

Taxability of Digital Goods & Services – An Indian Perspective

- May 4, 2023



AKM GLOBAL
TAX | CONSULTING | OUTSOURCING



Rising Star Association



INTERNATIONAL ACCOUNTING BULLETIN

Welcome – This Webinar Will Begin Momentarily



Housekeeping Items

- ☐ This webinar will be recorded.
- ☐ The link to the recording and PowerPoint will be posted on the Events registration page on LEA's member portal post webinar. An email will also be sent to today's attendees with this information.
- ☐ Please use the chat box to share comments or questions.
- ☐ This webinar is eligible for 1 Continuing Professional Education (CPE) credit.
- ☐ Four (4) polling questions – will be initiated throughout this webinar to monitor engagement as required by NASBA standards.
- ☐ Your CPE certificate will be emailed to you in a couple of weeks.
- ☐ You will receive an email asking you to complete an evaluation of this webinar. Please take time to complete this as your input is valuable when planning for future webinars.

Today's Presenter(s)



Amit Maheshwari

Managing Partner and
International Tax Lead



Sandeep Sehgal

Partner, Tax



Ikesh Nagpal

Head- Indirect Taxes



AKM GLOBAL

TAX | CONSULTING | OUTSOURCING

Table of Contents

- ❑ Digital Goods and Services
- ❑ Indirect Tax
 - E-commerce models, Issues
 - OIDAR services
 - Compliances
- ❑ Direct Tax
 - Equalisation Levy (EL) – Evolution and overview
 - Significant Economic Presence
 - Compliances and Conundrums
 - Emerging challenges
- ❑ Taxation of other digital goods and services
- ❑ BEPS 2.0: Pillar I and Pillar II with a case study on Permanent Establishment

Digital Goods and Services



- ☐ E-Commerce
- ☐ SAAS, PAAS, Cloud Services
- ☐ OIDAR
- ☐ AR/VR
- ☐ Crypto/NFTs

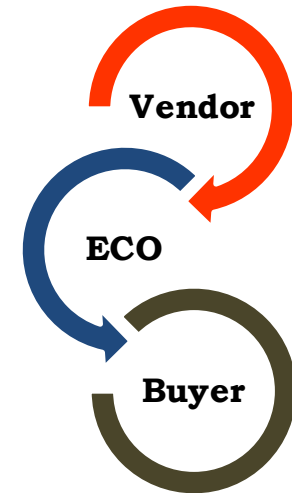
E-commerce

E-Commerce

- ☐ Buying and selling of goods or services;
- ☐ over the internet or other electronic networks;
- ☐ using electronic means such as computers, smartphones, or other internet-enabled devices.

E-Commerce Operator:

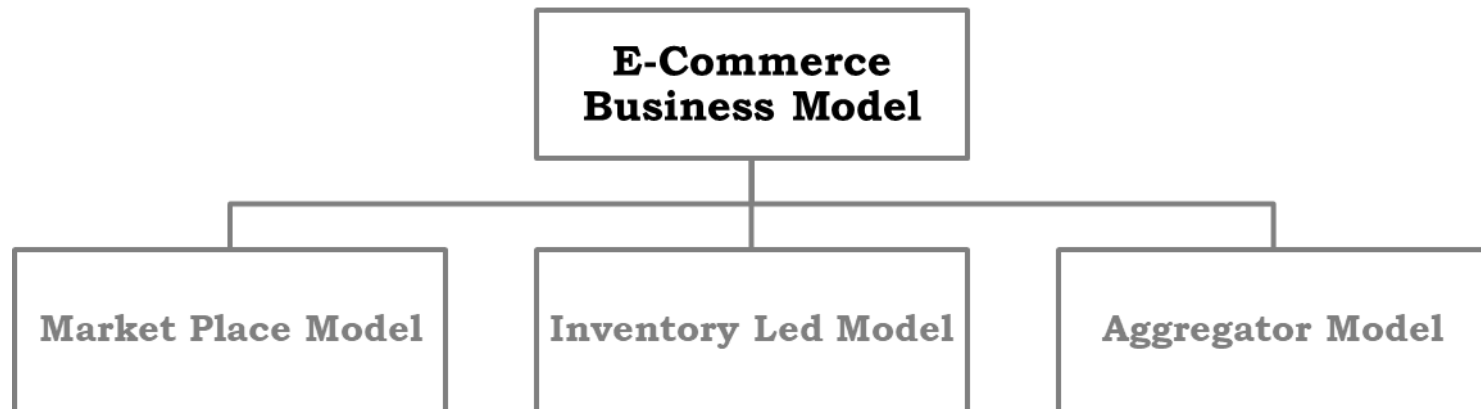
- ☐ An e-commerce operator is an individual, company, or organization
- ☐ provides an online platform or marketplace
- ☐ To facilitate electronic commerce transactions between buyers and sellers.



TATA
CLiQ



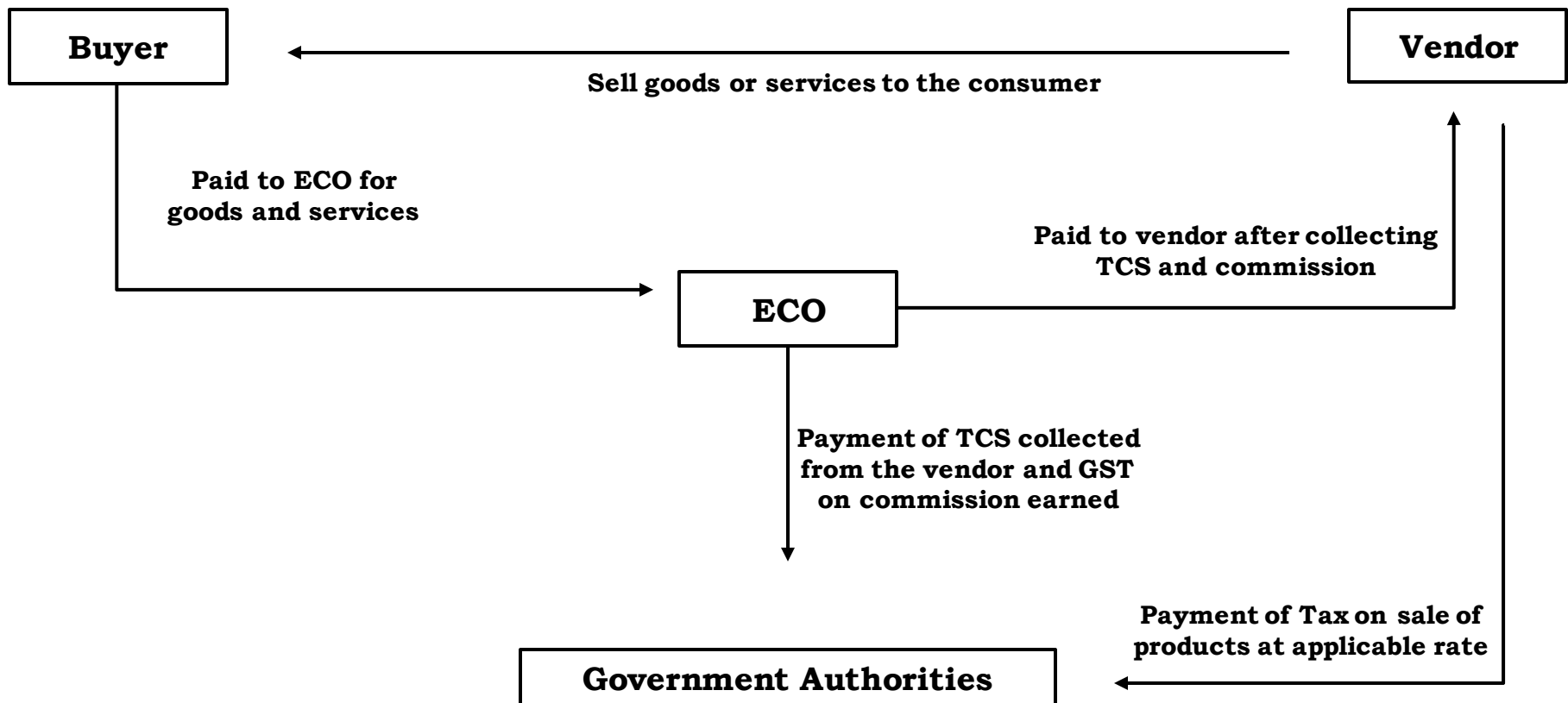
Uber



INDIRECT TAX

Market Place Model

Under this model, ECO acts as a facilitator between the vendor and the buyer.



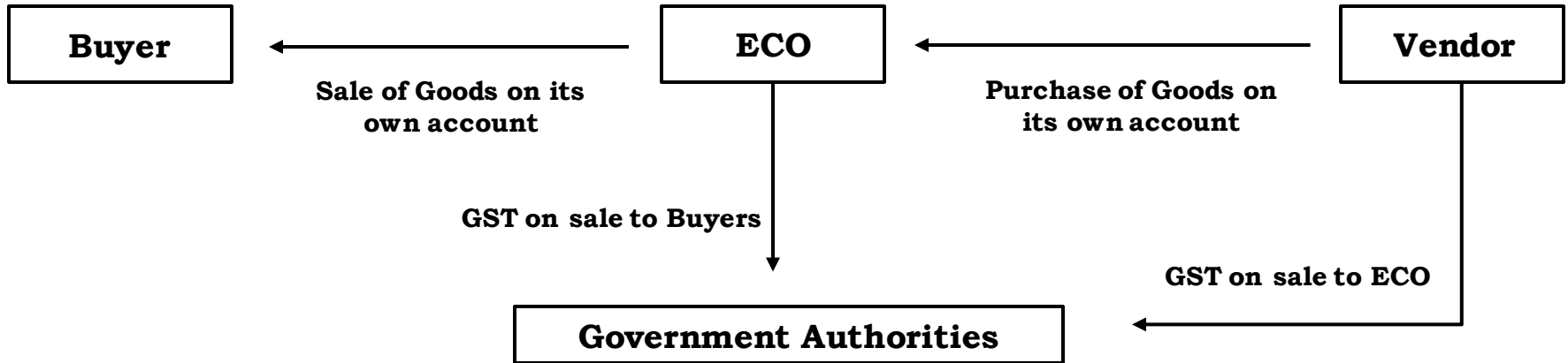
Issues related to Market Place Model

Potential Challenges Encountered in Various Marketplace Model Situations:

1. Registration under GST:
2. TCS Compliance
3. Discount provided by ECO to the consumers
4. Place of Supply
5. Customer to Customer Sales
6. More than one ECO
7. TCS in case of payment collected by payment agencies

Inventory Led Model

Under this model, ECO purchases and maintains inventory of goods/services and Sell directly to the consumers.

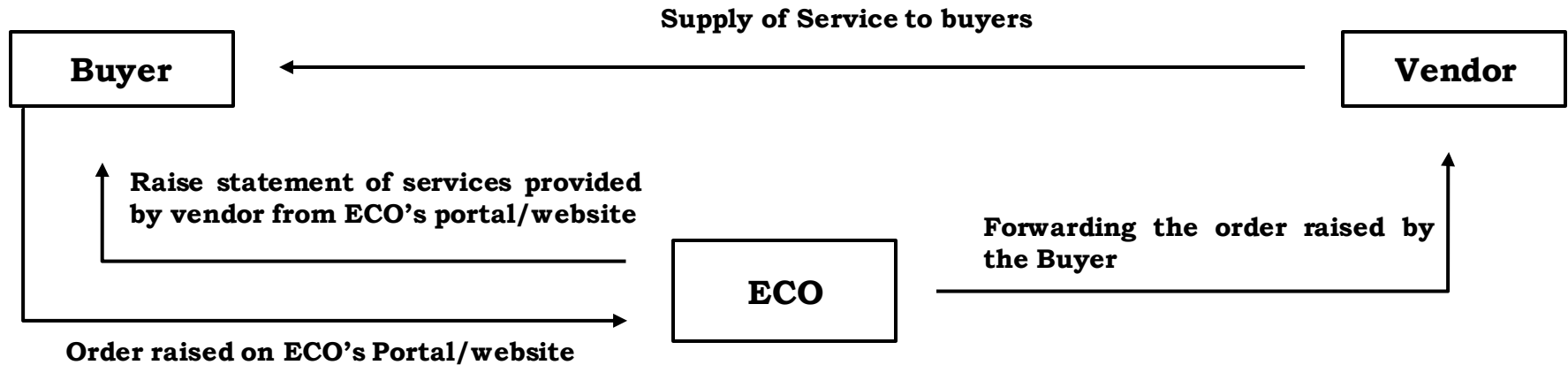


Potential Challenges Encountered in Inventory Led Model Situations:

- Registration under GST
- Input Tax Credit
- Place of supply
- Valuation

Aggregator Model

Under this model, E-Commerce platform connects a large number of unorganized merchants with the large number of buyers at their own image/ brand.



Applicability of special Provision under GST, where ECO is liable to pay GST on certain services namely;

- Hotel Accommodation services
- Passenger transportation services
- House-keeping services such as plumbing, carpentering etc;
- Restaurant Services

Issues related to Aggregator Model

Potential Challenges Encountered in Various Marketplace Model Situations:

1. Input Tax Credit
2. Place of supply
3. Valuation

Polling Question - 1

☐ **What are the various types of e-commerce model?**

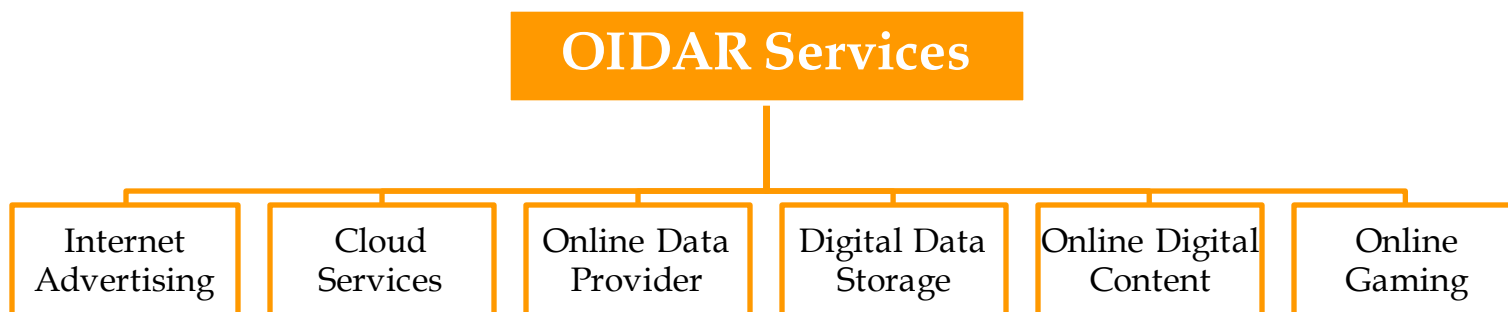
- A. MarketPlace Model
- B. Inventory Led Model
- C. Aggregator based model
- D. All of the above

OIDAR Services

Meaning of OIDAR Services: OIDAR Stands for Online Database Access and Retrieval services. These services are provided through a medium of Internet and these services are received as a non physical interface by the recipient of these services. **For example:** Online webinars, Downloading of an e-book, online gaming etc.

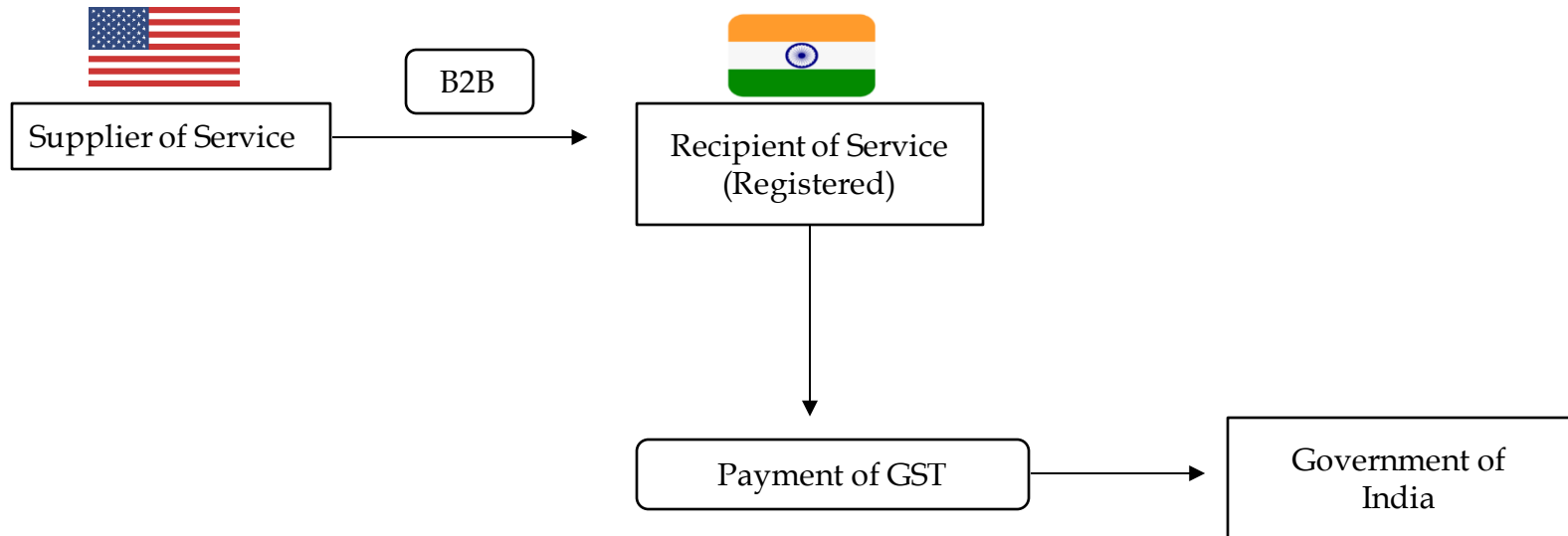
Conditions for qualifying as an OIDAR Services:

- ☐ Services whose delivery is mediated through internet or electronic network;
- ☐ The services cannot be provided in absence of Informational Technology; and
- ☒ ~~Services are essentially automated and it involves minimal human interventions.~~



Taxability of OIDAR Services

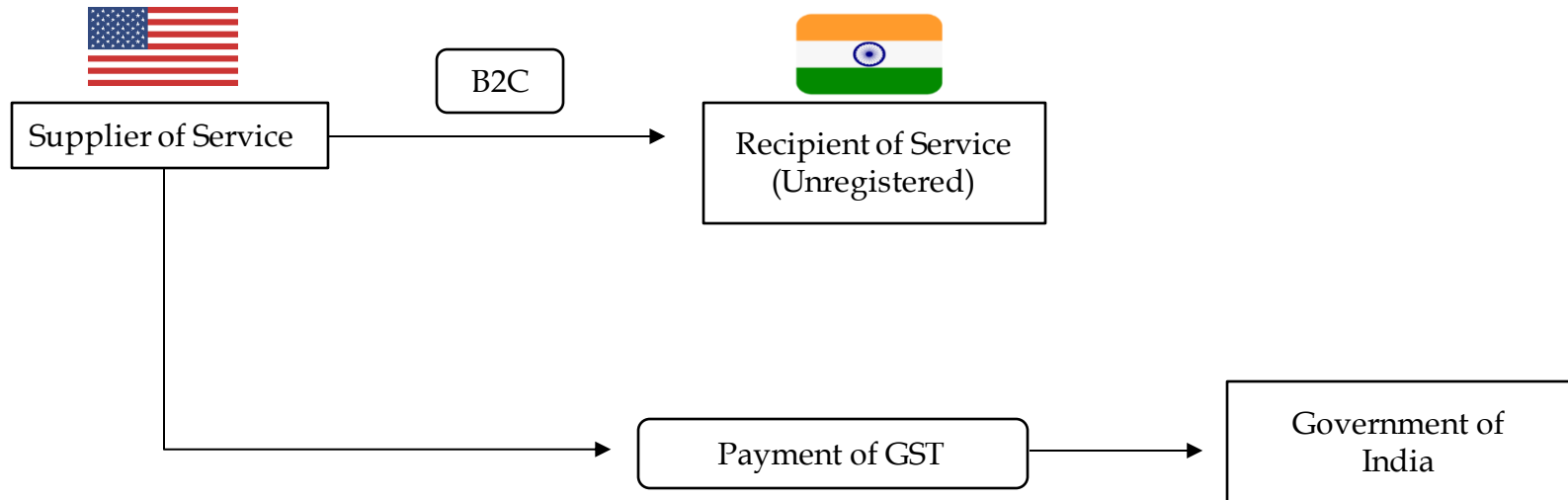
The supplier is located outside India, but Recipient (Registered) is located in India



Recipient is liable to pay tax under Reverse Charge

Taxability of OIDAR Services

The supplier is located outside India, but Recipient (Unregistered) is located in India



Supplier is liable to pay tax under Forward Charge

Compliance under Indirect Tax

Matching Concept

- Incurrence of Additional GST Obligations due to unreconciled revenue discrepancies

Registration requirements

- TCS registration in every state where the supplier is located

Supplier wise disclosure

- Calculation and Presentation of Supplier-specific and Monthly Tax Collected at Source (TCS)

TCS rate

- A tax rate of 1%, comprising either 0.5% CGST and 0.5% SGST, or alternatively, 1% IGST.

Additional TCS Return

- E-commerce operator to file a Monthly Return in FORM GSTR-8

Compliance under Indirect Tax

Compliance for ECO:

- ❑ ECO as well as a person who supplies goods or services or both through ECO is required to obtain registration under GST;
- ❑ TCS of 1% of “Net Value of Taxable Supplies” is required to be collected on the payments collected by ECO;
- ❑ **Returns:** Details of Outward supplies, Monthly Return, Annual Return, Reconciliation Statement, TCS Return.

Compliance for Vendors:

- ❑ The vendor is required to obtain registration under GST;
- ❑ TCS: Acceptance of TCS credit through GSTR-8A;
- ❑ **Returns:** Details of outward supplies, Monthly Return, Annual Return, Reconciliation statement.

Polling Question - 2

☐ What does ECO stands for?

- A. E-Commerce Operator
- B. E-Common Operator
- C. Both A & B
- D. None of the Above

DIRECT TAX

Background of EL

❑ BEPS Action Plan:

- More than 135 countries, including India have agreed to implement their BEPS Measures.
- India has adopted 9 out of 15 Action Plans, namely:
 - Action Plan 1: Address the tax challenges of Digital economy
 - Action Plan 4: Interest deductions and other financial payments
 - Action Plan 5: Countering harmful tax practices more effectively
 - Action Plan 6: Preventing treaty abuse
 - Action Plan 8-10: Align Transfer pricing outcomes with value creation.
 - Action Plan 13: To re-examine the Transfer Pricing Documentation
 - Action Plan 15: Multilateral Instruments.

❑ Equalization Levy:

- EL 1.0 introduced in India in 2016 to tax online advertising.
- EL 2.0 covers digital services.

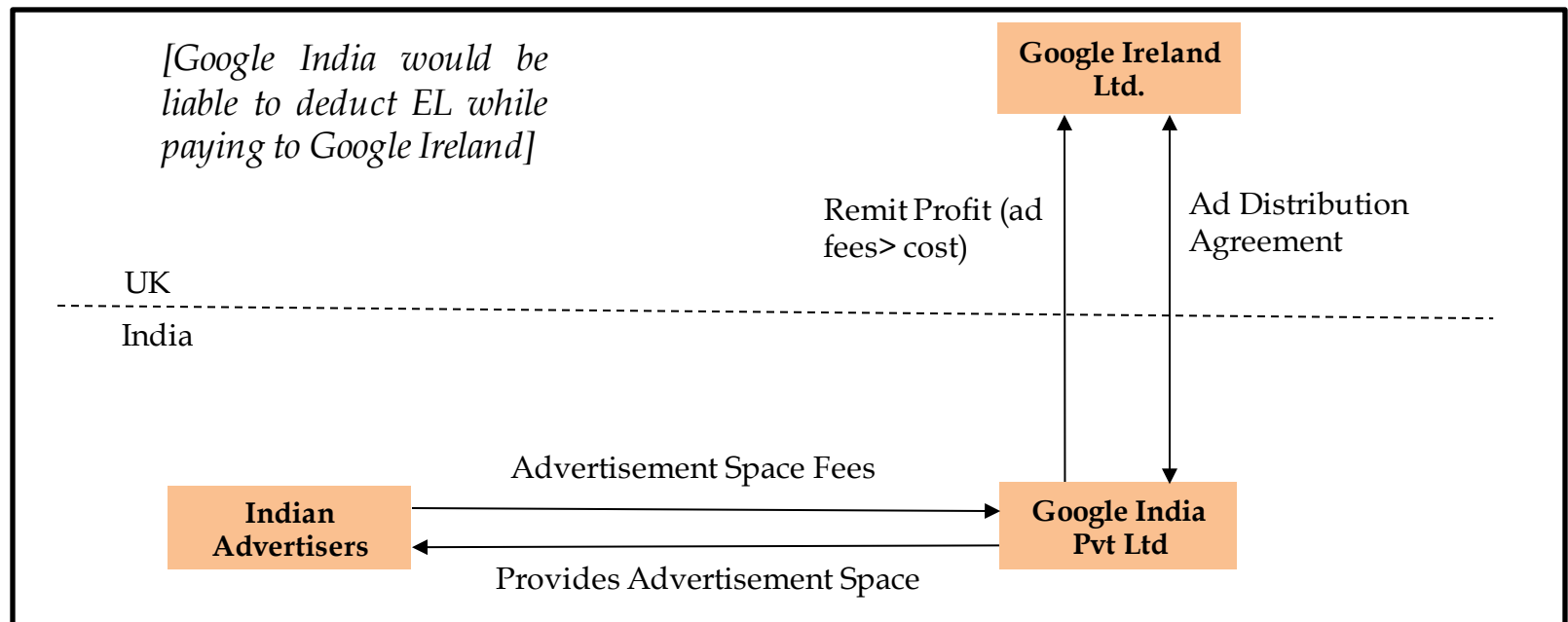
❑ Multilateral Instruments:

- MLIs aims to **prevent tax-treaty abuse** and enable the countries to modify their bilateral treaties without replacing existing tax treaties.
- Around 94 countries have signed the MLIs and are kept open for signature by other countries.
- It relies on the **voluntary actions** of nations.

Evolution of EL

❑ Case of Google India (P.) Ltd. v. Deputy Commissioner of Income-tax (International Taxation):

- Consideration received for sale of advertisement space on website is not covered under the definition of Royalty/Fee for Technical Service as per Article 12 of India-Ireland Treaty.
- It was held that such income shall not be taxable in the absence of PE of such foreign entity in India.
- EL 1.0 seeks to cover such other digital transactions (including advertisement space) which are presently outside the coverage of the present treaty provisions.



Evolution of EL

EL 1.0 introduced for the first time in 2016

- ❑ EL 1.0 is applicable at 6% on transactions such as online advertisement, digital advertising, and related services provided by non-residents.
- ❑ EL 1.0 exemption on the amount received by Non-resident service providers below USD 1,200 (approx.)
- ❑ EL 2.0 was introduced in 2020 at 2% on the consideration received/receivable by the non-resident e-commerce operator.

Applicability of EL 2.0	Recipient
Online sale of goods owned by non-resident ecommerce operator (ECO)	Any person resident in India
Online provision of services provided by ECO	Any person who buys goods or services (or both) using Indian IP address
Online sale of goods or provision of services (or both), facilitated by ECO	
Sale of advertisement which targets an Indian resident customer, through an Indian IP Address	Any non-resident in respect of offshore sale of advertisements
Sale of data collected from an Indian resident or a person who uses an Indian IP address	Any non-resident to whom data collected from an Indian resident is sold

Overview of EL 2.0

EL 2.0 does not apply when:

- ECO has a PE in India and such supply of goods/ services is effectively connected to such PE,
- **EL 1.0 @ 6%** is applicable on such transactions, or
- **Turnover** of ECO is less than INR 20 Million (~USD 243,000)

Important note:

- The income chargeable to EL (both 1.0 and 2.0) shall be exempt from tax under the Indian corporate tax law.
- EL 1.0 levy to be discharged by resident Indian payer
- EL 2.0 levy to be discharged by the non-resident e-commerce operator

Significant Economic Presence (A concept under the domestic law)

SEP was introduced in 2018 to tackle the loss of tax revenue due to innovative business model and to tax enterprises based on factors other than physical presence in the country.

Applicability

- Transaction of goods, services or property by non-resident exceeding INR 20 Million (~ **USD 243,000**)
- Systematic and soliciting of business activities with **3,00,000 users** in India.

Interplay of SEP and Tax Treaty

- No impact on the tax liability of non-resident since tax treaty provides favorable tax regime.

EL	SEP
EL is applicable on certain e-commerce services.	SEP has wider application applicable to every digital services deriving gain from India
The services chargeable to EL are exempt from tax under the Indian corporate tax law	Treaty benefits can be availed

Polling Question - 3

☐ **Do you know that India has introduced Equalisation Levy (EL)**

A. Yes, EL 1.0 and EL 2.0

B. No

Emerging Challenges in Digital Services

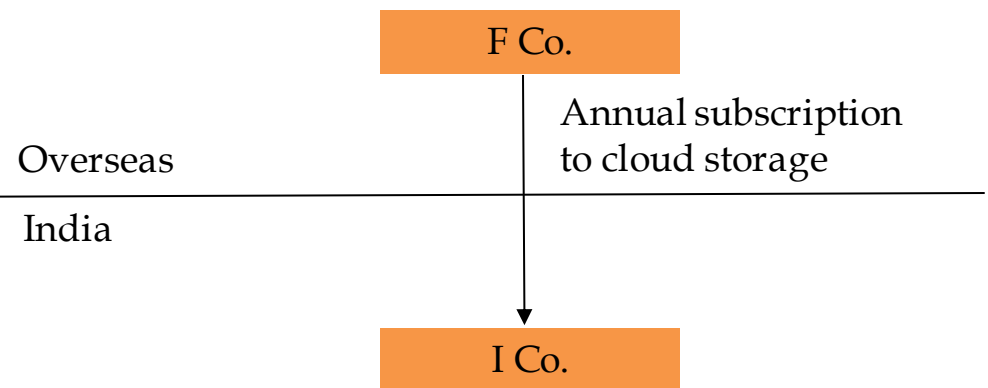
- No credit of EL allowed
- Separate charge, so tax treaty benefit is not available.
- There is no mechanism to claim refund of EL or to adjust it with income-tax payable.
- No mechanism for adjustment of sales return with the consideration received for EL.

Controversy with Royalty and FTS

Facts: I Co. purchases annual subscription and gets cloud storage space for the storage of data from F Co.

Issues:

- Whether payment would be covered under Royalty/FTS?
- Whether equalization levy payable by the foreign company?



Emerging Challenges in Digital Services

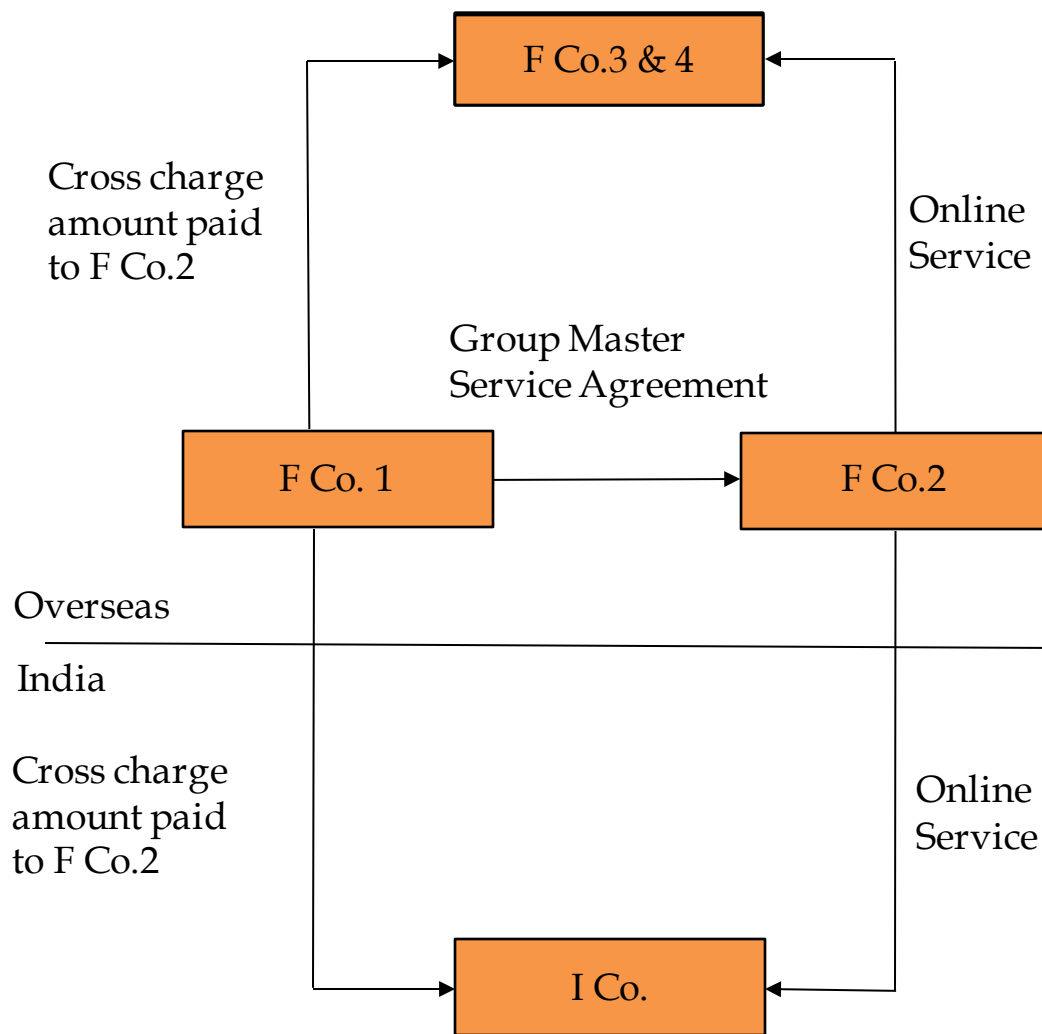
Controversy on royalty and FTS

Facts:

- F Co.1 enters into a master service agreement with foreign Co. 2 for services to be rendered to many group companies i.e., I Co., F Co.3 & F Co.4.
- F Co.2 renders services to all group companies including I Co. in India.

Issues:

- Whether the equalization levy applies?
- If yes, how to apportion the amount to services provided to I Co.?
- Whether tax u/s 195 is deductible on payment to F Co.1 by I Co.?



Compliance under Direct Tax

☐ Onus to pay

- EL 1.0 – Resident Indian
- EL 2.0 – Non-resident e-commerce operator

- ☐ Equalisation Levy Statement (Form-1) is to be furnished on or before 30th June of the financial year.
- ☐ In case there is a delay in payment - Interest is charged at 1 % of the outstanding levy for every month or part thereof is delayed.

Direct Tax Conundrum in taxing Digital goods and services

- ❑ Tax issues in taxing Digital goods and services are elucidated as:
 - No Advance Ruling mechanism for EL leads to uncertainty and litigations.
 - Undue compliance burdens include obtaining PAN, filing tax returns, depositing EL and filing EL statements, etc.

Taxation of other digital goods and services

Particulars	Applicability
SAAS, PAAS, Cloud Services	➤ Royalty if there is a right to use the intellectual property. Otherwise, EL implications would need to be examined.
Inventory led model	➤ Considered as having a business connection or permanent establishment in India. ➤ If the non-resident e-commerce operator has a turnover of more than INR 20 Million (~USD 243,000) in a financial year, they will be required to pay EL at the rate of 2% of the amount of consideration received for the supply of goods or services made to Indian residents.
Market Place/ Aggregator based model	➤ The EL will be applicable on the consideration received or receivable by the non-resident e-commerce operator, and not on the transaction value or commission earned by the e-commerce operator.
AR/VR	➤ PE exposure would need to be examined
Crypto/NFTs	➤ A special tax rate of 30% plus applicable surcharge and cess under the Indian domestic law
Virtual currencies	➤ A special tax rate of 30% plus applicable surcharge and cess under the Indian domestic law

Pillar I, Pillar II and the way forward

❑ Introduction:

- To tax the digital economy, the Two Pillar approach has been formulated.
- The final implementation plan for the two pillars was introduced in October'21, however, the implementation might occur in 2023.

❑ Overview:

- **Pillar I- *The Unified Approach*:**
 - Focuses on allocation of taxing rights between jurisdictions, profit allocation and nexus rules.
 - Approach seeks to accommodate new business models and expand taxing rights.
- **Pillar II- *Global Anti-base Erosion Rules (GLoBE)*:**
 - Coordinated set of rules to address profit shifting and unhealthy tax competition.
 - Proposed as a 'top up' tax to a minimum effective tax rate to provide level playing field for jurisdictions and taxpayers.

BEPS 2.0: Pillar 1 and Pillar 2

❑ Way Forward:

- The application of the Two-Pillar approach is expected to bring significant changes in the existing tax system.
- Countries like India are expected to benefit from this regime due to a large customer base for digital services.

The table elucidated below highlights both the positive impacts and the potential issues in relation to the OECD Pillar Approach.

Potential Positive Impact	Potential Issues
Prevents Profit Shifting and Base Erosion	Social Issues- countering the 'race to the bottom'
Minimizing Tax Burden on Consumers and Labour	Political Issues
Revenue Generation	Economic Issues
Incentivize tax havens to levy a tax themselves	Implementation Issues
Eliminate Race to the bottom Tax Competition	Increased Complexities and Procedural Compliances

Polling Question-4

☐ What is the purpose of two pillar approach?

A. To tax the digital economy

B. Not to tax the digital economy

Galileo International Inc*. *[2008] 19 SOT 257 (Delhi)

Computer reservation services and PE

Facts:

- ❑ The US co., a resident of USA, was engaged in the business of maintaining and operating the system for providing electronic global distribution services to airlines, hotels, tour and cab operators by connecting to Travel Agents (TAs) utilising a Computerized Reservation System (CRS).
- ❑ CRS would receive, process, store and disseminate data about flight schedules, room availability, fare information and provision for booking capabilities, etc. It maintained and operated a huge Master Computer System (MCS) in USA, which was connected, inter alia, to airlines' servers to/from which relevant data regarding flight schedules, seat availability, fare structures, flight connections, availability of facilities, etc., on a real-time basis was continuously sent and obtained.
- ❑ The US co. entered into a Distribution Agreement (DA) with an Indian company 'I'. 'I', which in turn, entered into a subscribers agreement with various travel agents (TA) to provide them with access codes, equipment, communications link and support services.
- ❑ The master computer system of the US co. was connected to TAs in India through a communication network arranged by a separate organization ('SITA'). The US co. at its own cost, had obtained connectivity services from its Data Centre in USA to the nodes of SITA in India.

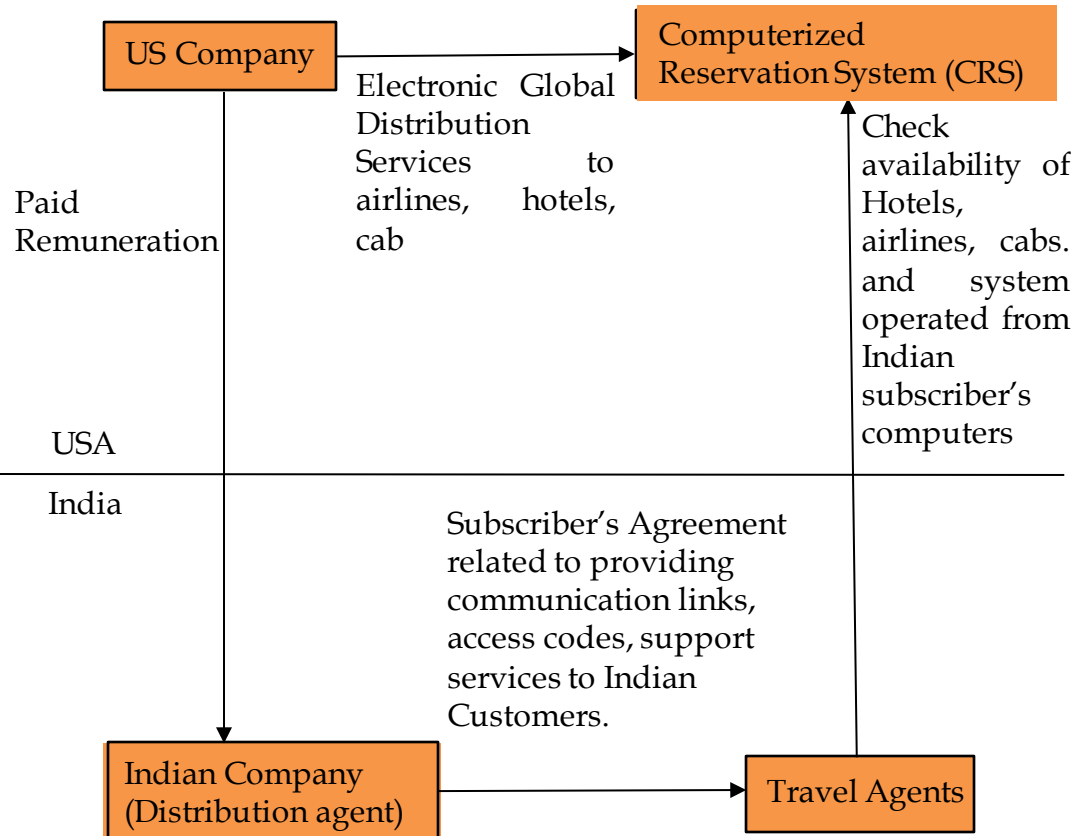
Galileo International Inc*. *[2008] 19 SOT 257 (Delhi)
Computer reservation services and PE

Issues:

❑ **Whether a US Co. had a PE in India?**

The CRS, which was the source of revenue was partially existent in the machines, namely, various computers installed at the premises of the subscribers. In some cases, the US co. itself had placed those computers and in all the cases the connectivity in the form of nodes leased from SITA were installed by the US co. through its agent. The US co. exercised complete control over the computers installed at the premises of the subscribers, which would amount to a fixed place of business for carrying on the business of the enterprise in India.

There is also existence of agency PE. However, the income attribution shall be NIL since the remuneration paid to the Indian agent exceeded the profits attributable to India.



The similar facts were reported in a recent apex court ruling in the case of Travel Port Inc [TS-218-SC-2023]

Contact Us

Head Office

Suite # 321, Tower A, Spaze I-Tech Park,
Sector - 49, Sohna Road,
Gurgaon - 122018, Haryana, India

Phone No: +91 124 6647500

Mobile No: +91 9810188104, +91 9811987402

Email: amit@akmglobal.com, sandeep.sehgal@akmglobal.in,
yeeshu.sehgal@akmglobal.in

www.akmglobal.com

Branches

Bengaluru | Delhi | Hyderabad | Mumbai | Pune | Singapore

