

Taxation of E-Commerce Transactions

Some Key Points

E-commerce means consumer and business transactions conducted over network, using computers and telecommunications. It includes on-line shopping, on-line trading of goods and services, electronic fund transfers, electronic data exchanges and on-line trading of financial instruments.

OECD defines e-commerce transactions as commercial transactions between individuals and organizations, based on the processing or transmission of digitized data units, sound and visual images, which are carried out over open networks (like internet) or closed networks (like minitel) with a gateway to open networks. This more specific definition would therefore exclude electronic data interchange (EDI), carried out over closed networks, if such EDIs are being used by themselves, without access to open network (example, credit cards used over a closed network, connecting specified merchants with a card organization).

Difficulties in taxing e-commerce transactions

- (a) Determination of economic attachment
- (b) Identification of the existence of permanent establishment
- (c) Tracing commencing and end point of transaction
- (d) Lack of documentation to know the nature of contract.

Business through e-commerce

- (a) Electronic advertising
- (b) Electronic sales
- (c) Electronic delivery

Question 1

Explain the core reasons for difference between the e-commerce transactions and the traditional business transactions causing difficulty to tax the income of e-commerce transactions.

Answer

The core reasons for difference between e-commerce transactions and traditional business transactions causing difficulty to tax the income from e-commerce transactions under the Income-tax Act, 1961 are **absence of national boundaries, non-requirement of physical presence of goods and non-requirement of physical delivery in e-commerce transactions**. Since e-commerce transactions are completed in cyberspace, it is often not clear as to the place where the transaction is effected, thereby causing difficulty in implementing source rule taxation.

Question 2

E-commerce transactions have replaced concepts generally associated with international transactions traditionally. Discuss briefly the issues involving such transactions.

Answer

E-commerce transactions, in its widest sense, means business transactions conducted over a network, using computers and telecommunication. E-commerce is a method of transacting business and is not a transaction by itself. Such a method will involve electronic advertising, electronic sales and electronic delivery.

The issues involving e-commerce transactions are as follows:

- (i) Traditional business rests squarely on the physical presence and delivery of goods, but e-commerce transcends geographical barriers.
- (ii) Income out of an international transaction is subject to tax both in the Home State by virtue of “personal attachment” to the transfer and in the host State by virtue of “economic attachment” to the income itself. Thus, this gives rise to double taxation of the same income.
- (iii) Tax treaties seek to tax profits on the basis of what is popularly known as “Permanent Establishment”. However, in the case of e-commerce transactions, no establishment is required across the border to carry on business.
- (iv) Taxable jurisdiction of any country covers its national boundaries. E-commerce takes place through satellite and the server can be in any part of the globe and in all probability, in a tax haven country.
- (v) For adopting the existing principles to e-commerce situations, there are two key areas:
 - (a) the extent to which a web-site can constitute a permanent establishment and how income may be attributed to it;
 - (b) the manner in which payments for digitized products are to be characterized.

The source rule of taxation embodied in section 9 will become increasingly difficult to apply and increasing emphasis would be given on the Residence Rule. Such a situation could spell diminishing revenues for developing countries, particularly in situations of technology transfers, where host States are generally developing countries.

Self-examination Questions

1. Explain what is meant by “e-commerce”.
2. Discuss the issues and problems in taxing e-commerce transactions.
3. Explain how businesses are transacted through e-commerce.
4. How is existence of a permanent establishment determined in e-commerce situations?
5. Explain in detail the manner of taxation of income arising from e-commerce transactions.