

# USA's S301 report on Equalisation Levy and Indian Response

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In news

India responses to S 301 report of US on Equalisation Levy

What is an equalization levy?

- The "Equalization Levy" is a tax aimed at taxing the digital transactions i.e. the income accruing to foreign e-commerce companies from India.
- Equalisation Levy was first introduced in India by Finance Act 2016 as a separate Chapter VIII titled 'Equalisation Levy' to provide for an equalisation levy to be deducted from amounts paid to a non-resident not having any permanent establishment in India, for specified services.
- It covers all business to business and business to consumer transactions, third-party and related party transactions, across digital and non-digital businesses, where goods and services are sold online.

Background

- The U.S. administration had announced initiation of **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 United Kingdom.
- With respect to India, the focus of the investigation was on the 2% Equalisation Levy (EL) levied by India on

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.

### India's arguments

- In this regard, the U.S. requested for consultations, and India submitted its comments to the US Trade Representative (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 extra-territorial 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 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 on non-resident e-commerce operator, not having a permanent establishment in India.
- The threshold for this levy is Rs. 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 extra territorial application as it applies only on 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.

#### USTR report (S-301)

- 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 equalisation levy – is discriminatory and restricts US commerce.**
- The US has held that India's digital tax (2 per cent) on technology majors is unreasonable, burdensome, and discriminatory against
- The USTR has noted that India's digital services tax (DST), or equalisation levy, was "actionable" under Section 301 of the Trade Act, which may mean retaliatory tariffs on Indian products.

- It found India's equalisation levy to be inconsistent with international tax principles because it failed to provide tax certainty, targeted revenues unconnected to a physical presence in India, and applied to revenue rather than income.
- Highlighting the supposed discrimination, the report said of the companies that were subjected to India's equalisation levy, 72 per cent were American.
- Section 301 of the US Trade Act empowers the USTR to investigate a trading partner's policy action that may be deemed unfair or discriminatory and negatively affects US companies, and take action, including tariff-based and non-tariff-based retaliation.
- Similar determinations were also made against Italy and Turkey on 6th Jan, 2021, itself.

### India's response

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.