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How we can help
The technology sector is undergoing a significant transformation with substantial disruptive innovation in an evolving digital world. New technologies such as Smart Mobility are moving to on-demand models that are driven by mobile apps; social media is disrupting traditional business models with social advertising, and peer-to-peer-payment and Internet of Things are coming into mainstream use with connected cars, devices, remote monitoring of health, etc.

Innovation in technology cuts across domains, purviews, dialect-related hindrances and demography, and has changed the way in which business is done. In terms of the business landscape, technology is being embraced in different segments and is driving development, business openings and associations amongst tech and non-tech organisations in different territories, for example, in Fintech, Edutech and Healthtech. This can be illustrated by highlighting how innovation has changed transportation in India. For example, hailing a taxi is now easy due to the latest technologies used by apps and smartphones, which enables us to book a cab with the click of a button. This has given a major boost to the taxi industry.

Technology is accelerating disruption across various sectors, and consumers are showing a strong appetite for and actively participating in a sharing-based economy in several sectors. This is driving organisations to develop on-demand sharing business models. Among the segments that are at the cutting edge of innovative disruption are the eCommerce and Internet sectors, which have seen unprecedented growth over the last few years. Moreover, the web is altering channel-related preferences and consumers are increasingly opting for an ‘online first’ approach in their shopping, beginning their research online and supplementing their search via web resources. However, they may conduct their transactions either online or offline (in-store).

eCommerce and internet businesses are driving the rapid growth of the domestic IT-ITeS industry, attracting unprecedented global interest and funding. Indian eCommerce and internet companies are growing rapidly with about 460 million internet users and a tele-density of around 85%. Increasing penetration of the internet, adoption of smartphones and minimal effort low-cost mobile devices, changing demographics, mobile-empowered youth and the emergence of tier 2 and tier 3 cities as major shopping hubs have been driving the growth of the industry, with new retail forces shifting its dynamics. Furthermore, the continued growth of large pure-play organisations that are powerhouses have moved retailers’ focus to the web channel. These companies are not only becoming gateways to product research but have also introduced consumers to new ways of viewing the retail process.

However, the transition of retail sales from the offline to the online mode—a multi-trillion dollar opportunity—is still in its early innings in India and there is significant opportunity for further growth. Continued refinement of technology, the addition of new analytics capabilities and rolling out of same-day delivery are key drivers that could accelerate the growth of the segment.

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1 India Internet Users — Internet Live Stats, accessed on January 16, 2017
2 India Telecom Stats: 7M New Mobile Subscribers Added in Jan-16, Tele-Density Crosses 80%, Trak.in, January 6, 2017
eCommerce and Internet businesses in India are slotted in two broad categories—based in India and operating outside India. Since the taxation system in India is source-based, i.e., the physical presence of an entity is required for a transaction to be taxable in India, the real test lies in bringing transactions conducted in the digital environment within the tax net. In order to address this, the Organisation for Economic Co-operation and Development (OECD) has constituted a committee to review digital transactions and formulated suitable measures to avoid tax leakages. The committee has suggested the implementation of the BEPS Action plans, which recommend ways of taxing transactions in the digital economy. Accordingly, the Government of India has introduced various measures such as the Equalisation Levy (at the rate of 6%) and enlargement of the scope of Service Tax (at the rate of 15%) to bring digital supplies under the ambit of these taxes. This has increased compliance-related requirements in business functions. However, since this concept is new in India, the authorities and business drivers are expected to witness controversies in the future.

In this report, we have attempted to showcase the various Direct Tax-, Indirect Tax-, Transfer Pricing- and Regulatory-related challenges eCommerce and internet businesses face, and the key areas on which they should focus. To incorporate a focused approach in our analysis, we have limited our coverage of businesses to five major business segments in the eCommerce and Internet sector—Over-the-Top (OTT), Online Advertising, eTail and Marketplace, Digital Payments and Cloud.

I hope you find this report interesting and would welcome your feedback on it.

With kind regards,
Sandeep Ladda
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Tax and Regulatory framework in India
A. Overview of key regulations

The rise of the internet economy has led to the emergence of a large number of technology service providers that use digital interfaces, and analytic and proprietary technologies to create disruptive business models. In particular, the eCommerce and digital payment segment has been evolving exponentially of late. This is posing challenges for start-ups (which find it difficult to operate as regulated entities) as well as for existing players (which need to align their business models to ensure their compliance with tax laws).

Regulations play a key role at various stages of the business lifecycles of eCommerce and internet companies when they set up their operations and design their operating models in their ongoing businesses, when they bring in local and foreign investors to fund them, and to expand their business operations organically and inorganically.

At each stage of their lifecycles, entities will need to be well-positioned to manage multiple and varied regulatory changes. Keeping a close watch on regulatory and government initiatives is therefore the only way in which they can prepare themselves to keep pace with future disruptions.

Increasing foreign investments in India, and simplification and rationalisation of policies are the focus areas of the present Government in its effort to create a positive regulatory environment in the country. Working towards this, it has notified the eagerly awaited guidelines to clarify India’s foreign investment rules relating to its marketplace-based eCommerce model. These guidelines have largely put to rest uncertainties relating to eCommerce business models (as well as FDI). In addition, RBI has been issuing guidelines from time to time to facilitate cross-border trade and payment transactions.

B. Overview of direct taxes in India

In India, direct tax is governed by the Income-tax Act, 1961 (the Act), along with the Income-tax Rules, 1962 (the Rules).

I. Overview of Income-tax on corporate income

A resident company is taxed on its global income; a non-resident one is only taxed on income that is received, accrued or deemed to accrue or arise in India. An organisation is considered to be a resident of India if it is incorporated in the country or its Place of Effective Management (POEM) is in India. The term POEM refers to the place where the company’s key management and commercial decisions (necessary for the conduct of the entity as a whole) are made in substance. An LLP registered in India is considered to be a resident in the country, except if control and management of its affairs are wholly located outside the country during the year.

The corporate tax rate for a resident company whose total turnover or gross receipts do not exceed INR 50 million is 25% and in other cases it is 30%. Foreign companies are taxed at the rate of 40% on the income they source from India. In addition, there are specific categories of incomes such as royalty, Fees for Technical Services (FTS) and interest, which attract lower tax rates that are applicable subject to satisfaction of prescribed conditions. Indian LLPs are taxed at the rate of 30%.

Resident and non-resident companies are also required to pay Minimum Alternate Tax (MAT) on their adjusted book profits if their tax liability on their total income is less than 18.5% of these. Alternate Minimum Tax (AMT) is levied on LLPs on their total adjusted income. Indian companies distributing or declaring dividends are also liable to pay Dividend Distribution Tax (DDT) at 15%.

II. Income-tax levied on non-resident or foreign companies

In the hands of a non-resident company, income is deemed to accrue or arise in India if:

• the company’s income is earned from any business connection, property, asset or source of income in India.

• interest, royalties and FTS are paid to a non-resident (subject to certain conditions).

• it has earned capital gains from transfer of assets situated in India. (This also includes transfer of shares or interest in a company situated outside India if such shares or interest directly or indirectly derives their substantial value from assets located in the country.)

India has entered tax treaties with over 85 countries to provide relief for income earned by Indian companies abroad as well as for income arising to foreign companies in India.

In order to avail of benefits under these tax treaties, foreign companies are required by Indian revenue authorities to provide a copy of the Tax Residency Certificates issued to them by revenue authorities in their countries of residence, along with appropriate details and documentation. An emerging issue faced by foreign entities, especially in the eCommerce and internet business, is whether their business activities in India are considered to constitute a permanent establishment (PE) in the country. However, there is limited guidance available for attribution of profits to such PEs and this continues to be a largely untested area from the standpoint of Transfer Pricing in the country.

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2 The CBDT has notified final POEM guidelines vide Circular No. 06 of 2017 dated 24 January, 2017.
3 Plus applicable surcharge and education cess
III. Compliance-related requirements

All assessees are required to obtain a Permanent Account Number (PAN) or Tax Registration Number and file tax returns in India if they earn taxable income in the country.

Non-residents (except companies) are required to file their tax returns by July 31. Resident and foreign companies, for which a Transfer Pricing accountant’s report with respect to their international or specified domestic transactions is not required, need to file their tax returns by September 30. Such organisations need to submit a transfer pricing accountant’s report to file their tax returns by November 30.

Residents or non-residents can approach the Authority for Advance Ruling (AAR) to determine their tax liability for their existing and proposed transactions, subject to certain conditions. However, while the AAR has a timeline of six months to dispose of applications, this generally takes one or two years, depending on pending applications. A ruling from the AAR is binding on applicant assessees and jurisdictional Income-tax authorities.

The Government of India has recently undertaken several initiatives, e.g., introduction of e-Assessment (whereby assessees are to file submissions via email), a Dispute Resolution Scheme to reduce litigation in India, reduction of corporate tax rates for specific companies, and so on. These schemes are directed at easing the process of doing business in India and cutting down on long-drawn-out litigation.

IV. Equalisation Levy and GAAR

In recent times, India’s digital economy has grown exponentially. This growth has brought in its wake inherent complexities. An Equalisation Levy (at the rate of 6%) was introduced with effect from June 1, 2016, to tax revenue earned by non-residents (who do not have a PE in India) from online advertisements, provision of digital advertising space, or any other facility or service for the purpose of such advertisements. This tax is only levied when the aggregate consideration for specified services exceeds INR 1,00,000 during a financial year.

Payers who are Indian tax residents or non-residents with a PE in India at the time they make such payments need to deduct the Equalisation Levy. Going forward, the scope of the levy may be expanded to cover other digital, eCommerce and internet transactions in light of the recommendations of the eCommerce committee set up by the Central Board of Direct Taxes (CBDT).

The Government of India has announced its implementation of the General Anti-Avoidance Rules (GAAR) from April 1, 2017 onwards. Under the provisions of GAAR, Indian tax authorities will have the power to invalidate any arrangement (either in whole or in part) as an Impermissible Avoidance Agreement (IAA) if its main purpose is to obtain a tax benefit. These provisions will be applicable if the tax benefit from an arrangement exceeds INR 30 million in a year. However, GAAR will not be applicable for investments made prior to March 31, 2017. The onus of substantiating that a transaction is not in the nature of an IAA lies on the taxpayer.

C. Overview of Transfer Pricing provisions in India

India’s Transfer Pricing law is broadly aligned with the OECD’s Transfer Pricing guidelines and focuses on identifying the key functions, assets and risks (FAR) of related parties in a transaction as well as on aligning the pricing policy agreed on by the parties involved in allocation of the FAR.

Some salient features of Transfer Pricing provisions in India:

I. Captive entities

Indian entities providing a captive platform, software development or related support services need to be compensated at arm’s length for such activities. If a cost-plus model is contemplated, it is imperative to consider Circular 6 of 2013 issued by the CBDT, which includes a list with criteria (relating to functions, assets and risks) that need to be satisfied to characterise an Indian enterprise as a low-risk entity (for R&D-related activities). In the event the cost-plus model is not appropriate, other approaches may be considered, including the profit split method.

Indian regulations also comprise safe harbour margins for some business activities. These include provision of software development services. However, safe harbour regulations have received a lukewarm response due to their high threshold. The Government is expected to revise the regulations and reduce the threshold in coming months.

II. Funding

eCommerce and internet businesses are driven by foreign investments in India. A key challenge is determination of returns attributable to an entity that only provides funding without playing a role in development or management of its business in India. The OECD’s guidance seems to suggest that an entity providing funding without actively participating in the business (generally referred to as a ‘cash box’) should only be eligible for a risk-free or risk-adjusted rate of return. However, we need to look at the guidelines in the context of the eCommerce sector in view of the importance of funding for eCommerce players, the majority of which are start-ups, as well as the risk of the investment failing.

The risk-adjusted return could be substantially high in the case of funding of eCommerce start-ups.
III. Returns attributed to intangible property such as platforms, brands and technologies

BEPS Actions 8-10 provides guidance on allocation of returns derived from exploitation of intangibles. This guidance suggests that returns derived from intangibles should be allocated to associated enterprises for functions performed, assets used and risks assumed in their development, enhancement, maintenance, protection and utilisation.

To provide certainty to taxpayers, Indian regulations include provisions relating to the Advance Pricing Agreement (APA), which allows unilateral, bilateral and multilateral APAs. An APA can be applicable for a period of five years, with the option of a rollback for up to four years. The Government’s APA programme has been progressing well and it has signed APAs with complex profit split methodologies. India has also implemented a successful Mutual Agreement Procedure (MAP) programme with major trade partners including the US, the UK and Canada.

To align India’s Transfer Pricing law more closely with international best practices, Budget 2017 proposes to introduce provisions relating to secondary Transfer Pricing adjustments. The Budget also intends to implement guidance provided under BEPS Action 4 and has introduced provisions to limit deductions on interest and other financial payments made to associated enterprises. Detailed regulations and clarifications on these provisions are awaited.

D. Overview of indirect tax laws in India

I. Service Tax

Service Tax is levied by the Central Government on provision of services in India. The current effective Service Tax rate is 15% (14% Service Tax, 0.5% Swachh Bharat Cess and 0.5% Krishi Kalyan Cess).

Any service (comprising an activity conducted by a person for another for a consideration) in a taxable territory is taxable unless it is included in the Negative List or has been notified as being exempt. The Place of Provision of Service Rules, 2012 needs to be analysed to determine whether a service has been provided in a taxable territory.

Typically, the liability to deposit Service Tax is on the service provider. However, in some cases, this liability has been shifted to the service recipient under the reverse charge mechanism.

II. Value Added Tax (VAT) and Central Sales Tax (CST)

VAT or CST is levied on sale of goods in India, depending on their movement. Sale involving such movement within a state constitutes an intra-state sale and attracts VAT. The general VAT rate ranges from 5% to 15%, depending on the nature of the goods and the relevant state VAT legislation.

Sale involving movement of goods from one state to another is subject to CST. The CST rate is either equivalent to the local VAT rate of the dispatching state or 2% in some cases.

VAT or CST is not levied on goods when a sale takes place outside India or in the process of products being imported or exported.

III. Customs Duty

Customs Duty is levied by the Central Government on import of goods to India. The liability to pay Customs Duty is on the importer.

The generic Customs Duty rate is 29.44% (and comprises various components). The actual rate depends on the nature of the products, the purpose of the imports, etc.

There are various other indirect taxes such as Excise Duty levied on manufacture of goods, Entry Tax and Local Body Tax on entry of goods into a state, and an R&D cess on import of technology and Entertainment Tax on transactions relating to entertainment.

Since the growth of the eCommerce and Internet sector is a relatively new development in India, the country’s conventional Indirect Tax regime has been largely unsuccessful in providing complete clarity on the appropriate tax treatment of such transactions. This has led to substantial litigation relating to indirect taxes.

IV. Goods and Service Tax (GST)

Currently, India has a highly complex tax environment due to multiple taxes and tax cascades. Therefore, a comprehensive consumption-based tax, to be levied on supply of all goods and services, has been proposed — GST.

Status of GST: Updated Model GST laws were released in November 2016 and the draft rules have been announced by the Government. The GST Council has deliberated on the Model GST laws, which were expected to be passed in the second half of the Budget session in Parliament in March 2017. Categorisation of GST rates is expected in April or May 2017 and the Government is looking at July 1, 2017 as the rollout date for GST. On the IT front, the registration migration process has already been initiated.

Dual GST model: There is to be a dual GST model, with intra-state transactions attracting CGST and SGST, and inter-state transactions attracting IGST.

GST is the most significant indirect tax reform ever proposed in India and will subsume the majority of taxes currently levied. Therefore, it is imperative to analyse its implications for all transactions taking place in the country.
Key segment-wise issues from the perspective of Regulatory, Direct Tax, Indirect Tax and Transfer Pricing
India's eTail and Online Marketplace segment continues to grow at a double-digit pace every year, taking a substantial share from physical retail stores bit by bit. Growing at a steady rate of 45% to 50% year on year, the market is expected to be in the range of US$ 28–30 billion by 2020. Online shopping is forecast to account for two-thirds of the total eCommerce market, edging out travel. And looking at its pace of current growth, the fashion and lifestyle segment is soon likely to emerge as the largest eTailing category. Other categories such as online food retail and furniture are still miniscule in size, but are witnessing increased traction with innovation.

Adoption of smartphones and increasing penetration of the internet have continued to drive the growth of the eTail and Online Marketplace, as is evident from the volume of business from Tier 2 and 3 towns. In 2016, the segment focused on providing a unique and diverse customer experience and improving its bottom line, compared to the discounts companies offered in previous years. In addition to offering an enhanced user experience and expedited delivery, organisations are now focusing on improving their hardware and mobile-centric apps, and increasing their investments in technologies such as artificial intelligence and virtual reality. Recurring trends in transformation, consolidation and investment in emerging technologies continue to evolve rapidly in the eTail and Online Marketplace segment. Moreover, the industry has seen several M&As in the past few months and increasing interest in digital assets from non-digital buyers. Furthermore, factors such as clarity on laws on eCommerce and subsequent opening up of FDI in the marketplace should also boost its growth.

Mobiles continue to play a critical role, and this year, the focus is expected to be on further improvements in last-mile delivery, building of hyperlocal networks as well as on attracting more small businesses online and helping them enter exclusive tie-ups with brands. With the emerging online medium of doing business, traditional retailers are also expected to explore the platform and adopt an omni-channel strategy. And as the industry moves from acquisition to retention of customers to ensure their sustainable growth and profitability, investors are likely to exit or consolidate their portfolios.

With more and more consumers preferring the online marketplace to traditional brick-and-mortar stores, the importance of the former has been growing at a rapid pace. Consequently, this business model has been a lucrative investment opportunity for foreign investors in India. However, due to its growing importance and exponential growth, the sector has been seeing protracted litigation relating to tax-related issues. Some major tax- and regulatory-related concerns encountered in this business model are discussed in the following pages.
Mechanics

Movement of goods
- Independent distributor sells to customers directly.
- Independent retailers list goods in the marketplace.
- Customers order goods from the marketplace.
- The marketplace informs independent retailers about processing customers’ orders.
- Independent retailers ship goods to customers.

Movement of consideration
- The marketplace entity charges a listing fee to independent retailers to list their goods.
- End consumers make payments through the following channels using these options:
  - Debit or credit card
  - Online banking
  - Digital payment
  - Cash on Delivery (CoD)
- The amount collected through the channels (mentioned above is deposited in escrow accounts.
- The marketplace pays independent retailers from such escrow accounts.
Alternatively, there are other business models in the eTail and Marketplace segment, which could add complexities to the model (as indicated above).

Direct Tax
Foreign company: When a foreign company transfers its intellectual property (IP) to set up a marketplace in India, it needs to be evaluated whether this transfer qualifies for royalty, especially in light of retrospective amendments under the Act and Indian tax treaties. Furthermore, it is imperative to analyse the implications of the Budget 2017 proposal relating to certain tax terms used in Indian tax treaties that have not been defined in these.
There is also a need to analyse the PE exposure of a foreign company in India, depending on the location of its server and its activities. If a PE is established for the foreign company, its payments arising in India will be subject to tax in the country at the rate of 40% on a net basis, according to the provisions of the Act.
Since the foreign company may earn a taxable income in India, it may need to comply with the country’s Income-tax return filing obligations to report income sourced from it.

Indirect Tax
A company will need to evaluate VAT- or CST-related implications (along with the tax rate) on goods sold by independent retailers or distributors to customers located around the country. Currently, there is ongoing litigation about who should pay VAT or CST on such sales (retailers or the marketplace). Various state VAT authorities contend that the marketplace may need to deposit VAT. The factual pattern and relevant state VAT legislation should be analysed by the company in this regard.
There is ongoing litigation about whether Entry Tax5 is applicable on goods entering a state (when purchased online). The validity of this has been challenged in various states and the matter is pending before the courts. Some courts have held in favour of e-Commerce players and granted a stay. There is a need to evaluate the implications of Entry Tax and who is required to deposit it—the end customer, logistics company or seller.

The implications of Service Tax on listing fees, commissions, etc., payable to the marketplace, along with availability of credit, needs to be analysed.
In addition, various other aspects such as taxability of discounts and discount funding, the applicability of waybills, the taxability of combo offers and digital supplies such as eBooks (whether liable to Service Tax or VAT or both) and other similar potential issues should be evaluated. However, the implications may differ from state to state.

Furthermore, if the marketplace is operated by an overseas entity and not an Indian one, the concept of the Online Information and Database Service (OIDAR) should be analysed wherein the overseas marketplace needs to be registered in India for specified digital services provided for B2C transactions (with effect from December 1, 2016). This has separate compliance-related obligations for overseas marketplaces and the impact needs to be analysed, based on facts and the nature of the service provided.

GST
Some important aspects to be analysed under GST:
- State in which GST needs to be paid
- Taxability of free supplies and reversal of credit
- Availability of credit for marketplace and independent retailers
- Requirement of TCS by marketplace and compliance measures associated with this
- Transition and cutover issues such as credit on transition stock, sales return and treatment of ongoing contracts
- Taxability in the case of overseas marketplace – OIDAR provisions
- Enablement of provision in GST to shift tax liability to marketplace for

PwC
supplies made through its portal by Indian merchants – to be analysed in detail

Various other aspects such as an advance on sale of goods, sale on a return basis, stock transfers, taxation of digital supplies and actionable claim, e.g., gift vouchers, requirement of registration, also need to be analysed.

**Transfer Pricing**

Where a foreign company owns the Intellectual Property Rights (IPR) in the technology platform on which an eTail and Marketplace business is run in India, the enterprise should ideally be entitled to an arm’s length royalty for granting use of the technology platform to the Indian marketplace entity. From the Indian Transfer Pricing perspective, the royalty rate needs to be justified by a comparability analysis being undertaken of the royalty rates charged by an independent entity for the right to use similar IPR under similar economic circumstances being granted.

An Indian marketplace entity will also need to establish the benefits derived by it from its use of the marketplace.

The marketplace model will require an Indian marketplace entity to be significantly capitalised and funded. Assuming that such funding is provided by a foreign company, it will be entitled to a return for providing funds to the Indian entity. The return will depend on the functions performed by the foreign company (in identifying the opportunity and deciding to invest in India through the marketplace model and deciding to bear the investment risk) and the risks it assumes (in carrying out relevant decision-making functions relating to the investment-related risk and in its having the financial capacity to take on this risk).

**Regulatory—FEMA**

Foreign Direct Investment (FDI) in the eCommerce sector has been subject to stringent regulations and a matter of significant debate over the last four to five years. In early 2016, the Government issued its guidelines to clarify rules for FDI in marketplace-based eCommerce models. Therefore, while structuring a marketplace business in India, a company needs to ensure its compliance with conditions set out in these guidelines (with a 25% cap for the sales of a vendor or group companies, with no direct or indirect influence of the prices of goods prices on the marketplace entity).

Currently, non-bank entities engaged in collecting money from customers to enable a settlement with sellers (generally known as payment gateway and aggregation services) are indirectly regulated by RBI. Such entities are required to set up special purpose bank accounts and ensure their compliance by means of prescribed debits and credits in their accounts. Moreover, while setting up the payment and collection process, a company needs to put in place the right process flow to collect funds received through online channels (cards, net banking, wallets, etc.), keeping in mind the defined roles and responsibility of bankers and entities, the chargeback process, etc.
2. Online advertising

Among all the major advertising markets in the world, India is one of the fastest growing. The country’s digital advertising sector is expected to grow at a CAGR of 35% in 2017. In terms of segments, companies spend the maximum time on surfing, followed by social media; expenditure on video ads such as on YouTube has also increased significantly. The Retail and Consumer Products, eCommerce and Automobile sectors have been the biggest drivers of digital growth in advertisements.

Advertising budgets are seeing a multi-year shift from the offline to the online mode due to changing consumer behaviour and proliferation of digital content. Moreover, technological advancement in new ad formats are driving increased engagements, conversions and value propositions for advertisers as well as new formats such as location-based and targeted ads based on behavioural data. User analytics has become a staple. As a result of users spending an increasing amount of time online, the internet has become the second-largest advertising medium after TV. Improving Return of Income (RoI), roll-out of new engagement measuring tools and enhanced targeting of ads are projected to drive additional ad revenues online. The share of the internet market is expected to grow as mobile and video drive internet consumption exponentially. In emerging segments, discovery of content and programmatic media buying have become popular. Additionally, programmatic advertising makes the process of buying ads more efficient and less expensive due to the use of automated software, data analytics tools and real-time bidding technology.

Since the online segment is still at a nascent stage, there are no standardised performance indicators or metrics for evaluating the effectiveness of content and brand marketing deployed while using technology. Therefore, measuring the RoI of advertisers, especially in the mobile domain, is difficult. The entry of international solution providers is also likely to intensify competition. Mobile is expected to be the biggest driver of the online segment in 2017 as advertisers continue to explore the medium and look at ways of leveraging it more effectively than at present. Social media is being increasingly integrated with traditional campaigns and social messaging applications are evolving to become multipurpose social platforms. The increasing use of ad blockers is likely to lead to personalised advertising with a significantly increased emphasis on ‘native’ ads, in-app ads and other high-quality ads.

There have been revolutionary changes in the international tax arena to bring transactions in the digital economy within the ambit of tax. In order to align itself with the best international practices, the Government of India has also been making certain changes, for instance, by bringing in a retrospective amendment in its definition of royalty and its implementation of GST and the BEPS Action Plan 1. Considering these upcoming developments in this segment, we have elaborated on prominent tax and regulatory-related issues faced by its business drivers in the following pages.
Relating to the definition of royalty and its implications under Indian tax treaties. Whether retrospective amendments made in royalty-related regulations on software, processes or equipment apply to Indian tax treaties under the Act has been a matter of protracted income-tax litigation in India. It is also imperative to analyse the applicability of Budget 2017 proposals pertaining to certain tax terms used in Indian tax treaties, which have not been defined in these treaties.

There have been cases where the income-tax authorities have alleged that Reseller Co. and/or its activities create private equity for Overseas Ad Co. in India, and its income should therefore be liable to tax in India at the rate of 40%.

Revenue generated by Indian advertisers’ advertisements may be subject to Equalisation Tax at the rate of 6% if the consideration exceeds INR 100,000 per annum from every advertiser. It may also need to be evaluated whether Equalisation Tax applies to payments received from Reseller Co.

Since Overseas Ad Co. earns an income from India that may be liable to tax under both the mechanics, it may be required to comply with India’s Income-tax return filing obligations to report income it has generated in the country.

It is important to evaluate whether Equalisation Levy needs to be withheld by Indian Reseller Co. while making payments to Overseas Ad Co. in light of compliance-related obligations.

Reseller Co. will also need to keep in mind perspective payments made by advertisers or their ad agencies in the form of ‘reseller fees’—whether such fees are paid for the use of a server, space, process, etc., as FTS under the Act (on the basis of retrospective amendments made in the definition of royalty and Indian tax treaties).

### Indirect Tax

It will need to be evaluated whether Service Tax will be applicable under the reverse charge to be paid by Reseller Co. on online advertising services and sharing of ad revenue. Availability of credit, as well as similar implications, will also have to be analysed when Overseas Ad Co. directly enters contracts with Indian advertisers. In addition, Service Tax-related implications for Reseller Co.’s services would have to be evaluated.

The taxability of support services (for identification of content) provided by Reseller Co. to Overseas Ad Co. will need to be analysed to check whether such services qualify as intermediary services. (If these services qualify as intermediaries, Service Tax may be applicable, since the service provider is located in India). Furthermore, OIDAR provisions need to be analysed for overseas suppliers in the case of B2C supplies.

### GST

The implications of GST will need to be evaluated on payments made by Reseller Co. to Overseas Ad Co. as well as on services provided by Reseller Co. It is important to analyse the place of supply to determine the location of the service recipient. (If the services are provided under a single contract, they may be provided or received in multiple states.)

Furthermore, OIDAR provisions need to be evaluated in the case of a supplier in the case of B2C supplies. In addition, the taxability of free-of-cost supplies as well as credit reversal on these should be analysed under GST.

Under GST, valuation of transactions between related parties is to be analysed according to Valuation Rules, which will be prescribed.
Transfer Pricing

Based on the actual roles and responsibilities of the employees of Reseller Co. and the key functions performed by them to manage the economically significant risks faced by their Indian operations, it will have to be evaluated whether Reseller Co. is a distributor or an entrepreneur.

If Reseller Co. is a distributor, it will need to be analysed whether it can be compensated either on the basis of an arm’s length net margin on its sales or at an arm’s length gross profit margin commensurate with the gross margins of comparable companies engaged in a similar business, depending on Reseller Co.’s quantum of marketing.

If Reseller Co. is an entrepreneur, takes independent business decisions and undertakes significant advertising and marketing activities in India, it should retain the residual profits derived from its Indian business, after remunerating Overseas Ad Co. for the intangibles used by it.

Since Reseller Co. is also engaged in identifying content for Overseas Ad Co., it should be analysed if it will be entitled to separate compensation for its content-identification functions.

If Reseller Co. is also engaged in procuring Indian content for Ad Co., it will need to be analysed whether it will be entitled to separate compensation for its procurement functions, either on a commission basis or on an arm’s length mark-up on the costs incurred by it on its procurement functions, depending on the value-added functions performed by Reseller Co. to procure the content.

Overseas Ad Co., which directly contracts with advertisers in India, may create a PE exposure in the country. However, attribution of profits to such a PE may pose a challenge because of limited guidance on the subject.

Regulatory — FEMA

Permissibility of payments made by Reseller Co. or Indian advertisers to Overseas Ad Co. will need to be analysed in light of import regulations and have in place the required documentation (fulfilment of contractual obligations, invoices, etc.) for submission to Indian bankers to remit fees to Overseas Ad Co. It is important that contractual documents are drafted appropriately to avoid unnecessary queries from bankers or RBI.
3. Over the Top (OTT)

Consumption of content has evolved over the past decade with consumers increasingly opting for on-demand entertainment via audio and video. A new medium in personal entertainment that has emerged over the last few years is over-the-top (OTT), a term used to describe delivery of entertainment (TV programmes, movies and music) via the internet, without consumers having to subscribe to a cable or satellite TV provider. India’s OTT market is expected to grow at a CAGR of around 30% over the next five years in terms of its viewer base as network infrastructure improves and service awareness increases.

India has seen the emergence of numerous OTT service providers in the last two years. Multiscreen video consumption, in hours, has been growing at more than 65% since 2015. India’s OTT market, especially video, is largely skewed in favour of advertising, and subscription video on demand represents the largest repository of on-demand content. With a significant rise in the use of smartphones and improved internet connectivity, consumers are increasingly embracing premium and subscription models to consume content. They are demanding high-quality and flexible original programming on demand and on numerous devices to satisfy their growing taste for ‘binge viewing’. OTT services offer the best outlet for this kind of consumption. On-demand models are changing consumers’ expectations of paid digital content with continuing migration from ownership to streaming and OTT.

In terms of challenges and opportunities, companies will have to monitor consumption patterns and customise their content in line with changing customer choices. This needs to be done in conjunction with ads and subscription revenues. The market now looks at OTT as a mainstream technology used to deliver content, but competition is expected in the form of international players. Furthermore, improvements are needed in IP laws to protect artists and support legal consumption in order to curb piracy, which is a major concern. This year, new players are expected to enter the arena and mobile consumption is set to continue to dominate the OTT segment. However, significant improvement in network connectivity, especially in Tier 2 and 3 towns, could prove to be the differentiator.

While improvement in IP laws is a welcome development to attract foreign players to enter this segment, taxation- and regulatory-related challenges continue to be a major issue faced by new players. Moreover, the continuing demand for clarity in tax laws in relation to the OTT business is proving to be a major road block in its growth. In our detailed discussion on the following pages, we have identified the major issues faced in the OTT business model.
Mechanics

Business conducted through Indian subsidiary

- Overseas OTT F Co. (OTT F Co.) obtains a licence from content providers located in India and outside it and provides it to Indian Co.
- OTT F Co. has a website on which content is hosted. The website and content are hosted on servers outside India.
- OTT F Co. may contact Indian subscribers or advertisers directly or appoint Indian Co. as a reseller to distribute Video on Demand (VoD) or OTT services to Indian subscribers and advertisement space to Indian advertisers.
- Indian subscribers will enter an end-user licence agreement (EULA) with Indian Co. and not Overseas OTT F Co.
- Nobody in India, including India Co., will be able to download content. Mirror servers could be deployed by OTT Co. in India to address latency-related issues.

Business conducted directly by OTT F Co.

The mechanics will be similar to those in the model given above, except that Indian customers will sign an EULA directly with OTT F Co. and pay the subscription fee to it.

Direct Tax

Overseas content provider: It is important to evaluate whether the consideration paid by OTT F Co. to obtain a licence from foreign content providers is taxable in India as royalty in light of the second source rule under the Indian domestic tax law and some tax treaties entered by India. Furthermore, provision of royalty under the Act allows exclusion of any content from sale, exhibition or distribution of cinematograph film. It therefore needs to be analysed whether the type of online content and medium of display at present can be considered to be within the ambit of the beneficial provisions. OTT F Co. should therefore evaluate its withholding tax obligations in India accordingly.

OTT F Co.: OTT F Co. receives a consideration from India Co., advertisers or subscribers. It needs to be evaluated whether this consideration from India Co., advertisers or subscribers qualifies as royalty (for copyright, process or equipment), considering the provisions of the Act and Indian tax treaties. Aspects such as claiming the benefit of exemption under the Act under the ambit of royalty if the consideration from India Co., advertisers or subscribers qualifies as ‘consideration from sale, distribution, exhibition of cinematographic film’, etc., need to be considered. Moreover, factors such as whether the content can be downloaded on subscribers’ devices and its period of validity will also have to be taken under consideration. There is therefore a need to be mindful of any PE-related exposure created for OTT F Co. by Indian Co. from its activities in India, the location of the mirror servers created, etc.

Revenues generated by the advertisments of Indian advertisers may be subjected to Equalisation Levy at the rate of 6% if the consideration exceeds INR 1,00,000 per annum from every advertiser. It may also need to be evaluated whether this levy will apply for payment made by Indian Co. as part of a reseller arrangement.

It is also imperative to analyse the applicability of Budget 2017 proposals relating to certain tax terms used in Indian tax treaties, which have not been defined in the treaties.

- Since OTT F Co. earns an income from India, it may need to comply with the country’s Income tax return filing obligations to report income it has generated in India.
- It is important to evaluate withholding tax obligations and Equalisation Levy-related obligations for Indian Co. while making payments to OTT F Co., other overseas advertising agencies, etc.

Indirect Tax

Subscription fees:

It needs to be evaluated whether Service Tax is applicable on subscription fees to be paid by Indian Co. to OTT F Co. on a reverse charge basis. Service Tax, if paid by Indian Co. under a reverse charge, should be available as an input credit to Indian Co. The Place of Provision of Service Rules, 2012 also needs to be evaluated to determine whether services are deemed to be provided in India.

If Indian customers sign an EULA directly with OTT F Co. and pay subscription fees to it, it will need to be evaluated whether the services provided by OTT F Co. can be classified as OIDAR services, i.e., provision of data or information, retrievable or otherwise, to any person or entity in electronic form through a computer network. With effect from December 1, 2016, overseas service providers need to be registered in India and deposit tax for OIDAR services provided to individuals or the Government. In the case of OIDAR services provided to registered customers, the liability to pay tax is on the customers under a reverse charge. OIDAR provisions need to be analysed in detail depending on the nature of the service provided.

In India, VAT- or CST-related implications for licence fees to be paid to OTT F Co. will also need to be evaluated if the content is to be downloaded by Indian Co., Indian advertisers, etc. If VAT is applicable, it will also have to be considered in which state it will need to be deposited, i.e., from the location from which the movement of the ‘goods’ originated. This will depend on where the situs of the sale is deemed to be.
Levy of Service Tax and the implications of VAT on provision of content by Content Co. to OTT F Co. will also have to be evaluated.

**Entertainment Tax**

In India, Entertainment Tax (ET) is levied by state governments on transactions in the entertainment domain. The term ‘entertainment’ usually includes amusement parks, video games, arcades, exhibitions, celebrity stage shows, sports activities, etc. In some states, Value Added Services (VAS), including ringtones and music, have also been covered.

To ascertain levy of ET across various states, the charging section, along with definitions under relevant legislation on ‘entertainment’, ‘proprietor’, ‘payment for admission’, ‘admission’, etc., needs to be analysed in detail.

**GST:**

The implications of GST on such services should also be analysed. The following are some important aspects:

- Taxation of intangibles: It should be analysed whether intangibles will be considered as goods or services under GST.
- Similar provisions for OIDAR continue under GST and will need to be analysed.

**Transfer Pricing**

Based on the actual roles and responsibilities of the employees of Indian Co. and the key functions performed by them to manage the economically significant risks facing the company’s Indian operations, it will have to be evaluated whether Indian Co. is a distributor or an entrepreneur.

If Indian Co. is a distributor, it can be compensated either on the arm’s length net margin on its sales or on an arm’s length gross profit margin basis, commensurate with gross margins earned by comparable companies engaged in a similar business, depending on the level of marketing functions carried out by it.

If Indian Co. is an entrepreneur, it takes independent business decisions and undertakes significant advertising and marketing activities in India, it should retain the residual profits derived from its Indian business after remunerating OTT F Co. for the intangibles (brand, server, website and content) deployed by it.

If Indian Co. is also engaged in procuring Indian content for OTT F Co., it needs to be analysed whether it is entitled to separate compensation for its procurement functions, either on a commission basis or based on an arm’s length mark-up on the costs incurred by it in its procurement functions, depending on the value-added functions performed by it to procure the content.

Indian Co. may earn an assured margin on its OTT revenues and recover the costs incurred by it in distributing VoD services to OTT customers. The residual amount may be paid to Content Co. Under this model, Indian Co. will be characterised as a low-risk distributor.

**Regulatory—FEMA**

The permissibility of payments made by Indian Co. or its Indian subscribers needs to be analysed in light of import regulations. There is also a need to have in place the required documentation (fulfilment of contractual obligations, invoices, etc.) for submission to Indian bankers for remittance of fees to OTT F Co. It is important that contractual documents are drafted appropriately to avoid unnecessary queries from bankers or RBI.

If third-party payment aggregators are involved in collecting funds from individual subscribers (using payment modes such as net banking and debit cards) for remittance to OTT F Co., it is imperative to ensure their compliance with provisions and instructions under the Payments and Settlements Act, 2007, and relevant RBI guidelines.
4. Cloud

Cloud is the latest and fastest growing trend in technology, with its architectural transition expected to continue to unfold in the coming decade. According to a recent study, the public cloud services market in India is projected to grow by more than 30% as more and more organisations adopt digital business strategies and move from legacy IT services to cloud-based ones. Enterprises are increasingly embracing the cloud option due to its agility, cost-effectiveness and scalability. In the different segments, the public cloud is growing faster than the private cloud, while hybrid cloud architectures are likely to continue to dominate enterprises’ cloud strategies. Cloud application services (SaaS) as well as cloud management and security services are witnessing exponential growth. The cloud is a major catalyst for significant shifts in the talent priorities of IT staff and data centres, and is changing IT spending behaviour as customers embrace cloud and shift their IT spending from capex to opex. The cloud model enables increased efficiency and is expected to partially mitigate some demand-related tailwinds from substantial growth of data and virtualisation of workload.

Cloud has become an innovation machine and is expected to strengthen in 2017. Cloud service providers have expanded rapidly in response to the surging demand for the cloud and have successfully achieved critical scale in the market. The growth in the number of cloud infrastructure players is forecast to continue due to the pressure on the margins of legacy hardware vendors. However, in spite of these benefits, there are serious issues relating to IT governance and security, and data breaches that affect cloud companies. Furthermore, the lack of cloud transition strategies and a standard methodology for service integration between business partners and the ecosystem also pose challenges. And as enterprises move towards the public and hybrid cloud environment, their IT infrastructure spending will increase. In this scenario, their capacity to scale up their computing and infrastructure capacity, based on demand, is likely to become much more flexible and agile than at present.

While the concept of the cloud has come a long way, a host of tax and regulatory controversies related to this business model needs to be addressed. We have highlighted some of the important issues faced in the following pages.
Mechanics

Foreign Co. manufactures printers and owns a server in the US. The company has a wholly owned subsidiary in India (Indian Co.), which provides software development services. Indian Co. also sells space on Foreign Co.’s server to customers for storage of data, and enables them to print the details from any location using Foreign Co.’s printers. Customers use software apps installed in the printer to avail of this facility. However, customers in India can also make payments directly to Foreign Co. to store data on its server. Alternatively, Indian Co. can buy space for its server from Foreign Co. and sell it to its customers in India.

Cloud models

- **Infrastructure as a Service (IaaS)**
  - Users can rent IT infrastructure such as data centres and network infrastructure equipment to deploy and run applications or store data.
- **Software as a Service (SaaS)**
  - SaaS is a software model provided by a vendor through an online service (the web or the internet).
  - Users do not need to install or maintain software applications on their computers.
  - The software is run on the provider’s cloud infrastructure and a user can access it on the web.
- **Platform as a Service (PaaS)**
  - PaaS enables companies to develop applications by using programming languages and tools.
  - The provider is responsible for maintaining and managing the IaaS on which the PaaS tools are hosted.

Direct Tax

Foreign Co. needs to evaluate whether payment received from Indian Co. or its customers for sale of space on a server is taxable as software royalty, process royalty or equipment royalty, especially in view of retrospective amendments and their implications under Indian tax treaties. Moreover, the company should be mindful that Indian Co. can create a PE for Foreign Co. in India, depending on the location of the server or website, the number of Foreign Co.’s employees visiting India, etc. Foreign Co.’s income will be taxable in India at the rate of 40% if PE is triggered. PE exposure would probably be high in the case of the IaaS model where services are provided through hardware or servers to customers in India.

In all the three models—IaaS, SaaS and PaaS—the cloud service provider (Foreign Co.) is required to maintain and operate the server or infrastructure and charge fees for its maintenance. It needs to be evaluated whether these fees qualify as FTS under the Act and Indian tax treaties (which may have a narrower definition). Additionally, nuances such as human intervention and the use of standard facilities would necessitate payment of fees.

If Foreign Co. transfers IP to Indian Co. to develop software, there is a need to analyse whether the amount payable by Indian Co. to Foreign Co. qualifies as royalty under the Act and Indian tax treaties.

Since Foreign Co. earns an income in India, it may be required to comply with the country’s Income-tax return filing-related obligations to report the income it has generated in India. It is therefore important for Indian Co. to evaluate its withholding tax obligations while making remittances to Foreign Co.

If Indian Co. has a development centre in a special economic zone (SEZ), it needs to analyse the applicability of tax holiday benefits under the Act. The company will also have to evaluate the eligibility of expenses for research and development (R&D) where its development centres conduct R&D activities.

Indirect Tax

It is essential to evaluate whether a transaction will be liable for VAT or Service Tax. VAT authorities may contend that there has been a transfer of the right to use these services (in the case of IaaS and PaaS or goods involved such as software in SaaS).

If VAT is applicable, the situs of the sale will need to be analysed to determine implications, if any.

On the other hand, Service Tax-related implications may come to the fore in all three models. In this case, the nature of the transaction and its factual pattern will need to be analysed to determine the nature of tax applicable and whether there is a requirement to pay tax under a reverse charge, along with the availability of credit to the recipient.

If Service Tax is applicable, the company will need to evaluate whether this involves use of OIDAR services. For OIDAR services provided by an overseas service provider to an individual or the Government of India, the liability to deposit tax may be on the overseas service provider who will be required to be registered in India to deposit tax. This needs to be analysed based on the flow of transactions and the nature of services provided.

GST

Development of software and transfer of the right to use it have been treated as a service under GST. The place where a service is provided will need to be analysed to determine the applicability of GST and whether there is a requirement to pay tax under a reverse charge. In the event of multiple locations, it has to be determined where the tax is to be deposited, and if intangibles are provided, whether these will be goods or services.
The concept of OIDAR continues under GST and the implications for overseas service providers will need to be analysed.

**Transfer Pricing**

**Provision of software development services by Indian Co.**

There is a need to evaluate whether Indian Co. will be entitled to arm’s length remuneration for providing software development services to Foreign Co. Remuneration to Indian Co. will depend on its characterisation in view of its Functions, Assets and Risks (FAR).

Typically, if Indian Co. does not perform significant activities with respect to software development, there is a need to evaluate whether all the significant assets are provided by Foreign Co. and Indian Co. does not incur any significant risks arising from software development. Accordingly, Indian Co. can be characterised as a low-risk-bearing entity and can be remunerated on a cost-plus basis.

If Indian Co. performs significant functions and faces material risks associated with software development, there may be a need to look at the eligibility of the share of profits generated by the software developed by it.

**Reselling of server space by Indian Co.**

Based on the actual roles and responsibilities of Indian Co.’s employees and the key functions performed by them to manage economically significant risks in its Indian operations, it will need to evaluate whether it is a distributor or an entrepreneur.

If Indian Co. is a distributor, it will have to evaluate whether it can be compensated either on the arm’s length net margin on its sales or on its arm’s length gross profit margin, and also whether these are commensurate with the gross margins earned by comparable companies engaged in a similar business, depending on the level of marketing functions carried out by Indian Co.

If Indian Co. is an entrepreneur that takes independent business decisions and undertakes significant advertising and marketing activities in India, there is a need to evaluate whether it should retain the residual profits derived from its Indian business after remunerating Foreign Co. for the intangibles used by it.

**Selling of server space by Indian Co. on behalf of Foreign Co.**

In this scenario, it is important to evaluate whether Indian Co. will be entitled to compensation for marketing and sales support services provided by it to Foreign Co. Depending on a functional analysis, Indian Co. may be remunerated on the costs incurred by it to provide such services in addition to an arm’s length mark-up on these costs. Alternatively, Indian Co. may be remunerated at an arm’s length percentage of the sales revenue generated by it from its Indian customers.

Selling of server space by Foreign Co. to customers in India may create a PE exposure for it in India. Attribution of profits to such a PE may pose challenges due to limited guidance available on the subject. Transfer Pricing considerations will be similar under different cloud models.

**Regulatory—FEMA**

There is a need to evaluate the permissibility of payments made by Indian Co. or the Indian customers of Foreign Co. in light of import regulations in India and formulation of the required documentation (fulfilment of contractual obligations, invoices, etc.) for submission to bankers in the country for remittance of funds to Foreign Co. It is important that contractual documents are drafted appropriately to avoid unnecessary queries from bankers or RBI.
5. Digital payments

Digital payment solutions are becoming more and more relevant in the Indian economy, which is driven by mobile-centric internet penetration. The digital payment market in India is expected to touch US$ 500 billion by 2020, with online shopping, payment of utility bills and entertainment being the top three user activities. Recent initiatives by the Government have triggered a strong drive towards the adoption of the digital payment mode and the rise of new market entrants. Mobile banking transactions tripled between 2012 and 2014, hitting 150 million in 2014. Pre-paid payment instrument providers (offering m-Wallets) have been attracting the growing interest of consumers and have motivated banks to invest in their own digital payment offerings, and mobile-wallet transactions have fast outstripped m-Banking transactions. Today, we are seeing the explosive growth of digital transactions and use of mobile wallets by consumers and mobiles in point of sale (PoS) by merchants. m-Wallets are being used for a variety of purposes from bill payments to food delivery and travel. Furthermore, the launch of the Unified Payment Interface (UPI) is expected to make transactions easier and significantly boost overall growth. With the recent ban on high-denomination currency notes, the Government is also encouraging the use of m-Wallets to achieve its vision of a cashless economy.

However, there are several issues facing users of mobile wallets. Currently, discounts and other incentives are predominantly used to attract customers and drive transactions. This has led to this model becoming a loss-making business. Customer retention and building of customer loyalty is another area on which companies will have to focus more. Other challenges relate to cyber security, achievement of scale with positive unit economics and acquisition of a substantially increased wallet share of the target customer segment. In the coming year, the focus is expected to be on provision of an intuitive and personalised experience to users of m-Wallets. Technological advancements in in-store acceptance of mobile wallets, PoS devices at offline outlets, interoperability of m-Wallets and an increase in their transaction limit are likely to drive their exponential growth in the future.

The importance of m-Wallets has increased significantly with the Government’s demonetisation drive and its dream of creating a ‘cashless economy’. The year 2017 is expected to witness a revolution in the digital wallet business, leading to a host of opportunities for new players to enter this business arena. However, since tax-related controversies are an inseparable part of any new development in the economy, in the following pages, we have elaborated on some major tax and regulatory issues that the digital payment business model is facing and is likely to continue to face.
Mechanics

- An online shopper in India buys goods worth US$ 100 from a seller in country A.
- The buyer makes his payment via a local payment gateway, i.e., company B.
- Company B charges US$ 2 as platform service fees and transfers it to company F (a foreign payment gateway with a global network).
- On receipt of funds from company B, company F charges US$ 1 as processing fees and remits the balance to company A.
- While transferring this amount to company A, company F charges US$ 2 as platform service fees.
- Company A deposits funds into the seller’s bank account in country A.
- Alternatively, there could be a model wherein there are two different payment gateways (A and B in this case) and no company F (global network) (herein referred to as an ‘alternative business model’).

Direct Tax

Foreign Co: It needs to be evaluated whether income earned by Foreign Co. in the form of processing fees qualifies as royalty for equipment or a process in light of retrospective amendments and their implications under Indian tax treaties. It should also be analysed whether the payment can be characterised as royalty or as a service and be considered an FTS, which, as defined under the Act, is wide in its ambit compared to its definition in tax treaties (especially Indian tax treaties with a narrow definition).

Since Foreign Co. earns an income in India, it may need to comply with Indian Income-tax return filing obligations to report income it has earned in the country.

Transfer Pricing

Company A, Company B and Foreign Co. are associated enterprises and contribute unique intangibles in the transaction flow (Company A and Company B own and manage relationships with the seller and buyer, respectively; Foreign Co owns the global payment network). Given the integrated nature of their operations and the unique intangibles contributed by them, there is a need to evaluate whether a profit split approach may be appropriate to determine the arm’s length compensation attributable to each entity, taking into consideration their unique contributions.

Regulatory—FEMA

Cross-border payments facilitated by non-banking players are regulated by RBI and are subject to stringent conditions, including limits on remittable amounts. In this case, the local payment-processing company (company B) will need to ensure its compliance with the prescribed conditions (opening of regulated accounts, submission of relevant documentation to Indian bankers, etc.) to facilitate collection of funds from local buyers and make settlements with overseas sellers within prescribed time limits.
Globally, PwC follows a ‘whole of business’ approach to address Tax and Regulatory related issues faced by businesses, wherein our Direct Tax, Indirect Tax, Transfer Pricing and Regulatory teams work in conjunction to provide a holistic view of problems arising from the functioning of businesses. We can guide you on all existing and future tax and regulatory issues that may arise in your organisation by offering you a wide range of advisory and compliance services in the eCommerce and Online sector.

With newly introduced regulations such as the Equalisation Levy on digital transactions as a part of the implementation of the BEPS Action Plan 1, introduction of GAAR in transactions (with effect from April 1, 2017), significant expansion of the ambit of levy of Service Tax through taxation of OIDAR services and consolidation of varied indirect taxes into a single mega-basket called GST, India is gearing up to make dynamic changes in its tax laws to bring these at par with international standards.

The eCommerce and Internet sector is tipped to be the drivers of India’s economy in times to come—sooner rather than later. In this scenario, we can help you keep pace with the ever-changing reforms in the tax and regulatory ecosystem by guiding you to effectively adopt a proactive approach in implementing these changes. We can also help you revisit your existing business outlook and act as a change driver to facilitate your shift from traditional offline business models to contemporary online ones.

We will be happy to help your organisation by providing well-thought-out and informed recommendations on a relevant future course of action to enable you to effectively address specific needs in your organisation.
Notes
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