

INDIA'S RESPONSE TO S 301 REPORT OF U.S. ON EQUALISATION LEVY

TAXTRU BUSINESS ADVISORS LLP

- The U.S. administration had announced the initiation of an investigation under section 301 of the U.S. Trade Act, 1974 against the **taxation on digital services** adopted or under consideration by countries, including the Equalisation Levy applied by India.
- Other countries under investigation include Italy, Turkey, and the United Kingdom.
- With respect to India, **the focus of the investigation was on the 2% Equalisation Levy (EL) levied by India on the e-commerce supply of services.** The U.S. investigation included whether the EL discriminated against the U.S. companies, was applied retrospectively, and diverged from U.S or international tax norms due to its applicability on entities not resident in India.
- In this regard, **the U.S. requested for consultations, and India submitted its comments to the USTR on 15 July 2020**, participated in the bilateral consultation held on 5 Nov 2020, *emphasizing that the EL is not discriminatory; but on the contrary seeks to ensure a level-playing field with respect to e-commerce activities undertaken by entities resident in India, and those that are not resident in India, or do not have a permanent establishment in India.*
- It was also clarified that the EL was applied only prospectively, and has no extraterritorial application since it is based on sales occurring in the territory of India through digital means.
- India-based e-commerce operators are already subject to taxes in India for revenue generated

from the Indian market.

- However, **in the absence of the EL, non-resident e-commerce operators (not having any Permanent Establishment in India but significant economic presence) are not required to pay taxes in respect of the consideration received in the e-commerce supply or services made in the Indian market.**
- The EL levied at 2% is applicable to non-resident e-commerce operator, not having a permanent establishment in India.
- The threshold for this levy is ₹ 2 crores, which is very moderate and applies equally to all e-commerce operators across the globe having business in India. The levy does not discriminate against any U.S. companies, as it applies equally to all non-resident e-commerce operators, irrespective of their country of residence.
- **There is no retrospective element as the levy was enacted before the 1st day of April 2020 which is the effective date of the levy.**
- It does not have extraterritorial application as it applies only to the revenue generated from India.
- **In addition, EL was one of the methods suggested by 2015 OECD/G20 Report on Action 1 of BEPS Project which was aimed at tackling the taxation challenges arising out of digitization of the economy.**
- The purpose of the Equalization Levy is to ensure fair competition, reasonableness, and exercise the ability of governments to tax businesses that have a close nexus with the Indian market through their digital operations.
- It is a recognition of the principle that in a digital world, a seller can engage in business transactions without any physical presence, and governments have a legitimate right to tax such transactions.
- The office of USTR on 6th Jan 2021 released its findings on the section 301 investigation into India's digital services tax (DST) and concluded that India's DST -the equalization levy - is discriminatory and

- restricts US commerce. Similar determinations were also made against Italy and Turkey on 6th Jan, 2021, itself.
- The Government of India will examine the determination/decision notified by the U.S. in this regard and would take appropriate action keeping in view the overall interest of the nation.

A Brief History and Way Forward

- USTR started an investigation in June last year against Equalisation Levy (EL), on the ground of Section 301 of the U.S. Trade Act of 1974.
- **The tax applied since April 1, 2020, covers all digital transactions in India, including e-commerce supplies by non-resident players.**
- Besides, the scope of DST was expanded to include transactions that use Indian data if the firm's revenue from India is Rs. 2 crore and above.
- The office of USTR said the law explicitly exempts Indian companies and targets non-Indian firms. This impacts U.S technology companies as they are taxed higher than their Indian counterparts. USTR noted that of the 119 companies liable under DST, 86 are U.S. companies.
- The tax is levied on companies with no permanent establishment in India and is applied to a firm's revenue rather than income. This is inconsistent with the international tax principles, it added.
- According to **the office's estimates, the tax creates an additional burden of \$30 million per year for the American companies**, *This is because India levies the digital tax on various categories of services that are not taxed in other countries.*
- In addition to this, USTR said DST increases the compliance cost of companies, which could run into millions.
- **Taking note of USTR's report, India said it would take appropriate action keeping in view the overall interest of the nation.**

Queries?

Feel free to reach us at :

Navjot.singh@taxtru.in/+91 99533 57999