EQUALISATION LEVY

TAXING CROSS-BORDER E-COMMERCE TRANSACTIONS

NOVEMBER 2020

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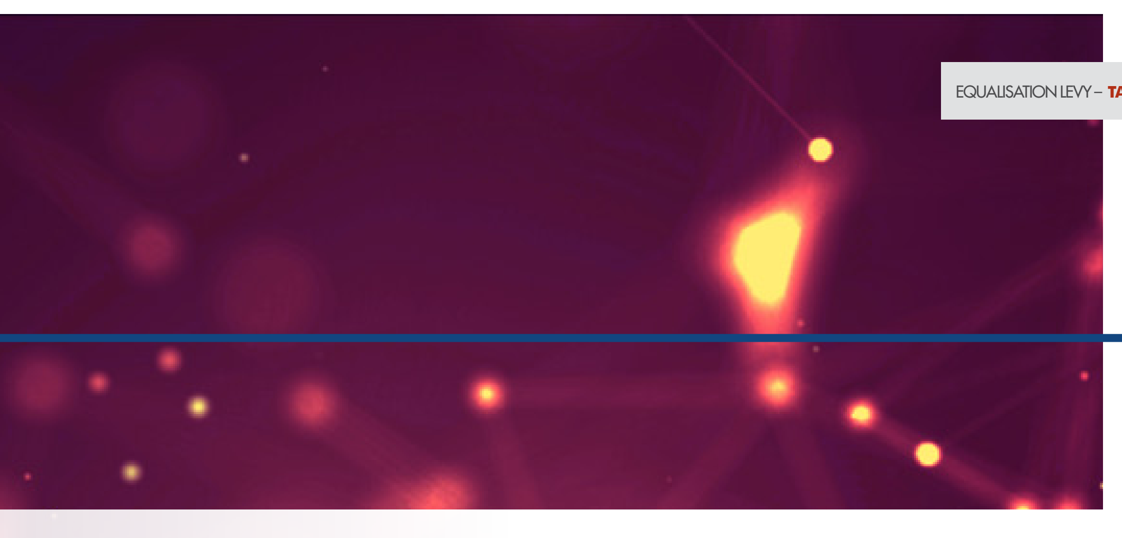

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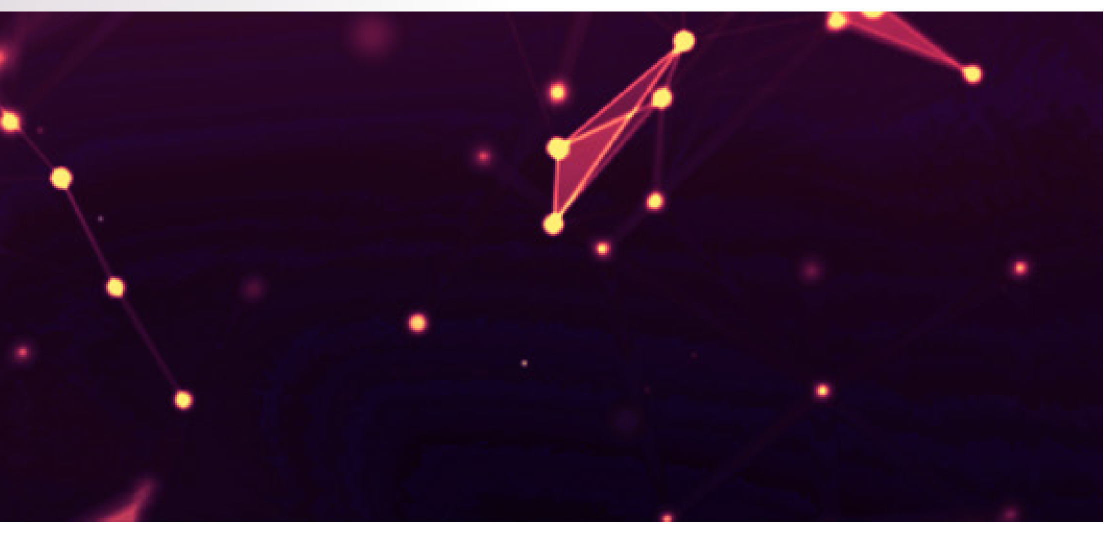


BACKGROUND

In today's world, with technology seeping into virtually every section of the economy, the 'digital economy' is becoming intertwined with the traditional economy such that making a clear delineation of the digital economy is getting harder and harder. Taxation is a very important aspect of any economy and is no different in a digital economy.

The changing business environment from the traditional brick and mortar system to the modern "digital system" has fundamentally changed the way businesses carry out their global activities. Enterprises can now carry out business across different jurisdictions without maintaining and/ or having a physical presence in a particular jurisdiction. For businesses making cross border supplies, digitalisation can radically alter the 'tax take' of a particular country.

It is not a secret anymore that the tax rules developed to cater to the traditional ways of doing business are not able to cope with current businesses and structures in the context of digital economy. Therefore, recognising the enormity of the situation and with a view to developing a unified approach for tackling the tax challenges posed by the digital economy, the Organisation for Economic Co-operation and Development ('OECD'), at the request of the G20 Finance Ministers, launched an Action Plan on Base Erosion and Profit Shifting ('BEPS') in July 2013. Action 1 of the BEPS Action Plan called for work to address the tax challenges of the digital economy. The objective of the plan was to develop a new set of standards for offering a global roadmap to governments to collect tax revenues, while simultaneously giving businesses the certainty needed to invest and grow. Although various measures[1] were considered in the preparation of BEPS' Action 1 final report[2] which was released in October 2015, none were recommended due to the expectation that other measures developed as part of the BEPS project will mitigate some of the tax challenges posed by the digital economy[3]. The BEPS project was followed by the OECD Secretariat's proposed "OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy" to comprehensively deal with the taxation of the digitalized economy . Earlier in October 2020, the OECD released two blueprints providing an update of the work done so far. Despite the effort over the least year, the progress in terms of building consensus is meagre. There is no agreement or plan on the minimum rate of tax to be proposed under Pillar Two. Also, there is no consensus on the manner in which profits are to be allocated under Pillar One. Whilst the proposed timeline for arriving at a consensus-based solution is pushed to mid-2021, several countries (including India) have announced interim measures in their domestic tax laws seeking to tax transactions arising on account of modern-day digital commerce. The fact that the United States has walked away from these efforts and is not inclined to implement the current proposals makes arriving at a consensus in the near future extremely difficult if not impossible.

India is amongst the frontrunners and has been strongly advocating source-based taxation with respect to the transactions undertaken in a digital economy. The Indian e-commerce market is expected to grow to $200 billion by 2027[4] and therefore the significance of India's fair share of digital tax cannot be over emphasized.

1. For instance, a new nexus in the form of a significant digital presence test, a withholding tax on certain kinds of digital transactions and equalisation levy
2. https://www.oecd.org/tax/beps/beps-actions/action1/
3. https://www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf
4. https://www.cnbctv18.com/retail/ecommerce-sector-to-touch-200-billion-by-2027-now-morgan-stanley-2331681.htm

Ecommerce: Highlights in India

- India e-commerce market expected to grow to USS 200 billion by 2027
- Currently there are 1-1.2 million transactions per day in e-commerce retailing
- Innumerable small and large e-commerce companies selling provisions and food items like Grofers, Big-basket, etc.
- Electronics is currently the largest segment in e-commerce in India with a share of 47 per cent and is expected to grow at a CAGR of 43 per cent by 2020
- The apparel segment has the second highest share of 31 per cent in the e-commerce retail industry
- With the increase in awareness about the benefits of online trading, there has been a significant rise in investment in e-commerce business. Hand in hand wish offline trading, many established businesses, e.g. Shoppers Stop or Lifestyle, have setup online transaction channels

As an early starter, India picked up on issues specific to the e-commerce industry way back in 2001 and set up a High Powered Committee ('HPC') constituted by the Central Board of Direct Taxes ('CBDT'). The HPC submitted its report on "Taxation and E-Commerce" in September 2001. The report considered and contemplated upon the need for introducing a separate tax regime for e-commerce transactions. However, based on the principle of 'neutrality', the HPC maintained that the existing laws back then were sufficient to tax e-commerce transactions and no separate regime for the taxation of e-commerce transactions was required.

More recently, considering the potential of the digital economy and to address the challenges in terms of taxation of digital transactions, in February 2016, a Report of the Committee (appointed by CBDT) on Taxation of E-Commerce was published. Several issues were analysed by the Committee in detail; for example, the current status of the Digital Economy and future growth, tax challenges from Digital Economy, issues related to value of data and user activity in multidimensional business models, options to address broader tax challenges of Digital Economy in the Indian context and its recommendations. The Committee in its Report in consonance with BEPS Action item 1 - *Addressing the Tax Challenges of the Digital Economy' considered three options to address broader tax challenges posed by the Digital Economy:*

- new nexus based on significant economic presence
- withholding tax on digital transactions
- equalisation levy

After analysing the options in detail, the Committee recommended that the only option that appeared to be feasible and could be resorted to, without violating the obligations under a Double Taxation Avoidance Agreement, was an 'Equalisation Levy' which was introduced vide Finance Act, 2016 (discussed in more detail later).

It would not be out of place to mention that, over the years, India has made significant changes to its domestic tax law in order to ensure that it receives its fair share of tax with respect to the digital economy. Some of the key changes include the amendment to the definition of *royalty* in 2012, the introduction of the *equalisation levy* in 2016 (restricted only to online advertisement services and provision of digital advertising space), introduction of Goods and Services Tax in 2017, the amendment to the definition of business connection to include a *'significant economic presence'* in 2018, and the introduction of *withholding tax* on domestic e-commerce transactions in 2020.

Recently, India expanded the scope of equalisation levy to include non-resident e-commerce operators within its ambit. **As per the expanded provisions, with effect from April 1, 2020, consideration received or receivable by a non-resident *e-commerce operator from e-commerce supply or services* is liable to equalisation levy at the rate of 2%.** The scope and impact of these provisions are discussed in greater detail in the ensuing paragraphs.

BRIEF OVERVIEW OF EQUALISATION LEVY PROVISIONS ON E-COMMERCE TRANSACTIONS

As aforementioned, any non-resident *e-commerce operator* who is engaged in *e-commerce supply or services* is liable to pay 2% of the amount of consideration as equalisation levy to the Indian exchequer.

For ease of reference, the key contours of the equalisation levy, as applicable to non-resident e-commerce operators, are tabulated below:

Applicability	Applicable on consideration received or receivable by non-resident e-commerce operator who is engaged in e-commerce supply or services made or provided or facilitated by it
Person responsible for paying equalisation levy in India	Non-resident e-commerce operator
Definition of *'e-commerce operator'*	E-commerce operator is defined to mean a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services, or both
Definition of e-commerce supply or services (i.e. specified services on which equalisation levy applies)	• Online sale of goods owned by the e-commerce operator; • Online provision of services provided by the e-commerce operator; • Online sale of goods or provision of services or both, facilitated by the e-commerce operator; • Any combination of above activities • Sale of advertisement which targets an Indian resident customer, or which targets a customer who accesses the advertisement through an IP address located in India • Sale of data collected from an Indian resident or from a person who uses an IP address located in India
Service recipient	• Any person resident in India; • Any person who buys goods or services (or both) using an IP address located in India; • Any non-resident in respect of offshore sale of advertisements which target Indian customers; • Any non-resident to whom data is sold which is collected from an Indian resident or from a person who uses an IP address located in India

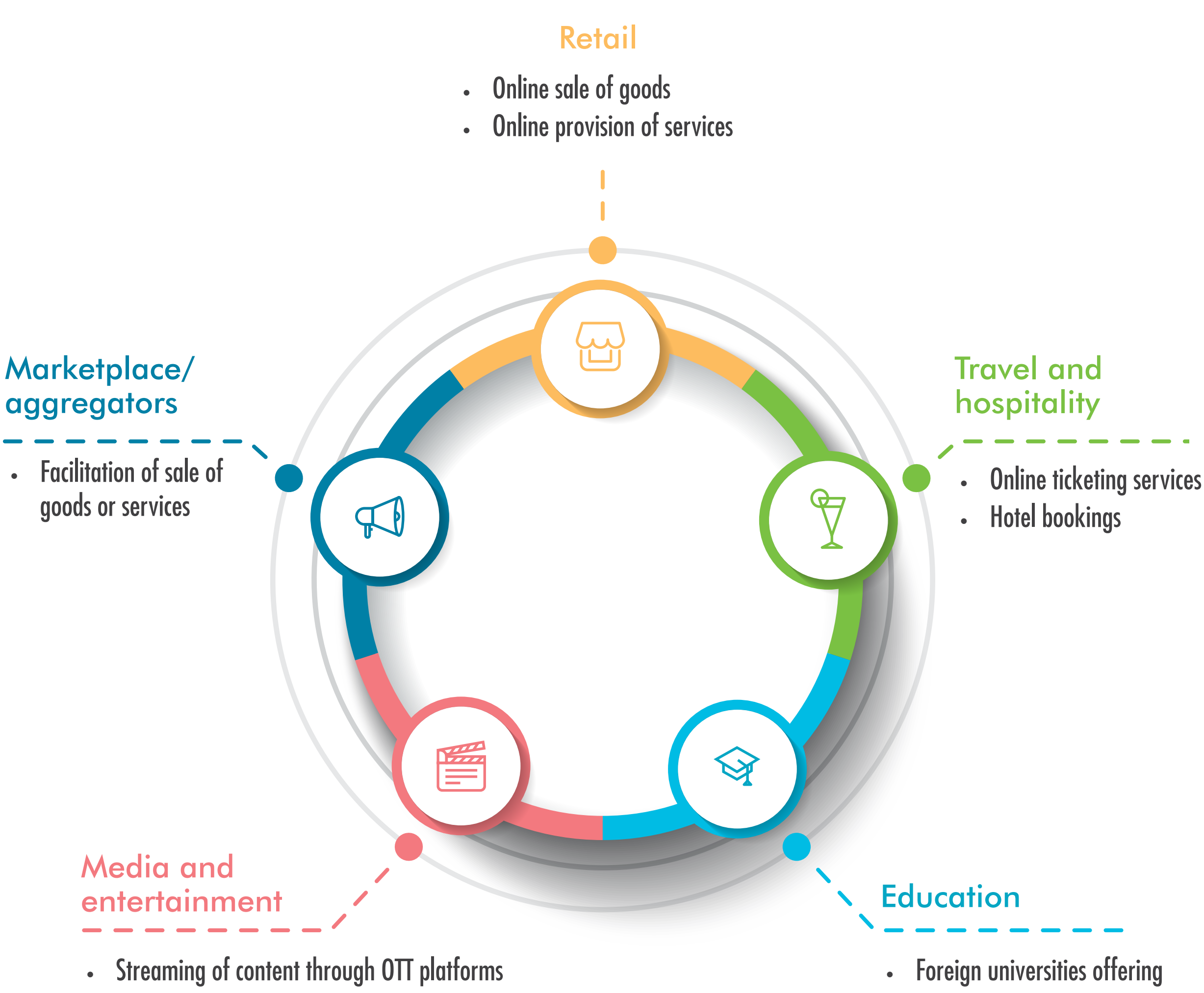
Rate of equalisation levy	2% of the consideration received / receivable by the e-commerce operator
Exemption from equalisation levy	Exemption is currently provided, inter-alia, in the following cases: • Non-resident e-commerce operators having a Permanent Establishment ('PE') in India and where the e-commerce transaction is effectively connected to such PE in India • Cases where the aggregate value of consideration for the specified transactions does not exceed INR 20 million (approx. USD 265,000) in a year.
Exemption from income-tax	As per the current provisions, transactions entered into on or after April 1, 2021 which are chargeable to equalisation levy are exempt from income-tax

As can be seen, the scope and coverage including the definitions of *e-commerce operator* and *e-commerce supply* or *services* are very wide and can have potentially far-reaching implications for transactions which may not be regarded to be in the nature of e-commerce as understood in common parlance.

INDUSTRY IMPACT

The practical challenges posed by the implementation of the equalisation levy have been exacerbated because there is currently very limited guidance available in the statute on a number of issues. Apart from the e-commerce retailers who predominantly transact through e-commerce business models, digitisation of business transactions is now common even amongst companies that traditionally operated through physical models. **The equalisation levy applies to an e-commerce operator which can potentially include not only e-commerce retailers/ marketplace operators but also businesses which operate under the brick and mortar model with a fair degree of digitisation.**

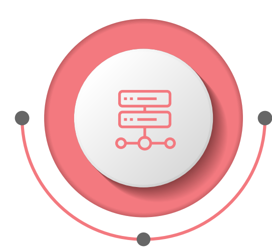
Several industries and business models could potentially be impacted under the equalisation levy provisions; some of which are illustrated below:



Other industries operating through a fair degree of digitisation can also get impacted under the equalisation levy provisions:

Communication

- Voice calls through internet
- Video conferencing



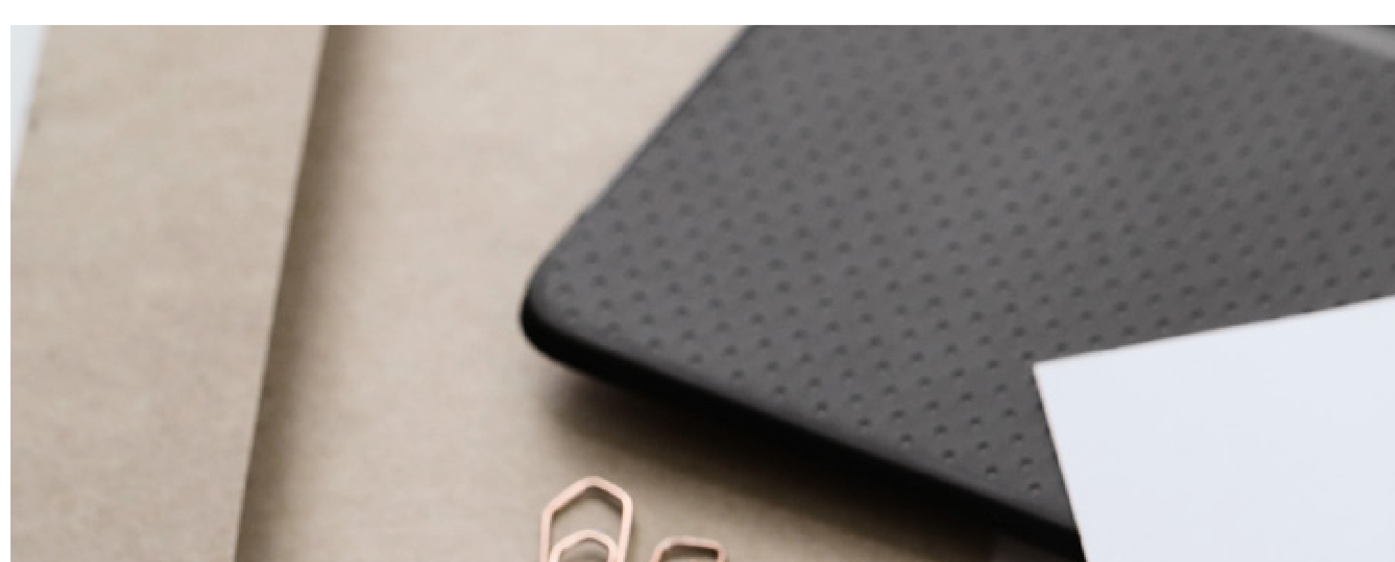
Information Technology

- Software sales
- Sale of customised software
- Provision of IT enabled services

Others

- Transactions through internal ERP platforms
- Front-end or back-end digitization
- Services / advice provided over an e-mail, telephone or any other form of electronic communication

As can be seen, the provisions of equalisation levy are broad enough to encompass digital transactions which can span across several industries; thereby making it extremely important for businesses to analyse and assess the impact of this levy on their business models. In the ensuing paragraphs, we have discussed few important facets such as compliance obligations, practical issues and challenges, potential business models which can get impacted and an overview of assessment and appeal mechanism provided for in the law.



WHAT ARE THE COMPLIANCE OBLIGATIONS?

The equalisation levy provisions cast an obligation on the non-resident e-commerce operator to pay equalisation levy within the following applicable due dates on a quarterly basis:

	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Date of ending of the quarter of the financial year	30th June	30th September	31st December	31st March
Due date for making payment	7th July	7th October	7th January	31st March

In order to enable the payment of equalisation levy, the CBDT has amended the existing payment challan (viz, ITNS 285) so as to permit the use of the same challan for payment of equalisation levy as applicable for non-resident e-commerce operators. It is important to note that the challan mandatorily requires the non-resident e-commerce operators to also quote their Permanent Account Number ('PAN') before making the payment. It may be noted that the mandate to obtain a PAN in India is procedural in nature despite there being no statutory requirement.

In addition to the quarterly payments, non-resident e-commerce operators are also required to file an Annual Statement on or before June 30th in respect of all such transactions conducted in the preceding financial year which runs from April to March. Failure to comply with the provisions (such as failure to deduct or pay the equalisation levy) attracts interest and penal consequences. Prosecution proceedings can also be invoked by Indian Revenue in certain circumstances.

PRACTICAL ISSUES AND CHALLENGES

Whom shall the equalisation levy apply to and who will be construed as an e-commerce operator?

What constitutes a digital or electronic facility/ platform? Is advice rendered through email or telephone covered?

Quantum of 'consideration' in context of marketplace models/aggregators to which the equalisation levy could apply

Applicability to inter-company transactions and reseller arrangements? No exemption provided

Applicability in cases where services are ordered or booked online but delivered offline? (say, hotel booking, etc.)

Mismatch between date of applicability of equalisation levy (April 1, 2020) and corresponding exemption from income-tax (April 1, 2021) - potential double whammy?

Will equalisation levy be creditable against taxes in overseas jurisdiction?

Interplay with indirect taxes

One-off transaction of a non-resident (while on a visit to India purchasing goods online (which are to be delivered at his residence overseas) using an India IP address

The aforementioned are just few of the issues which can arise while applying the provisions of equalisation levy; some of which are discussed below:

a. The present provisions do not provide sufficient guidance on applicability and procedural aspects of equalisation levy. Also, the constitutional validity of the levy and extra-territorial jurisdiction of the provisions could be debated aspects (discussed in detail below).

b. What constitutes a digital or electronic facility or platform is left open for interpretation. The Indian Revenue could potentially argue that an advice provided by a non-resident over an email or telephone would also constitute digital or electronic facility or platform which is used for online provision of services and therefore can fall within the ambit of e-commerce supply or services, hence liable for equalisation levy.

c. In a marketplace model, the way the provisions are worded seem to suggest that the equalisation

levy applies to the entire gross amount of consideration received by the e-commerce operator and not just on the commission or service fee retained by it. There could be arguments to suggest that levying equalisation levy on the gross amount could potentially result in absurd results which may not have been intended by the legislature. For instance, assuming a marketplace operator receives USD 1000 for online sale of goods; out of which USD 990 is remitted to the non-resident vendor (balance USD 10 retained being his commission) – in such a case, the quantum of equalisation levy, if levied on the gross amount (which works out to USD 20) would be more than the commission / income retained by marketplace operator which may not have been intended. Having said this, the law is unclear on this aspect and a conscious call would need to be taken by the taxpayers based on a literal interpretation of the provisions coupled with the intention of the legislature.

d. While the levy applies with effect from April 1, 2020, the corresponding exemption from income tax in the hands of non-resident recipient applies only from April 1, 2021. Given the same, there could be a potential double whammy in Financial Year 2020-21, where the same transaction is subjected to equalisation levy as well as taxable in India as royalty or fees for technical services.

e. Equalisation levy is introduced as a separate Chapter in the Finance Act and hence does not form part of the Income-tax Act, 1961 (though several provisions therefrom have been made applicable to equalisation levy). Thus, given that equalisation levy does not partake the character of income-tax, availability of credit of equalisation levy in the home country of the non-resident may not be possible. Whilst much will depend on the provisions of the domestic tax law of the foreign country in this regard, assuming the equalisation levy is not creditable, the same is likely to become a sunk cost in the hands of the non-resident.

f. The equalisation levy provisions do not provide any exemption for inter-company transactions. Thus, a back-to-back purchase order placed on an intranet / ERP software by a subsidiary or a distributor of a non-resident operator could potentially be subjected to equalisation levy. The provisions seem to focus more on how the contracts are entered into rather than how it is delivered to the end consumer. Based on the current provisions, transactions/ contracts entered into and concluded in physical form would not be covered but the same contracts entered into and concluded through a digital platform could potentially be covered in the ambit of equalisation levy.

g. There could be several cases where a service is booked online merely for the sake of convenience but is enjoyed offline. For instance, airline bookings or hotel bookings which are made over the internet. Whilst it can be argued that provisions of equalisation levy do not cover such transactions given that there is no online provision of service (as the service is actually availed/ enjoyed offline), the possibility of Revenue taking a contrary stand cannot be ruled out which can potentially result in a long drawn litigation.

h. Another example which could potentially attract this levy could be that of a non-resident (while on a visit to India) purchasing goods online (which are to be delivered at his residence overseas) using an Indian IP address. The way the provisions are worded even such one-off transactions may theoretically fall within the ambit of equalisation levy. It may very well be a daunting tax for the e-commerce operators to keep a tab on such transactions and thereby assess their consequential obligations.

The provisions do not specifically provide for separate window of Authority for Advance Ruling for equalisation levy transactions. Hence, access to Authority for Advance Ruling under Income-Tax Act, 1961 for equalisation levy could be denied.

Whilst the purported intent of introducing the equalisation levy is to bring the digital economy within the purview of income tax, the way it is being administered means that it acquires the character of an indirect tax levy. The import of goods is taxable under Customs law, whereas import of service is taxable under reverse charge basis under Goods and Services Tax. Overseas e-commerce supply would be subject to double taxation under equalisation levy as well as under custom / GST law. It poses further question regarding inclusion of equalisation levy for the customs valuation purposes.

Some other questions which arise from an indirect tax perspective are whether filing of equalisation returns by non-residents necessitates obtaining registration under goods and services tax and triggers compliances under such laws like collection of tax at source, etc.

There are agreements on tax treatment of the digital supply of goods within the framework of the World Customs Organisation; whether equalisation levy be seen violating those agreements is a question to be considered. The United States of America has launched probe against 'unfair digital service tax'.[5]

5. https://timesofindia.indiatimes.com/business/international-business/us-launches-probe-into-tax-on-amazon-netflix/articleshow/76186634.cms

ASSESSMENT AND APPEALS IN THE CONTEXT OF EQUALISATION LEVY

The scheme of the equalisation levy provisions (including the aspects pertaining to assessments and appeals) is tabulated below for ease of reference:

Relevant section of Finance Act, 2016	Provisions
163	Commencement and application
164	Definitions **[words not defined, shall have same meanings as assigned to them in the Act]**
165	Charge of equalisation levy on specified services
165A	Charge of equalisation levy on e-commerce supply of services
166	Collection and recovery of equalisation levy on specified services
166A	Collection and recovery of equalization levy on ecommerce supply or services
167, 168 and 169	Section 167 – furnishing of statement Section 168 – processing of statement (issuance of refund, intimation, etc.) Section 169 – rectification of mistake apparent from record
170 to 173	Applicability of interest on delayed payment and penalty for failure to deduct equalisation levy, failure to furnish statement, etc.
174 and 175	Appeal to CIT(A) and ITAT in respect of an order imposing penalty
176 and 177	Punishment and prosecution for false statement
178	Application of provisions of Income-tax Act, 1961 such as section 131, 133A, 156, Chapter XV and sections 220 to 227, etc.
179 and 180	Powers given to Central Government to make rules and remove difficulties

Some of the issues which could potentially arise in the context of assessments and appeals are listed below:

a. Recovery of equalisation levy if the non-resident fails to discharge his liability

- The provisions[6] pertaining to equalisation levy on online advertisements specifically provides that in case the resident payee fails to deduct the equalisation levy, then it is still liable to deposit the same with the Central Government, irrespective of non-deduction. However, the provisions[7] pertaining to equalisation levy on e-commerce transactions, do not grant recourse to the tax authorities to recover taxes in case a non-resident e-commerce operator fails to pay the levy within prescribed timelines. Does it mean that no recovery of equalisation levy is possible from the e-commerce operator if he doesn't discharge his liability?

- Also, there is no explicit power granted to the tax officer to pass an 'order' determining the levy and quantifying the amount of levy payable in a case where the non-resident e-commerce operator does not pay the same. The provisions of Section 168 (processing of statement) is applicable only when a statement is furnished by the e-commerce operator. The same has limited applicability and cannot be extended to determine the levy in absence of any statement furnished by e-commerce operator (including on the pretext that it is not subject to levy under equalisation levy provisions). Thus, any purported demand notice for recovery of equalisation levy which is issued without passing of an order may be said to be without jurisdiction[8] and non-est.

- However, the Revenue could argue that an order can be passed under the charging provision itself and there is no need to have a separate provision in this regard. Similarly, the Revenue could draw their powers of recovery under the same charging provision[9].

b. Time limit for collection and recovery of equalisation levy

- The provisions of the Act which provide for time limits for completion of assessment, recovery of taxes, etc. have not been imported in the equalisation levy provisions. Thus, assuming that an order levying the charge of equalisation levy can be passed, the law currently does not prescribe a specified time limit for the same.

- Whilst there could be two views on this subject, the preponderant judicial view in such cases is that the relevant action (i.e. passing of order) ought to be completed within a 'reasonable time'. The Courts in several cases have regarded 6 years to be a reasonable time period for completion of the relevant action in absence of limitation period in the law.

c. Appeal options available to the assessee

- The provisions[10] of equalisation levy provide that an assessee who is aggrieved by an order imposing 'penalty' passed by the Assessing Officer can appeal before the CIT(A) within the prescribed timelines. It is important to note that the right of appeal is provided only against a penalty order issued by the Assessing Officer and not against an order levying the primary/ base equalisation levy and corresponding interest, if any.

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6. Section 166(3) of Finance Act, 2016
7. Section 166A of Finance Act, 2016
8. Refer, illustratively, Rasiklal Amritlal Doshi v. Additional ITO [1961] 42 ITR 35 (Bom)
9. Section 166A of the Finance Act, 2016
10. Section 174 of the Finance Act, 2016

- Under the Act, an appeal[11] before the CIT(A) can lie against any order which is detrimental to the assessee. However, the said provision has not been imported in the equalisation levy provisions. Thus, it appears that there is no efficacious appellate remedy available to a taxpayer to appeal against the primary order which is passed assessing the equalisation levy in the hands of e-commerce operator.
- Accordingly, the only option available to a taxpayer would be to file a writ petition before the High Court challenging the primary/ base order which assesses the scope and quantum of equalisation levy.

d. Approaching the Authority for Advance Rulings ('AAR')

- There is no provision in the Finance Act, 2016 (read with Finance Act, 2020) which enables the non-resident to approach the AAR to decide on issues relating to applicability or otherwise of equalisation levy in a given fact pattern.
- However, reference in this regard may be made to section 10(50) of the Act which exempts the said income in the hands of the non-resident e-commerce operator.
- Given the same, a simplistic view could be to approach the AAR to determine whether the exemption under section 10(50) of the Act is available or not which would then be decided by the AAR basis the examination of equalisation levy provisions.
- On the contrary, one may argue that AAR does not have explicit powers to adjudicate on the issue as the scope of equalisation levy falls outside the purview of Act. As of now, there are no amendments made in the relevant provisions[12] which currently specifically include applicants in the context of excise duty, customs duty and service tax.
- Also, the Revenue could contend that section 10(50) of the Act just provides a consequential relief if equalisation levy is payable and thereby AAR cannot be approached for the same in absence of any enabling provisions in the statute.

e. Representative assessee

- If the non-resident e-commerce operator fails to discharge the equalisation levy, the same can be recovered from the Indian customer by treating him to be a representative assessee of the non-resident. However, recovery from the representative assessee should arguably be limited only in respect of the transactions which the Indian customer would have had with the e-commerce operator and not in respect of all the transactions which the e-commerce operator would have undertaken with the Indian customers. The Bombay High Court in *CIT v. Currimbhoy Ebrahim And Sons Ltd [1933] 35 BOMLR 914* have held that liability of a representative assessee can be enforced only with reference to the transactions affected by such representative assessee as the agent of non-resident and not on the basis of income/sales effected through other agencies employed by the non-resident. Similar proposition is also upheld by the Madras High Court in the case of *P. Subramaniam Chetty v. CIT [1962] 46 ITR 724.*

11. Section 246A(1)(a) of the Act
12. Section 245N – Definition of 'applicant' for purposes of AAR

f. **Assessee in default**

- Section 178 of Finance Act, 2016 imports, inter alia, the following provisions from the Act into the equalisation levy provisions:

a. Section 156 – Issue of notice of demand

b. Section 220 – Provisions pertaining to assessee in default

c. Section 221 – Penalty in case of assessee in default

d. Section 222 to section 227 – Tax recovery provisions in case of assessee in default

- Notwithstanding the validity of notice of demand in the absence of a valid order levying equalisation levy (as discussed in Point (a) above), if a notice of demand is issued for recovery of equalisation levy, the demand would need to be paid within 30 days of service of the notice.

- In case the demand is not paid within 30 days, the assessee shall be 'deemed to be in default' [S. 220(4)] and shall be liable to pay simple interest at 1% for every month or part of the month till the date of payment. Further, as per provisions of section 221 of the Act, a penalty may be levied by the Assessing Officer as he deems fit (which may not exceed the amount of equalisation levy that the non-resident e-commerce operator has failed to pay).

- Separately, sections 222-227 deal with rights and powers of the tax recovery officer in cases of assessee in default enabling such officers to recover taxes in cases of default. Accordingly, equalisation levy can be recovered (in cases of default) pursuant to sections 222-227 imported from the Act.

CONSTITUTIONAL VALIDITY OF EQUALISATION LEVY

Article 265 of the Constitution of India ('Constitution') states that "No tax shall be levied or collected except by the authority of law". Given the same, an argument could be advanced that charge of equalisation levy through the Finance Act in absence of any specific powers in the Constitution is in gross violation of Article 265 as the same is purported to be levied without the authority of law.

This is on account of the reasoning that given the scheme of relevant provisions of the Constitution[13], a plausible view appears to be that the imposition of equalisation levy is in contravention to the powers conferred on the Legislature [under Article 246A] and therefore is ultra vires the Constitution. In other words, one of the views is that the Parliament does not derive any powers to levy equalisation levy from any of the Articles of the Constitution given the manner in which they have been worded.

The CBDT Committee has justified the constitutionality of the equalisation levy on the ground that it is a levy on the gross amount of transactions or payments made for digital services. As per the Committee, the power to impose the levy arises from Entries 92C and 97 in the Union List of the Seventh Schedule to the Constitution. However, it is important to note that Entry 92C of the Union List has been omitted by the Constitution Amendment Act, 2016, hence no powers can be derived from this entry. Also, Entry 97, although residuary and to be read widely, is subject to matters not enumerated in List II and III of the Schedule VII of the Constitution. Another point to be noted is that Article 246A of the Constitution is notwithstanding the provisions of Article 246 and hence the levy of GST on supply of goods and services takes precedence over any other levy on such transaction, thus, resort to Entry 97 [residuary entry] may not be permissible.

13. Article 246(1), Article 246A and Article 248

INDIRECT TAX ISSUES

Whilst the purported intent of introducing the equalization levy is to bring the digital economy within the purview of income tax, the way it is being administered could mean that it acquires the character of an indirect tax levy.

There could be several areas of overlap with the indirect taxes, some of which may require detailed scrutiny. For example, any goods which are purchased online and shipped to India, will attract customs duty. Thus, the purchase of goods could be subject not only to customs duty but also to equalisation levy.

It could also have a bearing on questions of valuation for customs duty purposes – for example. whether or not equalisation levy is to be included as part of import value?

Some other questions which arise from an indirect tax perspective are whether filing of equalisation returns by non-residents necessitates obtaining registration under Goods and Services tax and triggers compliances under such laws in India.

There are agreements on tax treatment of the digital supply of goods within the framework of the World Customs Organisation; can equalisation levy be seen as violating those agreements is a question to be considered.

Is the government likely to introduce concepts and rules similar to place of supply rules to determine whether or not any transaction should be subject to equalisation levy?

CONCLUDING REMARKS

The OECD's BEPS Action 1 Final Report stated that any interim measures which may be implemented by any country ought to be in compliance with their international obligations, including tax treaties. However, given that equalisation levy is not a part of India's domestic tax law (it was introduced as a separate chapter in the Finance Act), non-residents may not be entitled to tax credit in their home jurisdiction.

Furthermore, the scope has been expanded significantly to cover a wide range of sale, service and facilitation transactions that are conducted online through a digital or electronic facility or platform. The provisions are drafted in a manner which targets not only highly digitalised business models, but also a number of routine transactions of a multinational group and their inter-group transactions.

Further, the threat of reprisals in form of trade barriers, sanctions, etc. from the United States of America cannot be ruled out. In the recent past, we have seen US proposing similar restrictions on France after the latter introduced digital tax; leading France to postpone the levy till the end of 2020.

From an operational point of view, there is a need to carefully segment the financials related to the in-scope transactions in order to comply with this new expansion of the levy.

Indeed, digitalisation has disrupted businesses by providing opportunities for modern businesses and evolving business models. The digital economy is swiftly becoming intertwined with the traditional economy, thus making it harder to clearly delineate the digital economy's true meaning. India has been at the forefront in terms of taxing the digital economy and the factors mentioned are becoming the new norm for taxing digital economies. Globally, several countries (such as the United Kingdom, Australia, Italy, Brazil, etc) have introduced similar tax proposals (such as digital service taxes) for the taxation of the digital economy. Also, it will be interesting to see how and when this levy is removed once a consensus is built up within the OECD on the taxation of digital transactions. Even if an agreement or consensus is reached, its implementation would be a bigger task given that multilateral instruments would have to be finalised, minimum rates have to be agreed upon and changes to domestic laws would need to be made to enable the implementation. In the meantime, the search for the holy grail of consensus will continue in an imperfect world with unilateral tax measures here to stay.

Whilst tax law continues to evolve, businesses will need to constantly reassess their operating models in order to assess impact, identify risks, explore planning opportunities, and meet their obligations.

HOW CAN DHRUVA ASSIST?

- **Evaluation and assistance in assessing the impact of equalisation levy**
    - Assist in determining transactions which fall under the ambit of the equalisation levy.
    - Advocacy on various aspects where the scope/applicability is not clear
    - Challenging the constitutional validity of the equalisation levy provisions before the Courts
- **Evaluating potential solutions / restructuring business models to mitigate the impact of equalisation levy**
    - Review / restructure existing business models and documentation
    - Evaluate potential opportunities to mitigate the incidence of the levy including setting up of legal entity in India
    - Cost-benefit analysis of paying equalisation levy in India versus conceding a Permanent Establishment in India including profit attribution thereon
- **Assistance in compliance**
    - Advise in putting requisite infrastructure / systems (ERPs, etc.) and other standard operating procedures in place for ascertaining the amount of equalisation levy payable in India
    - Where equalisation levy is applicable – obtain tax registrations, collate data and ensure levy is discharged to avoid interest/ penal consequences
    - Provide integrated and holistic solutions post considering levies under indirect tax and other laws e.g. OIDAR services

About Dhruva Advisors

Dhruva Advisors LLP is a tax and regulatory services firm, working with some of the largest multinational and Indian corporate groups. Its brings a unique blend of experience, having worked for the largest investors in India, advising on the largest transactions and on several of the largest litigation cases in the tax space. We also work closely with the Government on policy issues and with our clients on advocacy matters.

Key differentiators:

- Strategic approach to complex problems
- In-depth, specialised and robust advice
- Strong track record of designing and implementing pioneering solutions
- Trailblazers in tax controversy management
- Long history of involvement in policy reform
- Technical depth and quality

We believe in thinking out of the box, handholding our clients in implementing complex solutions and working towards achieving results. We have offices in Mumbai, Ahmedabad, Bengaluru, Delhi, Pune, Kolkata, Singapore and Dubai. We advise clients across multiple sectors including financial services, IT and IT-enabled services (ITES), real estate and infrastructure, telecommunications, oil and gas, pharmaceuticals, chemicals, consumer goods, power, as well as media and entertainment.

Dhruva Advisors is a member of the WTS Alliance, a global network of selected firms represented in more than 100 countries worldwide.

Our recognitions

- Dhruva Advisors has been consistently recognised as the “India Tax Firm of the Year” at the ITR Asia Tax Awards in 2017, 2018, 2019 and 2020.
- Dhruva Advisors has also been recognised as the “India Disputes and Litigation Firm of the Year” at the ITR Asia Tax Awards 2018 and 2020.
- W T S Dhruva Consultants has been recognised as the “Best Newcomer Firm of the Year” at the ITR European Tax Awards 2020.
- Dhruva Advisors has been recognised as the “Best Newcomer Firm of the Year” at the ITR Asia Tax Awards 2016.
- Dhruva Advisors has been consistently recognised as a Tier 1 Firm in India’s ‘General Corporate Tax’ and ‘Indirect Tax’ ranking tables as a part of ITR’s World Tax Guide. The firm is also listed as a Tier 1 firm for India’s ‘Transfer Pricing’ ranking table in ITR’s World Transfer Pricing guide.

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