



Budget 2017 May Bring More Tax Pain For Digital Transactions

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After taxing Indian advertising on foreign digital platforms and then Indian purchases from foreign e-commerce sites, the government may consider expanding the scope of these taxes, say tax experts.

8 of the 10 tax experts Bloomberg Quint spoke with expect an expansion of the Equalisation Levy that was introduced by the central government in the union budget 2016. The remaining two said that they won't be surprised if this happens.

What is Equalisation Levy?

Effective June 1, 2016, the government imposed a 6 percent tax on digital advertising where the service provider (platform) is a non-resident with no permanent establishment (PE) in India and the service recipient (advertiser) is an Indian resident or non-resident with a PE in India. A PE is tax language for a fixed place of business.

The levy is applicable if the transaction value exceeds Rs 1 lakh in a financial year.

The levy was recommended by an expert committee set up the finance ministry to look into the issue of taxation of digital economy.

Leading tax lawyer Nishith Desai, managing partner at Nishith Desai Associates told Bloomberg Quint that the committee's mandate was to find ways to bring to tax cross-border e-commerce transactions that otherwise escape traditional tax laws.

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The purpose of the levy is to tax income of such non-resident foreign companies which is otherwise not subject to tax under Income Tax Act, 1961. The Levy has been enacted in exercise of powers under Entry 92C of List I of Schedule VII of the Constitution – which was for taxation of services (this entry now stands deleted after the enactment of the 122nd Constitutional Amendment Bill pertaining to GST). While the levy seeks to tax income that would not otherwise have been taxable in India, the charging section and related provisions suggest that it is in fact an indirect tax, where the incidence of tax may be shifted to others in the value chain.

Nishith Desai, Managing Partner, Nishith Desai Associates

Equalisation Levy: Budget 2017 To Expand Applicability?

In its report, the expert committee had recommended that the levy should be imposed on other services as well, namely:

- Designing, creating, hosting or maintenance of website
- Digital space for website, advertising, e-mails, online computing, blogs, online content, online data or any other online facility
- Any provision, facility or service for uploading, storing or distribution of digital content
- Online collection or processing of data related to online users in India
- Any facility or service for online sale of goods or services or collecting online payments
- Development or maintenance of participative online networks
- Use or right to use or download online music, online movies, online games, online books or online software, without a right to make and distribute any copies thereof
- Online news, online search, online maps or global positioning system applications
- Online software applications accessed or downloaded through internet or telecommunication networks
- Online software computing facility of any kind for any purpose
- Reimbursement of expenses of a nature that are included in any of the above



The Amazon.com Inc. Amazon Web Services (AWS) Shield website is displayed on an Apple Inc. iPhone and iPad (Photographer: Andrew Harrer/Bloomberg)

Mukesh Butani, managing partner at BMR Legal said that he won't be surprised if Budget 2017 extends the levy to these services.

“ If you look at the expert committee report, you will see they have a broad category of services, and if you look at the explanatory memorandum in last year's budget, they had also said that to start with, we are imposing it on online advertising. If the government has to expand its tax base, this is the easiest thing it can do.

Mukesh Butani, Managing Partner, BMR Legal

Equalisation Levy + GST + Service Tax = Higher Cost For Indian Businesses?

Goods and Services Tax (GST)

The equalisation levy will not be subsumed under the Goods and Services Tax (GST), said Butani citing the recently released draft Model GST Law.

“ This increased cost will come on the Indian advertisers because the non-resident digital portal will say, look this is my price, now if tax is being levied, either I will add it to the price or you pay for it.

Mukesh Butani, Managing Partner, BMR Legal

Desai concurred with this view.

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If the levy is passed on to Indian businesses, it will be a cost in addition to GST which may be at the standard rate of 18 percent bringing the effective tax rate to approximately 25.5 percent. GST is also contemplated to have a higher tax rate of 28 percent for certain goods and services. When the scope of the levy is expanded and its rate is increased to the expected 8 percent, coupled with the 28 percent GST, the effective tax rate on all digital services imported by businesses, including start-ups, may be as high as 38.2 percent.

Nishith Desai, Managing Partner, Nishith Desai Associates

Service Tax

That high rate may be accompanied by possible double taxation. Because a [recent notification by the Central Board of Excise and Customs](#) (CBEC) brought many of the same services listed by the committee under the purview of indirect taxes.

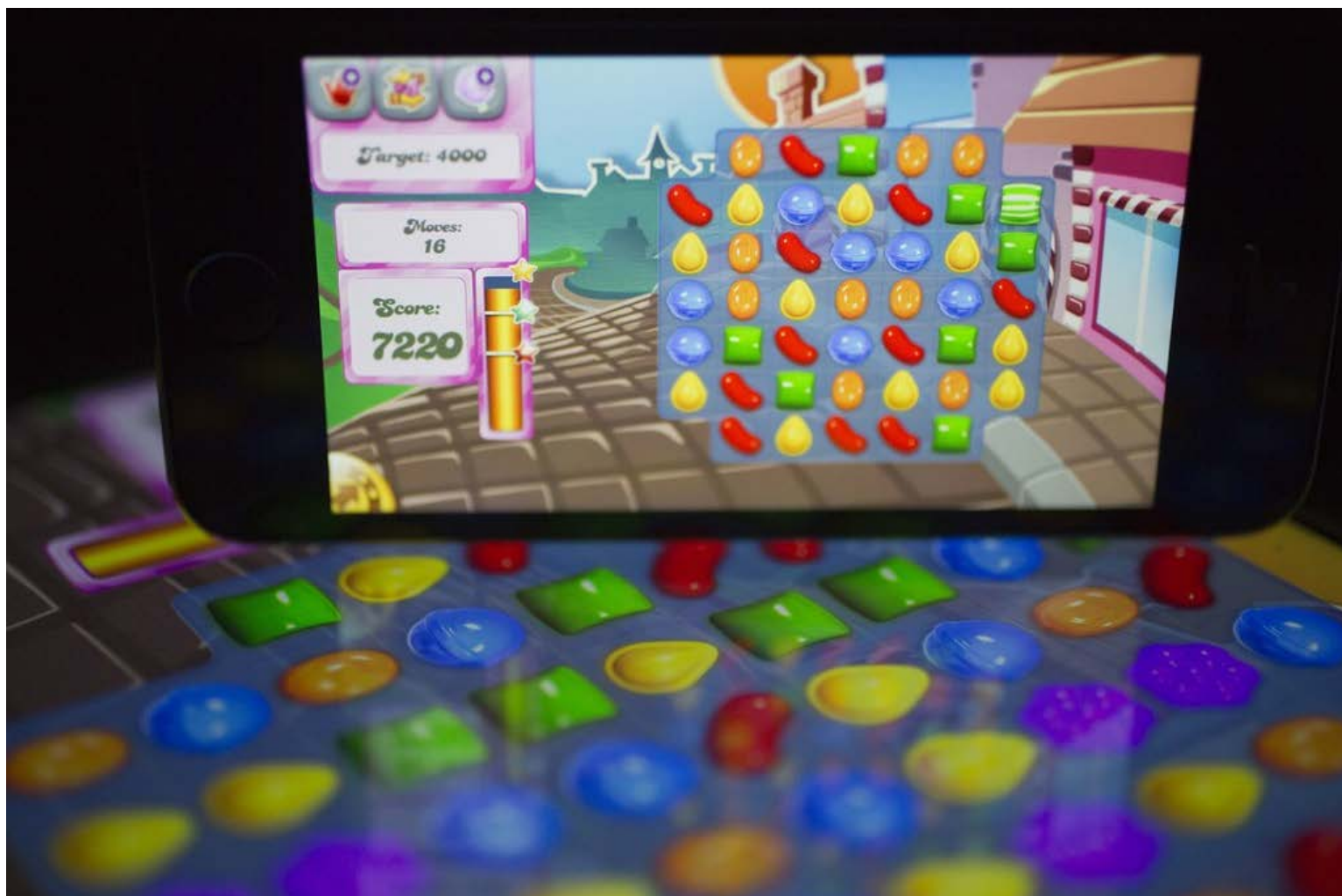
Starting December 1, 2016, a 15 percent service tax is applicable on all purchases from foreign websites including e-books, music, movies, internet advertising, providing cloud services, online games, software and other intangible products.

If the scope of the equalisation levy is expanded in Budget 2017, it may lead to the same transaction being taxed twice, Nishith Desai said.

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It is advisable for the government to avoid imposition of Equalisation Levy and just stick to indirect taxes in the form of a service tax. That should take care of revenue while not adversely affecting the consumer and business interest.

Nishith Desai, Managing Partner, Nishith Desai Associates



The “Candy Crush Saga” game is displayed on an Apple Inc. iPhone 5s and iPad Air (Photographer: Andrew Harrer/Bloomberg)

Increase In Business Costs

In April 2016, the Digital Economy Group, an informal group of leading U.S. and non-U.S. software and e-commerce companies, had written to finance minister Arun Jaitley opposing the equalisation levy. The letter, a copy of which is with Bloomberg Quint, stated that a 6 percent tax on gross revenue could result in an effective tax rate on net income that is far in excess of the Indian corporate income tax rate.

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A lower rate is appropriate since in most cases, the cost of the Proposed Levy will be passed on to the Indian payor, as is the case with other financial costs of importation, like customs duty

Digital Economy Group’s Letter To Arun Jaitley Dated April 24, 2016

Given this representation, it might be safe to assume that the burden of equalisation levy and any further service tax or GST could make online shopping a more expensive affair.

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