instalments over several years and keep such amounts invested in permissible instruments outside India, to avoid the need to bring back the funds within 180 days.

Another impediment arises from the fact that the law does not permit borrowings to acquire property overseas. Even if immovable property is purchased in instalments or under a staggered payment plan, there is a risk that the regulator may still view it as an indirect borrowing.

These myriad restrictions may deter investments in immovable property outside India or encourage innovative investment structures involving long-term leases or investment through subsidiary companies.

Even under the Overseas Direct Investment (ODI) route, there are restrictions for an Indian company to invest in real estate[1]. Buying an immovable property with an intent to lease is considered as real estate activity which is prohibited under the Overseas Investment rules.

On the other hand, a resident may invest in a limited liability partnership or company in India. Such a company may invest up to 400% of its net worth in a foreign company engaged in bonafide businesses other than real estate activity outside India. There is no restriction for such a foreign company to acquire real estate outside India. This route has been followed by residents to acquire immovable property outside India, by passing the regulatory constraints.

However, the RBI has noted a recent uptrend in investment in real estate abroad through the ODI route and is examining remittances to confirm that the objective of foreign company undertaking a bonafide business activity has not been violated in some instances.

Thus, it is essential to ensure that whenever such investments are made, the foreign entity is carrying out real business activities and is not set up for the sole purpose of acquiring immovable property.

2. Golden visas

A golden visa is a type of residency or citizenship programme offered by several countries worldwide, allowing HNIs to obtain residency or citizenship by making a specified investment in the host country. Such programmes have been gaining popularity amongst India's UHNIs who wish to diversify their portfolio, access numerous opportunities in business and education across the globe or obtain a second citizenship.

Golden visa programs are currently offered by several countries around the globe, including UAE, Portugal, Spain, Greece, Malta, Cyprus, the United States, and Canada. Generally, the investment required under the golden visa programme ranges from EURO 250,000 to EURO 2 million.

The applicability of TCS on LRS could lead to temporary blockage of funds for the individual but that is unlikely to have any significant impact on the investment decision of UHNIs from Golden visa perspective. However, the challenge is that, in most cases, the amount required is much higher than the annual LRS permitted. Using the consolidated limit of the family members to enhance the permissible remittance amount also creates a practical challenge, as in such cases, all the remitters may need to be co-owners in the investment, which may not comply with the eligibility criteria of a golden visa. These impediments will result in evaluation of innovative and complex models for investment.

3. Travel

There has been a 12% increase in foreign travel expenditure during the period October 2023 to March 2024 in continuance of the 'revenge travel' trend post the COVID-19 pandemic.

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1 "Real estate activity" means buying and selling of real estate or trading in Transferable Development Rights but does not include the development of townships, construction of residential or commercial premises, roads or bridges for selling or leasing.

It seems unlikely that TCS will impact spending for foreign travel, which is expected to continue to rise, at least in the short run.

4. Education

Education is another area that is showing a growing trend. There has been an 8% increase in overseas education expenditure during the period October 2023 to March 2024.

The aspiration for global exposure and lack of adequate seats in premier Indian institutes such as IIMs, IITs and NITs, indicates that the trend of young Indians applying for colleges and universities outside India will continue.

TCS is levied not only on the tuition fees paid for overseas education but also on remittance for students' living expenses[2], and this has impacted cash flows for families sending children abroad to pursue higher education. However, most Indians consider education a necessary expense, so TCS is unlikely to affect this outflow. This is more so in cases where education is funded by loans from specified institutions where the TCS rate is 0.5%. Overall, it seems unlikely that the increasing expenditure under this head will be adversely impacted.

5. Foreign events like weddings

As per estimates by the Confederation of All India Traders, nearly 5,000 affluent couples are hosting weddings abroad every year, and the total expenditure ranges from INR 75 thousand crore to INR 1 lakh crore. The government has initiated a 'Wed in India' concept to minimise the outflow on this front.

It is expected that the levy of TCS on this expenditure may give a boost to 'Wed in India.' The quantum of TCS may not by itself impact the decision of affluent families on such wedding celebrations, especially when the TCS is entirely creditable against the tax liability of the individual. However, the need to report the expenditure, as a result of TCS levy may prove to be a deterrent for some.

Key takeaways

Analysis of the data shared by the RBI thus reveals that:

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TCS does not appear to be a deterrent for remittances related to **education abroad and medical treatment**. This may be on account of the importance given by Indian families to their children's education, more so as the TCS rate in case remittance for education funded from loan taken from specified institutions is 0.5%. Similarly, for medical exigencies, the necessity of the expense seems to supersede inconvenience created by blockage of funds, if any, under TCS.

02

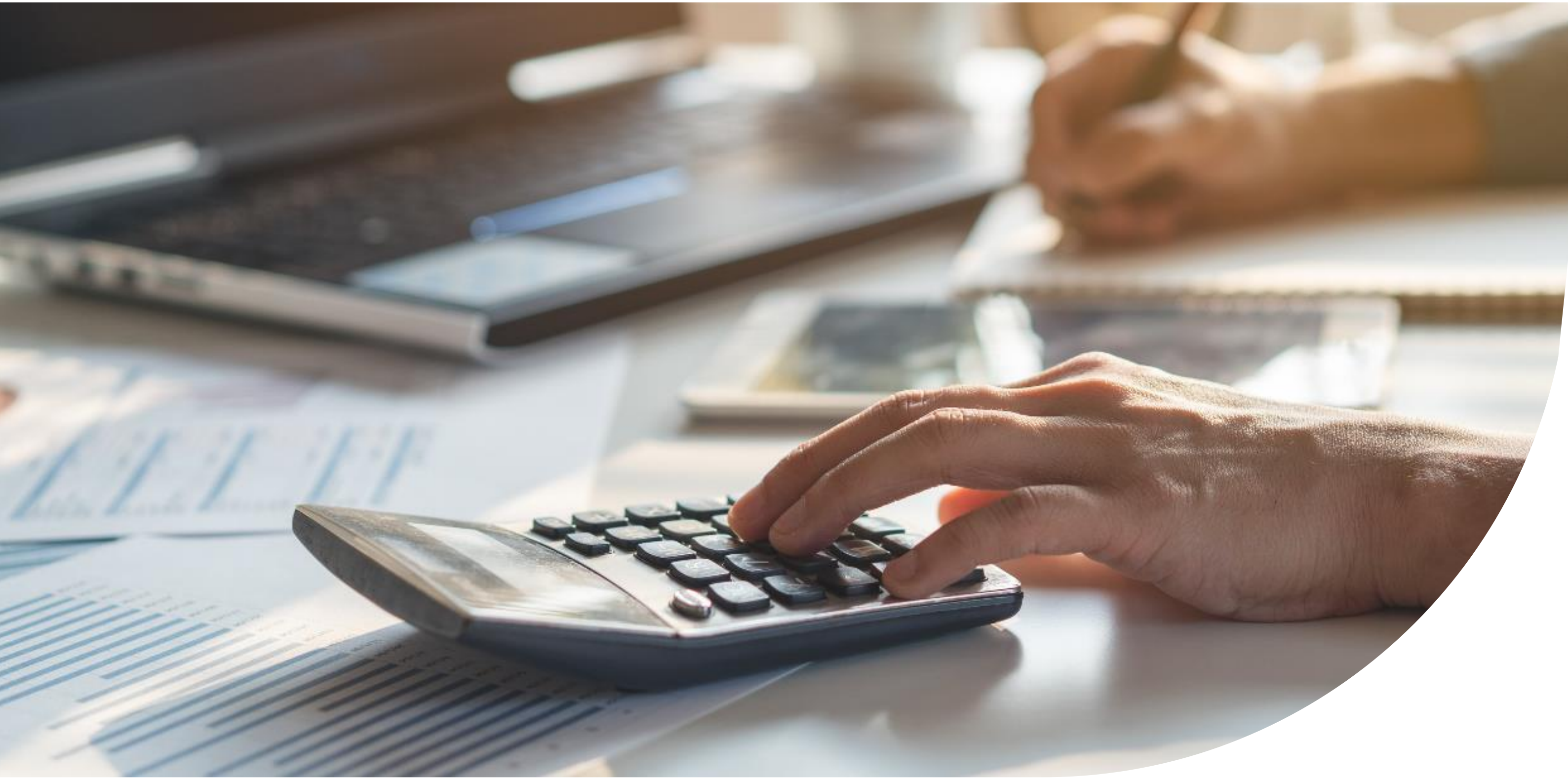
As far as remittances by HNIs on **travel and golden visas** are concerned, again, there seems to be no impact. The reason could be that TCS is creditable against the income tax liability. Since, the return processing time by the tax department has significantly improved, the cash flow impact during the intervening period may also not be an impediment.

03

In case of **purchase of real estate and investments abroad**, there is a decline. TCS creates a blockage of funds and need to restructure the manner of investment. Accordingly, the trend seems to be towards exploring alternative solutions.

It may be helpful to see if the government takes note of these trends to assess if the objective sought to be achieved by these changes could be achieved more effectively by simplification of the current regime and rationalisation of TCS rates.

2 FAQ no 7 of CBDT Circular No 10 of 2023 dated 30 June 2023



Grey areas

1. Are the sources of funds to be justified for remittances outside India?

The regulations do not mandate this, but, as per recent news reports, at least two private banks (one large and another mid-sized) have recently questioned clients on source of funds.

2. Are contributions to family trusts set up outside India included under the Liberalised Remittance Schemes?

The LRS does not specifically provide limits for trusts. However, our view is that contribution to an overseas trust where the beneficiaries are non-residents of India would be subject to LRS limits of the settlor. Similarly, distribution from the domestic trust to non-resident beneficiaries would also be covered by the LRS limit of the settlor. However, authorised dealer banks are taking diverse views on the matter.

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