CHAPTER 12

TAXATION OF DIGITAL TRANSACTIONS

LEARNING OUTCOMES

After studying this chapter, you would be able to -

- **appreciate** the meaning of e-commerce and how business is transacted through E-commerce;
- **identify** the issues and problems in taxing e-commerce transactions;
- **comprehend** the OECD recommendations for taxing e-commerce transactions under Action Plan 1 of Base Erosion and Profit Shifting (BEPS) project;
- **appreciate** the need for equalization levy;
- **comprehend and apply** the provisions of equalisation levy contained in Chapter VIII of the Finance Act, 2016 and the relevant Rules in problem solving and addressing related issues;
- **determine** the income arising on transfer of virtual digital asset and taxability thereof;
- **examine** the applicability of the provisions of tax deducted at source on transfer of virtual digital asset by a resident assessee.

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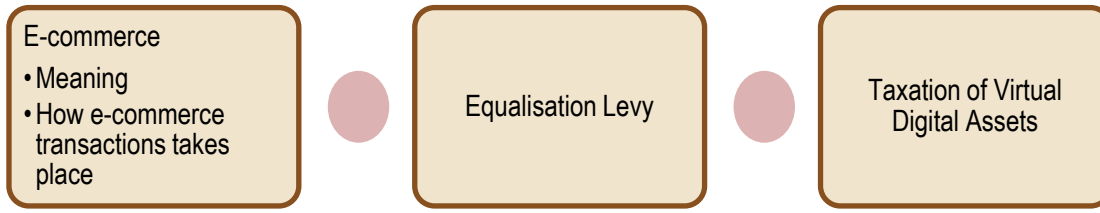
CHAPTER OVERVIEW



12.1 INTRODUCTION

The rapid growth of information and communication technology has resulted in substantial expansion of the supply and procurement of digital goods and services globally, including India. The digital economy is growing at a faster pace than the global economy as a whole.

At present, in the digital domain, business may be conducted without regard to national boundaries and may dissolve the link between an income-producing activity and a specific location. Hence, business in digital domain doesn't actually occur in any physical location but instead takes place in "cyberspace." Persons carrying business in digital domain could be located anywhere in the world. Entrepreneurs across the world have been quick to evolve their business to take advantage of these changes. It has also made it possible for the businesses to conduct themselves in ways that did not exist earlier, and given rise to new business models that rely more on digital and telecommunication network, do not require physical presence, and derives substantial value from data collected and transmitted from such networks.

The growth of e-commerce economy has revolutionised the concept of *brick and mortar* to *click and order.* The need for physical presence in a jurisdiction is consequently getting diminished. Therefore, due to transformed business models, communication with suppliers and customers take place virtually and digitally. Emergence of new age technologies such as 3D printing, sharing economy, internet of things etc. has revolutionised new business models in line with the digital epoch making it difficult to identify the location of source or origin point of a business transaction.

The expansion of business in digital form, give rise to certain tax challenges in relation to nexus, data and characterization of digital transactions. Over the years, to address these tax challenges certain developments are taking place to tax digital transactions which are carried out either by a

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non-resident non-corporate/ a foreign company or by a resident assessee. This chapter encompasses these developments introduced in the form of equalisation levy and taxation of gains arising on transfer of virtual digital assets by a resident assessee.

12.2 WHAT IS E-COMMERCE?

Clause (a) of *Explanation* to Section 194O defines "electronic commerce" to mean the supply of goods or services or both, including digital products over digital or electronic network.

E-commerce or electronic commerce is one of the main components of the Digital Economy. In its widest sense, it encompasses consumer and business transactions conducted over a network, with the help of computers and telecommunications. In other words, e-commerce refers to the exchange of goods or services for value on the internet. E-commerce, *inter-alia,* includes, online shopping, online trading of goods and services, electronic fund transfers, electronic data exchanges and online trading of financial instruments.

[1]OECD defines e-commerce as the sale or purchase of goods or services, conducted over computer networks by methods specifically designed for the purpose of receiving or placing orders. Accordingly, whether a commercial transaction qualifies as e-commerce is determined by the ordering method rather than the characteristics of the product purchased, the parties involved, the mode of payment or the delivery channel. The ordering process is considered as a crucial determinant of an e-commerce transaction in the OECD definition.

E-commerce facilitates trade across borders, increases convenience for consumers, and enables firms to reach new markets. E-commerce reforms have rapidly evolved through the development of new business models, which often integrate new and emerging digital technologies as well as new online payment mechanisms. Many e-commerce business models use online platforms, facilitating purchases between often unknown and dispersed buyers and sellers. Another emerging trend is the growth of subscription e-commerce business models, whereby users access goods and services in a continuous, recurring stream. E-commerce business models integrate digital ordering mechanisms alongside physical infrastructures, including within brick-and-mortar stores.

[1] OECD (2019), Unpacking E-commerce: Business Models, Trends and Policies, OECD Publishing, Paris, https://doi.org/10.1787/23561431-en.

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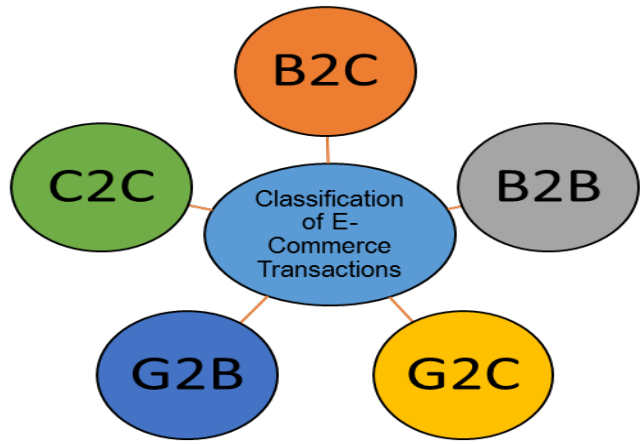
12.3 CONDUCT OF BUSINESS IN DIGITAL ECONOMY

E-commerce is a method of conducting business transactions and not a business transaction by itself. Therefore, the contents of a business transaction done through e-commerce means is no different from that of a business transaction carried out through traditional means.

New business models expand the e-commerce frontier in two ways. First, new business models can enable more transactions to move online in a given market or for a given set of participants. Second, new business models can enable whole new markets to emerge for goods and services that previously could not have been bought or sold online, or allow new participants to enter the market.

Digital technologies enable e-commerce innovations and often serve as the backbone of business model developments. Some of these technologies, like smart assistants enabled by artificial intelligence (AI), constitute new channels for selling or purchasing products over electronic networks. Similarly, online payment innovations can help to unlock e-commerce potential by promoting trusted online transactions between unknown parties.

Classification of E-commerce based on parties involved in transactions. Major types are mentioned below:



(i) **Business to Customers (B2C):** In this type of e-commerce, transactions take place between businesses and consumers. In B2C e-commerce, products or services are sold to end-users (i.e. consumers).

Examples: *Amazon.in, Flipkart.com, Myntra.com, Snapdeal.com etc. are the examples of B2C e-commerce businesses, where consumers can find almost anything be it books, electronic products like washing machines, USB storage devices, clothes, shoes or personal care etc.*

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(ii) **Business to Business (B2B):** In B2B e-commerce, transactions take place between two businesses.

Example: *IndiaMART, TradeIndia, Alibaba, go4WorldBusiness.com (an online B2B marketplace for global exporters and importers), Amazon, the US-based ecommerce giant etc are the example of B2B online platforms.*

(iii) **Government to Customers (G2C):** The online platform between a government and its citizens or consumers for paying taxes, registering vehicles, and providing information and services such as filing of income-tax return etc.

(iv) **Government to Business (G2B)/ Business to Government (B2G):** In G2B/ B2G e-commerce, an electronic exchange of any information between businesses and the government, usually using internet so the cooperation or communication takes place on the internet. In G2B, government agencies and business use websites, procurement marketplaces, applications, web services.

Example: *Government e-Marketplace (GeM), a one stop portal to facilitate online procurement of common use Goods & Services required by various Government Departments/Organizations / PSUs.*

INAM-Pro is a web based application, designed by National Highways and Infrastructure Development Corporation Ltd (NHIDCL) and launched by the Ministry as a common platform to bring cement buyers and sellers together.

(v) **Customer to Customer (C2C):** When goods or services are bought and sold between two consumers, C2C e-commerce business takes place.

Example: Olx, a C2C e-commerce online platform where customer sells his used goods to other customer; eBay, an online marketplace in which an individual sells a product or service to another.

E-Commerce Business Models

With the advancement of digitalization and emergence of new technologies, new forms of e-commerce business models have evolved. Some of such ways of transacting e-commerce business are discussed here below:

Online platform e-commerce business model:

In the context of e-commerce, online platforms act as intermediaries between buyers and sellers to facilitate the exchange of goods and services over the Internet. Buyers benefit due to the presence

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of variety of products available with diverse sellers. Likewise, sellers discover many buyers to whom they can sell their products. As compared to the physical stores, digital marketplace deliver variety of goods and service.

Meaning of Marketplace based model and Inventory based model of e-commerce[2]:

Marketplace based model *of e-commerce means providing an information technology platform by an e-commerce entity on a digital & electronic network to act as a facilitator between buyer and seller.*

Inventory based model of e-commerce *means an e-commerce activity where inventory of goods and services is owned by e-commerce entity and is sold to the consumers directly.*

Subscription e-commerce business model: Subscription business model is characterised by regular and recurring payments for the repeated provision of a good or a service. The subscription business model can relate to recurring purchases of digital goods and services, or a combination of both digital and tangible products (such as a newspaper subscription that includes access to digital content). Some current e-commerce subscription business models, such as Spotify or Netflix etc.

Digital identity and its potential for e-commerce: Digital identity refers to the set of information used by a computer to authenticate an identity. For example, India's Aadhaar programme issues a unique number to every Indian citizen which is a valid means of identification *vis-à-vis* the government as well as private Internet sites including Airbnb, Uber and digital wallet services.

Subscription access to tangible and bundled goods and services: A recent e-commerce trend has been the growth of subscription business models for tangible goods, including in categories like beauty supplies (Birchbox), minerals (Celestial Minerals), groceries (Blue Apron, Hello Fresh), snack foods (Nature Box), cosmetics and self-care products (Dollar Shave Club, Harry's), and many more.

Online-offline e-commerce business models: These business models serve as extensions of e-commerce, pushing the edges of online purchases into physical stores. Some business models combine online ordering with offline distribution, which may be useful to enable the online purchase of products whose quality may not be assessed from a distance, such as perishable goods like groceries. Many businesses have taken advantage of the ubiquity of digital technologies to grow business models based on a combination of both online and offline features. Other online businesses are moving offline by adding brick-and-mortar elements to enable the online sale of other goods, like clothing, where fit may be difficult to assess from a distance.

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[2] *Consolidated FDI Policy Circular of 2017, dated 28.8.2017 read with Press Note dated 26.12.2018*

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Mobile technologies - Helping e-commerce to flourish in brick-and-mortar stores: Mobile technologies empower consumers to perform a range of digital activities, including online shopping. Consumers use digital technologies throughout the commercial process, but smartphones enable buyers to compare prices, to do research and finally make transactions from any networked location.

Online groceries – e-commerce frontier: Many businesses are successfully selling perishable food and groceries online. Some online business models offer direct shipping of purchased groceries alongside guarantees related to quality and customer satisfaction to give consumers confidence in the purchase of perishable goods and services.

Innovative payment mechanisms: Safely and remotely exchanging money online, including across borders, is fundamental to e-commerce. Safe and effective online payment mechanisms facilitate trusted online transactions, boosting the growth of e-commerce between unknown buyers and sellers. Many online payment mechanisms are closely associated with the rise of e-commerce. In fact, one of the earliest online payment models is "Paypal", which is emerged in combination with the pioneering online auction house and e-commerce platform eBay, to enable safe online payments between the parties involved.

Digital wallets: An online payment can be broadly considered to be a "purchase order placed using devices connected to the Internet", a definition that is relevant to many forms of e-commerce. One mechanism of enabling online payments includes the use of digital wallets, also known as "e-wallets" or "electronic wallets".

Digital wallets allow e-commerce by enabling trusted transactions online, without which most e-commerce purchases would not be possible. Consumers may be more willing to do a transaction online using a digital wallet as opposed to directly sharing financial information with online retailers.

Mobile money - Extending e-commerce to the unbanked: Another form of payment innovation that enables e-commerce is the rise of a specific form of mobile payment, also known as "mobile money", particularly for unbanked people (i.e. those without access to financial services). Mobile money differs from digital wallets insofar that the mechanism for payment is conducted via mobile communication networks, and does not necessarily require an existing relationship with a financial services provider.

Mobile money is facilitated by mobile network operators who use a system of agents to accept regular currency in the form of cash and store an equivalent value in a digital wallet, which can then be transferred to other users or can be withdrawn later. Mobile money is connected with a mobile phone number and often uses two-factor authentication through a personal identification number issued at the point of registration. Mobile money can be transferred to others who are also registered

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with the same mobile money system, exchanged with merchants for goods and services, or can be withdrawn as cash from a mobile money agent. Mobile money can therefore act as a means of storing and transferring value in a secure and convenient way for unbanked people.

Resources: *The discussion on E-commerce Business Models in this chapter is essentially based on the text published in "Unpacking E-commerce: Business Models, Trends and Policies, OECD Publishing, Paris" available at https://doi.org/10.1787/23561431-en.*

12.4 TAXATION ISSUES RELATING TO DIGITAL ECONOMY

These new business models have created new tax challenges. The typical taxation issues relating to digital economy are:

(i) the difficulty in characterizing the nature of payment and establishing a nexus or link between taxable transaction, activity and a taxing jurisdiction,

(ii) the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

The digital business, thus, challenges physical presence-based permanent establishment rules. If permanent establishment principles are to remain effective in the new economy, the fundamental PE components developed for the old economy i.e. place of business, location, and permanency must be reconciled with the new digital reality. Further, characterizing the income as technical services becomes difficult since the technical services rendered digitally does not involve human intervention, as the digital platforms operate on sophisticated artificial intelligence mechanism. Hence the new digital business models gives rise to 'stateless income' and thereby going completely tax free.

12.5 OECD RECOMMENDATIONS UNDER ACTION PLAN 1 OF THE BEPS PROJECT

Due to the tax challenges arising from digitalization, the G20-OECD BEPS Action Plan Committee as part of its 2015 Action 1 Report identified a number of broader tax challenges raised by digitalisation, notably in relation to nexus, data and characterisation.

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The Action Report 1 analysed the following three options, namely -

(i) a new nexus rule in the form of a "***significant economic presence***" test,

(ii) ***a withholding tax*** which could be applied to certain types of digital transactions, and

(iii) ***an equalisation levy***, intended to address a disparity in tax treatment between foreign and domestic businesses where the foreign business had a sufficient economic presence in the jurisdiction

The OECD has recommended several options to tackle the direct tax challenges which include:

(1) Modifying the existing definition of permanent establishment to provide for whether an enterprise engaged in fully de-materialized digital activities would constitute a PE, if it maintained a significant digital presence in another country's economy.

(2) Introducing the concept of a virtual fixed place of business in the concept of permanent establishments i.e., creation of a permanent establishments when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website.

(3) Imposition of a final withholding tax on gross basis in case of certain payments made for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

It was concluded that countries could introduce any of these options in their domestic laws as additional safeguards against BEPS, provided they respect existing treaty obligations, or in their bilateral tax treaties. The above options can be resorted to as an interim measure until a clear solution emerges on taxing digital economy.

Taking into consideration the potential of new digital economy and the rapidly evolving nature of business operations, it becomes necessary to address the challenges in terms of taxation of such digital transactions. In order to arrive at a long term solution, the OECD along with the BEPS Inclusive Framework is working on arriving at a consensus based solution to tackle the tax challenges arising out of the digital economy as part of a 'Unified Approach' under Pillar One.

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12.6 EQUALISATION LEVY - CHAPTER VIII IN THE FINANCE ACT, 2016

Consequent to the BEPS Action Report 1, a committee was constituted by the CBDT to evaluate the alternatives suggested in the BEPS Action Report 1 for addressing the challenges arising on taxing the digital economy. Pursuant to the recommendations of the Committee, Chapter VIII of the Finance Act, 2016, titled "Equalisation Levy" was introduced. It provides for an equalisation levy @6% of the amount of consideration for specified services received or receivable by a non-resident not having PE in India, from a resident in India who carries out business or profession, or from a non-resident having PE in India. The Finance Minister, in his Speech while introducing the Finance Bill, 2016 stated as follows:

"151. In order to tap tax on income accruing to foreign e-commerce companies from India, it is proposed that a person making payment to a non-resident, who does not have a permanent establishment, exceeding in aggregate ₹ 1 lakh in a year, as consideration for online advertisement, will withhold tax at 6% of gross amount paid, as EL. The levy will only apply to B2B transactions."

One of the primary reasons for introducing the Equalisation Levy through the Finance Act is to deny tax treaty benefits, as otherwise it may defeat the entire purpose of introducing the Equalisation Levy. The CBDT constituted Committee specifically addresses this aspect in their report and clarifies that tax credit under the relevant tax treaties would not be available, since Equalisation Levy is not in the nature of income tax.

The CBDT issued a notification dated 27th May, 2016, stating that the provisions of Chapter VIII relating to the equalisation levy would come into effect from 1st June 2016. This Chapter extends to the whole of India except Jammu and Kashmir. It applies in respect of consideration received or receivable for specified services provided on or after 1.6.2016.

The key aspects related to Equalisation Levy have been discussed below.

(1) Meaning of "Equalisation Levy" [Section 164(d) of the Finance Act, 2016]:

Equalisation levy means the tax leviable on consideration received or receivable for any specified service..

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(2) Charge of Equalisation Levy on 'Specified Services' [Section 165 of Finance Act, 2016]:

(i) Equalisation levy @6% is leviable on the amount of consideration for specified service received or receivable by a person, being a non-resident from -

(a) a person resident in India and carrying on business or profession; or

(b) a non-resident having a PE in India.

(ii) Equalisation levy is not chargeable, where –

(a) the non-resident providing the specified service has a PE in India and the specified service is effectively connected with such PE;

(b) the aggregate amount of consideration for specified service received or receivable in a previous year by the non-resident from a person resident in India and carrying on business or profession, or from a non-resident having a PE in India, does not exceed ₹ 1 lakh; or

(c) where the payment for the specified service by the person resident in India, or the PE in India is not for the purposes of carrying out business or profession.

(3) Definition of "Specified Service" [Section 164 of the Finance Act, 2016]:

"**Specified Services**" means-

(i) Online advertisement;

(ii) Any provision for digital advertising space or any other facility or service for the purpose of online advertisement;

(iii) Any other service as may be notified by the Central Government.

Note – 'Online' means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network.

(4) Provisions of Chapter on Equalisation Levy:

Section	Subject	Provisions
166	**Collection & Recovery of Equalisation Levy on Specified Services**	
	Person responsible for deduction of equalisation levy	Every person, being a resident and carrying on business or profession or a non-resident having a permanent establishment in India shall deduct equalisation levy referred to in section 165(1) from the amount paid or payable to a non-resident in respect of the specified service.

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	Rate of equalisation levy	**6%** of the amount of consideration for specified service paid or payable to a non-resident in respect of specified service by a person resident in India and carrying on business or profession or a non-resident having a PE in India. The amount of consideration, the amount of equalisation levy, interest and penalty payable and refund shall be **rounded off to the nearest multiple of ten rupees**. For this purpose, any part of a rupee consisting of paise shall be ignored and, thereafter, if such amount is not a multiple of ten, then, if the last figure in that amount is five or more, the amount shall be increased to the next higher amount which is a multiple of ten and if the last figure is less than five, the amount shall be reduced to the next lower amount which is a multiple of ten [Rule 3 of Equalisation Levy Rules, 2016].
	Threshold limit	Equalisation levy is deductible if the aggregate amount of consideration for specified service in a previous year exceeds **one lakh rupees**.
	Time period for remittance of equalisation levy	The equalisation levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government **by the 7th of the month immediately following the said calendar month**. The assessee who is required to deduct and pay equalisation levy, shall pay the amount of such levy, by remitting it into the Reserve Bank of India or in any branch of the State Bank of India or of any authorised Bank accompanied by an equalisation levy challan. [Rule 4 of Equalisation Levy Rules, 2016]
	Consequence of failure to deduct equalisation levy	Any assessee who fails to deduct equalisation levy shall, notwithstanding such failure, be liable to pay the levy to the credit of the Central Government by the 7th of the month immediately following the said calendar month. Thus, if the assessee responsible for deducting equalisation levy, fails to so deduct, he has, in any case, to pay such levy to the credit of the Central Government by the 7th of the month immediately following the said calendar month.

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167	**Furnishing of statement**	
	Statement in prescribed form within time	Every assessee shall, within the prescribed time after the end of each financial year, prepare and deliver or cause to be delivered to the Assessing Officer or to any other authority or agency authorised by the Board in this behalf, a statement in the prescribed form, verified in the prescribed manner and setting forth the prescribed particulars in respect of all specified services during such financial year. The statement in respect of all specified services chargeable to equalisation levy during any financial year is required to be furnished electronically under digital signature or electronically through electronic verification code in **Form No. 1**, duly verified, **on or before 30th June** immediately following that financial year [Rule 5 of Equalisation Levy Rules, 2016]
	Time limit for filing a revised statement	An assessee who has not furnished the statement on or before 30th June immediately following the financial year or having furnished a statement within that time, notices any omission or wrong particulars therein, may furnish a statement or a revised statement, as the case may be. Such statement or revised statement has to be filed at any time **before the expiry of two years from the end of the financial year** in which the specified service was provided.
	Time limit for filing a statement in response to notice issued by the Assessing Officer	Where any assessee fails to furnish the statement within the prescribed time, the Assessing Officer may serve a notice upon such assessee requiring him to furnish the statement in the prescribed form, verified in the prescribed manner and setting forth the prescribed particulars, within such time, as may be prescribed. The Assessing Officer has been empowered to issue notice for furnishing such statement, which then has to be furnished, within 30 days from date of serving of such notice [Rule 6 of Equalisation Levy Rules, 2016]
168	**Processing of statement**	
	Manner of processing of statement	Where a statement has been made under section 167 by the assessee such statement shall be processed in the following manner, namely:—

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		(a) the equalisation levy shall be computed after making the adjustment for **any arithmetical error in the statement**; (b) the **interest**, if any shall be computed on the basis of **sum deductible or payable, as the case may be**, as computed in the statement; (c) the sum payable by, or the amount of refund due to, the assessee, shall be determined after adjustment of interest computed against the equalisation levy paid under section 166(2) or section 166A or interest paid section 170 and any amount paid otherwise by way of tax or interest; (d) an intimation shall be prepared or generated and sent to the assessee, specifying the sum determined to be payable by, or the amount of refund due to him; and (e) the amount of refund due to the assessee in pursuance of such determination shall be granted to him. However, no such intimation shall be sent after the expiry of **one year from the end of the financial year** in which the **statement or revised statement** is furnished.
	Prescribed form for service of notice of demand on the assessee	Where any levy, interest or penalty is payable under the equalisation levy provisions, a notice of demand in Form No. 2 specifying the sum so payable shall be served upon the assessee or e-commerce operator, as the case may be. Further, intimation issued upon processing of the **statement or revised statement** shall also be deemed to be a notice of demand [Rule 7 of Equalisation Levy Rules, 2016]
	Scheme for centralised processing of statements	For the purposes of processing of statements, the CBDT may make a scheme for centralised processing of such statements to expeditiously determine the tax payable by, or the refund due to, the assessee or e-commerce operator as required thereunder.
169	**Rectification of mistake**	
	Time limit for amending an intimation	With a view to rectifying any mistake apparent from the record, the Assessing Officer may amend any intimation issued under section 168.

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<tr><td></td><td></td><td>Such intimation can be amended within one year from the end of the financial year in which the intimation sought to be amended was issued.</td></tr>
<tr><td></td><td>Amendment can be made suo motu or brought to notice by the assessee</td><td>The Assessing Officer may make an amendment to any intimation, either suo motu or on any mistake brought to his notice by the assessee.</td></tr>
<tr><td></td><td rowspan="2">Opportunity of being heard to be given by the Assessing Officer before amending an intimation</td><td>An amendment to any intimation, which has the effect of increasing the liability of the assessee or reducing a refund, shall not be made unless the Assessing Officer has given notice to the assessee of his intention so to do and has given the assessee a reasonable opportunity of being heard.</td></tr>
<tr><td></td><td>Where any such amendment to any intimation has the effect of enhancing the sum payable or reducing the refund already made, the Assessing Officer shall make an order specifying the sum payable by the assessee and the provisions of this Chapter shall apply accordingly.</td></tr>
<tr><td>170</td><td>Interest on delayed payment of equalisation levy</td><td>An assessee who fails to credit the equalisation levy or any part thereof within the period specified u/s 166, to the account of the Central Government, has to pay simple interest at the rate of 1% of such levy for every month or part of a month by which such crediting of the tax or any part thereof is delayed.</td></tr>
<tr><td>171</td><td>Penalty for failure to deduct or pay equalisation levy.</td><td>
<table>
<tr><th>Nature of default</th><th>Penalty</th></tr>
<tr><td>Failure to deduct whole or part of equalisation levy u/s 166</td><td>In addition to payment of equalisation levy u/s 166(3) and interest u/s 170, penalty equal to the amount of equalisation levy that he failed to deduct would be leviable</td></tr>
<tr><td>Failure to remit equalisation levy to the Central Government on or before 7th of the following month,</td><td>In addition to paying the equalisation levy on specified services u/s 166(2) and interest u/s 170, a penalty of ₹ 1,000 for every day</td></tr>
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		after deduction of the same u/s 165(1)	during which the failure continues is leviable. However, such penalty shall not exceed the amount of equalisation levy that he failed to pay.
172	**Penalty for failure to furnish statement**	For failure to furnish the statement within 30th June of the immediately following year or within 30 days from the date of service of notice by the Assessing Officer, penalty of **₹ 100 for each day during which the failure continues** is leviable.	
173	**Circumstances when penalty cannot be imposed under section 171 and 172**	No penalty for failure to deduct or pay equalisation levy or failure to furnish statement shall be imposable, if the assessee proves to the satisfaction of the Assessing Officer that there was reasonable cause for the said failure. Further, no order imposing a penalty under this Chapter shall be made unless the assessee has been given a reasonable opportunity of being heard.	
174	**Appeal to Commissioner of Income-tax (Appeals).**		
	Time limit for filing of appeal against an order imposing penalty	An assessee aggrieved by an order imposing penalty under this Chapter, may appeal to the Commissioner of Income-tax (Appeals) within a period of **30 days from the date of receipt of the order** of the Assessing Officer	
	Fee for filing appeal	An appeal shall be in the prescribed form [Form 3] and verified in the prescribed manner. It shall be accompanied by a **fee of ₹ 1,000**. It may be filed electronically under digital signature or electronically through EVC. Any document accompanying Form No.3 has to be furnished in the manner in which Form No.3 is furnished [Rule 8 of Equalisation Levy Rules, 2016]	
	Provisions of the Income-tax Act, 1961 applicable in case of such appeals	Where an appeal has been filed, the provisions of sections 249 to 251 of the Income-tax Act, 1961 would, as far as may be, apply to such appeal. Section 250 specifies the procedure in appeal and section 251 enlists the powers of the Commissioner (Appeals).	

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175	**Appeal to Appellate Tribunal**	
	Assessee / CIT may file appeal to Appellate Tribunal against an order passed by Commissioner (Appeals) u/s 174	An assessee aggrieved by an order made by the Commissioner of Income-tax (Appeals) under section 174 may appeal to the Appellate Tribunal against such order. The Commissioner of Income-tax may, if he objects to any order passed by the Commissioner of Income-tax (Appeals) under section 174, direct the Assessing Officer to appeal to the Appellate Tribunal against such order.
	Time limit for filing appeal	An appeal shall be filed within **60 days** from the date on which the order sought to be appealed against is received by the assessee or by the Commissioner of Income-tax, as the case may be.
	Fee for filing appeal	The appeal shall be in the prescribed form [Form No.4] and verified in the prescribed manner. In the case of an appeal filed by an assessee or e-commerce operator, it shall be accompanied by a **fee of ₹1,000**. Also, the form of appeal, the grounds of appeal and the form of verification appended thereto shall be signed by the person specified in Form No.4, **as applicable to the assessee, as the case may be** [Rule 9 of Equalisation Levy Rules, 2016]
	Provisions of the Income-tax Act, 1961 applicable in case of such appeals	Where an appeal has been filed before the Appellate Tribunal under sub-section (1) or sub-section (2), the provisions of sections 253 to 255 of the Income-tax Act, 1961 would, as far as may be, apply to such appeal.
176	**Punishment for false statement**	If a person - (a) **makes a false statement in any verification** under this Chapter or any rule made thereunder; or (b) **delivers an account or statement, which is false**, and which he either knows or believes to be false, or does not believe to be true, he shall be punishable with imprisonment for a term which may extend to **three years and with fine**.
		An offence so punishable shall be deemed to be non-cognizable within the meaning of the Code of Criminal

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<table>
<tr><td></td><td></td><td>Procedure. This is irrespective of anything contained in the Code of Criminal Procedure, 1973.</td></tr>
<tr><td>177.</td><td>Institution of prosecution</td><td>Prior sanction of the Chief Commissioner of Income-tax is required for instituting prosecution against any person for any offence under section 176.</td></tr>
<tr><td>178.</td><td>Application of certain provisions of Income-tax Act, 1961</td><td>The following provisions of the Income-tax Act, 1961 shall so far as may be, apply in relation to equalisation levy, as they apply in relation to income-tax.
<table>
<tr><th>Section</th><th>Content</th></tr>
<tr><td>119</td><td>Instruction to subordinate authorities</td></tr>
<tr><td>120</td><td>Jurisdiction of income-tax authorities</td></tr>
<tr><td>131</td><td>Power regarding discovery, production of evidence, etc.</td></tr>
<tr><td>133A</td><td>Power of survey</td></tr>
<tr><td>138</td><td>Disclosure of information respecting assesses</td></tr>
<tr><td>156</td><td>Notice of demand</td></tr>
<tr><td>Chapter XV</td><td>Liability in special cases</td></tr>
<tr><td>220-227</td><td>- When tax payable and when assessee deemed in default,
- Penalty payable when tax in default,
- Certificate to Tax Recovery Officer,
- Tax Recovery Officer by whom recovery is to be effected,
- Validity of certificate and cancellation or amendment thereof,
- Stay of proceedings in pursuance of certificate and amendment or cancellation thereof,
- Other modes of recovery,
- Recovery through State Government.</td></tr>
<tr><td>229</td><td>Recovery of penalties, fine, interest and other sums</td></tr>
<tr><td>232</td><td>Recovery by suit or under other law not affected.</td></tr>
</table></td></tr>
</table>

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		260A	Appeal to High Court
		261	Appeal to Supreme Court
		262	Hearing before Supreme Court
		265 to 269	- Tax to be paid notwithstanding reference etc., - Execution for costs awarded by Supreme Court, - Amendment of assessment on appeal - Exclusion of time taken for copy, - Filing of appeal or application for reference by income-tax authority, - Definition of "High Court"
		278B	Offences by companies
		280A	Special Courts
		280B	Offences triable by Special Court
		280C	Trial of offences as summons case
		280D	Application of Code of Criminal Procedure, 1973 to proceedings before Special Court
		282	Service of notice generally
		288 to 293	- Appearance by authroised representative, - Rounding off of income, - Rounding off of amount payable and refund due, - Receipt to be given, - Indemnity, - Power to tender immunity from prosecution, - Cognizance of offences, - Section 360 of the Code of Criminal Procedure, 1973 and the Probation of Offenders Act, 1958, not to apply, - Return of income, etc., not to be invalid on certain grounds, - Notice deemed to be valid in certain circumstances,

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			- Presumption as to assets, books of account etc., - Authorisation and assessment in case of search or requisition, - Bar of suits in civil courts
179	**Power to make rules**	The Central Government is empowered to make rules for the purposes of carrying out the provisions of this Chapter.	
		In particular, such rules may also provide for all or any of the following matters, namely:— (a) the time within which and the form and the manner in which the statement shall be delivered or caused to be delivered or furnished under section 167; (b) the form in which an appeal may be filed and the manner in which it may be verified under sections 174 and 175; (c) any other matter which is to be, or may be, prescribed.	
		Every rule made under this Chapter shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of **30 days**. This period of 30 days may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree: (i) in making any modification in the rule, then, the rule shall thereafter have effect only in such modified form; (ii) that the rule should not be made, then, the rule would be of no effect. However, any such modification or annulment would be without prejudice to the validity of anything previously done under that rule.	

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(5) Relevant provisions in the Income-tax Act, 1961:

	Section	Provision
(i)	10(50)	In order to avoid double taxation on account of Equalisation Levy and income-tax liability under the provisions of the Income-tax Act, 1961, section 10(50) exempts any income arising from providing any specified service on or after the date on which the provisions of Chapter VIII of the Finance Act, 2016 comes into force and chargeable to equalisation levy under that Chapter. However, the income arising from providing specified services would not include any income which is taxable as royalty or fees for technical services in India under the Income-tax Act, read with the DTAA notified by the Central Government under section 90 or section 90A. Exemption under section 10(50) is available in respect of amounts which have been subjected to Equalisation Levy. However, in case of transactions in respect of which equalisation levy is not attracted, the provisions of the Income-tax Act, 1961, as applicable, will apply.
(ii)	40(a)(ib)	In order to ensure compliance with the provisions this Chapter, section 40(a)(ib) provides that if any consideration is paid or payable to a non-resident for a specified service on which equalisation levy is deductible, and such levy has not been deducted or after deduction, has not been paid on or before the due date under section 139(1), then, such expenses incurred by the assessee towards consideration for specified service shall not be allowed as deduction. However, where in respect of such consideration, if the equalisation levy has been deducted in any subsequent year or has been deducted during the previous year but paid after the due date specified under section 139(1), such sum shall be allowed as deduction in computing the income of the previous year in which such levy has been paid.

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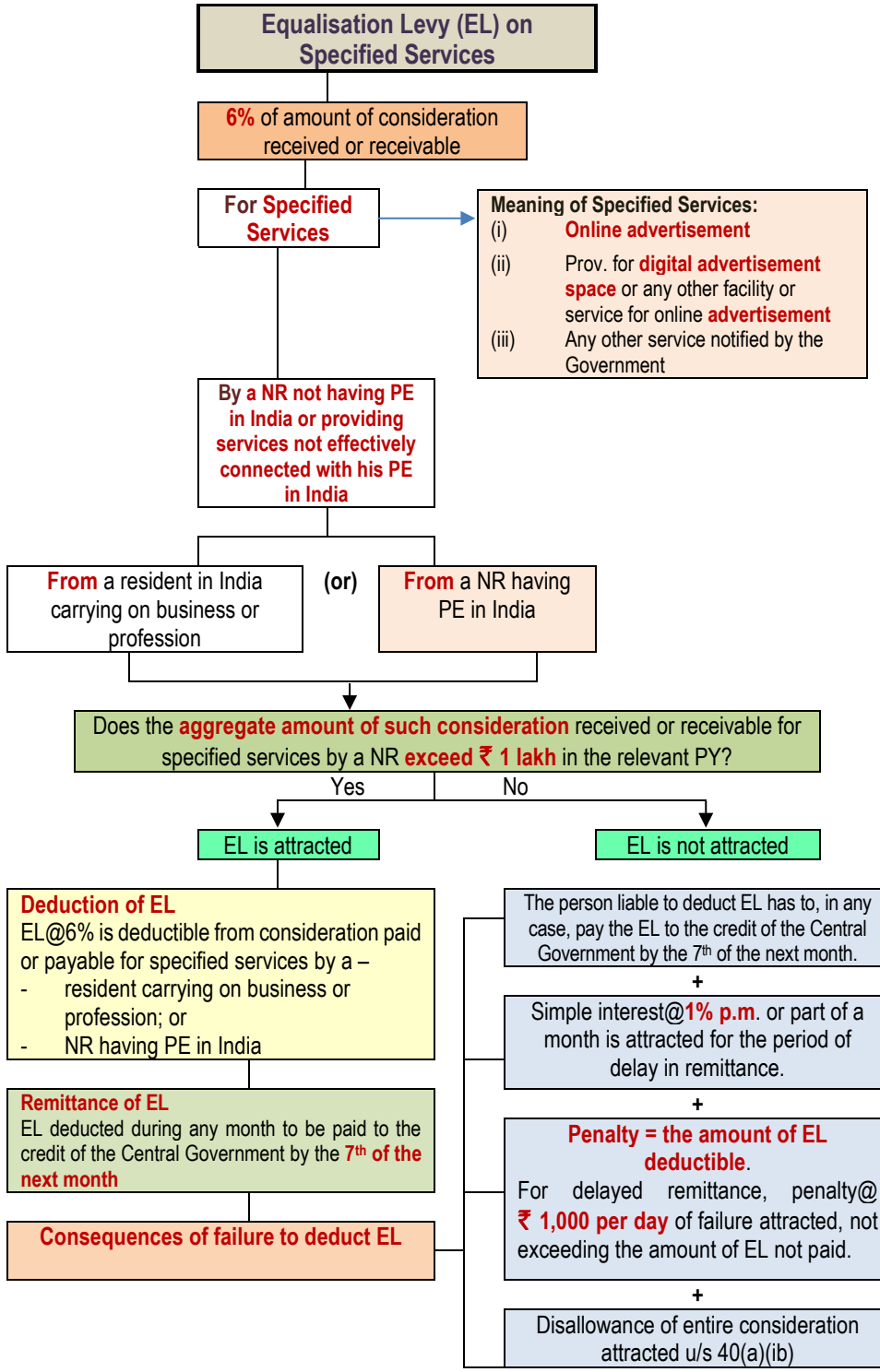

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12.7 TAXATION OF VIRTUAL DIGITAL ASSETS

There has been a phenomenal increase in transactions in virtual digital assets. Further, a market is emerging where payment for the transfer of a virtual digital asset can be made through another such asset. Accordingly, for the taxation of virtual digital assets, a scheme has been introduced by the Finance Act, 2022.

Meaning of virtual digital asset [Section 2(47A)]

It means -

(a) any information or code or number or token (not being Indian currency or foreign currency),

- generated through cryptographic means or otherwise, by whatever name called,
- providing a digital representation of value exchanged with or without consideration,
- with the promise or representation of having inherent value, or
- functions as a store of value or a unit of account including its use in any financial transaction or investment, but not limited to investment scheme; and
- can be transferred, stored or traded electronically;

(b) a non-fungible token or any other token of similar nature, by whatever name called;

The non-fungible token means such digital asset as may be notified by the Central Government.

Accordingly, the Central Government has, vide notification no. 75/2022 dated 30.6.2022, specified a token which qualifies to be a virtual digital asset as non-fungible token. However, it shall not include a non-fungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

(c) any other digital asset, as may be notified by the Central Government.

However, the Central Government may, by notification, exclude any digital asset from the definition of virtual digital asset subject to specified conditions.

Accordingly, the Central Government has, vide notification no. 74/2022 dated 30.6.2022, notified that the following virtual digital assets would be excluded from the definition of virtual digital asset–

(i) Gift card or vouchers, being a record that may be used to obtain goods or services or a discount on goods or services;

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(ii) Mileage points, reward points or loyalty card, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services;

(iii) Subscription to websites or platforms or application

Taxability of income from transfer of virtual digital assets [Section 115BBH]

(1) Tax rate on transfer of virtual digital asset – Where the total income of an assessee includes any income from the transfer of any virtual digital asset, such income would be taxed @30% under section 115BBH.

(2) No deduction allowed – In computing the income from transfer of virtual digital asset, no deduction would be allowed under any provisions of the Act in respect of any expenditure or allowance except cost of acquisition, if any. Further, no set off of any loss is allowed to the assessee from such income.

(3) Set off or carry forward of loss from transfer of virtual digital asset not allowed – Loss from transfer of virtual digital asset would **not** be allowed to be set off against income computed under any provision of this Act to the assessee and such loss would not be allowed to be carried forward to succeeding assessment years.

(4) Virtual digital asset need not to be a capital asset - The definition of "transfer" under section 2(47) would apply to any virtual digital asset, whether it is a capital asset or not.

Taxability of receipt of virtual digital asset as gift or for inadequate consideration [Section 56(2)(x)]

In order to tax gift of virtual digital asset in the hands of the recipient, section 56 has been amended to include virtual digital asset within the definition of "property".

Accordingly, if virtual digital asset is received by any person from any person

(i) **Without consideration:** The aggregate fair market value of such virtual digital asset on the date of receipt would be taxed as the income of the recipient, if it exceeds ₹ 50,000.

(ii) **For inadequate consideration:** If the difference between the aggregate fair market value and such consideration exceeds ₹ 50,000, such difference would be taxed as the income of the recipient.

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However, the exclusions from the applicability of section 56(2)(x) will apply to gift virtual digital asset also. For example, if virtual digital asset is received as a gift by an individual from his relative, the value of the same would not be treated as income.

TDS on payment on transfer of virtual digital asset [Section 194S]

(1) **Applicability and rate of TDS –** Section 194S requires any person who is responsible for paying to any resident any sum by way of consideration for transfer of a virtual digital asset to deduct tax @1% of such sum.

(2) **Time of deduction –** The deduction is to be made at the time of credit of consideration to the account of the resident or at the time of payment of such sum by any mode, whichever is earlier.

Where consideration is credited to any account in the books of account of the person liable to pay such sum, such credit of the sum is deemed to be the credit of such sum to the account of the payee and tax has to be deducted at source. The account to which such sum is credited may be called "Suspense Account" or by any other name.

(3) **Cases where the consideration for transfer of virtual digital asset is wholly in kind or partly in kind and partly in cash** – In a case where the consideration for transfer of virtual digital asset is

- wholly in kind or in exchange of another virtual digital asset, where there is no part in cash; or
- partly in cash and partly in kind but the part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of such transfer,

the person responsible for paying such consideration has to, before releasing the consideration, ensure that tax required to be deducted has been paid in respect of such consideration for the transfer of virtual digital asset.

(4) **Non applicability of TDS under section 194S –** No tax is required to be deducted under section 194S, where the consideration is payable by the person referred to in column (2) of the table below and aggregate value of such consideration during the financial year does not exceed the threshold limit in the corresponding row of column (3) of the table below:

(1)	Consideration is payable by (2)	Threshold limit (3)
(i)	Specified person, being an individual or a Hindu undivided family	≤ ₹ 50,000

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	- whose total sales, gross receipts or turnover from his business or profession does not exceed ₹ 1 crore in case of business or ₹ 50 lakhs in case of profession, during the financial year immediately preceding the financial year in which such virtual digital asset is transferred; or - not having any income under the head "Profits and gains of business or profession".	
(ii)	Other than specified person mentioned in (i) above	≤ ₹ 10,000

(5) Due date of remittance to Government Account [Rule 30] and Furnishing statement and certificate of TDS u/s 194S [Rules 31A and 31]

<table>
<tr><th>Sl. No.</th><th>(1)
Particulars</th><th>(2)
Specified Person</th><th>(3)
Exchange</th><th>(4)
Any other person</th></tr>
<tr><td>(i)</td><td>Rule 30 – Time of payment to Government Account</td><td>30 days from the end of the month of deduction</td><td colspan="2">In case of tax deducted in March, on or before 30th April.
In any other case, on or before 7 days from the end of the month of deduction.</td></tr>
<tr><td rowspan="3">(ii)</td><td>Rule 31A – Furnishing of Statement of TDS u/s 200(3)</td><td></td><td colspan="2"></td></tr>
<tr><td>Form</td><td>Form 26QE</td><td>Form 26QF</td><td>Form 26Q</td></tr>
<tr><td>Time</td><td>Within 30 days from the end of the month of deduction</td><td colspan="2">Common for Exchange and any other person
<table><tr><th>Qtr ending</th><th>Due date</th></tr><tr><td>30th June</td><td>31st July</td></tr><tr><td>30th Sep</td><td>31st Oct</td></tr><tr><td>31st Dec</td><td>31st Jan</td></tr><tr><td>31st March</td><td>31st May</td></tr></table></td></tr>
<tr><td>(iii)</td><td>Rule 31 – TDS Certificate</td><td>Form 16E to be furnished within 15 days from the due date of furnishing TDS statement in Form 26QE.</td><td colspan="2">Form 16A to be furnished within 15 days from the due date of furnishing TDS statement in Form 26QF/Form 26Q.</td></tr>
</table>

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ILLUSTRATION 1

Compute the income-tax payable by Mr. Abhinav, aged 32 years, who has the following income for the A.Y.2025-26:

(i)	*Interest on fixed deposits with SBI (Gross)*	*₹ 1,10,000*
(ii)	*Interest on savings bank account with SBI*	*₹ 15,000*
(iii)	*Consideration received for transfer of VDA*	*₹ 62,000*
(iv)	*Cost of acquisition*	*₹ 21,000*
(v)	*Expenses on transfer of VDA*	*₹ 1,000*

Mr. Abhinav has exercised option to shift out of section 115BAC.

SOLUTION

Total income (excluding Income from transfer of VDA) is below the basic exemption limit of ₹ 2,50,000. Therefore, tax on income, other than income from VDA, is Nil. Income of ₹ 41,000 (₹ 62,000 – ₹ 21,000) from transfer of VDA would be taxable@30% (plus cess of 4%), even if the total income including income from transfer of VDA is less than the basic exemption limit. The tax on income from transfer of VDA would be ₹ 12,792, being 31.2% of ₹ 41,000. The expenses on transfer of VDA is not allowable as deduction.

Section 194S provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of 1% of consideration. Hence, the transferee would have deducted tax of ₹ 620, being 1% of ₹ 62,000.

Tax@10% under section 194A would have been deducted by SBI from ₹ 1,10,000. TDS u/s 194A = ₹ 11,000

Net tax payable by Mr. Abhinav would be ₹ 1,172 (₹ 12,792 – ₹ 11,000 (TDS u/s 194A) – ₹ 620 (TDS u/s 194S).

ILLUSTRATION 2

Compute the income-tax payable by Mr. Siddhanth, aged 24 years, who has the following income for the A.Y.2025-26

(i)	*Income from Salaries (computed)*	*₹ 8,40,000*
(ii)	*Interest on savings bank account with Axis Bank*	*₹ 12,000*
(iii)	*Consideration received on transfer of VDA to Mr. Harsh*	*₹ 50,000*
(iv)	*Cost of acquisition of VDA transferred*	*₹ 5,000*

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Mr. Harsh is employed with ABC Ltd. on a monthly salary of ₹ 50,000. In addition, he has interest on savings bank account with Bank of India.

Mr. Siddhanth has not exercised option to shift out of section 115BAC. Ignore TDS on income other than VDA.

SOLUTION

Tax payable by Mr. Siddhanth for A.Y. 2025-26

Particulars		Amount in ₹
Total income (excluding income from transfer of VDA) [₹ 8,40,000 + ₹ 12,000]		8,52,000
Income from VDA (₹ 50,000 – ₹ 5,000)		45,000
Total Income		**8,97,000**
Tax on income other than VDA		
Upto ₹ 3,00,000	Nil	
₹ 3,00,001 to ₹ 7,00,000 @5%	₹ 20,000	
₹ 7,00,001 to ₹ 8,52,000 @10%	₹ 15,200	35,200
Tax on income from VDA @30%		13,500
		48,700
Add: Health and education cess @ 4%		1,948
		50,648
Less: TDS under section 194S [Mr. Harsh is a specified person since he does not have income under the head "Profits and gains of business and profession" and the consideration payable by him does not exceed ₹ 50,000. Accordingly, Mr. Harsh need not deduct tax u/s 194S on consideration payable to Siddhanth]		Nil
Net tax payable		**50,648**
Net tax payable (rounded off)		**50,650**

ILLUSTRATION 3

Compute the income-tax payable by Mr. Raj, aged 32 years, who has the following income for the A.Y.2025-26

(i)	*Business loss*	*(₹ 3,18,000)*
(ii)	*Interest on fixed deposits with HDFC Bank*	*₹ 18,000*
(iii)	*Consideration received on transfer of VDA*	*₹ 4,20,000*
(iv)	*Cost of acquisition of VDA transferred*	*₹ 20,000*

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SOLUTION

As per section 71, business loss of the current year can be set off against income from other sources of that year. Therefore, business loss of ₹ 3,18,000 can be set off against interest of ₹ 18,000 from fixed deposits.

As per section 115BBH, business loss cannot be set off against income from transfer of VDA. Therefore, balance business loss of ₹ 3,00,000 cannot be set off against Income from VDA of ₹ 4,00,000 (₹ 4,20,000 – ₹ 20,000). The same has to be carried forward to A.Y.2026-27 for set-off against business income of that year.

Tax on Income from VDA would be ₹ 1,24,800 (i.e., 31.2% of ₹ 4 lakh).

Section 194S provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of 1% of consideration. Hence, the transferee would have deducted tax of ₹ 4,200, being 1% of ₹ 4,20,000.

Net tax payable by Mr. Raj = ₹ 1,24,800 – ₹ 4,200 = ₹ 1,20,600.

(6) **Non-applicability of section 203A and 206AB on specified person -** The provisions of section 203A containing the requirement of obtaining TAN and section 206AB requiring higher rate of TDS for non-filers of income-tax return would **not** be applicable in case of specified person referred in 4(1).

(7) **Cross application of section 194-O and section 194S -** In case of a transaction where tax is deductible under section 194-O along with the section 194S, then, the tax shall be deducted under section 194S and not section 194-O.

(8) **Power of the CBDT to issue guidelines –** In case any difficulty arises in giving effect to the provisions of this section, the CBDT is empowered to issue guidelines, with the prior approval of the Central Government, for the purposes of removing the difficulty.

Every guideline issued by the CBDT shall be laid before each House of Parliament, and shall be binding on the income-tax authorities and on the person responsible for paying the consideration on transfer of such virtual digital asset.

Accordingly, the CBDT has, with the prior approval of the Central Government, vide Circular no. 13/2022 dated 22.6.2022, issued the following guidelines. These guidelines would apply only in cases where transfer of virtual digital asset is taking place on or through an Exchange. In other cases (like peer to peer and others) provisions of section 194S would apply and so far as these guidelines are concerned clarifications provided only in Question 6 shall apply.

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Question 1: Who is required to deduct tax when the transfer of virtual digital asset is taking place on or through an Exchange and payment is made by the purchaser to the Exchange (directly or through broker) and then from the Exchange it goes to seller directly or through the broker?

Answer: According to section 194S, any person who is responsible for paying to any resident any sum by way of consideration for transfer of virtual digital asset is required to deduct tax.

Thus, in a peer to peer (i.e., direct buyer to seller) transaction, the buyer (i.e., person paying the consideration) is required to deduct tax under section 194S. The tax so deducted is required to be deposited with Government in accordance with the time and procedure prescribed in the Act read with the relevant provisions of the Income-tax Rules, 1962.

After deduction, the deductor is required to furnish a quarterly statement (in Form No. 26Q) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962. For specified person Form 26QE has been introduced.

It may be clarified that the TDS shall be on consideration for transfer of virtual digital asset less GST. **[Clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions not conducted on or through Exchange]**

However, if the transaction is taking place on or through an Exchange, there is a possibility of tax deduction requirement under section 194S at multiple stages. Hence, in order to remove difficulties for transactions taking place on or through an Exchange, the following clarifications have been issued by CBDT :-

(i) **In a case where the transfer of virtual digital asset takes place on or through an Exchange and the virtual digital asset being transferred is owned by a person other than the Exchange:** In this case, buyer would be crediting or making payment to the Exchange (directly or through a broker). The Exchange, then, would be required to credit or make payment to the owner of virtual digital asset being transferred, either directly or through a broker. Since there are multiple players, to remove difficulty it has been clarified that:

1. Tax may be deducted under section 194S only by the Exchange which is crediting or making payment to the seller (owner of the virtual digital asset being transferred). In a case where broker owns the virtual digital asset, it is the broker who is the seller. Hence, the amount of consideration being credited or paid to the broker by the Exchange is also subject to tax deduction under section 194S.

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2. In a case where the credit/ payment between Exchange and the seller is through a broker (and the broker is not seller), the responsibility to deduct tax under section 194S shall be on both the Exchange and the broker. However, if there is a written agreement between the Exchange and the broker that broker shall be deducting tax on such credit/ payment, then broker alone may deduct the tax under section 194S. The Exchange would be required to furnish a quarterly statement (in Form 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962.

(ii) **In a case where the transfer of virtual digital asset takes place on or through an Exchange and the virtual digital asset being transferred is owned by such Exchange:** In this case, there are no multiple players. The buyer is required to deduct tax under section 194S. However, there may be a practical issue as the buyer may not know whether the virtual digital asset being transferred is owned by the Exchange or not. Hence, there may be genuine doubt in the mind of buyer with regard to its responsibility to deduct tax under section 194S. This difficulty would also be there if the buyer is buying virtual digital asset from an Exchange through a broker.

To remove this difficulty, it has been clarified that while the primary responsibility to deduct tax under section 194S, in this case, remains with the buyer or his broker, as an alternative the Exchange may enter into a written agreement with the buyer or his broker that in regard to all such transactions, the Exchange would be paying the tax on or before the due date for that quarter. The Exchange would be required to furnish a quarterly statement (in Form 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962. The Exchange would also be required to furnish its income tax return and all these transactions must be included in such return. If these conditions are complied with, the buyer or his broker would not be held as assessee in default under section 201 for these transactions.

Meaning of certain terms:

(i) The term "Exchange" means any person that operates an application or platform for transferring of virtual digital assets, which matches buy and sell trades and executes the same on its application or platform.

(ii) The term "Broker" means any person that operates an application or platform for transferring of virtual digital assets and holds brokerage account/accounts with an Exchange for execution of such trades.

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Question 2: Question no 1 was with respect to transactions where the consideration for transfer of virtual digital asset is not in kind. How will this operate in a situation where it is in kind or in exchange of another virtual digital asset?

Answer: In the above situation, the buyer will release the consideration in kind after seller provides proof of payment of such tax (e.g., Challan details etc.). In a situation where virtual digital asset "A" is being exchanged with another virtual digital asset "B", both the persons are buyer as well as seller. One is buyer for "A" and seller for "B" and another is buyer for "B" and seller for "A". Thus, both need to pay tax with respect to transfer of virtual digital asset and show the evidence to other so that virtual digital assets can then be exchanged. This would then be required to be reported in TDS statement along with challan number. Form 26Q has included provisions for reporting such transactions. For specified persons, Form 26QE has been introduced. **[Also clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions not conducted on or through Exchange]**

However, if the transaction is through an Exchange there is practical issue in implementing this provision. In order to address this practical issue and to remove difficulty, it is clarified that in such a situation, as an alternative, tax may be deducted by the Exchange. Such an alternative mechanism can be exercised by the Exchange based on written contractual agreement with the buyers/sellers.

If such an alternative mechanism is exercised,

(i) the Exchange would be required to deduct tax for both legs of the transactions and pay to the Government. In the Form 26Q it will need to report it as tax deducted on both legs of the transaction.

(ii) the buyer and seller would not be independently required to follow the procedure prescribed under proviso to section 194S(1) i.e., to ensure that the tax required to be deducted has been paid by the other person, before releasing the consideration.

(iii) The tax withheld in kind under section 194S and converted into INR shall be deposited in the Government Account as per the time line and process given in the Income-tax Rules 1962.

It has been clarified that there would not be any further TDS for converting the tax withheld in kind in the form of virtual digital asset into INR or from one virtual digital asset to another virtual digital asset and then into INR.

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Question 3: Whether the provision of section 194Q is also applicable on transfer of virtual digital asset?

Answer: Without going into the merit whether virtual digital asset is goods or not, it is clarified that once tax is deducted under section 194S, tax would not be required to be deducted under section 194Q. **[Also clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions also not conducted on or through Exchange]**

Question 4: Whether the consideration for transfer of virtual digital asset shall be on Gross basis after including GST/commission or it shall be on "net basis" after exclusion of these items.

Answer: In order to remove difficulty, it is clarified that the tax required to be withheld under section 194S shall be on the "net" consideration after excluding GST/charges levied by the deductor for rendering service.

Question 5: In transactions where payment is being carried out through payment gateways, there may be tax deduction twice. To illustrate that a person "XYZ" is required to make payment to the seller for transfer of virtual digital asset. He makes payment of ₹ 1,00,000 through digital platform of "ABC". On these facts liability to deduct tax under section 194S may fall on both "XYZ" and "ABC". Is tax required to be deducted by both?

Answer: In order to remove this difficulty, it is provided that in the above example, the payment gateway will not be required to deduct tax under section 194S on a transaction, if the tax has been deducted by the person ("XYZ") required to make deduction under section 194S. Hence, in the above example, if "XYZ" has deducted tax under section 194S on ₹ 1,00,000, "ABC" will not be required to deduct tax under section 194S on the same transaction. To facilitate proper implementation, "ABC" may take an undertaking from "XYZ" regarding deduction of tax.

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TEST YOUR KNOWLEDGE

Questions

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

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

3. *ABC Ltd., an Indian company, is carrying on the business of manufacture and sale of teakwood furniture under the brand name "PUREWOOD". In order to expand its overseas sales/exports, it launched a massive advertisement campaign of its products. For the purpose of online advertisement, it utilized the services of PQR Inc., a London based company. During the previous year 2024-25, ABC Ltd. paid ₹ 5 lakhs to PQR Inc. for such services. Discuss the tax implications/TDS implications of such payment and receipt in the hands of ABC Ltd. and PQR Inc., respectively, if –*

   (i) PQR Inc. has no permanent establishment in India

   (ii) PQR Inc. has a permanent establishment in India, and the service is effectively connected to the permanent establishment in India

4. *MNO Inc., a Country A based company, is carrying on the business of manufacture and sale of furniture under the brand name "PUREWOOD". In order to increase its share in Indian market, it launched a massive advertisement campaign of its products. For the purpose of online advertisement, it utilized the services of PQR Inc., a Country Y based company. During the previous year 2024-25, MNO Inc. paid ₹ 5 lakhs to PQR Inc. for such services. Discuss the tax implications in the hands of MNO Inc., if –*

   (i) both MNO Inc. and PQR Inc. have no permanent establishment in India

   (ii) MNO Inc. has a permanent establishment in India but PQR Inc. has no permanent establishment in India.

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Answers

1. 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, no requirement of physical presence of goods and no requirement of physical delivery (in certain cases). 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.

2. The typical taxation issues relating to e-commerce are:

(1) the difficulty in characterizing the nature of payment and establishing a nexus or link between taxable transaction, activity and a taxing jurisdiction,

(2) the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

3. Chapter VIII of the Finance Act, 2016, "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India.

"Specified Service" means -

(1) online advertisement;

(2) any provision for digital advertising space or any other facility or service for the purpose of online advertisement; and

(3) any other service as may be notified by the Central Government.

However, equalisation levy shall not be levied-

- where the non-resident providing the specified services has a permanent establishment in India and the specified service is effectively connected with such permanent establishment.
- the aggregate amount of consideration for specified service received or receivable during the previous year does not exceed ₹ 1 lakh.
- where the payment for specified service is not for the purposes of carrying out business or profession

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(i) Where PQR Inc. has no permanent establishment in India

In the present case, equalisation levy @6% is chargeable on the amount of ₹ 5,00,000 received by PQR Inc., a non-resident not having a PE in India from ABC Ltd., an Indian company. Accordingly, ABC Ltd. is required to deduct equalisation levy of ₹ 30,000 i.e., @6% of ₹ 5 lakhs, being the amount paid towards online advertisement services provided by PQR Inc., a non-resident having no permanent establishment in India. Non-deduction of equalisation levy would attract disallowance under section 40(a)(ib) of 100% of the amount paid while computing business income.

Since equalisation levy is attracted on the amount of ₹ 5 lakhs, the said amount is exempt from income-tax by virtue of section 10(50) of the Income-tax Act, 1961.

(ii) Where PQR Inc. has permanent establishment in India and the service is effectively connected to the permanent establishment in India

Equalisation levy would not be attracted where the non-resident service provider (PQR Inc., in this case) has a permanent establishment in India and the service is effectively connected to the permanent establishment in India. Therefore, the ABC Ltd. is not required to deduct equalisation levy on ₹ 5 lakhs, being the amount paid towards online advertisement services to PQR Inc, in this case.

Since equalisation levy is not attracted in this case, exemption under section 10(50) of the Income-tax Act, 1961 would not be available. Therefore, tax has to be deducted by ABC Ltd. at the rates in force under section 195 in respect of such payment to PQR Inc. Non-deduction of tax at source under section 195 would attract disallowance under section 40(a)(i) of 100% of the amount paid while computing business income.

4. Chapter VIII of the Finance Act, 2016, "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India.

"Specified Service" means

(1) online advertisement;

(2) any provision for digital advertising space or any other facility or service for the purpose of online advertisement and

(3) any other service as may be notified by the Central Government.

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However, equalisation levy shall not be levied-

- where the non-resident providing the specified services has a permanent establishment in India and the specified service is effectively connected with such permanent establishment.
- the aggregate amount of consideration for specified service received or receivable during the previous year does not exceed ₹ 1 lakh.
- where the payment for specified service is not for the purposes of carrying out business or profession.

(i) Where MNO Inc. and PQR Inc. have no permanent establishment in India

Equalisation levy would not be attracted in the present case since MNO Inc., a non-resident service recipient, does not have a permanent establishment in India. Therefore, the MNO Inc. is not required to deduct equalisation levy @ 6% on ₹ 5 lakhs, being the amount paid towards online advertisement services to PQR Inc.

(ii) Where MNO Inc. has a permanent establishment in India but PQR Inc. does not have a permanent establishment in India

In the present case, equalisation levy @6% is chargeable on the amount of ₹ 5,00,000 received by PQR Inc., a non-resident not having a PE in India from MNO Inc., a non-resident having a PE in India. Accordingly, MNO Inc. is required to deduct equalisation levy of ₹ 30,000 i.e., @6% of ₹ 5 lakhs, being the amount paid towards online advertisement services provided by PQR Inc., a non-resident having no permanent establishment in India. Non-deduction of equalisation levy would attract disallowance under section 40(a)(ib) of 100% of the amount paid while computing business income.

Since equalisation levy is attracted on the amount of ₹ 5 lakhs, the said amount is exempt from income-tax by virtue of section 10(50) of the Income-tax Act, 1961.

However, since PQR Inc. has a PE in India and advertisement services are effectively connected with the PE in India, such advertisement income would be deemed to accrue or arise in India in the hands of PQR Inc. under section 9(1)(i) and would be taxable in the hands of PQR Inc. under the Income-tax Act, 1961.

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