

AN EXPLORATORY STUDY ON THE TAXATION OF E- COMMERCE TRANSACTIONS IN INDIA

Abstract

The taxation of e-commerce transactions presents significant challenges due to the borderless nature of the internet and the intangible nature of goods and services involved. In India, the Central Board of Direct Taxes established the High Powered Committee (HPC) to study the need for a separate tax system for online transactions. The OECD's guiding principles were considered in the study, but the HPC argued that existing tax rules were sufficient for taxing e-commerce transactions based on the principle of neutrality. E-commerce encompasses a wide range of activities, from online goods sales to customer data collection for marketing purposes. Taxation of online transactions is complicated due to issues such as transaction encryption and difficulties in locating the transaction. Additionally, offline transactions that involve electronic payments further complicate the tax collection process. The OECD's report emphasizes principles of neutrality, efficiency, clarity, and flexibility for the taxation of e-commerce. Transfer pricing issues become more crucial in the era of e-commerce, requiring careful consideration of business functions and earnings allocation. Tax administration faces technological challenges in obtaining information from taxpayers and ensuring compliance while respecting privacy and data regulations. Disputes with tax authorities arise from identifying taxpayers, ensuring compliance, accessing records and encrypted data, and collecting tax from non-resident taxpayers. The judicial perspective on tax issues related to software classification and treatment remains ambiguous, contributing to conflicting tax treatment across different jurisdictions. Internet-based tax evasion strategies include

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transfer pricing, cost allocation, and establishing businesses in tax havens. In conclusion, as e-commerce continues to grow, the tax system must adapt and simplify within the government's administrative capacity. Striking a balance between increasing revenue and burdening taxpayers with higher tax rates is crucial to foster the growth of the Indian market.

Keywords: Efficiency, Transfer Pricing, Cross Border Accessibility, Certainty, Indian Economy etc.

I. INTRODUCTION

The taxation of e-commerce operations poses a number of challenges due to the lack of national boundaries and the tangible character of the goods and services being traded. Due to the internet's cross-border accessibility, e-commerce transactions may involve customers who are citizens of different nations. As a result, there may be multiple countries where the income from these transactions is taxed. As guiding principles for the taxation of e-commerce transactions, the rules developed by the Committee on Fiscal Affairs of the Organisation for Economic Cooperation and Development ("OECD") underlined neutrality, efficiency, certainty and simplicity, effectiveness and fairness, and flexibility

The High Powered Committee ("HPC") was established in India by the Central Board of Direct Taxes, and it submitted a report in September 2001. The report investigated and evaluated the demand for the creation of a special tax structure for online transactions. With a few exceptions, the HPC study took into account the OECD's guiding principles. The HPC countered that the present regulations are adequate to tax e-commerce transactions and that, in accordance with the "neutrality" concept, no special regime is required to tax e-commerce transactions.

Deals and sales are booming in the e-commerce industry. However, the sector does not heat up when it comes to taxes policy, particularly on Budget Day.

II. DEFINITION OF E - COMMERCE

According to Greenstein and Ferman" electronic commerce (e-commerce) is defined as the use of electronic transmission medium (telecommunication) to engage in the exchange, including buying and selling of products and services requiring transportation either physically or digitally from location to location."

E-commerce refers to any transaction involving the ownership or right to use goods or services that is carried out through a network mediated by a computer. E-commerce, in the eyes of the European Commission, encompasses more than just online goods sales. It consists of a discordant group of loosely defined behaviours including shopping, looking for products online, gathering information about products to buy, and executing the transaction like any other persistent economic activity. It involves conducting surveys of customer satisfaction, gathering data on consumers, and keeping databases of consumers for use in marketing, promotion, and other related tasks.

Using different combinations of businesses and consumers, the first phase of e-commerce gave rise to a new business nomenclature. Like traditional business methods, it offers advantages and disadvantages of its own. Consequently, e-commerce has inevitably economic landscape in a dynamic and participatory way.

III. TAXES ON ONLINE TRANSACTIONS

Over time, the Internet has changed many of the fundamental and well-established traditional concepts of direct and indirect taxation. The numerous taxation issues that e-commerce has raised are causing governments all over the world to struggle. This is due to a lack of adequate comprehension of the following:

- Due to the complex nature of the business offered through Internet business, etc., as well as the method of operation of Internet business, etc., the application of tax rules has grown increasingly difficult.
- The Information Technology Act of 2000, the first piece of legislation to address e-commerce, rarely makes any reference of the tax system. A sizable amount of the state's direct and indirect tax revenue is lost when online transactions are not taxed. Finding a solution to this important problem is required.

IV. BASIC TAXATION PRINCIPLES

The challenges associated with evaluating these transactions are exacerbated by the various tax laws and structures across different countries. The taxation policies of all countries are based on a number of fundamental principles. The most important ones are these four: effectiveness, equality, certainty, and positive economic impact. Making a rational tax policy requires an understanding of the nature of industry. Some of the following are peculiarities of the internet.

- It is a network of networks and cannot be owned or controlled by a single entity.
- This network of networks has the ability to send packets quickly from one computer to another.
- Data transmission between computers can take place without the need for a human intermediary.
- If only one machine is connected to the Internet, it may decide to change its route. The Internet has a wealth of information.
- The environment of the internet offers a graphical user interface that is easy to use.
- You can find a wealth of information almost anywhere in the world with just one click.
- It includes all boundaries, both geographical and territorial.

Activities on the internet are split into two categories. The first is a "access service" and the second is a "content service." In the former, people will have access to the Internet, whereas in the latter, informational content is transmitted electronically. To further differentiate, an online service provider (OSP) is a person who offers a service over the Internet, as opposed to an Internet service provider (ISP), who only offers the service of providing access to the Internet. They provide the service in exchange for subscription and use payments. Taxes are applied on these. The Internet includes content and material services, traditional retail transactions on an electronic medium, and electronic commerce involving digital goods, as was previously discussed. This would later lead to numerous issues with intellectual property.

- 1. Transactions Done Offline:** The term "offline transactions" refers to any transaction in which products and services are ordered, maybe paid for electronically, but delivered in another way. Currently, offline transactions make up the majority of e-commerce. These offline transactions, in contrast to typical transactions, were created through disintermediation. Online and offline transactions have different requirements for implementing sales tax and customs duties. In order to simplify or streamline the process without jeopardising income or other cross-border regulations, the tax authorities will need to re-evaluate their current methods of tax collecting.

2. Online Purchases: Any online transaction is referred to as being "online" in this sentence. These transactions are exceedingly challenging for tax authorities to manage. The following issues with internet transactions are felt by tax authorities:

- Unable to locate a transaction
- Transaction encryption
- Difficulties in recognising where a product is made or consumed;
- Collecting the tax from millions of end-users rather than a few intermediaries.
- Goods and services are defined
- Differences between several service categories

When it comes to tracking down transactions between Indian customers and foreign suppliers, when everything is done electronically, including the payment of money with electronic cash, tax collection authorities will be all but helpless.

3. Transaction Encryption: In the next two to three years, powerful encryption technologies will likely become widely utilised and accessible to the average Internet user. With the aid of these technologies, users can encrypt the entire transaction, making it so that only the parties involved can decrypt the data. This means that even if an income tax officer or other tax authority may halt a transaction, he won't be able to read it or comprehend its contents to determine whether or not the transaction contains accessible products. In addition to tax evaders, even the most upright person who simply wants his transaction to be secure when collecting taxes from end users will adopt encryption technologies.

V. TAXATION OF E-COMMERCE

- The meticulously designed tax structure in India gives both the Central and State Governments the authority to impose taxes.
- The central government is in charge of collecting direct taxes like corporate and individual income taxes.
- State governments are in charge of collecting local and state sales taxes.
- A clear, open, and consistent policy that defines income in accordance with the global norm should be used to properly write India's tax laws. The government should follow the OECD's neutrality standard for defining income from online transactions.

1. OECD Report: According to "The Economic Times" of June 3, 2000, the recent OECD research prepared the way for a statement of general taxation rules that should apply to e-commerce. All agreements to avoid double taxation must be evaluated. In essence, e-commerce should be taxed according to the same rules as traditional business.

- **Neutrality:** Taxation should be fair and neutral when applied to various forms of e-commerce in order to prevent double taxation or international non-taxation.
- **Efficiency:** Compliance expenses for companies and administrative expenses for governments should be kept to a minimum.
- **Clarity and Simplicity:** Tax laws should be straightforward and easy to comprehend so that tax payers are aware of their rights.

- **Effectiveness and Fairness:** Taxation should generate the appropriate tax revenue at the appropriate time, and the likelihood of evasion and avoidance should be kept to a minimum.
 - **Flexibility:** The taxation system needs to be adaptable and dynamic in order to keep up with changes in industry and commerce. Existing tax laws can be used to implement these objectives, and e-commerce shouldn't be subject to unfair tax treatment. The OECD ministerial summit that took place in Ottawa in October 1998 agreed with the aforementioned tenets.
2. **Transfer Pricing:** The OECD is aware that in the era of e-commerce, transfer pricing issues would become more crucial. Compared to traditional forms of trade, e-commerce is more distributed and collaborative, and its supply chain is inextricably linked. It promotes connectedness both inside and across groups. It will be challenging to decide which business functions should be given more weight when determining appropriate transfer pricing after taking into account the entirety of the current market, especially given how significantly e-commerce has altered the way in which intermediaries and business flows are distributed. Therefore, it should come as no surprise that both tax payers and tax collectors find it difficult to decide which corporate operations are important and then agree on an appropriate method of allocating earnings to them.

VI. TAX ADMINISTRATION: TECHNOLOGICAL ISSUES

Legislation that is based on an ethical and intellectual framework must strike a delicate balance between taking into account enforcement difficulties and administrative quirks. It is simply not an option for tax authorities to take action in the current e-business environment. Obtaining information from taxpayers and connected parties and guaranteeing tax compliance in an e-commerce world will be a growing concern, tax authorities around the world recognise. Many inquiries come up in this regard:

- Where and how transactions should be stored?
 - How specific should the record-keeping requirements be, and what is the appropriate standard?
 - How should tax compliance requirements and the restrictions imposed by various privacy and personal data regulations be reconciled?
 - It is practical or reasonable to demand that an online merchant register their business in each location where they conduct business or offer services.
 - How should new e-merchants and traditional catalogue companies who export goods from far-off places be treated equally?
1. **Disputes with the Tax Authorities:** Tax authorities appear to agree that the following are their main challenges when it comes to e-commerce:
- Identifying the tax payer, especially when an Internet user is involved.
 - Determining audit trial designs and audit risk assessments to assure compliance.
 - Having access to records and information that can be verified.
 - A response to the introduction of electronic money (e-cash) and guaranteeing an effective system for collecting tax, particularly from non-resident tax payers.
 - Gaining access to encrypted data.

To synchronise the taxes treatment, there must first be intergovernmental and multi jurisdictional cooperation and agreement. The way tax authorities operate needs to be drastically modernised. Cross-border online business activity must be watched carefully. The ability of the government to use technology must be improved.

- 2. A Judicial Perspective on Tax Issues:** The judiciary is stuck in the middle of the spectrum, responsible for interpreting various software programmes and bringing harmony to their naturally at odds handling. There is no precedent or law to guide them. Instead, in the US, state and federal taxing agencies have construed and classified software in ways that are most advantageous to their own safety rather than relying on the consent policies of relationships in their approach to software taxes. As a result, the criteria of tax treatment become irreconcilable. It is highly challenging to combine practically every state's taxing policy into one comprehensive piece of legislation, even within India.

Two principles were typically used by courts to categorise software as an intangible. They are:

- Software as knowledge
- Software encompasses an array of services.

- 3. Internet-Based Tax Evasion:** Transfer pricing is one of the traditional strategies used by businesses to evade taxes by moving revenues to nations with low tax rates.

- Artificial cost allocation against either domestic or overseas profits, depending on where the tax rates are more favourable.
- Establishing conduit or intermediate businesses outside of the home nation to handle and direct income from various overseas sources.
- Establishing base businesses in legal domiciles or tax havens.

VII. CONCLUSION

E-Commerce is still in its early stages, it is likely to become the future of international commerce. However, there are currently few concrete tax rules specifically addressing the taxation of E-Commerce. It is important for the tax system to be widened and simplified within the government's administrative capacity. The government aims to increase revenue, but taxpayers oppose higher tax rates. Therefore, a balance must be struck to ensure that exclusive taxes do not hinder the growth of the Indian market.

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