

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

"The existence of a website on Indian Soil constitutes a permanent establishment". Is this statement correct? Examine.

Answer

The term "permanent establishment" has not been defined in section 2 of the Income-tax Act, 1961. As per section 92F(iia), "permanent establishment" includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.

The term "permanent establishment" includes (a) a place of management (b) a branch, (c) an office, (d) a factory, (e) a workshop, (f) mines, (g) warehouse, etc. In most of the DTAAs, an

exhaustive definition of the term “permanent establishment” is given, wherein several more items are enumerated.

A website is a set of web documents belonging to a particular organization. It consists of data and programs in digital form, from which it is stored in a server which is accessible through internet.

A website does not normally imply “a fixed place of business”, even though in the case of some entities, some business could be transacted through a website. Thus, the mere presence of a website in Indian soil, without anything more, will not amount to a permanent establishment.

If the website contains merely information about the concern, the website cannot be regarded as a permanent establishment. Where the website is being used as a virtual office for transacting orders of purchases or sales or for rendering services on a more than casual basis, then it could be regarded as a permanent establishment.

Question 2

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 3

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

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“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.

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.