22 June 2020

To
Smt Nirmala Sitharaman
Minister of Finance,
Ministry of Finance, Government of India
Rajpath Marg, E Block, Central Secretariat,
New Delhi, 110011, India

Dear Honourable Minister,

Subject: Recommendations to address concerns of non-resident e-commerce operators on the provisions for Tax Deducted at Source under section 194-O of the Income-tax Act, 1961

The Asia Internet Coalition ("**AIC**") is an industry association that represents leading global internet companies on matters of public policy. To further its mission of fostering innovation, promoting economic growth, and empowering people through the free and open internet, AIC would like to take this opportunity to raise our concerns regarding the recently enacted Finance Act 2020 which expands the scope of the equalisation levy, which stands to directly and significantly impact a wide range of SMEs, start-ups and end-consumers in India. Further the Act also imposes new measures on Tax Deducted at Source (TDS) on E-commerce transactions and provisions on Tax Collected at Source (TCS)**.**

AIC is an industry association comprised of leading Internet and technology companies in the Asia Pacific region with an objective to promote the understanding and resolution of Internet and ICT policy issues. Our members are Airbnb, Amazon, Apple, SAP, Google, Booking.com. Expedia Group, Facebook, LinkedIn, LINE, Rakuten, Twitter and Yahoo (Verizon Media).

AIC has been actively engaging with the Government of India on several policy issues and has contributed to policy dialogues and development to promote the country's digital economy. In the past we have submitted key recommendations on best practices, particularly on data protection, cybersecurity, e-commerce and taxation, and we appreciate our continued engagement with the government on the policy making process.

Against the backdrop of digitalization and growth of digital services across the world, and increasing role of internet companies, we are submitting this letter to express our views and recommendations on the TDS on E-commerce transactions (Section 194-O) and Amendments under Section 206C on TCS, which were introduced in the Finance Act 2020.

As such, please find appended to this letter detailed comments and recommendations, which we would respectfully like the Ministry of Finance to consider. Furthermore, we welcome the opportunity to offer our inputs and insights on industry best practices, directly through meetings and discussions and help shape the dialogue for the advancement of the digital ecosystem in India. We are grateful to be able to present our concerns on the matter, and would also like to reiterate our continuous support and assistance to the Indian government in its efforts.

Should you have any questions or need clarification, please do not hesitate to contact me directly at Secretariat@aicasia.org

Please accept, Honourable Minister, the assurances of our highest consideration and we look forward to hearing from your office.

Sincerely,

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Cc:

- **Shri Anurag Singh Thakur, Minister of State for Finance, Ministry of Finance, Government of India**
- **Shri Dr. Ajay Bhusan Prasad Pandey, Finance Secretary**
- **Shri Ritvik Ranjanam Pandey, Joint Secretary, Revenue**
- **Shri Dr. Krishnamurthy Subramanian, Chief Economic Adviser**

Detailed Comments and Recommendations

Introduction

The Finance Act, 2020 has inserted a new section 194-O in the Income-tax Act, 1961 ('the Act') to provide that every e-commerce operator facilitating the sale of goods or provision of services of an Indian e-commerce participant through its digital or electronic facility or platform, shall be required to deduct tax at source at the rate of 1% of the gross amount of sale or service or both, facilitated by the e-commerce operator. The e-commerce operator is obligated to deduct such tax irrespective of whether the e-commerce operator is involved in collecting payment from the purchaser of such goods/ services or not.

The withholding tax provision under section 194-O of the Act stands on a different footing *vis-à-vis* other withholding tax provisions, wherein even though the transaction is between the purchaser of goods/services and e-commerce participants, the withholding tax obligation has been cast upon the e-commerce operator, who is merely facilitating the transaction.

The provision has been introduced with the intention to widen and deepen the withholding tax net by bringing resident e-commerce participants within its ambit. Accordingly, the provision should ideally target those resident e-commerce participants who are currently not undertaking due tax compliances. However, the provision in its current form casts an onerous obligation on non-resident e-commerce operators to withhold tax even with respect to those resident e-commerce participants which are registered under the GST and income tax laws, and thus are already under the tax net.

Given the complexities involved in the business model of various non-resident ecommerce operators ("NREO"), the new provision poses immense challenges for undertaking the requisite withholding tax

compliances with respect to the Indian service providers (being e-commerce participants). In this regard, the issues identified NREO have been elaborated for your consideration in the ensuing paragraphs along with the appropriate recommendations.

Key Issues and Recommendations

1) Exclusion of non-residents ecommerce operators ("NREO") from the applicability of section 194-O of the Act

Issue

- As per section 194-O of the Act, **'e-commerce operator'** means *"a person who owns, operates or manages digital or electronic facility or platform for electronic commerce"*. As the law reads today, no exception has been carved out for the applicability of this provision to non-resident e-commerce operators. Hence, it makes them obligated to deduct and deposit tax on payments made to e-commerce participants, resident in India.

- As per section 1 of the Act, provisions of the Act extend to the "whole of India", i.e. the provisions of the Act are applicable to the territory of India. The term 'e-commerce operator' referred to in section 194-O of the Act has to be read in conjunction with section 1 of the Act. A conjoined reading of both the provisions suggests that the scope of section 194-O of the Act, cannot operate extra-territorially. In other words, withholding tax compliances under section 194-O of the Act cannot be extended to non-residents in the absence of a territorial nexus with India.

- Withholding tax compliances in India involve onerous responsibilities such as obtaining tax deduction account number, withholding and depositing of taxes, filing withholding tax returns, etc. This would cause immense administrative inconvenience to NREO and hamper ease of doing business in India. Further, any inadvertent non-compliance because of the administrative inconvenience will also result in consequential interest and penal implications, eventually increasing the overall cost of doing business in India.

- In this regard, reference is also made to a Circular[1] issued by the Central Board of Direct Taxes ('CBDT'), wherein, foreign companies have been granted exemption from withholding tax compliance[2] with respect to payment for professional services rendered by specified[3] Indian residents. Such exemption was granted considering the practical challenges faced by the foreign companies in undertaking the withholding tax compliances. It is requested that a similar exemption, from withholding tax under section 194-O of the Act, be granted to NREO Such exemption may be granted through section 194-O(4) of the Act, which provides a window to the CBDT to issue guidelines if any difficulty arises in giving effect to the provisions of section 194-O of the Act. Apart from the reasons outlined above, the rationale for such exemption could be the fact that the income of the e-commerce participants (being Indian resident) would in any case be chargeable to income-tax in India, thereby resulting in no loss of revenue to the Indian tax authorities.

Recommendation
Owing to the extra-territorial effect of the provision, administrative inconvenience caused and no loss of revenue to the Indian tax authorities, it is strongly urged that NREOs should be exempted from undertaking any withholding tax compliances under section 194-O of the Act.

2) Practical challenges in deducting and depositing tax where certain settlement process is fully automated without human intervention.

Issue

[1] CBDT Circular No. 726, dated 18 October 1995

[2] Under section 194J of the Act

[3] Fees for professional services paid by foreign companies or foreign law and accountancy firms to persons resident in India

- There is a practical challenge in deducting and depositing tax where settlement process is fully automated, for example where settlement between the NREO and the service provider is done using the global virtual card system, it is fully automated without involvement of any manual process. Thus, there is no scope for the NREO to withhold any tax from the amount paid to the service provider.

  Considering the fact that this mechanism to settle dues of service providers (including Indian service providers) is deployed by the NREO worldwide, it is extremely challenging to revamp the whole automated system and make an exception with respect to the Indian service providers, to facilitate withholding of tax under section 194-O of the Act.

Recommendation
Given the practical challenges faced in withholding tax on certain payments made to the Indian service providers, NREOs should be granted exemption from undertaking any withholding tax compliances under section 194-O of the Act.

3) Impossible to deduct tax where payment is made directly by purchaser to the resident service provider

Issue

- As per Explanation to section 194-O(1) of the Act, the e-commerce operator is obligated to deduct tax even where the payment is made directly by the purchaser of goods/ services to the service provider, for transaction facilitated by an e-commerce operator.

- Accordingly, NREOs would be obligated to undertake withholding tax compliances even where payments are made directly by the purchaser to the service providers. It may be noted that in such a scenario, NREOs have no control over the payments made directly to the service providers and hence, practically it is impossible for NREOs to withhold any tax from such amount

- If the current provisions are given due effect, NREOs will have to deposit taxes from their own pocket, which would immensely stress their working capital. This will adversely impact the business of NREOs in India, especially for NREO who operate on very low margins.

- The Goods and Services Tax ('GST') laws provide for a similar provision[4] where e-commerce operators are required to collect tax at source ('TCS') on the amount paid to certain service providers. As per provisions under the GST laws, the liability on e-commerce operators to collect such tax arises only in a scenario where the consideration with respect to the supplies is to be 'collected' by the e-commerce operator. Thus, the e-commerce operator is liable to collect tax only where the payment to the service provider is made through the e-commerce operator. However, a similar provision is absent under section 194-O of the Act, creating an obligation upon the e-commerce operator to deduct tax even where the payment to the e-commerce participant (i.e. the service provider) is made directly by the purchaser of goods/ services.

Recommendation

Without prejudice to the requests made under point 1 and 2 above, given the impossibility and impracticality of withholding tax compliance by NREOs and consequential working capital impact, the withholding tax provisions under section 194-O of the Act should not be made applicable where payment is made directly by purchaser to the service provider. Necessary guidelines should be issued by the CBDT under section 194-O(4) of the Act to this effect.

4) Devising measures to ease compliance burden under section 194-O of the Act

Without prejudice the above requests, in the event where compliance is applicable and in order to ease out the compliance burden on non-resident e-commerce operators, the following recommendations should be considered:

[4] Section 52 of the Central Goods and Services Tax Act, 2017

a) Increase the threshold for applicability of the provision and extend the exemption to other entity forms

- Section 194-O(2) of the Act provides that an e-commerce participant, being an individual or a Hindu Undivided Family, would be exempt from applicability of these provisions, if:
  - Gross amount from sale or services or both during a previous year does not exceed INR 0.5 million; and
  - Such e-commerce participant has furnished a Permanent Account Number or Aadhaar Number to the e-commerce operator.

- The aforesaid exemption does not apply to other entity forms, such as company or partnership firms, irrespective of such entities being below the threshold envisaged under section 194-O(2) of the Act. Further, the threshold of INR 0.5 million is very low considering that the non-resident e-commerce operator, being a NREO, would be dealing with a number of service providers in India.
- Accordingly, restricting the exemption under section 194-O of the Act to a limited category of Individuals and Hindu Undivided Family would pose unnecessary compliance burden on the NREOs.

b) Filing of periodic statement in lieu of tax withholding and consequential compliances under section 194-O of the Act

- In view of the practical difficulties involved in undertaking withholding tax compliances by a NREO, the Government should consider prescribing a mechanism for filing of a periodic statement (say, on a quarterly or half-yearly basis) by such NREO to a designated authority, providing a list of the Indian residents to whom payment has been made by the NREO.

- Since the withholding tax incidence under section 194-O of the Act is on the resident e-commerce participant, such a mechanism would achieve the twin objectives of:

- Ensuring that the Government has the necessary data of Indian residents receiving income from the non-resident e-commerce operator; and
- It would also result in easing out the practical difficulty of undertaking withholding tax compliances by non-resident e-commerce operators in India.

- It is worth noting that the CBDT has prescribed a similar mechanism[5] with respect to payments made by foreign companies or foreign law firms to certain categories of Indian residents with respect to fee for professional services. The said mechanism was put in place by the CBDT after taking cognizance of the practical difficulties involved in undertaking withholding tax compliance by such foreign companies or foreign law firms.

c) Filing of declaration in lieu of undertaking withholding tax compliances

- Considering the practical challenges involved in undertaking withholding tax compliances by a NREO, a mechanism may be prescribed wherein such non-resident files an annual declaration to the effect that the resident e-commerce participant (i.e. service provider) has taken into account the amount due from the NREO while computing its taxable income. Such a declaration can be filed by the NREO on the back of confirmation received from the resident e-commerce participant. Once the declaration is filed, the same should be considered as a sufficient discharge of withholding tax obligations of the NREO and should not trigger any withholding tax proceedings for recovery of underlying tax or consequential interest/ penalty.

- While a similar mechanism is in place under the existing provisions[6] of the Act, the same does not absolve the payer from consequential interest implications. Further, the existing provisions also require obtaining and furnishing of Chartered Accountants certificate in case of each resident entity by the payer. Considering the huge volume of transactions and entities that the NREO would be dealing with, it would be administratively burdensome to obtain a Chartered Accountant's certificate from each resident e-commerce participant.

[5] CBDT Circular No. 726 dated 18 October 1995

[6] Proviso to section 201(1) of the Act

d) Authorizing Indian entity to undertake compliances on behalf of NREO

- The existing provisions of the Act[7] provide a window for a NREO, being an e-commerce operator, to authorize any person in India for the purpose of undertaking withholding tax compliances.

- As of now, there is no mechanism prescribed by the Government for authorizing any person in India by such NREO. In the absence of such a mechanism, the NREO would be burdened to carry out onerous withholding compliances (viz; obtaining tax deduction account number, withholding and depositing of taxes, filing withholding tax returns, etc).

- Without prejudice to other requests made in this letter, the mechanism for authorizing an Indian entity for undertaking withholding tax compliances on behalf of the NREO should be prescribed.

Recommendation

Without prejudice to other requests made in this letter, in order to alleviate voluminous compliances by NREOs, the Government should consider the following measures:

- The exemption under section 194-O(2) of the Act should be extended to entity forms viz; partnership firms, companies etc. and the threshold of INR 0.5 million should be enhanced to prevent undertaking withholding tax compliances for a large number of service providers.
- A mechanism should be prescribed for filing of a periodic statement by the NREO in lieu of undertaking withholding tax compliances, similar to the mechanism

[7] Section 194-O(6) of the Act read with section 204(v)

introduced by the CBDT for specified categories of payments made by non-resident companies [as stated in point b) above].

- A mechanism should be prescribed for filing of a declaration by the NREO stating that the respective service providers have considered the income received from the NREO for the purpose of paying income-tax thereon. Further, such declaration should absolve the NREO from any interest/ penal implications.
- Guidelines should be issued for authorizing an Indian entity by the NREO solely for the purpose of undertaking withholding tax compliances under section 194-O of the Act.

The aforesaid mechanisms/guidelines may be prescribed pursuant to section 194-O(4) of the Act, which provides a window to CBDT to issue guidelines if any difficulty arises in giving effect to the provisions of section 194-O of the Act.