Nishith Desai Associates

LEGAL AND TAX COUNSELING WORLDWIDE

Research

# Technology and Tax Series: Issue 6

## **Online Education Sector** –
Business Model Case Study

**November 2020**

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**Online Education Sector – Business Model Case Study**

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# 1. Introduction

Online education is here to stay. If growing penetration of the internet across the globe and a lack of competent staff in various schools and colleges across developing nations wasn't enough to drive market growth, the recent pandemic induced suspension of international travel, visa delays and immigration bans are only increasing the adoption of e-learning options amongst universities and students.

According to Research and Markets, the global online education market is projected to witness a CAGR of 9.23% between 2020 and 20205, resulting in a total market size of USD 319.167 billion in 2025, increasing from US$187.877 billion in 2019.[1]

The growing adoption of cloud-based solutions and declining hosting costs, coupled with the generation of an increasing volume of educational content coming online, and the growing acceptance of the effectiveness and flexibility afforded by online learning have fueled its adoption.

Educational institutions around the globe have begun to adapt to this new reality, and have forayed into the online education space, offering online courses to students around the world, including in India.

In the simplest form of the online learning model, a foreign university provides courses wholly online i.e., course material is electronically shared with students and pre-recorded or live classes are conducted via video conference. Additional interaction between students and teachers is undertaken online, in a forum and chat group, and exams are conducted in closed rooms online.

This basic model may be supplemented, such as where a foreign university licenses its content to educations institutions in India, who use it to teach students locally, or with faculty visits, student exchanges, credit transfer programs or twinning / collaborations.

1.



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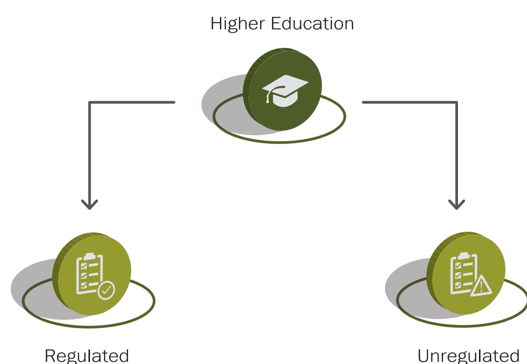
# 2. Education Laws in India

The higher education segment in India is typically divided in two broad segments:




## I. Regulated Sector

This segment includes:

- bachelor's/undergraduate degree courses
- master's/post-graduate degree courses
- diploma courses
- pre-doctoral/ doctoral programmes
- online education programmes (non-technical courses)

Under the University Grants Commission Act, 1956 (**"UGC Act"**), the right of conferring or granting degrees can be exercised only by a university or an institution deemed to be a university.[2] The UGC Act stipulates the criteria for an institution to qualify as a university or a deemed university, and contains provisions dealing with eligibility to, and the pre-requisites for, granting degrees.[3]

### A. Technical and Non-technical courses

The regulated sector can be further sub-categorized broadly into technical and non-technical education courses.

- *Technical courses:* 'Technical Education' has been defined in the All India Council for Technical Education Act, 1987 (**"AICTE Act"**) to mean "*programmes of education, research and training in engineering technology, architecture, town planning, management, pharmacy and applied arts and crafts and such other programme or areas as the Central Government may, in consultation with the AICTE, by notification in the Official Gazette, declare*".[4] The All India Council for Technical Education (**"AICTE"**) oversees technical education and the functioning of technical institutions within the country. A 'technical Institution', under the AICTE Act, refers to the institutions, other than universities, conducting courses or programmes in the field of Technical Education. Courses in technical programmes cannot be offered without prior permission of the AICTE.[5]
- *Non-technical courses:* Non-technical courses refers to courses other than technical courses. To the extent they lead to the award of a degree, diploma, etc., they are regulated by the UGC.

### B. Professional Councils

Statutory professional councils regulate certain professional courses in the country. They are responsible inter alia for recognition of courses, promotion of professional institutions and providing grants for programmes. The Medical Council of India, for instance, is empowered to prescribe minimum standards for medical education required for grant of recognized medical qualifications by universities or medical institutions in India. It is also responsible

2. Section 22 of the UGC Act
3. In 2018, the Ministry of Human Resource Development published the Higher Education Commission of India (HECI) Bill, 2018, to repeal the University Grants Commission (UGC) Act, 1956 inviting public comments. However, the Bill is yet to become law.
4. Section 2(g) of the AICTE Act
5. Section 2(h) of the AICTE Act.



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to give its recommendations to the Government for establishing new medical colleges. Similarly, Bar Council of India, Dental Council of India, Indian Nursing Council, etc., are some of the notable councils. These councils have been empowered to prescribe standards and formulate regulations with respect to their field of involvement.

## C. Distance Education

In addition to the in-person education offered through colleges and universities, the distance education sector also forms part of the formal education system in India. It was initially governed by the Distance Education Council (**"DEC"**) which was set up under the Indira Gandhi National Open University Act, 1985. However, in May 2013, the DEC was dissolved.[6] Subsequently, in May 2013, the Government, issued a notification transferring DEC's responsibilities to the UGC.[7] Vide notification dated June 17, 2013, the UGC adopted the Guidelines of the DEC on Minimum Requirements for recognition of Open and Distance Learning (**"ODL"**) institutions, till such time as it frames regulation for ODL institutions.[8] On June 23, 2017, the UGC notified the University Grants Commission (Open and Distance Learning) Regulations, 2017 (**"ODL Regulation 2017"**)[9], setting out the minimum standard of instruction required for granting degrees (at the undergraduate and post-graduate levels) through the ODL mode.[10][11] These regulations are only applicable to all degree programmes (other than programmes in technical courses, medical, dental, pharmacy and any programme which is not permitted to be offered in distance mode by the relevant regulatory body) offered by universities and institutions deemed to be universities.[12] The key conditions under the regulations include the following:

- higher educational institutions already offering[13] or intending to offer[14] programmes in ODL mode from the academic session 2018-19 and onwards have to seek approval for recognition from the UGC;
- in order to be recognized the higher educational institutions should have valid accreditation from National Assessment and Accreditation Council (**"NAAC"**) and complete five years of existence[15];
- permission to offer distance education programme in ODL mode will be granted course wise and prior permission is required with respect to each course to be offered in ODL mode;
- higher education institution can offer up to 20% of the total course being offered in each programme in a semester through online learning courses / massive open online course[16];
- the higher educational institution other than an Open University[17] is offering similar programme in the conventional mode of classroom teaching[18];
- higher educational institutions have to establish a centre for internal quality assurance exclusively for programmes to be offered in ODL mode within 1 year from these regulations come into force[19];
- higher educational institutes can fix the fee structure for its courses but the same has to be declared in its prospectus for admission and on the website.[20]

6. See https://www.ugc.ac.in/deb/MHRDLetter-16thMay2013.pdf (last visited on October 8, 2020).
7. *Ibid*
8. See https://www.ugc.ac.in/deb/notices/UGCNotification17thJune2013.pdf (last visited on October 8, 2020).
9. Available at https://www.ugc.ac.in/oldpdf/regulations/ distance%20 education%20regulations.pdf (last visited on October 8, 2020).
10. Regulation 2(m) of the ODL Regulation 2017, defines "Open and Distance Learning" mode as a mode of providing flexible learning opportunities by overcoming separation of teacher and learner using a variety of media, including print, electronic, online and occasional interactive face-to-face meetings with the presence of an Higher Educational Institution or Learner Support Services to deliver teaching-learning experiences, including practical or work experiences
11. Regulation 1(1) of the ODL Regulation 2017.
12. Regulation 1(3) of the ODL Regulation 2017
13. Regulation 3(1) of the ODL Regulation 2017.
14. Regulation 3(2) of the ODL Regulation 2017
15. Regulation 3(1)(viii) of the ODL Regulation 2017.
16. Regulation 3(1)(viii) of the ODL Regulation 2017
17. Regulation 2(n) of the ODL Regulation 2017 defines "Open University" as a University which imparts education through distance education or Open and Distance Learning mode using variety of Information and Communication Technology educational aids i.e. online education in the form of Open Educational Resources (OERs) or Massive Open Online Courses (MOOCs)etc.
18. Regulation 3 (1)(iii) of the ODL Regulation 2017
19. Regulation 8(1)(i) of the ODL Regulation 2017
20. Regulation 12(1)(a)(i) of the ODL Regulation 2017.



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Further, with respect to deemed universities, the ODL Regulation 2017 specifically states[21] that:

- an institute declared to be deemed to be university after May 26, 2010 is not allowed to conduct courses in the distance education mode;
- institute declared to be deemed to be university before May 26, 2010 is not allowed to conduct courses in distance mode from any of its off campus centres or off-shore campuses approved after 26th May, 2010;
- that a deemed to be university can operate only through its headquarters or from Government approved off-campus or off-shore campuses;
- approval for new courses and extension of approval of the courses already run by the deemed to be university under the distance mode would be granted by the UGC, subject to fulfillment of conditions laid down by the UGC.

## D.Online Education Programs

Various Massive Open Online Course (**"MOOC"**) initiatives have been started by universities and colleges, and by the Indian government as well. Some examples of MOOCs are:

- Birla Institute of Technology and Science (BITS) Pilani, IIT Bombay and IIM Bangalore have partnered with the MIT & Harvard's MOOC platform edX to offer MOOCs to their on-campus and off-campus students.
- As a government initiative, the Union Human Resource Development (**"HRD"**) Ministry had initiated its MOOC platform called SWAYAM, where professors of centrally funded institutions will offer online courses free of cost. SWAYAM was launched in 2016, with the goal to introduce over 350 new online degree, diploma, certification and other course such as MOOCs on this platform. The course offered through SWAYAM are regulated under the UGC (Credit Framework for Online Learning Courses through SWAYAM) Regulations, 2016 (**"SWAYAM Regulations"**).[22] The Swayam Regulations provide for credit mobility for credits earned through online learning courses through SWAYAM in the credit programme of educational institutions.[23] The union cabinet also approved the signing of a declaration of intent with the U.S. Department of State for US universities to offer post-graduate academic programmes with certification on the SWAYAM platform.[24] Further, technical education can also be provided through SWAYAM platform as per the AICTE Regulation (Credit Framework for online learning course through SWAYAM) Regulation, 2016.[25]

In 2018, the UGC recognized the validity of degrees, diplomas and certificates offered through online modes of education under its University Grants Commission (Online Courses or Programmes) Regulations, 2018 (**"Online Education Regulations"**).[26]

The Online Education Regulations apply to a University[27] and an Institution deemed to be a University.[28] As per these regulations, only nontechnical courses can be offered online. Further, any course or programme which requires a practical

21. Annexure IV, Part B of the ODL Regulation 2017.

22. See http://www.ugc.ac.in/pdfnews/0272836_moocs.pdf (last visited on October 9, 2020).
23. Regulation 6, SWAYAM Regulations, available at https://www.ugc.ac.in/pdfnews/4064990_UGC-(Credit-Framework-forOnline-Learning-Courses-through-SWAYAM)-Regulation,-2016. pdf (last visited on October 9, 2020).
24. See http://pib.nic.in/newsite/PrintRelease.aspx?relid=109984 (last visited on October 9, 2020).
25. See http://www.old.aicte-india.org/downloads/171415. pdf#toolbar=0 (last visited on October 9, 2020); See http://nptel. ac.in/LocalChapter/swayam/AICTE%20Credit%20Notification. pdf (last visited on January 25, 2019).
26. Regulation 2(q) of the Online Education Regulation defines 'Online Course or Programme' to mean the Course or Programme of studies which are delivered through online mode leading to award of a Certificate or Diploma or Degree by an approved Higher Educational Institution and recognised under these Regulations. Available at https://www.ugc.ac.in/pdfnews/7553683_OnlineCourses-or-ProgrammesRegulations_2018.pdf
27. Section 2(f) of the UGC Act, 1956 defines "University" to mean a University established or incorporated by or under a Central Act, a Provincial Act or a State Act, and includes any such institution as may, in consultation with the University concerned, be recognised by the Commission in accordance with the regulations made in this behalf under the UGC Act
28. Section 3 explains "Institutions Deemed to be Universities" to mean The Central Government may, on the advice of the Commission, declare by notification in the Official Gazette, that any institution for higher education, other than a University, shall be deemed to be a University for the purposes of the UGC Act, and on such a declaration being made, all the provisions of this Act shall apply to such institution as if it were a University within the meaning of clause (f) of section 2.



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or a laboratory course(s) as a part of its curriculum can also not be offered through the online mode.

For the purpose of obtaining recognition to offer online education, Higher Education Institutes[29] (**"HEI"**) should meet the criteria laid down under the Online Education Regulations.[30]

The HEIs which are given recognition may operate Online Course or Programme from the next academic session. Some of the key conditions under the Online Education Regulations for offering online education are as follows:

1. The Online Course or Programme should be delivered through the SWAYAM portal or any other learning platform after the same is verified and approved by the expert committee of the UGC.

2. The online learning should have a four quadrant 'approach', namely, tutorials, e-content, web resources and self-assessment.

3. Apart from the actual course or programme delivery, other components such as counseling process, online application processing and fee payment should also be provided through online mode.

4. The duration of the Online Course or Programme should be as below:

   a. For a Certification: The Online Course or Programme should be of minimum of six months' duration and would have a minimum twenty credits.

   b. For a Diploma: Online Course or Programme should be of minimum of one year duration and would have minimum forty credits.

   c. For a degree: The Online Course or Programme should for the same duration and for the same credits as specified by the UGC under Choice Based Credit System (CBCS).

   However, the maximum duration for completing the Online Course or Programme should be double the minimum duration of the course or programme or as laid down by the UGC from time to time.

5. The HEI can provide one or more academic sessions each year which begin either in July/ August or January/February each year.

The Online Education Regulations currently do not extend to non-technical courses or degrees / diplomas offered by institutes outside India.

## II. Unregulated Sector

The unregulated sector primarily comprises of:

- certification courses not leading to the award of a degree or diploma § vocational training;
- tutoring services / coaching classes

In the recent past, skill based courses, certification programmes, vocational training and tutoring have garnered interest amongst education service providers. This is because a significant percentage of students graduating from universities and colleges are not readily employable because of lack of skills. This results in students enrolling in coaching classes / vocational training classes and seeking certification courses to increase their scope of employability. Due to the growth of the unregulated education sector and the heavy enrollments, there has been a move to regulate some segments of this sector as well. For instance, tutoring classes are regulated in some states in India now.[31] The regulations however are not compliance heavy, but seek registrations of such institutes so that the government is aware of the number of such institutes that operate in a particular area. Further, there are certain do's and don't's prescribed under the regulations which are

29. Regulation 2(k) of the Online Education Regulations defines 'Higher Educational Institution' to mean a university covered under clause (f) of section 2 and an institution deemed to be a university under section 3 of the Act, which is imparting higher education or research therein by means of conducting regular classes or through Open and Distance Learning systems or through online education system

30. Regulation 4 of the Online Education Regulation. Some of the criterion are existence of at least 5 years; should be accredited to the National Assessment and Accreditation Council and have a score of at least 3.26 on 4; demonstration of capability for developing and producing Online Courses or Programmes; having access to SWAYAM.

31. In Goa, private coaching classes and tuitions are regulated under the Goa Coaching Classes (Regulation) Act, 2001. Maharashtra has taken steps towards regulation of coaching classes however, no law has been enacted in this regard till date. See https://timesofindia.indiatimes.com/home/education/ news/maharashtra-to-revise-draft-of-private-coaching-classesregulatory-bill/articleshow/66703586.cms



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aimed to encourage regular schools rather than focus on tuitions classes. Similarly, at times, AICTE regulates extends its jurisdiction to regulation certification courses as well with an aim to protect student interests.

# III. The operation of FEIs in the Regulated Sector

Currently, FEIs are not permitted to establish an independent campus in India for the purpose of degree programmes. As a step towards liberalization of the heavily regulated higher education sector, the government on September 10, 2013 had issued a press release[32] informing various stake-holders about its proposal to allow foreign universities to set up campuses in India as not-for-profit companies (without having to collaborate with domestic educational institutions). However, no action has been taken on this front as of now. Further, a bill titled 'The Foreign Educational Institutions (Regulations of Entry and Operations) Bill, 2010'[33] was introduced in the parliament to regulate entry and operation of FEIs in India to impart higher education. However, the bill lapsed in 2014. In 2016, Niti Aayog have submitted a report to the Prime Minister and the Human Resource Development Minister, calling for the invitation of foreign universities to set up campuses in India and their operations should be controlled by law, since the same will help meet the demand for higher education in the country, increase competition and subsequently improve standards of higher education.[34] However, currently, the only way FEIs can enter the regulated sector is by way of collaboration with Indian educational institutes.

Both the AICTE and the UGC have their own set of regulations to govern the operation of FEIs.

32. See http://pib.nic.in/newsite/PrintRelease.aspx?relid=99225 (last visited on October 9, 2020).
33. See http://pib.nic.in/newsite/PrintRelease.aspx?relid=70050 (last visited on October 9, 2020).
34. See http://indiatoday.intoday.in/education/story/foreign-university-campuses-in-india/1/644180.html (last visited on October 9, 2020)

## A. AICTE Regulations[35]

The AICTE Regulation for Entry and Operation of Foreign Universities/Institutions Imparting Technical Education in India, 2005 (**"AICTE Regulations"**) facilitate the entry of FEIs in India by way of collaboration with Indian educational universities/institutions for imparting technical education leading to the award of diplomas, degrees, etc. This is subject to satisfaction of prescribed conditions and obtaining registration from the AICTE. The registration is granted for a period specified at the time of registration. Key conditions under the regulations include the following:

- the FEI has to be approved and accredited with higher grades in its home country;[36]
- the Indian educational institution has to be an AICTE approved institution and registered as a not-for-profit entity;[37]
- the degree / diploma granted to students has to be recognized in the FEI home country;[38]
- the fee, quantum of student intake, admissions, entry-qualifications and conduct of courses should be as prescribed by AICTE form time to time;[39]
- the FEI has to submit a detailed project giving details regarding infrastructure facilities, facilities available for instruction, faculty, admission procedure, prescribed fee, courses, curricula, availability of requisite funds for operation for a minimum period of three years and other terms and conditions of collaboration, if any;[40]
- the FEI is responsible for obtaining accreditation from the National Board of Accreditation after two batches have passed out;[41]

35. See AICTE Regulation for Entry and Operation of Foreign Universities/Institutions Imparting Technical Education in India, 2005, available at http://www.ispepune.org.in/PDF%20ISSUE/2007/JISPE307/2009-12-23/009.PDF (last visited on October 12, 2020).
36. Conditions for Registration, Regulation 2 of the AICTE Regulations
37. Conditions for Registration, Regulation 1 of the AICTE Regulations.
38. Conditions for Registration, Regulation 3 of the AICTE Regulations.
39. Conditions for Registration, Regulation 9 of the AICTE Regulations.
40. Procedure for Registration, Regulation 2 of the AICTE Regulations.
41. Conditions for Registrations, Regulation 12 of the AICTE Regulations.



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- a performance guarantee fee is required to be paid at the time of seeking registration;[42]
- franchise arrangements are not permitted.[43]

Further, as per the AICTE (Grant of Approvals for Technical Institutions) Regulations, 2016, prior approval of AICTE is required for collaboration and twinning programme between Indian and foreign universities/institutions in the field of technical education, research and training.[44]

## B.UGC Regulations 2016[45]

The UGC (Promotion and Maintenance of Standards of Academic Collaborations between India and Foreign Educational Institutions) Regulations, 2016 (**"UGC Regulations 2016"**) allows FEIs to collaborate with Indian educational institutions (other than technical institutions) upon obtaining approval from the UGC.[46][47] Approval is granted for two cycles of the minimum duration of the degree programmes covered under the collaboration.[48] These regulations also cover twinning programmes whereby students may complete their course by part study in India and part study in the main campus of the FEI.[49] UGC Regulation 2016 have introduced an e-application process for seeking approvals for collaboration/ twinning programmes.[50] The key conditions under this regulations include the following:

- The FEI has to be accredited in its home country with the highest grade or its equivalent by an Assessment and Accreditation Agency (**"AAA"**) in its homeland.[51] The FEI also has to abide by other conditions prescribed by the Government statutory bodies;[52] the Indian educational institute has to be accredited with grade not less than A or its equivalent by any AAA authorized by the UGC;[53]
- the written memorandum of understanding to be entered into between the FEI and Indian educational institute after obtaining approval of the UGC;[54]
- the FEI has to submit details about the infrastructure facilities, facilities available for instruction, faculty, specified fee, courses, curricula, availability of requisite funds for operation for a minimum period of three years and other terms and conditions of collaboration,[55] if any;
- franchise arrangements are not permitted.[56]

*Autonomous colleges and institutes:* Autonomous colleges and institutes enjoy autonomy over their day-to-day functioning. In 2018, the government has taken measures to regulate autonomous colleges by introducing the Autonomous Colleges Regulations and the Grant of Graded Autonomy Regulations. The Grant of Graded Autonomy Regulations aim to provide autonomy to the HEIs based on quality benchmarks and categorizes universities into three categories – Category I, II and III based on benchmarks mentioned therein.[57] Category I & II Universities can hire foreign faculty, without approval of the Commission, who have taught at an institution appearing in top five hundred of any of the world renowned ranking frameworks. Further, Category I universities may engage in academic collaborations with foreign educational institutions without approval from the UGC.[58] The regulations are an example of the government's attempt

42. Procedure for Registrations, Regulation 5(b) of the AICTE Regulations
43. Conditions for Registration, Regulation 1 of the AICTE Regulations.
44. Regulation 4.1 of AICTE (Grant of Approvals for Technical Institutions) Regulations, 2016, available at http://www.old.aicteindia.org/downloads/reg_2016.pdf (last visited on October 12, 2020).
45. The UGC (Promotion and Maintenance of Standards of Academic Collaborations between India and Foreign Educational Institutions) Regulations, 2016, available at https:// www.ugc.ac.in/pdfnews/5003871_Foreign-CollaborationRegulations-2016-(1).pdf (last visited on October 12, 2020)
46. Regulation 1(2)(a) of the UGC Regulations 2016, available at https://www.ugc.ac.in/pdfnews/5003871_Foreign-CollaborationRegulations-2016-(1).pdf (last visited on October 12, 2020).
47. In 2017, the UGC issues draft University Grants Commission (Promotion and Maintenance of Standards of Academic Collaboration between Indian and Foreign Educational Institutions) Regulations, 2017. However, no further action has been taken on the these and the 2016 regulations remain in effect
48. Regulation 5(f) of the UGC Regulation 2016.
49. Regulation 2(m) of the UGC Regulation 2016
50. Regulation 5(b) of the UGC Regulation 2016.
51. Regulation 3(1)(a) of the UGC Regulations 2016.
52. Regulations 3(1)(c) of the UGC Regulations 2016.
53. Regulation 3(2)(a) of the UGC Regulations 2016.
54. Regulation 4 of the UGC Regulation 2016.
55. Regulation 5(b) of the UGC Regulations 2016.
56. Regulation 6(a) of the UGC Regulations 2016.
57. Government of India Press Release on Grant of Graded Autonomy Regulations available at http://pib.nic.in/newsite/PrintRelease.aspx?relid=180895, last accessed on October 12, 2020).
58. Regulation 4.0, Grant of Graded Autonomy Regulations



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to encourage foreign investment in the higher education space in India.

## C. Collaborations with Institutions of Eminence

To establish the Institutions of Eminence,[59] in 2017, the UGC notified regulations and guidelines pertaining to the same namely, UGC (Institutions of Eminence Deemed to be Universities) Regulations, 2017[60] (**"Institution of Eminence Regulations, 2017"**) for private institutions and UGC (Declaration of Government Educational Institutions as Institutions of Eminence) Guidelines, 2017[61] (**"Institution of Eminence Guidelines, 2017"**) for public institutions. Some of the key incentives under these regulations and guidelines are:

- exemption from Government approval for academic collaboration with foreign higher educational institutions ranked in top 500 in global ranking;[62]
- flexibility in admission of foreign student's subject to maximum of 30% of the strength of domestic students;[63]
- freedom to fix fees for both foreign[64] and domestic students;[65]
- freedom to offer courses within a programme, as well as to offer degrees in newer areas after approval from its governing council;[66]
- flexibility to determine course structure in terms of number of credit hours and years to take a degree[67] and in fixing curriculum and syllabus, with no UGC mandated curriculum structure;[68]
- freedom to offer online courses subject to condition that not more than 20% of the programme should be in online mode. However, certificate courses can be provided entirely through online mode;[69]
- freedom to hire foreign faculty on tenure or contract basis.[70]

Collaboration has therefore become easier for FEIs ranked in the top 500 global rankings.

59. Regulation 4.0, Grant of Graded Autonomy Regulations
60. See https://www.ugc.ac.in/pdfnews/5403862_Gazette-Institutionsof-Eminence-Deemed-to-be-Universities.pdf (last visited on October 12, 2020)
61. See https://www.ugc.ac.in/pdfnews/2170800_Guidelines-forEducational-Institutions-as-Institutions-of-Eminence-2017.pdf (last visited on October 12, 2020).
62. Clause 6.1 (j) of the Institution of Eminence Guidelines, 2017.
63. Clause 6.1 (a) of the Institution of Eminence Guidelines, 2017.
64. Clause 6.1(b) of the Institution of Eminence Guidelines, 2017.
65. Clause 6.1 (c) of the Institution of Eminence Guidelines, 2017
66. Clause 6.1 (d) of the Institution of Eminence Guidelines, 2017
67. Clause 6.1 (e) of the Institution of Eminence Guidelines, 2017
68. Clause 6.1 (f) of the Institution of Eminence Guidelines, 2017.
69. Clause 6.1 (g) of the Institution of Eminence Guidelines, 2017.
70. Clause 6.1 (m) of the Institution of Eminence Guidelines, 2017



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# 3. Legal Provisions

## I. The Income Tax Act, 1961

The taxation of income in India is governed by the provisions of the Income-tax Act, 1961 (**"ITA"**) which prescribes separate rules for the taxation of residents and non-residents. Under Section 4 read with Section 5 of the ITA, residents are taxable on their worldwide income, while non-residents are taxable only on India source income i.e., income that accrues or arises, or is deemed to accrue or arise, in India or is received or deemed to be received in India.

### A. Significant Economic Presence

Section 9(1) of the ITA elaborates on the scope of the phrase 'income deemed to accrue or arise in India'. Sub-section (i) of Section 9(1) provides that 'all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India', shall be deemed to accrue or arise in India. By virtue of section 5(2), as aforesaid, such income of non-resident is taxable in India.

Explanation 2A to section 9(1)(i) provides that a 'significant economic presence' (**"SEP"**) of a non-resident in India shall constitute a business connection in India. Explanation 2A[71] defines a SEP as:

- Transactions in respect of any goods, services or property carried out by a nonresident with any person in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year such amount as may be prescribed (no amount has as yet been prescribed).
- Any systematic and continuous soliciting of business activities or engaging in interaction with such number of users, as may be prescribed, in India through digital means (no such number has as yet been prescribed).

In case a non-resident has a SEP in India, the income of the non-resident attributable to the SEP will be taxable in India.

- The SEP provisions come into effect from April 1, 2021. While currently the thresholds to trigger an SEP, such as the number of users or transaction value, have not been notified, the satisfaction of such thresholds, as specified, could result in the existence of a SEP after March 31, 2021, resulting in a business connection in India.
- Explanation 3 to section 9(1)(i) of the ITA provides that in case a non-resident has a business connection in India, so much of the income as is attributable to such business connection is taxable in India.
- The Finance Act, 2020 (**"FA, 2020"**) expanded the attribution rules by inserting Explanation 3A[72] to

71. "Explanation 2A.—For the removal of doubts, it is hereby declared that the significant economic presence of a non-resident in India shall constitute "business connection" in India and "significant economic presence" for this purpose, shall mean—
(a) transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed; or
(b) systematic and continuous soliciting of business activities or engaging in interaction with such number of users in India, as may be prescribed: Provided that the transactions or activities shall constitute significant economic presence in India, whether or not—
(i) the agreement for such transactions or activities is entered in India; or
(ii) the non-resident has a residence or place of business in India; or
(iii) the non-resident renders services in India:
Provided further that only so much of income as is attributable to the transactions or activities referred to in clause (a) or clause (b) shall be deemed to accrue or arise in India."

72. "Explanation 3A.—For the removal of doubts, it is hereby declared that the income attributable to the operations carried out in India, as referred to in Explanation 1, shall include income from–
(i) such advertisement which targets a customer who resides in India or a customer who accesses the advertisement through internet protocol address located in India;
(ii) sale of data collected from a person who resides in India or from a person who uses internet protocol address located in India; and
(iii) sale of goods or services using data collected from a person who resides in India or from a person who uses internet protocol address located in India.



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section 9(1)(i) of the ITA (**"Expanded attribution rules"**). Explanation 3A provides that the income attributable to the operations carried out in India shall include income inter alia from:

- advertisements that target Indian customers, or
- sale of data collected from a person who resides in India or from a person who uses internet protocol address located in India;
- sale of goods or services using data collected from India.

The Expanded attribution rules apply to all business connection situations.

- Collection of tax revenue depends on quantum of income attributable to India. India has made reservations against the revised Article 7[73] of the OECD Model Tax Convention and has taken a stand that the process of attribution of profits by using functions performed, assets used and risks assumed (**"FAR"**) analysis, negates role of 'demand side factors' in the profitability of an enterprise.

Instead, the Central Board of Direct Taxes (**"CBDT"**) in its report on profit attribution to PE (**"Report"**) has considered options based on mixed approach which allocates profits between jurisdictions based on both demand and supply factors. Consequently, a 'fractional apportionment approach' based on apportionment of profits derived from India has been considered as the best option under the Report. A three-factor method based on one-third weight each accorded to sales (representing demand), manpower and assets (representing supply) has been proposed.

Importantly, the Report also dealt with profit attribution in case where business connection is established due to SEP in India. The Report provides for addition of a fourth factor of apportionment i.e., 'users' for businesses in which users contribute significantly to the profits of an enterprise. The degree of apportionment on basis of 'users' differs according to 'user intensity' in a business. For businesses with low and medium user intensity, users have been assigned a weight of 10% while other three factors have been assigned 30% weight each. For businesses with high user intensity, users have been assigned a weight of 20% while the share of assets and employees is reduced to 25% each and sales have been assigned 30% weight.

Though the definitions of "business connection" under Indian law is quite wide, relief may be available under an applicable tax treaty, under which a non—resident's business income is taxable only in the event the non-resident has a permanent establishment in India. The definition of permanent establishment under most tax treaties is presently narrower in scope than that of the "business connection" and the "significant economic presence". The typical types of permanent establishment are:

a. **A Fixed Base PE:** This refers to a fixed place of business through which the business of an enterprise is wholly or partly carried on and includes a place of management, a branch, or any other office, factory, sales outlet, etc. It is not always necessary that the fixed base be owned by a non-resident, and a PE may arise if a fixed place is at the disposal of the non-resident for a continuous period of time. Under most treaties, the maintenance of a fixed place of business in India for a non-resident, solely for the purpose of advertising, for the supply of information, for scientific research or for other activities which have a preparatory or auxiliary character, is deemed not to be a PE.

b. **Service PE:** This usually covers a scenario in which a non-resident furnishes services in India, other than "technical services", through employees or other personnel, and where such services are carried out in India for more than a certain period of time, in aggregate, (usually 90 days) within any 12-month period. As long as this aggregate threshold is not crossed, there should usually be no service PE risk for a non-resident enterprise furnishing services in India through employees or other personnel.

c. **Agency PE:** This covers a scenario in which a person in India (i.e., an 'agent') habitually

73. Under the Article 7 as modified by OECD in 2010, the OECD mandated the Authorized OECD Approach (**"AOA"**) as the preferred approach for attribution of profits to a PE. The AOA requires attribution of profits to the PE on the basis of functions performed, assets used and risks assumed (**"FAR"**) analysis per prescribed OECD's Transfer Pricing guidelines.



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exercises an authority to conclude contracts or secure orders on behalf of a non-resident. If the Indian agent has no such authority, or if the agent possesses independent status, the agent usually should not be considered to be an Agency PE of the non-resident in India.

*International Developments.* There have been recent international developments that may result in a non-resident being taxed in the source country even in the absence of a permanent establishment. However, these developments are still the subject of ongoing debate, and are yet to be codified in India's network of bilateral tax treaties.

In January 2020, the OECD released a statement (**"OECD Statement"**) outlining the architecture of the Unified Approach under Pillar One and welcoming the progress made on Pillar Two.[74] The OECD Statement endorses the Unified approach encompassing three types of taxable profits that may be allocated to a market jurisdiction i.e. Amount A, Amount B and Amount C. The OECD Statement provides that the Unified Approach is designed to adapt taxing rights by taking into account new businesses models and thereby expand the taxing rights of market jurisdictions (which, for some business models, is the jurisdiction where the user is located).

- New Taxing Right – Amount A:

  - Determination of residual profit: The primary response of the OECD Statement to tax challenges of the digitalisation of the economy is a new taxing right called 'Amount A' by which a country will be able to tax profit earned by a multinational without regard to whether the multinational has a physical presence in the country. Under Amount A, a share of the deemed residual profit will be allocated based on a formulaic approach to market jurisdictions using the new nexus standard that is not dependent on physical presence. The OECD Statement provides that the calculation of Amount A will be based on a measure of profit derived from the consolidated group financial accounts and suggests 'profit before tax' as the preferred profit measure to compute Amount A. Currently, the OECD Statement provides for a turnover threshold, in-scope revenue thresholds, business line profitability and de minimis test on aggregate residual profits. The appropriate amount/ percentages of these thresholds are yet to be provided by OECD.

  - In scope businesses: The OECD Statement provides two categories of businesses that will fall within the scope of Amount A namely:

    i. Automated Digital services (**"ADS"**) – These services will cover businesses that generate revenue from the provision of ADS that are provided on a standardised basis to a large population of customers or users across multiple jurisdictions. While the OECD Statement provides examples of business models that would be regarded as providing ADS, such as online search engines, social media platforms, online intermediation platforms (including online market places, irrespective of whether used by business or consumers), digital content streaming, cloud computing services, online advertising services etc. While the definition could include online education reliant on pre-recorded video lectures, and automated tests and other machine dependent platform-student interactions, online education which involves some human intervention, like live lectures, may or may not be covered under this definition;

    ii. Consumer facing business - This would cover businesses that generate revenue from the sale of goods and services of a type commonly sold to consumers, i.e. individuals that are purchasing items for personal use and not for commercial or professional purposes.

  - Establishing nexus with market jurisdiction: The OECD Statement provides for a new nexus rule based on 'significant and sustained' engagement with market jurisdictions for

74. OECD (2020), Statement by the OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy – January 2020, OECD/G20 Inclusive Framework on BEPS, OECD, Paris, available at www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-bepsjanuary-2020.pd



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in-scope businesses. The new nexus rule will be contained in a standalone rule to limit any unintended spill-over effects on other existing tax or non-tax rules. For ADS, the revenue threshold will be the only relevant test required to create nexus. For other in-scope activities, sustained interaction with market or physical presence or other additional factors are also necessary for creation of nexus.

- Elimination of double taxation: The OECD Statement recognises that it will be essential to have appropriate mechanisms to eliminate double taxation as Amount A is an overlay to the existing method of allocation of profits on basis of arms-length principle. In this regard, the OECD Statement states that mechanisms to eliminate double taxation in relevant tax treaties like Article 9(2) may not be useful given that Amount A is not premised on identifiable transactions between group entities. Further, in case where jurisdictions want to eliminate double taxation by way of providing credits, it will be necessary to determine which jurisdiction will have an obligation to eliminate tax and whether there can be any adjustments made to Amount A to avoid situations of double taxation.

- Interactions and potential of double counting: The OECD Statement states that there should be no significant interaction between Amount A and Amount B. In relation to interaction between Amount A and Amount C, the OECD Statement provides that there may be a case where both Amount A and Amount C are allocated to market jurisdiction like India as MNE group has a taxable presence in such jurisdiction. There exists a risk of double taxation due to double counting of profits in Amount A and Amount C. While the OECD Statement currently does not provide any mechanism to resolve double taxations in such cases, it may be useful for MNEs to re-visit their structures and agreements to obtain more clarity with respect to arms-length principle and distribution of profits within separate entities.

- Fixed remuneration based on arms' length price - Amount B:

  - Amount B is a fixed remuneration based on the arms' length price (**"ALP"**) for defined baseline distribution and marketing functions that take place between related parties in the market jurisdiction. Amount B does not create a new taxing right.

  - Amount B aims to simplify administration in transfer pricing (**"TP"**) rules for tax administrations, lower compliance costs for taxpayers and enhance certainty about pricing of transactions.

  - The OECD Statement acknowledges that the design of Amount B will need to ensure the baseline distribution and marketing activities are only remunerated in Amount B and not (again) in Amount C.

  - While the OECD Statement does not provide a clear definition of baseline distribution and marketing activities, the OECD Statement provides that definition of baseline distribution activities will include distribution arrangements with routine levels of functionality, no ownership of intangibles and no or limited risks

  - Further, as per the OECD Statement it is expected that treaty changes will not be required to implement the Amount B regime. Allocation of taxable profits to market jurisdictions under Amount B is based on the existing profit allocation rules (including reliance on physical presence).

## B. Royalties and Fees for Technical Services

Under sub-sections (vi) and (vii) of Section 9(1) of the ITA, the following incomes are also deemed to accrue or arise in India.

- *Royalties.* Income by way of royalties payable by a person resident in India, to a person resident outside India, except where the royalty is payable in respect of any right, property or information



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used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India, and income by way of royalties payable by a person resident outside India to a person resident outside India where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India.

- *Fees for Technical Services.* Income by way of fees for technical services paid by a person resident in India to a person resident outside India, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India, and income by way of fees for technical services paid by a person resident outside India to a person resident outside India where the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India.

In determining whether a payment amounts to royalty or fees for technical services, several issues arise in the Indian context as the definition of royalty under the ITA (particularly, after the clarificatory amendment introduced in 2012) is wider than the definitions accepted internationally.[75]

Though the definitions of fees for technical services and royalty under Indian law are quite wide, relief may be available under an applicable tax treaty, where the definitions of a fees for technical services and royalties are more in line with internationally accepted standards. For instance, a number of India's tax treaties include a 'make-available' requirement for services to constitute technical service. Under this definition, a service is made available only when the person acquiring the service is enabled to apply the technology. The fact that the provision of the service may require technical input by the person providing the service does not per se mean that technical knowledge, skills, etc. are made available to the person purchasing the service. Additionally, it should be noted that certain treaties, such as the US-India Tax Treaty expressly provide that amounts paid for teaching in or by educational institutions do not constitute fees for included (technical) services.

## C. Salaries

Under the ITA any 'salary' due from, or paid or allowed by, an employer or former employer to a taxpayer in a taxable year, whether paid or not, is chargeable to income-tax under the head "salaries"[76]. The ITA defines the term 'salary' to include, among others, wages, any annuity or pension, any gratuity, any fees, commissions, perquisites or profits in lieu of or in addition to any salary or wages.[77]

75. Explanation 2 to Section 9(1)(vi) defines "royalty" as *'consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains")* for—
(i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;
(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;
(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;
(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;
(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting *but not including consideration for the sale, distribution or exhibition of cinematographic films;* or
(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v).
Explanation 3 to Section 9(1)(vi) provides that "computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data.
Explanation 4 to Section 9(1)(vi) provides that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.
Explanation 5 to Section 9(1)(vi) provides that royalty includes and has always included consideration in respect of any right, property or information, whether or not—
(a) the possession or control of such right, property or information is with the payer;
(b) such right, property or information is used directly by the payer;
(c) the location of such right, property or information is in India.
The Explanation 6 to Section 9(1)(i) provides that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret.

76. Section 15 of the Income Tax Act, 1961.

77. Section 17(1) of the Income Tax Act, 1961.



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Further, under section 9(1)(ii) any income which falls under the head 'salaries' is deemed to accrue or arise in India, and is therefore considered taxable in India, if it is 'earned' in India.[78] The law also clarifies that salary payable for service rendered in India shall be regarded as income 'earned' in India for the purposes of the ITA.[79]

Thus, income in the nature of salary derived by a non-resident from the exercise of his employment in India, even if paid outside India, is ordinarily taxable in India by virtue of section 9(1)(ii) of the ITA, subject to relief under an applicable international tax treaty, as explained below.

Relief under a treaty may be available. Several of India's tax treaties provide for the salaries of foreign residents, including teachers and professors) to be taxed only in their country of residence, unless:

- the recipient is present in India for a period or periods exceeding in the aggregate 183 days in the relevant taxable year
- the remuneration is paid by, or on behalf of, an employer who is a resident of India; and
- the remuneration is borne by a permanent establishment or a fixed base or a trade or business which the employer has in India.

## D.Tax Treaty Relief

Under section 90(2) of the ITA, a person resident in a country with which India has a double taxation avoidance agreement is taxable as per the provisions of the tax treaty or the ITA, whichever is more beneficial.

Benefits under a tax treaty should be available as long as the non-resident entity is liable to tax under the laws of its country of residence. Section 90 (4) of the ITA further requires a non-resident claiming treaty relief to

- furnish a valid TRC issued by the government of its country of residence;
- provide certain additional information as prescribed from time to time.

The additional information is required to be furnished in Form No. 10F, prescribed under Rule 21AB(1) of the Income-tax Rules, 1962 (**"IT Rules"**). Rule 21AB(2) of the IT Rules states that Form No. 10F is required to be furnished only if the information required to be furnished therein is not already contained in the non-resident's TRC. However, in practice, Form No. 10F is furnished even when the TRC is as per the prescribed requirements.

## E. Withholding Tax Obligations

Under section 195 of the ITA, any person making a payment of a sum to a non-resident that is chargeable to tax under the ITA (read with the relevant provisions of a tax treaty) would be required to withhold tax on such sum at the appropriate rate. Such withholding is required to be made either at the time of payment or at the time of credit of income to the account of the non-resident, and is applicable to both resident and non-resident payors.

The applicable rates of withholding under the ITA are as follows:

| | **When the non-resident does not have a PE / business connection in India** | **When the non-resident has a PE / business connection in India** |
|---|---|---|
| Business profits qualifying as royalties | Taxable on a gross basis at 10 percent (or at lesser rates prescribed under a tax treaty) | Taxable at 40 percent to the extent of profits attributable to the PE (net of permissible deductions) |
| Business profits qualifying as FTS | | |
| Business profits not qualifying as royalties and FTS | Not taxable (unless there is a business connection in India) | |

78. Under section 9(1)(ii) of the Income Tax Act, 1961.

79. Explanation to section 9(1)(ii) of the Income Tax Act, 1961.



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Similarly, under section 192 of the ITA, any person (including a non-resident) responsible for paying any income chargeable to tax under the head "salaries" shall, at the time of payment, deduct income-tax on the amount payable, at the average rate of *income-tax* computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the taxpayer under the head "salaries" for that financial year.[80]

If any payment made to a non-resident is not subject to tax under the ITA, there should be no obligation to withhold tax on such payment.

## F. Taxation of Associations of Persons

An "association of persons" (**"AOP"**) is recognized as a separate category under the definition of 'person' under section 2(31) of the ITA and is hence a separate taxable unit.

The term AOP is not defined under the ITA and has evolved only through judicial precedents. It is a legal fiction recognized by the ITA for the purpose of imposing a charge of tax. AOP may be formed when two or more persons voluntarily combine in joint enterprise to carry on a business with a common purpose.

Thus, for an AOP to exist, the parties should jointly collaborate with a common design for the purpose of carrying on a business. The mere existence of common interest in a property or business does not create an AOP.

An AOP is said to be resident in India in a financial year "*in every case except where during that year the control and management of its affairs is situated wholly outside India*".[81] Hence, as per the provisions of the ITA, an AOP is considered to be a resident in India if the control or management of its affairs is situated *wholly or partially* in India. As a result, once an AOP is considered to be in existence, unless the control and management is wholly situated outside India, the AOP will be considered as an Indian resident for tax purposes.

80. Section 192 of the Income Tax Act, 1961.
81. Section 6(2) of the Income Tax Act, 1961.

If an AOP is constituted and such AOP is resident in India, the income of the AOP is taxable at the AOP level rather than at the level of the respective taxpayers constituting the AOP.

If the shares of the members of an AOP are indeterminate, the AOP would be taxed on its profits at the maximum marginal rate, i.e., 30% plus surcharge and cess (maximum approx. 42.74%). However, if the total income of a member is taxable at a rate higher than the maximum marginal rate (e.g., a non-resident that may be taxed at around 40% plus surcharge and cess), the total income AOP would be taxed at such higher rate.[82]

If the shares of a member of an AOP are determinate, the share of the relevant member shall be taxed in the hands of the AOP at the maximum marginal rate (or a higher rate if applicable to a specific member).[83]

Where the AOP is liable to tax at the maximum marginal rate or any higher rate, the members are not taxed on their share of profits in the AOP.[84] The members may however be subject to minimum alternative tax to extent the share of profits from the AOP is included in the respective members' book profits.[85]

Any payment whether in the nature of interest, salary, bonus, commission, remuneration or otherwise made by an AOP to its members would not be deductible under the ITA.[86]

Thus, in case of collaborations between an FEI and an Indian educational institution where the FEI provides course content, faculty training, etc. and the Indian educational institution is responsible with respect to infrastructure and other on-ground activities, there is a risk that both entities may jointly be treated as an AOP, depending on the nature of relationship between the entities. As the Indian educational institution is resident in India, such an AOP would also be treated as a resident of India. AOP classification could give to significant exposure

82. Section 167B of the Income Tax Act, 1961.
83. Id.
84. Section 86 of the Income Tax Act, 1961.
85. Section 115 JB of the Income Tax Act, 1961.
86. Section 40(ba) of the Income Tax Act, 1961.


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for FEI as AOPs resident in India are taxable on its worldwide income in India.

## II. The Equalization Levy

Equalisation levy (**"EL"**) was introduced in India with effect from June 1, 2016 under Chapter VIII of the Finance Act, 2016 (**"FA, 2016"**), as a separate, self-contained code, not forming part of the ITA. The EL as introduced by the FA, 2016 (**"2016 EL"**) was levied at rate of 6% on the amount of gross consideration received by nonresidents for online advertisement and related services provided to i) a person resident in India and carrying on business or profession; or ii) an NR having a PE in India.[87] Income arising from provision of online advertisement services which is subject to 2016 EL is exempt from income-tax under the ITA.[88]

The Finance Act, 2020 (**"FA, 2020"**) expanded the scope of EL to apply EL at rate of 2% (**"2020 EL"**) on the amount of consideration received or receivable by 'e-commerce operators' from 'e-commerce supply or services' made or provided or facilitated by it to:

i. person resident in India; or

ii. a non-resident under specified circumstances; or

iii. a person who buys such goods or services or both using an internet protocol (**"IP"**) address located in India.[89]

'Specified circumstances'[90] in case of a nonresident have been defined as:

a. Sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement through IP address located in India; and

b. Sale of data, collected from a person who is resident in India or uses IP address located in India.

Further, the term 'e-commerce operators' has been 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.[91]

The term 'e-commerce supply or services' is defined to mean i) online sale of goods owned by the e-commerce operator; ii) online provision of services provided by the e-commerce operator; iii) online sale of goods or provision of services or both, facilitated by the e-commerce operator; or iv) any combination of the above.[92]

- While the Expanded EL has been applicable from April 1, 2020; a corresponding exemption from income tax has been provided in the ITA for income arising from any e-commerce supply or services made or provided or facilitated on or after April 1, 2021.[93]

- Please note that the provisions in relation to the 2020 EL have been drafted very widely and do not enjoy the benefit of an explanatory memorandum or statement of intent clarifying the applicability of these provisions.

## III. Privacy and Data Localization Requirements

In the aftermath of the ruling by the Indian Supreme Court confirming the fundamental right to privacy,[94] the Government of India has enacted legislation mandating the storage of different types customer data on servers within India. The Personal Data Protection Bill, 2019 (**"PDP Bill"**) was introduced in the lower house of Parliament on December 11, 2019 and is currently under consideration by a Joint Parliamentary Committee set up by the Indian Government.[95] The PDP Bill provides different data

87. Section 165(1) of Finance Act, 2016
88. Section 10(50) of ITA.
89. Section 165A(1) of Finance Act, 2016.
90. Section 165A(3) of Finance Act, 2016
91. Section 164(ca) of Finance Act, 2016
92. Section 164(cb) of Finance Act, 2016
93. Section 10(50) of ITA
94. *Justice K.S Puttaswamy (Retd.) & Anr. vs. Union of India & Ors.*, 6 MLJ 267 dated August 24, 2017.
95. We anticipate at least 10-12 months until this proposed law is enacted (possibly even longer given the ongoing pandemic and Government prioritization of efforts), with additional time for implementation.



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localisation norms for 'sensitive personal data' (**"SPD"**) and 'critical personal data' (**"CPD"**). 'Personal data' has been defined to interalia mean data about or relating to a natural person who is directly or indirectly identifiable, having regard to any characteristic, trait, attribute or any other feature of the identity of such natural person, whether online or offline and shall include any inference drawn from such data for the purpose of profiling.[96] Further, SPD has been defined to mean such personal data, which may, reveal, be related to or constitute inter-alia financial data, health data, biometric data etc.[97] The Central Government has been given the power to notify such personal data that may be considered as CPD.[98]

In this regard, section 33 of the PDP Bill provides that i) a copy of all SPD must be stored in India but it may be transferred outside India ii) CPD must be processed only in India. Further, section 34 of the PDP Bill lays certain conditions on transfer of SPD and CPD outside India.

Further, the Reserve Bank of India (**"RBI"**) has also mandated payment system providers[99] to ensure that the entire data relating to payment systems operated by them are stored in a system only in India.[100] The frequently asked questions by RBI have clarified that this data should include the full end-to-end transaction details and information pertaining to payment or settlement transaction that is gathered / transmitted / processed as part of a payment message / instruction. This may, interalia, include customer data (name, mobile number, email, Aadhaar number, PAN number, etc.), payment sensitive data (customer and beneficiary account details); payment credentials (OTP, PIN, passwords, etc.) and transaction data (originating & destination system information, transaction reference timestamp, amount, etc.).[101] Considering the RBI directive is applicable to payment service providers and not to education service providers, it is likely that contractual obligations will be passed on from the payment service provider to the education service provider.

Given that foreign educational institutions without physical presence are likely to collect data from users, they will have to be mindful of the provisions provided under the PDP Bill and related tax risks that may arise. Having said the above, in relation to managing the data from Indian users, the foreign educational institutions have two choices. They can either store data on an Indian server and take control of such server or they can engage a local service provider to locally store data on any server in India without any control. In case a foreign educational institution exercises control over such servers in India and conducts some business which is not preparatory or auxiliary through such server, it is likely to form a PE thereby creating a huge tax risk for such foreign educational institution with significant income from India. Much of this would also depend on the final Personal Data Protection Act that is passed sometime in the future. However, considering the potential tax risks, it is important to track developments in this regard and reassess tax risks.

# IV. Consumer Protection Laws

The Consumer Protection (E-Commerce) Rules, 2020 (**"Rules"**)[102] have recently been enacted under the Consumer Protection Act, 2019 (**"Act"**). For the uninitiated, India recently revamped its consumer protection laws to bring in better mechanisms for redressal of disputes, stricter liabilities, etc.[103]

The new Rules govern not only commonly known and understood "e-commerce" platforms[104] where consumers can buy/sell goods, but are applicable to almost any platform or e-commerce provider, including

96. Section 2(28) of the PDP Bill.
97. Section 2(36) of the PDP Bill.
98. Explanation to section 2(33) of the PDP Bill.
99. Please note that the RBI directions are applicable to all Payment System providers authorized / approved by the RBI to set up and operate a payment system in India under the Payment and Settlement Systems Act, 2007.
100. https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11244&Mode=0
101. https://m.rbi.org.in/Scripts/FAQView.aspx?Id=130
102. The Rules came into force on July 23, 2020
103. See http://www.nishithdesai.com/information/news-storage/news-details/article/new-consumer-protection-law-in-india-broadening-the-horizon.html for a summary of the provisions of the Act
104. As per Rule 3(1)(i), a "platform" is an online interface in the form of any software including a website or a part thereof and applications including mobile applications;



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marketplace and inventory based models, which provide digital products or services to the consumer.[105]

*Is Ed-tech considered 'e-commerce' and the entity an 'e-commerce entity?*

The Act defines "e-commerce"[106] as buying or selling of goods or services[107] including digital products over digital or electronic network. With this wide a definition, any entity which offers services over the internet may be considered an "e-commerce entity".

Further, the Rules define an "e-commerce entity"[108] to mean any person who owns, operates or manages digital or electronic facility or platform for electronic commerce. This definition does not include a seller offering his goods or services for sale on a marketplace e-commerce entity.

Any Ed-Tech platform providing or facilitating services (such as online tutoring, test prep, skill based learning courses) etc. for a fee would likely fall within the definition of an "e-commerce entity".

Some clarity is provided in the Rules on different models of e-commerce entities.

The first classification is a "marketplace e-commerce entity" which is an e-commerce entity that provides an information technology platform on a digital or electronic network to facilitate transactions between buyers and sellers.[109] An Ed-tech platform model connecting prospective students to teachers or allowing students to purchase courses offered by different educational institutions from its platform may be covered within this definition if they are considered to be "facilitating transactions" between such students and course offerors. There are however some nuances to this connected with what is considered as offering a "service". This is discussed below.

The other classification covered specifically in the Rules is the "inventory e-commerce entity"[110] which is defined as an e-commerce entity which owns the inventory of goods or services and sells such goods or services directly to the consumers. Ed-Tech platforms that curate own courses and offer such courses on their platform are likely to be covered under this definition.

Depending on the model, Ed-Tech platforms will need to decide whether they are a market place or an inventory based e-commerce entity.

*Are the rules applicable to Ed-Tech platforms offering free or fremium services?*

The Rules are certainly applicable to EdTech platform which provides services for a fee. Platforms which offer services for free are exempted from the applicability of these Rules because definition of services in the Act does not include the rendering of any service free of charge.

However, questions remain on the treatment of platforms that operate on a freemium model or provide a combination of free services with paid upgrades. Such platforms will need to examine if the Rules will be applicable to all services provided or only to those aspects which are provided for a fee.

*Is 'education' a service?*

Conflicting views have been taken by courts in India on whether educational institutes can be said to provide a "service" and therefore if such institutions are governed by the provisions of the consumer protection laws in India.[111] Based on the judgments,

105. Rule 2 of the Rules provides that the Rules apply to *(a) all goods and services bought or sold over digital or electronic network including digital products; (b) all models of e-commerce, including marketplace and inventory models of e-commerce; (c) all e-commerce retail, including multi-channel single brand retailers and single brand retailers in single or multiple formats; and (d) all forms of unfair trade practices across all models of e-commerce.*

106. Section 2 of the Act

107. Section 2 of the Act defines "services" as *service of any description which is made available to potential users and includes, but not limited to, the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, telecom, boarding or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service.*

108. As per Rule 3(1)(b) of the Rules, "e-commerce entity" means any person who owns, operates or manages digital or electronic facility or platform for electronic commerce, but does not include a seller offering his goods or services for sale on a marketplace e-commerce entity

109. Rule 3(g) of the Rules.

110. Rule 3(f) of the Rules.

111. The Supreme Court in P.T. Koshy & Anr. Vs. Ellen Charitable Trust & Ors., 2012 (3) CPC 615 (SC), has held that students are not 'consumers', 'education' is not a commodity and educational institutions are not rendering 'service'. Another later judgment of the Supreme Court in Civil Appeal Nos. 7003-7004 of 2015, P. Sreenivasulu & Anr. Vs. P.J. Alexander & Anr., dated 09.09.2015, held that educational institutions would come within the purview of the Consumer Protection Act, 1986 and that education is a service



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it may be possible to say that since educational institutions are not for profit in nature and do not provide commercial services, they do not fall within the purview of the consumer protection law in India. However, educational institutions are differentiated from coaching institutes, test prep centres etc which fall within the purview of service providers.[112]

Based on the above, an educational institution providing courses online may/may not be governed by the Act and the Rules. Ed-Tech platforms that provide a range of services including courses offered by educational institutions may still have to comply with the Rules, at least to the extent the platform is said to be offering a service vis-à-vis the consumer. Since the applicability of the Rules depends on the model adopted by Ed-Tech platform, a case by case analysis will be required to determine if compliance with the Rules is required.

*Do these rules apply to foreign Ed-Tech platforms?*

The Rules specifically provide that an "e-commerce entity" which is not established in India, but systematically offers goods or services to consumers in India is also governed by the Rules. There is no threshold provided in the Rules for determination of the term "systematically". This will have to be determined on a case to case basis.

*What are the compliances required under the Rules?*

## A. Applicable to all e-commerce entities.

There are certain compliances which are applicable to all e-commerce entities. Some of the key compliances are:

- *Nodal officer:* The Rules also require e-commerce entities to appoint nodal officers or an alternate senior designated functionary who is resident in India, to ensure compliance with the Act.

- *Explicit consent for purchase:* As per the Rules, recording consent of a consumer's purchase of any goods or services should only be by way of an explicit and affirmative action. Consent cannot be recorded automatically (including in the form of pre-ticked checkboxes).

- *Grievance redressal mechanism:* Entities must establish an adequate grievance redressal mechanism and appoint a grievance officer for consumer grievance redressal. Name of the entity with its address of its headquarters and branches, designation and contact details (email, phone etc) of the grievance officer and customer care must be displayed prominently on the platform. This can be achieved by updating the website terms. Obligation to appoint grievance officer already exists under rules framed under the Information Technology Act, 2000. What is important to know is that e-commerce entities are required to ensure that the grievance officer acknowledges the receipt of any consumer complaint within forty-eight hours and redresses the complaint within one month from the date of receipt of the complaint

Additional compliances pertaining to levy of cancellation charges after purchase, refunds, price manipulations, differentiation between class of customers etc. are also provided in the Rules.

## B. Applicable to marketplace and inventory e-commerce entities

Some common compliances for both marketplace and inventory e-commerce entities include providing the following information in a clear and accessible manner to the customers:

- *Information on returns, refunds etc.:* It is now mandatory to provide information on return, refund, exchange, warranty and guarantee, delivery and shipment, modes of payment, any other similar information which may be required by consumers to make informed decisions.

- *Payment methods:* Necessary information on payment methods and security of those payment methods must be provided to consumer.

- Other information required to be provided includes any fees or charges payable by users,

112. See Manu Solanki and Ors v. Vinayaka Mission University and Ors., I(2020)C PJ210(NC )



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the procedure to cancel regular payments under those methods, charge-back options, if any, and the contact information of the relevant payment service provider.

## C. Applicable to inventory e-commerce entities:

- *No fake reviews:* Inventory e-commerce entity cannot falsely represent itself as a consumer and post reviews.
- *Return and refund in case of defect:* Platforms are required to provide refunds if services are defective, or if the goods or services are not of the characteristics or features as advertised;
- *Advertising standard:* Advertisements need to be honest and consistent with actual characteristics, access and usage of goods or services offered.

Inventory based platforms who vouch for the authenticity of goods or services (explicitly or impliedly) can be liable for actions taken in relation to authenticity of goods or services sold through the platform.

## D. Applicable to marketplace e-commerce entities:

- *Undertaking by sellers:* Entities must ensure that sellers[113] provide an undertaking to the entity to the extent that all descriptions, images and other content pertaining to the goods or service provided are accurate and correspond directly to the appearance, nature, quality, purpose and other general features specified in the undertaking;
- *Information:* The following information must be provided in a clear and accessible manner on the platform:
  - Details about the sellers;[114]
  - An explanation of the main parameters which are most significant in determining the ranking of goods or sellers on its platform
- *Terms and conditions:* The terms and conditions of the entity with its sellers must provide a description of any differentiated treatment which it gives or might give between goods or services or sellers of the same category. Based on this, entities will have to clarify if the entity provides sponsored results.

In addition to the above, the Rules also provide duties for sellers on marketplaces. Some such duties include:

- *Written contract:* Sellers must have a prior written contract with the entity;
- *Information from sellers:* Sellers must provide certain information to the e-commerce entity for display on its platform including total price with breakup of all charges, all mandatory notices and information provided by applicable laws; information on the goods/services offered, name and other details of the seller's grievance redressal officer[115];
- *No fake reviews:* Similar to the inventory model, sellers also are prohibited from posting fake reviews on the platform;
- *Return and refund in case of defect:* Sellers are required to provide refunds if services are defective, or if the goods or services are not of the characteristics or features as advertised

113. As per Rule 3(1)(k) of the Rules, "seller" means a "product seller" as defined under the Act. Section 2(37) of the Act defines a "product seller", in relation to a product, as a person who, in the course of business, imports, sells, distributes, leases, installs, prepares, packages, labels, markets, repairs, maintains, or otherwise is involved in placing such product for commercial purpose and includes— (i) a manufacturer who is also a product seller; or (ii) a service provider, but does not include— (a) a seller of immovable property, unless such person is engaged in the sale of constructed house or in the construction of homes or flats; (b) a provider of professional services in any transaction in which, the sale or use of a product is only incidental thereto, but furnishing of opinion, skill or services being the essence of such transaction; (c) a person who— (I) acts only in a financial capacity with respect to the sale of the product; (II) is not a manufacturer, wholesaler, distributor, retailer, direct seller or an electronic service provider; (III) leases a product, without having a reasonable opportunity to inspect and discover defects in the product, under a lease arrangement in which the selection, possession, maintenance, and operation of the product are controlled by a person other than the lessor;

114. As per Rule 5(3) of the Rules, details must including the name of their business, whether registered or not, their geographic address, customer care number, any rating or other aggregated feedback about such seller, and any other information necessary for enabling consumers to make informed decisions at the prepurchase stage

115. For a complete list of information to be provided, see Rule 6(5) of the Rules.



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# V. GST Framework

India's indirect taxation regime has been complex and cumbersome with Union and State Governments taxing different transactions and permitting overlap and ambiguity on certain transactions. The Constitution (One Hundred and First Amendment) Act, 2016 (**"Constitution Amendment Act"**) was both unprecedented and historical. On July 1, 2017, India has introduced a dual GST, with multiple classification of goods and services which vary from state to state. GST is categorized as Central Goods and Services Tax (**"CGST"**) to tax intra-state sale of goods and services; Integrated Goods and Services Tax (**"IGST"**) to tax inter-state sale of goods and services; or State Goods and Services Tax (**"SGST"**) levied by the respective States /union territory and governed under the relevant state GST laws. An IGST is levied on every interstate supply of goods or services by the central government under the IGST Act, 2017 (**"IGST Act"**). Further, every intrastate supply is concurrently subject to a CGST by the central government under the CGST Act, 2017 (**"CGST Act"**) and a SGST by the relevant state government under the relevant **SGST Act.**

## A. Basic GST Terms

- *Taxable events:* Under GST laws, the levy of tax is on "supply" of goods or services and on imports. All intra-state[116] / inter-state[117] 'supply of goods or services or both'[118] shall be liable to tax. The scope of 'supply' is wide in its scope to include all forms of supply of goods or services or both such as sale, transfer, barter, exchange, licence, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business. It also includes import of services, and activities specified in Schedule I and Schedule II. Therefore, a transaction which is not a sale, may yet be counted as a taxable event on which GST is payable. The wide expressions and the inclusive definition provide for all transactions, including incidental and ancillary goods / services being provided as being amenable to GST.

  The clarification issued by CBEC[119] (**"CBEC Clarification"**) reiterates the provision of the law and notes that following parameters may be considered:

  - Supply of goods or services. Supply of anything other than goods or services does not attract GST.
  - Supply should be made for a consideration, except in respect of supplies specified under Schedule I of the CGST Act, which are taxable even if made without a consideration.
  - Supply should be made in the course or furtherance of business.
  - Supply should be made by a taxable person.
  - Supply should be a taxable supply.
  - Supply should be made within the taxable territory.

  While the CBEC Clarification places emphasis on consideration, the presence or absence of consideration would become a question of fact that may not, by itself, prevent tax authorities from scrutinising transactions in detail and characterising a transaction as 'with consideration'.

- *Place of supply:* The governing law in relation to a transaction of supply of goods or services is to be determined on the basis of inter-state or intra-state supply of goods or services. If the supply is inter-state, then IGST law is to be applied. However, the supply is intra state, then CGST and SGST laws are to be applied. A cross-border supply of goods or service is subject to IGST, on crossing the Indian customs frontier. IGST is levied in addition to the basic custom duty levied on the value of the import transaction. In a cross-border

116. The intra-state supplies are supplies of goods or services where the location of the supplier and the place of supply are in the same state or same union territory.

117. The inter-state supplies include supplies of goods or services where the location of the supplier and the place of supply are in two different states, or two different Union territories, or a state and a Union territory; supplies of goods or services imported into India when the cross the customs frontiers of India; supplies of goods or services when the supplier is located in India and the place of supply is outside, to or by an developer in special economic zone or unit, or is a supply in the taxable territory and is not an intra-state supply nor covered elsewhere

118. Except alcoholic liquor for human consumption.

119. The meaning and scope of supply, available at http://www.cbec.gov.in/resources//htdocs-cbec/gst/eflier-meaningscopeofsupply14062017.pdf.



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supply of goods, the location of the importer (in case of imports) and location outside India (in case of exports) is considered. In a cross-border supply of services, the location of the service recipient or supplier depends on each transaction. Further, supply of services directly in relation to an immovable property, depends on the location of the immovable property.

- *Time of supply:* The element of time ascertains the rate of tax and when such tax is to be levied. Generally, the time of supply of goods is the earliest of the date of the invoice or last date of the prescribed period for issue of invoice, or date of receipt of payment. For a transaction on a reverse charge[120] basis, the time of supply of goods shall be earliest of the date of the receipt of goods, or date of payment as per the recipient's books of account or the date on which payment is debited in his account, or immediately after 30 days from issue of invoice, or date of entry in the recipient's books of account (where the above are not possible to determine).

- *Value of supply:* GST is computed on the value of the supply. The value of supply is the transaction value in case of unrelated transactions where the price is the sole consideration. For a transaction where the consideration is not wholly in money, or a transaction which is between distinct or related person (with or without agent), value of the supply is determined in a prescribed manner or on a recommendation of the GST Council. Further, a residuary method has also been prescribed to determine the value of supply of goods or services. Further, certain activities or transactions are neither treated as a supply of goods nor services. These transactions are prescribed[121] or include transactions undertaken by the Central Government, or a State Government or any local authority (engaged as public authorities, as may be notified by the government on the recommendation of the GST Council).

- *Taxable person:* A taxable person is a person who is either registered or liable to be registered under the provisions of the GST laws. The CGST Act requires that every supplier shall register from where he makes a taxable supply of goods or services only if the supplier has an aggregate turnover of INR 20 lakhs or more in a financial year.[122] However, this threshold is not applicable to foreign companies supplying Online Information Database Access and Retrieval services (**"OIDAR services"**) from outside India to Indian consumers or to nonregistered businesses in India,[123] and such foreign companies are required to register under the GST regime regardless of their size or the value of the services being supplied in India in a financial year.

  Certain persons required to obtain registration irrespective of turnover: a person making interstate supply; a casual taxable person and nonresident taxable persons; a person required to pay tax under reverse charge; a person making supply on behalf of other registered taxable person, whether as agent or otherwise; an input service distributors; a person making supply (except of branded services) through an e-commerce operator; an e-commerce operator; every person supplying OIDAR service from outside India to a person in India who is not a registered taxable person (B2C). A person exclusively supplying goods that are not liable to tax or exempt to tax, do not need registration. However, supplies with zero-rated tax requires a person to register in order to claim refund or credit.

- *Rates:* Under the GST regime, there are separate notifications providing tax rates for goods and services, with separate IGST, CGST, as well as SGST notifications. These notifications have been amended multiple times since GST has become effective. For ease of reference, we shall only refer to the IGST rates for goods and services, and the rates notifications for goods shall be collectively referred to as "Rates Schedule for Goods" while those for services shall be collectively referred to as "Rates Schedule for Services". The Rates Schedules for Goods and Services provide a

120. "Reverse charge" means the liability to pay tax by the recipient of supply of goods or services or both instead of the supplier of such goods or services or both under sub-section (3) or sub-section (4) of section 9, or under sub-section (3) or subsection (4) of section 5 of the IGST Act.

121. Schedule III, CGST Act.

122. Section 22(1), CGST Act.

123. Section 24(xi), CGST Act.



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detailed list of all goods and services and their applicable tax rates under GST, and there is a residuary classification under both Schedule which is taxable at 18 percent. Further, there are separate exemption notifications for goods and services under CGST, IGST and each SGST Acts.

The rate structure for services under CGST falls within the range of 0 percent, 2.5 percent, 6 percent, 9 percent or 14 percent and under IGST falls within the range of 0 percent, 5 percent, 9 percent, 12 percent, 18 percent or 28 percent. Most of the rate in relation to digital services falls under 18 percent. Supply of certain goods and services have been designated as 'Zero rated supply' of goods and services meaning although it is taxable supply, zero rate of tax would be charged in respect to such supply and input tax credit or refund can be claimed. Such supplies relate to: (a) exports of goods or services (ii) supply of goods or services to a Special Economic Zone developer or a unit.

## B.GST on Intangibles

Taxation of transactions in intangibles, particularly intellectual property (**"IP"**) rights, has historically been a contentious issue in India due to differential taxation regimes for sale of "goods" and provision of "services" coupled with the obscurity surrounding the classification of such transactions. This has been one of the most litigated areas of indirect taxation in India. Due to continuous overlap between the definition of 'goods' under the Constitution of India and the state sales tax / VAT laws with the definition of 'taxable services' under the Service Tax Act, it was a question to ascertain a transaction in intangibles as a sale of goods or a provision of service.

Under GST, the taxable event is the supply of goods or services. Therefore, the concepts of sale or deemed sale (as defined under the constitution) used under the VAT or central sales tax have become obsolete. The CGST Act defines goods as "every kind of movable property other than money and securities."[124] This definition is wide enough to include intangibles.[125]

Services have also been defined broadly to include, among other things, "anything other than goods, money and securities but includes activities relating to the use of money."[126] Thus, the distinction between mere permission to use IP and a transfer of the right to use the IP is no longer relevant; both are considered a supply of service under GST.

*Import of Intangibles*

Import of intangible goods appears to have been overlooked by the drafters of the GST, and there is an ambiguity regarding the taxation of such transactions. Section 5 of the IGST Act provides that IGST is chargeable on all interstate supplies of goods and services based on the value determined under section 15 and at a notified rate that shall not exceed 40 percent. Section 5 of the IGST Act (which is the charging provision for IGST) further states *"[the] integrated tax on goods imported into India shall be levied and collected in accordance with the provisions of section 3 of the Customs Tariff Act, 1975 on the value as determined under the said Act at the point when duties of customs are levied on the said goods under section 12 of the Customs Act, 1962."*

Therefore, determining when customs duty is levied is important to ascertaining whether IGST would be chargeable on a transaction involving the import of goods. Judicial precedents provide that customs duty is levied when goods are imported into India, that is, when they cross India's customs barriers. Decisions under the Central Sales Tax Act, 1956 (**"CST Act"**) have similarly equated the import of goods into India with the event of "crossing customs frontiers of India." While this phrase is not defined by the Customs Act, the CST Act defines "crossing the custom frontiers of India" as crossing the limits of the area of a customs station in which imported goods or export goods are ordinarily kept before clearance by custom authorities.

Because the point of taxation for imports under the Customs Act relates to the physical movement of goods across India's customs frontiers, it appears clear that no customs duty is due on the import of intangible goods. In turn, IGST is only applicable on import of tangible

124. Section 2(52), CGST Act.

125. The Model GST Law released by the Empowered Committee of State Finance Ministers in June 2016 specifically excluded intangibles from the definition of goods. This carveout was not been carried over into the final CGST Act.

126. Section 2(102), CGST Act.



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goods that physically cross the customs frontiers of India. It is not designed to apply to intangible goods that may be imported through a digital medium such as the internet. Intangibles could include IP such as software, copyrights, or trademarks assigned online by a person offshore to a person in India.

While these transactions would qualify as imports of goods, they have been (possibly inadvertently) overlooked by the charging section of IGST. Absent any conclusive judicial precedent on this point, it is unclear whether these transactions are subject to GST.

## C. OIDAR Services

Similar to the service tax regime that preceded it, the GST regime captures digital services within the definition of OIDAR services, which includes services 'whose delivery is mediated by information technology over the internet or an electronic network and the nature of which renders their supply essentially automated and involving minimal human intervention and impossible to ensure in the absence of information technology'.[127] The definition further provides a list of services within the definition of OIDAR services: advertising on the internet; providing cloud services; provision of e-books, movie, music, software and other intangibles through telecommunication networks or internet; providing data or information, retrievable or otherwise, to any person in electronic form through a computer network; online supplies of digital content (movies, television shows, music and the like); digital data storage; and online gaming.[128]

The distinction between OIDAR services and other types of services becomes particularly important when determining the place of supply of a service. Those transactions where the location of the supplier and place of supply of goods or services are in (i) two different States, (ii) two different Union territories; or (iii) a State and a Union territory are subject to IGST,[129] while those transactions where the two are in the same State or Union Territory are subject to CGST and SGST/UGST.[130] Further, imports of goods and services are also subject to IGST, and the term 'import of services' is defined as a supply of services where (i) the supplier of service is locations outside India, (ii) the recipient of service is located in India; and (iii) the place of supply is in India.[131] Accordingly, it becomes important to determine the place of supply of a service[132] to determine whether IGST would be applicable. The place of supply of OIDAR services shall be the location of the recipient of services, and a service recipient shall be deemed to be located in India, if any two of the following non-contradictory conditions are met:

- the location of address presented by the recipient of services through internet is in the taxable territory;
- the credit card or debit card or store value card or charge card or smart card or any other card by which the recipient of services settles payment has been issued in the taxable territory;
- the billing address of the recipient of services is in the taxable territory;
- the internet protocol address of the device used by the recipient of services is in the taxable territory;
- the bank of the recipient of services in which the account used for payment is maintained is in the taxable territory;
- the country code of the subscriber identity module card used by the recipient of services is of taxable territory; and
- the location of the fixed land line through which the service is received by the recipient is in the taxable territory.

It could be argued that services provided through electronic means, specifically OIDAR services, should fall within the residuary category under the Rates Schedule for Services and be subject to tax at the rate of 18 percent. However, the Rates Schedule for Services does not make a distinction between services based on their mode of supply. The separate

127. Section 2(17), IGST Act.
128. Section 2(17), IGST Act.
129. Sections 7(1) and 7(2), IGST Act
130. Section 8(1), IGST Act
131. Section 2(11), IGST Act.
132. Section 13, IGST Act.



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identification of OIDAR services with rate schedule may lead to litigation on classification.

Additionally, while the provision of B2C services by a non-resident to an individual in India is exempt from GST, this exemption is not available in the case such non-resident is providing OIDAR services.

## VI. Exchange Control Regulations

All cross-border flows of money into and outside India are regulated by the Foreign Exchange Management Act, 2000 (**"FEMA"**).

Under the FEMA, all transactions involving foreign exchange have been classified as either capital or current account transactions. All transactions undertaken by a person resident in India that do not alter his / her assets or liabilities, including contingent liabilities, outside India are generally regarded as current account transactions.

Under Section 5 of the FEMA, a person resident in India is permitted to sell or draw foreign exchange to or from an authorized person if such sale or drawal is for a current account transaction[133] However, this permission is subject to any reasonable restrictions that the Central Government (acting in consultation with the RBI) may prescribe. Presently, the restrictions imposed by the Central Government are set out in the Foreign Exchange Management (Current Account Transactions) Rules, 2000 (the **"CAT Rules"**).

The CAT Rules categorize current account transactions as follows (i) transactions which are prohibited, which are listed in Schedule I of the CAT Rules; (ii) transactions which require the prior approval of the Central Government, which are listed in Schedule II of the CAT Rules and; (iii) permissible transactions which are governed by Schedule III of the CAT Rules.

Under Schedule III, individuals can avail of foreign exchange facilities for the following purposes within the limit[134] of USD 250,000 per financial year:

a. Private visits to any country (except Nepal and Bhutan);

b. Gifts or donations;

c. Going abroad for employment;

d. Emigration;

e. Maintenance of close relatives abroad;

f. Travel for business, or attending a conference or specialized training or for meeting medical expenses, or check-ups abroad, or for accompanying as attendant to a patient going abroad for medical treatment/check-up;

g. Expenses in connection with medical treatment abroad;

h. Studies abroad;

i. Any other current account transaction[135]

133. *Section 2(j) of the FEMA defines a "current account transaction" as 'a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transaction includes: (i) payments due in connection with foreign trade, other current business, services and short-term banking and credit facilities in the ordinary course of business, (ii) payments due as interest on loans and as net income from investments; (iii) remittances for living expenses of parents, spouse, children residing abroad, and (iv) expenses in connection with foreign travel education and medical care of parents, spouse and children.'*

134. Additional remittances require the prior approval of the RBI.

135. Being a current account transaction not falling under Schedule I or Schedule II of the CAT Rules.



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# 4. Scope and Limitations of these Case Studies

The scope of this case study is limited to identify tax issues in relation to the entities operating in the online education ecosystem on the basis of analysis of their operational model and legal structure. The case study sets out both the operational features of online education models and looks at common structural issues that may arise in such models from an Income-tax, equalization levy, international tax, transfer pricing and Goods and Service tax (**"GST"**) perspective.

This case study does not deal with the validity of a particular degree, diploma or programme offered and consumer protection or data protection issues that may arise.



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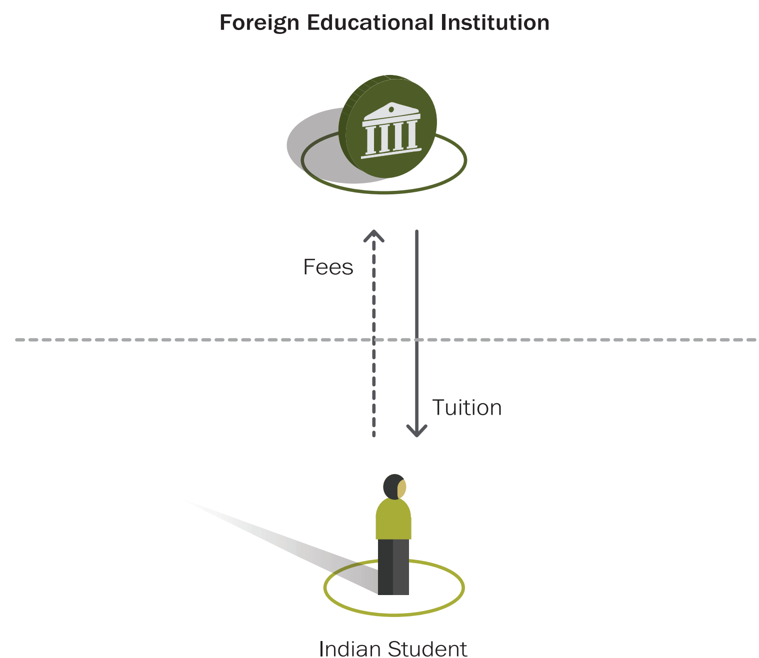
# 5. Structures Commonly Adopted by FEIs operating in the Unregulated Sector

In light of the various regulatory restrictions, FEIs seem to be focusing on the unregulated segments of the higher education sector to avoid regulatory hassles. Therefore, FEIs, in India offer programmes which result in grant of certificate of completion or credits for courses (instead of a degree or diploma). If the programmes are offered from outside India (for instance online mode) then degrees or diplomas are also sometimes issued to the students, depending on the nature of the programme from outside India. The validity and acceptance of such degrees in India remain a grey area under existing Indian regulations. Further, some states, depending on the nature of course and duration, regulate certificate programmes as well. Hence, carefully drafting the agreements, to be in sync with the regulations, is critical from a structuring perspective.

Some of the business models commonly adopted are:

## I. Model I - Online Only Diploma / Degree Program




The Online Education Regulations discussed above apply only to Indian institutes. They currently do not extend to programs offered by foreign education institutions in India. Courses or programmes offered directly through foreign education institutions from outside India are still unregulated. While such courses usually award certificate of completion to the successful candidate at the end of the course, some even award a degree from outside India for programmes completed via the online mode. Some of these courses are also self-paced and flexible with programme timing, schedule etc., resulting in higher enrollment ratio. Further, some programmes are highly interactive, and provide for online tutors and access to e-libraries as well.

These courses usually involve a payment from an Indian student to the FEI.

*Analysis*



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| Sr. No. | Transaction | Tax Implications |
|---|---|---|
| **a.** | In this model, the platform is proprietary, and owned by the FEI. Services are provided online through the platform, in return for tuition fees. | ▪ Implications under the ITA<br><br>At the outset, the FEI, being a non-resident is liable to be governed by the provisions of the ITA or relevant tax treaty, whichever is more beneficial. Under the ITA, tuition fees earned by a foreign university could be taxable as fees for technical services (**"FTS"**) at 10% on a gross basis. The ITA defines FTS to mean consideration for managerial, technical, or consultancy services, irrespective of whether such services are rendered in India or from outside India.<br><br>The ITA imposes withholding tax obligation on the receiver of services, i.e. students in this case. This means that students must withhold tax at the rate of 10% at the time of payment of fee.<br><br>For the purposes of withholding, the FEI will need to provide a Permanent Account Number (PAN) to the withholder. Further, this will also trigger the requirement for the foreign university to file a return of income in India. This process can be tedious and cumbersome.<br><br>▪ Tax Treaty Implications<br><br>The FEI should be liable to be taxed in India if the tuition fees qualify as FTS under a relevant tax treaty. Otherwise, the FEI should be liable to tax in India, only if it has a permanent establishment (**"PE"**) in India. If the FEI has a server in India, this is likely to result in a fixed place PE in form of server PE[136] in India if it has taken control of a server in India and conducts business which is not preparatory or auxiliary through such server. However, this risk can be mitigated if the FEI is able to avail of cloud services from a provider in India, as an alternative to the server.<br><br>Additionally, some treaties like the India-US Tax Treaty may explicitly provide that amounts paid for teaching in or by educational institutions will not qualify as FTS.<br><br>▪ Interplay of Fees for Technical Services and SEP<br><br>The characterisation of tuition fees assumes importance vis-à-vis constitution of SEP. While characterising the tuition fee as a fee for technical services is a more specific treatment, the risk of tax authorities alleging constitution of SEP cannot be ruled out. The tax authorities may allege constitution of 'business connection' through SEP test as the FEI is engaged in transaction in respect of services with students in India, resident in India. Pertinent to note that constitution of SEP depends on transaction value, or number of users – the thresholds of which are yet to be notified. In case SEP is constituted in India, the proportion of total income of the FEI attributable to the SEP will be taxable in India. However, in absence of any amendment in the tax treaties in relation to SEP, the FEI may not be liable to tax in India due to non-creation of PE<br><br>▪ Equalisation Levy<br><br>The EL should apply at rate of 2% on the amount of tuition fee received by the FEI. This is because the FEI would be hosting the course on its platform which should result in the course being offered as an 'e-commerce service' provided by the FEI which should be considered as an e-commerce operator, which owns and operates an electronic platform. |

136. Server PE is likely to arise when the business of a non-resident is carried out through the website hosted on a server in India and where the non-resident has the server at its disposal, in capacity of owner, lessee or otherwise.



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- **Pillar I Implications**

The OECD Statement provides for creation of a new taxing right in form of Amount A. Amount A will be calculated on the basis of profit before tax as per consolidated group financial statements.

- While the non-exhaustive list of business models to be considered as ADS do not specifically includes online education, it is possible that Model 1 may involve some element of ADS, such as digital content streaming,[137] The OECD Statement provides that in case of ADS, nexus will be determined basis the revenue threshold of A. In case A qualifies the revenue threshold, Amount A may be allocated to India irrespective of A not having any physical presence in India. It is also possible that online education service may be included within the category of consumer facing business, since its services are provided primarily to consumers.

- For ADS, the revenue threshold will be the only relevant test required to create nexus. For other in-scope activities, sustained interaction with market or physical presence or other additional factors are also necessary for creation of nexus.

- While the OECD Statement does not provide the appropriate amounts / thresholds for allocation of profits under Amount A, the Indian tax authorities are likely to argue for significant allocation of income to India due to student participation. More emphasis would be on apportioning residual income or Amount A directly in proportion to the number of students and where they are located.

- However, several countries and economic reports suggest that more value is contributed through the development of the software (in the case of education, this could also include course material) and its maintenance outside of India. In such a situation, whether more value is contributed by the software or through a larger customer base that accesses a simple software would need further examination

- Software or course involving a high degree of specialization and innovativeness should qualify for a lesser allocation when the OECD develops a digital differentiation key where different digital business models may have a varying range of allocation percentages based on their level of digital differentiation.

- Further, assuming that the same education services are offered to students around the world for a higher fee, it is possible that the Indian market while having more students may not be generating comparable revenue. In such cases as well the current Pillar I suggestions may result in sub-optimal allocation. However, a regional or a business line segmentation of profits would have a significant impact on allocation of profits in such a case.

137. However, if there is some human interaction involved in the provision of the online education services, it should not fall within the scope of ADS.



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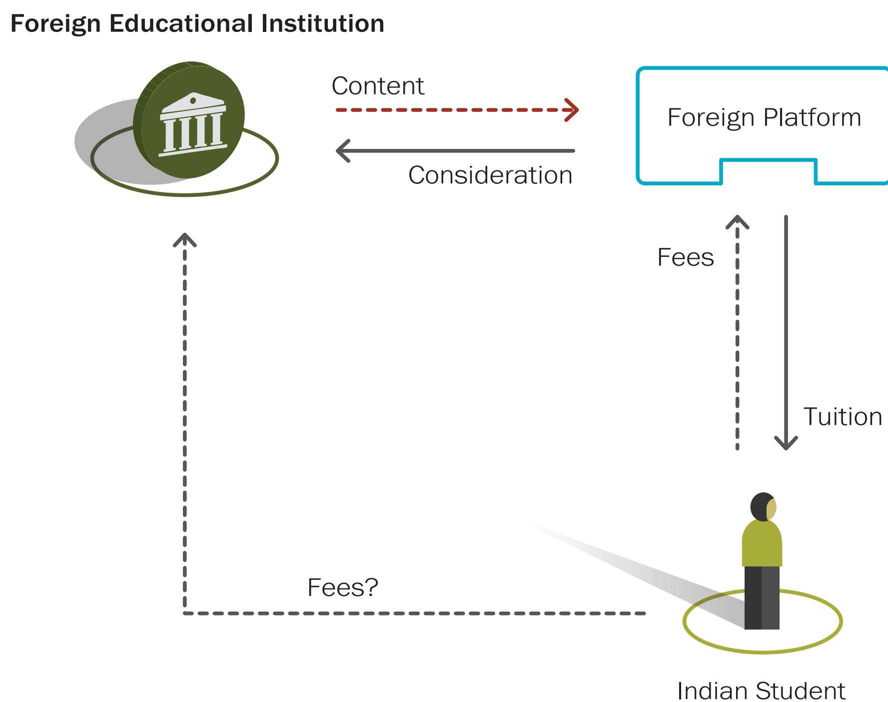
| | | |
|---|---|---|
| | | • GST implications<br><br>If the services are mostly automated (i.e., the lessons are pre-recorded, with minimal live interaction), they are likely to qualify as OIDAR services, and, since the reverse charge mechanism under GST will not apply to the Indian student, the FEI, should be liable to pay GST at rate of 18% on forward charge basis. The FEI would have to comply with mandatory GST registration with tax authorities. However, if the online education service involves some real-time live human involvement, such as live interactive session, then the service should not qualify as OIDAR and being a B2C service, should not be exempt from GST. |

# II. Model II – Online Platform Model




Similar, to Model I, in this set-up, the FEI offers courses through a platform. The FEI may license its courses to the foreign platform in exchange for consideration, or may choose to enter into an arrangement where tuition fees are passed through to it by the Platform, and it remunerates the Platform for its hosting service.

*Analysis*

| Sr. No. | Transaction | Tax Implications |
|---|---|---|
| **a.** | Services are provided online, through a third-party platform, in return for tuition fees. | ▪ Implications under the ITA<br><br>The tax implications would depend on the nature of the payment relationship between the Platform and the FEI. If the payments by the student are made to the platform, then the Platform would be taxable in India. However, if the payments are passed through to the FEI, then the FEI would be taxable in India. |



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The Platform/FEI, being a non-resident is liable to be governed by the provisions of the ITA or relevant tax treaty, whichever is more beneficial. Since the beneficial provisions dealing with FTS under most tax treaties require the claimant to be the beneficial owner of the FTS, the arrangement between the FEI and the Platform would need to be analysed to understand which entity would be entitled to treaty benefits. Where the Platform is the beneficial owner, the tax treaty between Indian and the jurisdiction where the platform is resident should be considered. Where the FEI provides the services directly and receives fees and is the beneficial owner, tax treaty between the India and the jurisdiction where the FEI is resident should apply. However, in case where the student pays fes to the Platform but the beneficial owner is the FEI, whether treaty benefits will be available to the FEI will need to be assessed. Under the ITA, tuition fees earned by the platform could be taxable as fees for technical services (**"FTS"**) at 10% on a gross basis. The ITA defines FTS to mean consideration for managerial, technical, or consultancy services, irrespective of whether such services are rendered in India or from outside India.

The ITA imposes withholding tax obligation on the receiver of services, i.e. students in this case. This means that students must withhold tax at the rate of 10% at the time of payment of fe e.

For the purposes of withholding, the Platform / FEI will need to provide a Permanent Account Number (PAN) to the withholder. Further, this will also trigger the requirement for the foreign university to file a return of income in India. This process can be tedious and cumbersome.

- Tax Treaty Implications

The Platform / FEI should be liable to be taxed in India if the tuition fees qualify as FTS under a relevant tax treaty. Otherwise, the Platform / FEI should be liable to tax in India, only if it has a permanent establishment (**"PE"**) in India. If the Platform / FEI has a server in India, this is likely to result in a fixed place PE in form of server PE[138] in India as it has taken control of a server in India and conducts business which is not preparatory or auxiliary through such server. However, this risk can be mitigated if the Platform / FEI is able to avail of cloud services from a provider in India, as an alternative to the server.

- Interplay of Fees for Technical Services and SEP

The characterisation of tuition fees assumes importance vis-à-vis constitution of SEP. While characterising the tuition fee as a fee for technical services is a more specific treatment, the risk of tax authorities alleging constitution of SEP cannot be ruled out. The tax authorities may allege constitution of 'business connection' through SEP test as the Platform / FEI is engaged in transaction in respect of services with students in India, resident in India. Pertinent to note that constitution of SEP depends on transaction value or number of users – the thresholds of which are yet to be notified. In case SEP is constituted in India, the proportion of total income of the FEI / Platform attributable to the SEP will be taxable in India. However, in absence of any amendment in the tax treaties in relation to SEP, the Platform / FEI may not be liable to tax in India due to non-creation of PE.

Some treaties like the India-US Tax Treaty may explicitly provide that amounts paid for teaching in or by educational institutions will not qualify as FTS.

138. Server PE is likely to arise when the business of a non-resident is carried out through the website hosted on a server in India and where the non-resident has the server at its disposal, in capacity of owner, lessee or otherwise.



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- Equalisation Levy

The EL should apply at rate of 2% on the amount of tuition fee received by the Platform as it is consideration for 'e-commerce service' provided by the Platform, being an e-commerce operator, which owns and operates an electronic platform. The Platform would also likely be regarded as facilitating the supply of e-commerce service (i.e., the education services) resulting in the applicability of EL.

- **Pillar I Implications**

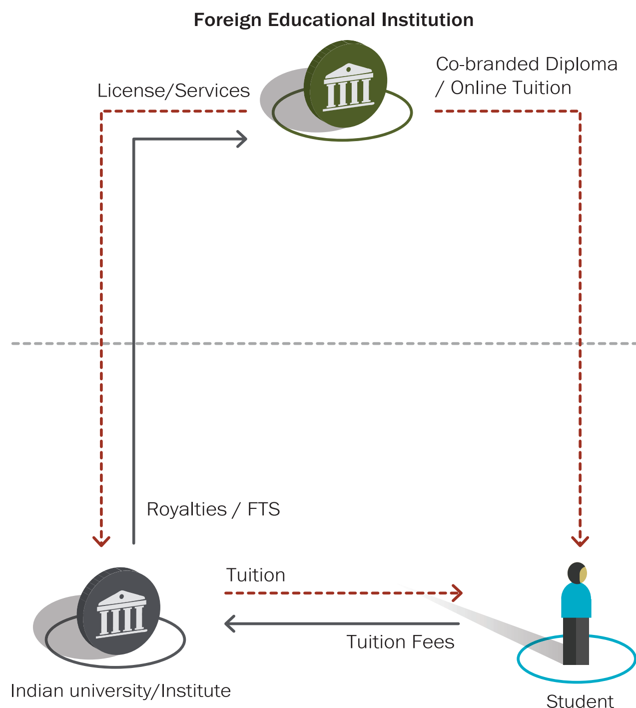
Same as Model I.

- GST implications

Where the Platform collects the tuition fees on its own account, if the services are mostly automated (i.e., the lessons are pre-recorded, with minimal live interaction), they are likely to qualify as OIDAR services, and, since the reverse charge mechanism under GST will not apply to the Indian student, the FEI, should be liable to pay GST at rate of 18%. The FEI would have to comply with mandatory GST registration with tax authorities. However, if the online education service involves some real-time live human involvement, such as live interactive session, then the service, as a B2C service, should not be exempt from GST.

Where the Platform passes the tuition fees through to the FEI, then the FEI may be required to discharge the GST, while the Platform should be exempt from GST as an intermediary.

# III. Model III – Online + On Campus Model



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As FEIs are not allowed to open a campus, or conduct regulated educational programmes independently in India, they enter into license arrangement with Indian educational institutions. Under such an arrangement, the FEIs usually license brand name, curriculum, know-how etc. to the Indian educational institute. Such a license can be granted directly by the FEI to the Indian educational institute, from outside India under an agreement. If the FEI is interested in an India presence, it can even set up an Indian centre (through a private limited company or a limited liability partnership), which offers a license to an Indian educational institute. The Indian educational institute then ends up offering the programmes to students in India, at its campus. Such program, may also involve some online content provided by the FEI, though this content would be accessed by the student at the Indian educational institutes campus. Typically, a certificate of completion is awarded to students at the end of the programme which is usually co-branded in the name of the FEI and Indian educational institute. It is important to note that this structure should be in the nature of a pure licensing arrangement and the FEI should not award any degree or diploma to students in India. Otherwise, the programme may fall under the purview of the regulated sector. Such an arrangement is a win–win for all as (i) the FEIs benefits from the license fee and goodwill generated because of its name being recognized in the Indian market; (ii) the Indian educational institute benefits from the license of curriculum and brand name of the FEI, which enable them to attract students to their institute; and (iii) the students get access to the curriculum and teaching methods of FEI in India itself, thus saving on costs.

In addition to granting a license of the brand, curriculum etc., FEIs may enter into services arrangement with the Indian educational institutes. Under such an arrangement, the FEI may provide services such as advising on standards for evaluation of students, qualification and recruitment of teachers, training teachers, advertising, inputs on infrastructure facilities etc. At times, FEIs also send their teacher and staff to the Indian educational institutes for teacher / student training programmes. The FEIs benefits from such an arrangement as it is able to exercise control over the curriculum, standard of education offered etc. Further, the FEI also earns from the service fee (in addition to license fee). The Indian educational institute benefits from the expertise and experience of the FEIs.

*Analysis*

| Sr. No. | Transaction | Tax Implications |
|---|---|---|
| | The FEI licenses its courses, and provides services to the Indian educational institution, in exchange for consideration. The Indian student pays the Indian Educational institution a tuition fee. | ■ Implications under the ITA<br><br>a. *Taxation of Income from Education under the ITA*<br><br>Under the ITA, and subject to a more comprehensive analysis of the FEI's specific programmes, license fees and service fees earned by a FEI could be taxable under domestic law as fees technical services (**"FTS"**) and royalties respectively at 10% on a gross basis. ITA defines FTS to mean consideration for managerial, technical, or consultancy services, irrespective of whether such services are rendered in India or from outside India.[139] Royalty has a detailed definition under ITA[140] and in summary is understood as meaning being consideration, including lump sum consideration for transfer of rights, including the grant of license in respect of a wide variety of intellectual property (patents, invention, copyrights etc.).<br><br>However, if the FEI has a business connection in India, income attributable to such business connection could instead be taxable at 40% (exclusive of surcharge and cess) on a net basis. The term "business connection" is of wide import and has only been defined in an inclusive manner. It has been judicially interpreted to |

139. Explanation 2 to Section 9(1)(vii) of the Income Tax Act, 1961.

140. Explanation 2 to section 9(1)(vi) of the Income Tax Act, 1961.



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| | | |
|---|---|---|
| | | postulate an element of a real and intimate relation with the territory of India and an element of continuity. It is similar to the concept of "permanent establishment" under tax treaties, though generally, its scope is wider than the scope of permanent establishment under tax treaties. It is possible that the tax authorities could argue that frequent visits by professors from the FEI result in the creation of a business connection in India. If a tax treaty applied, and such visits satisfied the requirements for the creation of a service PE in India, it is possible that income of the FEI attributable to the PE could be taxable in India.<br><br>b. *Taxation of Salary Income under the ITA*<br><br>Under the ITA any 'salary' due from, or paid or allowed by, an employer or former employer to a taxpayer in a taxable year, whether paid or not, is chargeable to income-tax under the head "salaries"[141]. ITA defines the term 'salary' to include, among others, wages, any annuity or pension, any gratuity, any fees, commissions, perquisites or profits in lieu of or in addition to any salary or wages.[142]<br><br>Further, any income which falls under the head 'salaries' is deemed to accrue or arise in India, and is therefore considered taxable in India, if it is 'earned' in India.[143] The law also clarifies that salary payable for service rendered in India shall be regarded as income 'earned' in India for the purposes of the ITA.[144]<br><br>Thus, income in the nature of salary derived by a non-resident from the exercise of his employment in India, even if paid outside India, is ordinarily taxable in India by virtue of section 9(1)(ii) of the ITA, subject to relief under an applicable international tax treaty, as explained below.<br><br>Although salaries paid to visiting faculty of the FEI should not be automatically regarded as having been earned in India, an assessment of the frequency and duration of visits to India would be relevant to determine whether the salaries paid to the FEI are taxable in India.<br><br>c. *AOP Risks*<br><br>An AOP is said to be resident in India in a financial year *"in every case except where during that year the control and management of its affairs is situated wholly outside India".*[145] Hence, as per the provisions of the ITA, an AOP is considered to be a resident in India if the control or management of its affairs is situated *wholly or partially* in India. As a result, once an AOP is considered to be in existence, unless the control and management is wholly situated outside India, the AOP will be considered as an Indian resident for tax purposes.<br><br>In case of collaborations between an FEI and an Indian educational institution where the FEI provides course content, faculty training, etc. and the Indian educational institution is responsible with respect to infrastructure and other on-ground activities, there is a risk that both entities may jointly be treated as an AOP, depending on the nature of relationship between the entities. As the Indian educational institution is resident in India, such an AOP would also be treated as a resident of India. AOP classification could give to significant exposure for FEI as AOPs resident in India are taxable on its worldwide income in India. |

141. Section 15 of the Income Tax Act, 1961.
142. Section 17(1) of the Income Tax Act, 1961.
143. Under section 9(1)(ii) of the Income Tax Act, 1961.
144. Explanation to section 9(1)(ii) of the Income Tax Act, 1961.
145. Section 6(2) of the Income Tax Act, 1961.



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d. *Withholding Taxes under the ITA*

Withholding taxes under the ITA should be applicable on the various streams of income involved in the proposed collaboration, as follows:

- *Withholding taxes on income from education:* Any person (including a non-resident) who is responsible for paying to a resident any sum in the nature of royalty or FTS is required to withhold 10% tax on such sum at the time of credit of such sum to the account of the payee, or at the time of payment why whatever mode, whichever is earlier.[146]

- *Withholding taxes on salary income:* Any person (including a non-resident) responsible for paying any income chargeable to tax under the head “salaries” shall, at the time of payment, deduct income-tax on the amount payable, at the average rate of income-tax computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the taxpayer under the head “salaries” for that financial year.[147]

- *Withholding taxes on taxable income paid to a non-resident:* under section 195 of the ITA, any person (including a non-resident) making a payment of a sum to a non-resident that is chargeable to tax under the ITA (read with the relevant provisions of a tax treaty) is required to withhold tax on such sum at the appropriate rate. Such withholding is required to be made either at the time of payment or at the time of credit of income to the account of the non-resident.

- Tax Treaty Implications

Since the definitions of FTS and royalty under Indian law are quite wide, the FEI should evaluate if it is entitled to benefit under the relevant tax treaty. If the treaty favors, a foreign university may not be required to pay any tax in India. Consequently, withholding tax obligations may also not arise. For instance, the US-India tax treaty provides that teaching in or by educational institutions does not constitute fees for included services. Therefore, US educational institutions should not be subject to tax in India by virtue of the relief under the treaty.

Thus, it is advisable for FEIs to analyze if it is entitled to treaty benefit or is liable to pay tax in India. This analysis should be done in the planning phase itself, as it can prove to be very helpful in the long run.

A similar exemption may be available with respect to salaries earned by personnel of the FEI who visit India to conduct in person courses or training sessions. Several of India’s tax treaties provide for the salaries of foreign residents, including teachers and professors) to be taxed only in their country of residence, unless:

- the recipient is present in India for a period or periods exceeding in the aggregate 183 days in the relevant taxable year

- the remuneration is paid by, or on behalf of, an employer who is a resident of India; and

- the remuneration is borne by a permanent establishment or a fixed base or a trade or business which the employer has in India.

146. Section 194J of the Income Tax Act, 1961.

147. Section 192 of the Income Tax Act, 1961.



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Such an exemption may be available even where the visiting faculty is independent i.e., not employed by the FEI. For example, the India-US Tax Treaty provides for taxation only in the jurisdiction of residence of the visiting individual unless:

- such person has a fixed base regularly available to him in the India for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in India; or

- if the person's stay in India is for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year.

- **Interplay of Fees for Technical Services and SEP**

It is possible that the FEI may be regarded as having a significant economic presence or in India, because, although its activities are essentially limited to licensing its courses and rendering services to its Indian partner, the SEP may be fulfilled event where the transactions of the FEI exceed a certain threshold (not yet specified). While this would be an absurd outcome, since the SEP should ideally only apply in digital context, on a technical interpretation of the SEP provisions are currently worded today, and in the absence of any clarifications, this remains a possibility. The characterisation of consideration received from the IEI also assumes importance vis-à-vis constitution of a business connection. While characterising the fee as a fee for royalty technical services is a more specific treatment, the risk of tax authorities alleging constitution of business connection cannot be ruled out. However, in case a business connection or SEP is constituted in India, the proportion of total income of the FEI attributable to the business connection or SEP will be taxable in India. However, under an applicable tax treaty the FEI may not be liable to tax in India due to non-creation of PE.

If the FEI has a PE in India, irrespective of whether the fees qualify as FTS or royalty, to the extent the fees earned from Indian students are attributable to the PE in India, it should be taxable in India at around 40% on a net basis.

- **Equalisation Levy**

It is unlikely that the EL will apply, since the FEI should not be regarded as an 'e-commerce operators' has that owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both.

- **GST**

The IEI, as a recipient of service should be liable to pay GST at rate of 12% or 18% on reverse charge basis on the consideration paid to the FEI for the license and services. The IEI would have to comply with mandatory GST registration with tax authorities but should be able to avail of GST credit against its outward supplies.



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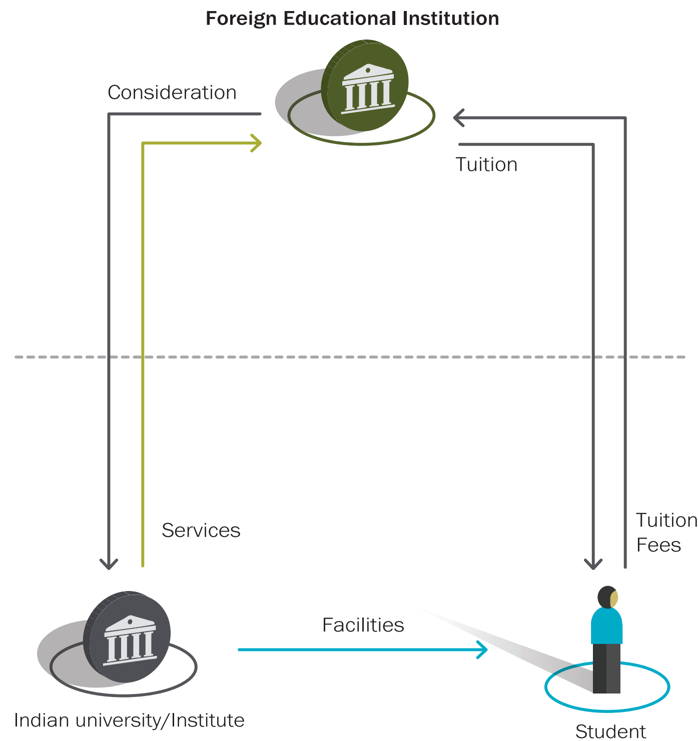
# IV. Model IV – Pathways Program / Credit Transfer




An FEI can engage an Indian service provide who renders services to the FEI. The student enrolls with the Indian service provider who provides an administrator to coordinate the course, which the takes student takes online but from the IEI's campus. The course studied in India is recognized by the FEI by giving credit equivalence to students. The student then transitions to the FEI and completes the course and gets a degree/ diploma. This helps students save costs, allows the FEI to have a brand name in India and the Indian service provider benefits from this model as well.

*Analysis*

| Sr. No. | Transaction | Tax Implications |
|---|---|---|
| | The FEI pays the Indian educational institution for services rendered. The Indian student pays the FEI a tuition fee. | ▪ **Implications under the ITA**<br><br>a. *Taxation of Income from Education under the ITA*<br><br>Under the ITA, and subject to a more comprehensive analysis of the FEI's specific programmes, tuition fees earned by an FEI could be taxable under domestic law as fees technical services (**"FTS"**) and royalties respectively at 10% on a gross basis. ITA defines FTS to mean consideration for managerial, technical, or consultancy services, irrespective of whether such services are rendered in India or from outside India.[148] Royalty has a detailed definition under ITA[149] and in summary is understood as meaning being consideration, including lump sum consideration for transfer of rights, including the grant of license in respect of a wide variety of intellectual property (patents, invention, copyrights etc.). |

148. Explanation 2 to Section 9(1)(vii) of the Income Tax Act, 1961.

149. Explanation 2 to section 9(1)(vi) of the Income Tax Act, 1961.



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However, if the FEI has a business connection in India, income attributable to such business connection could instead be taxable at 40% (exclusive of surcharge and cess) on a net basis. The term "business connection" is of wide import and has only been defined in an inclusive manner. It has been judicially interpreted to postulate an element of a real and intimate relation with the territory of India and an element of continuity. It is similar to the concept of "permanent establishment" under tax treaties, though generally, its scope is wider than the scope of permanent establishment under tax treaties.

b. The IEI would also be taxable in India on the payments received for services rendered. However, there should be no withholding tax requirements for the FEI in this regard. *Taxation of Salary Income under the ITA*

Under the ITA any 'salary' due from, or paid or allowed by, an employer or former employer to a taxpayer in a taxable year, whether paid or not, is chargeable to income-tax under the head "salaries".[150] ITA defines the term 'salary' to include, among others, wages, any annuity or pension, any gratuity, any fees, commissions, perquisites or profits in lieu of or in addition to any salary or wages.[151]

Further, any income which falls under the head 'salaries' is deemed to accrue or arise in India, and is therefore considered taxable in India, if it is 'earned' in India.[152] The law also clarifies that salary payable for service rendered in India shall be regarded as income 'earned' in India for the purposes of the ITA.[153]

Thus, income in the nature of salary derived by a non-resident from the exercise of his employment in India, even if paid outside India, is ordinarily taxable in India by virtue of section 9(1)(ii) of the ITA, subject to relief under an applicable international tax treaty, as explained below.

Several of India's tax treaties provide for the salaries of foreign residents, including teachers and professors) to be taxed only in their country of residence, unless:

- the recipient is present in India for a period or periods exceeding in the aggregate 183 days in the relevant taxable year
- the remuneration is paid by, or on behalf of, an employer who is a resident of India; and
- the remuneration is borne by a permanent establishment or a fixed base or a trade or business which the employer has in India.

Such an exemption may be available even where the visiting faculty is independent i.e., not employed by the FEI. For example, the India-US Tax Treaty provides for taxation only in the jurisdiction of residence of the visiting individual unless:

- such person has a fixed base regularly available to him in the India for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in India; or
- if the person's stay in India is for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year.

150. Section 15 of the Income Tax Act, 1961.
151. Section 17(1) of the Income Tax Act, 1961.
152. Under section 9(1)(ii) of the Income Tax Act, 1961.
153. Explanation to section 9(1)(ii) of the Income Tax Act, 1961.



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c. *AOP Risks*

An AOP is said to be resident in India in a financial year *"in every case except where during that year the control and management of its affairs is situated wholly outside India".*[154] Hence, as per the provisions of the ITA, an AOP is considered to be a resident in India if the control or management of its affairs is situated *wholly or partially* in India. As a result, once an AOP is considered to be in existence, unless the control and management is wholly situated outside India, the AOP will be considered as an Indian resident for tax purposes.

In case of collaborations between an FEI and an Indian educational institution where the FEI provides course content, faculty training, etc. and the Indian educational institution is responsible with respect to infrastructure and other on-ground activities, there is a risk that both entities may jointly be treated as an AOP, depending on the nature of relationship between the entities. As the Indian educational institution is resident in India, such an AOP would also be treated as a resident of India. However, if the role of both parties is distinct, clearly demarcated in the inter-se agreements, there should be minimal AOP risk.

d. *Withholding Taxes under the ITA*

Withholding taxes under the ITA should be applicable on the various streams of income involved in the proposed collaboration, as follows:

- *Withholding taxes on income from education:* Any person (including a non-resident) who is responsible for paying to a resident any sum in the nature of royalty or FTS is required to withhold 10% tax on such sum at the time of credit of such sum to the account of the payee, or at the time of payment why whatever mode, whichever is earlier.[155]

- *Withholding taxes on salary income:* Any person (including a non-resident) responsible for paying any income chargeable to tax under the head "salaries" shall, at the time of payment, deduct income-tax on the amount payable, at the average rate of income-tax computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the taxpayer under the head "salaries" for that financial year.[156]

- *Withholding taxes on taxable income paid to a non-resident:* under section 195 of the ITA, any person (including a non-resident) making a payment of a sum to a non-resident that is chargeable to tax under the ITA (read with the relevant provisions of a tax treaty) is required to withhold tax on such sum at the appropriate rate. Such withholding is required to be made either at the time of payment or at the time of credit of income to the account of the non-resident.

- **Tax Treaty Implications**

Since the definitions of FTS and royalty under Indian law are quite wide, the FEI should evaluate if it is entitled to benefit under the relevant tax treaty. If the treaty favors, a foreign university may not be required to pay any tax in India. Consequently, withholding tax obligations may also not arise. For instance, the US-India tax treaty provides that teaching in or by educational institutions does not constitute fees for included services. Therefore, US educational institutions should not be subject to tax in India by virtue of the relief under the treaty.

154. Section 6(2) of the Income Tax Act, 1961.
155. Section 194J of the Income Tax Act, 1961.
156. Section 192 of the Income Tax Act, 1961.



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Thus, it is advisable for FEIs to analyze if it is entitled to treaty benefit or is liable to pay tax in India. This analysis should be done in the planning phase itself, as it can prove to be very helpful in the long run.

A similar exemption may be available with respect to salaries earned by personnel of the FEI who visit India to conduct in person courses or training sessions.

- **Interplay of Fees for Technical Services and SEP**

The characterisation of tuition fees assumes importance vis-à-vis constitution of SEP. While characterising the tuition fee as a fee for technical services is a more specific treatment, the risk of tax authorities alleging constitution of SEP cannot be ruled out. The tax authorities may allege constitution of 'business connection' through SEP test as the FEI is engaged in transaction in respect of services with students in India, resident in India. Pertinent to note that constitution of SEP depends on transaction value or number of users – the thresholds of which are yet to be notified. In case SEP is constituted in India, the proportion of total income of the FEI / Platform attributable to the SEP will be taxable in India. However, in absence of any amendment in the tax treaties in relation to SEP, the Platform / FEI may not be liable to tax in India due to non-creation of PE.

- **Equalisation Levy**

It is unlikely that the EL will apply, since the FEI should not be regarded as an 'e-commerce operators' has that owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both.

- **GST**

The IEI, as an exporter of service should be exempt from GST. Similarly, the FEI should be exempt from GST as its services are rendered in a B2C i.e., to an Indian student. The services provided by the FEI should not constitute OIDAR, since they are rendered to the student within the confines of the IEI's campus.



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# Research @ NDA

**Research is the DNA of NDA.** In early 1980s, our firm emerged from an extensive, and then pioneering, research by Nishith M. Desai on the taxation of cross-border transactions. The research book written by him provided the foundation for our international tax practice. Since then, we have relied upon research to be the cornerstone of our practice development. Today, research is fully ingrained in the firm's culture.

Our dedication to research has been instrumental in creating thought leadership in various areas of law and public policy. Through research, we develop intellectual capital and leverage it actively for both our clients and the development of our associates. We use research to discover new thinking, approaches, skills and reflections on jurisprudence, and ultimately deliver superior value to our clients. Over time, we have embedded a culture and built processes of learning through research that give us a robust edge in providing best quality advices and services to our clients, to our fraternity and to the community at large.

Every member of the firm is required to participate in research activities. The seeds of research are typically sown in hour-long continuing education sessions conducted every day as the first thing in the morning. Free interactions in these sessions help associates identify new legal, regulatory, technological and business trends that require intellectual investigation from the legal and tax perspectives. Then, one or few associates take up an emerging trend or issue under the guidance of seniors and put it through our "Anticipate-Prepare-Deliver" research model.

As the first step, they would conduct a capsule research, which involves a quick analysis of readily available secondary data. Often such basic research provides valuable insights and creates broader understanding of the issue for the involved associates, who in turn would disseminate it to other associates through tacit and explicit knowledge exchange processes. For us, knowledge sharing is as important an attribute as knowledge acquisition.

When the issue requires further investigation, we develop an extensive research paper. Often we collect our own primary data when we feel the issue demands going deep to the root or when we find gaps in secondary data. In some cases, we have even taken up multi-year research projects to investigate every aspect of the topic and build unparallel mastery. Our TMT practice, IP practice, Pharma & Healthcare/Med-Tech and Medical Device, practice and energy sector practice have emerged from such projects. Research in essence graduates to Knowledge, and finally to *Intellectual Property*.

Over the years, we have produced some outstanding research papers, articles, webinars and talks. Almost on daily basis, we analyze and offer our perspective on latest legal developments through our regular "Hotlines", which go out to our clients and fraternity. These Hotlines provide immediate awareness and quick reference, and have been eagerly received. We also provide expanded commentary on issues through detailed articles for publication in newspapers and periodicals for dissemination to wider audience. Our Lab Reports dissect and analyze a published, distinctive legal transaction using multiple lenses and offer various perspectives, including some even overlooked by the executors of the transaction. We regularly write extensive research articles and disseminate them through our website. Our research has also contributed to public policy discourse, helped state and central governments in drafting statutes, and provided regulators with much needed comparative research for rule making. Our discourses on Taxation of eCommerce, Arbitration, and Direct Tax Code have been widely acknowledged. Although we invest heavily in terms of time and expenses in our research activities, we are happy to provide unlimited access to our research to our clients and the community for greater good.

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