A STEP BACK IS THE WAY FORWARD: SHOULD INDIA CONSIDER WITHDRAWING EQUALIZATION LEVY?

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ABSTRACT

Change in the way businesses are carried out due to digitalization has led to emergence of a whole new economy. International rules on taxation has not been revised to incorporate such businesses within its definition of permanent establishment which conceptualizes a physical presence. This definition was crafted for traditional ‘brick and mortar’ businesses and therefore fails digital businesses. Task Force on Digital Economy was established to evaluate modalities that the digital economy utilizes to add value and make profits, in order to understand how it fits in the existing system of taxation and whether any modifications are required. The Task Force identified various challenges the existing framework poses and also supplied three solutions to tackle these challenges.

India was at the frontier to take initiative and adopt these solutions. It established Committee on taxation of E-commerce which concluded its report in 2016 with recommendations of India’s course of action. It recommended the introduction of Equalization Levy, among other reasons, due to the non-feasibility of introduction of Significant Economic Presence in its domestic law without needing to renegotiate international treaties. In 2018, the Finance Act introduced an amendment in Section 9 to include Significant Economic Presence. This paper further debates whether there is a need to withdraw Equalization Levy when appropriate amendments of Significant Economic Presence have been made.

Keywords: OECD BEPS Action Plan 1, Equalization Levy, Committee on Taxation on E-Commerce, Finance Act 2018, Significant Economic Presence.
INTRODUCTION

Evolution in information and communication technology has inadvertently evolved the way businesses are conducted around the world.\(^1\) It has made technology cheaper, easily available, more powerful, and widely standardized, improving business processes and bolstering innovation across all sectors of the economy\(^2\). To provide some context to this statement, some statistics could help. The number of Internet-connected devices (12.5 billion) surpassed the number of human beings (7 billion) on the planet in 2011 and this number is only going to grow between 26 billion and 50 billion globally by 2020\(^3\). These devices are now used to do all those activities which required some level of human intervention for instance, bank online, job searching, shop online, email, read news online etc\(^4\). Internet has penetrated our daily lives so intrinsically, not realizing its contribution to our economy. For a business, it is now possible with extensive digital or telecommunication network, to have significant participation in the economic life of a jurisdiction without having any physical presence. Some economist, therefore, rightly call this unparalleled use of intangible assets\(^5\) the emergence of a whole new economy.

In this paper, the first section captures the historical perspective of rules of taxation and how this system fails to incorporate the ever-evolving business models in this digital economy. The second section summarizes and analyses the challenges posed by digital economy on the current tax regime as recognized by OECD BEPS Action Plan 1 and their suggestion (not recommendations\(^6\)) to tackle the same and India’s implementation/adopting of these suggestions. The author, lastly, also attempts to analyze and debate over India’s adoption of two suggestion, i.e. Equalization Levy (in


\(^3\) Indian Report, 12.

\(^4\) Indian Report, 12.

\(^5\) OECD 2015, 16.

\(^6\) They weren’t recommendations to be compulsory complied to but mere suggestion any country could adopt in order to tax digital presence provided countries do not deviate from their existing obligations in tax treaties.
2016) and Significant Economic Presence (w.e.f 2019-20) which were provided as alternatives in the OECD BEPS Action Plan 1 and whether the former must now be withdrawn.

REALIZATION OF TAX CHALLENGES DUE TO EVOLUTION OF NEW BUSINESS MODELS

With this advancement, the natural underlying question surfaces: whether taxation laws are able to take cognizance of these change in business structures? The Double Tax Avoidance Treaties\(^7\), international rules on double taxation largely follows the recommendations of four economists\(^8\) appointed by the League of Nations in the 1920s, long before technological advancement\(^9\). These economists categorized and recognized the right of taxation of both country of source\(^10\) and country of residence\(^11\) of the income.\(^12\)

A country of source had the right to tax foreign income only if it could be attributed to a “permanent establishment” (PE) in that country. This threshold conceptualizes a physical presence of business entity which differentiates businesses having significant economic presence\(^13\) in a tax jurisdiction from those having an economic participation of occasional nature\(^14\). PE as a threshold serves a vital purpose, as it attempts to impose the burden of cost of compliances and administration on only those businesses which significantly participates in an economy\(^15\). Nevertheless, the concept has evolved over time, modifying by the change in way businesses are conducted. It, now, envisages activities conducted\(^16\) by a dependent agent within the meaning of PE\(^17\). However, activities which

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\(^7\) India’s Double Tax Avoidance Agreement.

\(^8\) Professor Gijs Bert Bruins, Professor Luigi Einaudi, Professor Edwin Seligman and Professor Sir Josiah Stamp

\(^9\) Indian Report, 17.

\(^10\) Country where the income is earned or accrued.

\(^11\) Country where the taxpayer is resident.

\(^12\) Indian report 18.

\(^13\) This term is not used as one of the options suggested by the OECD BEPS Action Plan 1 which is later discussed in the paper. However, it is used in plain language.

\(^14\) Indian report 18.

\(^15\) Indian report 18.

\(^16\) Habitually concludes contracts or maintains stocks of goods or merchandise.

\(^17\) Section 9, Explanation 2 of the Income Tax Act, 1961; also, DTAA with Mauritius Article 5.4. there are similar agreements with other countries, https://www.incometaxindia.gov.in/pages/international-taxation/dtaa.aspx
are auxiliary and preparatory in nature are categorically excluded\textsuperscript{18} to fall outside the meaning of PE.

This definition crafted for traditional economy with ‘brick and mortar’\textsuperscript{19} businesses is bound to fail when it comes to digital economy. Undue advantage maybe be taken by foreign e-commerce giants to route their transactions through low tax jurisdictions thereby paying low or nil tax for the same in country of residence while simultaneously not attracting any tax liability in source country. This leads to double non-taxation of income on accounts of base shifting and jurisdictional arbitrage or in simple words profit shifting\textsuperscript{20}. Now this definition has become completely (or to some extent) outdated due to the emergence of digital enterprises\textsuperscript{21} requiring us to revisit the definition to incorporate the development of technology and ever evolving business models.\textsuperscript{22}

From Indian perspective, the need to tax income arising from digital presence and the inability due to the current tax regime was realized as early as 2011 when the Tribunal observed that the payment made for display of banner advertisement on a website cannot be characterized as royalty within the definition of Indian Income Tax Act, 1961 and therefore not taxable.\textsuperscript{23} Similarly, there were a series of case laws\textsuperscript{24} indicating the challenges of the current regime suffers, making these presences non-taxable.

**OECD BEPS ACTION PLAN 1 AND ITS ADOPTION BY INDIA**

OECD BEPS Action Plan 1 was the first of the fifteen reports\textsuperscript{25} and is dedicated to taxation on digital presence and understand the modalities digital economy utilizes to add value and make profits in order to understand how does it fit in the existing system of taxation and if it requires any

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\textsuperscript{18} Article 5.3 DTAA with Mauritius, https://www.incometaxindia.gov.in/pages/international-taxation/dtaa.aspx

\textsuperscript{19} It refers to company which need to have physical presence such as factory, outlet, warehouse, shop etc for its operations. The term is used to differentiate e-commerce businesses.

\textsuperscript{20} OECD, 2015.

\textsuperscript{21} Indian report 18.

\textsuperscript{22} Indian report 18.

\textsuperscript{23} Yahoo India (P) Ltd vs DCIT: 140 TTJ 195.

\textsuperscript{24} ITO vs Pubmatic India (P) Ltd: 60 SOT 54; Pinstorm Technologies (P) Ltd vs. ITO: (2012) 154 TTJ 173; eBay International AG vs. DDIT: (2012) 151 TTJ 769; ITO vs. Right Florists: 154 TTJ 142.

\textsuperscript{25} It addressed the challenges and suggest potential changes that can be brought about to tackle with the problems of base erosion and profit shifting.
modification. Although digital economy in itself do not generate unique BEPS issues, but then some of its key issues exacerbate BEPS risks\textsuperscript{26}.

For this purpose, Task Force on the Digital Economy (TFDE) was established\textsuperscript{27} and on consultation with various stakeholders, businesses, civil society, academicians and developing countries, published its report in 2015. It is important to note that India actively participated in this exercise\textsuperscript{28}.

\textbf{A. Challenges to the existing tax regime}

As already mentioned, taxability of foreign income depended upon the presence of PE which relates to physical presence (and its evolved definition\textsuperscript{29}). In traditional economy, this concept worked, as when foreign companies wished to expand its operations in a particular country they had to establish local infrastructure for various activities ranging from manufacturing, marketing, distributing, and thereby having a physical presence\textsuperscript{30}. Now these activities can be centrally managed which no longer needs local presence leading to this model being obsolete\textsuperscript{31}. TFDE recognised three challenges to the existing tax regime when it comes to incorporating digital economy viz., Nexus, Characterization and Data\textsuperscript{32}.

\textbf{a. Nexus}

Nexus, in context of a Permanent Establishment, means a physical presence (physical nexus with the country). Additionally, some elements are deemed to have nexus with the country. One such, a dependent agent who habitually concludes contracts for the foreign entity. However, advances in technology with sophisticated software Programme and algorithms has made concluding contracts to be done remotely without involving any personnel\textsuperscript{33}. Another concern which has surfaced where,

\textsuperscript{26} OECD 2015, 11.
\textsuperscript{27} A subsidiary body of the Committee on Fiscal Affairs (CFA) in which non-OECD G20 countries participate as Associates on an equal footing with OECD countries, was established in September 2013 to develop a report identifying issues raised by the digital economy and detailed options to address them by September 2014. (OECD BEPS ACTION PLAN 1- Final Report 2015, Executive Summary, page 1).
\textsuperscript{28} Indian Report, Executive Summary
\textsuperscript{29} See- Section II, para 2 of this paper.
\textsuperscript{30} OECD 2015, 98.
\textsuperscript{31} OECD 2015, 98.
\textsuperscript{32} The focus of this paper on the problems related to the former two challenges. Valuable of data is very technical problem, solution of which is still to be studied in great detail.
\textsuperscript{33} OECD 2015, 100.
technology adds value by virtue of customer and user interactions (participative network platform). These interactions which extends beyond the point of sale adds the value to a business and makes the products more attractive to potential customers\(^{34}\). Lastly, activities which were previously considered to be auxiliary and preparatory in nature have now transformed into core activities for businesses which work primarily on digital presence\(^ {35}\).

Technology has substantially affected the way core activities of a business are carried out i.e. source and acquire inputs, create or add value, market research, advertising, sale and then customer support, all contributing to income generation\(^ {36}\). For instance, a company in the business of manufacturing and retailing of clothes, resident of a low tax jurisdiction but sells worldwide (for the sake of convenience, India is the target country of sale). Now, it can maintain a website where products can be viewed (advertised online where servers are not in India), the product information and customer base can be tremendously expanded across borders, orders from target country can be taken its in residence (conduct activities remotely), customer support is also not in the target market (no local infrastructure or personnel). The only connection to the target country could be, that it does warehousing, which is expressly excluded\(^ {37}\) from the definition of business connection\(^ {38}\). Therefore, companies stationed in multiple jurisdiction is able to maneuver their tax liability by locating substantial business activities separate from ultimate market jurisdiction.

Therefore, one can deduce that it is easy to work around the scope of permanent establishment considering the change in the way businesses are now conducted. At the same time, although companies might have other reasons to have a taxable presence however, one shouldn’t understate the possible conflicts of the current regime.

b. Data

Digital technologies fosters collection, storage and use of data gathered remotely and from great distances from users, consumers or other sources of information which often form primary inputs

\(^{34}\) OECD 2015, 101.  
\(^{35}\) The OECD report illustrates this with an example- In a business model of online seller of physical products, a key component would be to provide quick delivery and thereby maintains a local warehouse. This will constitute a core activity for such a business model.  
\(^{36}\) OECD 2015, 100.  
\(^{38}\) India’s domestic law for the Permanent Establishment rule is the “business connection” rule under Section 9 of the Income Tax Act 1961- storage of goods are excluded.
in creating value to a business. User feedback, for instance, is used to understand a particular market and improve decision making. Expansive role of data in improving business models have raised issue as to whether any profits attributable to the remote gathering of data by an enterprise should be taxable in the State from which the data is gathered, as well as questions about whether data is being appropriately characterized and valued for tax purposes. However, before any profits can be attributed to these data, first issue is how to value these data.

c. Characterization

The issue of characterization, which given in India’s context could be referred to the case of Yahoo India (P) Ltd vs DCIT and many others following that, where the Tribunals were struggling to characterize different digital services into royalty (under the treaty definition royalties includes payment for rentals of commercial, industrial, or scientific equipment) fees for technical services or business profit. These characterizations are vital for the sole reason that business profits that can be attributed to a PE are taxable while royalty and fee for technical services are subject to withholding tax. with development of technology, payments made for platform-as-a-service transactions, software-as-a-service transactions, infrastructure- as-a-service transactions could fall within the scope of business profits or the former two. These characterization challenges will be more prominent with newer developments with respect to 3D printing.

B. Potential options to tackle these challenges

Written inputs of various stakeholders, academician, businesses etc. were perused at lengths in order to devise novel solutions to these broad tax challenges by the Task Force. It was realized that

39 OECD 2015, 102.
40 OECD 2015, 102.
41 140 TTJ 195.
42 ITO vs Pubmatic India (P) Ltd: 60 SOT 54; Pinstorm Technologies (P) Ltd vs. ITO: (2012) 154 TTJ 173; eBay International AG vs. DDIT: (2012) 151 TTJ 769; ITO vs. Right Florists: 154 TTJ 142.
43 OECD 2015, 104.
45 It provides businesses with an independently maintained platform upon which their web applications can be built, refined and deployed.
46 It is a software licensing and delivery model in which software is licensed on a subscription basis and is centrally hosted.
47 (Bloch, 2015; Bourreau, 2015; Brauner, 2015; Crémer, 2015; Hongler, 2015)
48 OECD 2015, 105.
these challenges cannot be tackled individually rather being overlapping in nature, the solutions needed to be general.\textsuperscript{49} The options analyzed\textsuperscript{50} were combined in three solutions suggested by the Task Force – Significant Economic Presence, Withholding Tax and Equalization Levy.

\textbf{a. Significant Economic Presence (SEP)}

The concept creates “a taxable presence in a country when a non-resident enterprise has a significant economic presence in a country on the basis of factors that evidence a purposeful and sustained interaction with the economy of that country via technology and other automated tools”.\textsuperscript{51} The Task Force was aware of the possibility of attracting remote transactions thereby increasing the cost of compliance of the taxpayer. Hence, they formulated certain factors on the basis of which SEP would be determined – Revenue- based, User- based and Digital factors.

- Revenue- based factors: A clearest indicators of SEP is the gross revenue generated from transactions concluded with customers in the country concerned. This gross amount must be set at a higher threshold factoring in the size of the country’s market thereby levelling with the burden of tax administration and cost of compliance.\textsuperscript{52} The Task Force also recommended anti- fragmentation rules considering the possibility of manipulations an enterprise might use, for instance artificially fragment aspects of its business to fall outside the threshold\textsuperscript{53}.\textsuperscript{54} However, revenue is not sufficient on a standalone basis but must be combined with other factors\textsuperscript{55}.

- User- based Factors: As discussed earlier, customer and user interaction adds value to a business. In order to analyse estimate the level of participation, certain variables must be considered such as the number of monthly active users (MAU) who are habitually resident of a given country using a platform. There are, however, some challenges to this as identifying a ‘unique user’ and where or not he is ‘active’ requires laying down of further

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\textsuperscript{49} OECD 2015,106.
\textsuperscript{50} Modifications to the exceptions from PE status, alternatives to the existing PE threshold, the imposition of a withholding tax on certain types of digital transactions, and the introduction of a tax on bandwidth use.
\textsuperscript{51} OECD 2015, 107.
\textsuperscript{52} OECD 2015, 108.
\textsuperscript{53} OECD 2015, 108.
\textsuperscript{54} These rules are discussed in detail in Action Plan 7 on Permanent Establishment.
\textsuperscript{55} OECD 2015, 107.
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detailed metrics. Another variable could be the volume of data collected from a taxable jurisdiction irrespective of how remotely it is stored and processed. Lastly, the volume of online conclusion of contract, for instance “terms of service”, in a taxable jurisdiction. This variable directly absolves the problem of dependant agent concluding contracts in a PE.

- Digital Factor: The reach of brick and mortar businesses is contingent on factors like store’s location, local marketing and promotion, payment options, and sales and customer service employees. Similarly, in digital economy, the reach of the business depends upon a local domain name i.e. local website address (.com; .in; .uk); a local digital platform and local payment options. The Task Force recognized these factors, although gave countries a leeway to determine factors for themselves which are unique to their market but also suggested that revenue-based factor is the main factor which cannot be substituted.

Significant Economic Presence is a suitable option to be incorporated in the definition of Permanent Establishment but for the issue of attribution of income that it entails. The difficulties in the rules of attribution makes this option not feasible for many countries, including India, hence alternative methods such as fractional apportionment i.e. apportion the profits of the whole enterprise to the digital presence either on the basis of a predetermined formula, or on the basis of variable allocation factors determined on a case-by-case basis. However, this method has its own limitation whereby it has the possibility of creating different results with different types of business models.

b. Equalization Levy (EL)

As the name suggest, Equalization Levy was suggested to bring about tax neutrality with respect to domestic and foreign entities as well as between digital economy and traditional brick and mortar businesses. Realizing the limitation of rules of attribution of income, Task Force suggest EL as an

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56 OECD 2015, 110.
57 Reliability and veracity of the information would also need to be ensured, to address fraudulent accounts, multiple accounts, false information volunteered by users, and “bot” produced data, to name a few.
58 For instance, a website devised with particular language option, currency valuation, delivery in a particular jurisdiction and so on.
59 For instance, prices in local currency connecting the payment option to local banks.
60 OECD 2015, 111.
61 OECD 2015, 112.
alternative to ‘Significant Economic Presence’ to address taxation on digital economy.\textsuperscript{62} The scope of the levy was kept flexible which could be as targeted as possible to address specific services or as broad as possible to encompass future development in the digital economy, depending upon the policy objective of a concerned country\textsuperscript{63}.

**INDIA’S ADOPTION OF THE SUGGESTIONS OF OECD BEPS ACTION PLAN 1**

India was an active participant being a part of G-20 countries and OECD sending representatives and written submission. Perusing various judicial precedence suggests that India has been struggling to tax digital economy\textsuperscript{64} for a long time and therefore was one of the first countries to act upon the Final Report, amending its domestic laws in order to incorporate these suggestions. Central Board of Direct Taxes established a Committee on taxation of E-commerce\textsuperscript{65} (hereinafter referred to as ‘Committee’) which placed extensive reliance on Action Plan 1 and concluded its Report\textsuperscript{66} from Indian perspective with certain recommendations\textsuperscript{67}.

\textbf{a. On Significant Economic Presence}

While noting that the first option, of including SEP in domestic laws (“business connection”)\textsuperscript{68}, will adequately (possibly be the ideal solution to tax digital economy) plug the loophole in the nexus rule, nevertheless it would be ineffective unless appropriate modification is also made in the nexus rules in the tax treaties (“permanent establishment”). Adoption of SEP in the domestic law was not considered feasible due to the shortcomings and ambiguities of the rules on attribution of income discussed at lengths by OECD report, however the same also set down an alternative attribution rule i.e. fractional apportionment. The Committee Report discusses little to nothing on this alternative, only stating that there is difficulty in its application. Nevertheless, it also recognises

\textsuperscript{62} OECD 2015, 115.
\textsuperscript{63} OECD 2015, 116.
\textsuperscript{64} Supra 41, 42.
\textsuperscript{65} The Committee was established with the sole objective to examine the challenges posed by the existing tax regime and give implementation to the Report on Action Plan 1 of Base Erosion & Profit Shifting (BEPS) Project.
\textsuperscript{67} Indian Report, 21.
\textsuperscript{68} Indian Report, 68.
that even further understanding into these issues must be undertaken to find solutions which are simpler, predictable and certain.  

b. On Equalization Levy

The Committee Report revolved around the vices of the other two options which lead them to choose Equalization Levy as the only feasible option. As Equalization Levy requires no particular prescribed design to be adhered, it could be moulded according to the policy priority. It is a tax on gross payment rather than on income which makes it different from corporate income tax thereby eluding the problems attached to rules on attribution of profit as well as the breaching tax treaties. The other two option (withholding tax is not covered by this paper) still lacks clarity and universal consensus on many aspects (factors signifying SEP, issue of attribution and so forth) which would require further detailed analysis of its impact. Apart from the ease in application, the committee was of the opinion that the measure will bring greater certainty and predictability to all the stakeholders by enabling them to better manage their business thereby contribute to a balanced tax environment in the country.

WITHDRAWAL OF EQUALIZATION LEVY, A WAY TO GO?

In 2016, India was eager on taxing the digital economy on an immediate basis which was not possible by introducing SEP then, thus, introduced Equalization Levy. India introduced Equalization Levy under Chapter VIII of Finance Act, 2016 effective from 1st June 2016. The levy is chargeable at the rate of six percent of the amount of gross payment exceeding one lakh rupees, for any specified service receivable by a non-resident person from a resident of India carrying on business or profession in India, or from a non-resident having a PE in India. India adopted the balancing view of the scope of this levy as suggested by the Task Force applying to

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69 Indian Report, 72.
70 ibid
71 ibid
72 Indian Report, 83.
74 Section 165 (2) of Finance Act, 2016 is the charging section whereas specified services is defined under Section 164 (i) of Finance Act, 2016.
75 Section 165(2) of Finance Act, 2016.
certain online advertisements in any manner and other services which may be notified at a later point. The introduction of Equalization Levy was heavily criticised, among other thing, for excessive rate of tax as well as the malicious way of introducing it in the Finance Act in order to evade breaching of tax treaties.

In 2018, a new chapter began for India in the field of taxation on digital economy by virtue of Finance Bill 2018⁷⁶. India proposed to amend clause (i) of sub-Section (1) of Section 9 of the Indian Income Tax Act, 1961 to provide that ‘significant economic presence’ shall also constitute ‘business connection’.”⁷⁷

India eagerly adopted SEP to its domestic rule of PE, being the first and only country to have adopted two out of the three solutions suggested by the Task Force. With the language of the provision, it suggests that the factors determining the economic presence is similar to those enumerate by the Task Force i.e. Revenue, User and Digital. However, the threshold for each one of them is yet to be decided after consultation with relevant stakeholder. This is seen as a welcomed move as opposed to when Equalization levy was introduced, the decision on the features of the levy was completely unilateral without any consultation. These thresholds will soon be introduced before the amendment take effect from 1st April, 2019.

The underlying questions now surfaces whether we need Equalization Levy when the necessary amendment has been made in the permanent establishment rule of domestic law to rectify the loopholes. There are strong arguments for retaining Equalization levy, one of them being that EL and SEP are harmonious as they are two separate taxes levied on separate tax base. SEP attracting income while Equalization Levy does not strictly fall within either direct or indirect tax system. Although there is an overlap in their scope, SEP being wider encompassing services which are

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⁷⁶ Finance Bill, 2018, also refer to the Memorandum to the Finance Bill, 2018, Income Tax Dept. page 8
It defined the scope of SEP as –
“(i) any transaction in respect of any goods, services or property carried out by a non-resident 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 the amount as may be prescribed; or
(ii) Systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.
targeted by EL, there is, nonetheless, no double taxation due to the exemption provided in Section 10 (50) of the Income Tax\(^{78}\). Therefore, the two taxes can co-exist harmoniously.

The Committee in its report emphasized on the feasibility of Equalization Levy as it would not require any modification of tax treaties where SEP even though introduced in the domestic law would be ineffective until tax treaties are modified. Therefore, withdrawing the same would put India in the same position as pre- 2016, having no regime for digital economy and a significant impact on the state revenue. Therefore, as suggested by Task Force, Equalization Levy is kept outside the purview of limitations imposed by tax treaties, a feature which makes it the only option that can be adopted without violating treaty\(^{79}\).

As it is there were strong criticism when Equalization Levy was introduced, now with the adoption of SEP the arguments for its withdrawal has become stronger. Although, Equalization Levy might be clear, certain and predictable however one can argue that it lacks in equity. It was supposed to bring about tax neutrality between domestic and foreign service providers as per the suggestion of Task Force. However, India did not adopt the report as it is, and only imposed this levy on foreign service providers. Moreover, levy is on transaction and not income thereby being separate from corporate income tax. The foreign entity might not be doubly taxed in India being the country of source, however, it might be taxed in its resident country due to non-availability of tax credit for the same income leading to double taxation.

Secondly, the Task Force intended the two option to be chosen alternatively to overcome the difficulties of rules of attribution of income. Countries could choose any of the options depending on the feasibility of its tax regime and also suggested supplementing with additional options once they become feasible\(^{80}\). Exactly the approach taken by India, where it considered Equalization levy feasible then and SEP feasible now. The Committee also observed its temporary nature for a solution to the taxability problem.

Thirdly, Equalization Levy being outside the scope of Income tax Act, 1961 enjoys the benefit of not being bound by Section 90 which provides a foreign entity a more beneficial provision of the two, the treaty or domestic law. Therefore, Equalization Levy is to be compulsorily levied thereby


\(^{79}\) Indian Report, 85.

\(^{80}\) Indian Report, 78.
overriding the treaty rules, ‘a unilateral treaty override’ which could look badly upon India in international setting. However, the Committee in its report defends this accusation by claiming consensus of G-20 and OECD countries of such an override in the OECD report.

Lastly, the Task Force report does discuss the relationship of levy with corporate income tax and fears the risk of double taxation of the same income by levy at source and tax in residence country. However, the Report recommends solutions to avoid this risk by either excluding the subject matter of levy from that of corporate tax or by allowing tax credit. However, India has done neither. The subject matter of the corporate income tax (i.e. the significant economic presence rule) is wide enough to incorporate the scope of the levy. Similarly, India has also not allowed tax credit as it is not tax on income.

CONCLUSION

Tax on digital economy was brought about to bring neutrality among the various business models. The question as to whether or not India has been able to achieve is still premature as India adopted Equalization levy to have an immediate revenue gain. On the other hand, for SEP, India has invited recommendations and suggestions from various stakeholders, academician, businesses and industry in order to set a threshold which would be better able to tackle various challenges. It would be interesting how India will tackle the issues such as valuation of data, rules on attribution of income and characterization.

It is difficult to gauge what India course of action would be in response to the debate over withdrawal of the former, however it cannot completely ignore the criticism from the industry and the arguments against such a levy. For this purpose, as recommended by both the Reports, periodical assessment must be made on the implementation and impact of these changes, particularly Equalization Levy if there are talks on its withdrawal. India has, as yet, not published any such report, however, OECD published an Interim Report in 2018. Nevertheless, the 2018 report does not discuss the impact of India’s Equalization Levy in much detail.

81 OECD 2015, 117.
82 Indian Report, 110; OECD 2015, 138.
In view of the above challenges, it would only be solved with some universal consensus on the new nexus based significant economic presence rule and the parameters for the same\textsuperscript{83}. That can be a long wait which could involve revenue loss, prolonged handicap for resident companies from unfair competition, distortion of ownership and production\textsuperscript{84}; which is why attempts must be made to modify these rules bilaterally, for now.

\textsuperscript{83} Indian Report, 104.