



## **Taxation Issues in Online Marketing in India**

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### **ABSTRACT**

The rapid pace of growth of the e-commerce industry is not only indicative of the increasing receptiveness of the public but has also brought to the fore the issues that the legal system of the country has been faced with. The e-commerce sector has advanced significantly from the early years when the internet was a novel phenomenon to more recently when it has become a fundamental requirement for every family in most major cities. With the adoption of several laws under the Information Technology Act, of 2000 to address a variety of problems arising from the usage of the Internet, the legal system has continuously attempted to catch up. Furthermore, individuals are now able to simply copy content and deceive other users because of new IP concerns that have emerged in e-commerce transactions. So, much more is required in order to successfully control the complex network. Hence, for e-commerce enterprises to succeed in this field, a thorough awareness of the legal framework and the potential problems that an e-commerce business might encounter, together with appropriate risk management measures, has become imperative. E-commerce is evolving daily and will continue to do so in the days to come. It is also branching out into ever-newer formats. These days, mobile commerce is likewise growing to be a significant industry. The necessity of the hour is to create new legislation, change current laws, and continuously monitor, revise, and adapt. As a result, our state will profit from e-commerce technologies while simultaneously generating more money to meet its socioeconomic demands. In order to monitor all e-commerce transactions, an effective and comprehensive infrastructure must be established in addition to the development of the regulatory and statutory framework. Together with providing officers of the business tax department with the required skill upgrades, better audit trails and authorization control must be developed. For effective administration, improved consumer education and cooperation among states are essential. The IT infrastructure must handle transactions that occur across many states and even countries.

**Keywords:** E-Commerce, Taxation, Income Tax Act, IT Act.

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### **1. Introduction**

In India, e-commerce is expanding quickly. The development of e-commerce in India throughout the years has been examined in the study published by the IMRB (Indian Market Research Bureau) and IMAI (Internet and Mobile Association of India). E-commerce has given dealers new methods to evade taxes. A record of the movement of the e-money is now being kept in an accounting electronic payment system. Nevertheless, neither the unaccounted-for system nor the electronic system contains any such record. In this instance, tax administrators are unable to link payments and receipts to individual taxpayers. In these systems, instances of under- or non-reporting are frequent. Indian tax authorities have been attempting to tax internet-based business models and e-commerce in a way that is at odds with international standards. Due to this, multinational companies that serve Indian consumers have experienced challenges, and there has been extensive litigation in this area, particularly in connection to the characterization of income and withholding taxes. It is crucial to properly establish e-commerce business models in order to reduce tax risks, particularly the risk of taxation. The Delhi Tribunal has held that where the taxpayer availed of data processing services performed by a company based out of India, for its Indian operations, then in the absence of any right to secret process that was made available by the foreign company to the taxpayer coupled with the fact that the foreign company performed support functions using its own intellect, there can be no income in the nature of royalty.

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### **2. Sales Tax Issues**

Sales tax is important in the context of e-commerce transactions when it comes to the selling of intangible products. In this regard, the Supreme Court has ruled that intangible products, including software installed on a physical medium, technical know-how, and other intellectual property rights, are considered goods for the purposes of sales tax. Moreover, it has been ruled that any intellectual property that has been included in a medium for the purpose of transfer or communication cannot be divided. Software sales are taxed since they are considered sales of tangible goods. The transfer of IP may therefore be subject to CST as well as VAT. Tax experts say that under the present legal framework, it may be challenging to hold businesses like Facebook, Google, Yahoo!, and Twitter accountable or to claim that they have been dodging taxes. According to the current Indian legal framework, these online businesses that don't function as permanent premises could not be subject to taxation. The majority of our legislation discuss firms' presence in India as offices or distribution centers. So, even if online businesses have a sizable client base in India, these tax regulations cannot be applied to them. By experimenting with some of the law's provisions, the nation's tax officials appear to be attempting to remedy this problem. They argue that because these businesses operate outside of India, the earnings from such businesses need to be taxed here. The income-tax authorities have decided that

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maintaining a server in India should be viewed as similar to a company's permanent establishment here in certain situations, while in others they have argued that running a website outside of the nation is equivalent to a company's presence here.

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### 3. Tax Evasion Issues

Whether or not these businesses may be accused of tax evasion doesn't appear to have a clear answer. Simply put, they can be avoiding taxes. Yet legally, it is impossible to hold them accountable. The law has a gaping hole in it. Theoretically, these businesses are doing legal and are not breaking any laws. Yet if the government so desires, there could be a method to request that these businesses share specifics of the advertising money they produce in India. As the business is created here, taxes should ideally be collected here. There are legal gaps in the system. There is no definitive method for taxing international e-commerce enterprises due in large part to geography-specific source restrictions. This problem is not exclusive to India. Authorities all across the world struggle with this issue. This problem is being addressed through Base Erosion and Profit Sharing (BEPS) projects. The Income-Tax Appellate Tribunal (ITAT) in Kolkata ruled in April 2013 that payments made to internet advertising companies like Google and Yahoo! in India were not subject to taxation. In an appeal filed by Right Florist Pvt Ltd, which had spent around Rs 35 lakh for its adverts on the Yahoo! and Google websites in 2005–2006, George Mathan and Pramod Kumar made the decision. The panel decided that the websites could not be interpreted as foreign companies with taxable presence in India or as permanent premises of such companies. Also, since the web servers are situated outside of India, there is no risk to India's long-term establishment. So, these earnings should be subject to taxation in the nations where the servers are situated. It is unclear where the servers for India are situated.

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### 4. Contract Laws

The fundamental guidelines outlined in the Indian Contract Act, of 1872 (ICA), stipulate that a legitimate contract must have been made with free consent and for a lawful consideration between two adults, apply to electronic contracts. E-contracts are allowed under Section 10A of the Information Technology Act of 2000 (IT Act). So, it is necessary to study the ICA and IT Act together in order to comprehend and provide e-contracts legal legitimacy. The Evidence Act's Section 3 also stipulates that the evidence may be in electronic form. In *Trimex International FZE Ltd. Dubai v. Vedanta Aluminum Ltd.*,<sup>[1]</sup> the Supreme Court determined that correspondence between parties through email addressing their respective duties counts as a contract.

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### 5. Taxation Issues

E-commerce has several challenges. How to describe income and the approach towards residence-based and source-based taxation techniques are some of the conceptual issues posed by e-commerce. The global character of e-commerce transactions makes it difficult to determine "jurisdiction," which is a fundamental concept in taxation. The existence of certain organizations nearly entirely online and the use of communication tools and technology to conduct interactions with directors or shareholders provide another challenge to traditional company tax laws. E-commerce basically raises questions about when, when, and how taxes may be imposed at a time when local markets are becoming global marketplaces. Identity verification in e-commerce transactions is a significant problem. In cyberspace, it might be challenging to identify the persons involved in transactions. This may make it impossible to impose taxes on transactions involving residents and non-residents. Tax administrators are greatly hampered by features like encryption, fragmented transmission, usage of proxies, and diverting mechanisms even when the ownership of a website or IP is proven. It might be difficult to confirm the other party's identity. When claiming to be a resident of a nation with which India has a treaty in order to be eligible for a lower or zero rate of withholding tax on royalties, an electronic products or service supplier may not actually be.

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### 6. Committee Report (HPC)

It can be challenging to use source ideas to connect an item of revenue with a geographic entity in the era of e-commerce since many of the commodities and services traded may be of an intangible character. Many of the current distinctions between local and international commerce, as well as between on-shore and off-shore operations, are muddled by intangible transactions. A High-Level Committee was established in India in 1999 under the leadership of Shri. Kanwaljeet Singh to investigate the different facets of e-commerce and provide several solutions. In order to prevent base erosion, it recommended a modest withholding tax as a potential e-commerce tax. The goal was to protect the assesses from double taxes. So, let's say the assessed has legally claimed that he paid deductible expenses since he imported items from a foreign supplier. As the government does not have a tax for imported products or services in the first place, if it permits this, the tax base would be eroded.

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### 7. Impact of E-Commerce on Taxation

Every person who is in charge of paying a non-resident a sum that is payable under the terms of the Income Tax Act is obligated to withhold income tax from such payment. The assumption is that the payee will receive a set-off for this withholding tax in his own country, preventing double taxation. Yet it depends on the Double Taxation Avoidance (DTA) Agreements that India has with other nations, as well as on whether other nations will permit offset for the withholding tax that businesses registered under their flag must pay in the foreign nation. Based on the aforementioned scenario, one may wonder if a taxpayer who has paid this withholding tax can claim a foreign tax credit in his home country. There will be no allocation of foreign tax credits for any taxes withheld due to base erosion under the DTA that India has with Australia, Belgium, the Netherlands, Germany, Malaysia, Singapore, the United

States of America, and the United Kingdom. Hence, the High-Powered Committee's suggestion that e-commerce be subject to a withholding tax is unworkable, because different types of transactions may have distinct tax ramifications, and the problem of categorization is crucial. A royalty will apply if only a portion of the product's rights is transferred. As a result, the state where the payment occurs may tax it. The payment will be categorized as business profits if the website owner has a Permanent Establishment in the originating state. The nation of origin has the authority to tax royalties and technical services, but not corporate profits. In terms of India, the word "royalty" has been defined as the compensation resulting from the transfer of all or any rights in relation to a copyright or a scientific work under Explanation 2 to section 9(1)(vi) of the Income Tax Act, 1961. The taxation of payments resulting from all types of transfers is permitted under the wide definition of royalty. Any payments made in India for the online transmission of software or other digital goods would be categorized as royalties under the Income Tax Act, 1961, in this context.

Regarding the withholding tax problem, the non-resident seller has the option to offset the income tax TDS against the income taxes he must pay in his own country. When it comes to VAT, the Indian Government bears the set-off costs rather than the government of the seller. As a result, it is inappropriate to raise the argument that the planned handling of e-commerce causes base erosion. We can impose a single indirect tax on the import of goods and services for the sake of ease and efficiency, and we won't be taxing the income of non-residents. It is clear where the Organisation for Economic Co-operation and Development (O.E.C.D.) and India diverge on the subject of payment classification. There are 11 problems out of the 28 that have different categorizations. The O.E.C.D. has classed the transactions in all 11 of the aforementioned categories as commercial earnings, making it illegal for the nation of payment to impose taxes on any of these transactions. Nonetheless, as per the India-UK Treaty and the Income Act of India. In accordance with the India-U.S.A. Treaty, India has the authority to tax certain transactions as Tax Deducted at Source

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## 8. Conclusion

The law in India is still developing with regard to questions of jurisdiction and enforcement in e-commerce. In general, municipal legislation provides for "long-arm jurisdiction," which means that the execution of such local laws has extra-territorial applicability if a person's action or inaction has an unlawful or detrimental effect on the country's territory. I've included a few Indian legal rules that allow for such long-arm jurisdiction below. Our analysis-based advice addresses every aspect of e-commerce-related challenges. Customers can access any country's servers or mirror servers when doing e-commerce transactions. Consequently, it cannot be stated that these servers are permanent establishments. Due to the fact that these earnings are considered company profits and the business concerns do not have a permanent location in India, numerous commercial companies are making money from the sale of goods or services in India but are not paying taxes on them. I am thus arguing that setting a threshold for revenue creation within a nation may be a potential answer. Regardless of whether the transaction is classified as royalties or commercial earnings, anyone receiving more than the threshold will be required to submit his tax returns in India and pay the tax. Tax at source (T.D.S.) will be withheld by the payers, who will then deposit it with the Indian government.

There isn't yet a single framework that all of the countries have agreed to. Each country has a unique legal and tax structure that is autonomous and separate for e-commerce. The G.S.T. framework is already in existence in certain states, such as the EU, while V.A.T. is used in other states, such as India, and retail taxes are used in yet other nations, such as the USA. As a result, the tax on online sales is only an extension of the existing tax legislation. It is necessary to provide a thorough foundation for e-commerce transactions. A review of the "I.T. Act 2000" is necessary. The O.E.C.D. erred in trying to categorize the transactions based on the type of revenue since each state sought to make the definition of royalty as broad as possible in order to be able to tax the transaction. As a result, we advocate that the source-based tax concept be based on the existence or lack of source rather than on the type of revenue. Uncertainty over the legal jurisdiction of contracts involving foreign parties, the absence of dual-key pairs for persons and businesses, and problems with the protection of individual rights, including domain names, are some of the gaps in the IT Act that need to be addressed.

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## REFERENCES

- [1] (2010) 3 SCC 1