

India proposes equalization levy on digital e-commerce transactions in 2016 budget

EY Global Tax Alert Library

Access both online and pdf versions of all EY Global Tax Alerts.

Copy into your web browser:

www.ey.com/taxalerts

Executive summary

Under Action 1 of the Organisation for Economic Co-operation and Development's (OECD's) base erosion and profit shifting (BEPS) Action Plan, the OECD had considered, *inter alia*, an equalization levy (i.e., a tax to equalize the tax burden on remote and domestic suppliers of similar goods and services) as one option to tax digital transactions. While the final Action 1 report released in October 2015 (see EY Global Tax Alert, *OECD issues final report on the tax challenges of the digital economy under Action 1*, dated 23 October 2015), did not recommend introducing such a levy as an internationally agreed standard at this stage, it did state that countries could introduce one in their domestic laws as an additional safeguard against BEPS, provided they respect existing treaty obligations, or include them in their bilateral tax treaties.

In the Indian fiscal budget presented on 29 February 2016, Finance Minister Arun Jaitley proposed inserting a new chapter titled *Equalization Levy* in the Finance Bill 2016 to provide for an equalization levy of 6% of the amount of consideration for specified services received or receivable by a nonresident not having a permanent establishment (PE) in India, from a resident in India who carries out business or profession, or from a nonresident having a PE in India.

This Alert summarizes the key provisions relating to this levy.

Detailed discussion

Equalization levy

The equalization levy has been defined as “tax leviable on consideration received or receivable for any specified service under the provisions of this chapter.”

The levy would fall under a separate, self-contained code and would not be part of the *Income Tax Act, 1961*.

Services covered

The equalization levy would apply at a rate of 6% on the gross consideration payable for a “specified service.”

Specified service is defined as follows:

- ▶ Online advertisement
- ▶ Any provision for digital advertising space or any facility/ service for the purpose of online advertisement
- ▶ Any other service which may be notified later by the central government

The Finance Minister in his budget speech stated that the equalization levy is aimed at taxing business-to-business (B2B) e-commerce transactions. Therefore, the scope of the levy may be expanded to cover a wider range of digital goods and services as time progresses.

Applicability

The levy will be applicable on the payments received by a nonresident service provider from an Indian resident or an Indian PE of a nonresident in respect of the specified service.

The levy would not be applicable to nonresident service providers having a PE in India, as they will be subject to regular PE-basis taxation. The levy is currently applicable only on B2B transactions, if the aggregate value of consideration in a year exceeds approximately US\$1,500.

Date of applicability and treatment of income under income tax law

The Government will notify the date from which this provision shall be effective.

To avoid double taxation of income which has been subject to an equalization levy, such income will be exempt in the hands of the nonresident under the *Income Tax Act, 1961*.

However, one would need to evaluate the possibility of claiming a tax credit for such levy in the home country of the nonresident service provider.

Who needs to comply

Every resident person and foreign company (having a PE in India) is required to withhold the equalization levy when making payment to a nonresident service provider. The compliance procedure is similar to withholding tax provisions already prevalent in India.

While the compliance obligation is largely on Indian residents, the levy would be withheld when making payment to nonresident service providers. Service recipients are required to comply and also file an annual statement in respect of services received.

Delayed payment carries a fee of simple interest at 1% of the outstanding levy for every month or part thereof that payment is not made.

Consequences of noncompliance by service recipient

- ▶ Penalty for failure of payment:
 - Equalization levy was not deducted: The penalty is equal to the amount of the levy that the assessee failed to deduct (along with interest and the outstanding levy amount)
 - Equalization levy was deducted but not deposited: The penalty is equal to INR1,000 for each day the failure continues, but not to exceed the amount of the equalization levy that the assessee failed to pay (along with interest and the outstanding levy amount)
 - Disallowance of such expenditure in the hands of the payer (unless the defect is rectified)
- ▶ Penalty for failure to file statement of compliance: INR100 for each day the noncompliance continues
- ▶ Prosecution: If a false statement has been filed, the person may be subject to imprisonment of a term of up to three years and a fine

Other issues

As with other cases of remittance in India, it would be in the ordinary course of business for an Indian service recipient to ask the nonresident service provider for a “No PE” declaration in order to enable the recipient to decide on the applicability of the equalization levy.

Online advertising services are separately subject to service tax at a rate of 14.5% (the Finance Bill 2016 proposes increasing that rate to 15%) on a reverse charge basis which is to be collected and discharged by the Indian service recipient.

Impact

This is the first significant step taken by India to tax digital economy transactions. As the other services and rules relating to the proposed equalization levy are notified, we will have better insights into the scope and intent of the levy.

For additional information with respect to this alert, please contact the following:

Ernst & Young LLP (India), Mumbai

▶ Sudhir Kapadia +91 22 6192 0900 sudhir.kapadia@in.ey.com

Ernst & Young LLP (India), Hyderabad

▶ Jayesh Sanghvi +91 40 6736 2078 jayesh.sanghvi@in.ey.com

Ernst & Young LLP, Indian Tax Desk, New York

▶ Riad Joseph +1 212 773 4496 riad.joseph1@ey.com
 ▶ Amit Gouri +1 212 773 7096 amit.gouri1@ey.com
 ▶ Sameep Uchil +1 212 773 4862 sameep.uchil@ey.com

Ernst & Young LLP, Indian Tax Desk, San Jose

▶ Neeraj Khubchandani +1 408 947 5600 neeraj.khubchandani@ey.com

Ernst & Young LLP, Indian Tax Desk, Chicago

▶ Romit Patel +1 312 879 2526 romit.patel1@ey.com

Ernst & Young LLP, Asia Pacific Business Group, New York

▶ Chris Finnerty +1 212 773 7479 chris.finnerty@ey.com
 ▶ Kaz Parsch +1 212 773 7201 kazuyo.parsch@ey.com
 ▶ Bee-Khun Yap +1 212 773 1816 bee-khun.yap@ey.com

Ernst & Young Asia Pacific Business Group, Houston

▶ Trang Scott +1 713 751 5775 trang.scott@ey.com

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

© 2016 EYGM Limited.
All Rights Reserved.

EYG no. CM6293

1508-1600216 NY
ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com